ASIC

Australian Securities & Investments Commission

REPORT 516

Review of mortgage broker remuneration

March 2017

About this report

At the request of the Government, ASIC conducted a review of the mortgage broking market to determine the effect of current remuneration structures on the quality of consumer outcomes.

This report sets out the findings of that review.

In light of our findings, we have also included a series of proposals to improve consumer and market outcomes. These proposals will be subject to consultation with stakeholders.

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- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
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Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

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Examples in this report are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

Contents

Executive summary

1 In November 2015, ASIC was asked by the then Minister for Small Business and Assistant Treasurer (now Minister for Revenue and Financial Services) to review the mortgage broking market to determine the effect of current remuneration structures on the quality of consumer outcomes.

2 This review had four main objectives:

(a) *Remuneration for brokers*—We sought to identify and value the remuneration arrangements that exist in the mortgage broking market, including both cash incentives (e.g. commissions) and other benefits available to brokers (e.g. 'soft dollar' benefits).

(b) *Outcomes for consumers*—We sought to assess consumer outcomes in the mortgage broking market. These outcomes related to the features, pricing and performance of loans provided through brokers, together with a review of how brokers distributed loans between lenders (including whether ownership relationships between lenders and other industry participants affected loan flow).

(c) *Remuneration for other participants*—We reviewed the remuneration arrangements for lenders' own staff who provide home loans (e.g. through bank branches), as well as the consumer outcomes linked to this distribution channel. This put the remuneration arrangements and consumer outcomes of the mortgage broking market in a broader context and provided comparisons across distribution channels. We also sought to document the size and remuneration arrangements of two other distribution channels within the home loan market: comparison websites and individuals who receive remuneration for merely referring consumers to brokers and lenders (known as 'referrers').

(d) *Access to aggregators' panels*—We looked at the composition of aggregators' lender panels, including whether smaller lenders could access those panels.

3 We also sought to understand the governance and oversight arrangements in place within relevant industry participants in relation to remuneration structures and consumer outcomes.

4 This report sets out our findings. In light of our findings, we have also set out a series of proposals to improve consumer and market outcomes. These proposals will be subject to consultation with stakeholders.

Our work on home lending

5 Since assuming responsibility for the regulation of consumer credit, ASIC has done a considerable amount of work in relation to home lending and mortgage brokers. Recently, we have published a number of reports following industry reviews of how lenders and brokers provide interest-only home loans, to ensure that consumers are not being placed into unsuitable loans and loans they cannot afford.

6 Our recent reports have resulted in industry participants making changes to their processes, to raise home lending standards and ensure consumers are being provided with suitable loans. The timing of these changes means they will not be reflected in the data we collected for this review. For some of the findings in this report, the recent changes made by industry will be relevant.

7 We have also taken significant action in relation to loan fraud, where brokers and the staff employed by lenders have been found to falsify documents when arranging loans for consumers. To date, ASIC has banned 74 individuals or companies from providing credit services (including 32 permanent bans).

8 ASIC has also brought criminal prosecutions against 14 credit service providers; with 12 having been convicted of fraud or dishonesty offences relating to the provision of false and misleading information/documents to lenders in client loan applications. These documents were submitted with the intention of deceiving lenders into believing that the borrowers were in better financial positions than they were, to improve the likelihood of the loans being approved and remuneration (usually commissions) being paid.

Scope of our review

9 Consumers generally seek a home loan for one of a number of purposes—for example, to buy a home, to construct a new home or refinance an existing home loan. Alternatively, a consumer may be using the home as security to take out or refinance a loan for another personal purpose. The home may be used as the consumer's own residence or rented out as an investment property. Our review covered home loans for all these purposes.

Note: We did not examine loans for non-personal purposes (e.g. business purposes) even where the loan was secured by a consumer's home. We also did not examine certain specialist types of home lending as part of this review, including reverse mortgage products or lending to self-managed superannuation funds. Where we identify concerns with those types of lending, we may conduct separate reviews of those specialist products.

10 In December 2016, lending for home loans by Australian deposit taking institutions (ADIs) was worth $1,493.5 billion, with an average loan balance

of $257,000 across 5.7 million loans. ADIs are estimated to account for 92% of the home loan market, with other types of lenders accounting for the remaining 8%: see paragraphs 237–245.

11 In shopping around for a home loan, consumers have several options, including:

(a) speaking directly to the lender;

(b) using the services of a broker; or

(c) using online services (e.g. the lenders' own website or comparison websites).

12 Our review included an assessment of the remuneration paid in each of these distribution channels. In addition, it included a review of the remuneration being paid by to those who merely refer consumers to lenders (known as 'referrers') including lawyers, accountants and other service providers.

13 In this report, in describing the commission payments, bonus payments and soft dollar benefits received by brokers and others, we may refer to these payments or benefits being 'conflicted' or creating 'conflicts of interest'. In this sense, we are using the everyday meaning of those terms rather than a special legal meaning.

14 An important question that we considered in preparing for this review was what consumers expected of brokers. For example, do consumers expect the broker to shop around for the loan among a large number of or even all available lenders? Are consumers looking to get the cheapest available loan or the loan with the most features?

The role of aggregators

Within the mortgage broking market, businesses known as 'aggregators' act between brokers and lenders by providing technology and administrative support (e.g. facilitating the processing of applications and providing training and professional development programs for brokers).

Brokers also rely on aggregators because they have contractual arrangements with lenders, which allow the brokers operating under the aggregator to arrange loans from those lenders. Lenders that have these arrangements with aggregators are considered to be on the aggregator's 'panel'. If a lender is not on an aggregator's panel a broker (linked or working through that aggregator) will generally be unable to place business with that lender.

Aggregators play an important role in the industry, even though many consumers would not be aware of their existence:

- Many brokers operate under the Australian credit licence (credit licence) of an aggregator, rather than holding their own licence. In such cases, the aggregator is responsible for the conduct of the broker under the *National Consumer Credit Protection Act 2009* (National Credit Act).

> - Lenders generally pay commissions to aggregators, rather than directly to brokers. Aggregators charge their brokers for their services.
> - Broker businesses and brokers usually have arrangements with only one aggregator.
>
> The role of aggregators is explained in more detail in Section B.

15 In conjunction with this review, we undertook quantitative research through a consumer survey to understand what consumers look for in a broker. The two most common responses were that the consumer was looking to the broker to access a wider range of loans and to get a better deal. For consumers who had recent experience with a broker or who intended to use a broker in the near future, almost 60% considered that the broker could get them a better deal than going directly to the lender.

16 Under the current law, brokers are required (as are lenders) to ensure that the loan recommended to the consumer is 'not unsuitable'. Whether loans result in good consumer outcomes is a broader concept than whether the home loan is 'not unsuitable' for a particular consumer. As a result, our review examined consumer outcomes in a broader context.

17 In addition, our review also sought to understand the impact of current remuneration and ownership structures within the mortgage broking market on competition between lenders and brokers (with the resultant pressure on price and quality of product).

The importance of the broker channel

18 Brokers play a very important role in the home loan market. They are responsible for arranging around half of all home loans in Australia. Consumers are increasingly turning to brokers to get help in obtaining a home loan—in 2012 brokers arranged 47.7% of home loans for the lenders in our review. In 2015, this increased to 54.3%.

19 Brokers arranged almost 520,000 new home loans from the lenders in our review in 2015 (compared to 340,000 in 2012).

20 Brokers can play an important role in promoting good consumer outcomes and strong competition in the home loan market.

21 From a consumer outcomes perspective, in a well-performing market brokers can help:

(a) match the needs of the consumer with the right home loan product and lender;

(b) navigate the home loan application process, which can be daunting for many consumers; and

(c) improve consumer understanding of home loans and financial literacy.

22 From a competition perspective, brokers have the potential to:

(a) play a valuable role in providing a distribution channel for lenders—especially smaller lenders—without their own distribution network (e.g. branches);

(b) exert downward pressure on home loan pricing, by forcing lenders to compete more strongly with each other for business.

23 Remuneration and ownership structures can, however, inhibit the consumer and competition benefits that can be achieved by brokers. In setting out our findings, we have made a number of proposals to improve consumer outcomes and competition: see paragraph 112. These proposals should strengthen the positive contribution that brokers provide in this sector. Some of the proposals also aim to improve the operation of the home loan market more generally.

24 We also consider that our proposals will improve the trust and confidence that consumers can have in brokers.

Key findings

25 In this summary, we set out 13 separate findings from our review. Some of our findings relate specifically to the broker channel. Other findings relate to the market as a whole (i.e. to loans sold through brokers and the lenders' own direct channels).

Finding 1: The standard commission model is almost universal

26 Brokers almost universally receive commissions paid by the 'supply side' of the market (i.e. the lender or aggregator), rather than by the consumer. Our review identified significant variability and complexity in remuneration structures between industry participants. The common element across all remuneration structures for brokers, however, was a standard commission model made up of an upfront and a trail commission.

27 Based on the information collected in this review, lenders paid approximately:

(a) $1.42 billion in upfront commissions on $175 billion of home loans in 2015 (compared to $729 million on $98 billion of home loans in 2012); and

(b) $984 million in trail commissions on an average outstanding balance of $545 billion of home loans in 2015 (compared to $733 million on an average outstanding balance of $380 billion of home loans in 2012).

Note: Figures are based on lenders' loan flow data for 20 aggregators (the 14 aggregators in this review plus an additional six): see paragraphs 1057–1058. These amounts may include amounts paid under bonus commission arrangements (see paragraph 37) as lenders were generally unable to separate those payments from standard commission payments.

28 For a $500,000 home loan, a typical upfront commission of 0.62% would result in a payment by the lender of $3,100 to the aggregator. Typically a trail commission of 0.18% would also be paid by the lender to the aggregator, amounting to around $900 in the first year, and declining each year as the consumer pays down home loan. The aggregator would take some of this commission and pass the rest on to the broker business. On average, the broker business would receive upfront commission of 0.54% and trail commission of 0.14%.

29 This standard model of upfront and trail commissions creates conflicts of interest. There are two primary ways in which these conflicts may become evident. Firstly, a broker could recommend a loan that is larger than the consumer needs or can afford to maximise their commission payment. This may also involve recommending a particular product or strategy to maximise the amount that the consumer can borrow (e.g. through the choice of an interest-only loan). In this report, we have referred to this as a 'product strategy conflict'. Alternatively, a broker could be incentivised to recommend a loan from a particular lender because the broker will receive a higher commission, even though that loan may not be the best loan for the consumer. We refer to this as a 'lender choice conflict'.

30 We found that commissions may be paid in a way that could result in product strategy conflict. In general, because commissions are linked to the size of the loan, the more that a consumer borrows, the more the broker will be paid. In practice, we found it common for remuneration structures to pay commission on the total amount of borrowing approved, rather than the amount of funds actually drawn down.

31 We found that loans provided through the broker channel are on average larger and have a higher loan-to-valuation ratio (LVR) than loans provided directly through lenders: see Finding 5.

32 We also found that the standard commission structures are likely to result in a higher level of lender choice conflict as there is significant variability in the value of commissions paid by different lenders. Even when limiting our review to the commission rates paid only by ADIs, the differences in rates of upfront commission paid to individual broker businesses tended to vary between lenders by at least 0.10%, while variations of up to 0.30% were not uncommon. An increase of 0.10% commission on a $500,000 loan equates to an extra $500 paid to the broker business. These differences were also evident for trail commissions, where variations in the rates of commission tended to be between 0.05% and 0.15%.

33 The standard commission model also had the following features:

(a) *Clawback arrangements*—Most lenders had clawback arrangements in place if a loan did not continue for a certain minimum period (commonly two years, known as 'the clawback period'). These arrangements are designed to discourage brokers from refinancing (or 'churning') consumers to a new lender (since the broker can potentially earn a new upfront commission with a new lender, adding costs to lenders and ultimately consumers). If a loan is refinanced or paid out within the clawback period, the lender will recover some or all of the upfront commission paid to the aggregator, who will then recover the commission from the broker. We found that lenders typically recovered between 4% and 10% of upfront commissions as a result of their clawback arrangements.

(b) *Discounts on interest rates*—In some cases, the broker's commission could be negatively affected if they arranged a further (non-advertised) discount on the interest rate to be paid by the consumer. This creates a clear conflict of interest.

34 This commission model did not apply to staff employed by lenders in our review; however, such staff did receive bonus payments: see Finding 2.

35 We consider that changes could be made to the standard commission model to reduce the risk of brokers seeking to inappropriately maximise their commissions. We recommend that a further review is conducted in three to four years to determine whether further (and more fundamental) changes to the standard model are required.

36 We also consider that other remuneration arrangements in addition to this model are even more likely to create conflicts of interest and increase the risk of poor consumer outcomes: see Findings 2 and 3.

Finding 2: Brokers are paid bonus commissions *and* lenders' staff are paid bonus payments

37 In addition to receiving upfront and trail commissions for each individual loan they arrange, aggregators also receive bonus commissions from lenders which can be passed on to brokers. The two main types of bonus commissions are as follows:

(a) *Volume-based commissions*—Lenders may pay these commissions to aggregators for reaching a target in loan settlements over a particular period (e.g. a month or year), which means the closer the aggregator gets to the target, the greater the incentive they have to write additional business for that lender. This creates conflicts of interest for either the aggregator, which is in a position to influence the products recommended by the broker (see, for example, paragraphs 257–261) or, if the commission is passed on, for the broker.

(b) *Campaign-based commissions*—These additional commissions paid by lenders or aggregators on top of the usual upfront and trail commissions can create a stronger incentive (and conflict of interest) for a broker to recommend a loan from a lender that is offering extra commission.

38 The data we obtained shows that bonus commissions may affect broker behaviour. For example, for one lender offering higher commissions for a limited period, the volume of home loans sold increased by a factor of over four.

39 Payment of bonuses to staff is an area of similarity in remuneration for the broker channel and lenders' staff. The value of bonuses for some major bank staff can be very high—both in absolute dollar terms (e.g. we saw bonuses of over $300,000), but also relative to the person's base salary (e.g. bonuses could be more than 200% of the person's base salary). Lenders' staff can also be remunerated for each loan they sell, although their overall bonus payment may also be influenced by other factors (e.g. customer satisfaction metrics).

40 Bonus commission and bonus payments supplement the standard incentives that are in place, including by strengthening the incentives to place consumers in larger loans. Given the additional conflicts of interest created by bonus commissions and bonus payments, we are concerned that they may be leading to some of the poor consumer outcomes described in this report.

41 To reduce conflicts of interest and the risk of poor consumer outcomes, we propose that the industry moves away from bonus commissions in the broker channel and bonus payments to lenders' staff: see Proposal 2.

Finding 3: Soft dollar benefits are widely used in the broker channel

42 In addition to monetary commissions, brokers also receive soft dollar benefits from lenders and aggregators. The main types of soft dollar benefits are as follows:

(a) *Loyalty programs*—These programs (known as 'broker clubs') are made available to brokers depending on their loyalty to the lender (i.e. the amount of business a broker directs to a lender). Like other types of loyalty programs, membership of broker clubs can be tiered (e.g. silver, gold or platinum membership—much like an airline frequent flyer program) according to how much business a broker directs to a lender. This further exacerbates a broker's conflicts of interest. The types of benefits that brokers receive in broker clubs include improved service levels from the lender, better commission rates and access to hospitality.

(b) *Travel and hospitality-related benefits*—We reviewed examples of overseas travel benefits, including travel to overseas conferences to locations such as the Caribbean, Los Angeles and Hawaii, which were worth several thousand dollars to the brokers attending and cost over $1 million for the aggregator.

43 As with bonus commissions, we consider that the provision of soft dollar benefits is likely to be a significant motivator for brokers to send loans to a lender to qualify for those benefits even where the choice of lender may not be in the consumer's interest (i.e. lender choice conflict). This may include placing consumers in larger loans (i.e. product strategy conflict) and lead to poor consumer outcomes described in this report.

44 The conflict from broker clubs may be direct; such as higher commission rates directly incentivising the broker to recommend the lender's home loans. It may also be indirect; for example, improved service levels will allow the broker to have more loans approved by the lender in a shorter time, which will result in more commission being paid to the broker.

45 We found that soft dollar benefits are more often offered by larger lenders: see Finding 9.

46 To reduce conflicts of interest and the risk of poor consumer outcomes, we propose that the industry moves away from soft dollar benefits: see Proposal 3.

Finding 4: Consumers who use brokers are different to consumers who go directly to lenders

47 The raw data we collected showed that there are clear differences in the types of consumers going to brokers compared to those going directly to lenders. For example, consumers going through a broker tended to:

(a) be younger by about two years; and

(b) have incomes that were around $6,000 lower.

48 The differences in types of consumers using each distribution channel could, on their own, create different consumer outcomes.

Note: It was not part of this review to understand why these differences in borrower characteristics were exhibited; we may explore this in our follow-up work.

49 For this reason, we applied statistical analysis (or 'controls') to the raw data to allow for more meaningful comparisons ('apples with apples') to be made across distribution channels. If a particular finding points to different consumer outcomes across the two main distribution channels, the use of controls means that the different outcomes are not likely to be caused by the differences in types of consumers using each distribution channel.

50 In describing our findings on the borrower characteristics of consumers who use brokers or go directly to lenders (and the loans obtained through these channels), we indicate whether the findings are based on the raw data we collected or the controlled data.

Finding 5: Loans obtained through brokers are larger, and more likely to be interest-only

Larger loans and higher LVRs

51 Even after controlling for differences, compared to consumers going directly to lenders, we found that consumers going through broker channels obtained:

(a) loans with higher LVRs (typically between 1 and 4%, depending on the lender); and

(b) larger loans in dollar terms.

52 These findings take into account many of the differences in characteristics of consumers who use brokers and those who go directly to lenders. Based on the raw data alone, the broker channel produces even higher LVRs (average of 12.7% higher across lenders in 2012, and 7.1% higher in 2015), and even higher loan amounts (9.4% higher in 2012, 7.4% higher in 2015).

More interest-only loans

53 Even after controlling for differences, compared to consumers going directly to lenders, we found that consumers going through broker channels obtained significantly more interest-only loans: for all eight lenders reviewed, brokers arranged at least 50% more interest-only loans, and up to four times as many interest-only loans in the case of one lender.

54 All other things being equal, loans with higher amounts, and/or interest-only terms will cost the consumer more in interest and may take longer to pay down. Whether or not this is a poor consumer outcome depends on whether the loan met the consumer's requirements and objectives and did not result in the consumer experiencing financial hardship. For example, if a consumer is placed in a larger loan than they needed, this is clearly a poor consumer outcome (and may also breach responsible lending laws).

55 ASIC has recently released two reports following an industry-wide review of interest-only home loans: see Report 445 *Review of interest-only home loans* (REP 445) and Report 493 *Review of interest-only home loans: Mortgage brokers' inquiries into consumers' requirements and objectives* (REP 493). These reviews have resulted in improvements to industry standards that will not be reflected in these findings.

56 We will continue to monitor this issue as part of our ongoing work. We also consider that the improvements to remuneration structures we are proposing could have a positive impact on this finding: see Proposal 1.

Finding 6: Interest rates are not different between distribution channels

57 We tested the interest rate that applied when loans were sold to see if brokers were obtaining better-priced loans (anecdotal feedback to us suggested this might be the case and our consumer research indicated that many consumers consider that brokers get a better deal than going to the lender directly). The data we obtained did not show a consistent trend that brokers obtained either cheaper loans or more expensive loans.

58 This was the case in the raw data and also when we controlled for differences in the types of consumers using the two channels and the features of the home loan. When we controlled for differences, some lenders provided brokers with slightly cheaper loans while others provided cheaper non-broker loans. In either case, the differences were small.

Finding 7: Lenders *and* brokers did not make sufficient inquiries into consumers' expenses

59 We obtained information from lenders about the level of consumer expenses provided to lenders by brokers, or directly to lenders. The responses were consistent with concerns that ASIC has previously raised about lenders and brokers not making sufficient inquiries into consumers' expenses, although as we discuss later, more recent improvements will not be reflected in these results.

60 We tested the adequacy of lenders and brokers' assessments of consumer expenses by reviewing the distribution of expense figures across loans. Many lenders test consumers' nominated expenses against a benchmark, such as the Household Expenditure Measure (HEM). HEM is a conservative measure of expenditure, rather than a typical or average figure, which means that many consumers will have higher expenses than HEM.

61 We identified significant numbers of loans across several lenders where the consumer expenses were stated to be equal to the HEM benchmark. While lenders and brokers may be able to use benchmarks such as HEM as part of their process for verifying consumers' expenses, they are still required to make inquiries into the consumer's actual expenses. The proportion of loans we reviewed where the consumer's expenses were equal to or very close to the HEM benchmark suggests that these inquiries were not occurring properly.

62 Our recent review in REP 445 of responsible lending obligations in relation to interest-only home loans addressed the way in which benchmarks are used and inquiries about consumer expenses are made. This review has resulted in improvements to industry standards that will not be reflected in these findings. Since the publication of REP 445, ASIC has been working with lenders to improve the inquiries and verification of expenses.

63 The Australian Prudential Regulation Authority (APRA) has also amended its residential mortgage lending standards to provide more detailed guidance on the estimation of living expenses and compliance with responsible lending requirements: see Prudential Practice Guide APG 223 *Residential mortgage lending*. In addition to ASIC and APRA's work on improving home lending standards, the industry has been working on an initiative to improve how information about a consumer's expenses is collected.

64 We will continue to monitor this issue as part of our ongoing work.

Finding 8: For some lenders, loans provided through brokers are more likely to go into arrears than loans provided directly to consumers

65 We considered whether broker loans performed better or worse than non-broker loans from a repayment perspective. We measured this by assessing whether the loan had ever gone into arrears by 30 days and by 90 days.

66 Based on the raw data, we found that loans through brokers were more likely to have gone into arrears by both 30 days and 90 days. However, this finding was reduced (and for some lenders no longer apparent) after controlling for differences in consumers between the distribution channels.

67 The largest difference after controlling the data was a 25% greater chance of a broker loan entering 30 day arrears, while for some lenders the differences were much smaller (or no longer present). Put another way, the largest difference in outcomes (when controlling the data) means that an arrears rate of 1% in the direct channel would be an arrears rate of 1.25% in the broker channel.

68 Similarly, the raw difference in 90 days arrears for loans issued in 2012 was reduced or, for some lenders, removed after controlling for differences in consumers between distribution channels. However, for one lender, there was still a 25% greater chance of a broker loan entering 90 days arrears. For a more detailed discussion of this finding, see Section F.

69 We also assessed the value of additional payments made by consumers to the loan (i.e. as an indication of their capacity to pay more than the current required payments if interest rates increased). We measured this in two ways: one which included the value of the offset balance and one which did not include the offset balance.

70 On both measures, the raw data showed that, for most lenders, consumers with loans through brokers made less additional payments on the loan. After we controlled the data, on both measures the difference was less pronounced but still evident for most lenders: see Section F.

71 We consider that the proposed improvements to remuneration structures (see Proposal 1) and recent improvements to lending standards should have a positive impact on this finding. We will monitor this issue as part of our ongoing work.

Finding 9: Competition in the home loan market is affected by ownership and the limited ability of some lenders to access and remunerate brokers

72 Our review identified that competition in the home loan market is affected by ownership relationships between lenders and aggregators and the inability of smaller lenders to access or remunerate brokers in the same way as larger lenders.

73 Within consumer markets, better outcomes are usually seen where businesses compete with each other by offering the best product or service at the best possible price to the consumers, rather than competing with each other to offer better incentives to the distributors of their products.

74 In the home loan market, this means that lenders should be primarily competing on the best home loan and customer service, rather than competing by offering higher commissions to aggregators and brokers.

Ownership structures

75 Ownership by lenders of aggregator businesses is a form of vertical integration, where the manufacturer of the product (the home loan) also owns the distribution network for the product (aggregators). Given the role that aggregators play between lenders and brokers, the ownership of the aggregator will have an impact on brokers.

76 In reviewing the impact of ownership structures, we considered all loans funded by a particular lender—that is, loans that carry the lender's brand, as well as loans that may be branded by the aggregator but funded by the lender (known as 'white label' loans).

77 Three lenders in our review had ownership stakes in one or more aggregators: National Australia Bank (NAB), Commonwealth Bank of Australia (CBA) and Macquarie Bank (Macquarie).

NAB

78 NAB owns three large aggregator businesses—Finance & Systems Technology, Professional Lenders Association Network and Choice Aggregation Services: see Section B. NAB's market share of home loans provided by brokers who are associated with NAB-owned aggregators is higher than its overall market share. Based on loan flow data from 2015, brokers associated with each of the NAB-owned aggregators directed

approximately 22% of home loans to NAB-branded or NAB-funded white label home loans, in comparison with NAB's overall (both NAB-branded and NAB-funded) market share of 13.2%.

Note: These figures are based on loan flow data obtained by ASIC for 2015 (see Appendix 1).

79 For each of the NAB aggregators, the additional loan flow sent to NAB (compared to NAB's average flow from all aggregators) largely resulted from the sale of NAB-funded white label loans by the aggregator. That is, while the value of NAB-branded loans sold by the aggregators was consistent with the industry average, the aggregators also sold significantly more NAB-funded white label loans.

80 NAB also has white label arrangements with aggregators that it does not have an ownership stake in. Among the non-owned aggregators, the share of the aggregators' loan flow from NAB-funded white label home loans was much smaller than that of NAB's owned aggregators; ranging between 0.3% and 2.3% (compared to between 8% and 10% for NAB-owned aggregators): see Table 10. Some of the white label arrangements with those non-owned aggregators were new in 2015 and loan flows may not have reached their potential levels.

CBA

81 CBA has a controlling ownership stake in Aussie Home Loans and a minority stake in another large aggregator, Mortgage Choice:

(a) *Aussie Home Loans*—Taking into account both CBA-branded and CBA-funded home loans provided through brokers who are part of Aussie Home Loans, CBA's market share through Aussie Home Loans was 37.3%, compared to its overall market share of 20.9%. As with NAB, most of the additional loan flow sent to CBA by Aussie Home Loans resulted from the sale of CBA-funded white label loans.

Note: CBA-funded loans include Bankwest loans and Aussie Home Loans-branded products.

(b) *Mortgage Choice*—In contrast to Aussie Home Loans, brokers that are part of Mortgage Choice directed 25.1% of loan applications to CBA-branded, which is more than CBA's overall market share of 20.9%. There were no white label arrangements between CBA and Mortgage Choice.

82 CBA did not have white label arrangements with any non-owned aggregators in this review.

Macquarie

83 Macquarie had varying ownership stakes in a number of aggregators, including Yellow Brick Road, Connective, Vow and Australian Finance Group (AFG). Its market share of home loans provided by brokers who are part of these businesses varied considerably, but was significantly higher for some of those businesses than its overall market share. For Yellow Brick Road, Macquarie's market share was 23.4%, which was significantly higher than its overall market share of 4.8%; made up entirely of Macquarie-funded white label loans.

Note: Macquarie sold its interest in AFG in September 2016. See paragraph 808 about the business model of Yellow Brick Road.

84 While the findings for Macquarie were mixed, overall there is evidence from the data for 2012–15 that ownership structures—particularly when combined with white label arrangements—have an impact on loan flows in the home loan market.

Brokers' choice of lenders

85 An aggregator can play an important role in promoting competition in the home loan market by maintaining a large and varied selection of lenders on its panel. We found that, on average, the aggregators in our review sent loans to 29 lenders.

86 However, in practice, we found that broker businesses tended to recommend loans from a much smaller number of lenders. We found that individual broker businesses had four preferred lenders, which received 80% of loans (by value) from that business.

Note: Those four lenders were different between broker businesses.

87 What a 'selection of lenders' means is also an important issue. An aggregator may offer what appears to be a large selection of lenders on its panel. However, in practice, the number of lenders actually providing home loans to consumers through the aggregator may be significantly less than the number of home loan products (or home loan 'brands') on the aggregator's panel. For example, while an aggregator such as Aussie Home Loans may have CBA-branded loans, Aussie Home Loans-branded loans and Bankwest-branded loans on its panel, all three of these brands are funded by the same lender (CBA).

Ability of smaller lenders to compete

88 Customer-owned banking institutions (e.g. mutual banks, credit unions and building societies) appeared on far fewer aggregators' panels, both across the 20 largest aggregators and in total. This may reflect a number of factors, including the cost and/or resources required from lenders to join a panel or the

choice of an aggregator to limit its panel to a selection of lenders. On this basis, the customer-owned banking institutions will have access to fewer brokers.

89 The reduced access to aggregators' panels by customer-owned banking institutions is compounded by the fact that, even where a smaller lender is on an aggregator's panel, remuneration structures—in particular bonus commissions and soft dollar benefits—make it hard for smaller lenders to compete with larger lenders. We found that volume-based commissions (i.e. above the standard commission payments) are generally paid by larger lenders and that the main broker clubs are also provided by larger lenders.

90 In contrast, we found that campaign-based commissions were generally offered by lenders other than the major banks. While those smaller lenders can increase home loans sales through such offers, we are concerned if this is occurring because of stronger conflicts of interest.

91 We consider that the improvements to remuneration structures we are proposing and a new public reporting regime could improve competition in the home loan market: see Proposal 5.

Finding 10: Lenders provided bigger loan discounts for new loans in 2015 compared with 2012

92 In reviewing the data we obtained for over one million loans provided in 2012 and 2015, we compared the actual interest rates paid by consumers for these loans.

93 It is common in Australia for lenders to have a 'standard variable rate' (SVR) home loan and provide a margin discount off the SVR to consumers. The discount is fixed and applies for the life of the loan. These discounts may be advertised or be negotiated on a case-by-case basis and may be tiered depending on the value of the home loan and other borrower characteristics.

94 Lenders may adjust their variable home loan interest rates by changing their SVR, or through changes in advertised or unadvertised discounts. Changes to the SVR flow through to existing loans linked to the SVR in a uniform manner, but the actual rate paid will depend on the discount obtained by the consumer when they first obtained the loan.

95 As a result of this pricing model, lenders can compete for market share by varying the level of discount off the SVR for different segments of new borrowers. Providing a higher or lower level of discount for new borrowers means that the interest rate for existing borrowers is not affected (unless these borrowers refinance elsewhere).

96 We found that lenders have been offering new borrowers better discounts than existing borrowers. In 2015, two of the largest lenders in Australia

provided home loans that had, on average, approximately a 0.25% larger discount than loans provided in 2012.

> Note: This finding is consistent with analysis by the Reserve Bank of Australia (RBA). See, for example, RBA, Handout prepared for House of Representatives Standing Committee on Economics, 22 September 2016.

97 We are concerned that consumers with existing home loans:

(a) may not be aware that they will benefit from refinancing their home loans; or

(b) even if they are aware, may be reluctant to refinance due to the cost, time and inconvenience involved.

98 We consider that a new public reporting regime could improve outcomes for consumers by providing greater transparency around pricing for new and existing loans: see Proposal 5.

Finding 11: Those who merely refer consumers to lenders are paid almost as much as brokers, despite doing much less than brokers

99 Mortgage referrers are individuals or businesses that provide a referral service to lenders or brokers. Some of the most common referrers are real estate agents, financial planners, accountants and lawyers. However, referrers may also include other types of individuals and organisations, including property developers and non-profit organisations.

100 We found that referrers are paid almost as much as brokers. Like brokers, they receive an upfront commission when a loan application is successful. On average, lenders paid 0.46% of the loan amount as an upfront commission, although for some groups of referrers this was as much as 0.56%

101 This level of commission-based remuneration is paid even though referrers play a very limited role. The referrers we reviewed all operated under a licensing exemption. Under this exemption, they are permitted to merely refer a consumer to a lender, and in doing so they are required to disclose what remuneration they may receive. They cannot provide advice to consumers, or assist them in applying for a home loan. Referrers are also not subject to the responsible lending conduct obligations in the National Credit Act.

102 The remuneration paid to referrers may give them an incentive to do more than they should to ensure that the loan application is successful and they receive their commission. ASIC has been separately investigating a number of cases where referrers have acted improperly in assisting consumers to apply for credit (including the falsification of payslips).

103 We propose that the remuneration for referrers be reviewed by lenders to ensure that it is not leading to poor outcomes. We will follow up with

lenders to ensure that they are properly managing risks with referrers. We also propose that lenders significantly increase their governance and oversight of the referrer channel as for brokers to ensure that misconduct is not occurring: see Proposal 6.

Finding 12: Governance and oversight need to be improved

104 ASIC is particularly interested in the governance frameworks of lenders, aggregators and broker businesses to support consumer-focused culture and the reward and incentive structures in the home loan market.

105 We found that the design and review of remuneration and governance structures in this market (both for lenders' direct channels and the broker channel) do not focus sufficiently on the conduct of brokers or lenders' staff dealing directly with consumers, or on the quality of consumer outcomes.

106 This was particularly exhibited through:

(a) a lack of consistent governance structures to incorporate a consumer focus in the design of incentive schemes and to identify specific features of incentive schemes that may increase the risk of mis-selling home loans;

(b) a focus on a portfolio view of negative loan performance rather than on individual consumer outcomes; and

(c) a lack of measures to deal with misconduct and poor practices of brokers and lenders' staff

107 We propose that lenders and aggregators improve their governance and oversight of individuals who sell home loans, and place greater importance on fostering a consumer-centric culture: see Proposal 6.

Finding 13: Data quality and public reporting

108 We encountered a series of significant issues with the availability and quality of key data sought from participants in this review, which affected our ability to analyse the data for some of our core review objectives. It also raises concerns with the participants' ability to monitor consumer outcomes in relation to their businesses.

109 Lenders could not generally automatically track whether a particular loan was arranged by a particular individual broker or broker business. This had the following flow-on effects:

(a) Lenders did not have systems that allowed them to readily track the amount of remuneration paid to individual brokers, or whether remuneration was paid to particular brokers.

(b) Lenders did not have systems that allowed them to readily track the amount of soft dollar benefits provided to individual brokers and there was no reporting to the relevant aggregator of the soft dollar benefits provided by lenders to the individual brokers.

(c) Lenders could not readily provide ASIC with details such as the credit licence number or authorised credit representative number of these individuals or businesses, or the information provided was incorrect or outdated. This increases the risk that lenders may be dealing with unlicensed persons and also makes it easier for problematic individuals in the industry to move from one employer to the next without consequences.

(d) Lenders could not provide ASIC with home loan data or consumer outcomes for individual brokers or broker businesses. This means that lenders have little visibility of patterns of poor loan performance connected to these individuals or businesses.

110 We also found that there is little data available to the public that provides consumers with information relevant to market outcomes across different distribution channels.

111 We consider that in order to improve governance and oversight of individuals who sell home loans (see Proposal 6) industry participants must improve the availability and quality of data. We also propose that, in order to improve transparency in the mortgage broking market, there be a new public reporting regime: see Proposal 5

Proposals for consultation to improve consumer outcomes

112 We have put forward six proposals to improve consumer outcomes and competition in the home loan market, including:

(a) changing the standard commission model to reduce the risk of poor consumer outcomes;

(b) moving away from bonus commissions and bonus payments, which increase the risk of poor consumer outcomes;

(c) moving away from soft dollar benefits, which increase the risk of poor consumer outcomes and can undermine competition;

(d) clearer disclosure of ownership structures within the home loan market to improve competition;

(e) establishing a new public reporting regime of consumer outcomes and competition in the home loan market; and

(f) improving the oversight of brokers by lenders and aggregators.

113 We consider that these proposals should be implemented before a further review of the market is conducted in three to four years to determine whether additional changes are required.

114 We also propose to conduct a targeted review of the suitability of advice provided by brokers (including through a shadow shopping exercise) commencing in 2017.

Proposal 1: Improving the standard commission model

115 The standard commission model of upfront and trail commissions could encourage brokers to place consumers in larger loans, even when this may not be in the interests of the consumer. To reduce the risk of this occurring, we propose that lenders change their standard commission arrangements so that brokers are not incentivised purely on the size of the loan.

116 For example, lenders could reflect the LVR of the loan (and other considerations such as compliance metrics) in how they calculate upfront and trail commissions. We also propose that lenders do not structure their incentives in a way that encourages the creation of larger loans that initially have large offset balances.

117 We note that the Australian Bankers' Association (ABA) is currently conducting a review of incentives paid to both staff and third parties. In its media release, the ABA stated:

> Building on the 'Future of Financial Advice' reforms, we will immediately establish an independent review of product sales commissions and product based payments with a view to removing or changing them where they could lead to poor customer outcomes. We intend to strengthen the alignment of remuneration and incentives and customer outcomes. We will work with regulators to implement changes and, where necessary, seek regulatory approval and legislative reform.

Note: See ABA, 'Banks act to strengthen community trust', 21 April 2016.

118 The ABA review, which is being conducted by Stephen Sedgwick AO, provides an opportunity for the banking industry to re-consider the standard commission model. The ABA and other stakeholders—including other lenders and brokers—should consider how they can work together to respond to this proposal.

Proposal 2: Moving away from bonus commissions and bonus payments

119 While bonus commissions and bonus payments do not necessarily cause poor consumer outcomes, they are a form of remuneration structure that creates a higher risk that brokers will place consumers with lenders for the wrong reasons.

120 Bonus commissions have raised concerns in other parts of the financial services industry. The prohibition on volume-based commissions introduced by the Future of Financial Advice (FOFA) reforms is now being extended to life insurance as part of the Government's reforms to life insurance commissions.

121 We consider that the risks posed by bonus commissions (e.g. volume-based commissions) in other parts of the financial services industry also apply in the home loan market. Accordingly, we propose that the industry moves away from bonus commissions and bonus payments.

122 The ABA review provides an opportunity for the banking industry to act on this proposal.

Proposal 3: Moving away from soft dollar benefits

123 Soft dollar benefits also increase the risk of poor consumer outcomes. Like bonus commissions, soft dollar benefits have been prohibited in other parts of the financial services industry under the FOFA reforms. We therefore propose that the industry moves away from giving soft dollar benefits.

124 We consider that the ABA review of incentives also provides an opportunity for the banking industry to act on this proposal.

Proposal 4: Clearer disclosure of ownership structures

125 To reduce the impact of ownership structures on competition in the home loan market, we propose that participants in the industry more clearly disclose their ownership structures. This proposal is consistent with the findings and recommendation of the Financial System Inquiry to:

> Rename 'general advice' and require advisers and mortgage brokers to disclose ownership structures.
>
> (Recommendation 40) (*Financial System Inquiry final report*, p. 271)

126 We consider that clearer disclosure of ownership structures should extend beyond mortgage brokers and apply to all players in the home loan distribution chain, including lenders, aggregators, and brokers.

127 Clearer disclosure should occur in marketing material and at all distribution points (e.g. websites and physical premises).

Proposal 5: A new public reporting regime

128 To improve transparency in the mortgage broking market, we propose that there be public reporting on:

(a) the actual value of remuneration received by aggregators and the potential value if all criteria for remuneration are satisfied;

(b) the average pricing of home loans that brokers obtain on behalf of consumers;

(c) the average pricing of home loans provided by lenders according to each distribution channel; and

(d) the distribution of loans by brokers between lenders to give consumers a better indication of the range of loans that brokers within the network offer.

Proposal 6: Governance and oversight

129 To reduce the risk that remuneration structures may result in poor consumer outcomes and inhibit competition, there is a need for all industry participants to place greater importance on fostering a consumer-centric culture and take more care in the design and monitoring of remuneration structures.

Design of remuneration structures

130 We expect lenders, aggregators and broker businesses to embed the principle of obtaining good consumer outcomes as a guiding factor in the design of their remuneration arrangements (both in the broker channel and in relation to their own staff).

131 We also expect aggregators to recognise that, as the party that passes commissions from lenders to brokers, they are well placed to ensure that such remuneration is consistent with the attainment of good consumer outcomes.

Oversight of brokers

132 Lenders and aggregators should improve their oversight of brokers and broker businesses.

133 We expect lenders to:

(a) require aggregators, through their relevant commercial agreements, to actively monitor the consumer outcomes being obtained by brokers and broker businesses;

(b) provide consistent reporting to aggregators to allow adequate oversight of brokers and broker businesses; and

(c) use a consistent process to identify each broker and broker business (e.g. use of the Australian credit licensee or credit representative number where relevant, or a unique number provided by the aggregator).

134 We expect aggregators to:

(a) require lenders, through their relevant commercial agreements, to provide consistent reporting to the aggregator on the outcomes obtained by individual brokers and broker businesses, including those relating to loan pricing, features, clawbacks, and refinancing and default rates;

(b) actively monitor the consumer outcomes being obtained at a broker and broker business level, including those relating to loan pricing, features, clawbacks, refinancing and default rates, and distribution of loans among lenders; and

(c) retain this information in a way that can be provided to ASIC to allow us to review outcomes across the mortgage broking market.

What we did in this review

135 In our review, we focused on the way in which commissions and other remuneration passes between each of the participants in the mortgage broking market, rather than simply considering the remuneration received by the individual broker who recommends a home loan product to the consumer. We considered that the remuneration received by other participants (e.g. aggregators and broker businesses) was also likely to influence the outcomes that consumers receive.

136 Our review covered 17 lenders (representing over 19 different brands), 14 aggregators and 44 broker businesses. Together, we estimate the lenders and aggregators each covered over 90% of the home loan market and mortgage broking market.

Lenders

137 We selected the lenders on the basis of size and diversity, ensuring that we included representation from major banks and other banks, customer-owned banking institutions (e.g. credit unions) and non-bank lenders. We categorised each lender for the purposes of this review: see Table 1.

138 The review included the sub-divisions of CBA and Westpac. Although these sub-divisions are not separate legal entities from the main bank, we treated these divisions as separate lenders as we were advised by the relevant banks that the divisions operated under separate systems and processes to the main bank.

Table 1: Lenders covered by ASIC's review

Major banks	• Australia and New Zealand Banking Group Limited (ANZ) • Commonwealth Bank of Australia (CBA) and Bankwest • National Australia Bank of Australia (NAB) and Advantedge Financial Services Pty Ltd • Westpac Banking Corporation and St George Bank (including Bank of Melbourne and BankSA)
Foreign bank subsidiaries	• ING Bank (Australia) Limited • Citigroup Pty Limited
Other banks	• Bank of Queensland Limited • Bendigo and Adelaide Bank Limited • Macquarie Bank Limited • Members Equity Bank Limited • Suncorp-Metway Ltd
Customer-owned banking institutions	• Australian Central Credit Union Ltd (People's Choice Credit Union) • Credit Union Australia Limited • Police & Nurses Limited
Non-bank lenders	• Liberty Financial Pty Ltd • Pepper Group Limited

Note: See paragraph 241 for the meaning of 'lender' as used in this report.

Aggregators

139 The aggregators covered by our review included the 10 largest aggregators, plus four of the next 10 largest. Some of these aggregators are owned or part-owned by lenders covered by our review: see Section B. We categorised each aggregator for the purposes of this review: see Table 2.

Table 2: Aggregators covered by ASIC's review

Large aggregators	• AHL Investments Pty Ltd (Aussie Home Loans) • Australian Finance Group Ltd (AFG) • Finance & Systems Technology Pty Ltd (FAST) and Professional Lenders Association Network of Australia Pty Limited (PLAN) and Pennley Pty Limited as trustee for the Pennley Unit Trust (Choice Aggregation Services) • Connective Credit Services Pty Ltd
Mid-tier aggregators	• Mortgage Choice Limited • Loan Market Pty Limited • Smartline Home Loans Pty Ltd • Vow Financial Pty Ltd (Vow)

Smaller aggregators	• Astute Financial Management Pty Ltd • eChoice Home Loans Pty Ltd • Outsource Financial Pty Limited • Yellow Brick Road Finance Pty Limited

Note: Yellow Brick Road purchased Vow in 2014.

Brokers and broker businesses

140 In recognition of the effort required by the broker businesses selected for our review, we sought to limit the number of businesses involved. We chose to review brokers from only eight of the aggregators involved in our review. From each of these aggregators, we choose two of the largest businesses, two small businesses and two other businesses.

141 In addition, we chose six additional broker businesses representing a particular business model, including businesses that used a fee-for-service or rebate model.

142 In total, we sent requests to 52 businesses. We received responses from 44 businesses, representing 198 brokers in 2015.

Comparison websites and referrers

143 Based on our desktop research, we chose four popular comparison websites to take part in this review. In addition, we included three businesses that sit between lenders and referrers (known in this report as ‘referrer aggregators’): see Section B.

Our approach to the data

144 In our review, we focused on identifying and assessing:

(a) the remuneration structures that exist in the mortgage broking market and, to provide a point of comparison, those that exist for lenders’ staff who recommend home loans to consumers;

(b) the outcomes demonstrated in the home loan market for individual home loans originated in 2012 and 2015;

(c) the outcomes demonstrated in the home loan market for the distribution of loans between lenders between 2012 and 2015;

(d) the arrangements that lenders, aggregators and broker businesses have in place to mitigate the risk that those structures will result in a conflict of interest for brokers and lenders’ staff; and

(e) the size and remuneration arrangements of comparison websites and the unlicensed referrer channel.

145 We obtained information about the operation of the participants' businesses in relation to home loans, together with a large volume of data on home loans originated in 2012 and 2015 by the lenders (home loan data) and the distribution of home loans by aggregators to lenders between 2012 and 2015 (loan flow data). See Appendix 1 for further details on our data collection process.

146 We reviewed the data on the remuneration payable in the home loan market to describe the way in which brokers, lenders' staff, comparison websites and referrers are remunerated. We also reviewed the data to describe the processes undertaken by lenders, aggregators and broker businesses to reduce the risk that those remuneration arrangements will result in poor consumer outcomes.

147 We analysed the home loan data and loan flow data to understand both the consumer outcomes arising from the performance of loans originated through brokers (using loans originated through the lenders' own proprietary channels as a comparison) and also the way in which loans are distributed between lenders by brokers.

A Background and methodology of our review

Key points

In undertaking this review, we engaged with a large number of industry stakeholders and collected a significant amount of data relating to the home loan market.

This process provided a rich source of data with which to assess how brokers are remunerated and the outcomes that consumers are obtaining with their home loans.

However, we also found that many industry participants struggled to provide some of the data that we sought, which raised concerns about those participants' ability to monitor consumer outcomes for their businesses.

Background to our review

148 In November 2015, ASIC received a written request from the then Minister for Small Business and Assistant Treasurer (now Minister for Revenue and Financial Services) to review the mortgage broking market (the review) to determine the effect of current remuneration structures on the quality of consumer outcomes. The Government requested that the review be completed by the end of 2016.

Note: In December 2016, the Minister gave ASIC a short extension to finalise the review, to manage the significant volume of data involved.

Methodology of our review

149 Appendix 1 sets out the full details of the methodology of our review. In summary, we:

(a) reviewed 82 participants;

(b) participated in approximately 100 meetings;

(c) issued 73 information requests using ASIC's formal information gathering powers;

(d) issued 52 other requests for information; and

(e) analysed 1.4 million lines of home loan data.

150 We acknowledge and appreciate the considerable time and effort review participants have invested in assisting ASIC with our review.

Participants

151 We selected approximately 100 industry participants, representing a wide range of industry stakeholders, who play key roles in the home loan end-to-end value distribution chain, to participate in our review:

(a) *Lenders*—We selected 17 lenders (representing over 19 brands). These lenders combined have a majority market share and include the major banks, a mixture of mid-tier banks, foreign banks, customer-owned banking institutions and non-bank lenders.

(b) *Aggregators*—We selected 15 aggregators. These aggregators combined have a majority market share and include a mixture of large, mid-tier and smaller aggregators, with varying ownership structures (including those owned by lenders) and licensing structures (credit representatives and licensees).

(c) *Brokers*—We selected 55 brokers. These brokers represented a cross-section of the industry, including large, mid-tier and small brokers, brokers who operate a variety of business structures (e.g. franchisee, independent contractor, fee-for-service and commission-based models), brokers with different licensing structures (e.g. credit licensees and representatives), and brokers from different geographical locations.

(d) *Comparison websites*—We selected four popular home loan comparison websites to participate in the review.

(e) *Referrer aggregators*—We selected three referrer aggregators. These referrer aggregators combined have a majority market share and represent a wide range of referral sources, including professional and non-professional businesses, clubs, schools and other non-profit organisations, and property developers.

152 We also consulted widely with other stakeholders throughout the course of the review, including, but not limited to:

(a) domestic and international government agencies, including the RBA, the Australian Competition and Consumer Commission (ACCC), APRA, Treasury, and overseas regulators;

(b) industry associations, including the Mortgage and Finance Association of Australia (MFAA), the Finance Brokers Association of Australia (FBAA), the Customer Owned Banking Association (COBA), the ABA and the Australian Finance Conference (AFC);

(c) external dispute resolution (EDR) schemes, including the Credit and Investments Ombudsman (CIO) and the Financial Ombudsman Service (FOS);

(d) new and emerging start-up, financial technology (fintech) and other mortgage-related businesses; and

(e) consumer advocates, including community legal centres, Legal Aid, and other consumer advocacy groups.

Consultation process

153 We hosted two roundtables and sought written feedback from stakeholders to help determine the appropriate scope of the review. These processes gave stakeholders the opportunity to share their ideas and insights on the scoping considerations and questions set out in our paper, *Review of mortgage broker remuneration structures: Scoping discussion paper—February 2016*.

154 At the conclusion of these processes, we finalised the scope of the review in our paper, *Review of mortgage broker remuneration structures: Final scope—May 2016*. This paper set out the review parameters along with the scoping considerations in our earlier paper.

155 In the final scope, we noted that the review parameters may shift throughout the course of the review if we considered it appropriate, necessary or in the public interest to do so. We also noted that we may consider out-of-scope items, or matters arising from this review, separately in the future.

156 The key scope items from the final scoping document are set out in Table 3.

Note: Some terms in this report may be different than those used in scoping documents.

Table 3: Key scope items

Scope item	What we will do
Participants	We will review the remuneration arrangements of all industry participants forming part of the value distribution chain. Participants will include lending institutions, aggregation and broking entities, associated mortgage businesses (e.g. comparison websites and market-based lending websites), and referral and introducer businesses.
Products	We will review the remuneration arrangements associated with the sale of residential mortgage products (including white label products) only. Other products (e.g. reverse mortgages and construction loans), which do not comprise a predominate proportion of the home lending mortgage market, are out of scope.
Channels	We will review remuneration structures across lender, broker, online, and referrer and introducer channels.
Ownership structures	We will review the ownership structures of all participant types. These structures may include fully vertically integrated businesses and other types of commercial alignments between review participants (e.g. equity stakes or licensing arrangements).

Scope item	What we will do
Remuneration structures	We will review the remuneration structures (including non-monetary benefits) that relate to the distribution of home lending products present throughout the value distribution chain. The review will predominantly focus on the remuneration arrangements of lender, aggregator, broker, and referrer and introducer staff associated with the sale of residential mortgage products.
Consumer outcomes	Consumer outcomes are multifaceted, and comprise a series of factors—such as price, product accessibility, product features, loan performance—which may vary in importance from consumer to consumer. We will focus on consumer outcomes that have the potential to be impacted by behaviour driven by different remuneration structures.
Sample size	We will review a cross-section of lending institutions, aggregation and broking entities, associated mortgage businesses, and referral and introducer businesses to provide a representative reflection of the market. Selected participants will be informed from May 2016 onwards.
Data	Where applicable, we will measure loan performance data over a five-year period.

Data availability and quality

157 We collected a significant amount of data, both quantitative and qualitative, to conduct this review. The quantitative data included information on 1.4 million individual home loans plus sales and commission information on over $550 billion of new home loans: see Appendix 1.

158 Although we collected a significant amount of data for this review, we encountered notable issues with the availability and quality of key data sought from participants. This affected our ability to perform relevant analysis for some of our core review objectives and also raised concerns with participants' ability to monitor consumer outcomes for their business.

Home loan data

159 As noted in Appendix 1, before issuing formal requests for home loan data, we undertook a pilot process with each lender participating in the review. The purpose of the pilot was to identify where existing regulatory reporting could be leveraged to minimise duplication, and identify any difficulties in the provision of particular data sets.

160 Feedback from lenders indicated the following:

(a) Over 10% of the home loan data sought was simply not available, as it was either not collected at all, or was collected but not retained in a readily accessible format. This included information relating to complaints, fraudulent activity and legal proceedings.

(b) Over 20% of the home loan data sought was collected at loan origination, but was loaded and stored electronically in legacy systems (or separate systems) which were not traditionally used for standard reporting purposes. This data required significant investment by lenders to extract it and caveats were largely placed over the data's quality.

(c) Close to 5% of the home loan data sought was collected at loan origination, but was only available from particular dates.

(d) Over 15% of the home loan data sought was deemed not applicable by lenders, who typically noted that such information was collected and held by other participants in the value distribution chain. On further investigation, we found that a substantial percentage of this subset of information was not collected or held by any review participants.

161 After we issued formal requests for information, lenders and aggregators in our review encountered further issues in extracting the information and could provide less information than originally sought.

162 For many participants, it became readily apparent that some of the data we sought (and expected would be obtained, retained and used by management in the ordinary course of their business) was not data that the participants had previously considered to be either necessary to the management of their business or required at the level of granularity that we sought.

163 For example, for many lenders and aggregators, the information sought was generally available on a loan portfolio basis, but was simply not available on a loan-by-loan basis, which affected our ability to analyse individual consumer outcomes and remuneration of individual sales personnel.

Benefits of increased data analysis

After we received the data, we were advised by some participants that they would be updating their internal management information systems to include the categories of data requested by ASIC. These participants advised that they had found the ASIC-requested data useful for their own business management purposes.

Identity of aggregators, broker businesses and brokers

164 We found that lenders had considerable problems in providing information about the identity of the aggregators, broker businesses and brokers with which they dealt.

165 In providing the home loan data, many lenders could not provide complete information about the aggregator through which a loan was provided. We recognise that this information may have been held in other systems (as the lender would need the information to process commission payments). However, for many lenders, it appears that this information is not held in a way that can be readily associated with individual home loans.

166 Lenders in the review could generally not provide details of the businesses under which an individual broker may operate. This means that lenders are unlikely to be aware of the connections between brokers who work for the same business and cannot track loan outcomes across those brokers.

167 Lenders also had difficultly providing complete and accurate information about individual brokers they had dealt with. This was shown in the home loan data and our request for details of the brokers who had membership in a broker club: see paragraphs 641–646.

168 In relation to the home loan data, most lenders could not provide the credit licence or credit representative number of the broker through whom a loan was sold: see paragraph 642. For broker clubs, some lenders either could not provide the number or provided incorrect or outdated numbers.

169 For this reason, we could not track outcomes on an individual broker basis. This would also make it difficult for lenders to undertake the same analysis.

170 The inability to provide complete and accurate data for individual brokers not only raises concerns about credit licensees' ability to retain basic information, but also to comply with their obligations under provisions such as s31 of the National Credit Act: see paragraph 184. For example, it may be difficult for a credit licensee to prove that are not conducting business with unlicensed persons when they cannot provide, or do not maintain, accurate licensing information.

Note: All references to sections in this report are to the National Credit Act, unless otherwise specified.

Remuneration data

171 The lack of complete and accurate information about individual brokers through whom loans are sold meant that we could not track the remuneration paid to individual brokers across the industry.

172 In addition to the home loan data, we sought information about other matters such as the value of soft dollar benefits given to brokers and lenders' staff. In many cases, lenders and aggregators could not provide this information as it was not recorded in a readily accessible manner: see, for example, paragraph 682.

How credit is regulated in Australia

Development of the national credit legislation

173 ASIC took over the regulation of consumer credit on 1 July 2010 under the National Credit Act (2010 credit reforms).

174 Before 1 July 2010, consumer credit was primarily regulated by the states and territories under the Uniform Consumer Credit Code (UCCC). ASIC's jurisdiction over credit was limited to the consumer protection provisions in the *Australian Securities and Investments Commission Act 2001* (ASIC Act).

175 The UCCC was developed before non-bank home lending, securitisation and the use of mortgage brokers became common features of the home loan market. As a result, it did not address many of the issues arising from these developments and, most particularly, it did not regulate the intermediary and advice role played by mortgage brokers.

176 In response to these and other issues, the 2010 credit reforms established a national consumer credit framework, administered by ASIC as the single national regulator.

177 The central elements of the credit reforms include:

(a) a licensing regime that imposes minimum standards of conduct on credit industry participants, including requirements for:

(i) competence;

(ii) mandatory membership of an ASIC-approved EDR scheme;

(iii) compensation arrangements; and

(iv) adequate compliance and risk management systems; and

Note: The licensing regime also provides mechanisms to cancel credit licences and ban persons from engaging in credit activities, thereby excluding unscrupulous operators.

(b) responsible lending obligations, which mandate that credit licensees must make inquiries into a consumer's objectives and financial situation and verify their financial situation. Credit licensees must assess this information and not provide or suggest credit to a consumer that will not meet the consumer's objectives or is unsuitable for the consumer's financial situation (i.e. the consumer will not be able to meet their financial obligations without substantial hardship).

178 Lenders must also comply with the National Credit Code (at Sch 1 to the National Credit Act), which largely mirrors the now-superseded UCCC, with some key enhancements.

179 The combination of the licensing framework and responsible lending obligations set out in the National Credit Act, and the obligations set out in

the National Credit Code, provide a robust regulatory framework for credit providers and intermediaries (including mortgage brokers)—setting out what they must do before providing credit or credit services.

Credit licensing framework

180 Chapter 2 of the National Credit Act provides the licensing framework for persons who engage in 'credit activities'. This term broadly covers:

(a) providing credit;

(b) performing the obligations, and exercising the rights, of a credit provider for a credit contract (either as the credit provider or on behalf of a credit provider); and

(c) providing credit services, which includes:

   (i) providing credit assistance (e.g. by suggesting that a consumer, or assisting a consumer to, apply for a particular credit contract with a particular credit provider); and

   (ii) directly or indirectly acting as an intermediary between a credit provider and a consumer, wholly or partly for the purpose of securing a provision of credit for the consumer.

Note 1: See Div 3 of Pt 1-2 of the National Credit Act for the full meaning of 'credit activity', and the different kinds of credit activities.

Note 2: Guidance on the credit licensing framework is set out in Regulatory Guide 203 *Do I need an Australian credit licence?* (RG 203).

181 To engage in credit activities, a person must:

(a) hold a credit licence;

(b) be able to act as a representative of another person who is a credit licensee—either as an employee or director of the licensee or of a related body corporate of the licensee, or as a 'credit representative' of the licensee; or

(c) be able to rely on an exemption from the licensing requirement (either as a principal or as a representative of another person who has the benefit of an exemption): s29.

182 The legislation does not prescribe the licence structure that needs to be adopted by a particular business. For example, a broker could:

(a) hold its own credit licence; or

(b) act as a representative of another credit licensee (e.g. an individual broker could be appointed as a credit representative of a corporate entity that operates a broader broker business, or of an aggregator).

183 Existing exemptions from the licensing requirement will not generally apply to brokers or aggregators. However, persons involved in referring consumers

to brokers, aggregators or lenders may have the benefit of an exemption that covers some referral activities: see reg 25 of the National Consumer Credit Protection Regulations 2010 (National Credit Regulations).

Note: All references to regulations in this report are to the National Credit Regulations, unless otherwise specified.

184 A credit licensee must not conduct business with another person who is contravening the requirement to be licensed. To ensure that they do not themselves commit an offence, credit licensees need to ensure that others they do business with are covered by a licence or an exemption: s31.

Credit licensee obligations

185 The general conduct obligations of credit licensees are set out in s47. These obligations include requirements to:

(a) do all things necessary to ensure that the credit activities authorised by the licence are engaged in efficiently, honestly and fairly; and

(b) 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 because of credit activities engaged in by the licensee or its representatives.

Note: ASIC guidance on the general conduct obligations is set out in Regulatory Guide 205 *Credit licensing: General conduct obligations* (RG 205).

Efficient, honest and fair

186 This obligation 'requires the licensee to conduct itself in a way that is consistent with, and reflects an appreciation of, the need to meet community standards of efficiency, honesty and fairness': see Explanatory Memorandum to the National Consumer Credit Protection Bill 2009 at para 2.110.

187 Section 180A provides an additional remedy for consumers if a credit service provider engages in unfair or dishonest conduct that results in a consumer entering into a credit contract they would not have otherwise entered into, or that has different terms to a contract the consumer would have entered into apart from the conduct. 'Engaging in conduct' is defined to include *not* performing an act, and so encompasses failing, unfairly or dishonestly, to disclose information to a consumer.

188 Section 180A outlines a number of factors relevant to determining whether particular conduct is unfair or dishonest. The list of factors is not exhaustive—conduct may be considered dishonest or unfair without the presence of any of the factors. However, if any of the circumstances outlined in s180A exist, the court must take into account those circumstances and the level to which they affected the consumer's interests.

189 The listed factors include whether the consumer was at a special disadvantage in dealing with the credit service provider, and also whether:

(a) the conduct involved a technique that manipulated the consumer or should not in good conscience have been used;

(b) the credit service provider could determine or significantly influence the terms of the credit contract; and

(c) the terms of the transaction involving the conduct were less favourable to the consumer than the terms of a comparable transaction—that is, if the consumer could have entered into a comparable transaction on more favourable terms, it suggests that entry into the less favourable contract may be a result of unfair or dishonest conduct.

Note: For a discussion of s180A, see the Explanatory Memorandum to the Consumer Credit Legislation Amendment (Enhancements) Bill 2012 at paras 2.29–2.57.

190 The Explanatory Memorandum to the Consumer Credit Legislation Amendment (Enhancements) Bill 2012 notes that:

> The power of the court to make orders to prevent the provider of credit services from profiting from their unfairness or dishonesty recognises that the provider of credit services may not be remunerated directly by the consumer, but may receive, and be motivated by, financial benefits such as commissions from third parties. The purpose of giving the court the power to require them to disgorge these payments ensures these persons should not be able to profit from unfair or dishonest conduct in situations where the consumer was not charged a fee.

Conflicts of interest

191 This obligation deals with the situation where an interest of the licensee (e.g. an incentive to earn higher commissions) conflicts with a legal obligation or duty that person has to the consumer (e.g. an obligation or duty that arises under statute, at common law, or under a contract between the licensee and the consumer).

192 Under the National Credit Act, the licensee has obligations to comply with specific requirements (e.g. the requirement to not suggest or assist a person to enter an unsuitable credit contract) and the general conduct obligations (e.g. the obligation to not engage in unfair or dishonest conduct).

193 If there is a potential conflict between these interests, the licensee must have in place adequate arrangements to ensure that clients are not disadvantaged by that conflict. In RG 205, we note that whether arrangements are adequate will depend on the particular circumstances in each case.

194 RG 205.82–RG 205.83 gives an example of circumstances in which commissions received by a broker are volume based. It notes that arrangements put in place by the broker to ensure clients are not disadvantaged by the potential conflict of interest would need to ensure that the broker and its representatives do not favour achievement of volume targets over obligations owed to their clients.

195 This may include compliance arrangements to ensure that representatives do not suggest that clients enter into an unsuitable loan. It may also include arrangements to ensure that the broker and its representatives do not engage in unfair or dishonest conduct that encourages the consumer to enter into a contract that, while not unsuitable, has less favourable terms than a comparable contract that is available to the consumer.

Note: When we refer to 'conflicts of interest' in this report, this expression should be given its ordinary meaning rather than its legal meaning (unless otherwise specified). The ordinary meaning is necessarily broader than the legal meaning.

Disclosure requirements

196 Licensees must provide consumers with information about how the persons who provide credit services to them are remunerated, including through commissions. A number of documents setting out this information are provided at different points in an application for credit.

Note: We have provided guidance on the disclosure obligations in Information Sheet 146 *Responsible lending disclosure obligations—Overview for credit licensees and representatives* (INFO 146).

197 For disclosure of commissions, the relevant documents are:

(a) *credit guide*—given by credit assistance providers, credit providers and the credit representative of those licensees;

(b) *credit proposal disclosure document* (proposal document)—given by credit assistance providers; and

(c) *pre-contractual disclosure statement*—given by credit providers.

Note 1: 'Commission' is defined in s5 as including any financial or other benefit in the nature of a commission. It can include non-monetary benefits, such as attendance at events.

Note 2: Some changes have been made to the disclosure requirements in the National Credit Regulations, including for credit assistance providers that are franchisees, product designers or mortgage managers. INFO 146 outlines these different obligations.

Credit guide

198 A credit guide must be given as soon as it is apparent that a licensee or their credit representative is likely to provide credit assistance to, or enter into a credit contract with, a consumer: s113 and 158. The purpose of this document is to give the consumer key information—about the credit licensee or credit representative, their obligations, and the consumer's rights—early in the credit transaction so the consumer is informed and aware of necessary matters before deciding to use the services of the licensee or credit representative.

Note: The requirement to provide a credit guide is analagous to the requirement in Pt 7.7, Div 2 of the *Corporations Act 2001* for holders of Australian financial services (AFS) licences and their representatives to provide a Financial Services Guide (FSG).

199 Credit guides must generally include information about any commission that:

(a) the licensee, or its employees, directors or credit representatives, is likely to receive from credit providers with whom the licensee conducts the most business; or

(b) the credit representative is likely to receive from the licensees for whom it is a credit representative.

200 Credit guides may also include a reasonable estimate of the amount, or range of amounts, of commissions and information on the method for working out those amounts. However, this more detailed information can be replaced by a statement that the licensee or credit representative has in place arrangements to make that information available and will provide it to the consumer on request: regs 27 and 27B.

201 If the licensee or credit representative has a volume-based commission arrangement with a credit provider or other person (under which the total amount of commission payable increases as the total volume of business arranged by the payee with the payer increases), the credit guide needs to include additional information about that arrangement: regs 26A(3) and 27A(4).

202 The credit guide must also state whether a commission is likely to be paid by the licensee to a third party for referring credit business or business proposed to be financed by the credit contract: regs 26A(2) and 27A(2).

203 A franchisee of a licensee that is appointed as a credit representative (which may include some brokers that have franchise arrangements with an aggregator) does not need to give a credit guide if:

(a) under the franchise agreement, they are subject to, and required to comply with, the policies of the licensee; and

(b) the credit guide of the licensee explains that the licensee takes responsibility for credit activities engaged in by the credit representative (reg 28P(1)).

Proposal document

204 A licensee that provides credit assistance must give a proposal document at the same time as providing credit assistance: s121. This document sets out the costs to the consumer of using the licensee's services, including any commissions the licensee may receive on the particular credit contract being proposed.

205 The proposal document must contain a reasonable estimate of the total amount of any commission that the licensee, or its employees, directors or credit representatives, is likely to receive on the credit contract and the method used for working out that amount. It must also contain a description of the commission that breaks down the total amount to identify and provide

a detailed description of each kind of commission (e.g. financial benefit, advertising subsidies, attendance at events), including who it will be paid to and who it will be paid by (i.e. the commission may be payable by a person other than the lender, such as an aggregator). Estimates of the amount of commission must be expressed in a way specified in reg 28G, to enable the consumer to understand the dollar value of the commission.

206 The proposal document must also state whether a commission is likely to be paid by the licensee to a third party for referring the credit business or business proposed to be financed by the credit contract. If it is, the document also needs to include details of that commission: reg 28G(6).

207 Mortgage managers do not need to include in their proposal document estimates of the amount of commission in some circumstances: regs 28H(2) and (3). The mortgage manager must tell the consumer about their agreement with the credit provider and that the mortgage manager is not acting for the consumer regarding the managed contract.

Pre-contractual statement

208 Before a credit provider can enter into a credit contract with a consumer, the credit provider must give the consumer a pre-contractual statement that includes specified details about the terms of the contract: s16 and 17(14) of the National Credit Code. The pre-contractual statement can be given in the form of the proposed contract document, or as a separate document.

209 If a commission is to be paid by or to the credit provider for the referral of credit business or business financed by the contract, the contract document and pre-contractual statement must set out who is paying and who is receiving the commission, and the amount (if ascertainable).

Note: Under the National Credit Code, ‘commission’ includes any form of monetary consideration or non-monetary consideration to which a monetary value can be assigned: see s204 of the National Credit Code. It does not include fees payable by a supplier under a merchant service agreement with the credit provider, an amount payable for a credit-related insurance contract or commission paid to employees of the credit provider: s17(14) of the National Credit Code.

Comparison with international jurisdictions

210 We compared the regulation of brokers in the United Kingdom, Netherlands and New Zealand.

211 The United Kingdom and the Netherlands responded to the impact of the 2008 global financial crisis on the home loan market with tighter lending standards, including more regulatory oversight of the broker channel. All forms of commission to brokers are now banned in the Netherlands, and trail commissions are rare in the United Kingdom and not standard practice in New Zealand.

United Kingdom

212 In the wake of the global financial crisis, the United Kingdom embarked on a regulatory review of remuneration structures in the financial services industry. As a result of this review, a number of regulatory changes were made, including banning commission payments to financial advisers and other intermediaries for investment products sold to retail clients. A separate review of the home loan market (known as the Mortgage Market Review) also led to a number of reforms, but not to the banning of commissions for mortgage brokers.

213 Instead, in April 2014 new responsible lending rules were introduced by the UK Financial Conduct Authority (FCA), including requirements for the lender to assess the affordability of the loan and to stress-test the loan for expected future interest rate rises. The reforms also outlawed 'non-advised' (or execution-only) sales of home loans to most categories of borrower.

214 The UK broker industry is currently characterised by smaller broker businesses serving a local clientele, with nearly 70% of broker businesses employing just one or two brokers. Around 50% of broker businesses are 'directly authorised' by the FCA (similar to holding a credit licence in Australia), while others are 'appointed representatives' of authorised brokers (similar to being an authorised representative of a credit licensee in Australia).

215 In an 'advised' sale, the broker or lender recommends an appropriate loan to the consumer based on their needs and is required to act in the consumer's best interests. Furthermore, as of 21 March 2016, the FCA's rules incorporate the Mortgage Credit Directive 2014/17/EU (Mortgage Credit Directive), which is the European Union framework of conduct rules for home loan providers. The Mortgage Credit Directive includes a requirement that the remuneration of home loan sales staff (whether staff of lenders or brokers) should not be contingent on sales targets, nor should remuneration structures incentivise staff to sell a given number or type of home loan.

216 In 2015, brokers were responsible for around 70% of home loan sales by value (67% by number) in the United Kingdom. This is up from around 50% in the 2009–10 financial year, after the global financial crisis.

Note: See FCA, Feedback Statement FS16/3 *Feedback statement on call for inputs on competition in the mortgage sector*, May 2016.

217 UK mortgage brokers are paid either via upfront commission from the lender, a fee for service from the consumer, or a combination of both. Fees for service paid by the consumer of between £200–500 have become more common, often together with an upfront commission paid by the lender. The typical upfront commission amount in the UK is lower than in Australia (at around 0.4% of the loan value) and, unlike Australia, there are no trail commissions.

218 The lack of trail commissions has been seen by some as a potential driver of churn in the UK home loan market, where many consumers are in short-term (often two years) fixed-rate home loans. While there is no trail commission structure, some lenders have started to introduce payments to brokers who recommend that the consumer *stay* in the product (with a re-fix of the interest rate). Before making the recommendation, the broker is required to re-assess the suitability of the loan. In 2016 approximately half of the 10 largest lenders offered such payments to brokers.

219 The FCA recently commenced a market study examining further aspects of the UK mortgage market, including outcomes for consumers according to whether they use broker or non-broker channels. One focus of the FCA's current market study is on whether the available tools (including advice from lender or broker, as well as price comparison websites and mortgage calculators) help home loan consumers make effective decisions. A second focus is on whether the commercial arrangements between lenders, brokers and others (e.g. real estate agents) lead to conflicts of interest or misaligned incentives to the detriment of consumers. The FCA plans to publish an interim report on this work in mid-2017: see FCA, MS16/2 *Mortgages market study*.

The Netherlands

220 As in the United Kingdom, the severe impact of the global financial crisis on the home loan market, together with an insurance mis-selling scandal, led the Netherlands to introduce a series of regulatory reforms to financial advice. In the Netherlands, home loans are typically fully advised products bundled with life insurance and involve complex tax arrangements. Before the regulatory reforms, brokers received commissions from life insurance providers as well as home loan lenders.

221 Reforms focused at first on capping the high fees charged and commissions paid by the insurance industry but eventually extended to other products, culminating in a total ban from 2013 on commission payments for the sale of complex financial products, which included home loans. The Netherlands Government has since requested an evaluation of the effects of the commission ban, to be carried out in 2017 by the relevant regulator, the Autoriteit Financiële Markten (AFM)

222 After the commission ban, mortgage brokers trialled a number of remuneration arrangements (e.g. charging an hourly rate for advice, flat fees). The most common remuneration structure currently is an upfront flat fee of around 2,000 to 2,500 euros. Both the lenders and brokers also have responsible lending obligations.

223 Interest-only home loans with an LVR greater than 50% were also banned. It is important to note, however, that the Netherlands home loan market operates differently to Australia. Not only are mortgages sold with life insurance, but

also principal-and-interest home loans have traditionally been allowed to have LVRs in excess of 100%. The Netherlands Government has now mandated a gradual reduction (of 1% each year) of the maximum allowed LVR, until it reaches 100% in 2018. In this environment of high LVRs, most owner-occupiers can claim a tax refund on a portion of their home loan interest repayments. Tax deductions can also be claimed for a range of fees associated with buying a home, including mortgage broker fees.

224 Since the banning of broker commissions, the broker channel has dropped its market share only slightly compared to the lender-direct channel, from around 50% to 45% of the home loan market. To mitigate the potential effects on broker channels of the commission ban, lenders are required to separately price the fees charged for home loan advice and to price those fees appropriately (i.e. not cross-subsidise them). So while consumers may pay less to get home loan advice from a lender than a broker, the difference is not large. As in the United Kingdom, consumers can get a home loan without getting advice (i.e. execution-only); most do not choose this option.

New Zealand

225 Mortgage brokers operating in New Zealand must be Registered Financial Advisers on the Financial Service Providers Register or be employed by a Qualifying Financial Entity, like a bank. Mortgage brokers must:

(a) act with due care, diligence and skill;

(b) provide information to consumers about how they are paid; and

(c) belong to an EDR scheme.

226 Since June 2015, lenders must adhere to the Responsible Lending Code and ensure that mortgage brokers have appropriate training and systems in place to ensure compliance with the Lender Responsibility Principles.

227 Mortgage brokers in New Zealand are paid either an upfront commission only (upfront-only model) or a combination of upfront and trail commissions (upfront-and-trail model). Commissions in the upfront-only model are typically paid at a higher rate (e.g. one major lender pays 0.85% of the loan amount), whereas commission rates in the upfront-and-trail model appear to be similar to those paid in Australia. As in Australia, the fee-for-service model exists but is a less common remuneration structure.

228 The broker channel does not represent as large a share of the home loan market as in Australia; however, the major lenders report that around 40% of their home loans are now sold through brokers. The market in New Zealand is dominated by the same big four banks as Australia—ANZ, Westpac, Bank of New Zealand (owned by NAB) and ASB Bank (owned by CBA)—and non-bank lenders have a much smaller presence.

229 In 2016, the Reserve Bank of New Zealand introduced temporary limits on certain types of home loan in banks' lending portfolios, to reduce the amount of low-deposit home lending. These limits restrict investor home loans with an LVR higher than 60% to no more than 5% of a bank's new lending, while owner-occupier home loans with an LVR higher than 80% are restricted to 10% of new lending. There are various exemptions, including refinanced loans and loans for new housing. Some media commentary in New Zealand has suggested the Reserve Bank's temporary lending restrictions may further boost the use of mortgage brokers, as consumers will be forced to seek access to a wider range of lenders to secure a home loan.

230 We also note that in 2016 the New Zealand Government agreed to introduce a stricter licensing, conduct and disclosure regime for a range of finance, insurance and credit intermediaries, which would see mortgage brokers subject to a best interests duty. Under the proposed regime, commissions would be retained, but service providers would be subject to stronger disclosure requirements when selling these products to consumers.

B The mortgage broking market: An overview

Key points

Brokers have a significant and growing share of the home loan market and now account for the sale of more loans than lenders' own distribution channels (e.g. through branches, mobile lenders, and over the telephone).

As part of the value distribution chain, aggregators sit between lenders and brokers and are responsible for passing on commissions from lenders to brokers.

In addition, aggregators create a panel of lenders from which brokers can recommend loans. Access to the aggregator's panel is necessary for lenders to access the broker distribution channel. The customer-owned banking institutions included in our review appear on far fewer panels and, even when on a panel, have access to fewer individual brokers.

White label loans—that is, loans that carry the aggregator's brand but are funded by a lender—account for a substantial portion of the loans sold through brokers.

Home loans may also be sold through comparison websites and referrers. The latter channel is growing in size and involves unlicensed businesses and individuals referring consumers to the lender or broker.

Growth in the mortgage broking market

231 In March 2003, ASIC published Report 19 *A report to ASIC on the finance and mortgage broking industry* (REP 19).

232 This report reflected the mortgage broking market in Australia in the early 2000s, which included the following broad categories of intermediaries:

(a) *Mortgage and finance brokers*—These entities helped consumers select a loan, arrange paperwork for the loan application and assist with negotiations with the lender. In general, brokers did not have a continuing relationship with the consumer after the loan was obtained.

(b) *Mortgage managers*—These entities developed under arrangements with a new wave of non-mainstream wholesale lenders, to help consumers complete loan applications and, after approval of the loan, to administer the loan on behalf of the lender by accepting payments, issuing statements, monitoring defaults and responding to borrower inquiries.

233 The mortgage broking market was dominated by a number of 'aggregators', which provided infrastructure and administrative support to brokers who agreed to become members—organising a panel of lenders and facilitating

the processing of applications—and in return entering commission-sharing arrangements with the broker members.

234 At that time, there was considerable growth in the mortgage broking market; commissions were the dominant method of remuneration for brokers and there was a shift in distribution channels used by lenders from branch networks to brokers: see Section 1 of REP 19.

235 Since 2003, Australia's housing market has seen rapid growth, which has increased the demand for both home loans and mortgage broker services. There are now over 5,000 broker businesses operating in the mortgage broking market.

236 In comparing the four quarters ending December 2013 and the four quarters ending December 2014, the Australian Bureau of Statistics (ABS) Housing Loan statistics recorded a $93.7 billion increase in home lending. According to the Mortgage and Finance Association of Australia (MFAA), brokers accounted for $43.7 billion of this increase. In a study commissioned by the MFAA, Ernst & Young Australia noted that mortgage brokers accounted for around 25% of business flow in 2003, and now consistently account for approximately half of all home loans (both new and refinanced).

Note: See Ernst & Young Australia, Observations on the value of mortgage broking: Prepared for the Mortgage & Finance Association of Australia (PDF 3.19 MB), May 2015. This data is based on an APRA survey of ADIs released in January 2003, which indicated that the size of the broker-introduced loan market (as at June 2002) was $86.6 billion with approximately 802,000 loans outstanding. Brokers were most prominent in the home loan market, accounting for $76 billion of total home loans outstanding. Around 23% of ADI home loans were broker introduced.

Industry participants and their roles

Lenders

237 Lenders in the home loan market include ADIs and other, non-ADI, lenders that only engage in lending activities (and not deposit-taking activities that are part of an ADI's banking business).

238 The latest housing finance report published by the ABS indicates that, as at the end of June 2016, ADIs held a 92% share of the market for home loans to households (covering both owner-occupied and investment housing), with securitisation vehicles and other lenders holding the remaining 8%.

Note: See statistics released by ABS, *Housing finance—Australia* (September 2016), Table 12. Note that this table indicates that separate data for owner-occupied and residential investments was not available.

239 The latest APRA statistics on ADI property exposures indicate that at the end of December 2016 ADIs held $1,493.5 billion in residential terms loans to households (including both owner–occupier and residential investment loans).

240 Of the ADI lenders, the home loan market is divided (as at the end of December 2016) between:

(a) major banks—CBA, NAB, Westpac and ANZ—which together hold $1,203.7 billion (a share of around 80.5%);

(b) 27 other domestic banks—including second–tier and smaller banks, and mutual banks—which together hold $194.2 billion (a share of around 13.0%);

(c) seven foreign subsidiary banks, which hold $58.5 billion (a share of around 3.9%);

(d) 58 credit unions, which hold $27.1 billion (a share of around 1.8%); and

(e) four building societies, which hold $9.8 billion (a share of around 0.7%).

Note: See statistics released by APRA, *Quarterly authorised deposit-taking institution property exposures* December 2016 (released 28 February 2017).

241 We note that the concept of a 'lender' as used in this report is different than the concept of a 'credit provider' used in the credit legislation. A 'credit provider' is the lender of record—the entity named in the loan documentation. However, in practice a number of other entities could be viewed by consumers as being the 'lender'.

242 Examples include the following:

(a) A credit provider could be an unlicensed 'special purpose funding entity' (e.g. a securitisation vehicle), which effectively provides the funds for the loan but relies on another licensee (e.g. a loan originator) to perform its obligations and exercise its rights as the credit provider on its behalf. This other licensee may be viewed more generally as the lender for the loans that it services on behalf of the credit provider.

Note: The licensee that services loans under arrangements with this kind of credit provider is not required to comply with the requirements in Pt 3-1 (responsible lending requirements for licensees that provide credit assistance, which include disclosure requirements): see notional s112 inserted by reg 3.24 of Sch 3 to the National Credit Regulations (modifications for special purpose funding entities).

(b) A licensee may provide credit assistance as a 'mortgage manager'—that is, a licensee that has a written agreement with a credit provider or a third party who is authorised to act for a credit provider (e.g. a loan originator for a special purpose funding entity). Under that agreement, the licensee is required to manage the relationship with the consumer on a day-to-day basis for the credit provider in accordance with the credit provider's policies and procedures, and contracts and associated documentation are branded or co-branded with the name of the licensee.

Note: See reg 26 for the definition of 'mortgage manager'. Mortgage managers must comply with the requirements for credit assistance providers in Pt 3-1. The credit guide must include an explanation of the relationship between the mortgage manager and the credit provider: see reg 26A. There are some different disclosure requirements for certain kinds of commission received by mortgage managers—if these apply, the mortgage manager must tell the consumer that they are not acting for the consumer in relation to the managed contract: see reg 28H.

243 Mortgage manager businesses entered the market in 1980s and steadily increased their market share to about 15%: see MFAA, *Inquiry into competition in the banking and non-banking sectors: Submission by the Mortgage and Finance Association of Australia* (PDF 465 KB), July 2008.

244 As noted in REP 19, there may be some consumer risks if the distinction between mortgage manager and broker is not clear (e.g. where the consumer does not understand the basis on which the mortgage manager acts and expects that when it provides credit assistance it is acting for the consumer). The requirement for an explanation of the relationship between the mortgage manager and the credit provider seeks to address this risk, and promotes the view that mortgage manager is performing the role of the lender.

245 Feedback from industry suggests that the concept of 'mortgage manager' has fallen out of favour in recent years, and 'white label' arrangements have become more common. For a further discussion of the nature and prevalence of white label and mortgage manager arrangements, in the context of the broking market, see paragraphs 309–322.

Aggregators

246 Since REP 19 was published in 2003, aggregators have consolidated their position in the industry to become an integral part of the industry for both lenders and brokers. From initially providing a path for new brokers to access lenders through accreditation, they have become a key intermediary between brokers and lenders by aggregating loan volumes. In order to submit loan applications to a lender, brokers typically need to be part of an aggregator's network and submit the application through that aggregator.

247 Lenders do not normally have a direct contractual relationship with brokers. Rather, the lender will have a contractual relationship with the aggregator, which in turn has a relationship with the broker. We understand that the reasons for this practice are:

(a) lenders do not want to deal with hundreds or thousands of mortgage brokers on an individual basis; and

(b) most lenders have volume and compliance requirements that an individual broker may not be able to maintain.

248 Based on the data provided by the 19 lenders in this review, in 2015, those lenders received $185 billion of home loans originated through aggregator channels and only $1.2 billion of home loans directly from a broker (where an aggregator was not involved).

249 In their capacity as the intermediary between the lender and the broker, the aggregator undertakes a number of important functions:

(a) *Creating and providing access to a panel of lenders*—Aggregators may seek to add lenders to their panel for a number of reasons, including the size of the lender (e.g. major banks will typically be included on an aggregator's panel) and diversity in the range of available lenders to satisfy consumer preferences. The profile of an aggregator's lender panel is very important to consumer choice, as brokers associated with the aggregator will generally only be able to recommend and arrange loans with a lender on the approved panel (see paragraphs 323–327).

(b) *Providing infrastructure and administrative support*—As the aggregator sector has become more competitive, aggregators have provided more support to their brokers, including through systems and technology that improve the efficiency of the brokers' business operations, and marketing and promotional support to attract new borrowers and retain existing ones. One form of support includes access to product recommendation software (see paragraphs 257–261).

(c) *Providing training and professional development programs*—Aggregators may provide training and professional development programs for their brokers (see RG 203 and Report 330 *Review of licensed credit assistance providers' monitoring and supervision of credit representatives* (REP 330)).

(d) *Enabling brokers to operate without their own licence*—Some aggregators may allow a broker to provide credit services as their representative under the aggregator's credit licence. This may particularly benefit new brokers who do not have sufficient experience to meet the competence requirements for holding a credit licence, or who do not have sufficient levels of business and resources to make obtaining and maintaining a licence viable (see paragraphs 180–195).

Note: Although aggregators are often seen as providing the 'acting as an intermediary' form of credit service, their licence authorisations also cover provision of credit assistance. They may choose to appoint brokers as their credit representatives, and accept responsibility for compliance with the additional obligations that apply to licensees that provide credit assistance (under Pt 3-1).

250 Aggregators generally charge a fee for offering these services to brokers. These fees may be in the form of a percentage of the fees or commission received from the lender, or they may charge fees on a per-transaction, monthly or annual basis. Some aggregators also charge a joining administration fee or franchise fees. Different fees are likely to be charged

depending on whether the broker is a licensee or a credit representative, the latter having a higher fee reflecting the higher level of service and responsibility involved in the representative relationship.

251 The role taken by aggregators may depend on their business model. For example, some aggregators operate a franchise model—that is, brokers enter a franchise agreement under which they receive the benefit of lead generation, systems and support, and use of the aggregator's brand in the provision of services and marketing materials. Four such aggregators in this review reported that under their franchise agreements, brokers are required to act as the aggregator's credit representatives (rather than holding their own licence or being a credit representative of another licensee).

252 This may indicate that aggregators using this model wish to increase the level of control that they have over their broker network. It also increases the level of legal responsibility these aggregators have under the National Credit Act for the conduct of the brokers and for maintaining their training and competence to provide credit services.

253 For this review, we did not explore the nature of the franchise relationship between an aggregator and broker business/broker, other than to ask the aggregators whether they operated a franchise model. Just over 40% of aggregators reported that they operated a franchise model. A further 30% stated that they had a mix of brokers who operated under a franchise model and others who operated under their own brand. The remaining aggregators reported that their brokers always operated under their own brand, rather than the aggregator's.

Aggregator services: Credit representatives

254 To understand credit representative arrangements, we asked the aggregators to respond to some questions separately about broker businesses/brokers that act as a credit representative of the aggregator, and those who hold their own credit licence or who are a credit representative of another credit licensee (both of which we refer to as a 'non-credit representative'). For example, when we asked about the processes that an aggregator has to review a broker's application to be accredited, we asked whether that process differed between brokers who were credit representatives and those who were not.

255 We found that the aggregators' responses did not vary significantly between credit representatives and non-credit representatives. This indicates that these aggregators do not generally take a different approach to credit representatives and non-credit representatives.

Note: Four aggregators reported that they only deal with broker businesses/brokers that are credit representatives of the aggregator. Those aggregators could not provide responses to questions about practices and processes for non-credit representatives. This resulted in slight differences in proportional results for credit representatives and non-credit representatives.

256 We have noted in this report any material differences we saw in the responses of aggregators about arrangements for brokers that are not credit representatives of the aggregator compared to those who are.

Aggregator services: Product recommendation software

257 Approximately 85% of aggregators reported that they made product recommendation software available for use by their broker network. This software is a form of support service to their brokers, helping the broker to develop a product recommendation for the consumer.

258 Given the prevalence of such software, we asked aggregators to explain how certain elements of this software operated.

259 Aggregators reported that the software generally takes into account product features and pricing (both interest and fees) in the recommendation. It is also common for the software to include information about lenders' credit risk policies (for approximately 75% of aggregators who provide such software) and the identity of the lender (for approximately 60% of aggregators who offer such software). Brokers can typically sort the results by the same factors (i.e. they can prioritise the results by any of the relevant factors).

Note: Three aggregators reported that their white label product would top the rankings in the product recommendation software if certain conditions were met. They did not provide details of those conditions.

260 No aggregators reported that the software made available to their brokers takes into consideration loan approval times or other service levels of the lender.

261 We consider that taking into account some factors (e.g. commission structures for particular products or lenders) is likely to create a concern given the risk of recommendations generated by comparison software influencing brokers to suggest that consumers enter loans that are more financially beneficial to the broker or the aggregator. No aggregators reported that the software made available to their brokers takes into consideration the commission structure when providing rankings to products.

Role of the aggregator in mitigating risks for lenders

262 As part of this review, we sought to test the extent to which aggregators may, or may be expected by lenders to, go beyond their legal obligations under the National Credit Act in overseeing the conduct of brokers (particularly where the broker is not the aggregator's credit representative).

263 Because lenders do not have direct contractual relationships with the brokers that distribute their loans, they may rely more on aggregators to ensure the quality of advice provided in relation to their products, and the quality of the

responsible lending processes that are undertaken in forming the broker's preliminary assessment of whether the loan is unsuitable for the consumer.

Note: In Regulatory Guide 209 *Credit licensing: Responsible lending conduct* (RG 209), we recognise that lenders may be provided with information about the consumer by a credit assistance provider, which they may use in completing their own responsible lending inquiries and assessments: see RG 209.54–RG 209.56. We note that reasonable and prudent lenders will have processes in place to ensure the reliability of any information collected by third parties, including information in a preliminary assessment.

This could include a combination of approaches such as:

(a) conducting 'spot checks' on some of the information by re-verifying it;

(b) ensuring the lender only uses information in preliminary assessments from intermediaries that have robust compliance arrangements; and

(c) having processes to actively discourage inappropriate practices (e.g. ensuring that any incentives offered to intermediaries encourage, rather than discourage, appropriate information collection practices).

264 Broker businesses may be small enterprises with limited resources. Where a lender distributes its loans through an aggregator that deals with smaller broker businesses that are credit licensees, it needs to manage the conduct risk that may arise from the actions of the broker business. We note that lenders do retain a level of control by maintaining discretion about whether to accredit a particular broker to distribute their loans: see paragraphs 362–370. However, we sought to understand whether lenders may seek to impose contractual obligations on aggregators to have strong oversight/control measures in place to further limit the risks of poor broker conduct.

265 Overall, it seems that lenders do not impose these obligations on aggregators: see Section H for a discussion of governance and oversight.

Brokers

266 There are a number of different business models under which a broker may operate depending on whether:

(a) they work as an individual or as part of a broker business; and

(b) if they are part of a broker business, they are an owner or director, employee or an independent contractor within that business.

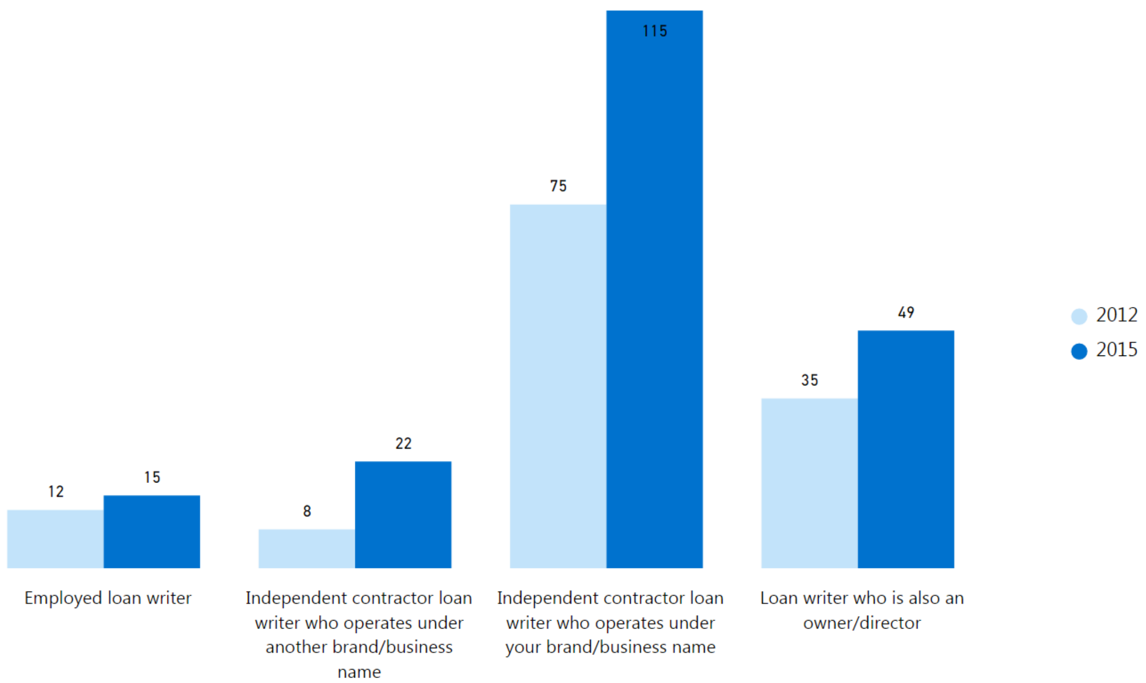
267 In addition, a broker may operate under their own business name or under the business name of the broker business.

268 We received survey responses from 44 broker businesses as part of this review. We found that over 90% of the businesses surveyed included a broker who was an owner or director of the business. For larger broker businesses, this dropped to 60%. This indicates that in larger businesses it is less common for the senior management/owner to directly provide services to consumers (although it is still not uncommon).

269 The other categories of brokers were much less common. Around 35% of businesses surveyed had a broker who is an independent contractor operating under the business' name, while around 10% of businesses had an independent broker operating under a different name. Around 20% of businesses surveyed had employed brokers.

270 A total of 128 brokers in 2012 and 198 brokers in 2015 were identified by the 44 broker businesses that responded to the survey. The businesses classified the brokers on the basis shown in Figure 1.

Figure 1: Number of brokers within each broker category



Note: See paragraph 271 for a description of the trends shown in this figure.

271 Although more businesses reported having a broker who was an owner or director of the business (35 in 2012 and 49 in 2015), overall there were more independent contractors (75 in 2012 and 115 in 2015). This indicates that where a business includes an independent contractor, it is likely that they will have more than one such broker working within the business.

> Note: The data in Figure 1 was based on a survey of broker businesses made up of an equal selection of large, mid-tier and smaller businesses (see paragraph 140). As such, it gives equal weight to each of those types of business.

272 As described in Section A, a broker provides credit assistance under the National Credit Act and must hold a credit licence or be a credit representative of a credit licensee. If the broker or business for which the broker works does not hold its own credit licence, an aggregator will often appoint the broker as its credit representative. In this way, aggregators provide both aggregation services and the licence under which the broker operates.

273 Broker businesses generate their revenue in two ways:

(a) a commission for providing the service and arranging the home loan that is paid by the lender whose loan they sell (where that payment is channelled through the aggregator); or

(b) a fee for service charged to the consumer (this remuneration model is rare in Australia; if a fee is charged, the business may rebate any commission earned through the loan to the consumer).

Note: For our findings on how broker businesses/brokers are paid, see Section C.

274 How the broker business or broker is paid is relevant to whether they may refer to themselves as ‘independent’ or ‘impartial’ (or similar). The National Credit Act prohibits a broker from using such terms if they receive and retain any commission payments. The broker business or broker may be entitled to use those terms if they rebate any commission received to the consumer.

275 As part of this review, we asked lenders and aggregators whether they sought to restrict the broker’s ability to rebate the commission received by the broker to the consumer. While no lenders sought to impose restrictions, two aggregators noted that their agreement with the broker imposes limitations on the broker. A further aggregator noted that while not prohibited under the agreement with the broker, it was against the aggregator’s policy for commissions to be rebated.

Comparison website providers

276 Comparison websites are a source of lead generation for lenders. In addition to providing a platform for consumers to compare home loan products and prices, comparison websites have steadily grown their presence and importance in the mortgage broking market by offering other services such as ratings and annual awards for various products and product providers.

277 The websites are not product issuers themselves and generally do not provide consumers with credit assistance.

278 Comparison websites are generally a free service to consumers and are used as a primary research and reference tool for consumers when familiarising themselves with what home loan products and prices are available in the market. Comparison websites also allow consumers to quickly compare and verify information that might be given to them by brokers.

279 Lenders may have arrangements with comparison websites under which the lender will pay the website for click-throughs by consumers to the lender’s website. Nine out of the 19 lenders in our review reported that they had paid a comparison website for such a click-through in 2015 (up from five in 2012). Those lenders reported a total of almost 5,600 leads being provided in 2015 (compared to 3,300 leads in 2012).

280 As part of this review, we sought to understand whether comparison website providers had any arrangements for users of their website to obtain a discount on the price of a home loan that was not generally available to the public. All four websites we surveyed advised that this was not the case.

Referrers

281 Mortgage referrers (sometimes also known as ‘introducers’) are individuals or businesses that provide a referral service to lenders or brokers. Under this arrangement, a consumer supplies their details to the referrer and agrees to either a lender or broker contacting them directly. Referrals such as these are often known as ‘leads’.

282 Some of the most common referrers are real estate agents, migration agents, financial planners and other professional services referrers. However, referrers can also include many other types of individuals and businesses, including property developers and non-profit organisations.

283 Referrers may be engaging in credit activities by ‘acting as an intermediary’ between the consumer and the lender or broker, and so may require a credit licence. However, many referrers rely on an exemption from the requirement to hold a credit licence if they are engaging in simple referral activities: see reg 25.

284 We asked lenders and aggregators whether they sought to restrict brokers from passing on some of their commission to referrers. No lenders reported that they sought to impose such restrictions. Around one third of aggregators reported that the referral agreement with the broker did include limitations. However, based on aggregators’ additional comments, these provisions did not appear to prohibit a broker from making such payments; rather, they appeared to require the broker to comply with the relevant legislative provisions.

285 Aggregators generally could not provide details of the value of referrals made to brokers; while aggregators may keep a record of referral agreements, the relationships are managed by broker businesses, not the aggregator.

Lenders’ arrangements with referrers

286 Referrers generally:

(a) have direct agreements with one or more lenders or broker businesses; or

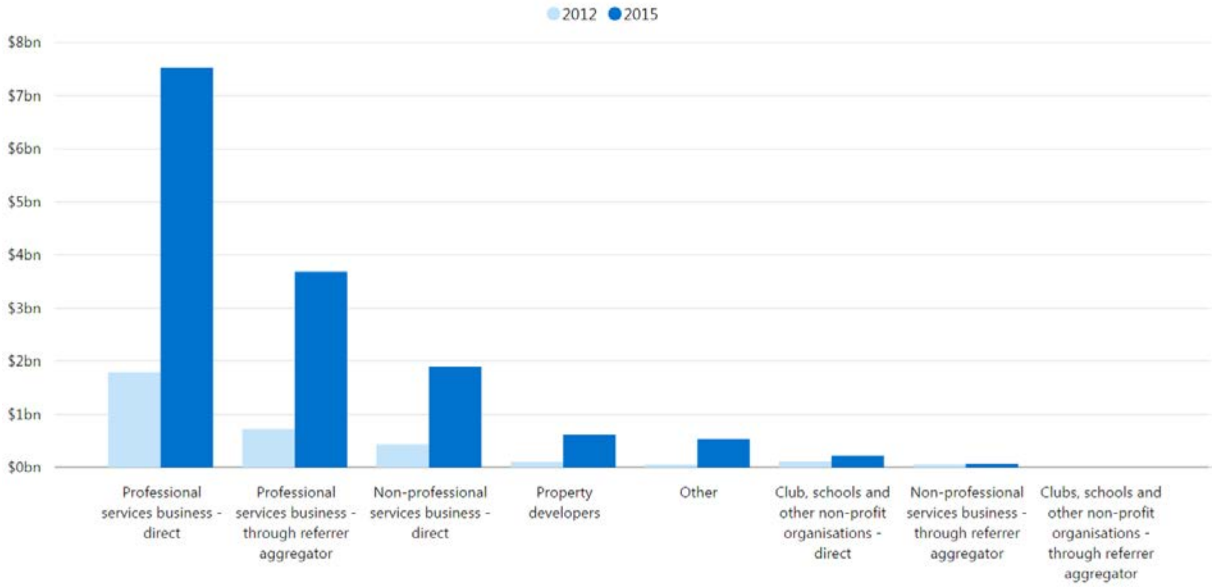
(b) operate under an aggregator structure to access multiple lenders (in this report, we call such aggregators ‘referrer aggregators’).

287 The number of referrals being made to lenders, either by the referrer directly or through a referrer aggregator has increased significantly. The total number

of home loans sold after a referral increased from 8,124 in 2012 to 26,106 in 2015, representing an increase in value from $3.3 billion to $14.6 billion.

288 Figure 2 shows the value of home loans that resulted from a referral in 2012 and 2015 across the different types of referrers.

Figure 2: Value of home loans that resulted from a referral by referral entity type



Note: See paragraphs 289–290 for a description of the trends shown in this figure.

289 Referrals by professional services businesses (either directly or through a referrer aggregator) made up the bulk of referrals, with one out of three of these referrals coming through a referrer aggregator.

290 While the value of home loans sold as a result of a referral increased significantly between 2012 and 2015, over 87% of those sales were by two major banks.

Ownership and distribution channels

291 As part of this review, we collected data on the ownership of brokers and aggregation businesses. Over the last 10 years, there has been an increase in vertical integration of brokers, aggregators and lenders.

Ownership of aggregators

Two out of the four major lenders hold equity interest in at least one aggregation business:

- CBA is a majority shareholder of Aussie Home Loans, with ownership increasing from 30% in 2008 to 80% in 2013. CBA also holds 16.6% interest in Mortgage Choice.

- NAB owns 100% of Choice, FAST and PLAN, which account for approximately 30% of all brokers in Australia.

Non-major lender Macquarie holds a large stake in an aggregation business, having acquired 25% of Connective in 2013. Macquarie also holds approximately 10% in Yellow Brick Road (through which they own a shareholding in Vow). Macquarie previously owned a minority shareholding in AFG, however divested this share in September 2016.

292 Three out of four major lenders also hold stakes in smaller lenders, regional lenders and online lenders:

(a) Bankwest was bought by CBA in 2008 and ceased to exist as a standalone licensee in 2012.

(b) St George (and all St George brands) merged with Westpac in 2008 and ceased to exist as a standalone licensee in 2010, having been absorbed into the wider Westpac Group.

(c) NAB established UBank as a division of NAB in 2007. UBank is an online bank brand and has no physical branches.

293 ANZ has made no significant acquisitions of any aggregation businesses, smaller lenders or competitors.

294 There were no ownership arrangements reported between referrer aggregators or comparison websites and other review participants.

Direct versus broker channels

295 Home loans may be distributed through the lender's own direct channels, using its own staff and infrastructure.

296 Brokers have become a significant distribution channel and, as mentioned earlier, accounted for almost 57% of loans written in 2015 by lenders in this review.

Note: This figure is based on calculations by ASIC using data supplies by lenders.

297 Brokers are also the primary distribution channel for non-major and regional lenders, allowing them to compete with larger lenders that have their own direct distribution channel.

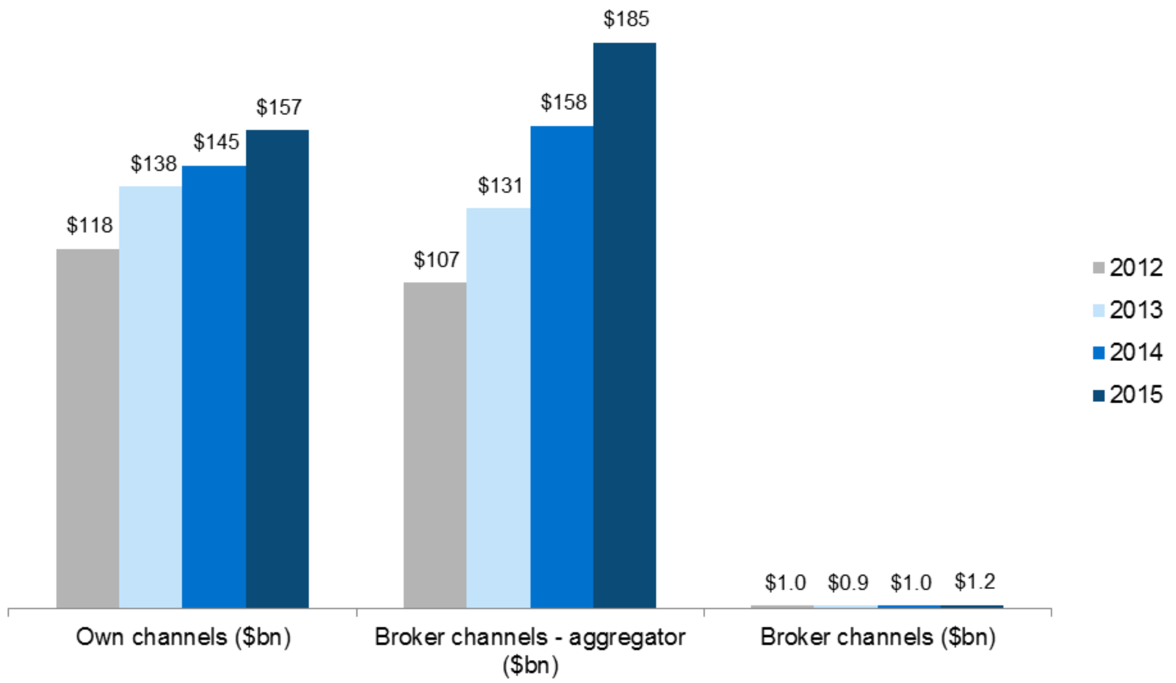
298 Figure 3 sets out the total value of loans written by the 19 lenders in this review, separated into home loans arranged:

(a) through direct channels (increasing from $118 billion in 2012 to $157 billion in 2015);

(b) through brokers working under an aggregator (increasing from $107 billion in 2012 to $185 billion in 2015); and

(c) by brokers with whom consumers dealt directly (increasing from $1 billion in 2012 to $1.2 billion in 2015).

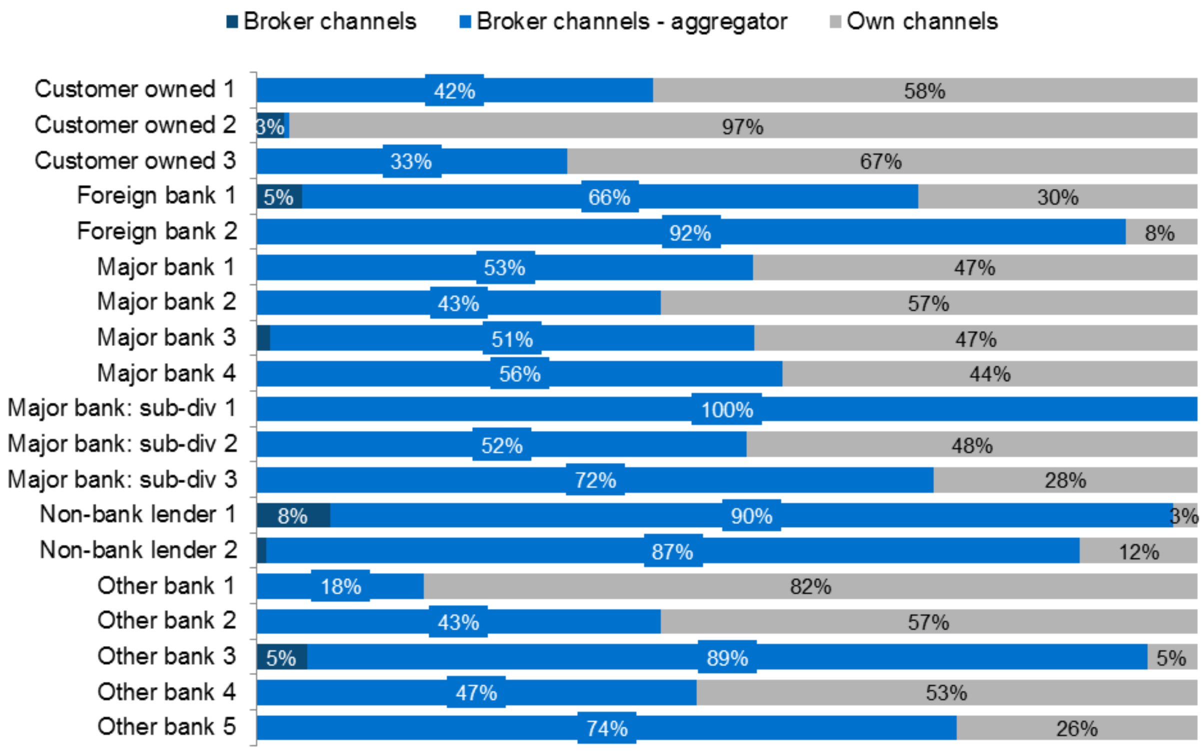
Figure 3: Total value of loans written by lenders for each channel



Note: See paragraph 298 for a description of the trends shown in this figure.

299 Figure 4 sets out the proportion of loans sold through direct channels, through brokers working under an aggregator, and by brokers with whom consumers dealt directly for each of the 19 lenders in the review.

Figure 4: Proportion of loans originated through brokers for each lender in 2015



Note: See paragraphs 300–301 for a description of the trends in this figure.

300 There is considerable variability in the proportion of loans sold through broker channels compared to lenders' own channels. The major banks received between 43% and 56% of home loans through brokers channels (almost all of which was through brokers working under an aggregator).

301 Customer-owned banking institutions tended to receive less business through the broker channel compared to other lenders (between 2% and 42%), while the non-bank lenders' reliance on broker channels is evidenced by the high proportion of loans received through that channel (87% and 98% including all broker loans).

Products and services offered

302 Lenders offer consumers a suite of products through the broker channel—including, but not limited to:

(a) investor home loans;

(b) owner-occupier home loans;

(c) reverse mortgages;

(d) commercial loans;

(e) personal loans;

(f) credit cards; and

(g) property and loan-related insurance products.

303 After consultation with stakeholders, we decided in this review to focus only on home loans (including white label loans). Other products (e.g. reverse mortgages and construction loans), which do not comprise a predominant proportion of the home-lending market, are outside of the scope of the review and were not considered for the purposes of this report.

304 We have not reviewed non-home loans (e.g. commercial loans or personal loans), other than to the extent that they have a material impact on remuneration for home loans.

Home loans

305 Home loans include owner-occupier loans, available for consumers who plan to live in the property, and investment loans, for consumers wishing to add property to their investment portfolio. The property is purchased as an investment and typically rented out to tenants. Consumers wanting a home loan may purchase an existing property, build a new home or renovate an established property.

306 The interest rate on a home loan may be wholly variable or fixed for a specified term. The loan account may also be split so that a part (e.g. 50%) of the loan is variable while the rest (e.g. 50%) is fixed for a specified term.

307 A home loan may also include a number of features, such as:

(a) a principal-and-interest repayment option or interest-only repayment option;

(b) a discount on the lender's advertised interest rate;

(c) the option of additional repayments on the loan;

(d) the option of early repayment of the loan;

(e) an offset account;

(f) a redraw feature;

(g) a higher LVR; and

(h) a higher borrowing capacity.

308 Not all home loans will include all of these features—different loans will have different features. Many lenders also offer packages (usually involving an annual cost) that entitle the consumer to a wider range of loan features and often include a discount on the advertised standard interest rate.

White label loans

309 White label home loans are loans that are issued under the brand name of another business. In the mortgage broking market, the brand name is usually that of the aggregator and, typically, the particular white label loan will be sold exclusively through that aggregator's broker network. The white label loan will not be available through other aggregators or through direct channels.

310 While the loan is offered using the brand name of the aggregator, the actual lender is generally responsible for the initial assessment of the loan application and all the servicing tasks associated with that loan.

311 From a consumer perspective, white label home loans are often marketed as simple but cost-effective alternatives to standard home loan offerings.

312 In addition to white label loans, an aggregator may offer loans using its brand name through a mortgage manager arrangement. Under this type of arrangement, the aggregator (i.e. the 'mortgage manager') accesses a line of funds from a lender to offer home loans under the aggregator's brand. In contrast to a white label arrangement, the aggregator takes a more active role in the loan application process and the subsequent management of the home loan. The division of responsibility between the lender and mortgage manager depends on the terms of the arrangement.

313 In some cases, the distinction between loans issued under white label arrangements and mortgage manager arrangements is not always clear. For example, we note that when giving us information about the types of loans sold through their broker networks, aggregators did not appear to distinguish between loans issued under white label and mortgage manager arrangements.

314 In preparing for this review, we were informed by some industry participants that use of mortgage manager arrangements has decreased over recent years, with a shift to white label arrangements.

Prevalence of white label and mortgage manager arrangements

315 We asked lenders to tell us about their arrangements with a list of 20 aggregators (the 14 aggregators in this review plus an additional six). Four lenders reported that they had a white label arrangement with at least one aggregator. In addition, four lenders reported that they had mortgage manager arrangements with at least one aggregator (including two of the four lenders that also offered white label loans).

316 These lenders reported having a white label arrangement with 11 out of the 20 aggregators. In addition, the lenders reported having mortgage manager arrangements with two of those aggregators. We note that a number of aggregators were identified as having both white label and mortgage manager arrangements with multiple lenders.

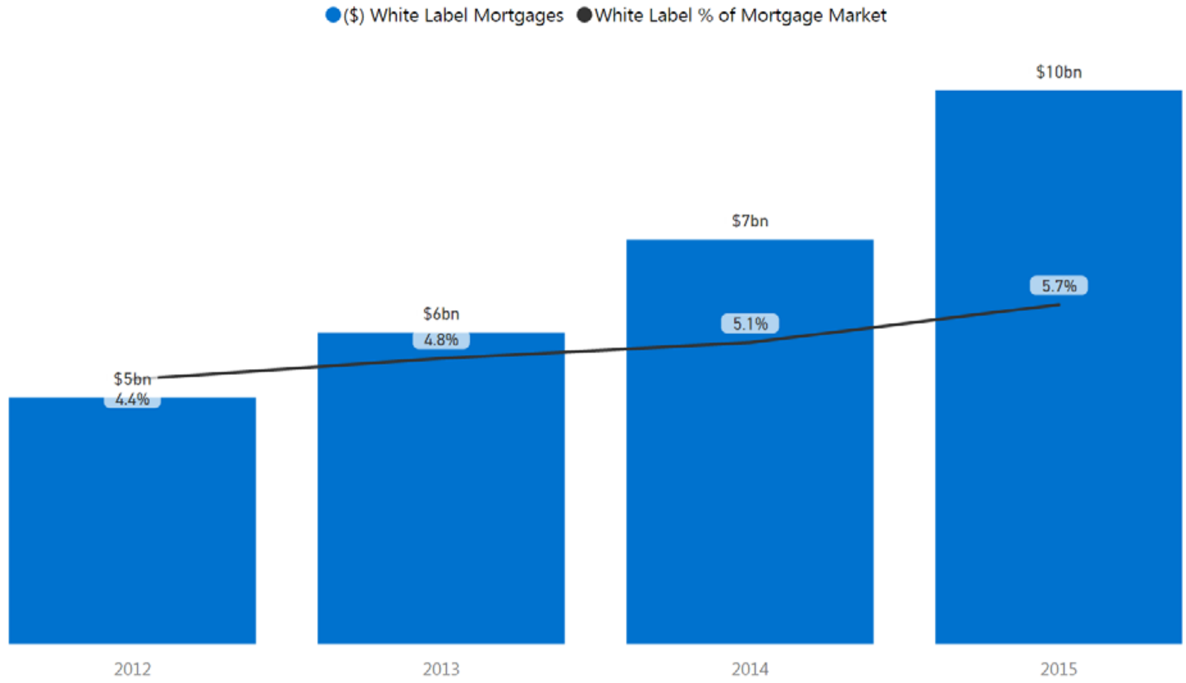
317 Most lenders who have white label and mortgage manager arrangements with aggregators also offer home loans under their own brand. For example, Macquarie issues loans under the Macquarie brand and also, through an arrangement with the aggregator, Mortgage Choice, under the name ‘Mortgage Choice Home Loans’. The brokers in Mortgage Choice can sell both Macquarie and Mortgage Choice home loans, effectively making the two Macquarie-funded products compete with each other.

318 Advantedge Financial Services (which is part of the NAB Group) is an exception as all the home loans it sells are under a white label or mortgage manager arrangement with other entities (including aggregators). It does not make available ‘Advantedge’ branded home loans.

Value of loans issued under white label or mortgage manager arrangements

319 Figure 5 shows the value of white label loans reported by aggregators. As noted earlier, it appears that aggregators may not distinguish between loans issued under a white label or mortgage manager arrangement. It is therefore likely that this figure shows the combined value of such loans.

Figure 5: Value of white label loans issued through brokers



Note: See paragraph 320 for a description of the trends shown in this figure.

320 The value of white label loans—both the absolute value and as a proportion of the total loans issued through brokers—has increased from 2012–15. In 2015, white label loans accounted for almost 5.7% of the home loans sold by brokers, up from around 4.4% in 2012.

321 As discussed in paragraph 798, one aggregator sold more white label loans than loans of any other lender.

322 This indicates that the provision of white label loans is an increasing focus for aggregators. In their dual role as aggregator (with all the attached responsibilities) and a quasi-lender, we would expect aggregators to carefully understand and assess whether these arrangements are resulting in good consumer outcomes.

Aggregator panels and broker accreditation

323 An important role that aggregators play is having arrangements with lenders in place to facilitate brokers arranging home loans with individual lenders. These arrangements encompass several things, including having the necessary systems and procedures in place to enable business by the broker. Lenders that have these arrangements with aggregators are considered to be on the aggregator's 'panel'. If a lender is not on an aggregator's panel, then a broker may be unable to place business with that lender.

Note: In addition to a lender being on the relevant aggregator's panel, a broker may also need to be individually 'accredited' by the lender (see paragraphs 362–370).

324 While brokers ordinarily recommend loans from the aggregator's panel of lender, in preparing for this review some stakeholders raised the possibility that a broker may recommend loans 'off-panel' (i.e. loans offered by lenders that are not on the aggregator's panel).

325 We asked aggregators whether they allowed their network of brokers to do this. Almost 60% of aggregators said that brokers who were their credit representatives could not recommend off-panel loans. However, this dropped to 10% for brokers who are not the aggregator's credit representative. All but one aggregator said that brokers did not need to notify the aggregator if they recommend a loan from an off-panel lender.

326 We also asked broker businesses whether brokers could recommend loans from off-panel lenders. Approximately 50% of businesses (which were not sole operators) said that brokers could do so.

327 We sought to analyse the home loan data to understand how often this practice occurred; however, lenders could not generally provide the required broker data for each loan to allow us to do this.

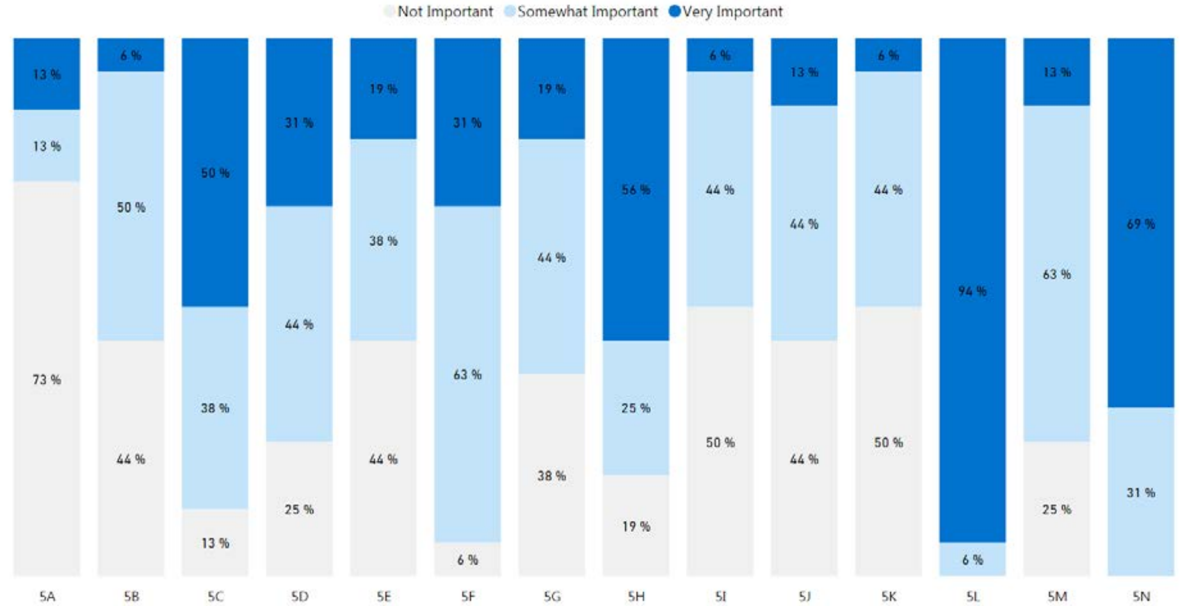
Why lenders join or leave an aggregator's panel

328 We sought to understand the reasons why a lender would join an aggregator's panel. We also sought to understand the number and make-up of aggregators with whom the lender has relationships. While it could be assumed that a lender would want to be part of as many aggregators' panels as possible, this was not always the case.

329 In addition to our main information collection process, we also sought qualitative feedback from customer-owned banking institutions (including those who were not participants in the review) about their reasons for participating (or not participating) in the mortgage broking market. This was undertaken with the assistance of COBA.

330 Firstly, we asked lenders to rate the importance of certain matters in their decision to join an aggregator's panel: see Figure 6.

Figure 6: Importance of reasons for joining an aggregator's panel



Note 1: See paragraphs 331–333 for a description of the trends shown in this figure.

Note 2: In this figure, these codes are used to indicate the following responses to question 5 in the lenders' survey:

5A = the existence of an ownership relationship with the lender;

5B = the independence of the aggregator from other lenders;

5C = the financial strength of the aggregator;

5D = the ability of the aggregator to access consumers across a wide geographic area;

5E = the ability of the aggregator to access consumers across a specific, targeted geographic area;

5F = the ability of the aggregator to target a broad base of customer types;

5G = the ability of the aggregator to target a specific base of customer types;

5H = the projected volume of residential mortgages originated through the aggregator;

5I = the projected volume of other products and services originated through the aggregator;

5J = the uniformity of brokers under that aggregator;

5K = the diversity of brokers under that aggregator;

5L = the aggregator's risk control framework;

5M = the ease with which the lender can be added to the aggregator's panel; and

5N = the ability and willingness of the aggregator to provide access to their brokers for business development opportunities

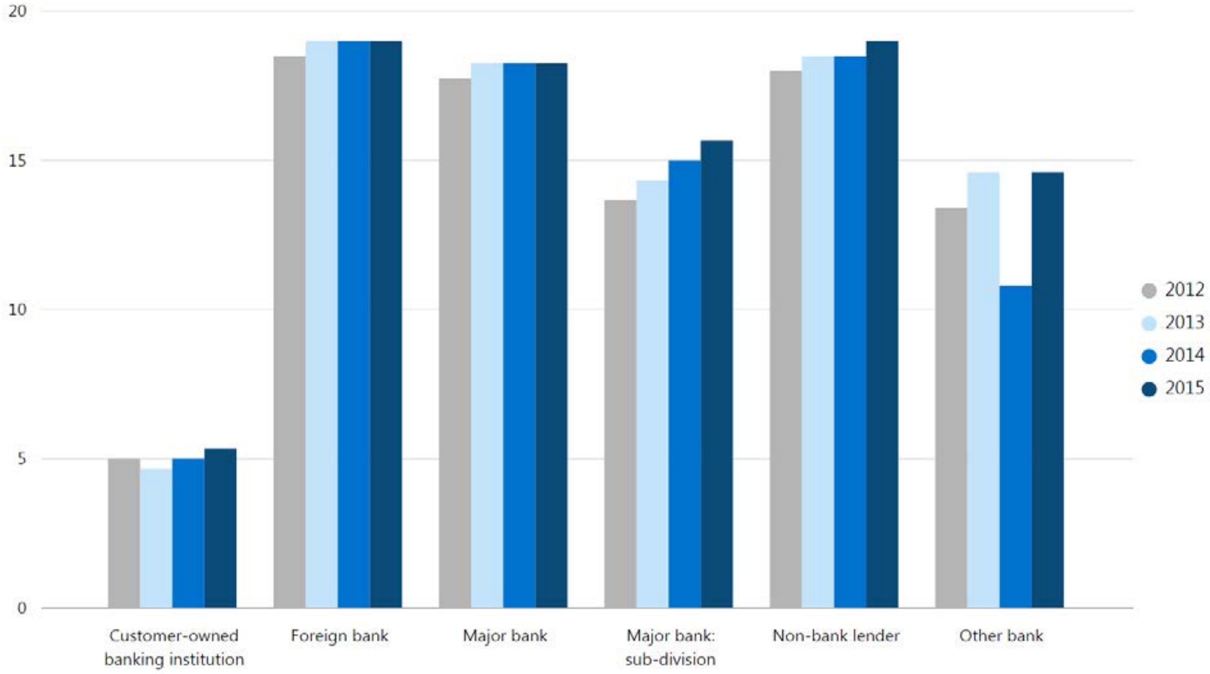
331 Most lenders (73%) responded that not owning an aggregator was not important to their decision (i.e. a lack of ownership does not stop the lender from joining the panel). However, a substantial portion (50%) indicated that the existence of an ownership relationship between the aggregator and *another* lender was somewhat important to their decision.

332 Lenders seemed to place a high degree of importance on the relevant aggregator's risk control framework (94% rated this as very important). However, we found that this was not reflected in the way the lender set out the aggregator's obligations in the agreement or in the controls and culture section: see Section H for a discussion of governance and oversight.

333 The financial strength of the aggregator seemed to be one of the most important criteria for lenders (50% rated this very important and 38% somewhat important). Lenders also appeared to value the ability of aggregators to target a broad base of consumers over a wide geographic area (31% rated this very important and 44% somewhat important).

334 Secondly, we asked lenders to tell us whether they had a relationship with anyone on a list of the 20 largest aggregators: see Figure 7.

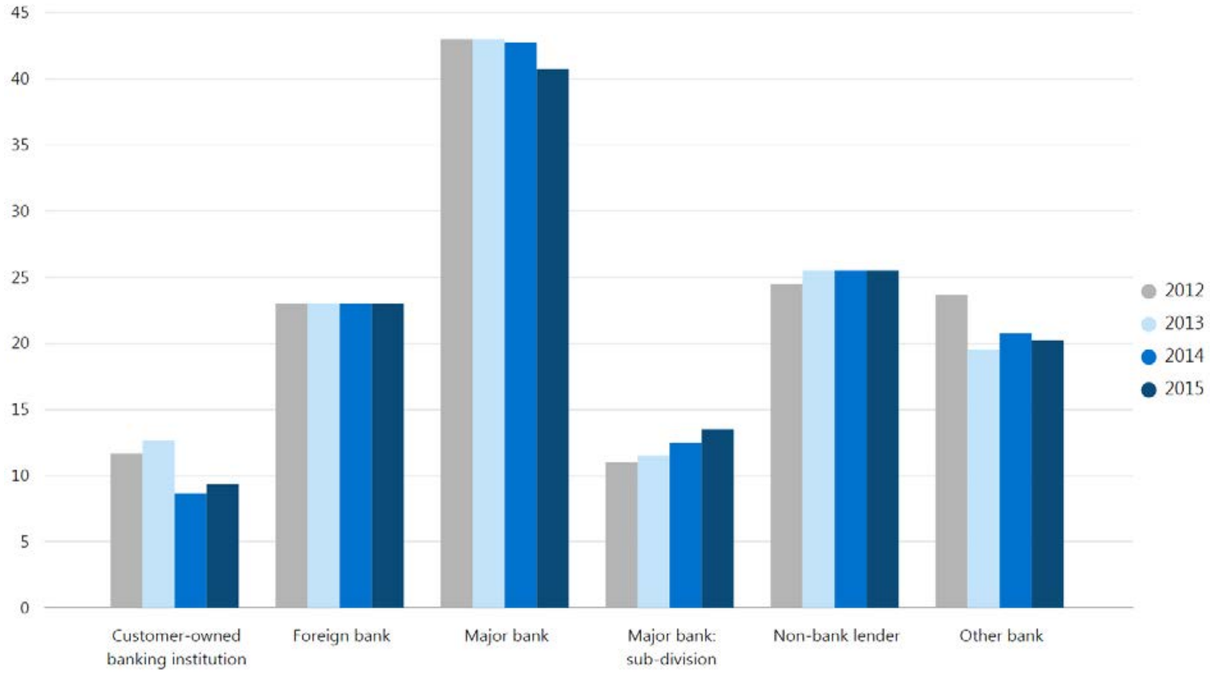
Figure 7: Number of aggregators per lender (20 largest aggregators)



Note: See paragraphs 336–337 for a description of the trends shown in this figure.

335 We also asked lenders to list all the aggregators with which they had a relationship. The average number of relationships is set out in Figure 8.

Figure 8: Average number of aggregators per lender (All aggregators)



Note: See paragraphs 336–337 for a description of the trends shown in this figure.

336 Interestingly, when the question expanded beyond the 20 largest aggregators, the average number of relationships for major banks increased. This appears to be the result of two major banks having substantially more aggregator relationships than the other lenders.

337 For both questions, customer-owned banking institutions have substantially fewer relationships with aggregators (although those relationships were evenly split between the largest aggregators and other aggregators).

338 We explored the reasons why customer-owned banking institutions may have relationships with fewer aggregators in our discussions with the members of COBA.

339 Two COBA members told us that a barrier to entry for smaller lenders was the cost of setting up and maintaining the required information technology (IT) infrastructure to communicate with aggregators’ IT platforms. To receive home loan applications electronically, lenders need to use portals that can communicate with aggregators’ platforms. In addition, most brokers expect to be able to lodge applications electronically and may be reluctant to use a lender with whom they have to lodge paper applications.

340 Another issue for smaller lenders is the potential problem of receiving too many home loan applications to process within a reasonable timeframe, given their more limited resources and scale. Having relationships with a smaller number of aggregators is one way to control the volume of applications received; another is to offer more niche home loan products.

341 Some smaller lenders commented on the preference of some aggregators to deal only with larger lenders. One small lender also noted their inability to compete with larger lenders in sponsoring aggregators' conferences and other professional development days for brokers. This lender rejected a major aggregator who was putting pressure on them to contribute significant funds to networking events for brokers.

342 This smaller lender commented:

> most brokers deal with 4–6 lenders on a regular basis and it's very hard to break into that group for a new lender, even more so for smaller lenders (in other words, the volume of lenders and products on the panels makes it difficult to break into established networks) particularly when we're unable to sponsor industry events.

343 Other smaller lenders commented on the potential reputational risks of using the broker channel and the loss of face-to-face contact with their borrowers that many smaller lenders value highly. However, most considered this risk was offset by the benefits of growing their business and reaching a wider geographical market—and a younger market—despite the need to grow in a conservative and measured way given the costs involved.

344 We also asked the lenders in our review about their processes for reviewing the ongoing suitability of, and maintaining a relationship with, aggregators. This included how frequently they reviewed:

(a) the sales volumes of the aggregator;

(b) the credit profile or performance of residential loans originated through the aggregator (e.g. home loan default rates); and

(c) the risk controls of, and compliance by, the aggregator and its broker businesses/brokers.

345 Most lenders reported that they regularly reviewed the sales volumes of aggregators. It appeared to be common practice to review sales volumes on a monthly and yearly basis. Although less common, most lenders had a process to review the credit profile or performance of home loans originated through the aggregator. Approximately 60% of lenders did so monthly.

346 We note that, while these lenders may review the credit profile or performance at a whole-of-aggregator level, there did not seem to be any processes for such reviews on a broker business or broker basis: see paragraphs 993–1000. As a result, it is unclear whether lenders could identify problems at a broker business or broker level, where they do not cause a significant effect on the overall aggregator results.

347 Just over 60% of lenders stated that they had a process to review the risk controls of, and compliance by, aggregators and broker businesses/brokers, typically on an annual basis. Based on the commentary, these processes

generally seemed to be limited to reviewing a sample of loan files rather than the underlying control and framework.

348 We also asked whether, in 2012 and 2015, any lender–aggregator agreements had been terminated as a result of this review process. We specifically asked whether the termination was due to proven or suspected misconduct by the aggregator or its broker businesses/brokers, or concerns with risk and compliance controls within the aggregator. No lenders reported that any agreements had been terminated on that basis (although it was noted that relationships with particular brokers may have been terminated).

Why aggregators add or remove lenders from a panel

349 For a lender's home loans to be recommended by a broker, that lender needs to be added to the aggregator's 'panel'. The panel is a list of lenders with which the aggregator has entered into a contractual relationship. However, as discussed at paragraphs 793–803, merely being added to a panel does not guarantee the lender any significant flow of loans.

Note: There may be limited circumstances where a broker may recommend an 'off-panel' home loan (see paragraphs 324–327).

350 To understand an aggregator's process for adding a lender to their panel, we asked a series of questions about their approach to:

(a) major banks;

Note: In this context, we expect that aggregators considered the major banks to be limited to the primary brands of CBA, Westpac, ANZ and NAB, rather than sub-brands such as Bankwest, St George and UBank.

(b) other banks;

(c) customer-owned banking institutions; and

(d) non-ADI lenders.

351 We asked aggregators, for each type of lender, whether they considered that their panel required:

(a) as many of that type of lender as possible (or, in the case of the major banks, all of those lenders);

(b) a selection of that type of lender; or

(c) none of that type of lender.

352 All the aggregators responded that the panel should include all the major banks.

353 Approximately 65% of aggregators said that the panel should include 'as many as possible' other banks, while the remaining aggregators considered that the panel only required a 'selection of' other banks. One aggregator's reason for answering 'as many as possible' was that more choice is always better for consumers (this is in contrast to our findings on the limited number of lenders

actually recommended by individual broker businesses, as discussed in paragraphs 799–806). Another aggregator highlighted the need to satisfy regional or local consumer preferences. The reason given for choosing only 'a selection' was to avoid requiring brokers to be familiar with too many lenders.

354 In contrast to 'other banks', only 21% of aggregators considered that their panel should include 'as many as possible' customer-owned banking institutions. Almost 65% of aggregators considered that the panel should include 'a selection of' these lenders. One aggregator considered that there was no specific need to include these lenders on their panel. That aggregator noted that a lender's product offering was the important consideration, rather than the type of lender.

355 The reasons given by the aggregators who considered that their panel required a 'selection of' customer-owned banking institutions included a need for diversity for clients and to satisfy client preference for these lenders.

356 Almost 45% of aggregators stated that their panel should include 'as many as possible' non-ADI lenders. The remaining aggregators considered that their panel should include a 'selection of' non-ADI lenders. The ability for these types of lenders to service particular specialties (including credit-impaired borrowers and those who fall outside standard credit policies) and offer unique solutions were given as reasons to include them on the panel. One reason given for limiting non-ADI lenders was the risk that these businesses may have potential funding issues in poor economic conditions.

357 We also asked aggregators to rank a series of factors in order of importance when choosing which lenders to add to their panel from each lender type (e.g. what were important factors when choosing which customer-owned banking institutions to add to the panel and whether those factors are the same when considering whether to add a non-ADI lender).

358 The same factors were considered as important across all four lender types. The three most important factors were, in descending order, 'Financial strength/ stability', 'Value for money offered by the lender', and 'Client expectation'.

359 As part of the list of factors, we asked aggregators to rank the importance of the following statements in relation to commissions:

(a) 'Maximise commission payable to brokers';

(b) 'Commission rates are similar to other lenders'; and

(c) 'Maximise commission and other amounts payable to the aggregator'.

360 None of those factors ranked highly for the aggregators. However, 'Commission rates are similar to other lenders' was somewhat more important than 'Maximise commission payable to brokers'. The final statement, 'Maximise commission and other amounts payable to the aggregator' was ranked low by most aggregators.

361 As a general observation, it appears that major banks are generally selected for panels because they are major banks. Other lenders seem to need a reason to be added to a panel, either based on products they offer or because they offer an alternative that may appeal to some consumers (e.g. an alternative to a major bank).

How brokers are accredited

362 Whether a particular broker that operates through an aggregator can sell a particular lender's home loans depends on the lender 'accrediting' that broker. Accreditation is an additional governance step taken by lenders, which generally involves basic checks such as licensing status or membership of an industry association: see paragraph 1007.

363 We asked lenders whether, under their lender–aggregator agreements, they are required to accept all brokers put forward by the aggregator or whether they have a discretion on which brokers to accredit or maintain as accredited. Most lenders (approximately 85%) reported that they retain absolute discretion whether to accredit a particular broker, or maintain that broker as accredited.

364 We asked aggregators about their requirements for brokers to be accredited by lenders. Overall, aggregators generally appeared not to dictate which lenders a broker must be accredited with. This means that brokers can largely choose which lenders they deal with in an aggregator's panel.

Note: A broker may also recommend a loan from an 'off-panel' lender; however, we understand that this is not standard practice (see paragraphs 324–327).

365 In particular:

(a) around 20% of aggregators reported that they required brokers to be accredited with all lenders on the aggregator's panel;

(b) one aggregator stated that they set out the specific lenders with which brokers must be accredited;

(c) one aggregator reported that they required brokers to be accredited by the lender that is a related body corporate of the aggregator (out of a total of nine aggregators that are related to lenders); and

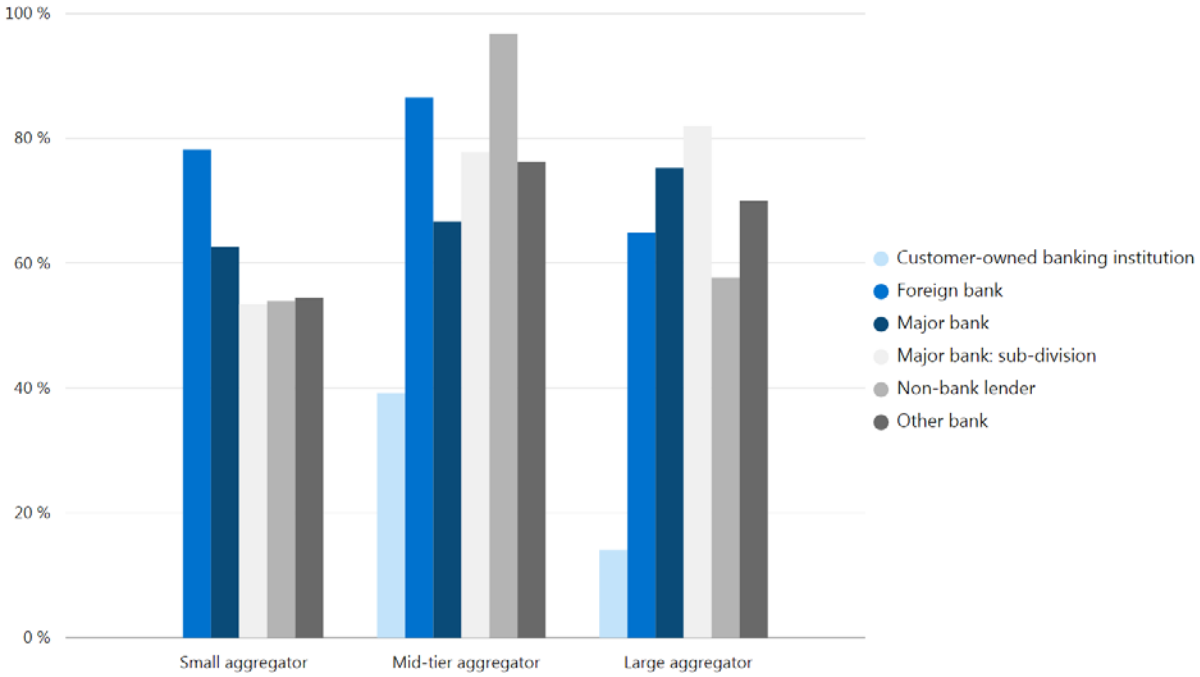
(d) two aggregators stated that brokers must be accredited with the lender that issues that aggregator's white label product (out of a total of 12 aggregators that identified as offering white label products).

366 We asked lenders, for the aggregators with which they had an agreement, how many brokers they had accredited for those aggregators. CBA had agreements with 19 of the 20 aggregators in our list and generally had the most brokers accredited for each of those aggregators. On that basis, we used CBA's numbers of accredited brokers as a baseline with which to compare the other lenders.

367 Figure 9 shows the number of brokers accredited with each type of lender as compared to CBA.

Note: This figure does not include one small aggregator with which CBA does not deal. None of the customer-owned banking institutions dealt with this aggregator either.

Figure 9: Average number of brokers accredited per aggregator (as a proportion of CBA's brokers)



Note: See paragraphs 369–370 for a description of the trends shown in this figure.

368 Compared to the average for each type of lender, CBA had significantly more brokers accredited for each aggregator. On a lender-by-lender basis, CBA generally had more accredited brokers for each aggregator (although there were a handful of exceptions).

369 Mid-tier aggregators tended to have a proportionally higher number of brokers accredited with non-ADI lenders, which probably reflects those lenders' specialised status in the industry (i.e. brokers will seek to become accredited with those lenders so they can recommend those specialised products when necessary).

370 Interestingly, customer-owned banking institutions had significantly fewer brokers accredited from each aggregator with which they dealt (and had no relationships with aggregators that we categorised as 'smaller aggregators'). This appears to indicate that not only do customer-owned banking institutions have arrangements with fewer aggregators, they also have access to fewer brokers within the aggregators with which they deal.

C How aggregators and brokers are paid

Key points

Aggregators and brokers are primarily remunerated through commissions paid by lenders. Brokers can also receive soft dollar benefits, including overseas trips awarded on the basis of home loans sales.

We found significant variation in the arrangements that exist in the mortgage broking market, with differences in both the rates of commission payable and the methods of calculation of commission.

The standard commission model is supplemented by bonus commissions and soft dollar benefits; both of which are likely to be significant motivators for brokers to send loans to a lender to qualify for those benefits (even where the choice of lender may not be in the consumer's interest).

Overview

371 Brokers typically do not earn a salary, and generally do not charge fees directly to consumers. Therefore, most brokers' entire income is derived from commissions. In addition, brokers may have access to various soft dollar benefits that are linked to the sale of home loans.

372 Both of these types of payments are designed to provide incentives for particular broker conduct in relation to choice of home loan products for consumers, and have the potential to cause conflicts between the interests of the consumer and the interests of the aggregator or broker.

373 Remuneration structures in the mortgage broking market can broadly be grouped into the following categories (although, our review found that there is significant variation and complexity within each category):

(a) upfront commissions (paid by the lender when the loan is taken out);

(b) trail commissions (paid by the lender each month while the loan is active);

(c) volume and non-volume bonuses (paid on top of other commissions if the qualifying criteria are met); and

(d) non-monetary (or 'soft dollar') benefits.

Upfront and trail commissions

374 The use of upfront and trail commissions, which are determined as a percentage of the value of the loan, was apparent across all arrangements in our review. The level of commissions varied between lenders and, in some

cases, also within lenders on an aggregator-by-aggregator basis. Upfront and trail commissions did not appear to be influenced by the cross-selling of other products with the loan.

375 Typically, the commission payments will be paid by the lender to the aggregator. The aggregator will retain a portion of the payment and pass the rest on to the broker.

376 In 2015, based on data we received from aggregators, the average rate of upfront commission and annual rate of trail commission paid by lenders to aggregators was 0.62% and 0.18%, respectively. On a $500,000 home loan, this equates to an upfront payment of $3,100 and a trail payment of $75 per month (or $900 in the first year of the home loan).

377 The average rate of upfront commission and annual rate of trail commission passed on by aggregators to broker businesses was 0.54% and 0.14%, respectively. On a $500,000 home loan, this equates to an upfront payment to the broker business of $2,700 and a trail payment of $58 per month (or $700 in the first year of the home loan).

378 Based on the difference between the rates of commission received by the aggregator and those paid onto the broker business, it appears that the aggregator retains just under 15% of the upfront commission and just over 20% of the trail commission.

379 There was considerable variation in the rates paid by different lenders. We observed that the upfront commission for brokers operating under one particular aggregator differed by up to 0.68% between lenders. This means that the upfront commission on a $500,000 loan could vary by up to $3,400 depending on the lender chosen.

380 Even the variation in the rates of commission paid to individual broker businesses by ADIs alone tended to be at least 0.10% between lenders, while variations of over 0.30% were not uncommon.

381 Various factors can have an impact on the particular rate of commission—for example:

(a) the type of home loan chosen;

(b) the credit limit of the loan;

(c) the LVR;

(d) the borrower’s credit risk;

(e) whether the loan is for owner-occupier or investment purposes; and

(f) the loan payment type (e.g. principal and interest or interest only).

382 We also found broker remuneration arrangements that allowed the broker to further discount the interest rate paid by the consumer, with a corresponding

negative impact on the broker's commission. While the ability of the broker to provide a further discount can potentially benefit consumers, we are concerned where this type of arrangement creates a clear conflict of interest for the broker.

383 We found significant variation in the extent to which each of the factors listed above influenced the rate of commission. In addition to these factors, the rate of trail commission for some lenders, which is paid on a monthly basis while the loan is active, increases the longer the home loan is open.

Bonus commissions

384 Bonus commissions are payments made by a lender to an aggregator or an aggregator to a broker on top of standard commission payments, where the payment is subject to the aggregator or broker meeting certain targets (e.g. the sale of a certain amount of a lender's loans over a year).

385 We saw a variety of bonus commissions being made available to aggregators—both volume and non-volume based. Based on the information provided by aggregators, it was unclear how much of these bonus commissions were passed on to the broker

386 Volume-based payments are dependent on the volume of home loans sold. For example, one offer in our review included a bonus commission that was calculated as a percentage of the total loans written in a year. The bonus started at 0.10% and increased up to 0.35% if at least $150 million in loans was sold in the year. This means that the lender was paying a much higher commission (i.e. upfront plus volume-based commission) to the aggregator for loans sold after the total value of loans exceeded $150 million.

387 We found there was a large degree of variation in the payment of volume-based commissions, which are usually agreed to by a lender on an aggregator-by-aggregator basis (i.e. the same offer is not made to all aggregators).

388 Non-volume based payments are payments that are dependent on something other than the volume of home loans sold. Examples in our review included payments based on the rate of home loan applications converted into settled loans, the proportion of applications that were submitted online and the average LVR of home loans settled.

389 We also identified 'campaign-based' commissions, which are higher rates of upfront and trail commissions offered on a time-limited basis. Lenders may use these offers to increase the flow of broker-originated loans on a targeted, short-term basis. As discussed in Section E, we observed that some brokers sent more loans to lenders who were offering campaign-based commissions during the offer period.

Soft dollar benefits

390 Soft dollar benefits given to brokers by lenders or aggregators include any rewards that are not cash. Receipt of the benefits can depend on the sale of all home loans (or specific types of home loans like white label loans).

391 The two most important forms of soft dollar benefits identified in our review were:

(a) broker clubs offered by some lenders and aggregators (which are a form of loyalty program); and

(b) free attendance at conferences, including those held in overseas locations.

392 Broker club membership is offered to individual brokers by lenders based on the value of loans sent to the lender, and offers benefits such as enhanced service from the lender and access to hospitality events hosted by the lender. We found that there are different tiers within broker clubs, each offering different levels of benefits.

393 High concentrations of loans were written by brokers to lenders that offered membership in a broker club. In one case, 11 members of a lender's highest broker club tier (out of a total of over 14,000 brokers) wrote approximately $1 billion of loans in 2015 (or 3% of all loans written by brokers for that lender). We re-confirmed this finding with the lender.

394 We observed aggregators offering soft dollar benefits to their top performing brokers, including free attendance at overseas conferences. In some cases, attendance was offered specifically based on the broker's sale of white label loans rather than all loans. One aggregator paid over $1 million on one such conference; an all-expenses paid Caribbean cruise with a per-broker cost of $13,000.

Effect of commissions and incentives on conduct

395 There is a risk that some types of arrangements—specifically, those under which the aggregator or broker is motivated primarily by the desire to maximise their commissions or other benefits—could result in poorer outcomes for consumers.

396 In our view, bonuses—including volume and non-volume based bonus commissions, campaign-based commissions and soft dollar benefits—present an increased risk of poor consumer outcomes. If the bonus payment is passed on to the broker, this could act as an incentive for the broker to recommend those lenders' loans above those of other lenders.

397 If retained by the aggregator, the bonus could encourage the aggregator to seek to influence the recommendations of the brokers. Given their position

between lenders and brokers, aggregators could have significant scope to influence the loan recommendations of the brokers in their networks.

398 This could be through the provision of product recommendation software that gives preference to lender paying bonus commissions: see paragraphs 257–261. Alternatively, it could be through providing more access to brokers for those lenders (e.g. through annual broker conferences or training programs) for business development purposes.

399 Campaign-based commissions may encourage brokers to sell particular loan products to consumers for reasons that do not align with consumers' needs (e.g. to realise a special benefit during the campaign offer period).

400 Soft dollar benefits, even if not in the form of a direct monetary incentive, may have an impact on a broker's choice of product or lender, or lead a broker to process a greater number of loans, to obtain the benefit (e.g. enhanced lender service or attendance at an overseas conference). This is of particular concern where the consumer may end up with a home loan that does not meet their needs.

401 Another example of a potential tension between brokers' and consumers' interests is that a broker may recommend that a consumer take out a higher value loan to maximise the amount of their commission or benefit (which is calculated on the value of the loan). We consider this risk could be reduced if lenders pay upfront commission only on the amount the consumer uses.

402 While some lenders have taken steps in this direction by calculating the upfront commission on the amount drawn down, no lenders reduce the commission based on the amount in the offset account. Our review of the home loan data found that brokers may be putting consumers into higher value loans: see paragraphs 837–842.

How we calculated remuneration

403 For this review, our general approach to collecting information about the industry was to obtain relevant information through the use of survey questions. The questions covered topics that we considered important based on our preliminary work and were structured so that respondents had to give a closed answer.

404 We took this approach as it would not have been feasible to request and examine all the relevant documents (e.g. contracts and internal policies and procedures) from the large number of participants in the limited time available.

405 However, in some areas we took a dual approach by asking a limited number of survey questions about key elements of remuneration arrangements and

requesting copies of ‘term sheets’ between lenders and aggregators, and aggregators and broker businesses/brokers.

406 Term sheets are documents setting out the agreed terms between lenders and aggregators or brokers, and include contracts and letters of variation. We did not ask for copies of the written contractual arrangements between broker businesses and individual brokers.

Note: In this report, we refer to these documents collectively as ‘term sheets’, even though many of the terms we received for remuneration arrangements were contained in contract variations and additions sent by email or letter.

407 Based on the information we collected about remuneration arrangements, we note the following:

(a) *Volume of information*—Our request for term sheets produced a large number of documents, around 7,000 pages for lender–aggregator relationships alone. In the time available, it was not practical to undertake a comprehensive review of these documents. However, we have been able to carry out a targeted assessment of term sheets focused on key matters relevant to our review of broker remuneration.

(b) *Complexity of arrangements*—Most of the remuneration arrangements were complex. We found that in many cases the original term sheets were modified by later correspondence between the parties. These later documents frequently varied terms and commission types and amounts, without establishing a new single document that detailed all of the currently applicable terms of the arrangement. All of these documents needed to be read together to understand how the arrangements worked, which made it a more difficult and time-consuming process. One reason for the use of multiple documents may be due to legacy accounts, takeovers and mergers in the industry, with contract addendums overlayed on original terms rather than revising the contract documents.

(c) *Variations in rates*—A significant proportion of term sheets disclosed a commission rate that was different from the current rates.

408 Although we sought to review term sheets for both financial and non-financial incentives, term sheets generally did not appear to include all non-financial rewards (e.g. broker clubs and hospitality, which were offered as a matter of practice rather than forming a part of the agreement).

409 Lenders confirmed that they did not pay commissions directly to broker businesses or brokers for loans placed with the lender through an aggregator, unless the lender had a direct contractual relationship with the broker (although such arrangements are uncommon). For this reason, our review focused on cash incentives paid to broker businesses or brokers by aggregators only, which predominantly involved the on-payment of commissions received by aggregators from lenders.

410 In this report, we describe the rates of commission that were *actually* received by aggregators and broker businesses as derived from the loan flow and home loan data provided to ASIC.

Commissions from lenders to aggregators

411 We reviewed lenders' responses to our survey and lenders' term sheets setting out their remuneration arrangements with aggregators.

412 In response to our survey, lenders confirmed that their remuneration arrangements with aggregators were primarily based on an upfront commission and trail commission, each of which was calculated as a percentage of the loan value.

Note: Some survey responses from lenders indicated that fixed dollar commissions were paid on some less common types of home loans that were outside the scope of our review (e.g. equity release and bridging loans).

413 As well as understanding how upfront and trail commissions were calculated, we sought to understand:

(a) the prevalence and nature of short-term variations to the commission structure offered by lenders (referred to in this report as 'campaign-based commission structures');

(b) the prevalence and nature of accelerated rates of commission or 'bonus' commission payments between lenders and aggregators; and

(c) provisions relating to the recovery of commissions already paid (i.e. 'clawbacks') and stoppage of ongoing trail commission payments.

Upfront commissions

414 All term sheets we reviewed had a base or standard rate of upfront commission that was paid as a percentage of the loan amount.

Note: For a discussion of what different lenders mean by 'loan amount' for the purposes of determining commissions or other incentives that are payable, see paragraphs 440–451.

415 The rate of upfront commission paid by all lenders to aggregators as disclosed in the term sheets ranged from 0.375% and 1.1%, but was usually between 0.5% and 0.8%. Based on the term sheets, many lenders paid each aggregator in their network the same upfront commission; however, some lenders varied amounts between aggregators. Based on our lender survey, approximately 70% of lenders reported that they paid the same rates of upfront and trail commission to all aggregators with which they dealt.

416 Where individual lenders did vary the rate of upfront commission paid to aggregators in their networks, term sheets indicated that the difference in

what was paid to different aggregators by that lender generally ranged from 0.05–0.10%, although it was sometimes much larger—up to around 0.20% (and, in one case, up to nearly 0.50%).

417 We asked lenders whether they varied their standard commission structure during each year between 2012 and 2015. Based on lenders' responses, it appeared that lenders, on average, varied approximately 20–30% of agreements each year.

Loan-specific factors that affect the rate of upfront commission

418 In our survey, we asked lenders about the loan-specific factors that could affect the rate of upfront commission they paid to aggregators, and the overall metrics that could affect those rates for individual loans. These factors are important as they may affect the advice and assistance provided by the broker to a consumer. For example, these factors may result in brokers structuring loan applications or recommending particular products based on the ability to earn a higher commission.

419 We provided a list of factors to lenders and asked them to state whether each factor could affect the rate of upfront commission paid on a specific loan. The factors and responses were:

(a) the type of home loan chosen (six lenders);

(b) the credit limit of the home loan (five lenders);

(c) the LVR (three lenders, with one other lender suggesting it was a factor for some, but not all, of its lender–aggregator agreements);

Note: Lenders' term sheets indicated that some lenders paid higher upfront commission for loans with a lower LVR.

(d) the credit risk of the borrowers (two lenders);

Note: Further analysis of the term sheets identified that one of these lenders varied upfront commissions based on the risk rating of the loan. The effect of the risk rating was that aggregators would be paid a higher rate of upfront commission for loans with a higher credit risk (where a higher interest rate would apply to those loans). Conversely, the other lender paid higher commission for 'prime' loans (i.e. loans that met its standard lending criteria) than for 'near prime' loans (i.e. loans that were usually provided to self-employed consumer or consumers who may have an adverse credit history). Near prime loans also tended to attract a higher interest rate.

(e) whether the loan was for an owner-occupier or investment property (one lender); and

(f) the loan payment type, such as principal-and-interest or interest-only repayments (one lender).

420 One lender noted that the rate payable was also dependent on whether the loan was placed in a securitisation vehicle, in which case the lender paid an additional amount of commission (as a percentage of the loan).

421 Three lenders reported that the upfront commission payable on the loan may be reduced if the broker negotiates a pricing discount for the consumer. Two of those lenders may reduce the upfront commission rate if the broker negotiates a lower interest rate of the home loan, while the other lender may reduce the upfront commission if the broker negotiates for the application fee to be waived.

422 No lenders reported that the rate of upfront commission was dependent on the broker selling other products with the home loan (including a home loan ‘package’ that may be offered with the loan), although some lenders noted that a separate payment may be made for sales of those products.

Note: For a discussion of cross-selling arrangements, see paragraphs 597–611.

423 Six lenders advised that there were no loan-specific factors that affected upfront commissions and that aggregators would receive the same commission regardless of the loan product or structure chosen. In other words, the rate of upfront commission was the same for all loans provided by the lender through the aggregator.

424 Our review of term sheets identified other factors affecting upfront commissions:

(a) one lender varied the upfront commission payable if the amount of new money being lent was very small, while others paid no commission for small top-ups or smaller loans; and

(b) for any commission to be paid, one lender required at least 75% of the credit limit to be drawn down (the upfront commission was based on the amount drawn down and not the full limit).

425 No lenders reported changing the loan-specific factors that affected the rate of upfront commission between 2012 and 2015 (other than those arising from a lender entering the broker market or the introduction of a new product range).

Trail commissions

426 For all lenders surveyed, trail commissions were paid monthly. The rate was calculated as the monthly allocation of an annual percentage of the ongoing loan amount while the loan continued. Trail commissions ceased to be paid after a loan was repaid.

Note: We had heard anecdotally that trail commission payments did not start until after the first year. However, we did not find any reference to this in our review of term sheets.

427 Trail commission rates varied across lenders, but generally ranged from 0.1–0.35% of the ongoing loan amount annually. Similar to upfront

commissions, some lenders paid each aggregator the same rate of commission, while others varied the rate between aggregators.

428 We observed from the term sheets that lenders broadly structured trail commission percentages in two ways: flat and tiered.

429 Flat trail commissions provide the same commission percentage rate regardless of how long a loan has existed (e.g. 0.15% per year). Roughly half the lenders paid flat trail commissions.

Note: However, one lender that paid a flat rate of trail commission varied that rate based on the total amount of lending placed by the aggregator with that lender (effectively a 'volume-based trail commission'); the greater the volume, the higher the rate of trail commission paid.

430 Lenders that paid tiered commissions generally increased the rate of commission after each year for a fixed number of years (usually three years). Some lenders did not start to increase the rate until the loan had been opened for several years (e.g. three or four years). Lenders commonly applied two or three tiers, while one lender used four tiers. In all cases, the maximum rate of commission was reached by year five, if not earlier. From survey responses, in 2015 eight lenders increased the rate of trail commission based on the length of time the loan was opened (an increase of one lender from 2012).

431 Based on the term sheets, one lender allowed aggregators to claim an amount upfront that represented their entitlement to trail commissions if they waived their rights to an ongoing trail commission.

432 The payment of ongoing trail commissions usually provides an incentive to aggregators and brokers to put forward higher quality loans where consumers are less likely to default on their obligations. However, the option to waive trail commissions in favour of an upfront payment removes this incentive and is likely to increase the risk that aggregators and brokers will be less selective about which loans they put through to the lender. We would expect this lender to assess whether there is a difference in performance of the loans where this right has been exercised.

Loan-specific factors that affect the rate of trail commission

433 Overall, 15 lenders surveyed stated that there were no loan-specific factors that affected the rate of trail commission paid. However, this appeared to be inconsistent with lenders' responses to other survey questions that indicated there were influencing factors, including:

(a) the type of home loan sold, with some products having a lower rate (two lenders);

(b) the credit limit of the loan (one lender);

(c) the LVR (one lender);

(d) the assessed credit risk of the consumer (two lenders).

Note: As with upfront commissions, two lenders appeared to have a divergent approach—one paid a higher rate of trail commission for consumers who met standard lending criteria, while the other paid a higher rate for loans to higher-risk consumers.

(e) as noted above, the length the loan had been opened, with trail commissions increasing over time (eight lenders).

434 Two lenders also reported that the rate of trail commission on a loan may be reduced if the broker negotiates an interest rate discount for the consumer.

435 Generally, lenders reported little change to these factors between 2012 and 2015, other than one lender who had introduced a tiered trail commission structure.

Why lenders pay trail commissions

436 Trail commissions operate as an incentive for brokers not to 'churn' their clients from one lender to another. Although a broker can earn another upfront commission if they do refinance a consumer with an existing home loan from one lender to another, they will lose their trail commission.

437 Trail commissions also exist in other parts of the financial services industry where commissions are still paid. In particular, trail commissions will continue to be permitted—up to a limit—under the pending reforms to the life insurance advice industry.

438 Although it is in lenders' interests to deter brokers from refinancing consumers with different lenders, trail commissions may be of concern where consumers would, in fact, be better off if they refinanced to another lender (e.g. because of a more competitive interest rate available).

439 Based on the data we reviewed, we did not identify trail commissions directly leading to poor consumer outcomes.

How the 'loan amount' is calculated for upfront and trail commissions

440 As noted earlier, all lenders calculated the upfront and trail commission based on the loan amount. However, the amount of commission paid depended, among other things, on how the lender defined the 'loan amount'.

441 This issue may be important in understanding whether a lender's commission structures are more likely to increase the risk of inappropriate advice being given to a consumer by a broker. In particular, some stakeholders have expressed concerns that brokers may recommend to consumers that they take out a loan that is larger than originally desired to maximise the commission.

442 A consumer is less likely to accept this advice if they will be charged interest on the additional funds. As a result, the consumer would be more likely to accept the broker's advice (i.e. to borrow a higher amount) if they could leave the additional funds in the loan account (i.e. as a redraw amount) or in an offset account.

Note: For a discussion about brokers recommending larger loans, see CHOICE's comments on their 2015 'Mortgage broker shadow shop'.

443 In our survey, we asked lenders to explain how they defined the loan amount for the purposes of calculating upfront and trail commissions, across ordinary home loans that have a fixed term (referred to in this report as 'non-line of credit home loans') and lines of credit. We also asked lenders whether the home loan amount was reduced by any other considerations (e.g. the balance in an offset account).

Non-line of credit home loans

444 When calculating *upfront commissions* for non-line of credit home loans, survey responses were as follows:

(a) Five out of 19 lenders based the loan amount on the amount actually drawn down. For these lenders, any funds left in the account were not included in the balance when calculating the upfront commission. All other lenders either calculated the loan amount on the approved credit limit or, based on internal policies and procedures, required the loan to be fully drawn down at settlement (which would have the same effect).

(b) No lenders reduced the amount used for the purpose of calculating the upfront commission by the amount held in an offset account.

445 These approaches do not appear to be designed to reduce the risk that a broker will recommend a higher loan to obtain a greater commission. While some lenders have taken steps to reduce this risk by paying commissions only on the drawn-down amount, brokers could still recommend that consumers place the additional funds in an offset account.

446 When calculating *trail commissions* for these home loans, survey responses were as follows:

(a) All but one lender surveyed calculated the trail commission based on the ongoing or prevailing loan balance from time to time. The other lender calculated the loan amount on the original loan amount.

(b) All lenders reduced the loan amount for calculating trail commissions in line with extra repayments, including redraw amounts.

(c) In contrast to upfront commissions, 10 lenders reduced the loan amount used to calculate trail commissions by the amount held in an offset account.

Lines of credit

447 Survey responses indicated that lenders calculated *upfront commissions* on lines of credit in one of three ways:

(a) based on the assigned credit limit (five lenders);

(b) based on a fixed percentage of the assigned limit (seven lenders); and

(c) based on the amount actually drawn down within a specified period (three lenders).

Note: A line-of-credit home loan is a credit facility, secured against a home, which can be reused over and over again.

448 The remaining four lenders did not offer lines of credit.

449 Several lenders reported that for the purpose of calculating upfront commissions, the loan amount could be reduced based on other factors, without providing details.

450 All lenders who offered lines of credit used the balance of the loan at the time of calculation when determining *trail commissions*.

451 All lenders noted that line-of-credit products do not come with offset accounts.

Value of upfront and trail commissions

452 The 14 aggregators in our review were asked to provide month-by-month details of the loans sent to all lenders with which they dealt (i.e. not just the 19 lenders in this review). This loan flow data included the number and value of new loans in that month, the number and value of outstanding loans and the commission payments made by each lender in that month.

453 Lenders were asked to provide data for all home loans provided in 2012 and 2015: see paragraphs 1053–1056.

454 We used this information to derive average commission rates and per-loan dollar payments.

455 For more detailed analysis of this data, see Appendix 2.

Derived rates of upfront and trail commission paid to aggregators

456 The median values of *upfront commission* rates paid to aggregators (based on aggregators' loan flow data) ranged from 0.46–0.65% of the loan amount, with the industry mean being 0.62%.

457 Within an aggregator, the difference between the lowest and highest paying lenders was 0.16–0.60%. For a broker choosing between recommending a loan from these lenders, this could mean an extra $800 to $3,000 in upfront commission payable to the aggregator on a $500,000 loan.

Note: The difference between the lowest and highest paying lenders is calculated at, respectively, the 5th and 95th percentile. As a result the difference between the absolute lowest and highest paying lenders will be greater.

458 Across all aggregators the lowest average upfront commission rate paid by a lender was 0.01% and the highest average rate was 1.56%.

459 Using aggregators' loan flow data, we estimated the average annual rate of *trail commission* payable by lenders for each aggregator. The median value of the trail commission rates ranged from 0.15–0.19% of the loan amount, with the industry mean being 0.18%.

460 Within an aggregator, the difference between the lowest and the highest paying lenders ranged from 0.06–0.17%. This could mean an extra $300–$850 per year in trail commission on a $500,000 loan balance, depending on which lender was chosen by the broker.

Note: The difference between the lowest and highest paying lenders is calculated at, respectively, the 5th and 95th percentile. As a result the difference between the absolute lowest and highest paying lenders will be greater.

461 Across all aggregators the lowest annual rate of trail commission rate paid by a lender was 0.01% and the highest average rate was 0.35%.

Note: The above distribution is the average rate calculated across all loans introduced through the aggregator to the particular lenders. Further variation may occur between the rates paid for each individual loan sent to the lender by the aggregator.

Derived per-loan value of upfront and trail commission paid to aggregators

462 In preparing for this review, a number of industry participants told us that the work done by a broker on a loan is generally not dependent on the size of the loan. For this reason, we also derived the average per-loan amount of upfront and trail commission.

463 Based on aggregators' loan flow data, the average per-loan amount of upfront commission received from lenders varied from almost $0 to over $5,000. This was the average amount of upfront commission paid for *all loans* sent by the aggregator's broker network to that lender. The wide variation is therefore a result of a combination of different rates of upfront commission and loan sizes placed with particular lenders.

464 We also calculated the amount of upfront commission paid on particular loans by lenders. These amounts also varied widely (as would be expected when the commission depends on the loan amount), ranging from almost $0 up to over $7,400, which was paid by one lender as an upfront commission on 5% of loans sold by brokers in 2015.

465 Using aggregators' loan flow data, we estimated the average annual per-loan amount of trail commission paid by each lender to each aggregator. These average amounts varied from less than $100 to over $750.

466 For individual loans (based on lenders' home loan data), the estimated annual amount of trail commission ranged from almost $0 up to over $2,200.

Campaign-based commission structures

467 In preparing for this review, a number of stakeholders told us that lenders may offer higher rates of commission on a short-term basis from time to time. In this report, we refer to these offers as ‘campaign-based commission structures’. Stakeholders also noted that lenders typically expect that the additional commissions paid under such arrangements will be passed on to brokers by aggregators, unlike some other bonus commission payments (see paragraphs 475–502) that may be retained in full by the aggregator.

468 We understand that lenders may use these offers to increase the flow of broker-originated loans on a targeted, short-term basis. Some stakeholders noted that this type of arrangement may be offered at particular points in the lender’s business cycle (e.g. to meet sales targets just before the end of the business year).

469 However, such offers may increase the risk of brokers being improperly influenced to recommend a lender’s home loan, instead of other, more suitable loans.

470 We analysed the impact on lenders’ loan flow of some campaign-based commission structures offered between 2012 and 2015: see paragraphs 786–792. Based on our review of term sheets, we noted some overlap between campaign-based commission structures and volume-based commissions: see paragraphs 480–489.

471 In our survey, we asked lenders whether they had offered a special rate of commission (either upfront or trail) on a short-term basis at any time between 2012 and 2015. We also asked lenders to include details of these campaign-based commission structures with copies of their term sheets.

472 Six lenders reported that they had offered some form of campaign-based commission structure between 2012 and 2015. These structures were typically offered by non-major banks (although one sub-division of a major bank did provide such an offer in 2014). The offers usually related to the rate of upfront commission. However, one lender reported that, for a short period of time, they offered to pay trail commissions earlier for home loans that met certain criteria (including having an LVR below a certain threshold).

473 Apart from this offer, campaign-based commission structures generally involved a temporary increase in the rate of upfront commission paid on loans. For example, in 2015 one lender offered to increase the rate of upfront commission to 1% (from a previous rate of 0.88%, which itself was an increase over their standard rate of 0.65%) for a four-month period.

474 Another lender offered a campaign-based commission structure in 2013 that was dependent on the volume of settlements by a broker within a four-month period, where a broker could earn an additional 0.30% bonus commission for

settling more than $3 million in home loans. We understand that this offer was targeted specifically at brokers rather than at aggregators.

Accelerated rates of commission and bonuses

475 In our preliminary work for this review, stakeholders told us that some lenders may pay additional amounts of commission to aggregators based on overall metrics, either volume or non-volume based. Such amounts may be treated as an accelerated rate of commission on a specific loan based on overall metrics, or as a lump sum bonus payment that is dependent on, or calculated on, the total value of loans originated over a particular period.

476 In substance, there is little difference in how the additional amount is treated, although it may affect whether or not the additional amount is passed through to the broker by the aggregator (i.e. a ‘bonus’ payment is less likely to be passed on to brokers).

477 In our survey, we asked lenders whether there were any overall volume or non-volume based metrics that could affect the rate of upfront or trail commission paid to aggregators. We also asked whether, for each year between 2012 and 2015, a bonus had been paid to a list of 20 aggregators (the 14 aggregators surveyed as part of this review and an additional six aggregators). The bonus could be based on volume or non-volume metrics.

478 There were some inconsistencies in lenders’ responses to these questions. We expect that this may be due to differences in the way lenders see the particular additional payments (i.e. whether they are based on an accelerated rate of commission or are considered a bonus payment).

479 Overall, we found the different forms of bonuses (regardless of how they are described) to be complex and, in many cases, poorly defined in the term sheets (such that they are unlikely to have been reviewed by the lenders’ legal and compliance teams). We also query how these arrangements can be disclosed to consumers if they are not drafted clearly in the term sheets.

Volume-based commissions

480 We sought to understand whether there were any overall volume-based metrics that would result in an accelerated rate of commission being paid on particular home loans, or as a periodic lump sum bonus. Based on survey responses and our review of term sheets, there appeared to be a large variety of such additional payments being made available to aggregators.

481 In this context, ‘volume-based commission’ means a payment that is dependent on the overall volume of sales of home loans (regardless of how this is described).

482 In response to our survey, four lenders (including two major banks, one other bank and a credit union) reported that the rate of upfront commission paid was affected by the total value of home loans sold in a particular period. Two of these lenders introduced this feature between 2012 and 2015. Another lender had removed this feature since 2015.

483 In contrast, five lenders (including two major banks and three other banks) reported that they had paid a 'bonus' to an aggregator in 2014 that was dependent on the overall volume of home loans sold.

Note: The difference in these results is most likely due to lenders interpreting the particular survey questions differently.

484 The criteria for these payments were described in different ways by lenders. Examples included payments that are dependent on:

(a) total volume of sales in a particular period; or

(b) incremental growth in outstanding home loans over a particular period (which would take into account both new sales and retention of existing home loans).

Note: We identified one arrangement under which the bonus may be recoverable if there is negative growth in a subsequent year.

485 Based on our review of term sheets, these arrangements generally appeared to be negotiated by lenders with each aggregator (i.e. lenders do not seem to make the same arrangements available to all aggregators they deal with).

486 Table 4 gives an example of one lender's volume-based commission from 2014.

Table 4: Example of a volume-based commission (2014)

Commission tier	Bonus rate	Volume lower limit	Volume upper limit
Base tier	0%	$0	$80m
First tier	0.1%	Greater than $80m	$110m
Second tier	0.2%	Greater than $110m	$150m
Third tier	0.35%	Greater than $150m	$200m
Above 200	0%	Greater than $200m	No upper limit

487 Based on this bonus arrangement, the aggregator would receive a bonus commission equal to 0.35% on combined loan balances of $150–200 million in one year. As standard upfront commission rates tend to be around 0.60% of the loan amount, this would have the effect of increasing that more by more than half.

488 Some offers involved additional payments calculated on both volume and non-volume based criteria: see paragraphs 490–493. For example, one lender offered a bonus to one aggregator that was calculated on a pure volume basis. The lender then offered to increase that bonus by up to 50% if the aggregator exceeded certain quality-based measures and portfolio growth rates (both of which appeared to be poorly defined). It also appeared that failure to meet required growth rates could decrease the bonus that would otherwise be paid.

489 These bonus payments were not specifically identified in many of the term sheets between aggregators and broker businesses, and not all of them may be passed on to brokers.

Non-volume based incentives

490 We sought to understand whether there were any non-volume based metrics that would result in an accelerated rate of commission being paid on particular home loans or a periodic lump sum bonus being paid.

491 In this context a ‘non-volume based incentive’ means a payment that is dependent on something other than the value of home loans sold.

492 Based on our review of term sheets, there are a wide variety of such payments, including those that are dependent on:

(a) the rate of conversion of home loan applications into settled loans;

(b) the rate of approval of home loan applications;

(c) the proportion of applications that are submitted online;

(d) the quality of loan applications submitted by a broker (i.e. complete and without errors); and

(e) the average LVR across home loans settled.

493 Some examples of non-volume based bonuses include:

(a) a settlement conversion bonus that was paid if the percentage of applications to settled home loans exceeded 60%, where the rate of bonus depended on the percentage of applications settled and the overall value of loans originated in that year (with the maximum bonus equal to 0.15% of the total loan volume in that year); and

(b) an online application bonus that paid a bonus of up to 0.05% of the loan volume if at least 95% of applications were submitted online.

Value of bonuses derived from the aggregators’ loan flow data

494 Aggregators’ loan flow data included details of the value of bonus payments that were made by lenders (i.e. payments that were not ordinary upfront and trail commissions).

495 Aggregators identified that they had received bonus payments from 14 of the 19 lenders in our review between 2012 and 2015. This was more than the number of lenders in our survey who stated that they had paid bonus payments. Some additional bonus payments reported by aggregators may relate to campaign-based commission structures. However, this would not completely account for the difference.

496 Aggregators were not asked to differentiate bonus payments into volume and non-volume based amounts. As such they could be related to either volume based criteria or non-volume based criteria, or a mix of both.

497 Aggregators provided a dollar amount for each bonus they received from lenders, with significant variation in the dollar value of these payments. In 2015, the value of bonus payments ranged from very small amounts (e.g. less than $1,000) up to approximately $1.5 million.

498 We used the dollar value of bonus payments to calculate the value of the payment as a percentage of the total loans originated in the 12 months before the payment was made. This provided an estimate of the bonus payment rate.

499 Based on this analysis, it appeared that the rate of bonus payments ranged from very small (e.g. 0.001% of the total loan flow in the year) up to 0.084%. Values of between 0.020% and 0.050% were not uncommon.

Note: This is the average annual rate across the full four years. The value of the bonus payment as a percentage of loan flow in any one year may be greater.

500 We also derived the average annual base commission rate based on aggregators’ loan flow data: see paragraphs 456–461. For the lender who paid a bonus rate equivalent to 0.084%, this had the effect of increasing the average annual upfront commission rate from 0.68% to 0.76%.

501 The bonus payment between this lender and this aggregator was the equivalent of an additional $253 per loan, which increased the average per–loan commission amount from $2,037 to $2,290.

502 Other examples included a bonus payment equivalent to:

(a) 0.057%—this had the effect of increasing the upfront commission rate from 0.54% to 0.60%, or the average amount of upfront commission paid on home loans by $139 (from $1,336 to $1,475); and

(b) 0.041%—this had the effect of increasing the upfront commission rate from 0.62% to 0.66%, or the average amount of upfront commission paid on home loans by $107 (from $1,602 to $1,709).

Note: These figures are based on the aggregators’ loan flow data. In some cases, the lenders’ loan flow data showed different values of bonus commission. This indicates that lenders and aggregators may not treat such payments in the same way.

Clawback and commission suspension arrangements between lenders and aggregators

503 Clawback and commission suspension arrangements between lenders and aggregators (and ultimately brokers) are an important aspect of the overall commission arrangements. They have the potential to result in an aggregator (and typically a broker) having to pay back commissions already received and/or lose their right to future payments on a loan.

504 Commissions are typically clawed back if a loan is repaid or discharged early, or suspended if a loan goes into significant arrears. However, such provisions may also apply to other situations (e.g. if a loan is found to have involved fraudulent conduct).

505 We sought to understand the nature of clawback and commission suspension arrangements between the lender and the aggregator. We also sought to understand the frequency with which these rights were exercised by lenders.

Clawback of commissions

506 All lenders reported that their agreements with aggregators permitted them to clawback commission payments in certain circumstances.

507 The term sheets generally allowed for upfront commissions, in whole or in part, to be clawed back by the lender if the loan was terminated before a specified period (recovery period) had elapsed, usually including if the loan was refinanced.

508 Term sheets indicated that some lenders sought to clawback upfront commissions in other circumstances—including if, during the initial period of the loan term (e.g. in the first six months to two years, depending on the lender), the consumer:

(a) fell into arrears of 30, 60 or more days;

(b) defaulted; or

(c) did not draw down the loan funds.

509 From our review of term sheets, we observed that clawback arrangements for upfront commissions generally applied for 12, 18 or 24 months. Many arrangements required 100% of commissions to be refunded to the lender if the loan was terminated (or the other circumstances occurred), within 12 months of origination.

510 For some loans that terminated after 12 months, the percentage of upfront commission refunded under the clawback arrangement reduced (e.g. 50% down to 0% if the loan exceeded 24 months). One lender required upfront commissions to be refunded only if the loan terminated in the first six months.

Clawback and suspension of trail commissions

511 Trail commissions are generally payable while a home loan continues; however, we observed that some lenders required these commissions to be refunded or suspended in some circumstances. All lenders reported in the survey that their agreements with aggregators permitted them to recover and suspend trail commission payments from the aggregator in certain circumstances.

512 The situations where lenders reserved the right to suspend trail commissions varied more than for clawback of upfront commissions. Examples included where:

(a) the home loan was in arrears (this was most common and depending on the lender, could be anywhere from 30 days in arrears or longer);

(b) the lender suspected broker misconduct or unlicensed activity (pending investigation of the situation); and

(c) the balance of a line-of-credit home loan exceeded the permitted credit limit by a certain percentage.

513 Some lenders also reserved the right to suspend trail commissions if, at any point, the total value of outstanding loans with the aggregator or the monthly commission payments due to the aggregator fell below a minimum threshold.

Rates of clawback and commission recovery

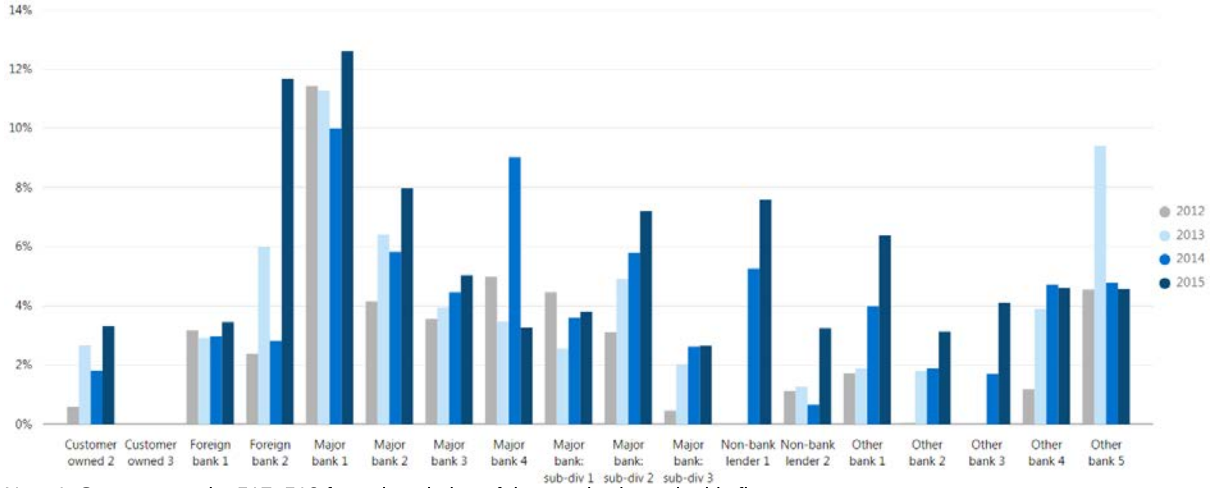
514 As part of the data collection process, we asked the 19 lenders in our review to provide month-by-month details of loans originated through each of 20 aggregators (14 in this review plus an additional six), including commission payments and clawback and commission suspension information.

Upfront commissions

515 We asked lenders to provide details of the value of upfront commissions clawed back each month. We also asked the lenders to separate those figures based on whether the clawback was due to the loan being repaid or discharged early or for another reason (including misconduct of the broker). Only a few lenders provided separate figures for the value of upfront commissions that were clawed back for reasons other than the loan being repaid or discharged early.

516 Figure 10 shows the average percentage of upfront commission recovered by each lender on a year-by-year basis due to the loan being repaid or discharged early.

Figure 10: Proportion of upfront commission clawed back due to the loan being repaid or discharged early



Note 1: See paragraphs 517–518 for a description of the trends shown in this figure.

Note 2: See Appendix 1 for an explanation of the meaning of the lender descriptions used in this figure.

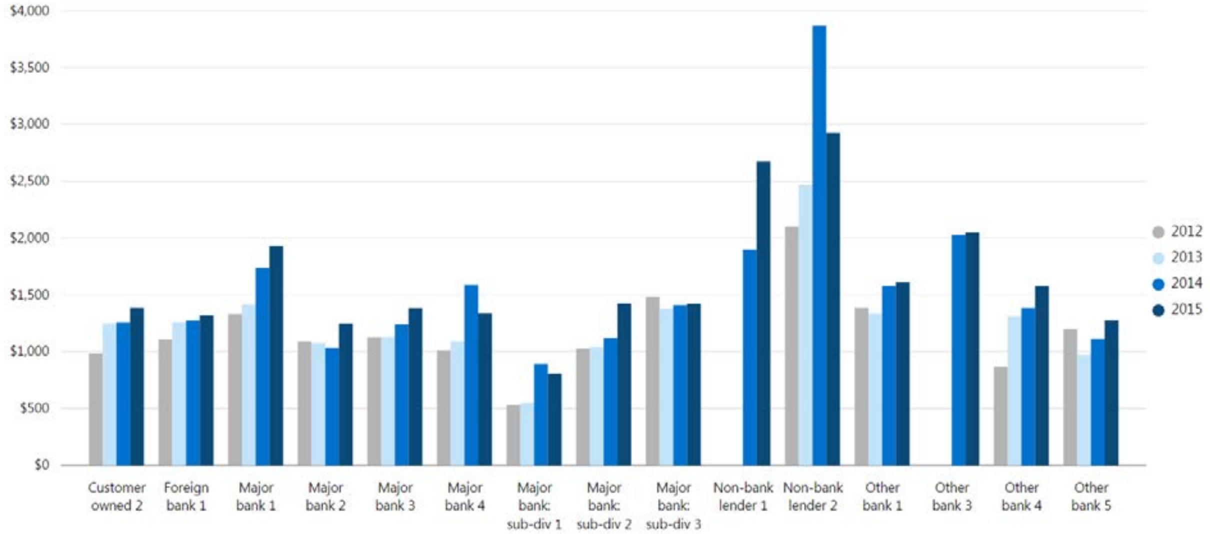
517 The proportion of upfront commission clawed back due to the loan being repaid or discharged early varied significantly between lenders, and for some lenders, over time. In 2015, two banks (one major bank and one other bank) recovered more than 10% of the upfront commissions paid.

> Note: One sub-division of a major bank advised that they were not able to differentiate the reasons for clawback. We have assumed all reported clawbacks were as a result of the loan being repaid or discharged early and are shown in the above figure.

518 Eight lenders provided details of upfront commissions recovered for reasons other than the loan being repaid or discharged early; however, these were minimal.

519 Figure 11 shows the average value of each clawback as a result of a loan being discharged early. The same labels are used as in Figure 10.

Figure 11: Average value of each clawback of upfront commission due to the loan being repaid or discharged early



Note 1: See paragraph 520 for a description of the trends shown in this figure.

Note 2: Not all lenders provided data for us to calculate the average value of each clawback of upfront commission.

520 The average value of upfront commissions recovered across all lenders exceeded $1,000. For the two non-bank lenders, this was nearly $3,000.

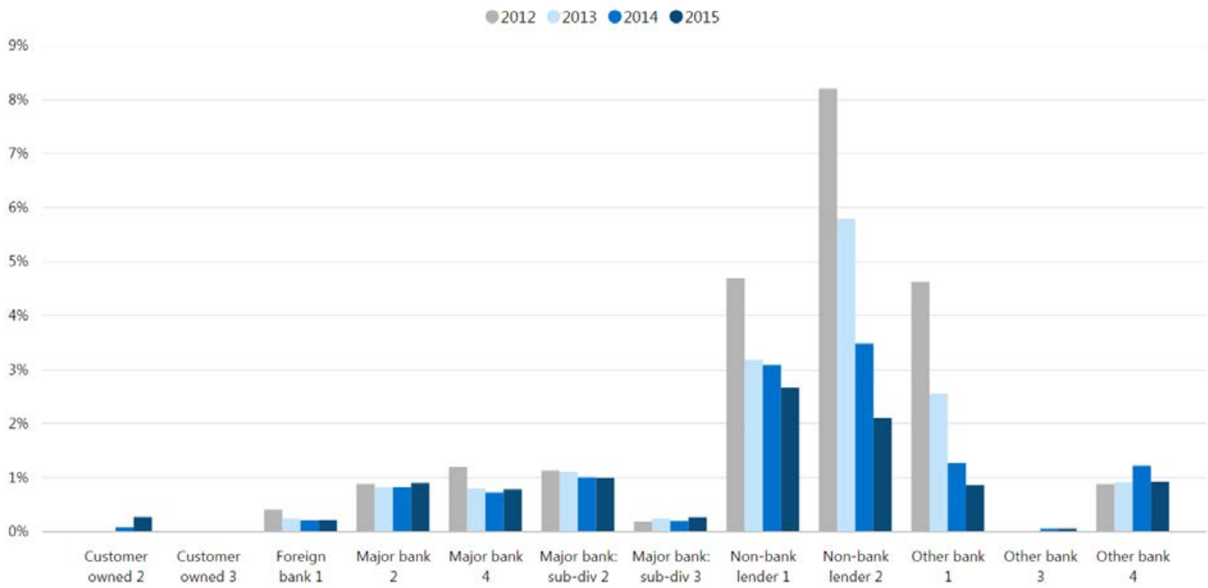
Trail commissions

521 We asked lenders to provide details of the value of trail commissions recovered each month and the value of home loans that were affected by the suspension of trail commissions.

522 Only nine lenders (out of 19) reported any recovery of trail commissions from 2012–15. These amounts were insubstantial other than for one lender, who reported trail commission recovery of over 3% in one year. Apart from this lender, recovery of trail commissions did not appear to be a significant component of commission recovery arrangements between lenders and aggregators.

523 Twelve lenders provided us with data on loans that had been affected by suspension of trail commissions due to the loan being in arrears. Figure 12 shows the value of home loans as a percentage of overall outstanding home loans affected by the suspension of trail commissions due to the loan being in arrears.

Figure 12: Value of home loans as a percentage of overall outstanding home loans affected by suspension of trail commissions due to loan being in arrears



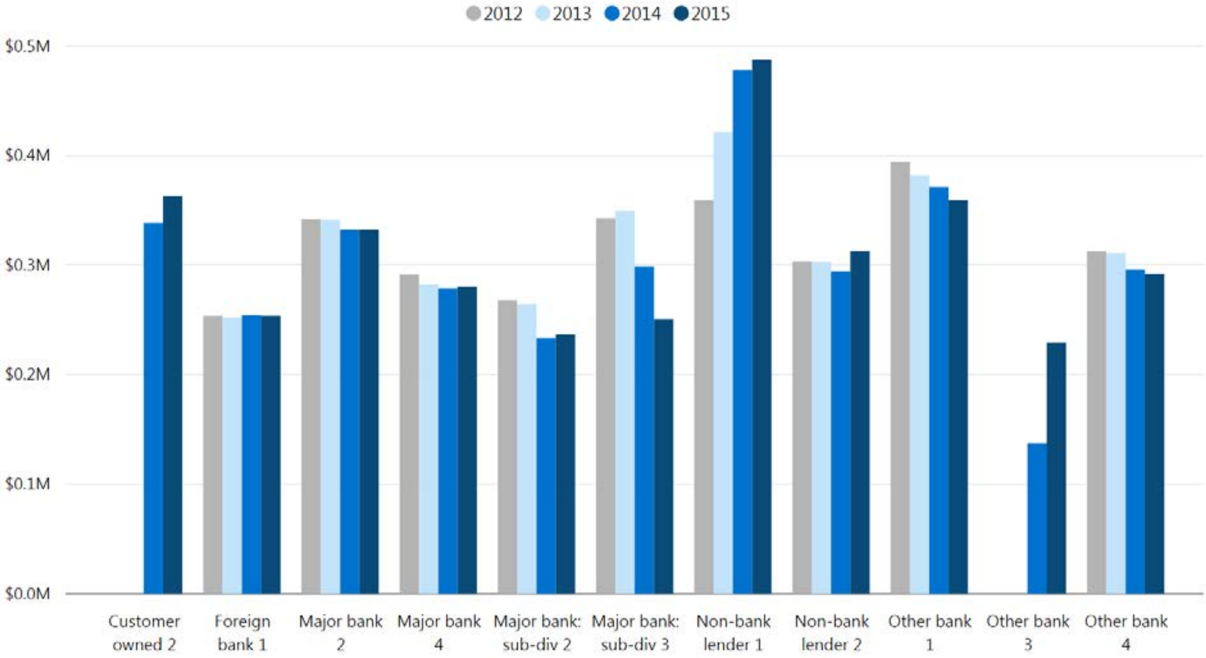
Note: See paragraph 524 for a description of the trends shown in this figure.

524 The data reported by three lenders indicated that in 2012 at least 4% of their home loans (by value) were affected by suspension of trail commissions (i.e. the loans were sufficiently in default for commission recovery). For each lender, this percentage decreased each year to 2015.

525 We also asked lenders to tell us the value of home loans affected by commission suspension for reasons other than the loan being in arrears. Four lenders reported any such loans. One major bank reported approximately 0.7% of their broker-introduced loans being affected in 2015. The other three lenders reported insignificant amounts.

526 Figure 13 shows the average value of each loan that was affected by the suspension of trail commissions due to the loan being in arrears.

Figure 13: Average value of each loan that was affected by suspension of trail commissions due to loan being in arrears



Note: See paragraph 527 for a description of the trends shown in this figure.

527 The average value of a home loan affected by the suspension of trail commissions in 2015 ranges from just over $200,000 up to almost $500,000.

Commissions from aggregators to broker businesses

528 Aggregators pass on the commissions received from lenders to broker businesses or brokers in one form or another. In doing so, they receive payment from the broker business or broker for their aggregation services.

Note: We asked aggregators whether, if an individual works in a broker business, the aggregator pays the commission to the business (who pays it to the broker) or to the broker directly. Unlike lenders, who typically only pay commissions to aggregators, aggregators reported a mixed approach. Just over 40% of aggregators paid commissions only to broker businesses. The remaining aggregators paid both businesses and individual brokers.

529 A broker business will generally pay the aggregator in one of two ways:

(a) the aggregator may take a portion of the commission received from the lender and pass on the rest (and potentially charge other fees); or

(b) the aggregator may charge a periodic fee that is not directly related to the sale of any particular home loan and pass on the full commission.

530 In either case, in this report we refer to the amounts levied by aggregators as ‘fees’ for providing aggregation services. How an aggregator levies its fees may have a material impact on the way that commissions are passed on to brokers. For example, one aggregator passes on to brokers the same rate of commission for all lenders with which it deals (i.e. the fees that it retains from the commission paid by each lender differs). This aggregator considers that some of the conflicting nature of commission payments is removed so that its brokers do not have incentive to send loans to the highest commission paying lender.

Fees charged by aggregators

531 We sought to identify the nature and extent of fees aggregators charged broker businesses for their services. Responses to our survey and our review of term sheets indicated that fees are charged in a variety of ways. For example, some aggregators charged a monthly fee regardless of the flow of loans put through by the broker. Other aggregators retained a portion of commissions earned from loans put through by the broker before passing on the remainder.

532 Responses to our survey indicated that approximately one third of aggregators had the same fee structure for all of their broker businesses.

533 Around 30% of aggregators indicated that they allowed broker businesses to choose the type of fee structure from a number of options.

534 The most common types of fees were those charged for each on-payment by the aggregator of upfront and trail commissions to the broker business. This was usually charged as a percentage of the commission amount received from the lender, although some aggregators reported charging a flat amount.

535 Many of the aggregators’ term sheets we reviewed indicated that a fixed percentage of upfront commissions received from lenders was passed on to brokers, usually around 80% or more of the upfront commission (which would equate to a 20% ‘fee’ charged by the aggregator). In contrast, a few aggregators passed on much smaller amounts, less than 40% in some cases.

536 We also reviewed term sheets where commissions were passed on to broker businesses at variable rates. For example, some aggregators applied a tiered structure for the percentage of the commissions they passed on to brokers. In some cases, higher percentages were paid to broker businesses that had higher volumes of loan amounts settled.

537 Almost 50% of aggregators reported that they may charge periodic fees to broker businesses. Some term sheets indicated that, due to the payment of periodic fees, the aggregator would pass on all of the commission received.

538 In relation to periodic fees:

(a) two aggregators stated that the fee decreased when the total number or value of home loans originated through the broker business increased (no aggregators increased the fee in those circumstances);

(b) one aggregator stated that, in some cases, the fee depended on the total value of white label loans sold;

(c) three aggregators stated that the fee depended on the number of brokers accredited in some or all cases; and

(d) three aggregators stated that the fee depended on the fee structure chosen by the broker business.

539 Less common fees included sign-on fees payable when the broker business first joined the aggregator's network or a new broker was brought into the business. Aggregators also reported charging fees if a broker was appointed as the aggregator's credit representative. One aggregator noted that it charged a marketing fund contribution fee.

Short-term discounts

540 We asked aggregators whether they offered any short-term fee discounts, either as a general offer to all broker businesses or only to specific broker businesses. These offers would be similar in nature to the campaign-based commission structures that some lenders offer. We asked this question for home loans in general and, specifically, for any white label home loans.

541 Aggregators did not generally make these types of offers available either for home loans generally or white label home loans. A small number of aggregators noted that as an ongoing practice, they may offer special introductory arrangements to new brokers (through reduced fees or higher percentages of commission being passed on to broker businesses).

Value of upfront and trail commissions

542 In addition to month-by-month details of all loans that were sent to lenders by each aggregator, we asked the 14 aggregators to provide yearly data on the origination of loans by 15 separate broker businesses (per aggregator). This included the number and value of new loans in that year, the number and value of outstanding loans and the commission payments that were passed on to the broker business for each lender.

543 We used this information to derive average commission rates and per-loan dollar payments for the individual broker businesses.

Derived rates of upfront and trail commissions paid to broker businesses

544 The median values of the upfront commission rates passed on to broker businesses from aggregators ranged from 0.46–0.65%, with the industry mean being 0.54%.

545 Within an aggregator, the difference between the lowest and highest paying lenders ranged from 0.13–0.70%. For a broker choosing whether to recommend a loan from these lenders, this could mean an extra $650–3,500 in upfront commission payable on a $500,000 loan.

> Note: The difference between the lowest and highest paying lenders is calculated at, respectively, the 5th and 95th percentile. As a result the difference between the absolute lowest and highest paying lenders will be greater.

546 Among all aggregators, the lowest average upfront commission rate passed on was 0.00% and the highest average rate was 3.23%.

547 The above ranges reflect the rates of upfront commission paid by all lenders across all broker businesses reported on by the aggregator. We also looked at the range of rates of upfront commission paid to each individual broker business for loans funded by the ADIs in the review.

> Note: By including only the rates of commission paid by ADIs, we have excluded the higher rates of commission that may be paid by non-ADIs on non-conforming loans.

548 We continued to see considerable variation between the lowest paying and highest paying ADI lenders within the individual broker businesses. Variations tended to be at least 0.10% (i.e. $500 of upfront commission on a $500,000 loan), while variations of over 0.30% were not uncommon.

549 The median values of the trail commission rates passed on to broker businesses by the aggregator ranged between 0.08% and 0.16% of the loan value, with an industry mean of 0.14%.

550 Within an aggregator, the difference between the lowest and highest paying lenders ranged from 0.11–0.28%. This could mean the difference of an extra $550–1,400 per year in trail commission that is passed on to the broker business on a $500,000 loan, depending on which lender was chosen by the broker.

> Note: The difference between the lowest and highest paying lenders is calculated at, respectively, the 5th and 95th percentile. As a result the difference between the absolute lowest and highest paying lenders will be greater.

551 Across all aggregators the lowest average annual trail commission rate passed on to a broker business was 0.00% and the highest average rate was 0.73%.

552 As with the rates of upfront commission, we looked at the range of rates of trail commission paid to each individual broker business by the ADIs in the review. Again, we saw considerable variation between the lowest paying and highest paying ADI lenders within the individual broker businesses. Variations tended to be between 0.05% and 0.15%.

Derived per-loan values of upfront and trail commissions paid to broker businesses

553 As with the per-loan values of the commission paid to aggregators, we sought to understand the distribution of the average per-loan amounts of upfront and trail commissions paid to broker businesses.

554 Based on aggregators' loan flow data, the average per-loan amount of upfront commission paid to broker businesses varied from $0 to over $10,000.

555 The estimated average annual per-loan amount of trail commission paid to broker businesses by individual lenders varied from $0 to over $1,000.

Clawback arrangements between aggregators and brokers

556 We asked aggregators some questions about their clawback arrangements with broker businesses and brokers. Specifically, we asked whether the agreement with the broker business allowed the aggregator to recover commissions from broker businesses or directly from the broker. All aggregators could recover commissions from broker businesses. All but two aggregators stated that they could not recover commissions directly from a broker with whom they did not have a direct contractual relationship.

Offsets for commission clawbacks

557 We asked aggregators whether they could directly recover commissions that had been clawed back by the lender from a broker who sold the loan, or whether they recovered the amount from the broker business in which the broker worked (where relevant).

558 Around 75% of aggregators could recover amounts from the broker business employing the broker (some for home loan related commissions only, others for any payments due to the business). The remaining aggregators could only recover against payments due to that particular broker.

Commission-sharing arrangements between aggregators and brokers

559 As part of our review, we sought to understand the extent to which aggregators:

(a) inform brokers within their networks about commissions received from lenders (including base rates of commission, campaign-based commission structures or bonus arrangements); and

(b) share any commissions received from lenders under campaign-based and bonus arrangements.

Note: We also asked about arrangements for other forms of payments between lenders and aggregators (see paragraph 587).

560 We asked aggregators whether they were required under the contract with brokers to disclose the value of the following forms of commission paid by the lender:

(a) the base rate of commission received from lenders;

(b) any volume or non-volume based rates of commissions (including whether those bonus commissions were paid);

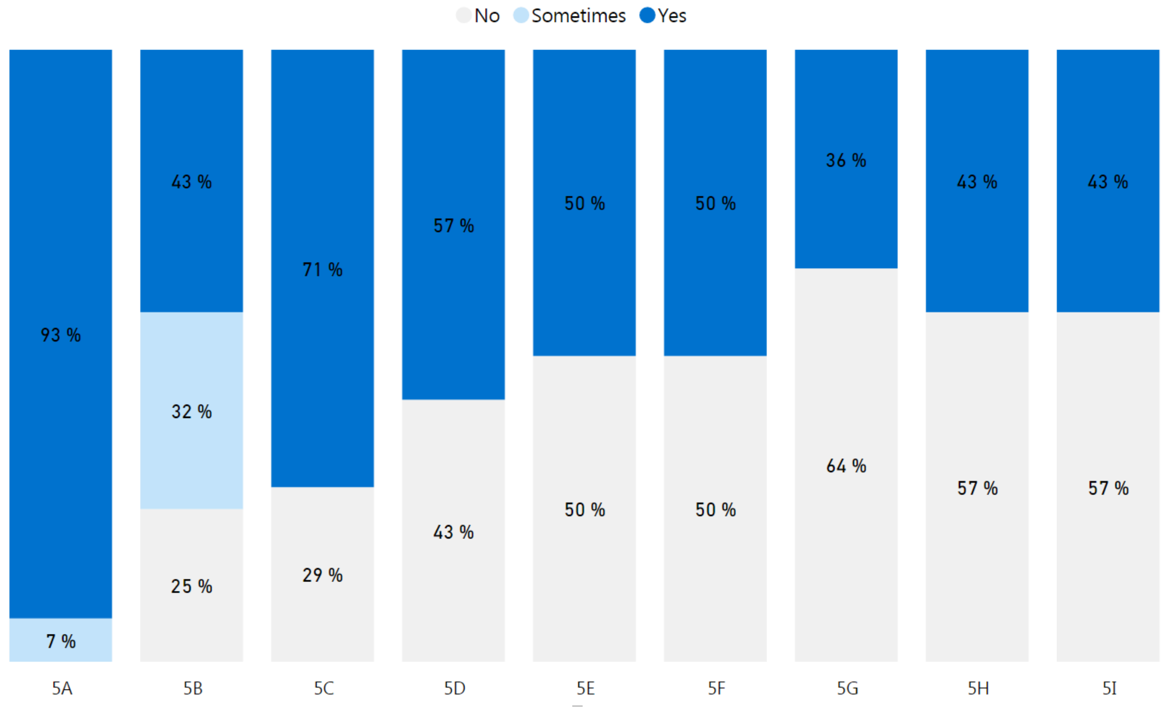
(c) any campaign-based commission structures that apply from time to time and the amount receive under those arrangements; and

561 Around 50% of aggregators reported that they are required to disclose the base rate of commission to the broker. However, few aggregators reported an obligation to disclose any other forms of remuneration that may be received from lenders. This was the case for brokers who were credit representatives of the aggregator and those who were not.

562 While few aggregators reported that they were required under the contract to disclose details about remuneration, it seemed to be a more common practice to do so (although this practice was not universal and did not cover all forms of remuneration).

563 Figure 14 shows the aggregators’ response to our question on whether, as a matter of practice, they disclosed to brokers details of lender payments.

Figure 14: Disclosure to brokers of lender payments received by the aggregator



Note 1: See paragraph 564 for a description of the trends shown in this figure.

Note 2: In this figure, these codes are used to indicate the following responses to question 5 in the aggregators' survey:

5A = the base rate of commission the broker receives from lenders;

5B = any volume-based rates of commission the broker may receive from lenders;

5C = any non-volume based accelerated rates of commission the broker may receive from lenders;

5D = any campaign-based commission structure that applies from time to time;

5E = whether the conditions for a volume-based rate of commission were achieved;

5F = whether the conditions for a non-volume based rate of accelerated rate of commission were achieved;

5G = the amount of commission that was received under a volume-based rate of commission;

5H = the amount of commission that was received under a non-volume based rate of commission; and

5I = the amount of commission that was received under a campaign-based commission structure.

564 In practice, most aggregators disclosed the base rates of commission (93%) and non-volume based accelerated rates of commission (71%) received from lenders. However, broker businesses/brokers were less likely to be given information about other payments or when the conditions for payment of a particular accelerated rate of commission were satisfied.

565 We also sought to understand whether aggregators passed on commissions under campaign-based commission structures or bonus arrangements. In particular, we asked whether aggregators pass on to broker businesses/ brokers some or all of the amount of commission received under:

(a) volume-based rates of commission;

(b) non-volume based accelerated rates of commission; and

(c) campaign-based commission structures.

566 Aggregators typically passed on some bonus commission payments (whether volume or non-volume based) or campaign-based commissions received from lenders. Approximately 60% of aggregators stated that they would pass each type of payment on to the broker business/broker, as with upfront and trail commissions. The remaining aggregators stated they would pass on some benefits, but on a different basis to the standard commission sharing rate.

Note: From the term sheets, it was not clear whether bonus payments are passed on to brokers. In many cases, aggregators' term sheets described upfront commissions paid to brokers as a percentage of the commissions the aggregator receives, so these other incentives may also be received by the broker. However, this may depend on how upfront commissions are paid to aggregators (e.g. whether they are paid as a lump sum including the incentives or as a series of separate payments).

We identified one aggregator who paid a 'performance bonus' based on the level of settlements per month that exceeded a specified amount of loans (this amount was not subject to a clawback arrangement). However, most aggregators did not appear to provide bonus payments, or specifically provide for bonuses paid by lenders to be passed on to broker businesses.

Commissions from broker businesses to brokers

567 Where an individual broker operates under a broker business (as opposed to having a direct relationship with the aggregator), the arrangements between that broker and the business will be relevant to the way in which the individual is ultimately remunerated.

Note: We also asked aggregators whether they sought to restrict or influence the amount of commission that broker businesses pass on to brokers. All aggregators reported that they did not (i.e. the business was free to pass on payments to brokers as it saw fit).

How broker businesses pay their brokers

568 We asked broker businesses whether or not brokers who worked in their business received commissions for each home loan they sold (assuming they satisfy any applicable minimum thresholds). We also asked whether their total remuneration was based solely on commission from the sale of these products and services.

Note: We also asked broker businesses whether brokers receive a salary (see paragraphs 577–579).

569 Broker businesses reported the following details:

(a) *Independent contractors*—These contractors receive a commission payment for each home loan they sell (as reported by all 21 broker businesses). All but one business stated that independent contractors (whether operating under the business brand or not) were remunerated wholly based on commission (i.e. they do not receive a salary).

(b) *Owner/director brokers*—Over 85% of owner/director brokers receive a commission payment for each home loan they sell and approximately 90% were remunerated wholly based on commission (i.e. owner/director brokers do not usually receive a salary).

(c) *Employee brokers*—Around 50% of broker businesses reported that employee brokers are remunerated for each home loan sold. Likewise, around 50% of businesses reported these brokers were remunerated wholly based on commission (only nine broker businesses in our survey that reported having employee brokers).

570 Overall, broker businesses and brokers confirmed that most brokers are remunerated wholly based on commission.

Calculation of payments made to brokers

571 For broker businesses and brokers who received commission payments, we asked them a series of questions about how the payments are calculated, including:

(a) how much of the commission payment is retained by the business;

(b) whether the amount retained by the business differs for upfront or trail commissions;

(c) whether the amount retained by the business depends on the total volume written by the broker (e.g. whether the broker receives a greater proportion of the commission if they write more loans in the year); and

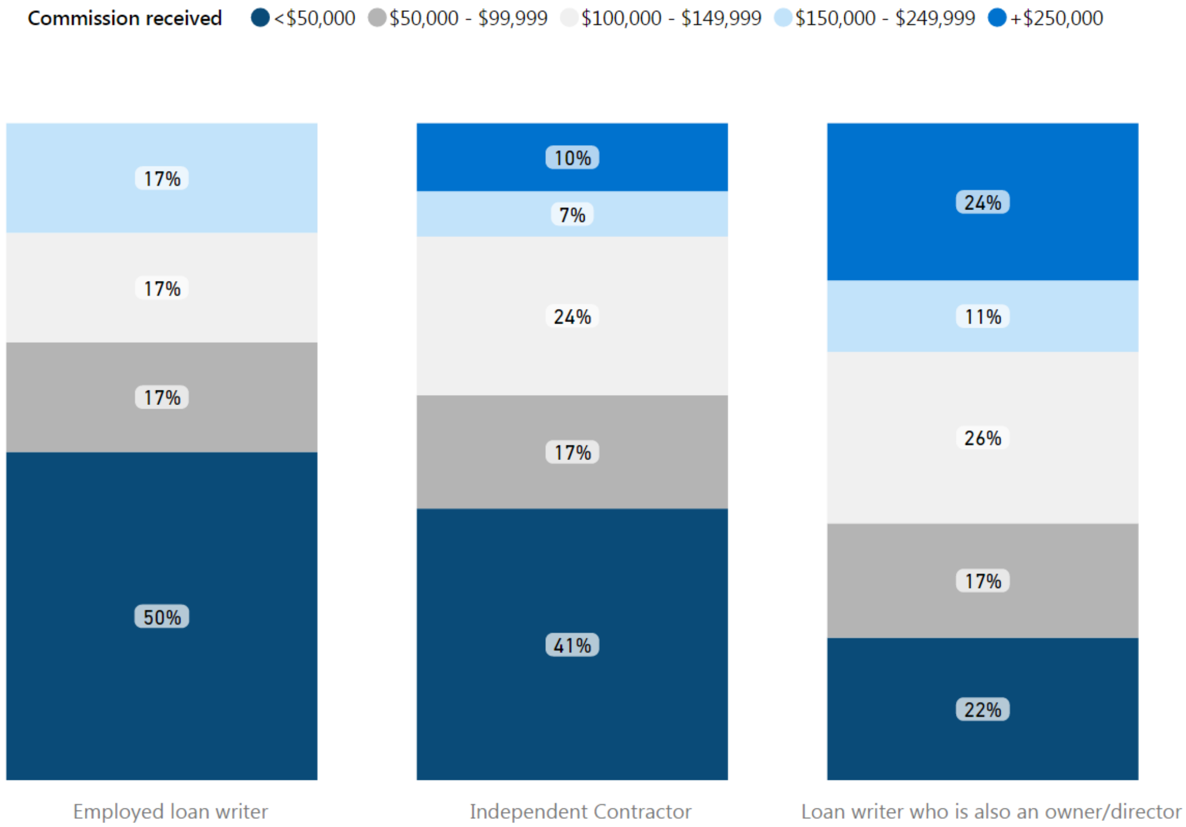
(d) whether the amount retained by the business differs depending on which lender was involved, the type of the loan sold or other criteria.

572 There was minimal variation in the way broker businesses paid individual brokers: most businesses passed through the commission to the individual broker, having retained a set amount or percentage regardless of volume or lender.

Value of commission payments to brokers

573 We asked broker businesses about the average annual value of commissions for brokers for each broker category: see Figure 15.

Figure 15: Average annual value of commissions (by broker category)



Note: See paragraph 574 for a description of the trends shown in this figure.

574 Approximately, 60% of owner/director brokers received more than $100,000 in commissions in 2015 (with almost a quarter receiving over $250,000). However, a significant percentage of brokers under each category received less than $50,000 commission in the year (although, it is possible that employed loan writers may have also received a salary: see paragraphs 575–579).

Clawback arrangements between broker businesses and brokers

575 Broker businesses stated that the commission was clawed back in full from the individual broker in almost every case, although a small number of businesses noted that this may not be the case for some employed brokers.

576 Most businesses indicated that they recovered the clawed-back commission by offsetting the amount against future commission payments to the broker. However, some businesses stated that they required immediate repayment of the amount from independent contractors or owner/director brokers.

Other remuneration (including salary, cash payments and fees)

Salary arrangements

577 Brokers do not typically earn a salary. Based on survey responses, just over 15% of owner/director brokers earned a salary. For owner/directors, earning a salary means drawing down profits from the business. As expected, almost no independent contractors earned a salary.

578 Employed loan writers were more likely to receive a salary. Of the nine broker businesses that reported having employed brokers, seven reported that those brokers received a salary and one business reported that some employed brokers received a salary.

Note: Employed brokers accounted for 15 out of 198 brokers covered by the businesses who responded to our survey. Responses to the question about brokers earning a salary were somewhat inconsistent with responses to another question, where four out of nine businesses stated that employed brokers were wholly remunerated by commissions.

579 For the few employed brokers who received a salary, the average salary amount was approximately $54,000 in 2015 ($49,000 in 2012).

Sponsorship and other payments by lenders and aggregators

580 In preparing for this review, we were advised by some industry participants that lenders may offer 'sponsorship payments' to aggregators, which provide the lender with benefits such as being able to attend the aggregators' conferences: see paragraphs 658–665.

581 To understand more about these arrangements, we asked lenders what types of payments (other than commissions) they give to aggregators or brokers. We also asked aggregators whether they make any such payments to brokers.

Lenders' payments to aggregators

582 We asked lenders whether they had made any payments to aggregators for commencing or continuing to place loans with the lender. No lenders reported such payments (although one lender noted that the prevalence and impact of sponsorship arrangements between lenders and aggregators have, in practice, a similar effect).

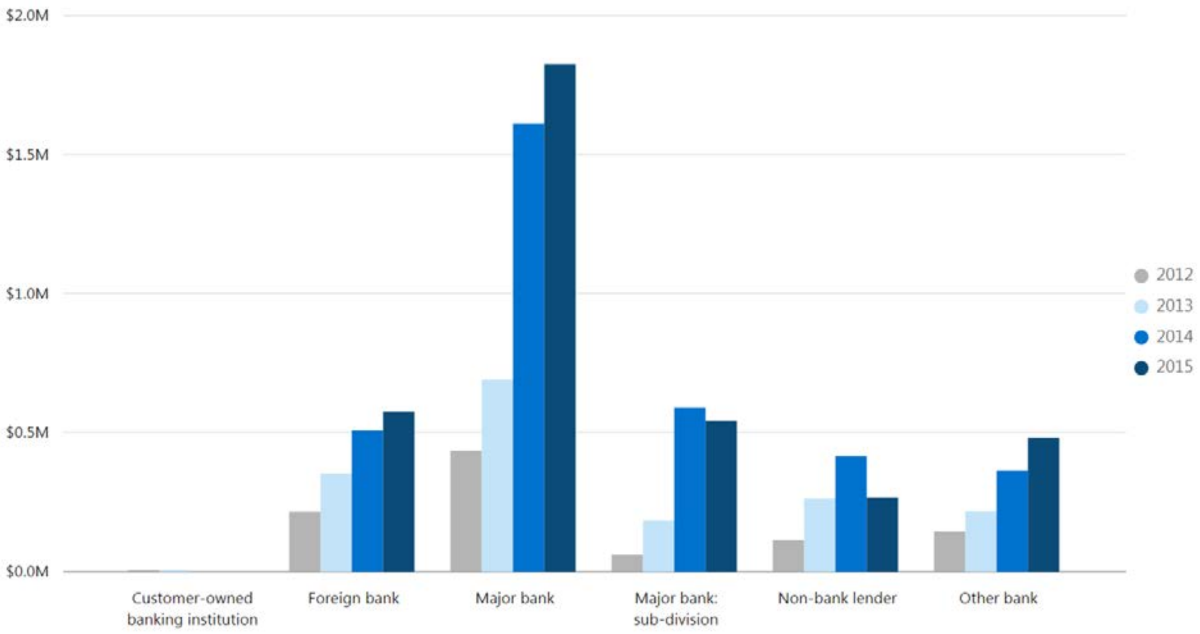
583 We also asked lenders whether they had made any type of sponsorship payments. Most lenders reported that they had made such payments to aggregators. For example, approximately 85% of lenders had made payments or provided benefits to either sponsor conferences or provide prizes in competitions run by aggregators.

Note 1: In response to our question to aggregators about whether they offered such sponsorship arrangements to lenders, all but two aggregators responded that they allow lenders to pay for 'sponsorship packages'.

Note 2: In response to our question to lenders about whether they had sponsored broker businesses directly, approximately 25% of lenders said that they had made such payments to broker business but on a much smaller scale than to aggregators.

584 Figure 16 shows the value of average value of sponsorship-type payments made by each category of lenders from 2012–15.

Figure 16: Average value of sponsorship payments made by lenders (2012–15)



Note: See paragraphs 585–586 for a description of the trends shown in this figure.

585 The value of sponsorship-type payments increased significantly between 2012 and 2015 (although those paid by non-ADI lenders slightly decreased from 2014–15). The average amount of sponsorship paid by major banks increased from approximately $300,000 in 2012 to over $1.3 million in 2015. Banks other than the major banks and non-ADI lenders also reported making significant payments; in some cases over $500,000 on average. Customer-owned banking institutions reported paying little in the way of sponsorship-type payments.

586 At an industry–wide level these payments have gone from approximately $3.6 million in 2012 to over $13.7 million in 2015.

587 We asked aggregators whether they tell their brokers about the value of the sponsorship payments or share those payments with the brokers. All aggregators reported that they generally did not give this information to brokers (they are not required to do so) and did not share the value of the sponsorship with brokers.

Note: While aggregators did not share the payments with brokers, we understand that many of the sponsorship payments go towards putting on the courses or conferences that an aggregator may provide to high-performing brokers (see paragraphs 658–665).

Aggregators' payments to broker businesses

588 We also asked aggregators whether they made any payments to broker businesses as a condition of commencing or continuing to be a part of the aggregator's network. Aggregators' responses suggested that such payments were not common. One aggregator said that it may provide payments to broker businesses to 'onboard' that business (i.e. to bring the business into the aggregator's network).

589 In relation to sponsorship-type arrangements, aggregators' responses indicated that very few of these payments were made by aggregators to broker businesses. Approximately 25% of aggregators had made payments to sponsor a conference run by a broker business.

Fees paid by consumers

590 Another potential source of income for brokers are fees charged directly to consumers. While brokers typically rely on commissions paid by lenders for revenue, we sought to understand how fees may be charged and how prevalent this is in the mortgage broking market.

591 We asked lenders and aggregators whether they sought to restrict brokers' ability to charge fees directly to consumers. Almost all of the lenders reported that their agreements with aggregators are silent on this issue. A small number of lenders stated that their agreements did impose some restrictions; however, they did not provide details of those restrictions.

592 Three aggregators reported that their agreements restricted brokers' ability to charge the consumer a fee. For another three aggregators, while not prohibited by the agreement, it was against their policy for such fees to be charged.

Note: We also asked aggregators whether they would share in any fee revenue received from consumers. Only one aggregator said they may potentially share in the revenue.

593 We asked broker businesses and brokers whether they charged consumers a fee to arrange home loans and, if so:

(a) how the fee was usually calculated;

(b) whether it was up to the broker to decide whether consumers are charged a fee and the size of the fee;

(c) whether the broker received the fee; and

(d) whether payment of the fee was required before the loan was arranged (i.e. before the work was done).

594 A small proportion of broker businesses indicated that they sometimes charged an upfront fee for their services. Reasons for the fee included where the work was complex or intensive, or where lenders did not pay commissions for the service being provided.

595 Approximately 85% of businesses stated that they did not give brokers the option of charging upfront fees to consumers.

596 Where broker businesses allowed a fee to be charged, most businesses reported that the broker was responsible for setting the amount and received the whole fee. Of these businesses, 50% required upfront payment of the fee and 50% allowed the fee to be paid after the loan was arranged.

Cross-selling

597 Cross-selling occurs in the mortgage broking market when brokers attempt to sell other financial products to a consumer at the same time as a home loan. We sought to understand the importance of this practice for brokers. Overall, it does not appear to be a significant source of revenue for brokers.

598 We asked lenders about cross-selling arrangements they had with aggregators and brokers. We also asked brokers about any arrangements where they could earn additional income for cross-selling other products and services.

Payments made by lenders to aggregators or brokers

599 Lenders reported that cross-selling arrangements between lenders and aggregators or lenders and brokers were not common. However, responses did set out some instances of cross-selling arrangements.

600 One major bank appeared to have a well-developed cross-selling program for a number of products and services, including home loan consumer credit insurance, credit cards, other consumer credit products, transaction accounts and other deposit products, business or commercial products, life insurance, home insurance, and financial advice services.

601 Other lenders' cross-selling programs involved a more limited set of products. For example:

(a) one lender had arrangements for consumer credit insurance, both for home loans and other products;

(b) a small number of lenders had arrangements for other consumer credit products (e.g. personal loans);

(c) one lender had arrangements for transaction accounts;

(d) two lenders had arrangements for home insurance and, for one of these lenders, other general insurance products; and

(e) one lender had arrangements for a superannuation product.

602 Payments from lenders to aggregators ranged from negligible amounts to almost $2 million in one year. The highest amount was from a major bank, which had arrangements to cross-sell a wide range of products, with most of this amount related to transactions accounts. This lender made annual payments to individual aggregators ranging from around $20,000 up to over $1 million during the four-year period.

603 It appears that cross-selling of financial products and services offered by panel lenders are unlikely to be a significant source of income for brokers.

Payments made to brokers

604 We sought to identify the nature and extent of payments received by broker businesses for cross-selling products on behalf of lenders and other third parties.

605 Firstly, we asked aggregators whether they permitted the broker to receive payments, independently of any agreement arranged by the aggregator, from:

(a) panel lenders for products other than home loans (e.g. through cross-selling of the lenders' other products); or

(b) providers (other than lenders) for cross-selling other products and services.

606 We asked this question separately in relation to brokers who were credit representatives of the aggregator and those who were not. Just under 50% of aggregators said that brokers who were credit representatives were not permitted to receive those types of benefits (outside any agreement arranged by the aggregator). This dropped to around 20% for other brokers. Aggregators also reported that brokers are not generally required to notify the aggregator if they receive a payment under an arrangement from a third party.

607 We also asked broker businesses whether brokers could receive payments for cross-selling a range of products and services other than home loans. A significant portion of businesses reported that brokers could receive payments for cross-selling traditional banking products (e.g. transaction accounts) or insurance products relevant to the home loan (e.g. consumer credit insurance or home insurance). The most common arrangement was for home insurance (80% of broker business).

608 Significantly fewer broker businesses reported arrangements for other products and services. For example, we asked whether brokers could receive payments for products and services offered by various forms of 'debt management firms', as discussed in Report 330 *Paying to get out of debt or clear your record: The promise of debt management firms* (REP 330). These firms include businesses that offer services such as credit repair, debt negotiation and/or bankruptcy services, and budgeting. Only a small number of broker businesses reported any such arrangements.

609 One business, in their commentary, reported cross-selling arrangements for property referrals organised through the relevant aggregator. As we did not specifically include this option, these types of arrangements may be more common.

610 We asked broker businesses whether they allowed individual brokers to receive payments from third parties for selling their products and services or leads to the third party. Approximately 50% of businesses (which were not sole operators) responded that brokers could maintain such relationships.

611 We also asked broker businesses about the average value of commissions paid to brokers for these other products and services. The amounts reported were relatively small, typically around $1,000 to $2,000 per year.

Soft dollar benefits received by brokers

612 Soft dollar benefits include any rewards that are not cash. This can include such things as hospitality and travel, including travel to overseas conferences. Such benefits have the potential to increase the risk of poor consumer outcomes for home loans sold by brokers.

613 As part of our review, we sought to understand how common the provision of soft dollar benefits was in the mortgage broking market. We focused on four types of soft dollar benefits:

(a) broker clubs offered by some lenders and aggregators;

(b) free attendance at courses or conferences linked to the sale of home loans;

(c) competitions (e.g. trade promotions) under which entry is linked to the sale of home loans; and

(d) other rewards and recognition (e.g. hospitality).

614 We sought to quantify the value of the soft dollar benefits being given to brokers by lenders and aggregators. We found that in many cases lenders and aggregators were unable to provide accurate data on the value of rewards, as records were not retained as standard practice.

Broker clubs

615 Broker clubs are a form of incentive that is offered to qualifying brokers by some lenders and aggregators. Typically entry to the broker club depends on the broker satisfying certain criteria (e.g. meeting particular sales targets).

616 Membership of the club usually provides the broker with a range of non-monetary benefits (although, based on the responses from lenders, it appears that they may also provide direct monetary incentives to members). Some lenders operate broker clubs that involve multiple ‘tiers’, with benefits given to brokers based on the tier they qualify for.

617 The impact on consumer outcomes of a lender or aggregator offering a broker club is likely to depend on both the criteria for accessing the club and also the benefits that are given by being in the club.

618 If the criteria for accessing the club are sales based, there is a risk that a broker may send loans to the provider of the club to obtain the benefits of the club (even though the home loan recommended may not be the best choice for the consumer). However, even if the criteria for entry are entirely non-volume based, broker clubs may still increase the risk of poor consumer outcomes depending on the nature of the benefits offered under the club.

619 For example, if the benefits include better and quicker service levels from the lender (e.g. through dedicated loan assessment teams within the lender), there is a risk that the broker may recommend that lender's home loan without considering whether the home loan is the best choice for the consumer. A benefit such as better service levels may result in additional monetary benefits to brokers in the club as they can process more home loans in a given period due to the better lender service levels.

620 This does not mean that we consider that all broker clubs are likely to result in poor consumer outcomes. We understand that many lenders may have introduced broker clubs to recognise good work being done by certain brokers, and that the benefits granted under the club (e.g. through improved service levels) have the potential to result in better outcomes for consumers going through those brokers.

Overview of lenders' broker clubs

621 We asked lenders whether they operated any form of 'broker clubs' and, if so, whether membership was offered on the same terms to all brokers under all aggregators.

622 Lenders reported the following (in 2015 unless otherwise stated):

(a) Broker clubs were offered by nine out of 19 lenders in this review.

(b) Broker clubs were offered by six out of seven lending brands within the major lenders. This was an increase of one from 2012.

(c) Broker clubs were offered by three out of 12 of the other lenders within the sample. This was an increase of one from 2012.

(d) No customer-owned banking institutions operated broker clubs.

(e) Broker clubs were made available on the same terms to all brokers under all aggregators by eight out of nine lenders who offered clubs.

623 These broker clubs were provided by lenders as a matter of practice, rather than a requirement of the agreement between the lender and aggregator.

624 We sought to understand the qualifying criteria for the broker clubs established by lenders. We asked whether the criteria included:

(a) sales of home loans;

(b) sales of white label loans specifically;

(c) sales or referrals for other products or services (i.e. cross-selling);

(d) non-sales based criteria; and

(e) a subjective assessment.

625 In response, lenders reported the following:

(a) Eight out of nine lenders based qualification for a broker club on the sales of home loans. Typically this was on a monthly or quarterly basis; however, some lenders also considered yearly sales. One lender considered portfolio growth rates in addition to pure sales figures.

(b) Where the sale of home loans was the basis for qualification, this would include the broker's own sales. For six lenders, sales by other brokers within the same business were also relevant.

(c) One lender considered the sale of white label loans specifically when assessing qualification for the broker club.

(d) Lenders did not take into account the sale of other products and services.

(e) A number of lenders took into account non-sales based criteria (e.g. quality of applications). One lender also considered 'advocacy' of the broker towards the lender's brand as part of the relevant criteria.

(f) All but one lender said that entry to a broker club was at least partly dependent on a subjective assessment of the broker by the lender.

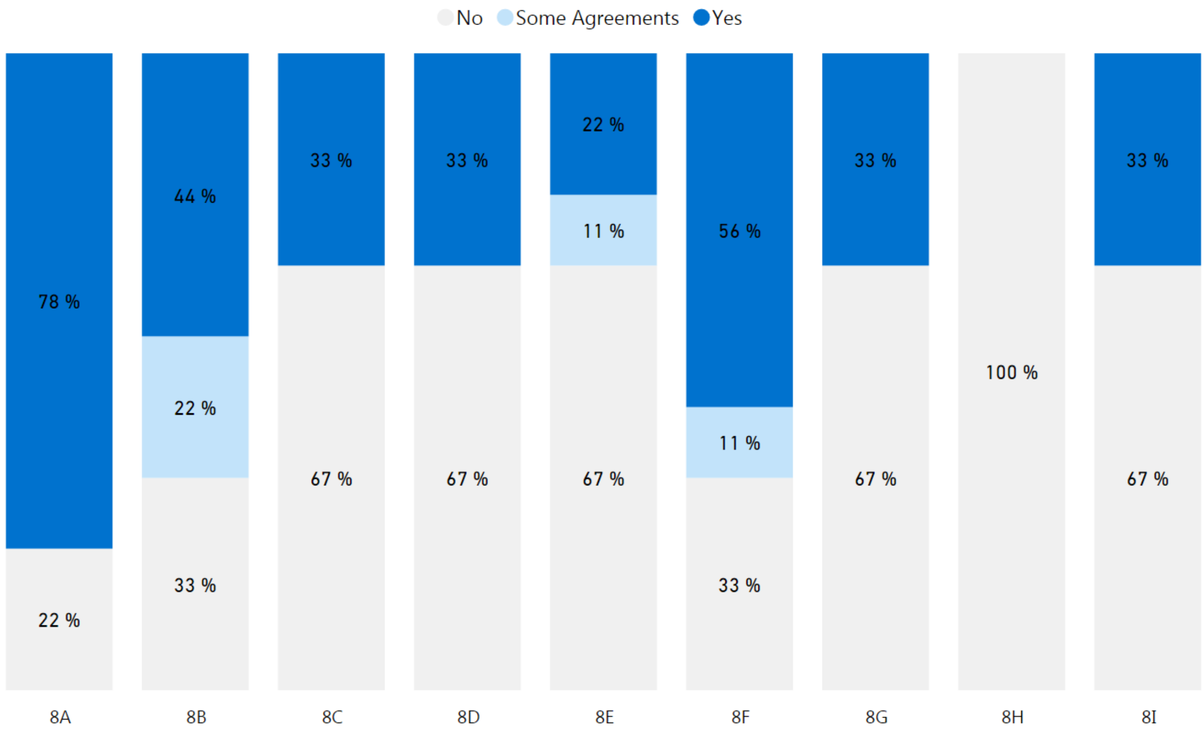
(g) One lender noted that brokers under certain aggregators were, by agreement with those aggregators, automatically awarded membership in the broker club.

626 Most lenders offering broker clubs acknowledged that the qualification criteria were not always strictly enforced and that brokers may be offered membership even if the criteria were not satisfied.

627 Lenders operating broker clubs usually reassessed eligibility on a quarterly basis, although a few made the assessment on a monthly or half-yearly basis. The criteria for remaining within a broker club were the same as for entry, although most lenders again acknowledged that discretion may be used to allow a broker to maintain a particular status in the club even if the relevant criteria were not met.

628 We sought to understand the types of benefits that lenders may provide under a broker club: see Figure 17.

Figure 17: Benefits given by lenders to broker club members



Note 1: See paragraphs 629–632 for a description of the trends shown in this figure.

Note 2: In this figure, these codes are used to indicate the following responses to question 8 in the lenders' survey:

8A = enhanced service levels by the lender;

8B = enhanced access to lender's underwriting staff;

8C = enhanced access to lender's business development staff;

8D = enhanced access to staff who can agree to loan discounts;

8E = enhanced access to courses or conferences;

8F = enhanced access to hospitality;

8G = improved commission rates;

8H = improved commission recovery terms; and

8I = other.

629 Some of the benefits available to brokers under the 'other' category (provided by 33% of lenders) included better access to property valuations that would make the loan application process easier, and a rewards scheme under which points could be earned and redeemed for rewards and prizes.

630 Benefits such as enhanced access to hospitality (56% of lenders), improved commission rates (33% of lenders), and the provision of rewards points provide direct monetary and non-monetary benefits to the broker. As such, they are likely to increase the risk that brokers may prioritise earning those benefits over consumers' needs.

631 Many of the other benefits tended to focus on providing enhanced service levels to brokers (78% of lenders). Such benefits can have a positive consumer impact, as the broker can obtain a loan for the consumer more quickly. In the case of improved access to lenders' staff with discretion to

provide a discount (33% of lenders), this could result in cheaper loans than what would otherwise be available from that lender (although not necessarily cheaper than loans from other lenders).

632 However, even such potentially consumer-friendly benefits have potential to influence brokers to sell a home loan of the provider of the broker club to obtain or retain the broker's club status. As noted previously, quicker and better service from a lender can result in additional monetary benefits to the broker by allowing the broker to submit more home loan applications.

633 To understand the impact of the broker clubs on brokers, it is important to understand the potential value of those benefits to brokers. We asked lenders whether they had a specific budget for providing benefits under the broker club or recorded the value of the benefits provided to brokers in the club.

634 Most lenders reported that they did not have a specific budget for providing benefits to broker club members. Two out of the nine lenders that operated broker clubs stated that they recorded the value. One additional lender noted that they tracked the value of monetary benefits but not soft dollar benefits (e.g. the value of the improved service levels given to the broker).

635 One lender was able to provide a value of the benefits provided under the broker club, which was just over $150,000 in 2015. It is unclear whether this included a value of the soft dollar benefits that were provided. Another lender noted that the benefits provided under the club were in the form of rewards points, which could be converted to rewards or prizes. The value of those converted points was minimal. No other lenders could provide a value of the benefits provided to brokers under the broker clubs.

636 We also asked lenders whether they advised the relevant aggregator or broker business when giving a broker access to a broker club. Aggregators or broker businesses should be aware of which benefits are being provided so they can assess whether there is a risk of these benefits improperly influencing brokers' loan recommendations.

637 We found that seven out of nine lenders do not notify aggregators, while six out of nine lenders do not notify broker businesses.

638 In addition, we asked broker businesses and brokers for their feedback about the broker club programs offered by some lenders. Generally brokers considered being a part of a broker club as a good thing. One broker commented that being with one particular lender gives them better pricing and faster turnaround times for consumers compared to the lender's competitors. Another broker commented that broker clubs 'drive better customer outcomes and reward those brokers with more experience and skills as they are writing more business on a regular basis'.

639 While the feedback notes the potential positive consumer outcomes from broker clubs (e.g. faster turnaround times), it does also indicate that the brokers themselves see access to the clubs as being a factor that influences which loan the broker recommends to the consumer. This concern was reflected in the feedback of a small number of who noted that broker clubs could negatively impact consumer outcomes.

Data on lenders' broker clubs

640 We asked lenders to provide a list of all brokers in each tier of their broker clubs, together with the value of the loans introduced by each of those tiers (as a proportion of overall loans introduced by brokers).

641 We also asked lenders to provide the credit licence or credit representative number of each of these brokers so we could track the loans originated through those brokers across all lenders (using the home loan data) and test the consumer outcomes of those loans (e.g. features and performance of loans and whether the broker obtained a better interest rate for the consumer).

642 Unfortunately, as noted earlier, lenders were generally not able to provide that level of detail in the home loan data, which meant we could not track the loans originated by broker club members across all the lenders in this review.

643 Table 5 shows the number of brokers that are members of each tier of each lender's broker club as a proportion of the total number of brokers that lender had accredited in 2015, together with the proportion of home loans sold by brokers that year.

Table 5: Membership and value of loans sold by broker clubs

Name	Highest status (% of brokers with status)	Highest status (% of broker loans written)	Second highest status (% of brokers with status)	Second highest status (% of broker loans written)	Third highest status (% of brokers with status)	Third highest status (% of broker loans written)
Other bank 1	1.11%	34.90%	20.33%	31.10%	N/A	N/A
Other bank 2	3.62%	30.64%	N/A	N/A	N/A	N/A
Major bank: sub-div 1	1.71%	28.00%	4.84%	21.00%	24.56%	36.00%
Major bank: sub-div 2	13.10%	44.00%	N/A	N/A	N/A	N/A
Major bank 1	0.08%	3.00%	1.07%	14.00%	4.61%	22.00%
Major bank 2	9.06%	38.00%	N/A	N/A	N/A	N/A
Major bank 3	3.33%	9.00%	N/A	N/A	N/A	N/A
Major bank 4	3.96%	31.00%	22.67%	40.00%	N/A	N/A

644 The proportion of broker loans written by members of broker clubs is high across all lenders and all tiers. This is particular evident in the highest tiers of some of the lenders' broker clubs. In the case of major bank 1, the members of the highest tier were on average each responsible for selling over $90 million of that lenders' home loans.

645 While we recognise that other factors may be involved, this does appear to indicate that broker clubs are associated with—if not the cause of—brokers channelling loans to a limited number of lenders. For a further discussion of brokers' tendency to recommend loans from a limited range of lenders, see Section E.

Overview of aggregator broker clubs

646 We also asked aggregators whether they operated any form of broker clubs. We found the following (in 2015 unless otherwise stated):

(a) Broker clubs were offered by seven out of 14 aggregators. This was an increase of two since 2012.

(b) Broker clubs tended to be offered by mid-tier and large aggregators more often than small aggregators.

(c) Broker clubs offered by aggregators were typically made available to all brokers linked with that aggregator as a matter of practice, rather than under the broking agreement.

647 As with lenders, we sought to understand the qualifying criteria for the broker clubs established by the aggregators. We asked whether the criteria included:

(a) sales of home loans;

(b) sales of white label loans specifically;

(c) sales or referrals for other products or services (i.e. cross-selling);

(d) non-sales based criteria; and

(e) a subjective assessment.

648 In response, aggregators reported the following:

(a) All the aggregators who operated broker clubs based qualification on the sales of home loans. Typically this was on a half-yearly or yearly basis. One lender noted that qualification was based on revenue earned rather than simple sales volumes.

(b) The aggregators typically included the broker's own home loan sales. A number of aggregators also considered sales by other brokers within the same business.

(c) Two aggregators took into account the sales of white label loans specifically when assessing qualification.

(d) Three aggregators took into account the sale of other products and services.

(e) Two aggregators took into account non-sales based criteria. For one aggregator, this included the broker's audit results and net promoter score (which is a measure of customer satisfaction: see paragraph 983).

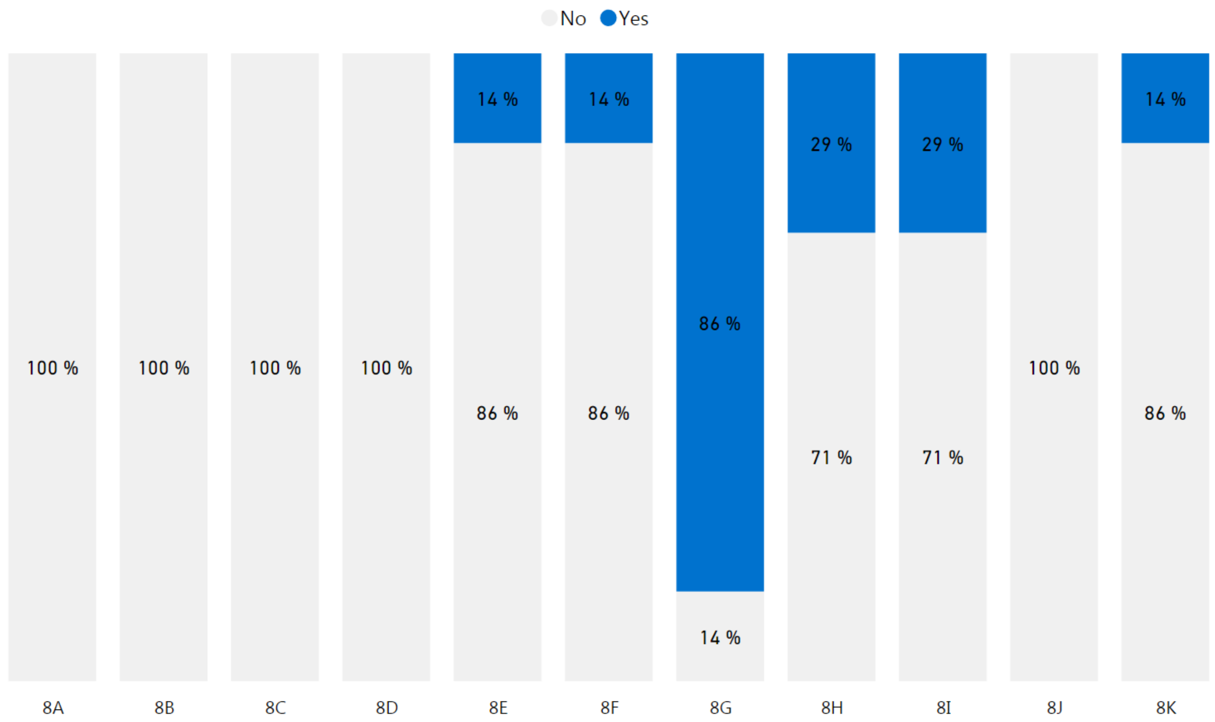
(f) Two aggregators said that entry to the broker club was at least partly dependent on a subjective assessment of the broker.

649 Four out of seven aggregators said that the eligibility criteria were applied strictly.

650 Most of the aggregators reassessed eligibility for a broker club on an annual or longer basis, although a few assessed eligibility on a quarterly or half-yearly basis. The criteria for remaining within a broker club were the same as for entry, although a number of aggregators acknowledged that discretion may be used to allow a broker to maintain a particular status in the club even if the relevant criteria were not met.

651 We sought to understand the types of benefits aggregators may provide to members of broker clubs: see Figure 18.

Figure 18: Benefits given by aggregators to broker club members



Note 1: See paragraph 652 for a description of the trends shown in this figure.

Note 2: In this figure, these codes are used to indicate the following responses to question 8 in the aggregators' survey:

8A = enhanced service levels by the lender;

8B = enhanced access to lender's underwriting staff;

8C = enhanced access to lender's business development staff;

8D = enhanced access to staff who can agree to loan discounts;

8E = enhanced service levels by the aggregator;

8F = enhanced access to aggregator's business development staff;

8G = enhanced access to courses or conferences;

8H = enhanced access to hospitality;

8I = improved commission rates/reduced aggregator fees;

8J = improved commission recovery terms; and

8K = other.

652 In contrast to lenders, the benefits offered by aggregators to members of broker clubs typically focus on the provision of enhanced access to courses or conferences (86%). In effect, membership of an aggregator's broker club is the way in which the broker obtains access to these courses and conferences: see paragraphs 658–665.

653 Unlike lenders, many of the aggregators either had a specific budget for providing benefits to broker club members or recorded the value of the benefits given to members. We expect that this may be partly due to the confined nature of the benefits offered by aggregators.

654 Five out of seven aggregators had a specific budget for broker clubs, ranging from $60,000 to over $1 million. Three out of the seven aggregators recorded the value of benefits, with value ranging from approximately $65,000 to almost $600,000.

Other forms of soft dollar benefits

655 In general, brokers may receive three forms of soft dollar benefits: courses and conferences, hospitality, and competitions.

656 For each type of benefit, we sought to understand the nature of the benefit and the extent to which it is available to brokers.

657 We also sought to understand the steps taken by the relevant industry participant to mitigate the risk that the provision of the benefit could result in poor consumer outcomes, due to a broker being overly focused on obtaining that benefit. For a further discussion of these mitigating steps, see Section H.

Courses and conferences

658 In preparing for this review, a number of stakeholders raised concerns with us about the ability of brokers to become entitled to courses or conferences paid by aggregators or third parties (including lenders), particularly overseas conferences.

659 To understand the prevalence and nature of such benefits, we asked aggregators a series of questions about whether brokers could attend courses or conferences in Australia or overseas paid for by:

(a) the aggregator; or

(b) third parties, including lenders.

660 In relation to courses or conferences paid by the aggregator, approximately 33% of aggregators reported that brokers could become entitled to courses of conferences in Australia based wholly or partly on the sale of home loans by the broker. This was the case for both 2012 and 2015. In contrast, approximately 65% of aggregators reported that brokers could become entitled to courses or conferences held overseas based on sales by that broker. This was an increase from around 35% in 2012.

661 We also asked aggregators to tell us the number of brokers who were granted these benefits. The number of brokers ranged from zero to over 1,600. Based on the particular aggregator's comments, we believe the higher number relates to brokers who attended ordinary professional development sessions put on by the aggregator and is not a true reflection of the number of brokers who qualified for these benefits based on sales volumes.

662 Apart from this higher number, it appears that the number of brokers attending courses or conferences, where attendance is determined by sales volume, is around 100–200 for large aggregators (this includes courses or conferences in Australia or overseas).

> Note: We also asked aggregators to provide the total value of courses or conferences paid for by the aggregator. Based on the comments provided, it appears that aggregators had differing interpretations of what should be included in this figure. It is therefore not possible for us to report a definitive finding on the amount spent. Nevertheless, it appears that larger aggregators spent around $500,000 to $1 million a year on these types of benefits. Small aggregators spent considerably less.

663 In relation to courses or conferences paid by third parties (including lenders), around 20% of aggregators reported that brokers could also become entitled to such courses or conferences based on sale of home loans. Approximately 25% of aggregators stated that they kept a record of courses or conferences awarded to brokers by third parties. However, none of these aggregators could provide data on the number of brokers who took up such benefits when paid for by third parties, or the value of those benefits.

664 We asked brokers and broker businesses for feedback on their ability to attend courses or conferences paid for by aggregators or lenders. Responses ranged from one broker who was unaware of any courses offered by lenders or aggregators, to several whose aggregators paid for their attendance at state and national events one day per quarter.

665 While most brokers who responded to this question indicated that these professional development events were paid for by the aggregator or lender, several other brokers stated that they paid for attendance at such events themselves. One broker noted that professional development was the broker's responsibility and should be funded by the broker's business. Other

brokers noted that courses and conferences were a good way to stay up to date with changing policies, sales training and new product knowledge.

Competitions

666 In preparing for this review, stakeholders reported to us that it was possible for brokers to receive entry into competitions (including trade promotions), where the entry or the prize was dependent on the sale of home loans. We sought to understand the prevalence and nature of these benefits.

667 Such competitions may be used as a targeted tool to incentivise brokers to generate sales generally or for particular products. As with other forms of soft dollar benefits, the competitions may increase the risk of poor consumer outcomes if participation and eligibility criteria are inappropriate. This could include where eligibility is solely based on, or overly emphasises, achieving sales volumes.

668 To understand the prevalence and nature of such benefits, we asked aggregators whether they ran competitions for brokers on a regular basis where entry to the competition was wholly or partly dependent on sales of home loans. Approximately 30% of aggregators reported that they ran such competitions on a regular basis.

669 The aggregators that ran such competitions stated that the provision of these benefits would be subject to the aggregator's policies and procedures dealing with conflicts of interest and that they would ordinarily keep a record of a broker's participation (as noted by one aggregator, the rules of trade promotions often require such records to be maintained).

670 However, none of these aggregators reported that they had a process to review these records as part of their risk and compliance reviews. Where competition entry is dependent on maximising sales, we consider it may be appropriate to review the sales of the winner before providing the prize.

671 We also asked aggregators whether brokers had access to competitions run by third parties (including lenders), where entry is wholly or partly dependent on sales. Approximately 80% of aggregators stated that brokers have access to these benefits provided by third parties.

672 Approximately 15% of aggregators stated that they had a formal policy that required a case-by-case assessment of whether it was appropriate for brokers to receive the benefit from a third party. This figure represents responses by aggregators who answered for their own credit representatives. The figure for brokers who were not the aggregators' credit representatives was lower.

673 Around 50% of the aggregators noted that, while there was no formal policy, brokers would be expected to consider whether it was appropriate to accept the benefit. Aggregators did not generally record the value of these benefits provided by the third party. Only two aggregators reported that they

recorded the value of benefits given to brokers under competitions run by third parties (where that recording is subject to a minimum threshold).

674 We question whether it is appropriate to rely on brokers, who are the intended recipients of the benefit, to make this assessment themselves (in the absence of a process to record and monitor the acceptance of these benefits).

675 We asked broker businesses and brokers to provide their feedback on competitions that allowed them to win prizes from aggregators or lenders. Interestingly, a significant number of brokers who responded raised concerns about such competitions and the risk that they may drive poor consumer outcomes. One broker stated ‘lenders and aggregators should not run competitions based on volumes’. Another broker commented that competitions could create biases towards a particular lender.

Hospitality

676 Hospitality includes benefits such as attending sporting or cultural events, meals and other similar functions. We consider that small offers of hospitality are unlikely to influence a broker’s product recommendations.

677 However, more significant forms of hospitality may increase the risk of a broker recommending a home loan that is not the best option for a consumer, particularly if the hospitality is explicitly or implicitly tied to the sale of home loans by the broker.

678 Approximately 60% of aggregators stated that they provided ad hoc hospitality to brokers. Just over half of those aggregators said they kept a record of brokers’ acceptance of that hospitality (some of which was subject to a minimum threshold). However, only one aggregator stated that they actively reviewed the record as part of their risk and compliance reviews.

679 It appears that some aggregators may have had a different interpretation of what constituted ‘hospitality’ in this question. For example, some aggregators referred to programs under which they pay for attendance for top brokers at overseas conferences as hospitality. We assumed that these programs would be counted as a ‘course or conference’.

680 We also asked whether the broking agreement dealt with the acceptance of hospitality by brokers from third parties (including lenders). Most aggregators reported that the agreement did not include explicit provisions. However, some aggregators had general provisions relating to conflicts of interest.

681 As with other types of soft dollar benefits, very few aggregators had a formal policy on acceptance by brokers of ad hoc hospitality from third parties. Some aggregators noted that the broker would be expected to undertake this assessment themselves. Three aggregators reported that they kept a record of benefits received from third parties (which was subject to a minimum threshold).

682 We also asked lenders whether they provided ad hoc hospitality to broker businesses or brokers. Most lenders reported that they provided such hospitality. Of these lenders, almost 70% said that they kept a record of what was given; some noted that this was subject to a minimum threshold (usually around $100–200).

683 Lenders did not typically notify the aggregator or broker business (where relevant) when they provided ad hoc hospitality to brokers (either for a specific benefit or on a general reporting basis). Only two lenders noted that they may, depending on the circumstances, notify the aggregator of specific hospitality being provided.

684 We asked broker businesses and brokers for their feedback about the provision of ad hoc hospitality by aggregators or lenders. Brokers generally took the view that the provision of hospitality was not inappropriate and could promote strong performance and good sales. One broker commented that ‘awards by aggregators promotes and rewards business standards, including consumer outcomes’.

685 One broker, however, expressed concerns with some forms of hospitality based on sales rather than quality of submissions, noting ‘the additional reward for the amount of sales could influence a broker’.

686 Another broker commented that hospitality was previously prevalent in the industry but that more recently ‘aggregators or lenders rarely offer anything of real value’. His view was echoed by another broker who commented that recognition in the form of hospitality was generally of ‘minimal value’.

Value of soft dollar benefits given to brokers

687 While aggregators and lenders did not generally retain comprehensive records of the type and value of soft dollar benefits provided to brokers, a number of aggregators did give us details of some of these benefits. These aggregators disclosed details of almost $3 million of soft dollar benefits in 2012 and $6 million of benefits in 2015. We note that these figures only represent the value of benefits recorded by the aggregators and the amount of benefits actually provided would be greater. No aggregator reported any cancellation or recovery of soft dollar benefits.

Note: We have excluded the value of courses or conferences which, based on aggregators’ comments, appeared to be available to all brokers, regardless of sales.

688 Very few aggregators could provide any data on the value of soft dollar benefits provided to brokers by third parties, including lenders.

689 Some aggregators could not provide the details of the number of brokers who received a particular benefit. After excluding the value of those benefits, the average value of a benefit provided to a recipient was equal to

$1,300 per recipient in 2012 and $1,450 in 2015. It is possible that some brokers received more than one benefit.

690 The actual per-recipient value of benefits varied widely. The highest value benefit disclosed in 2015 (on a per recipient basis) was an all-expenses paid overseas trip for the aggregator's top brokers (with partners). The per-recipient value of this benefit was almost $13,000 (with a total cost to the aggregator of over $1 million). In addition, another aggregator ran a competition with a first prize value of $30,000.

691 The benefits provided to brokers commonly involved the aggregator paying the costs of travel or attendance at a function. These benefits were generally offered to those brokers who either satisfied a specific sales target, or who were among the top sellers over a particular period. One aggregator noted that the recipients of the overseas travel involved the top 25 brokers in that year (less than 1% of the total number of brokers for that aggregator).

692 The largest values disclosed by aggregators for individual events typically related to travel offered under 'high-flyers' programs. Based on the information provided by aggregators and our own desktop research, such travel included trips to the Caribbean, Los Angeles and Hawaii. We note that, even if such travel involves professional development sessions, it is still likely to be a strong incentive for brokers to seek to qualify.

693 Other than travel and functions, a small number of aggregators reported programs that involved the provision of other types of soft dollar benefits (e.g. consumer goods and gift vouchers). Some aggregators also reported the provision of cash prizes.

694 It appears that the criteria for receiving some benefits from a number of aggregators related to the sale of that aggregator's white label product specifically (rather than all home loans sold by the broker). This is particularly the case for some aggregator's 'high-flyer' travel programs. We note that such benefits have a heightened risk of inappropriate product recommendations being made by the broker, as they provide particular incentives to brokers to promote those loans over all other loans.

D How other participants are paid

Key points

Home loans are sold to consumers through channels other than brokers.

Lenders sell home loans through their own staff, who may earn bonuses on the sale of loans. These bonuses are, in some cases, similar to commissions received by brokers. However, lenders' staff usually receive a guaranteed salary.

Lenders may also use referrers (usually unlicensed individuals or businesses). These referrers provide consumer details to lenders so they can sell loans to those consumers. Payments made to referrers are of a similar size to the upfront commissions paid to brokers.

Comparison websites are another channel for the sale of home loans.

Overview

695 In this section we review the remuneration arrangements of three other home loan distribution channels:

(a) lenders' staff;

(b) referrers; and

(c) comparison websites.

696 Lenders' staff who are responsible for the sale of home loans generally receive a salary. This is in contrast to brokers who are generally paid based wholly on commissions from sales. There were some exceptions—for example, 'franchise' home loan sellers, who appear to operate in line with the broker model (although they sell only one lender's products).

697 Lenders' staff can still receive cash incentives related to the sale of home loans. These payments are described as 'bonuses' rather than 'commissions'. We saw significant variation in the value of these bonuses, from very small amounts (including many staff who received no bonus) to large amounts totalling hundreds of thousands of dollars. Overall, major banks tended to pay considerably higher cash incentives to their staff than other lenders.

698 While the bonuses resembled the commission payments to brokers, there were some important differences. Some lenders reported that the bonus was not calculated for each individual home loan sale. Rather, it was based on an overall assessment of the staff member's performance, with the level of sales

being one component. Other lenders reported that while staff members could be remunerated for each sale, other non-sales based criteria also applied.

699 Overall, lenders' staff appeared to access fewer soft dollar benefits than brokers.

700 Referrers are generally individuals or businesses who provide referral services to lenders or brokers (i.e. by passing on consumer details to these entities). Referrers do not need to hold a credit licence under the National Credit Act.

701 Referrers who provided leads to lenders received on average $2,557 per settled loan, which equates to 0.46% of the loan value. For some types of referrers, this could be as much as $3,043 or 0.56% of the loan value. This was similar to the rates of upfront commission paid to brokers, even though referrers are not allowed to provide the level of advice and services offered by brokers.

702 Aggregators were unable to provide us with details of the value of remuneration paid by brokers to their referrer networks.

703 We also reviewed the remuneration arrangements between lenders and comparison websites. Payments by lenders to these websites increased substantially between 2012 and 2015. These payments were often made on the basis of click-throughs (i.e. where consumers use a link on the comparison website to access the lender's website). Payments for such click-throughs were reported to be between $70 and $250 each time.

Lenders' staff

Role of staff

704 Lenders' staff are often involved in the sale of home loans. In assessing consumer outcomes in Section F, we compared home loans sold through brokers to loans sold by lenders' staff. Given the importance of this comparison, we gathered information from lenders about how these staff are remunerated.

Note: We asked lenders about the remuneration arrangements for their staff whose job predominantly involves the sale of home loans to retail consumers. The remuneration arrangements for other staff may be different.

705 A key difference between the remuneration of brokers and lenders' staff is that the lenders' staff are on a base salary and, as such, do not need to achieve sales to make a guaranteed income. However, bonuses and other forms of incentive are also a feature of the remuneration of lenders' staff and are therefore worth comparing with how mortgage brokers are remunerated.

Note: In July 2016, the banking industry commissioned an independent review through the ABA into retail banking remuneration. The review is examining payments and commissions made to bank staff as well as to third parties, and includes remuneration for selling and providing advice on products such as transaction accounts, general insurance products, consumer credit insurance, home loans, personal loans, credit cards and small business loans. It covers consumer-facing employees, contractors and third parties, as well as non-consumer facing roles such as the managers and supervisors of those staff. For more information, go to Retail Banking Remuneration Review.

706 For our review, we asked about the different categories of staff engaged in selling home loans. The main categories were:

(a) specialist home lending staff at the branch or sales office (branch staff)—these staff can be employed directly by the lender or through a franchise;

(b) specialist home lending staff in call centres (telephone sales staff);

(c) specialist home lending staff who visit consumers in their homes or workplaces (mobile lending staff)—these staff can be employed directly by the lender or through a franchise;

(d) specialist home lending staff at a franchised branch or sales office (franchised staff); and

(e) any other staff whose main job is selling home loans.

707 We also asked how sales staff are categorised for the purpose of the National Credit Act (e.g. as a credit representative of the lender or as an employee under the lender's credit licence).

708 As expected, we found that most branch, telephone sales and mobile lending staff are employees of the lender and can engage in credit activities under the lender's credit licence without further authorisation: s29(3)(b)(i). However, members of some lenders' sales staff were either credit representatives or there was a mixture of employees and credit representatives.

709 Lenders who operated a franchise model noted that members of their sales staff were either credit representatives or a mix of credit representatives and employees.

Non-variable remuneration

710 Nearly all of the lenders' staff received a base salary, except for some franchised mobile lending staff who operated more like brokers. The average base salary varied widely between lenders and across categories of staff.

711 Overall, base salaries ranged from a minimum of $28,700 (for telephone sales staff of a mid-tier lender) to $107,004 (for 'other' sales staff of a foreign bank). See Table 6 for the base salaries across different staff categories in 2015.

Table 6: Base salaries across different staff categories

Staff category	Base salary
Telephone sales staff	The average base salary ranged between $28,700 and $79,117. There was a tendency for major lenders, mutual banks and credit unions to pay a slightly higher average base salary than other types of lenders. The average base salary for the highest earning 5% of staff (which ranged from $59,400 to $89,900) was significantly higher than the average base salary for the lowest earning 5% of staff ($28,700 to $73,233).
Branch staff	The average base salary ranged between $64,700 and $88,200. There was tendency for major lenders to have the widest range of average base salaries, paying the maximum and the minimum average values. The average base salary for the highest earning 5% of staff (which ranged from $77,000 to $120,000) was significantly higher than the average base salary for the lowest earning 5% of staff ($47,100 to $75,000).
Mobile lending staff	The average base salary ranged between $75,000 and $102,000. There was tendency for mid-tier lenders to pay a slightly higher average base salary than other types of lender. The average base salary for the highest earning 5% of staff (which ranged from $85,000 to $120,000) was significantly higher than the average base salary for the lowest earning 5% of staff ($62,500 to $80,000).
Other home loan sales staff	The average base salary ranged between $61,000 and $107,000; however, the number of responses in this category was small.

Cash incentives

712 We sought to understand which categories of staff received cash incentives that were directly or indirectly related to the sale of home loans.

713 We found that most lenders across most staff types pay some form of incentive that is directly or indirectly related to the sale of home loans. Such payments are referred to as a ‘bonus’ by most lenders, rather than as a commission payment. However, for some franchised staff, the payment is known as a ‘commission’. The difference in terminology can be important, as it can signal differences in the way that the cash incentive is awarded.

Note: Some lenders who stated that they did not pay cash incentives noted that staff members could participate in a variable rewards scheme. Based on the description of these schemes, it appears that a staff member’s success in selling home loans could influence the incentives they received (i.e. when assessing that staff member’s performance in the relevant time period). An indirect incentive could therefore be tied to the sale of home loans and these lenders should have answered ‘yes’ to this question.

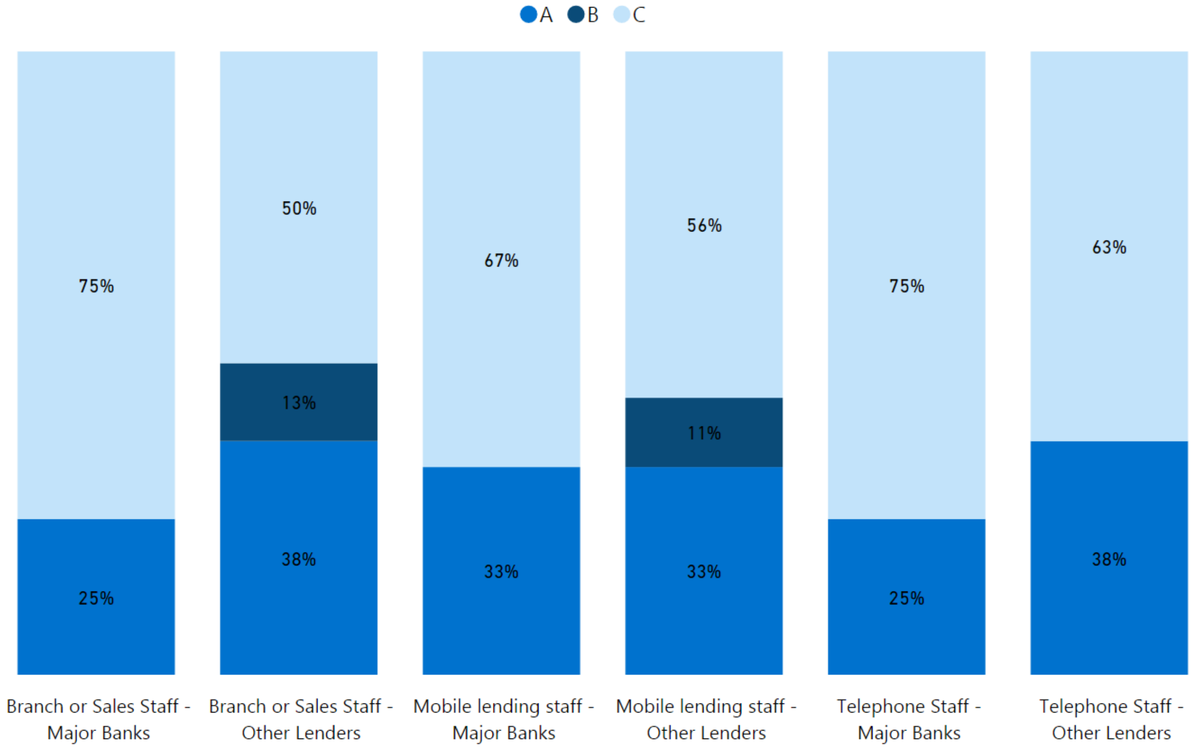
How cash incentives are calculated and paid

714 We asked on what basis the bonus was calculated, whether on each home loan sold or on broader performance criteria. Where it was based on each home loan sold, we also asked whether the bonus was dependent on other, non-sales based criteria.

715 A bonus payment calculated on each sale of a home loan is, in essence, similar to a sales-based commission. This is because the sales person—whether the lender's staff member or a broker—is aware of the value of the cash incentive that will flow from the sale, which provides a direct incentive for the person to sell the home loan. The direct connection between the sale and the cash incentive may be affected by the impact of other, non-sales based criteria on the bonus payment: see paragraphs 719–733.

716 Figure 18 sets out the findings on how bonus payments are calculated for telephone sales staff, branch sales staff employed directly by lenders, and mobile lending staff employed directly by lenders. There was insufficient data from lenders to report any findings on the other types of staff.

Figure 18: How bonus payments are calculated (telephone sales staff, branch staff, and mobile lending staff)



Note 1: See paragraphs 717–718 for a description of the trends shown in this figure.

Note 2: In this figure:

A = an amount based on the loan writer's overall performance;

B = an amount calculated on each home loan sold (subject to criteria for any applicable minimum thresholds); and

C = an amount calculated on each home loan sold (subject to criteria for any applicable minimum thresholds) but also subject to other non-sales based criteria.

717 Our findings were as follows:

(a) *Branch staff*—One major bank and three other lenders calculated the bonus payments for branch staff based on an assessment of the overall performance of the staff member. Another lender calculated the bonus payment on each home loan sold, without reference to other, non-sales based criteria. The remaining lenders calculated a bonus payment on each home loan sold, although the payment was also subject to other, non-sales based criteria.

(b) *Mobile lender staff*—One major bank and three other lenders calculated the bonus payments for mobile lending staff based on an assessment of the overall performance of the staff member. Another lender calculated the bonus payment on each home loan sold, without reference to other, non-sales based criteria. The remaining lenders calculated a bonus payment on each home loan sold, although the payment was also subject to other, non-sales based criteria.

Note: Only three major banks reported having non-franchised mobile lending staff, which accounts for the difference in the proportions in the figure.

(c) *Telephone sales staff*—One major bank and three other lenders calculated the bonus payments for telephone sales staff based on an assessment of the overall performance of the staff member. The remaining lenders calculated a bonus payment on each home loan sold, although the payment was also subject to other, non-sales based criteria.

718 No lenders changed their approach between 2012 and 2015.

Factors affecting the payment of cash incentives

719 We asked lenders whether a cash incentive could be reduced or increased based on other factors.

720 Except for franchised staff, lenders could usually reduce a cash incentive if a staff member did not:

(a) meet quality metrics (e.g. errors on loan applications);

(b) comply with general risk, compliance and operations requirements; or

(c) display organisational values.

721 Lenders were less likely to be able to increase the cash incentive for staff members who did display these factors.

722 Some lenders could also reduce or cancel a cash incentive based on poor customer satisfaction metrics and high complaint numbers. However, lenders were less likely to reduce cash incentives based on loan account performance (e.g. default, closure or cancellation rates).

723 For franchised staff, lenders were less likely to be able to reduce a cash incentive based on the factors in paragraph 720, other than in response to loan account performance (e.g. default, closure or cancellation rates). This indicates that the cash incentives paid to franchised staff are more in line with commissions paid to brokers.

724 We asked whether any part of the cash incentive was deferred (i.e. earned in a remuneration period but received by the staff member at a later date).

725 Deferred payment of cash incentives was relatively common for branch and mobile lending staff. Just under half of the lenders also took this approach for telephone sales staff. Overall, major banks deferred payment of cash incentives more often than other lenders.

726 We asked if a cash incentive was paid automatically without any subjective assessment of the staff member's entitlement, and who was typically involved in that decision. All lenders confirmed that there was a subjective assessment of the staff member's entitlement to a cash incentive and also the value of that incentive. This assessment usually involved a number of people within the lender. It also appeared that a similar number of people were responsible for deciding whether a cash incentive would not be paid, or would be reduced compared to what would otherwise be paid.

727 Many lenders reported that an 'accelerator' applied to cash incentives. An accelerator is a feature of a remuneration structure that results in a higher per unit incentive, subject to satisfying specific criteria (e.g. a sales volume). Such accelerators typically operate if the relevant sales target is exceeded and could apply to the sales in a period between one month and a year.

728 In contrast to broker channels, lenders did not typically assign a nominal value of cash incentives payable per home loan sold. However, a small number did so for mobile lending, branch and telephone sales staff. These values ranged from 0.03% of the loan value to 0.35%. Similar to brokers, franchised staff were also given a nominal value of cash incentives payable per home loan sold.

729 We asked whether the amount payable, for cash incentives on the sale of home loans was dependent on the value of sales or a range of other measures (e.g. profitability, cross-selling and number of sales), or whether it was a mix of factors. Most lenders stated that it was a mix of factors; however, a small proportion stated that it was solely dependent on the value of sales.

730 Cash incentives were paid by most lenders as a lump sum, covering all cash incentives earned in that period (not just for the sale of home loans).

731 Most lenders did not reduce a cash incentive if the home loan was repaid or discharged before the incentive was calculated. Likewise, a cash incentive that had been paid was not recoverable if the loan was repaid or discharged early or the loan defaulted, except for franchised mobile lenders.

732 We also asked if lenders reduced a cash incentive if the staff member provided a non-advertised interest rate discount for the home loan: one lender did so in 2015, while three did so in 2012 for some categories of staff.

733 Lenders could usually cancel or recover cash incentives based on factors such as customer complaints, poor customer feedback, poor quality metrics for business practices, or non-compliance with general risk, compliance and operational requirements. Where a cash incentive was recoverable, lenders would typically offset the amount against future payments.

Value of cash incentives paid to lenders' staff

734 We asked lenders to provide details of the value of cash incentives paid to their staff in 2015. This included the average value of incentives paid across all staff, from the lowest earning 5% of staff to the highest earning 5% of staff.

735 The average value of cash incentives varied widely across categories of staff and of lenders. Overall, values ranged from as low as $0 to almost $2 million, with franchised mobile lending staff receiving much higher cash incentives than other staff categories. This was consistent with our observation that franchised mobile lending staff operated more like brokers.

736 Overall, major lenders paid considerably higher cash incentives than other types of lenders across all staff categories. Table 7 sets out the ranges for each staff category.

Table 7: Value of cash incentives across different staff categories

Staff category	Value of cash incentives on an annual basis
Telephone sales staff	The average cash incentives ranged between $918 and $14,000. There was a tendency for major lenders to pay a higher average cash incentive than other lenders. Between 0% and 71% of telephone sales staff did not receive any cash incentives, depending on the lender. The average cash incentive for the highest earning 5% of staff (which ranged from $50 to $109,000) was significantly higher than the average cash incentive for the lowest earning 5% of staff ($0 to $10,688).
Branch staff	The average cash incentive ranged between $1,400 and $24,000. There was tendency for major lenders to pay higher average cash incentives than other lenders. Between 18% and 58% of branch staff did not receive any cash incentive. The average cash incentive for the highest earning 5% of staff (which ranged from $2,850 to $141,000) was significantly higher than the average cash incentive for the lowest earning 5% of staff ($0 to $4,400).
Mobile lending staff	The average cash incentive ranged between $0 and $46,000. There was tendency for major lenders to pay higher average cash incentives. Between 7% and 71% of staff in this category did not receive any cash incentives. The average cash incentive for the highest earning 5% of staff (which went as high as $294,000) was significantly higher than the average cash incentive for the lowest earning 5% of staff (up to $10,000).
Other home loan sales staff	The average cash incentive for other staff ranged between $5,300 and $377,000. Between 0% and 19% of staff did not receive cash incentives; however, the number of responses in this category was small.

Cash incentives paid to lenders' staff for cross-selling products

737 Our review sought to identify the nature and extent of cash incentives for the cross-selling of products by lenders' staff. We sought to understand whether staff members can earn cash incentives for selling or making a referral on a number of different products and services.

738 We found that most lenders enabled their staff to earn cash incentives for the cross-sale of general insurance products, both those related to the home loan and also other forms of general insurance. Some lenders (less than half) also enabled staff to earn cash incentives for the sale of other products, such as:

(a) consumer credit insurance, both for the home loan and other credit products;

(b) other credit products, including credit cards;

(c) deposit products, including offset accounts;

(d) business or commercial financial products; and

(e) financial advice services.

739 Cash incentives for the cross-selling of other financial products and services were generally more common in the major banks.

740 Lenders' staff could not earn cash incentives for sales or referrals relating to credit repair, for-profit budgeting, or debt negotiation and/or bankruptcy services (except for one lender, who indicated that mobile lending staff could earn cash incentives for sales or referrals relating to debt negotiation and/or bankruptcy services).

Soft dollar benefits received by lenders' staff

741 As with brokers, we sought to understand whether lenders' staff could receive soft dollar benefits (e.g. courses and conferences, hospitality and competitions).

Courses and conferences

742 Our review sought to identify the nature and extent of courses and conferences paid for by lenders for their staff. We asked whether staff members could be entitled to courses or conferences depending, in whole or in part, on the level of sales of home loans by that staff member: see Table 8.

Table 8: Professional development benefits

Activity type	Entitlement to this benefit
Australian course or conference paid for or subsidised by the lender	For a minority of lenders, branch, mobile lending and telephone sales staff could be entitled to such benefits. In each case, less than a third of lenders said that the staff member could receive the benefit. Franchised staff were not able to receive this benefit from any lenders.
International course or conference paid for or subsidised by the lender	This was generally not provided by lenders, with the exception of one lender who had provided this for branch staff.
Australian course or conference paid for or subsidised by a third party	A few lenders (two or less) permitted branch or mobile lending staff to accept these benefits.
International course or conference paid for or subsidised by a third party	This was generally not allowed by lenders, with the exception of one lender who had permitted this for branch staff.

Hospitality

743 We sought to understand whether, and to what extent, lenders provide ad hoc hospitality to their staff (i.e. forms of hospitality and benefits that have a monetary value, such as gift cards) and whether or not this hospitality is recorded.

744 We found that provision of these types of benefits to lenders' staff depended on the type of staff member. This ranged from almost 80% of relevant lenders making these benefits available to branch staff, to just below 45% of lenders stating that telephone sales staff could receive these types of benefits. Lenders did not provide these types of benefits to franchised staff. Lenders generally kept a record of these benefits, although usually only if the benefit exceeded a threshold value (typically around $200–300).

745 We also asked whether, and to what extent, lenders permitted their staff members to accept other forms of rewards and recognition from third parties (regardless of whether those benefits were dependent on sales) and whether this hospitality was recorded. Around 50% of lenders allowed staff to accept these types of benefits from third parties (although this figure was less for some categories of staff, such as telephone sales and mobile lending staff). Of the lenders who permitted staff to receive benefits from third parties, approximately 60% kept a record of those benefits, although this was only if the benefit exceeded a threshold value (typically around $200–300).

746 We asked lenders for details of the value of hospitality benefits given in 2012 and 2015. We note that most lenders were unable to provide complete details of these payments.

Competitions

747 We asked lenders whether they ran competitions for their staff on a regular basis in which entry to the competition was wholly or partly dependent on sales. We found that approximately half of lenders ran competitions for their branch and mobile lending staff. A small proportion of lenders ran competitions for telephone sales staff. Lenders did not typically run competitions for franchised staff.

748 We also sought to understand whether lenders' staff had access to competitions run by third parties in which entry was wholly or partly dependent on sales. We found that lenders did not generally permit staff to participate in competitions run by third parties; however, a small number of lenders permitted branch, mobile lending and telephone sales staff to participate in these competitions.

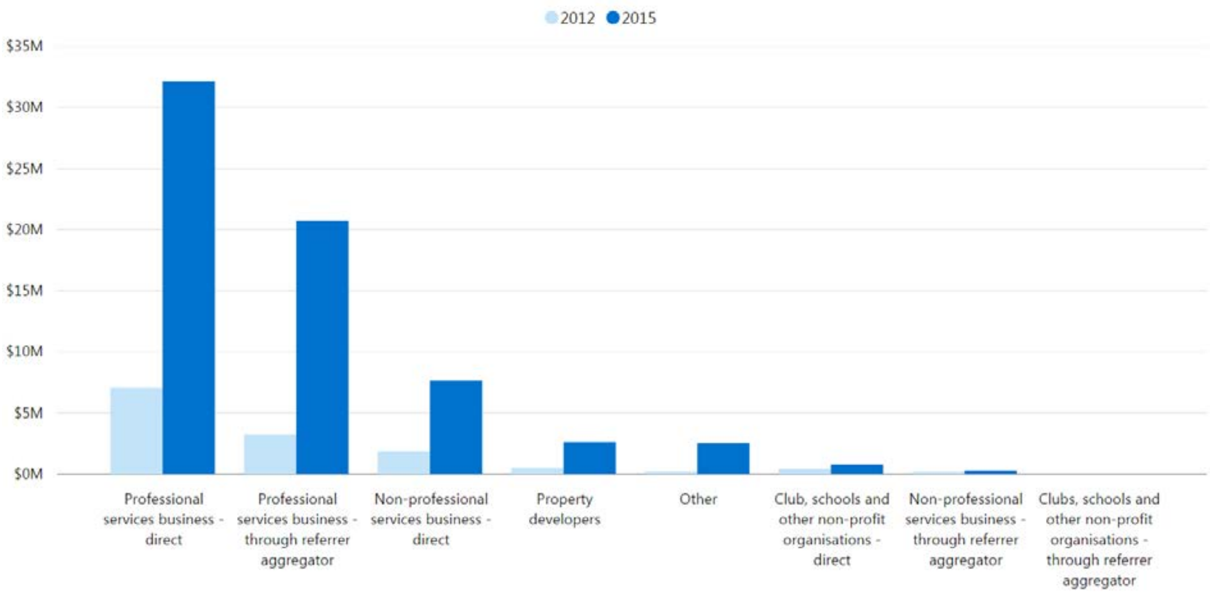
Referrers in the home loan market

749 Our review considered the value of payments made by lenders to referrers (including referrer aggregators).

Note: As described in paragraph 285, aggregators could not tell us the value of payments made by brokers to referrers.

750 In 2015, a total of $67 million was paid to referrers (up from $13 million in 2012). Figure 19 sets out value of total payments made to referrers by lenders in 2012 and 2015 across the different types of referrers.

Figure 19: Value of payments to referrers for home loan sales



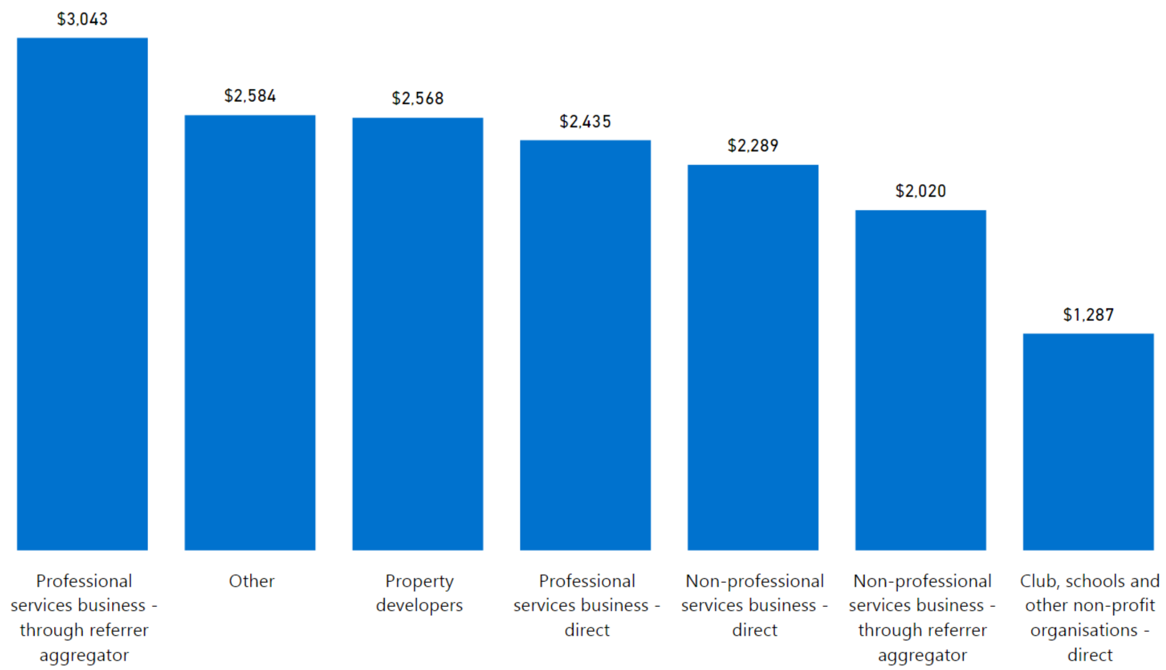
Note: See paragraph 751 for a description of the trends shown in this figure.

751 Most payments were made to professional services businesses, either directly (ranging from around $7 million in 2012 to $32 million in 2015) or through referrer aggregators (around $3 million in 2012 to around $21 million in 2015). Other payments to referrers included those to non-professional services businesses (over $1.8 million in 2012 to around $7.6 million in 2015) and property developers (less than $1 million in 2012 to around $2.6 million in 2015). Payments to clubs, schools and other non-profit organisations were of lower value.

752 At an industry level, we estimated that in 2015 lenders paid referrers an average of $2,557 per referral that resulted in a settled loan, or 0.46% of the loan value: see Figure 20. However, there was considerable variation between payments to different types of referrers. This ranged from $1,287 per loan (representing 0.35% of the loan value) for clubs, schools and other non-profit organisations to $3,043 (representing 0.56% of the loan value) for professional services business (where the referral came through a referrer aggregator).

753 Such payments are similar to the value of upfront commissions paid to brokers even though referrers are, under the law, not providing the level of advice and service offered by brokers. Given the growing size of the referrer industry and the remuneration levels available to unlicensed intermediaries, ASIC will continue to monitor developments in this area.

Figure 20: Average payment per referral that resulted in a settled loan (by source)



Note: See paragraph 752 for a description of the trends shown in this figure.

Comparison websites

754 Our review considered the nature and value of payments made between comparison website providers and lenders. We asked comparison website providers and the lenders to detail the payment structures in place, and whether or not such payments were disclosed to consumers.

Payments for listing products and click-throughs

755 We sought to confirm whether lenders made specific payments to comparison website providers to list their home loan products on their websites. All of the comparison website providers we reviewed stated that lenders do not make payments to list products on the websites.

756 We also asked whether payments made to comparison websites by lenders are based on the number of click-throughs or successful conversion of leads. Three of the four comparison website providers stated that payments are made by lenders to them based on a mixture of click-throughs and successful conversions. We asked these websites for details of these payments.

757 One comparison website only started direct monetisation of leads in September 2015, so the total payments received were significantly lower than the other websites. The other three comparison websites were paid an average of approximately $3.8 million dollars in 2015. This represented a growth in payments of approximately 68% since 2012. The highest amount earned in 2015 was approximately $4.5 million.

758 Lenders reported that a paid click-through from a comparison website could cost between $70 and $250 each time.

Rating and awards

759 Comparison websites often also provide consumers with ratings for various loans and other financial products. The loans may be given a value-based rating on price and features. Other rating calculations may comprise of specific methodology based on benchmarks, requirements and criteria.

760 We sought to identify whether lenders made specific payments in relation to product rating systems offered by comparison websites (e.g. ‘five star rating’ or ‘best lender award’). Details included the total value of payments, how often lenders are required to make payments, whether or not lenders can make a payment to increase the number of stars/rating received, and whether or not such payments were disclosed to consumers.

761 We found that lenders cannot make payments to have their products featured in the rating systems or awards offered by comparison websites. Winners are usually published on the comparison website and this is not paid. However,

lenders can make payments to use awards, ratings, logos and badges in their marketing materials after the ratings and award winners have been declared.

762 One comparison website advised that the awards are conducted annually and lenders do not need to enter these awards. Winners are limited to the top 10% of products in each category, based on value to consumers, as determined by information collected in the comparison website's database. Lenders cannot pay a fee to be considered for an award and all lenders are eligible for an award.

Advertising fees

763 We also sought to identify whether lenders can make payments to increase the prominence of their home loan product in marketing material or on websites developed and/or distributed by comparison website providers (other than in algorithms that are used to rank products). Examples might include being listed first under 'sponsored results' or using a larger logo.

764 All comparison website providers advised us that lenders could not make payments to increase the prominence or ranking of their products in product comparison tables. Lenders could also not make payments to increase the prominence of a home loan product in the algorithm used by comparison websites to list products for consumers.

765 However, most providers confirmed that for a fee lenders may place advertising on a selected area of the website (e.g. banners and widgets) within the comparison table itself or in emails to the comparison website's member base.

766 We did not receive full data on the value of any advertising payments made by lenders to comparison websites. However, in 2015 one comparison website received $625,000 in advertising fees and another received approximately $125,000. Collectively, this was over double the amount of advertising revenue received in 2012, again highlighting the increasing growth of the comparison website use by both consumers and lenders.

Other payments

767 Our review found that comparison websites receive other types of revenue, from services such as:

(a) the sale of advertising space on the website or in marketing emails;

(b) subscription products that allow lenders access to competitor data and research; and

(c) market research services.

Disclosure of payments

768 We sought to understand whether or not the payments received by comparison websites were disclosed to consumers.

769 We asked what type of disclosure consumers are given about payments by lenders to comparison websites. One provider advised that promotional placements are marked as 'advertisements' or 'sponsored'. Others managed disclosure through disclosure documents such as Financial Services Guides (FSGs) and credit guides.

770 Only one website advised that remuneration arrangements were disclosed to consumers in an FSG and a 'How we get paid' statement. However, our review of the websites found that information about remuneration arrangements was generally disclosed in an FSG or credit guide downloadable from the website.

771 We note that consumers are not required to read or access FSGs or credit guides before using the websites.

E Competition in the home loan market

Key points

This section summarises our findings on consumer outcomes relating to the choice of lender recommended by brokers.

Paying higher upfront commissions, particularly campaign-based bonus commissions, can result in a lender selling more loans through brokers.

While brokers may have access to home loans sold by a large number of lenders, brokers generally recommend loans from a small number of lenders.

Ownership of aggregators by lenders is affecting loan flows in the home loan market, particularly if the aggregator also sells white label loans funded by the lender.

Overview

772 To understand how broker remuneration and ownership structures between lenders and aggregators might influence which lender is recommended by a broker, we analysed loan data for $550 billion of new home loans provided through 678 combinations of lenders and aggregators between 2012 and 2015.

773 We used this data to analyse:

(a) the impact of commission structures on the loan flow from aggregators to lenders (including campaign-based bonus commissions);

(b) the variability in the number of lenders recommended by brokers; and

(c) the impact of ownership structures on the loan flow from aggregators to lenders.

774 We found that campaign-based bonus commissions do work: for one lender offering higher commission for a limited period, the volume of home loans sold increased by a factor of over four.

775 Apart from campaign-based bonus commissions, we found that paying a higher upfront commission may assist larger lenders to get more loans (this may not work as well for smaller lenders).

776 On average, aggregators sent loans to 29 lenders in 2015. However, this breadth of lenders is not reflected in the data for individual broker businesses. We found that on average broker businesses sent over 80% of loans to the four most commonly recommended lenders for the business.

777 We found that ownership of aggregators by lenders affected loan flows in the home loan market, particularly if the aggregator also sold white label loans funded by the lender.

778 Three lenders with ownership stakes in aggregators generally received a proportionate number of loans sold under their own brand from their owned aggregator. For some of those lenders, when taking into account the value of white label loans funded by the lender, they received a significantly higher proportion of the aggregator's loans (compared to the lender's overall market share).

Effect of commissions on loan flow

779 We analysed aggregators' monthly loan flow data to test the effect of upfront commission payments from lenders to aggregators on the flow of loans being sent by the aggregator to the lender.

Note: In this context, 'flow' refers to the *value* rather than the *number* of loans being sent through an aggregator to a lender.

780 While it is difficult to isolate the impact of commissions on loan flow due to other factors, some observations can be made.

781 We also analysed promotional offers through campaign-based commission structures, where brokers were offered higher upfront commission rates from certain lenders. We sought to understand what happened to loan flows during those promotional periods: see paragraphs 786–792.

Upfront commissions

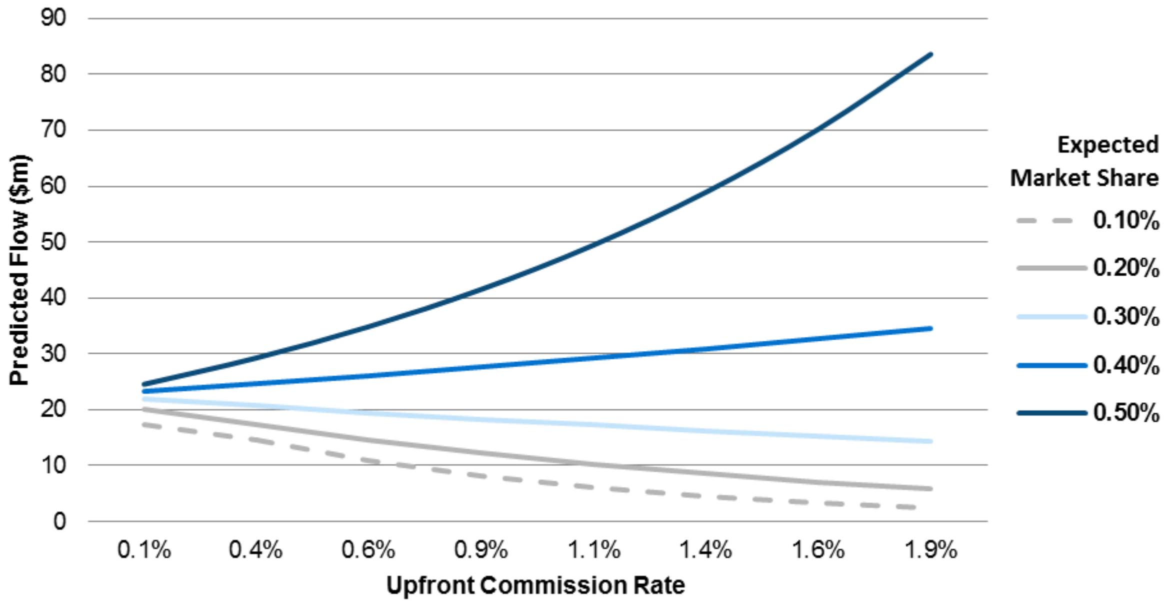
782 We analysed the effect of the upfront commissions on loan flow by combining two regression models. The first model tested the effect of certain factors on the probability that at least one loan would be settled between a lender/aggregator within a month. The second model tested the effect of these factors on the size of the loan flow, when it was already known that the flow would occur. These two models were combined to determine the relative effect of the factors on the expected loan flow in a month.

783 Figure 21 shows the effect of the rate of upfront commission on loan flow based on expected market shared for each lender–aggregator combination.

Note: The expected market share was calculated for each year from 2012–15.
The highest expected market share aligns to the largest lenders and aggregators.
For the purposes of this calculation:

$$\text{Expected market share} = \frac{\text{Flow to lender}}{\text{Total flow}} \times \frac{\text{Aggregator flow}}{\text{Total flow}}$$

Figure 21: Expected flow ($ million) for lenders–aggregators based on variations in annual rate of upfront commission and expected market share (%) of lenders



Note: See paragraph 784–785 for a description of the trends shown in this figure.

784 For lender–aggregator combinations with a larger expected market share, a given increase in the rate of upfront commission was associated with a greater increase in the loans flowing from that aggregator to the lender. This appears to suggest that for larger lenders the rate of upfront commission is a stronger lever to increase the value of loan flow.

785 Interestingly, for lender–aggregator combinations with a smaller expected market share there seemed to be a slightly negative relationship between the rate of upfront commission paid by smaller lenders and the flow of loans from aggregators. We note that this result seemed to be influenced by several smaller lenders who paid very high commission rates that did not have a corresponding boost in loan flow.

Campaign-based commission offers

786 We analysed the impact of five campaign-based commission structures offered by three lenders in 2013, 2014 and early 2015, together with an additional long-term increase in the rate of upfront commission offered by one of those lenders.

> Note: We were not able to look at some of the campaign-based offers as the dates of the campaigns overlapped with other campaigns or were in late 2015 (so that the effect was not evident in the data we collected, which ended in December 2015).

787 Table 9 sets out our observations on the impact of these offers.

Table 9: Effect of campaign-based commission offers on loan flow and market share

Lender	Campaign dates	Campaign type	Increase in average loan flow (during/after)	Average market share (before/during/after)	Increase in average market share (during/after)
Other bank 1 (campaign 1)	Start of 2014 (ongoing)	Ongoing increase in upfront rate to 0.88%	During: 2.1 times After: 4.4 times	Before: 0.04% During: 0.09% After: 0.17%	During: 2.3 times After: 4.2 times
Other bank 1 (campaign 2)	Middle of 2015 (4 months)	Further increase in upfront rate to 1.00%	During: 1.6 times After: 1.9 times	Before: 0.44% During: 0.60% After: 0.67%	During: 1.4 times After: 1.5 times
Other bank 2 (campaign 1)	Early 2013 (4 months)	Bonus upfront commission of up to 0.30%	During: 1.7 times After: 1.6 times	Before: 0.52% During: 0.81% After: 0.69%	During: 1.5 times After: 1.3 times
Other bank 2 (campaign 2)	Late 2013 (3 months)	Bonus upfront commission of up to 0.30%	During: 0.7 times After: 2.0 times	Before: 0.69% During: 0.47% After: 1.28%	During: 0.7 times After: 1.9 times
Other bank 2 (campaign 3)	Early 2014 (3 months)	Bonus upfront commission of 0.10%	During: 0.8 times After: 1.2 times	Before: 1.46% During: 1.03% After: 1.43%	During: 0.7 times After: 1.0 times
Non-bank lender	Early 2015 (2 months)	Bonus upfront commission of 0.10%	During: 0.9 times After: 1.3 times	Before: 0.45% During: 0.40% After: 0.49%	During: 0.9 times After: 1.1 times
Other bank 3	Late 2014 (3 months)	Increase in upfront rate to 0.80%	During: 1.3 times After: 2.7 times	Before: 2.54% During: 3.23% After: 6.50%	During: 1.3 times After: 2.6 times

Note 1: As Other bank 1's first campaign was an ongoing offer, we have calculated only for a three-month campaign period.

Note 2: Average figures for 'after' in Other bank 2's first campaign are calculated over two months, due to overlapping campaigns.

Note 3: Average figures for 'before' in Other bank 2's second campaign are calculated over the previous two months, due to overlapping campaigns.

Note 4: Other bank 3's commission offer was accompanied by a consumer offer involving a discounted interest rate and fees.

788 We first looked at the average flow of loans to the lender in the three months before the campaign offer started. We then compared this to the loan flow *during* the offer and, recognising that the impact of the campaign would be delayed due to loans taking up to 90 days to settle, in the three months *after* the campaign. The average loan flow during and after the campaign is shown in Table 9 as a multiple of the average flow before the campaign.

Note: In reviewing the impact of the campaign-based offers, we noted that the increased rate of upfront commission or bonus commission only became evident in the rates actually paid by the lenders *after* the offers finished. This is due to the delay in the loan application process and settlement of the loan (which is when the commission is paid).

789 In addition, we looked at the impact (during these three periods) on the lender's share of the market, in absolute and relative terms.

790 In each case, the flow of loans to the lender increased substantially, between 1.2 and 4.4 times the flow in the three months *after* the campaign (when loans applied for by consumers during the campaign would settle) compared to the three months *before* the campaign.

791 As well as the increase in loan flow, each lender also experienced an increase in their market share after the campaign-based offers, although this increase was typically smaller than the increase in loan flow. Based on the absolute value of each lender's market share, the lenders that offered these campaign-based commission structures were relatively small (although 'Other bank 3' captured 6.50% of the broker market as a result of its offer in late 2014).

Note: 'Other bank 2' offered three separate campaign-based offers through 2013 and 2014, making it harder to separate the impact of each offer on the loan flow. However, an increase in loan flow is clearly shown in the three months after each offer.

792 Given the individual circumstances of the lenders involved, we could not accurately assess whether the increase in loan flow or market share was maintained after the campaign offer finished.

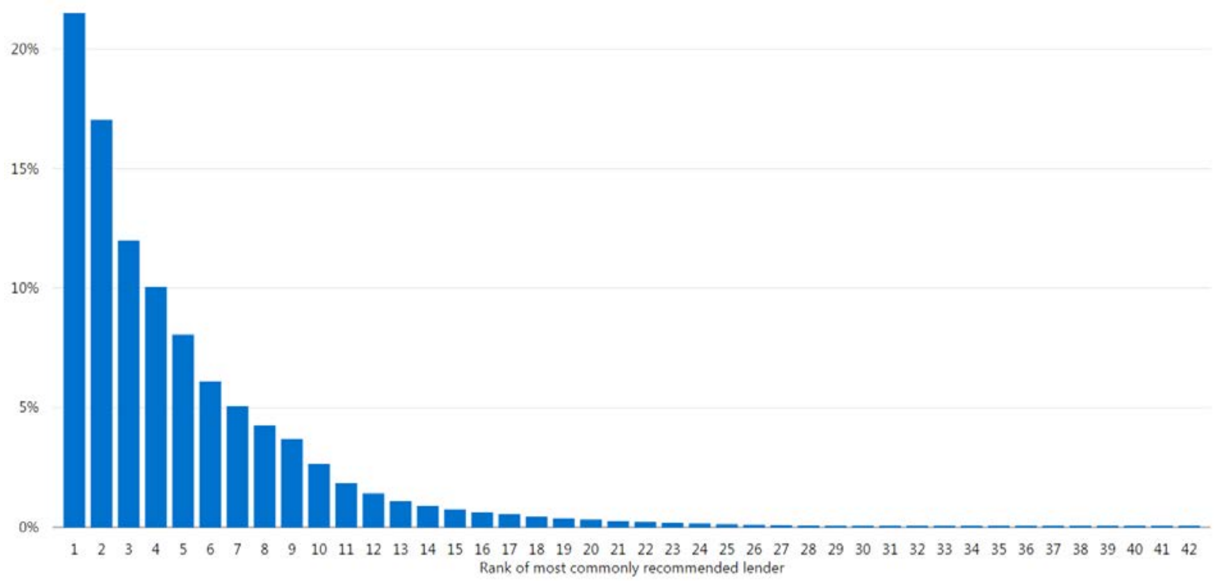
Lenders used by aggregators and brokers

793 On average, aggregators sent loans to 29 lenders in 2015, with a range of between 17 and 42 lenders. These figures remained stable from 2012.

794 A reasonably small number of lenders accounted for most of the loans provided by each aggregator. Figure 22 shows what percentage of loans (by value) each aggregator sent to its most commonly recommended lenders. That is, the figure shows what percentage of loans sold through an aggregator went to the most commonly recommended lender, then the second lender and so on.

Note: The most commonly recommended lender may differ for each aggregator. For example, if Aggregator A recommended more loans (by value) from CBA, then CBA would be that aggregator's number one ranked lender. If Aggregator B recommended more loans from NAB, then NAB would be that aggregator's number one ranked lender.

Figure 22: Proportion of loans (by value) sent to aggregators' most commonly recommended lenders in 2015



Note: See paragraph 795 for a description of the trends shown in this figure.

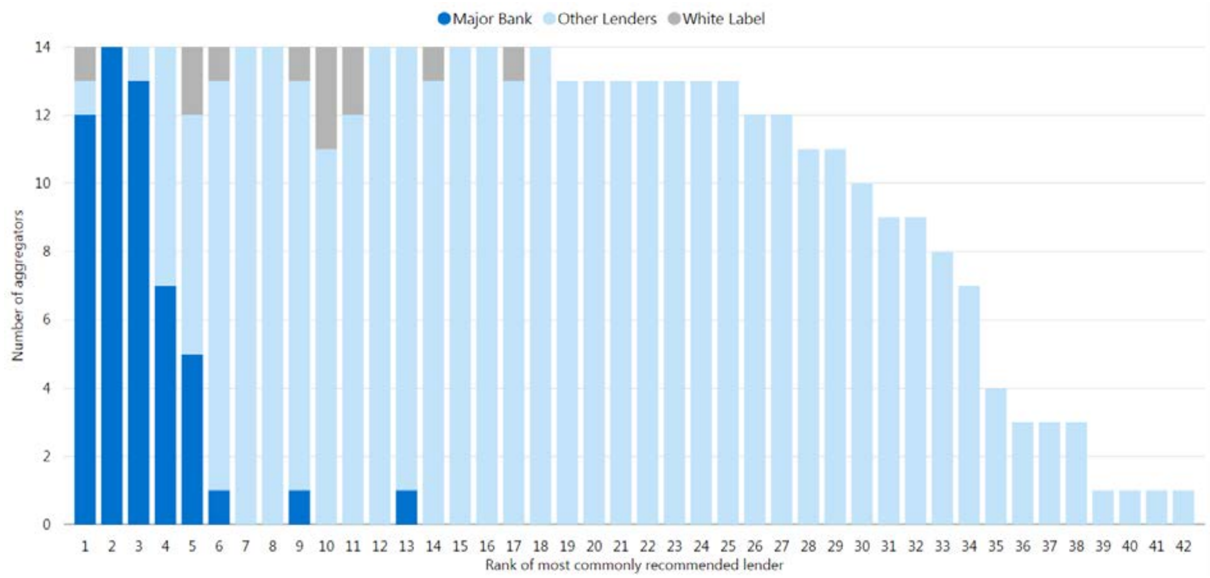
795 On average, in 2015 aggregators sent approximately 22% of loans to their most commonly recommended lender. The second and third lenders received 17% and 12% of loans, respectively. Overall, 80% of loans (by value) were distributed across seven lenders.

Note: In this context, the sub-divisions of major banks count as a separate lender. A white label home loan offered by the aggregator also counts as a separate lender.

796 The lenders that received the most loans from aggregators tended to be major banks. Figure 23 shows the most commonly recommended lenders for the aggregators by type of lender.

Note: We limited the categorisation to major bank, white label and other lenders. This is because we did not categorise the other banks, customer-owned banking institutions and non-bank lenders that did not form part of this review. In this context, a 'major bank' does not include the banks' sub-divisions.

Figure 23: Classification of most commonly recommended lenders used by aggregators/brokers



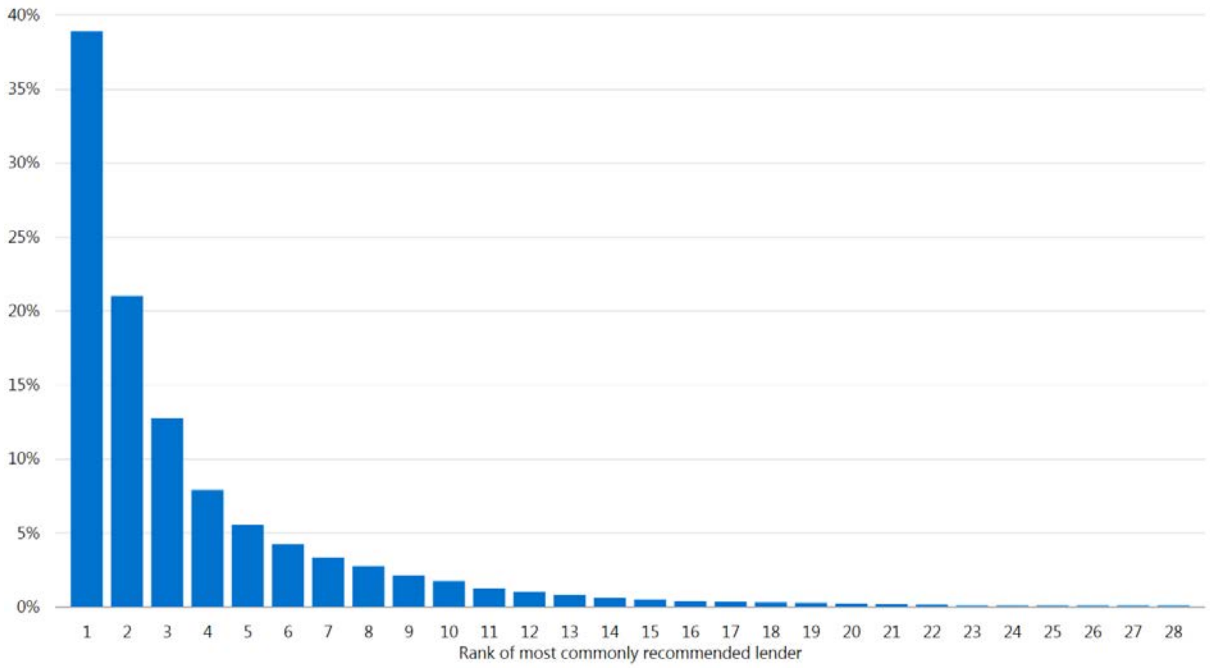
Note: See paragraphs 797–798 for a description of the trends shown in this figure.

797 The most commonly recommended lender for 12 out of 14 aggregators was a major bank. Major banks also accounted for most aggregators' second to fifth most recommended lenders.

798 Interestingly, for one aggregator, the white label home loan offered by that aggregator accounted for more home loans than any lender.

799 The concentration of lenders is even more pronounced for individual broker businesses: see Figure 24.

Figure 24: Proportion of loans sent to broker businesses' most commonly recommended lenders



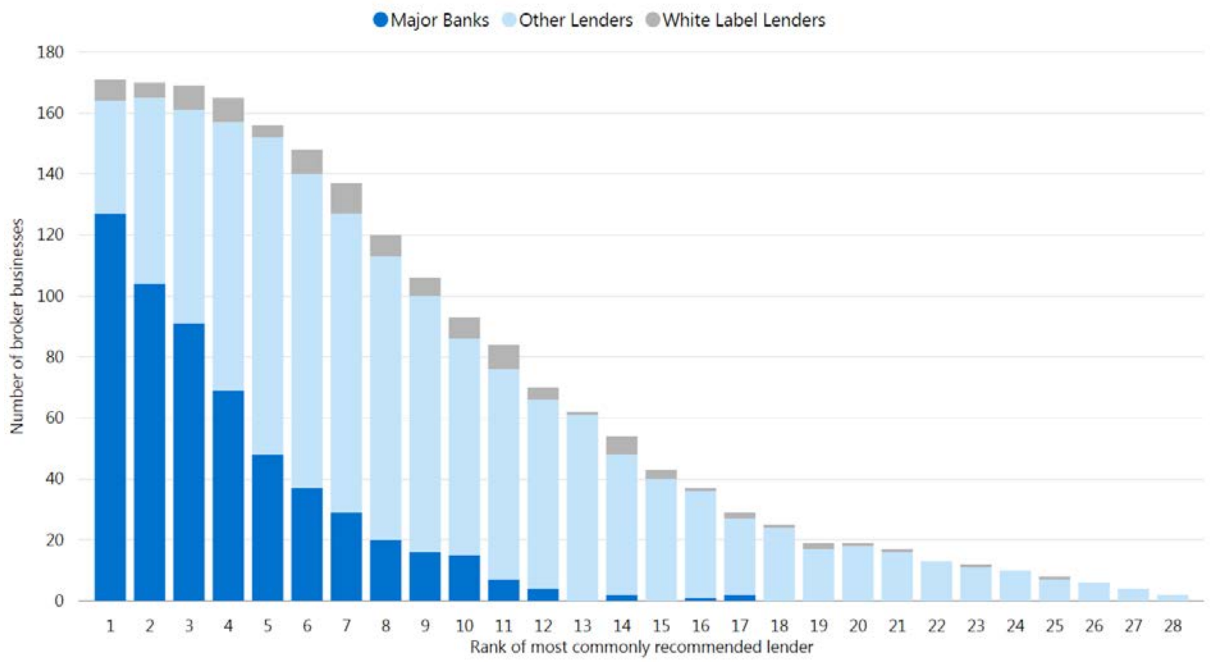
Note: See paragraph 800 for a description of the trends shown in this figure.

800 Broker businesses on average sent almost 40% of loans to their most commonly recommended lender. The second and third lenders received 21% and 13%, respectively. Overall 80% of loans (by value) were distributed across four lenders. These figures are calculated at the broker business level; the concentration at an individual broker level may be higher.

801 This indicates that, while an aggregator may have a large panel of lenders, brokers are more likely to send loans to a small number of lenders.

802 Broker businesses' most commonly recommended lenders tended to be the major banks. Figure 25 shows the most commonly recommended lenders for broker businesses by type of lender.

Figure 25: Most commonly recommended lenders used by broker businesses



Note: See paragraph 792 for a description of the trends shown in this figure.

803 The most commonly recommended lender for 74% of broker businesses was a major bank. Major banks also accounted for 61% of broker businesses' second most and 54% of their third most recommended lenders. White label loans were most commonly recommended by some broker businesses.

Note: Again, in this context, a 'major bank' does not include the banks' sub-divisions.

Value of loans received from owned aggregators

804 Among the participants in this review, there are ownership relationships involving three lenders and nine aggregators. These relationships involve minority, majority and full ownership stakes: see paragraph 291–294.

Note: Macquarie divested its share of AFG in September 2016.

805 We compared the proportion of loans that each owned aggregator sent to the lender that owns it against the proportion of loans that the lender received from all aggregators in our review in 2015: see Table 10.

806 We did this based on the value of loans sold under the lender's own brand (i.e. excluding the aggregator's white label loans, which were funded by the lender) sold through the aggregator and also based on the total value of loans issued and funded by the lender that were sold through the aggregator (i.e. which includes the aggregator's white label loans).

Note: For the purposes of this analysis, we aggregated the value of loans issued by Advantedge with NAB, and those issued by Bankwest with CBA.

Table 10: Comparison of loans provided through owned aggregators

Lender–aggregator relationship	Extent of ownership by lender	Lender's overall market share within the broker channel (% of loans by value)	% of the aggregator's loan flow (by value) sent to the lender (excluding white label loans)	% of the aggregator's loan flow (by value) sent to the lender (including white label loans)
CBA–Aussie	Majority owned	20.9%	22.8%	37.3%
CBA–Mortgage Choice	Minority owned	20.9%	25.1%	25.1% (no white label loans)
Macquarie–AFG	Minority owned	4.8%	5.2%	5.2% (see note
Macquarie-Connective	Minority owned	4.8%	4.0%	4.4% (see note)
Macquarie–Vow	Minority owned	4.8%	3.2%	6.3%
Macquarie–Yellow Brick Road	Minority owned	4.8%	0%	23.4%
NAB–Choice Aggregation Services	Full ownership	13.2%	12.6%	22.6%
NAB–FAST	Full ownership	13.2%	13.7%	21.8%
NAB–PLAN	Full ownership	13.2%	11.9%	22.5%

Note: For Macquarie–AFG and Macquarie–Connective, the volume of white label loans was minimal as Macquarie only began issuing white label loans for these aggregators in late 2015.

807 The proportion of non-white label loans sent by the aggregator to the lender that owns it was generally in line with that lender's overall share of loans issued through all aggregators (although Mortgage Choice sent a slightly higher proportion of loans to CBA than the bank averaged across all aggregators).

808 However, when including the value of white label loans issued by the lender that had an ownership stake in the aggregator, for some combinations the proportion of loans sold through the aggregator that are issued by that lender was significantly greater than the lender's share of the overall value of loans provided through all aggregators.

Note: The business model of some aggregators involves the promotion of their own branded products (i.e. arranged through white label arrangements) in preference to other lenders (e.g. Yellow Brick Road). This may account for a higher proportion of white label loans being sold by that aggregator.

809 This was particularly the case for CBA–Aussie and NAB-owned aggregators.

Note: The proportion of CBA-funded loans being sold by Aussie (37.3%) has increased considerably since 2012. In 2012, 28.7% of loans sold by Aussie were CBA-funded. Interestingly, the increase has been entirely the result of Aussie selling CBA-funded white label loans; the proportion of loans sold by Aussie that are made up of CBA or Bankwest-branded loans dropped from 27.9% in 2012 to 22.8% in 2015.

810 These findings appear to indicate that an ownership stake alone does not result in a higher than average flow of home loans being sent through the aggregator to the lender; rather, a white label arrangement is also important.

811 To test whether a white label arrangement between a lender and aggregator on its own has a similar effect, we compared the same data for each of the other white label arrangements identified by the lenders (i.e. where there was no ownership relationship between the lender and aggregator): see Table 11.

Note: We have again aggregated the value of loans issued by Advantedge with NAB.

Table 11: Comparison of loans provided through aggregators with white label arrangements

Lender– aggregator relationship	Nature of relationship	Lender's overall market share within the broker channel (% of loans by value)	% of the aggregator's loan flow (by value) sent to the lender (excluding white label loans)	% of the aggregator's loan flow (by value) sent to the lender (including white label loans)
Macquarie–Aussie	No ownership	4.8%	3.9%	6.5%
Macquarie–Mortgage Choice	No ownership	4.8 %	2.2%	5.2%
NAB–AFG	No ownership	13.2%	7.7%	11.1%
NAB–Mortgage Choice	No ownership	13.2%	9.0%	9.3%
NAB–Smartline	No ownership	13.2%	6.3%	8.5%
Pepper–AFG	No ownership	0.6%	0.3%	0.6%
Pepper–Vow	No ownership	0.6%	0.5%	N/A

Note: For Pepper–Vow, Vow did not separately identify which Pepper-issued loans were white label loans. For NAB, some of these white label arrangements were new in 2015 and the loan flows may not have reached their potential levels.

812 For NAB and Pepper, where there is a white label arrangement but not an ownership relationship, the loan flow from the aggregator to the lender appeared to be at or below the average flow the lender received from all aggregators in our review. This is in contrast to the loan flow that NAB received from its owned aggregators.

813 It seems that the combination of an ownership relationship with a white label arrangement may result in a higher than average loan flow between related aggregators and lenders compared to all aggregators.

Interest rates through owned aggregators

814 When considering the quality and performance of loans originated through broker channels (see Section F), we examined whether consumers who obtained loans through a broker associated with an owned aggregator were given a higher or lower interest rate than consumers who went through other brokers.

Note: We also examined whether consumers who obtained loans through a broker channel received higher or lower interest rates than those who went directly to the lender (see paragraph 836).

815 There was no clear indication that interest rates obtained through brokers associated with owned aggregators were different to those obtained through other brokers. Overall, while there were some differences, these were typically small (i.e. one or two basis points) and did not show a clear pattern (i.e. some lenders loans were on average slightly cheaper through owned aggregators, while others were slightly more expensive).

F Quality and performance of loans

Key points

This section summarises our findings on the differences in outcomes for consumers according to whether or not they had obtained their loan through the broker channel, or directly from the lender.

Based on a review of approximately 1.4 million loans written by 17 lenders in 2012 and 2015, we found that consumers who used brokers tended to:

- have a larger home loan;
- hold properties of lower value;
- have a higher LVR;
- be more likely to take out interest-only loans; and
- have a higher loan-to-income ratio.

Overview

What we found

816 We undertook a detailed analysis of approximately 1.4 million individual loans provided by 17 lenders in the years 2012 and 2015 to gauge the impact on consumer outcomes from obtaining loans through the broker channel.

Note: We used loans obtained in 2012 and 2015 as the former provided a view of how the loans have performed over time while the latter provided the most up-to-date view of the issue. We were unable to analyse the data of two lenders due to the quality of the data provided.

817 In both 2012 and 2015, we found that consumers who used brokers tended to:

(a) have a larger loan;

(b) hold properties of lower value;

(c) have a higher LVR;

(d) be more likely to take out interest-only loans; and

(e) have a higher loan-to-income ratio.

818 We also found that consumers who borrowed through a broker:

(a) made lower additional payments on their loans (both in dollar terms and as a proportion of the loan amount); and

(b) were more likely to be more than 30 days and more than 90 days in arrears (although this was less prevalent after controlling for borrower and loan characteristics).

819 The data we obtained allowed us to undertake a controlled review in which we could compare the outcomes across both distribution channels for similar consumers with similar loan products. On this basis, differences between the two channels were less marked, as discussed in detail below.

820 Where possible, we also assessed the impact of commissions on consumer outcomes. The results were uneven. For example, there appeared to be a relationship between the level of broker commission and the LVR. However, we did not identify any consistent trends between commissions and other factors such as loan arrears.

Our approach: Comparing 'like with like'

821 By comparing loans obtained through brokers with loans obtained through direct channels, we could identify differences in the loan features and the loan outcomes across the two channels.

822 However, these outcomes were not necessarily caused by the channel and may instead reflect differences in the types of consumers who tended to seek loans through brokers or directly through lenders. As shown below, the basic consumer profile through each channel varied based on factors such as age and income.

823 As a result, when we examined differences in the features of the loans taken out by consumers and the outcomes of those loans across the two channels, it was important to ensure that we compared outcomes for similar consumers.

824 This is reflected in our approach to the data. While we noted some basic differences in loan features between channels, in examining leverage and the proportion of interest-only loans, we also controlled for borrower characteristics in each channel. The result shows that part of the difference in outcomes is driven by these consumer differences.

825 Similarly, for loan performance, we needed to ensure that we compared similar consumers with similar loan products. In examining additional payments and arrears, we controlled for known borrower characteristics and basic features of the loan.

826 Even after applying these controls, there were still differences in loan features and performance between the two channels. Although these differences were observed, we cannot always explain the causes of these differences. Further work (e.g. a shadow shopping exercise or analysis of individual files) may be required to better understand the causes, and to determine whether any regulatory or policy response is required.

827 For the purposes of our analysis in this section:

(a) the term 'raw difference' refers to the difference of the metric being reviewed across all transactions (or on the basis of the raw data);

(b) 'controlling for borrower characteristics' indicates a comparison between broker and non-broker channels, given the same consumer age, income, expenses, employment status, property value, occupation, unemployment rate, marital status, housing status, property purpose, and state or territory; and

(c) 'controlling for loan features' indicates a comparison between broker and non-broker channels, given the same loan type, loan purpose, interest rate discount, number of debtors and loan term.

Data quality

828 The quality of the home loan data and idiosyncrasies across lenders in the way they collected and reported data prevented us from conducting our examination of loan features and performance across the industry as a whole.

829 As a result, modelling with controls was limited to examining differences in loan features and performance between broker and direct channels *within* each lender. Given the number of models required to be constructed to examine relationships within each lender, the analysis of differences with controls has been limited to a selection of nine lenders representing major banks, their sub-divisions and other banks.

Note: In some comparisons we have set out the results for less than nine lenders, as in some cases, there were insufficient transactions for a meaningful analysis to be made or, due to the idiosyncrasies of the lender, the comparison was not appropriate.

Borrower characteristics

830 Non-broker originated loans grew by approximately 14% between 2012 and 2015, while broker-originated loans grew at the considerably stronger rate of 49% (from 253,804 to 378,636). In 2012, broker-originated loans represented around 42% of total loans (by number) and the proportion had gone up to 49% in 2015.

831 In both 2012 and 2015, compared to consumers who obtained loans through lenders' direct channels, consumers who used brokers generally tended to:

(a) be younger;

(b) have a lower income; and

(c) have a full-time job (see Table 12).

Table 12: Borrower characteristics (broker and non-broker)

Mean	Broker (2012)	Non-broker (2012)	Broker (2015)	Non-broker (2015)
Age	39	42	40	42
Income	$105,000	$114,000	$117,000	$123,000
Property value	$585,000	$667,000	$699,000	$780,000
Full-time employment	75%	71%	73%	69%

832 In 2015, relative to those who did not use a broker, a slightly higher proportion of borrowers who used a broker were employed full time (73% compared with 69%), while the proportion was somewhat lower for part-time workers (3.5% compared with 6.6%) and retirees (0.6% compared with 3.1%).

833 As part of our analysis, we collected both internal and external credit scores for consumers from lenders. However, the external scores could not be reliably applied as some lenders did not systematically collect and record them. The internal scores also exhibited significant data issues and were not comparable across lenders.

Loan purposes

834 For loan purposes, the most significant growth between 2012 and 2015 was recorded for ‘Other’ and ‘Refinance’ in broker-originated loans, followed by ‘Construction’: see Table 13.

Table 13: Growth in number of loans between 2012 and 2015 by originator

Loan purpose	Broker	Non-broker
Construction	60.6%	5.4%
Further advance	-16.5%	15.6%
Other	82.3%	23.7%
Purchase (existing dwelling)	33.8%	11.9%
Purchase (new dwelling)	36.3%	34.8%
Purchase (other)	45.9%	8.0%
Refinance	78.9%	19.3%

Loan features

835 Based on the raw data, in both 2012 and 2015, relative to those who borrowed through lenders' direct channels, consumers who used brokers tended to:

(a) have a larger loan;

(b) hold properties of lower value;

(c) be more likely to take out interest-only loans; and

(d) have a higher income-to-loan ratio (see Table 14).

836 We further examined differences between interest rates paid by consumers who used a broker and those who did not. While there were some signs of slightly lower interest rates being paid by consumers who used a broker, these differences were not considered to be statistically significant.

Table 14: Loan characteristics (broker and non-broker)

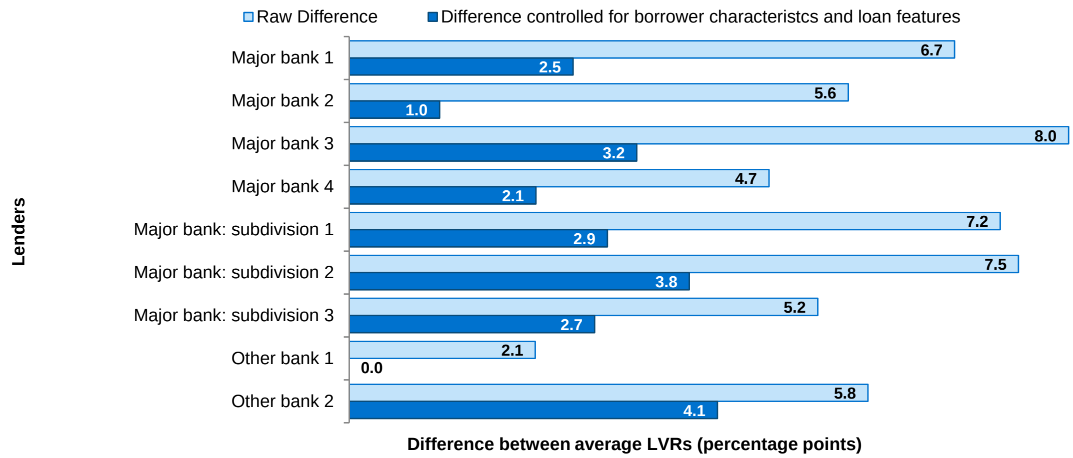
Mean	Broker (2012)	Non-broker (2012)	Broker (2015)	Non-broker (2015)
Loan amount	$381,000	$348,000	$451,000	$420,000
Property value	$585,000	$667,000	$699,000	$780,000
Direct average of LVRs	76%	67%	75%	70%
Interest-only loans (as a percentage of total loans)	23%	12%	29%	17%
Loan-to-income ratio	4	3.5	4.1	3.8

Leverage

837 Compared with those who borrowed through direct channels, consumers who used brokers tended to have greater leverage (indicated by a higher LVR). This is consistent with our previous observations that those who borrow through brokers tend to have a combination of larger loans and lower property values.

838 We found that the raw data indicated that LVRs were between two and eight percentage points higher for loans originating through the broker channel. After controlling for borrower and loan characteristics, the LVRs remained between one and four percentage points higher for loans through broker channels: see Figure 26 and Table 15.

Figure 26: Difference between average LVRs of loans in 2015 (broker and non-broker)



Note: See paragraph 838 for a description of the trends shown in this figure.

Table 15: Difference in average LVRs between broker and non-broker originated loans

Controlling variables	Lowest difference in range (in percentage points)	Highest difference in range (in percentage points)
None	2.1	8.0
Borrower characteristics	1.2	8.9
Borrower characteristics and loan features	0.0	4.1

839 We also analysed the raw data to see the percentage of loans with an LVR of more than 80% across both distribution channels, which is when a borrower is likely to need lender's mortgage insurance (LMI).

840 LMI is an insurance product that protects the interests of the lender if the borrower defaults on the loan. It allows the lender to claim any shortfall in the amount owing under the home loan from the LMI insurer (after the sale of the property) rather than seeking payment of this amount from the borrower. It assists lenders to broaden the pool of consumers to whom they can lend by spreading the financial risk of the borrower defaulting.

841 Based on the raw data, we found a significant difference in the split of loans across the two distribution channels using the LVR value of 80% as a reference. For direct sales, the percentage of all loans with an LVR above 80% was well below 50% for both 2012 and 2015, while over 50% of all loans arranged by brokers in both 2012 and 2015 had an LVR of more than 80%: see Table 16.

Table 16: Percentage of loans with an LVR of more than 80% (by distribution channel)

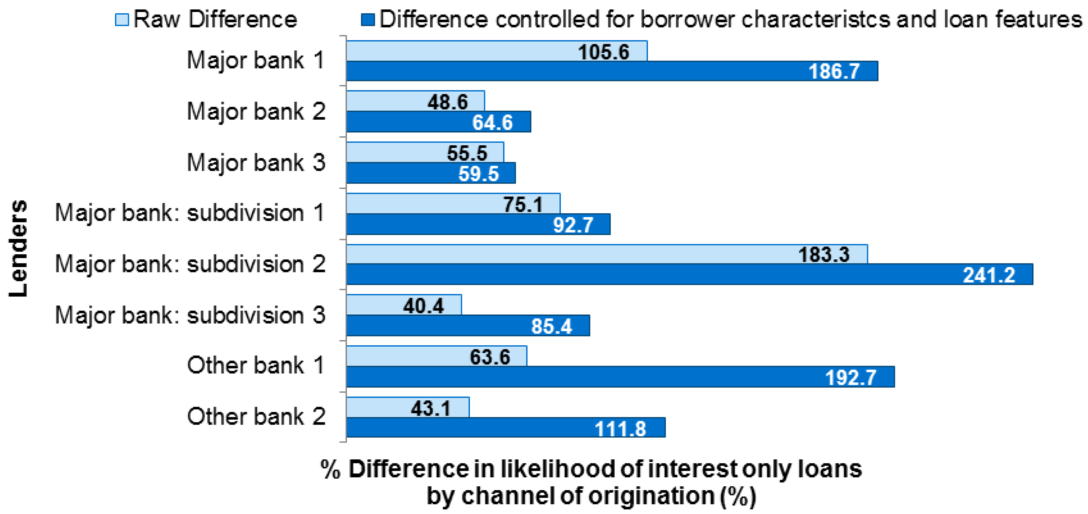
	2012	2015
Direct sales	36.9%	42.8%
Broker channel	55.2%	57.5%

842 There was some evidence of a relationship between the amount of broker commission and LVR. Generally, a higher rate of trail commission appeared to correspond with a higher LVR. There did not appear to be a relationship between upfront commissions and the value of LVR.

Interest-only loans

843 Based on the raw data, for all eight lenders reviewed, interest-only loans were much more likely to have been originated by a broker. This trend was strengthened when results were controlled for borrower characteristics: see Figure 27.

Figure 27: Likelihood of loans being interest-only in 2015 (broker and non-broker)



Note: See paragraph 843 for a description of the trends shown in this figure.

844 Controlling for borrower characteristics and loan features did not mitigate this result, suggesting that these factors have very little correlation with whether the loan is interest only.

845 Lenders who wrote loans on the basis of a ‘full term’ method of calculating repayments (for the purpose of assessing serviceability) were more likely to provide interest-only loans, compared to those who used a ‘residual term’ method.

Note: Under the ‘full term’ method of assessing serviceability, repayments are calculated on a principal-and-interest basis on the full term of the loan. For example, if a consumer applies for a 30-year loan with an interest-only period of 10 years, the assessment is based on principal-and-interest repayments over a 30-year period, even though the principal-and-interest period is only 20 years. Under the 'residual term' method, repayments for the purposes of assessing the consumer's capacity are calculated on a principal-and-interest basis on the residual term of the loan after the interest-only period has expired. For example, if a consumer applies for a 30-year loan with an interest-only period of 10 years, the assessment is based on principal-and-interest repayments over the residual term of 20 years.

846 Following recent work by ASIC and APRA on interest-only loans, we do not expect any lenders to be currently using the full term method.

Length of interest-only period

847 Based on the data available, there was no clear evidence for interest-only loans of a relationship between the length of the interest-only period and the loan channel (broker or non-broker). Results were mixed and depended on the lender (noting that lenders offer different ranges of interest-only periods).

848 Some broker-originated loans were likely to have longer interest-only periods, while other loans originated by non-brokers had longer interest-only periods. In other cases, there was no significant difference between interest-only loan periods for loans originated by brokers and non-brokers.

849 However, lenders who used the full term method of loan assessment were more likely to be linked to loans with longer interest-only periods, compared to those who used the residual term method.

Consumer outcomes and the responsible lending obligations

850 As noted earlier, consumers who used brokers were more likely to:

(a) borrow more money; and

(b) take out an interest-only loan.

851 The consequence of these outcomes is that these consumers are likely to pay more in interest charges. The extent of this difference can be significant, as illustrated by the following comparison between a principal-and-interest loan and a loan with an interest-only period.

852 Assuming the same interest rate, on a 30-year loan of $500,000, the consumer will pay approximately:

(a) $37,000 more under a loan with a five-year interest-only period; and

(b) $80,000 more under a loan with a 10-year interest-only period.

Note: This comparison assumes that the interest-only and principal-and-interest home loans have the same interest rate and term, and that the borrower makes all repayments when due under the contract. Repayment amounts are calculated using the MoneySmart calculator assuming a 6% constant interest rate. It does not take into account the effect of any funds that may be held in an offset account.

853 A loan that may cost the consumer more does not in itself mean the broker has failed to comply with the responsible lending obligations. This will depend on whether the loan met the consumer's requirements and objectives (e.g. there may be other benefits to the consumer that balance the additional interest charges payable) and did not result in the consumer experiencing financial hardship.

854 We have undertaken a recent review of the interest-only home loan market to investigate the level of compliance by brokers in:

(a) identifying consumers' requirements and objectives; and

(b) providing a loan that is suitable.

855 Our findings are set out in Report 493 *Review of interest-only home loans: Mortgage brokers' inquiries into consumers' requirements and objectives* (REP 493) and are based on a review of the responsible lending practices of 11 large Australian mortgage brokers when assisting consumers to apply for interest-only home loans.

856 While we found examples of practices that place brokers at risk of being unable to demonstrate compliance with their responsible lending obligations, about 80% of applications reviewed included a statement explaining how the interest-only feature of the loan met the consumer's underlying requirements and objectives.

Loan performance indicators

Additional payments

857 Based on the raw data, for most lenders in our review, consumers who used a broker made lower additional payments (including redraw and offset account balances) on their loans. This finding was consistent in both 2012 and 2015, measured in dollar terms and as a proportion of the loan amount: see Table 17.

Table 17: Additional payments on loans, including redraw and offset account balances (broker and non-broker)

Mean	Broker (2012)	Non-broker (2012)	Broker (2015)	Non-broker (2015)
Additional payments	$36,000	$43,000	$63,000	$73,000
Additional payments (as a percentage of the loan amount)	8.8%	11.4%	12%	14.4%

Note: Additional payments in dollar figures are higher for 2015 than 2012 due to the higher proportion of offset facilities in 2015.

858 After controlling for borrower characteristics and loan features, the differences in outcomes between the distribution channels become less prevalent. However, for seven out of nine lenders these differences still suggest that loans sold through brokers have lower additional payments: see Table 18.

Note: We have used loans from 2012 in this comparison as any differences in additional payments being made may not yet be evident on loans from 2015.

Table 18: Difference between additional payments on loans from 2012, including redraw and offset account balances (broker and non-broker)

Lender	Raw difference	Difference controlled for borrower characteristics and loan features
Major bank 1	9%	0%
Major bank 2	-8%	-3%
Major bank 3	-34%	-4%
Major bank 4	-31%	-3%
Major bank: subdivision 1	0%	0%
Major bank: subdivision 2	-25%	-2%
Other bank 1	-47%	-6%
Other bank 2	-67%	12%

859 We also tested whether consumers who used a broker made lower additional payments, excluding the balance of the offset account.

Note: A consumer who borrows more money than they initially need may place the additional funds in the offset facility. Those funds would therefore not represent genuine additional payments to the loan.

860 Based on the raw data, for most of the lenders in our review, consumers who used a broker made lower additional payments on their loans when we excluded the offset account balances. This finding was consistent in both 2012 and 2015 (when measured in dollar terms and as a proportion of the loan amount) and was also more pronounced than our finding when the calculation of additional payments included the offset account balance: see Table 19.

Table 19: Additional payments on loans, including redraw balances only (broker and non-broker)

Mean	Broker (2012)	Non-broker (2012)	Broker (2015)	Non-broker (2015)
Additional payments	$15,000	$22,000	$15,000	$30,000
Additional payments (as a percentage of the loan amount)	4%	7%	3%	7%

Note: Additional payments in dollar figures are higher for 2015 than 2012 due to the higher proportion of offset facilities in 2015.

861 After controlling for borrower characteristics and loan features, the differences in outcomes between the distribution channels became less prevalent. However, it was still evident for all lenders and was more pronounced than when the calculation of additional payments included the offset account balance: see Table 20.

Table 20: Difference between additional payments on loans, including redraw balances only (broker and non-broker)

Lender	Raw difference	Difference controlled for borrower characteristics and loan features
Major bank 1	-28%	-6%
Major bank 2	-34%	-13%
Major bank 3	-44%	-12%
Major bank 4	-34%	-6%
Major bank: subdivision 1	-42%	-6%
Major bank: subdivision 2	-45%	-16%
Other bank 1	-61%	-17%
Other bank 2	-59%	-24%

Loan arrears

862 Loans that were obtained through the broker channel were also more likely to have been more than 30 days and more than 90 days in arrears. Again, this becomes less prevalent when controlling for borrower and loan characteristics, although it remains observable in some cases: see Table 21 and Table 22.

Table 21: Difference between 30-day loan arrears, sample entities (broker and non-broker)

Lender	Raw difference	Difference controlled for borrower characteristics and loan features
Major bank 1	44%	21%
Major bank 2	35%	19%
Major bank 3	16%	0%
Major bank 4	23%	10%
Major bank: subdivision 1	11%	0%

Lender	Raw difference	Difference controlled for borrower characteristics and loan features
Major bank: subdivision 2	31%	25%
Other bank 1	68%	20%

Note: The ‘difference in arrears model’ is the percentage difference in the likelihood of broker-originated loans going into arrears compared to non-broker originated loans. Positive values on the table indicate that the chance of a broker-originated loan going into arrears is higher than for a non-broker originated loan.

Table 22: Difference between 90-day loan arrears, sample entities (broker and non-broker)

Lender	Raw difference	Difference controlled for borrower characteristics and loan features
Major bank 1	40%	25%
Major bank 2	43%	24%
Major bank 3	36%	0%
Major bank 4	25%	11%
Major bank: subdivision 1	3%	0%
Major bank: subdivision 2	23%	0%
Other bank 1	79%	0%

863 There does not appear to be any significant relationship between the level of broker commissions (either upfront or trail) and the level of 30-day or 90-day loan arrears.

864 Having controlled for borrower characteristics and loan features, it is evident that a higher loan-to-income ratio results in an increase in the odds of the loan going into arrears. A 10% increase in loan-to-income ratio increases the likelihood by a range of 0–1.3% for 30 days arrears and a range of 0–1.5% for 90 days arrears.

Loan performance and assessment of expenses

865 We also reviewed how brokers assessed a consumer’s living expenses, based on the figures the consumer nominated to the lender. The responses were consistent with concerns that ASIC has previously raised about lenders and brokers not making sufficient inquiries into consumers’ expenses.

866 We found indications that both brokers and lenders’ staff may have failed to make proper inquiries about a consumer’s expenses. It also appears that many lenders may not retain information about consumers’ expenses to allow them to assess whether their processes are working properly.

867 Under the National Credit Act, credit licensees (both lenders and brokers) must comply with responsible lending obligations when arranging or providing home loans. These obligations require licensees to:

(a) make reasonable inquiries about a consumer's financial situation;

(b) take reasonable steps to verify the consumer's financial situation; and

(c) on the basis of these inquiries and steps, offer credit products only when the consumer can meet the repayments without substantial hardship.

868 The Explanatory Memorandum to the National Credit Act discusses the nature of the obligation to make inquiries into the consumer's financial situation in the following terms, at paragraph 3.141:

> Reasonable inquiries about the consumer's financial situation could ordinarily include inquiries about the amount and source of the consumer's income, determining the extent of fixed expenses (such as rent or contracted expenses such as insurance, other credit contracts and associated information) and other variable expenses of the consumer (and drivers of variable expenses such as the number of dependents and the number of vehicles to run, particular or unusual circumstances). The extent of inquiries will however depend on the circumstances.

869 Many lenders test a consumer's nominated expenses against a benchmark such as the Household Expenditure Measure (HEM). Such benchmarks can be used by lenders to verify whether the expense information provided by the consumer is accurate.

870 The HEM benchmark was developed in 2011 by the Melbourne Institute of Applied Economic and Social Research at the University of Melbourne. It represents an estimate of the spending habits of Australian families. As an example, food bought from the supermarket and children's clothes are treated as absolute basics, while a meal at a restaurant or adult clothes are considered discretionary basics.

871 The HEM benchmark uses median expenditure on goods and services with variations according to whether they are characterised as 'absolute basics' or 'discretionary basics'. It takes the median expenditure on absolute basic goods and services and combines this with the 25^{th} percentile of expenditure on discretionary basic goods and services.

872 In simple terms, the use of these percentile figure means that:

(a) 50% of consumers can be expected to have expenditure on 'absolute basic' goods and services that is higher than the HEM benchmark; and

(b) 75% of consumers can be expected to have expenditure on 'discretionary basic' goods and services that is higher than the HEM benchmark.

873 If a lender's assessment of a consumer's expenses was robust and broadly consistent with the methodology underlying HEM, we would expect that most consumers would have expenses higher than the benchmark.

874 As part of the home loan data, we asked lenders to provide details of:

(a) the actual expense amount disclosed by the consumer as recorded by the broker or staff member (disclosed expense amount); and

(b) the benchmark expense amount the lender used to assess whether the disclosed expense amount was accurate.

875 Many lenders could not readily provide us with this data on a systematic basis. This indicates that those lenders may not be in a position to review whether their processes to inquire about, and verify, consumers' expenses are working properly. For example, by not readily having access to this information across the loan portfolio, a lender cannot assess whether the distribution of consumers' disclosed expenses (as recorded by brokers or lenders' staff) reflects the expected distribution of expenses as predicted by the HEM benchmark (which would provide an indication of whether the lenders' processes to inquire about consumers' expenses were working).

876 For home loans from 2015, only eight out of 19 lenders could provide enough data on disclosed and benchmark expense amounts for us to compare the two figures.

877 We found that for a significant number of home loans for each of those lenders, the disclosed expense amount was the same as the benchmark amount used by the lender. This was the case for loans sold through brokers and through the lenders' staff (although loans sold through a broker were slightly more likely to have a disclosed expense amount which was the same as the benchmark).

878 Figure 28–Figure 30 demonstrate the distribution of disclosed expenses as a proportion of the benchmark for three lenders. A ratio less than 1.0 means that the disclosed expense amount was less than the benchmark. A ratio of one indicates that the disclosed amount was exactly the same as the relevant benchmark.

Figure 28: Distribution of disclosed expenses as a proportion of benchmark (Major bank 1)

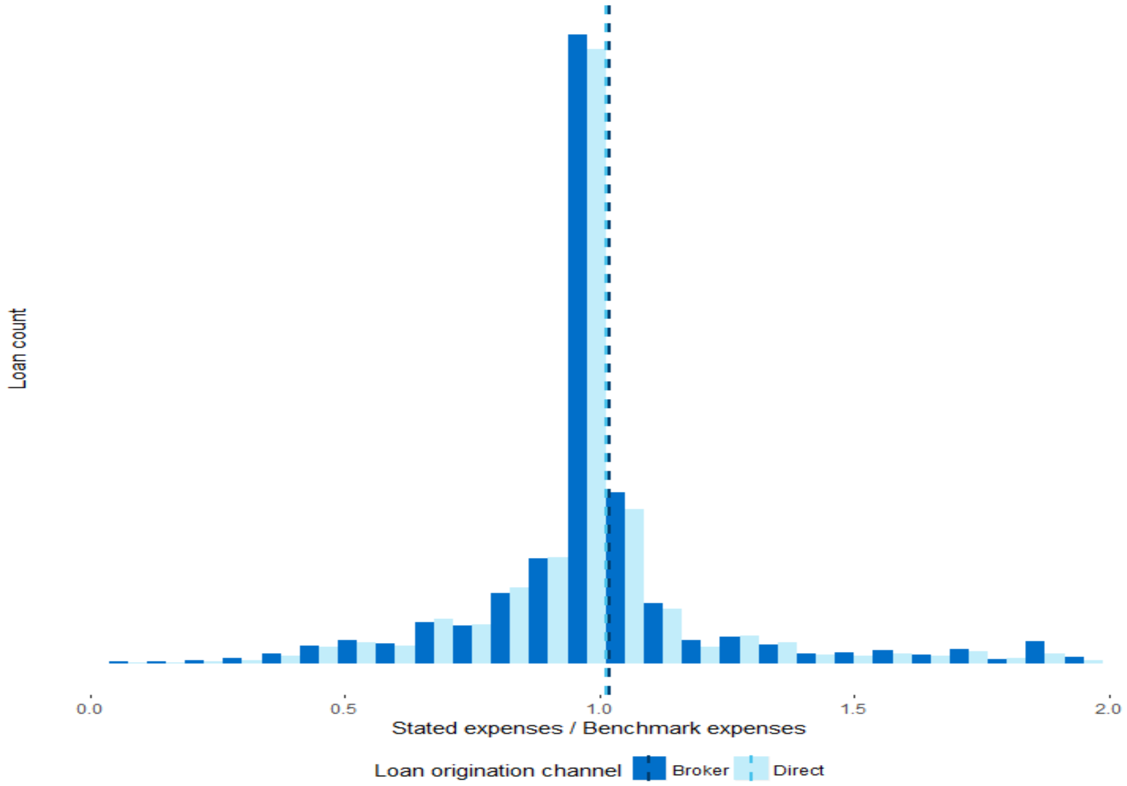


Figure 29: Distribution of disclosed expenses as a proportion of benchmark (Major bank 2)

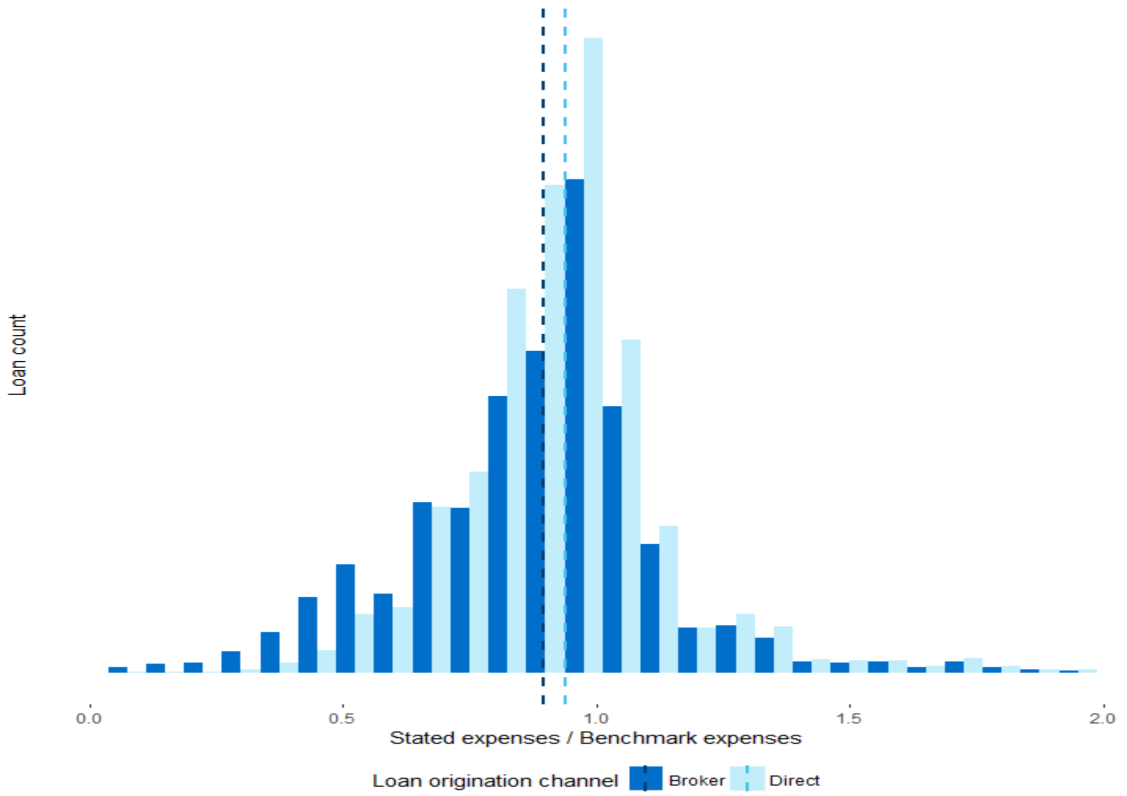
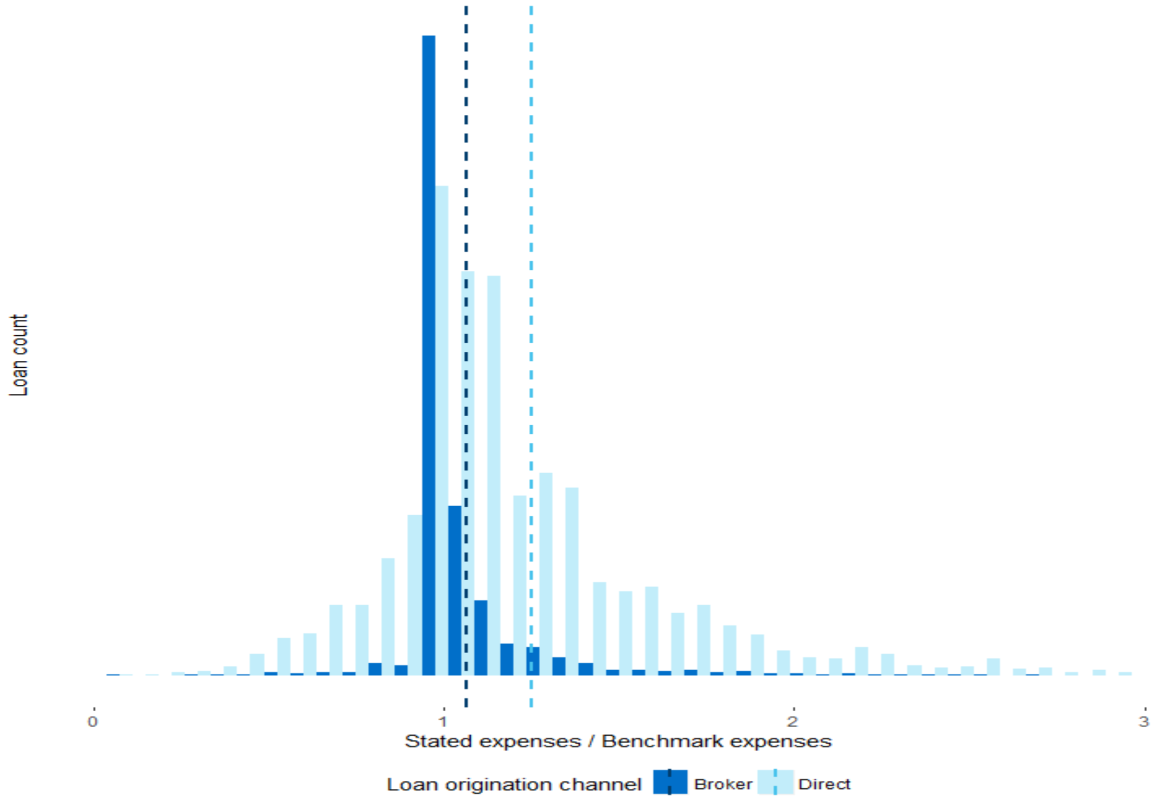


Figure 30: Distribution of disclosed expenses as a proportion of benchmark (Major bank 3)



Note: See paragraphs 879–880 for a description of the trends in Figure 28–Figure 30.

879 In each example, for both broker-originated and non-broker originated loans, there is a large spike of loans at a ratio of one. In two of the examples, the mean value of the ratio is around one or less (in the second example, the mean for broker-originated loans was 0.90 and for lenders' staff 0.94). This was reflected in the data for most of the eight lenders.

880 For the third lender, the mean of the ratio was well above one (one of the few such cases, although this lender also had a significant spike at one). The mean for loans through this lender's staff was 1.24 (compared to a mean for broker-originated loans for this lender of 1.06).

881 These results do not reflect the expected distribution of expenses across a large group of consumers (i.e. as predicted by the HEM benchmark). A lender monitoring the distribution of disclosed expenses would recognise that this indicates that brokers and staff may be submitting home loan applications without genuinely inquiring about consumers' expenses.

882 Our recent review in REP 445 of home loan responsible lending obligations for interest-only loans addressed the way in which benchmarks are used and inquiries about consumer expenses are made. This review has resulted in improvements to industry standards that will not be reflected in these

findings. Since the publication of REP 445, ASIC has been working with lenders to improve inquiries into and verification of consumers' expenses.

883 APRA has also amended its residential mortgage lending standards to provide more detailed guidance on the estimation of living expenses and compliance with responsible lending requirements: see Prudential Practice Guide APG 223 *Residential mortgage lending*.

884 As well as ASIC and APRA's work on improving home lending standards, the industry has been working on an initiative to improve how information about consumers' expenses is collected.

885 We will continue to monitor this issue as part of our ongoing work.

Discounting of home loans: 2012 and 2015

886 We also reviewed whether consumers who took out loans in 2015 were given better interest rates than those who took out loans in 2012. We found that this was the case for most lenders. This comparison was done on a lender-by-lender basis, rather than on the basis of broker and non-brokers loans: see paragraph 836 for our comparison of interest rates on broker and non-broker loans.

887 It is common for home loans in Australia to be priced relative to a 'standard variable rate' (SVR). This is a reference rate: the actual interest rate paid by consumers is equal to the SVR plus or minus a margin. By setting the interest rate on the loan in this way, the lender can adjust the one SVR and the interest rate paid by all borrowers will move in line with that change.

888 As part of the home loan data, we obtained details of the interest rate that applied to each home loan when the loan was opened. Simply comparing the interest rates at the start of the loan from 2015 to those from 2012 will not give a proper indication of whether lenders gave better rates to either of those groups of consumers. Instead, we compared the actual rates to a reference rate to create a discount margin. We then compared the discount margins from 2015 to those from 2012.

Note: We used column K in the Reserve Bank of Australia's Indicator Lending Rates—F5 (Excel file, 195 KB).

889 Across all but one of the banks, the discount margin for loans in 2015 was greater than that in 2012: see Table 23.

Table 23: Additional discount margin for loans from 2015 compared to 2012

Lender	All loans	Loans less than $500,000	Loans greater than $500,000
Major bank 1	0.28	0.26	0.27
Major bank 2	0.11	0.08	0.12
Major bank 3	0.09	0.06	0.11
Major bank 4	0.26	0.26	0.22
Major bank: subdivision 1	-0.03	-0.04	-0.02
Major bank: sub-division 2	0.26	0.25	0.22
Major bank: sub-division 3	0.27	0.24	0.33
Other bank 1	0.21	0.19	0.22
Other bank 2	0.32	0.33	0.26
Other bank 3	0.31	0.28	0.35

G Consumers' experiences with loans

Key points

As part of our review, we undertook quantitative research through a series of omnibus surveys to better understand consumers' perceptions of brokers, including their high-level views of the value offered by brokers.

Consumers told us that they have multiple reasons for using a broker. Brokers need to identify and consider those reasons and, if they conflict, help the consumer to decide which are more important.

Some consumers demonstrated a level of confusion about how brokers are paid, with a substantial proportion mistakenly believing that brokers are paid the same amount regardless of which loan is taken out.

Disclosure under the National Credit Act may not give consumers information about all benefits that are payable to brokers, or information about ownership relationships between the lender and the aggregator or broker.

Overview

890 In our review of mortgage broker remuneration, we focused on arrangements between lenders, aggregators, brokers and other industry participants in the value distribution chain. In particular, we sought to understand what incentives are paid to whom, and how this affects consumer outcomes as demonstrated through specific home loans and overall loan flow data.

891 To provide some relevant context for our review, we also sought to better understand consumers' perceptions of brokers, including their high-level views on the value proposition offered by brokers.

892 We undertook quantitative research by surveying a representative sample of the Australian adult population through a series of online omnibus surveys conducted by Galaxy Research. We asked participants up to seven questions, depending on their level of experience using brokers. For a detailed explanation of the survey methodology, see Appendix 1.

893 We found that consumers use a broker for a variety of reasons, including both convenience and price. Consumers may also be looking for multiple, potentially conflicting, features in a home loan. Brokers must identify and consider what consumers are looking for and, if there are conflicting needs, help them decide which factors are most important. Brokers need to keep a record of this process so that they can demonstrate how they have complied with their responsible lending obligations.

894 There is also a level of uncertainty about the role of brokers (e.g. whether they are acting in consumers' interests) and whether brokers get paid different amounts depending on the loan they assist consumers to obtain.

895 There are various requirements for details of commissions and bonus payments payable to brokers and aggregators to be disclosed to consumers. Bonus payments made to lenders' staff do not need to be disclosed to consumers.

896 There is no requirement that brokers or aggregators disclose whether they are owned by a lender.

Consumers' perceptions of mortgage brokers

What we did

897 We engaged Galaxy Research to ask a small series of questions in three of their fortnightly online omnibus surveys in September and October 2016. Each survey included 1,000 Australian adult participants, with 3,000 participants in total, although not all participants answered all questions.

898 Our analysis generally focused on two key subgroups:

(a) 1,000 research participants who were representative of general consumers (general consumers); and

(b) 490 research participants who had used a broker to obtain a home loan in the last two years and/or intended to use a broker in the next 12 months (consumers with recent experience/future intention to use a broker).

899 Further explanation of the survey methodology, see Appendix 1.

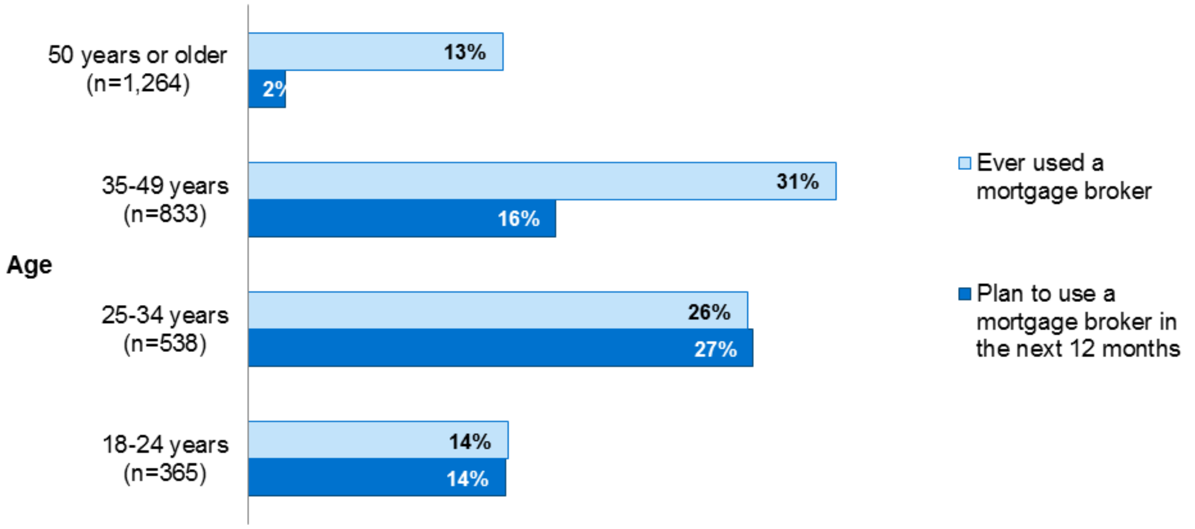
Consumers' use of brokers

900 Overall, the research indicated that 32% of all 3,000 consumers who participated in the omnibus surveys had never had a home loan, while 51% had obtained a home loan directly from a bank or other lender and 21% through a broker. Few consumers had obtained a home loan both directly and using a broker (the cross-over was only 4% of all respondents).

901 Around 75% of consumers aged 35–49 years and 50 years or older had obtained a home loan before (73% and 79%, respectively), with lower proportions of consumers having obtained a home loan before in the age brackets 18–24 years (34%) and 25–34 years (57%).

902 Figure 31 shows the proportion of consumers in each age bracket who had ever used a broker and who intended to do so within the next year.

Figure 31: Previous experience and future intention to use mortgage brokers, by age group



Questions: 'If you have ever had (or refinanced) a home loan how did you do this?' (multiple response question) and 'In the next 12 months, do you expect to use a mortgage broker to obtain (or refinance) a home loan?' (single response question).

Base: All respondents (n=3000).

Note 1: See paragraph 903 for a description of the trends shown in this figure.

Note 2: Data is weighted by age, gender and location.

903 In summary:

(a) Consumers aged 50 years or older (13%) and 18–24 years (14%) were least likely to have used a mortgage broker before. This figure was notably higher for consumers aged 35–49 years (31%) and, to a lesser extent, 25–34 years (26%).

(b) Overall, 12% of all consumers surveyed said they intended to use a broker in the next 12 months. The figure was higher for consumers aged 25–34 years (27%) and far lower for those aged 50 years or older (2%).

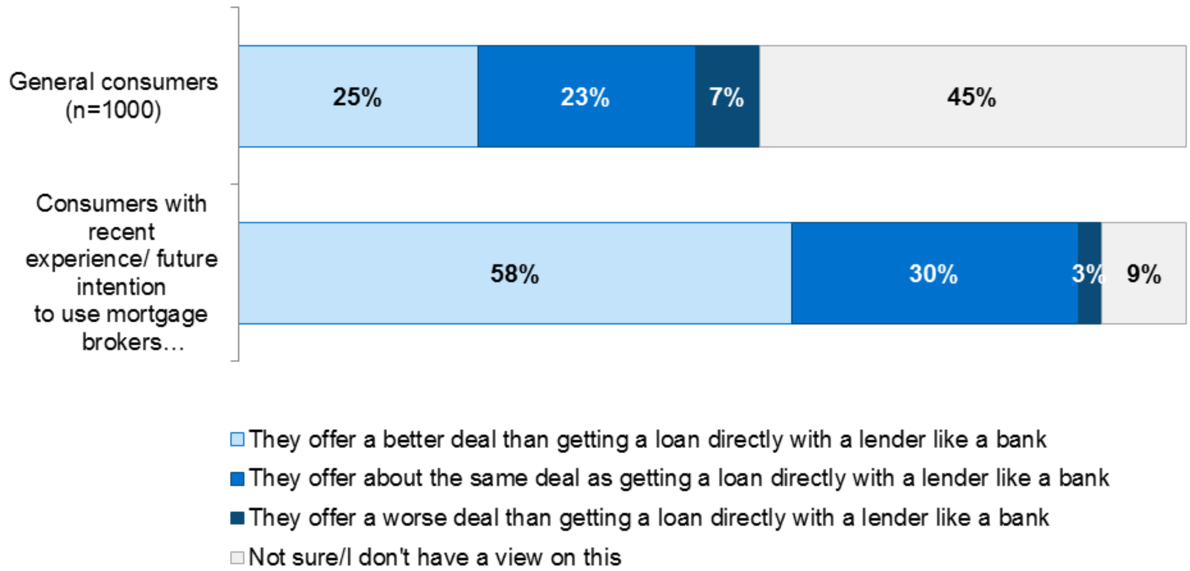
Overall impression of brokers

904 We asked the two subgroups of survey participants, 1,000 general consumers and 490 consumers with recent experience/future intention to use a broker, about their overall impression of the deal offered by brokers and how this compared with their impression of obtaining a home loan directly from a lender.

905 As shown in Figure 32, consumers with recent experience/future intention to use a broker (58%) were much more likely than general consumers (25%) to consider that brokers offered a better deal. Very few consumers with recent experience/future intentions thought that brokers offered a worse deal (3%, compared to 7% of general consumers).

906 General consumers were far more likely to feel unsure about whether brokers offered a better, the same or worse deal (45%, compared to 9% of those with recent experience/future intentions).

Figure 32: Overall impression of mortgage brokers



Question: Which of the following best matches your overall impression of mortgage brokers? (single response)

Base: General consumers (n=1000) and consumers with recent experience/future intention to use mortgage brokers (n=490).

Note 1: See paragraphs 905–906 for a description of the trends shown in this figure.

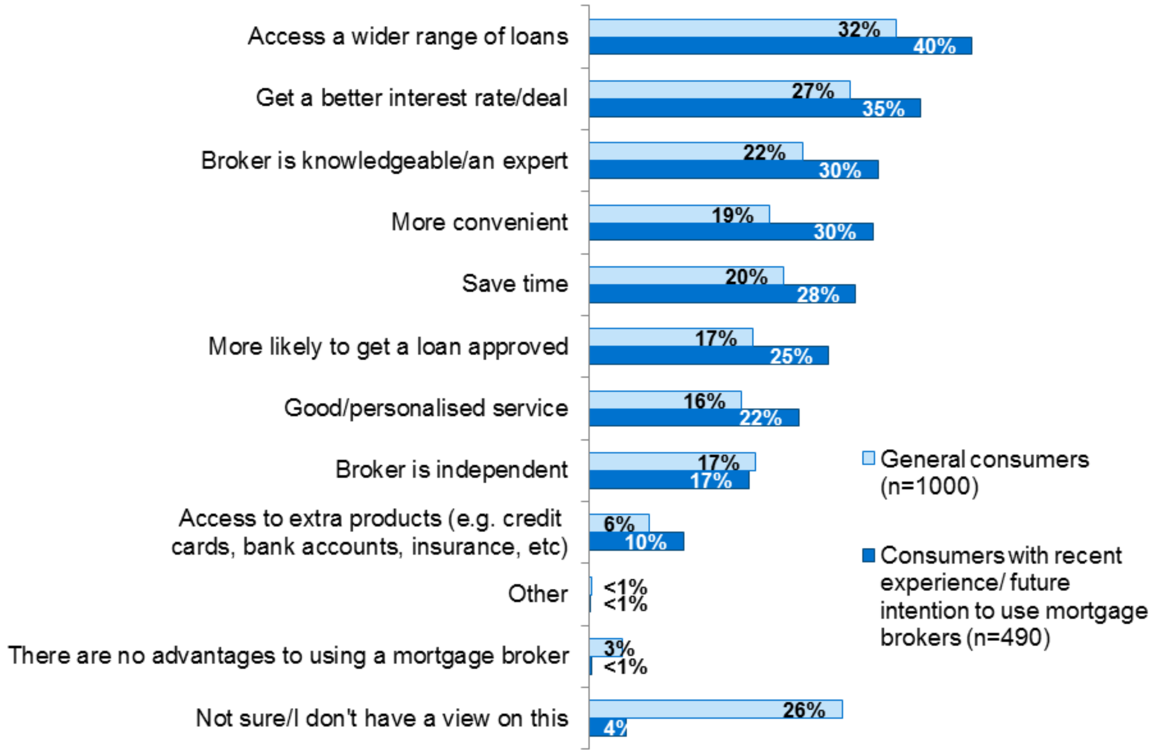
Note 2: Data is weighted by age, gender and location.

Main reasons consumers use brokers

907 We asked respondents from each of the subgroups to indicate up to three main reasons why people might use a broker. As shown in Figure 33, the most common reasons cited by those with recent experience/future intention to use a broker were to access a wider range of loans (40%) or to get a better interest rate or deal (35%), although a sizable share of respondents selected alternative reasons.

908 Accessing a wider range of loans and getting a better interest rate or deal were also the factors most commonly selected by general consumers (32% and 27%, respectively). However, general consumers were typically less likely to nominate reasons why people might use a broker and more likely to indicate that they were unsure (26%, compared to 4% of those with recent experience/future intention).

Figure 33: Main reasons why people use a mortgage broker (up to three options selected)



Question: If you have a view, what do you think are the main reasons why people might use a mortgage broker? Please select up to three options. (Multiple response)

Base: General consumers (n=1000) and consumers with recent experience/future intention to use mortgage brokers (n=490).

Note 1: See paragraphs 907–908 for a description of the trends shown in this figure.

Note 2: Data is weighted by age, gender and location.

909 Figure 33 suggests a wide variety of reasons consumers use a broker. Further analysis of the results indicates that a clear majority of consumers with recent experience/future intention to use a mortgage broker (74%) selected multiple reasons for doing so. This suggests that many consumers are likely to have more than one objective or requirement when using a broker.

910 Many of the reasons cited are based on convenience (e.g. save time, more convenient, more likely to get a loan approved, good/ personalised service) while other reasons are more focused on price (e.g. getting a better interest rate/deal). Other reasons may cover both convenience and price (e.g. access to a wider range of loans).

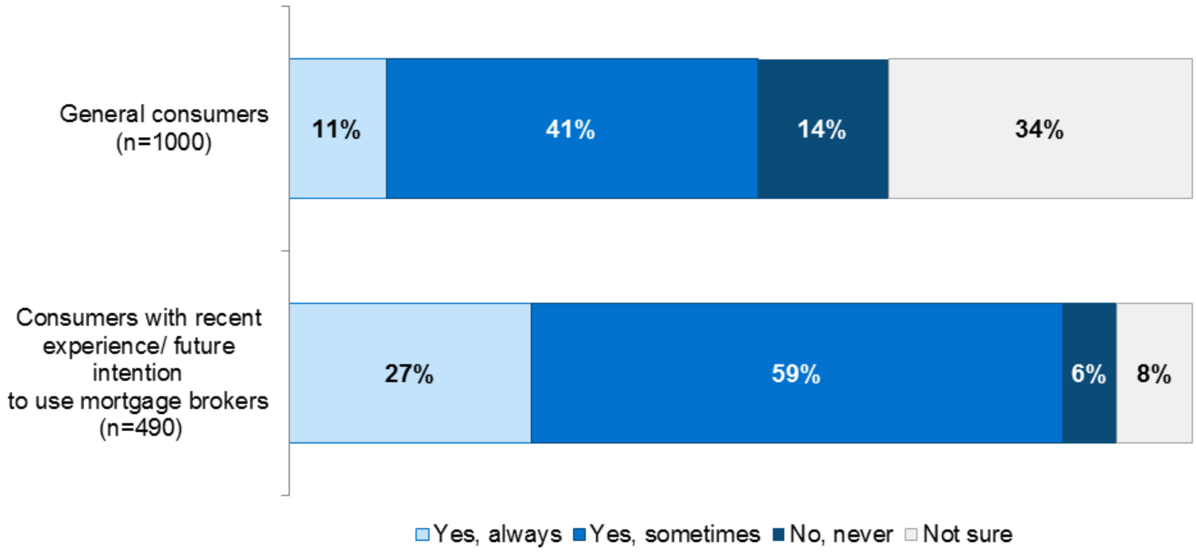
911 The survey results indicated that many consumers gave multiple reasons for using a broker that spanned both convenience- and price-related factors. For example, respondents with recent experience/future intention to use mortgage brokers who nominated ‘saving time’ as one of the main reasons people might use a broker usually selected as their next responses ‘more convenient’ (40%), ‘access a wider range of loans’ (35%) and ‘get a better interest rate/deal’ (28%).

Whether brokers put consumers' needs first

912 We asked respondents from the subgroups whether they thought brokers put consumers' needs first. As shown in Figure 34, for consumers with recent experience/future intention to use brokers, the majority (86%) considered that brokers would put consumers' needs first, at least to some extent. Most (59%) felt that brokers would 'sometimes' put consumers' needs first, while 27% felt they would 'always' do so.

913 In contrast, general consumers were much more likely to indicate they were unsure (34%) and only around half (52%) felt that brokers would put consumers' needs first, at least to some extent. 11% of general consumers thought brokers would 'always' do so and 41% indicated they would 'sometimes' do so.

Figure 34: Whether mortgage brokers put customers' needs first



Question: Do you think a mortgage broker would put your needs first? (Single response)

Base: General consumers (n=1000) and consumers with recent experience/future intention to use mortgage brokers (n=490).

Note 1: See paragraphs 912–913 for a description of the trends shown in this figure.

Note 2: Data is weighted by age, gender and location.

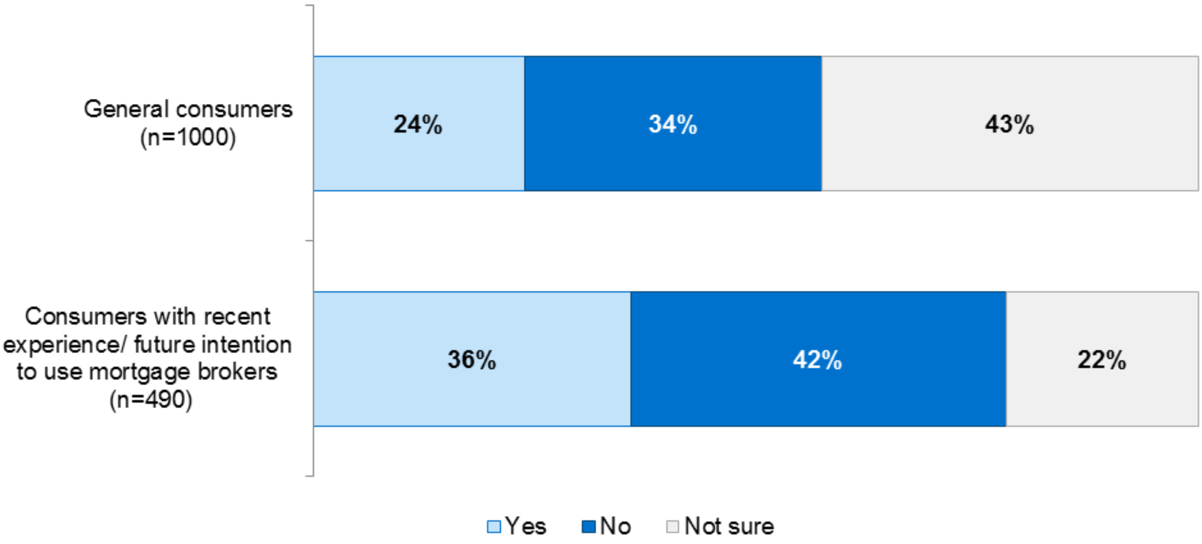
How brokers are paid

914 We asked respondents from the subgroups for their views about whether brokers get paid the same regardless of the loan they assist consumers to obtain. The responses as shown in Figure 35 suggest that many consumers may be unclear or confused about how brokers get paid.

915 Consumers with recent experience/future intention to use a broker most commonly indicated that brokers do *not* get paid the same regardless of the loan (42%). However, almost as many (36%) held the mistaken belief that brokers get paid the same regardless of the loan. A sizable portion (22%) indicated they were unsure.

916 General consumers were more likely to indicate they were unsure (43%), while around one-third (34%) thought that brokers do *not* get paid the same regardless of the loan and 24% thought they do get paid the same.

Figure 35: Whether mortgage brokers get paid the same regardless of the loan



Question: Do you think a mortgage broker gets paid the same regardless of which loan you take out? (Single response)

Base: General consumers (n=1000) and consumers with recent experience/future intention to use mortgage brokers (n=490).

Note 1: See paragraphs 914–916 for a description of the trends shown in this figure.

Note 2: Data is weighted by age, gender and location.

917 While consumers with recent experience/future intention to use mortgage brokers were more likely to hold a view on this topic (i.e. fewer 'not sure' responses), they were also more likely than general consumers to hold the mistaken belief that brokers are paid the same regardless of the loan.

918 Relevantly, the law requires that brokers disclose their actual remuneration after consumers have selected the loan they want to apply for. They would therefore be unaware of what the broker would be paid for arranging other loans, unless they specifically inquired about this.

Impact on disclosure of different business models

Loan distributed directly by the lender using branch staff

919 The only disclosure document provided to consumers by lenders that contains information about commissions likely to be paid by the lender is its pre-contractual statement. This is given late in the process of applying for a loan—at or before the time the offer of a loan made to the consumer.

Note: See s16 and 17(14) of the National Credit Code.

920 This statement needs to include details of commissions paid by the credit provider for the introduction of credit business (e.g. real estate agents or accountants). However, this does not include any commissions or bonus payments paid to employees of the credit provider. While employees may be paid a range of volume-based incentives that could influence the way the consumer proceeds with their loan application, there will be no information provided to the consumer about these incentives. Employees of the lender do not have any of their own disclosure obligations (unlike credit representatives).

Note: The kinds of commissions that may be disclosed in the pre-contractual statement include referral fees payable to comparison sites (in some circumstances) or other referrers, and commissions payable to aggregators that introduce credit business. The statement needs to include details of who will pay and who will receive the commission, and the amount, if it is ascertainable at the time the statement is given: see s17(14) of the National Credit Code.

Loan distributed using a broker and aggregator

921 As credit licensees or credit representatives that provide credit assistance to consumers, aggregators and brokers are required to give their own disclosure documents which include information about commissions they are likely to receive. These disclosure obligations are broadly outlined in Section A.

922 A consumer dealing with a broker will receive the following information:

(a) *General information about the different kinds of commissions the broker is likely to receive*—For example, the consumer will generally be informed at an early stage, in a credit guide, that the broker receives both upfront and trail commissions within a particular rate range directly or indirectly from the lenders with whom they arrange loans.

(b) *More detailed information about each commission*—In the proposal document, the consumer will be given information about each kind of commission the broker is likely to receive for the particular loan that the consumer chooses. This information needs to be provided in a way that enables the consumer to understand what each kind of commission is, the estimated dollar value of each kind of commission and who pays it. This more detailed information will include commissions paid by persons other than the lender, such as commissions paid by the aggregator.

Note: For the disclosure obligations in Ch 3, a 'commission' includes any financial or other benefit in the nature of a commission: see s5 of the National Credit Code.

(c) *Information about any volume bonus arrangements the broker has (whether with a lender or another person, such as an aggregator)*—For example, the consumer will be informed in the credit guide that there are volume-based arrangements in place and who those arrangements are with. If a volume-based arrangement may affect the amount of commission received in relation to the particular loan being proposed, the proposal document will need to state the maximum amount that the broker could receive as a result of that arrangement.

Note: See reg 26A (for a licensee's credit guide), reg 27A (for a credit representative's credit guide) and reg 28G (for the proposal document).

(d) *Information about the broker's lenders*—The consumer will be given the names of the six lenders with whom the broker arranges the most business.

923 However, in some cases the consumer may not receive any information about benefits that may be received by the broker because they are not considered by the broker to be 'in the nature of a commission'. For example, in some cases membership to a broker club may not be considered by the broker to be a commission, although it may involve the broker being rewarded for sending more loans to that particular lender. See Section C for information on broker clubs.

924 The consumer may also not receive clear information about volume-based arrangements under which the broker is penalised for lower volumes, rather than receiving additional commission for higher volumes of business.

925 The consumer will not necessarily receive detailed information about the kinds of commissions that are paid by lenders to the aggregator. If the aggregator is providing credit services by 'acting as an intermediary' rather than providing credit assistance (which may be the case if the broker holds their own credit licence), the aggregator does not have to give its own disclosure documents. This might mean that the consumer is not made aware of some kinds of commissions that could indirectly influence the service ultimately provided by the broker (e.g. volume-based arrangements that affect the commissions or other benefits paid by a lender to the aggregator but which are not necessarily passed on to the broker in the same form).

926 If the broker acts as a credit representative of the aggregator, the aggregator will be providing credit assistance and have its own disclosure obligations. In this case, the detailed information in the proposal document must cover each kind of commission received by either the aggregator as the licensee or the broker as the credit representative, and so may provide a more complete picture of the commissions that may affect the service provided.

927 There is no requirement that brokers or aggregators disclose whether they are partially or wholly owned (either directly or indirectly) by a lender.

928 For white label loans branded as the broker or aggregator's loans, consumers will get information on who the actual credit provider is in various documents including the loan contract. Nonetheless, we suspect that consumers may not understand what a white label home loan is, who the credit provider is and what links there are between the credit provider and the broker or aggregator.

Commissions paid to referrers

929 The consumer will also receive information about commissions that are paid to other persons that refer them to a broker or lender for the purpose of obtaining a loan. This information may be provided to the consumer in the following ways:

(a) *By the referrer*—If the referrer relies on the licence exemption for referrers, they must disclose to the consumer any benefits, including commission, they or an associate may receive for the referral. This information needs to be provided at the same time and in the same form as the referral. For example, if the referral is through a website, the commission information must be contained on the website; if the referral is made during a conversation, the commission information must be provided during that conversation.

Note 1: See reg 25.

Note 2: If the referrer is a licensee or credit representative that is providing a credit service by 'acting as an intermediary', they will not have any obligation to disclose information about how they are paid.

(b) *By the lender* (if the referral is to a lender)—The pre-contractual statement will include this information, though it may only include the amount of the commission if it is ascertainable at the time the statement is given. For example, flat fees that are payable on a successful referral will generally be ascertainable and disclosed. Commissions that are conditional on other factors, such as the volume of successful referrals within a specified period, may not be ascertainable at the time of the statement, and so the amount may not be included (although the fact that the commission is payable and who pays and who receives it must still be disclosed).

Note: See s16 and 17 of the National Credit Code.

(c) *By the broker* (if the referral is to a broker)—The broker's credit guide (either as a licensee or as a credit representative) will include information about the kinds of third party (e.g. real estate agents) that the broker pays commission to and a statement that the consumer can request a reasonable estimate of the amount and how the commission is worked out. The proposal document must also state if commission is likely to be paid by the licensee to a third party on the credit contract being proposed and, if so, who pays and who receives the commission, and the amount if known or a reasonable estimate.

Note: See reg 26A (for the licensee's credit guide), reg 27A (for the credit representative's credit guide) and reg 28G (for the credit proposal). The amount of commission, or a reasonable estimate, does not need to be included if it is contingent on conduct of other consumers who may be referred, but the proposal must still contain information about factors contributing to the amount of commission payable by the consumer: see reg 28G(7).

H Governance and oversight

Key points

When designing and reviewing remuneration and governance structures, lenders, aggregators and broker businesses do not focus sufficiently on the conduct of brokers or lenders' staff, or on the quality of consumer outcomes.

This was particularly exhibited through a lack of consistent governance structures to incorporate a consumer focus in the design of incentive schemes and to identify specific features of incentives scheme that may increase the risk of mis-selling of home loans.

Where misconduct or poor practices were identified, benefits received from that misconduct did not seem to be clawed back.

Overview

930 We asked lenders, aggregators and broker businesses a number of questions about their governance and oversight arrangements, which we consider are indicators of an entity's culture. For example, responses to these questions could indicate that consumer outcomes play a central role, or that an entity's culture focuses on achieving sales, through their incentive and remuneration structures, at the expense of consumer outcomes.

931 Responses generally indicated that many of the factors that ASIC considers are important indicators of culture are not adequately addressed by lenders, aggregators and broker businesses. Although entities may seek to address their culture in other ways, we have highlighted potential risks to entities by not taking the steps discussed in this section.

932 We also did not identify a clear focus on ensuring good sales conduct and positive consumer outcomes either in the design or review of remuneration structures or in monitoring the conduct of brokers or lenders' staff.

933 For lenders this appeared to be the case for both their own employees and even more so for third-party channels (i.e. aggregators and broker businesses). Lenders' oversight of aggregators and broker businesses tended to focus on a portfolio view of negative loan performance (e.g. arrears and defaults) or other circumstances that may result in commission clawback (such as early termination of loans). However, this oversight did not seem to be intended to drive good sales conduct or positive consumer outcomes.

934 Further, broker businesses did not appear to be set up to assess whether remuneration structures resulted in positive outcomes. These businesses generally did not have the authority to influence remuneration structures, which were usually designed by lenders and aggregators.

935 In particular, where misconduct or poor practices were identified, benefits received from that misconduct did not seem to be clawed back. We consider that measures such as clawback of commissions provide a powerful incentive to focus on good sales conduct and positive consumer outcomes.

Design and approval of remuneration structures

936 Rewards and incentives play a significant role in driving conduct by:

(a) affecting the priorities of brokers and lenders' staff, which in turn affects an entity's culture; and

(b) encouraging and reinforcing particular conduct.

937 Rewards and incentives also have the potential to create conflicts of interest. Examples include rewarding strategies that focus on short-term sales targets or providing incentives (including soft dollar benefits) to promote particular products, particular attributes of products (e.g. larger loans) or products of a particular lender.

938 Such incentives may encourage brokers and lenders' staff to promote particular products even if they are less suitable for the consumer.

939 We consider that an appropriately designed and transparent remuneration structure is likely to:

(a) facilitate more rigorous scrutiny by consumers, auditors and regulators; and

(b) reduce the risk of conflicts of interest arising that lead to poor consumer outcomes.

Person(s) responsible for designing and approving remuneration structures

940 We asked lenders, aggregators and broker businesses about the person(s) responsible for designing and approving home loan remuneration structures (including ad hoc incentives such as campaigns or competitions). In particular, we asked about their roles and how they were remunerated (e.g. based on the business or the individual meeting certain sales thresholds).

Business role of person(s) responsible

941 Responsibility for the design of remuneration structures varied across lenders, aggregators and brokers. Generally, those responsible ('designers') were middle or senior level business executives (e.g. Head/General Manager of Sales and Distribution, Head of Mobile Lending).

942 Notably, we identified that designer(s) within:

(a) aggregators and broker businesses tended to be employed at a more senior level than designers within lenders; and

(b) lenders tended to vary between distribution channels (i.e. different designers existed for direct and third-party distribution).

943 Similarly, responsibility for approving remuneration structures ('approvers') varied significantly. Generally, the person(s) responsible for approval were very senior executives (or committees comprised of senior executives), including in some instances the board and chief executive officer.

944 As with the designers, we identified that the approver(s) within lenders tended to vary by distribution channels (i.e. different approvers exist for direct and third-party distribution).

945 There was limited information to suggest that independent critical functions within the businesses (e.g. legal, risk, compliance and assurance functions) held a significant role in the design and approval of remuneration structures.

Remuneration of person(s) responsible

946 Lenders, aggregators and broker businesses generally remunerated the person(s) responsible for designing and approving remuneration structures through a combination of base salary and short-term and long-term incentives. In limited circumstances, this may include business profits, dividends or equity shares. The incentives, at least in part, are typically based on the business unit achieving certain sales targets.

Processes for designing, reviewing and amending remuneration structures

Incorporating organisational values and consumer outcomes in remuneration structure design

947 We asked lenders, aggregators and broker businesses about the values and principles that underpin their processes for designing, reviewing and approving remuneration structures.

948 Responses indicated that organisational values are considered by most lenders and aggregators in the design process for home loan remuneration structures, typically when designing balanced scorecards and performance

review processes. Broker businesses largely responded that such values are not considered, noting that broker businesses do not typically have the authority to design the remuneration structures that apply to their businesses.

949 Most lenders and aggregators reported that they incorporate a consumer outcomes focus in their design of remuneration structures. We observed significant variation in the nature and degree of this focus:

(a) some entities comply with minimum legislative requirements only, while others go beyond this and develop policies and procedures to encourage better consumer outcomes; and

(b) some entities explicitly incorporate consumer outcomes elements into balanced scorecards or more generally into values assessments.

950 However, it was not apparent that lenders considered or applied a consumer outcomes focus for broker businesses, noting that these businesses and the brokers who operate under the business were not assessed under lenders' balanced scorecards.

951 If lenders and aggregators do not include consumer outcomes considerations in their design of remuneration structures, there is an increased risk that sales incentives will override consumer outcomes.

Reviewing and amending remuneration structures

952 We found significant inconsistency across lenders, aggregators and broker businesses in the level of activities undertaken to proactively:

(a) identify specific features of incentive schemes that might increase the risk of mis-selling of home loans by brokers and lenders' staff; and

(b) implement controls to adequately mitigate increased risk.

953 Just over 50% of lenders and aggregators reported that they had such review practices, with controls implemented largely via balanced scorecards or performance review processes. Responses indicated that:

(a) these measures were slightly more prevalent for their own staff than for third-party channels; and

(b) no broker businesses reported that management undertook such activities.

954 Lenders and aggregators reported significant variations in the frequency of their reviews and amendments to remuneration structures. Some reported ad hoc reviews or reviews only in response to market or regulatory conditions, with others undertaking more structured periodic reviews.

955 Infrequent reviews of remuneration structures may increase the risk that such remuneration structures will become unsuitable over time (e.g. where there are product, market and regulatory changes).

956 Around 50% of responses indicated that reviews included a focus on the fair treatment of consumers. Some entities reported that they did this by explicitly incorporating fair treatment of consumers into balanced scorecards or more generally into values statements.

957 Responses also advised that changes to remuneration structures were generally reflected in individual employment contracts, as well as aggregator and broker agreements and performance management agreements (where applicable). Our review of lenders' term sheets with aggregators highlighted that these agreements were piecemeal, often with amendments and variations overlaying the original agreements. We found it confusing to work through the multiple documents setting out the commission and other benefits provided under each arrangement.

958 We asked broker businesses whether the commissions payable to brokers are dependent on a subjective assessment of the overall performance of the broker by their manager, or by metrics such as customer satisfaction or complaint data. Broker business generally reported that, while these factors may be considered by the business, they would not affect the commission paid to the broker.

Involvement of critical functions in remuneration structures

959 We sought to understand the role of critical functions—such as credit risk, legal, compliance and assurance functions—in the design and approval of home loan remuneration structures.

Input and independence of critical functions

960 Most lenders and aggregators reported that critical functions provide input and oversight into the design and review of remuneration structures, but this role does not extend to approval. We identified that in some cases input is provided only on request, rather than as part of an established process.

961 All lenders and aggregators reported that critical functions have reporting lines that are independent of the home lending businesses they support. In contrast, all broker businesses we surveyed reported that critical functions do not provide input into design or have independent reporting lines. However, smaller broker businesses are generally unlikely to maintain these functions in-house.

Remuneration of critical functions

962 A significant majority of lenders, aggregators and broker businesses reported that bonuses or other incentives for critical functions do not depend on the sales performance of the home lending businesses they support. Similar

results were reported for management responsible for monitoring brokers and lenders' staff.

963 However, critical functions and management responsible for monitoring brokers and lenders' staff may receive some limited or very indirect payments based on overall business performance.

964 All lenders, aggregators and broker businesses reported that their credit risk functions (where applicable) were not renumerated based on the volume of home loan products sold. Some lenders indicated that the quality of home loan products sold was one component of remuneration for their credit risk functions (i.e. incentives may be cancelled if quality thresholds are not met).

965 Overall, critical functions generally appeared to be structured to independently review and provide design input into home loan remuneration structures, although their role and level of input varied. We consider that maintaining separate remuneration structures and independence for critical functions is likely to improve their ability to promote compliance without being conflicted by incentives linked to sales targets.

Board and senior management involvement

Board involvement

966 We asked lenders, aggregators and broker businesses a series of questions about how their boards, or relevant committees constituted by board members, ensure appropriate governance for:

(a) remuneration structures (including rewards and incentives) for selling home loan products;

(b) sales conduct for home loan products; and

(c) quality of outcomes for home loan consumers.

Note: Only one broker business in our review sample has a business structure which includes a Board that was separate from management, reflecting the small size of many broker businesses.

967 In particular, we asked how boards receive reports and convey messages in these areas. We also asked questions about how the board communicates with critical functions and receives feedback from relevant stakeholders.

968 We see governance and remuneration structures within an entity as key drivers of corporate culture. A strong and effective governance structure, which provides effective oversight to the board, supports the board's ability to promote good culture.

969 Deficiencies in a board's oversight mechanisms increase the risk of poor culture developing. Remuneration structures that drive poor sales conduct and poor consumer outcomes may continue undetected or unaddressed.

Reporting to the board

970 We asked lenders, aggregators and broker businesses whether boards, or relevant committees constituted by board members, were provided with reporting across the distribution channels (direct and broker channels) about remuneration structures, sales conduct and the quality of consumer outcomes.

971 We also asked whether boards, or relevant committees, could demonstrate how they respond to these reports (e.g. in their meeting minutes). Responses indicated significant inconsistencies between the reporting that the boards of lenders and aggregators, or relevant sub-committees, could produce.

972 These items were commonly not standing board meeting agenda items. It could also generally not be demonstrated how boards responded to these items in meeting minutes (i.e. minutes were often drafted in broad terms).

Reports on remuneration structures

973 Approximately 50% of lenders and aggregators advised that they could produce board reports about home loan remuneration structures. This included reports made by or to the board or relevant committees, reports canvassing new or material changes to remuneration structures, and general half year and annual reporting.

Reports on sales conduct

974 In contrast, most aggregators, but not lenders, advised that they could produce board reports about sales conduct and performance. Where lenders' boards could produce reports, reporting included board and audit reports. A small number of lenders noted that related matters, such as conduct risk, would be discussed on an exception or materiality basis.

Reports on the quality of consumer outcomes

975 Most lenders, aggregators and broker businesses advised that they could not produce board reports about the quality of home loan consumer outcomes. Where reports could be produced, reporting included customer satisfaction survey results (noting that the surveys may not address loan performance), material internal and external dispute resolution matters, and audit results.

Internal audit reporting

976 We asked lenders, aggregators and broker businesses about the relationships between the board, or relevant committees, and their internal audit function. We asked whether, as a part of their normal audit process, the board receives reporting from this function about assessment of remuneration structures, sales conduct and the quality of consumer outcomes.

977 Responses generally indicated that boards do not receive such reporting. Where reports are provided, it was primarily included as one component of general complaints, audit, compliance and/or assurance reporting. Some lenders noted that internal audit covered home lending on a cyclical basis only, and reporting would be prepared accordingly.

978 Overall, we observed generally low levels of reporting to boards on remuneration structures, sales conduct and consumer outcomes. In particular, reporting on consumer outcomes appeared to focus on customer satisfaction ratings (such as 'net promoter scores'). We consider this to be a limited mechanism for assessing the quality of consumer outcomes.

979 We consider that reporting on these matters would provide boards with greater insight into whether remuneration arrangements are fit for purpose, mitigate the risk of undesirable sales behaviours, and prevent consumer detriment.

Ongoing communication by and to the board

980 We also asked lenders, aggregators and broker businesses a series of questions about whether their boards receive and seek feedback from various internal and external stakeholders about remuneration structures, sales conduct and the quality of consumer outcomes.

981 We asked these questions to understand how boards proactively promote, monitor and assess the impact of the entity's culture on conduct (including conduct driven by remuneration structures) and make changes where necessary.

Board communication with assurance functions

982 Most lenders, aggregators and broker businesses advised that their board or relevant committee minutes could not show whether and to what extent the board or committee had communicated with assurance personnel (first line, second line or third line) on these matters.

> Note: In risk management, first-line assurance is provided by operational management, second-line assurance is provided by dedicated risk management and compliance staff and third-line assurance is provided by independent audit staff.

983 Where such minutes or reporting existed, it appeared to be an exception or it was discussed as a general theme (i.e. conduct risk or net promoter scores generally).

Note: A net promoter score (or NPS) is a measure of customer satisfaction derived from asking consumers how likely they would be to recommend a product or service (e.g. an individual broker) to a friend or colleague.

Feedback sought by the board

984 Most lenders and aggregators also advised that their board, or relevant committee, did not actively seek feedback on these matters.

985 However, they advised that their board, or relevant committee, did have processes in place to receive unsolicited or solicited feedback on these issues.

986 Predominant methods for the collection of feedback were through whistleblowing or speak up/out policies and programs, net promoter score surveys, and customer experience and satisfaction surveys (noting again that some surveys may not explicitly canvass conduct or sales issues).

987 Overall, lenders and aggregators generally appeared to not have clear proactive measures to identify, manage and mitigate remuneration risks. This may make it more difficulty for boards to ensure, or have comfort, that remuneration arrangements are fit for purpose, mitigate the risk of undesirable sales behaviours, and prevent consumer detriment.

988 Broker businesses tended to not have a board that was separate to their management or individual brokers.

Management teams that support the board

Monitoring activities

989 We asked lenders, aggregators and broker businesses a series of questions about what steps their management takes to monitor remuneration structures, sales conduct and consumer outcomes.

990 We found significant inconsistency between the nature and level of monitoring undertaken by management across lenders, aggregators and broker businesses.

Remuneration structures

991 Most lenders reported that management monitored remuneration structures. Monitoring was conducted by a variety of personnel—including the chief executive officer, human resources, and pricing, risk and compliance committees—with reports provided to pricing and remuneration oversight

committees. Deficiencies in monitoring predominantly related to a lack of monitoring of third party distribution channels, such as broker businesses.

992 In contrast, aggregators and broker businesses undertook significantly less monitoring in relation to remuneration structures. Where there was monitoring, aggregators typically focused on audit and customer satisfaction results, periodic performance and salary reviews or responded to market changes. Broker businesses indicated any such monitoring typically took the form of ad hoc or monthly business reporting.

Sales conduct and activities designed to identify trends and outcomes

993 A significant number of lenders and aggregators reported that management undertook monitoring in relation to sales conduct. This included reviewing sales, profitability and performance dashboards (one of the most prevalent types of monitoring), files, complaints and consumer experience reporting, audit results, and first-line and second-line assurance processes. Monitoring by lenders of third-party channels (e.g. brokers) was more limited than monitoring of their own employees.

> Note: Many lenders had difficulty in providing some elements of home loan data to us. While we recognise that lenders will have their own forms of monitoring, this difficulty indicated to us that such reviews may focus on the portfolio performance, rather than at an individual sales level.

994 We identified that:

(a) only a small number of broker businesses reported that management undertook such monitoring (predominantly through ad hoc reviews); and

(b) monitoring was more limited in lenders' third-party distribution channels compared to lenders' own employees.

995 We also asked a series of questions specifically about sales conduct and whether management monitors particular potential indicators of poor sales conduct. This included whether management monitored the sales trends for individual brokers and lenders' staff. Responses indicated significant inconsistencies between lenders, aggregators and broker businesses.

996 Approximately 50% of lenders and aggregators reported that they undertook additional scrutiny of high-performing persons or those with unusual sales trends, and took steps to identify miss-selling or inappropriate behaviour motivated by financial gain. Monitoring included reviewing high or unusual sales performers, outliers and exceptions, and audit or file reviews—either on an ad hoc or periodic basis. Brokers reported that management largely did not undertake such monitoring.

997 Slightly more lenders than aggregators reported that their management provided additional scrutiny of an individual's sales activity around

incentive scheme features that indicated increased risk (e.g. sales patterns before and after a target has, or has not, been met, penetration rates for cross-selling, or variations in the mix of products sold). No broker businesses reported that management undertook such monitoring.

998 A significant majority of aggregators and broker businesses did not review their brokers on loan performance outcomes (e.g. loans with high default or arrears rates). Comments suggested that the ability of an aggregator or broker's business to conduct this monitoring largely depends on the contractual relationship and willingness of the lender to provide critical information.

Note: To the extent that the loans of a particular broker or broker business are performing badly across a number of lenders, the aggregator is best placed to understand these trends (if it is given the appropriate information).

999 In contrast, we identified that just over half of lenders reviewed individual brokers and staff members on loan performance outcomes, although these reviews generally appeared to be undertaken at a portfolio level, and mainly focused on arrears data.

1000 A significant majority of responses indicated that monitoring programs did not include mystery or shadow shopping programs. Where such programs were undertaken, they were largely done on an ad hoc or unstructured basis.

Quality of consumer outcomes

1001 Approximately 50% of lenders and aggregators reported that management undertook monitoring of the quality of consumer home loan outcomes. This included by reviewing net promoter scores, customer satisfaction metrics (noting that these metrics may not address loan performance and typically are conducted only for settled loans), complaints, files, arrears data, fraud metrics, audit results and post-settlement calls. Some responses indicated that senior management received mystery shopping reports.

1002 Contractual arrangements with lenders, and the lender's willingness to provide reports, determined how much loan performance reporting aggregators received.

1003 Only a small number of broker businesses reported that management undertook such monitoring, and this was predominantly through net promoter scores or similar data on settled loans only.

1004 Overall, a lack of clear proactive processes for management to undertake regular and robust monitoring of remuneration structures, sales conduct and the quality of consumer outcomes may increase the risk that instances of poor conduct are not identified or addressed.

1005 We sought to understand the extent to which lenders use their contracts with aggregators to exercise a level of control over brokers by imposing obligations on the aggregator to monitor their broker network's compliance with the National Credit Act and other laws. Overall, lenders do not typically impose a specific obligation on the aggregator to monitor such compliance.

1006 We asked lenders and aggregators about their processes to undertake due diligence when the lender or aggregator accredits a broker. We also asked lenders and aggregators what oversight processes they undertake on an ongoing basis.

1007 Overall, while aggregators and some lenders undertake due diligence or oversight processes for brokers, these processes are largely limited to basic matters such as licensing status or membership of an industry association. We found that generally lenders and aggregators did not undertake more detailed reviews, such as obtaining direct feedback from clients (beyond that relating to an assessment of the client's 'satisfaction'), and did not consider whether the broker had obtained good consumer outcomes for those clients.

Reporting by critical functions

1008 Lenders, aggregators and broker businesses stated that senior management, or other relevant committees, largely do not receive reports from internal audit functions about remuneration structures, sales conduct or the quality of consumer outcomes.

1009 Where such reporting was received, it primarily related only to sales conduct by direct, rather than third- party, distribution channels. No such reporting was done by broker businesses.

1010 Failure by management to receive reporting designed to identify and mitigate key risks, trends and outcomes may increase the risk that instances of poor or undesirable conduct are not captured and addressed.

1011 Lenders have the right to clawback commissions if a home loan is paid out or discharged early. The frequency with which lenders exercise these rights for loans originated through particular brokers or broker businesses is a valuable tool to influence the sales conduct of those individuals or businesses. However, only 20% of lenders reported that they had a process to review overall commission recovery rates to identify potential cases of broker misconduct.

1012 Aggregators are in a position to monitor commission recovery rates across all of their lenders. However, only 20% of aggregators reported that they reviewed those rates to help identify potential cases of broker misconduct.

Incorporating culture into business practices

1013 As highlighted earlier, rewards and incentives play a big role in driving conduct by:

(a) influencing priorities and behaviour, which in turn affect an entity's culture; and

(b) acting as a motivator and reinforcer of conduct.

1014 We consider that good conduct can be achieved by embedding good culture into all business practices. This can help to remove gaps between an entity's desired values and actual conduct.

1015 We asked lenders, aggregators and broker businesses what measures they use to assess how the entity's culture is embedded in the conduct of their brokers and staff, and whether the results of these assessments were escalated to senior management.

1016 For example, we asked them what steps they take to:

(a) receive consumer feedback;

(b) test home lending practices to ensure they align with the entity's values and policies, and what controls are incorporated into the design of home loans to reduce risk of non-compliance (including what trigger events are profiled or flagged for further review); and

(c) identify and escalate potential trigger events that may indicate poor quality consumer outcomes or sales conduct, and whether 'flags' are subsequently applied to help identify conduct or compliance issues.

1017 We also asked whether participants have formal processes in place that allow brokers and staff to escalate concerns they may have with the method of sales of home loans to consumers and/or outcomes received by consumers.

Consumer feedback tools

1018 Lenders, aggregators and broker businesses use a range of tools to receive consumer feedback. These tools include customer satisfaction calls and surveys, social media, post-settlement and anniversary surveys, limited mystery shopping, and focus groups, complaints recording and ad hoc market research. However, responses indicated significant inconsistency in how and when these tools are used.

1019 Data from these sources is typically escalated to senior management via monthly feedback or dashboard reporting, trackers, and executive agenda items. Broker businesses only escalated consumer feedback to senior management in limited circumstances.

Testing, controls and profiling

1020 Most lenders and aggregators reported that their first-line and second-line assurance functions test home lending practices to ensure they align with their entity's values and policies. Testing was predominantly conducted through monitoring frameworks, compliance reporting, audit programs and file reviews. Aggregators reported brokers who were credit representatives of the aggregator were tested more frequently. Testing by broker businesses was typically limited.

Note: Based on the responses, aggregators that were owned by a lender reported more testing than other aggregators. We note that it is not clear whether this is a result of the ownership structure or whether it reflects the fact that aggregators owned by lenders may be larger and have more mature compliance programs.

1021 Most lenders reported that they incorporated controls into the design of home loans to reduce the risk of non-compliance, mainly through a product design framework and review procedures. Broker businesses and aggregators largely reported that they did not incorporate controls as they were not the product manufacturer. Aggregators also reported that they had:

(a) no controls even where they had white label arrangements; and

(b) a lack of controls around selecting approved products for their panels.

Escalating examples of poor practices

1022 Most lenders and aggregators reported that they have formal processes for brokers and staff to escalate concerns about sales practices and the quality of consumer outcomes. These included whistleblower programs, integrity officers, speak up/out policies and codes of conduct. These programs were far less prevalent within broker businesses.

Dealing with poor conduct

1023 We asked lenders, aggregators and broker businesses a series of questions about their methods and sanctions to penalise poor sales conduct. A wide range of sanctions were used to address poor sales conduct and consumer outcomes. Sanctions ranged from warnings and counselling processes, through to termination or removal of accreditation.

1024 Depending on the circumstances, a mixture of financial and non-financial sanctions were applied occasionally, as required or in structured periodic cycles (e.g. through the annual process for setting a staff member's bonus).

1025 Responses indicated that:

(a) lenders typically applied sanctions only for their own staff (i.e. they did not seek to sanction brokers for poor conduct);

(b) lenders were generally unaware of actions taken by aggregators for misconduct by brokers; and

(c) broker sanctions tended to be either warnings or terminations.

1026 Generally, sanctions that resulted in one form of remuneration being cancelled or recovered (e.g. commission clawback) did not result in other forms of remuneration also being cancelled or recovered.

1027 For broker businesses, we saw little evidence that sanctions for poor conduct that resulted in the cancellation of soft dollar benefits (e.g. courses and conferences) would or did result in other forms of remuneration (including commissions) being cancelled or recovered.

1028 Because aggregators sit between lenders and brokers, the lender's right to recover damages for broker misconduct is generally with the aggregator. If exercised fully, that right can act as a powerful incentive for aggregators to ensure that brokers are doing the right thing.

1029 We asked lenders whether they had actually sought to recover any losses from aggregators due to broker misconduct (i.e. other than clawback of commissions resulting from a home loan being repaid or discharged early). No lenders reported that they had made any attempts to recover such losses from aggregators in 2012 and 2015.

Note: Only two lenders could provide figures for losses they suffered as a result of broker misconduct. Such losses totalled $1.7 million in 2012 and $100,000 in 2015. We consider that this is unlikely to be a true reflection of lender losses from broker misconduct in those years.

Training

1030 Regular and appropriate training is important for brokers and lenders' staff to maintain knowledge of an entity's home lending business practices, including its values and expectations of attitudes and behaviours of product advisers.

1031 Credit licensees (such as lenders, aggregators and broker businesses) also have specific obligations under the National Credit Act to ensure their representatives are adequately trained and competent to engage in the credit activities authorised by their licence. We have set out our expectations for training of credit licensees in Regulatory Guide 206 *Credit licensing: competence and training* (RG 206).

1032 We asked lenders, aggregators and broker businesses whether they had:

(a) specific training programs that illustrated the conduct expected for the sale of home loan products; and

(b) compliance and risk management processes to maintain brokers' and staff members' knowledge of the values and behaviours expected by the entity.

1033 Responses indicated that training programs varied significantly.

Lenders' programs

1034 Lenders' training on sales conduct differed considerably. Training programs were largely implemented only for their own staff, with less than half of lenders maintaining training programs for third-party channels (e.g. aggregators, brokers and other associated businesses such as introducers and referrers).

1035 Just over half of training programs were compulsory. Training for branch and telephone sales staff was generally compulsory. For most compulsory programs, a range of penalties applied for non-compliance with training requirements. Penalties ranged from consequence management processes (i.e. warnings and counselling) to financial penalties (reduction in incentives) to inability to perform a function (i.e. unable to process and submit home loan applications) until training was completed. Where data was available, participation rates for non-compulsory training ranged from approximately 45–100%, with higher rates for sales-based programs.

1036 Lenders typically maintained a separate consequence management framework for brokers. Generally, brokers must comply with compulsory training requirements or face losing their accreditation. If referrers and introducers were required to attend training, they could not refer potential consumers to the lender until it was completed.

1037 Lenders followed up those who did not attend compulsory training across all channels (e.g. through regular reporting to line managers or business development managers, automated reminders, and remedial training). To a lesser extent, lenders also followed up on staff who failed training-related assessments. Some lenders reported that for third-party channels, follow ups were conducted only for credit representatives (not credit licensees).

1038 All lenders had a significant number of compliance training programs across all channels, including ongoing compliance and risk management training—focusing on topics such as National Credit Act compliance, Australian Consumer Law, fraud and general banking knowledge—and culture training.

1039 Training programs for third party channels were typically delivered by slightly different methods (i.e. professional development days canvassing technical updates, bulletins and webinars, and by business development managers and/or industry associations). There was a general expectation that aggregators would provide training to ensure compliance by brokers with various aspects of relevant National Credit Act requirements.

Aggregators' programs

1040 A significant majority of aggregators had training programs for their own staff, as well as for broker businesses generally and broker businesses that use their aggregation services. Training included webinars, technical updates, bulletins, compliance-focused workshops, professional development events, conferences and ongoing training.

1041 Aggregators' training programs relating to compliance were largely compulsory. Some aggregators suggested that even if training was not compulsory, it was considered best practice and highly encouraged. Compulsory training appeared largely confined to brokers who were the aggregator's credit representatives. Some aggregators required participation in training programs if performance standards were not met. Most aggregators reported that they followed up on those who did not attend compulsory training or failed any related assessments.

1042 Aggregators applied a range of penalties for those who did not attend compulsory training—from requiring additional training/coaching, remedial audits and counselling, to suspension and termination of employment. These penalties generally applied only to aggregators' own staff and credit representatives.

1043 Where aggregators recorded participation rates for non-compulsory programs, these ranged from approximately 30–100%, with higher participation rates for sales-based programs.

Brokers' programs

1044 Brokers' training predominantly involved professional development events conducted by lenders or aggregators. A few broker businesses advised that they supplemented these events with in-house webinars, workshops, and focus groups dealing with compliance and risk management processes.

1045 Participation in these events was largely non-compulsory, with attendance ranging from 50–100%. Results suggested that independent contractors, who work within the broker business but not under the brand itself, do not typically attend these trainings.

1046 Only one broker indicated that there could be penalties for non-attendance at compulsory training. A small number of broker businesses indicated that they have follow-up procedures for brokers who do not attend compulsory training.

1047 Regular training provides an important avenue for reinforcing the conduct expected from brokers and staff members. Failure to apply appropriate consequences for non-compliance with training requirements lessens their effectiveness in reducing instances of non-compliance and poor sales behaviours.

Appendix 1: Methodology for this review

Data collection from industry

1048 We obtained both qualitative and quantitative information from industry participants, through survey questionnaires and data requests, respectively.

Survey questionnaires

1049 The qualitative information for this review was largely obtained through the use of a survey-type questionnaire for each of the industry participants (apart from requesting term sheets from lenders and aggregators: see paragraphs 405–406). These surveys asked a series of questions about the way the business operated, largely using a ‘closed-question’ methodology.

Note: For example, we asked broker businesses to answer the question, ‘Is the remuneration for [brokers] solely based on commission from the sale of products and services (including residential mortgages)?’ The broker businesses were then presented with a list of options that permitted them to answer ‘Yes’, ‘Some brokers’ or ‘No’.

1050 In addition, we asked industry participants to provide quantitative data on actual outcomes for relevant topics. This included matters such as the value of cash incentives paid to brokers and lenders’ staff, the value of soft dollar benefits and the amount of remuneration that was recovered from brokers and lenders’ staff.

1051 Given the large number of participants and the wide-ranging nature of the review, we did not generally ask for copies of documentation (e.g. policies and procedures) to support the participants’ responses to the survey questionnaires. Where necessary, we may follow up this review with further requests for that documentation.

Data requests

1052 We also asked lenders and aggregators to provide two large data sets relevant to this review.

Home loan data

1053 Firstly, we asked each lender to provide 157 data fields for each home loan originated by that lender in 2012 and 2015 (referred to in this report as ‘home loan data’), whether through broker channels or the lender’s own proprietary channels.

1054 These data fields included de-identified data about borrowers (including application information), the loan features and pricing, the loan performance since origination, and the channel through which the loan was sold (including any commission directly attributable to the sale paid to the loan seller).

1055 We asked for data on loans from 2012 so that the relevant loans had been open long enough to provide a good indication of the performance of those loans. We asked for data on loans from 2015 to understand more recent remuneration arrangements for the sale of home loans.

1056 Before asking for the home loan data, we conducted a pilot process with each lender. As a result of that process, we changed or removed some of the data fields requested. Many lenders still struggled to provide some of the data requested at an individual loan-by-loan basis: see paragraphs 159–163. We still received a very large and rich data set containing information on approximately 1.4 million loans.

Loan flow data

1057 Secondly, we asked both lenders and aggregators to provide month-by-month data on the sale of lenders' home loans through aggregators from 2012–15 (i.e. four full years of data). The lenders provided data for 20 aggregators (the 14 aggregators in this review plus an additional six), while aggregators provided data for all lenders with which they dealt. The data included details of the value of new and outstanding home loans, commission payments on those home loans, and the clawback of commissions (referred to in this report as 'lenders' monthly loan flow data' and 'aggregators' monthly loan flow data'). The aggregators' monthly flow data covered $550 billion of new home loans sold in those four years.

1058 We also asked aggregators to provide similar types of data on loans sold by individual broker businesses that operated under the aggregator. This information was obtained on a year-by-year basis for 2012 to 2015 (referred to in this report as 'aggregators' yearly loan flow data').

Categories of lenders and aggregators

1059 We have used the following terminology to describe different categories of lenders in the figures and charts in this report:

(a) major bank;

(b) major bank: sub-division;

(c) foreign bank;

(d) other bank;

(e) customer-owned banking institution; and

(f) non-bank lender.

1060 'Major bank: sub-division' includes Bankwest, Advantedge and St George. For a list of the other lenders in this review by category, see Table 1. For a list of the aggregators in this review by category, see Table 2.

1061 Some figures and charts display results at an individual lender or aggregator level (e.g. ‘Major bank 1’ or ‘Large aggregator 1’). Unless noted otherwise, the labels used in different figures or tables do not refer to the same lender or aggregator (e.g. ‘Major bank 1’ does not always refer to the same major bank).

Consumers’ perceptions of mortgage brokers

Omnibus survey

1062 In the omnibus survey for consumers, we included several high-level incidence and usage questions (on whether consumers had previously used a broker and whether they intended to do so in the future) and several additional questions to explore consumers’ attitudes and perceptions of brokers in more detail.

1063 All 3,000 research participants were invited to answer the high-level incidence questions. A reduced number of respondents were asked to answer the additional questions.

1064 In our analysis, we focus primarily on two key subgroups that answered the additional, more detailed questions: 1,000 general consumers (general consumers) and 490 consumers who either had recent experience in using a broker (i.e. within the past two years) or stated the intention to do so within the next year.

Note: Stated intentions will not necessarily translate into actual behaviour.

1065 In the first survey, all 1,000 respondents were invited to answer the additional questions, ensuring a robust base of general consumers for analysis. We conducted the second and third surveys to increase the sample of respondents with at least some level of engagement/experience with brokers.

1066 Of the 490 consumers with recent experience/future intention to use a broker, around one quarter (28%) indicated that they had used a broker in the past two years but did not intend to again in the next year, 20% had used a broker in the past two years *and* intended to again in the next year, and the remaining 53% stated that they had *not* used a mortgage broker in the past two years but intended to in the next year.

1067 Of those without recent experience who stated their intention to use a broker in the next year, the clear majority (73%) had previously obtained a home loan either directly through a lender or through a broker more than two years ago.

1068 Research participants were aged 18 years and older and were distributed throughout Australia, including both capital city and non-capital city areas. They were recruited from a certified online panel provider. The data was weighted to reflect the Australian adult population by age, gender and region (according to the latest ABS data).

1069 All survey results are based on self-reported attitudes and perceptions. Respondents could provide multiple responses to some questions; therefore, some response categories sum to more than 100%.

Margin of error

1070 As this research was based on a sample of people and not the entire population, the data is subject to sampling error. Table 24 indicates the likely margin of error for estimates (at a 95% confidence level) expressed as the number of percentage points above or below the estimated result.

1071 For example, with a sample size of 490 respondents and an estimated result of 50%, the margin of error is ±4.5%. This means we can be 95% confident that the true proportion lies between 45.5% and 54.5%.

Table 24: Survey margin of error (percentage points ± estimated result)

Sample size	50%	40% or 60%	30% or 70%	20% or 80%	10% or 90%
490	±4.5%	±4.4%	±4.1%	±3.6%	±2.7%
1,000	±3.2%	±3.1%	±2.9%	±2.5%	±1.9%
3,000	±1.8%	±1.8%	±1.7%	±1.5%	±1.1%

Appendix 2: Value of upfront and trail commission based on data provided by lenders and aggregators

1072 This appendix sets out the distribution in the rates and values of upfront and trail commissions to aggregators and brokers based on data supplied by lenders and aggregators.

1073 The rates and values of upfront and trail commissions paid to aggregators by lenders are based on:

(a) the home loan data provided by the lenders; and

(b) the loan flow data provided by aggregators, showing on a month-by-month basis the details of loans sent by the aggregator to all lenders it dealt with (i.e. not just the 19 lenders in this review).

1074 The rates and values of upfront and trail commissions paid to broker businesses by aggregators are based on the loan flow data provided by aggregators, showing on a year-by-year basis the details of the loans sent by the particular broker business to all lenders (i.e. not just the 19 lenders in this review).

1075 The rates and values of these commissions are represented through box plots in Figure 36–Figure 45.

1076 Each box plot represents the distribution of either the rate or dollar value of commission. The rectangle represents the second and third quartiles (i.e. 25–75% of the values), with the line down the middle representing the median value. Where there is only a single vertical line (rather than a rectangle) it means that the values are highly concentrated.

1077 The horizontal lines represent either the maximum data point or 1.5 times the difference between the 75th and 25th percentile from the edge of the box. The dots represent the values that lie outside of this range.

Note: A white label arrangement under which a lender agrees to issue loans under the aggregator's name is treated as a separate data point in this appendix.

1078 In addition, we have calculated the range of rates of commission paid to individual broker businesses reported on by the aggregators for home loans funded by the ADIs in the review. We have included each broker business that originated more than 100 loans through those ADI lenders in 2015.

Note: By including the rates of commission paid by ADIs alone, we have excluded the higher rates of commission that may be paid by non-ADIs for non-conforming loans.

1079 Table 25–Table 38 set out this information for rates of upfront commission and Table 39–Table 52 for rates of trail commission.

Note: The labels for lenders and aggregators used in the figures and tables in this appendix refer to the same the same lender or aggregator. For example, 'Large aggregator 1' refers to the same large aggregator in all the figures and tables in this appendix.

Rates and values of commission paid to aggregators

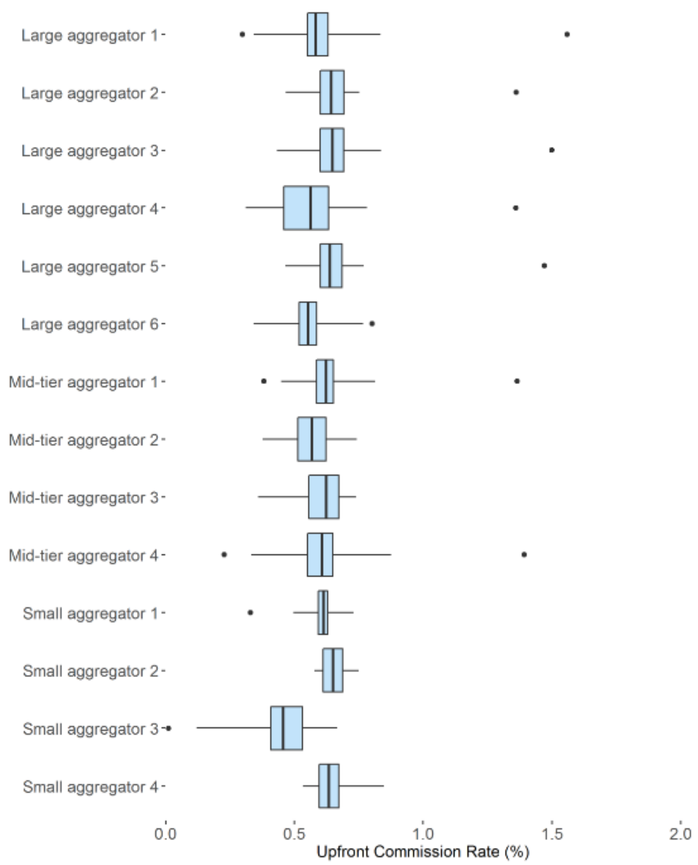
Distribution of rates of upfront commission

1080 From the loan flow data provided by aggregators we derived the average rate of upfront commission paid by each lender to each aggregator. We did this by dividing the sum of the upfront commission disclosed in a year by the sum of the loan flow from that aggregator to that lender in the year.

1081 Figure 36 sets out the distribution of the average rates of upfront commission that each aggregator received from each lender during 2015.

1082 For each aggregator, we have included the loan flow data and commission from any lender with at least $5 million loan flow from the aggregator in the year. Each box plot represents the range of rates of upfront commission available from different lenders to the aggregator (which may then be passed through to the brokers within the aggregator's network).

Figure 36: Distribution of average rates of upfront commission paid by lenders to each aggregator



Source: Aggregators' loan flow data

Note: See paragraphs 1083–1085 for a description of the trends shown in this figure.

1083 The median values of the average rate of upfront commission paid to aggregators ranged from 0.46% to 0.65% of the loan amount, with the industry mean being 0.62%.

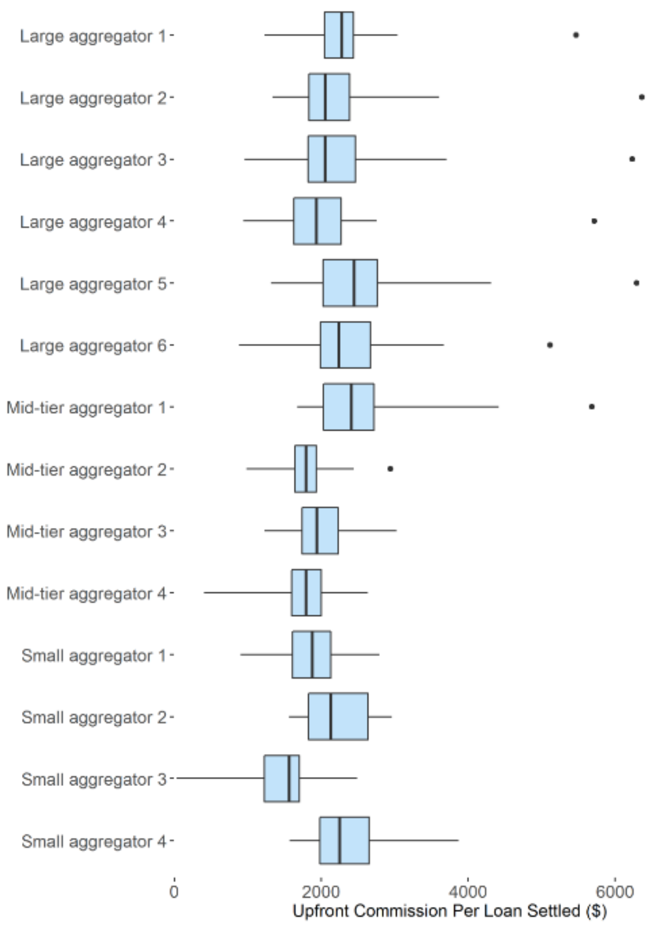
1084 Within an aggregator, the difference between the rate at the 5th percentile (i.e. the lowest paying lenders) and the 95th percentile (i.e. the highest paying lenders) ranged between 0.16% and 0. 60%.

1085 Across all aggregators, the lowest average rate of upfront commission paid by a lender was 0.01% and the highest average rate was 1.56%.

Distribution of upfront commission amounts

1086 Figure 37 sets out the distribution of the average per-loan value of the upfront commission paid by each lender to each aggregator derived from the loan flow data provided by the aggregators for 2015.

Figure 37: Distribution of average per-loan values of upfront commission paid by each lender to each aggregator



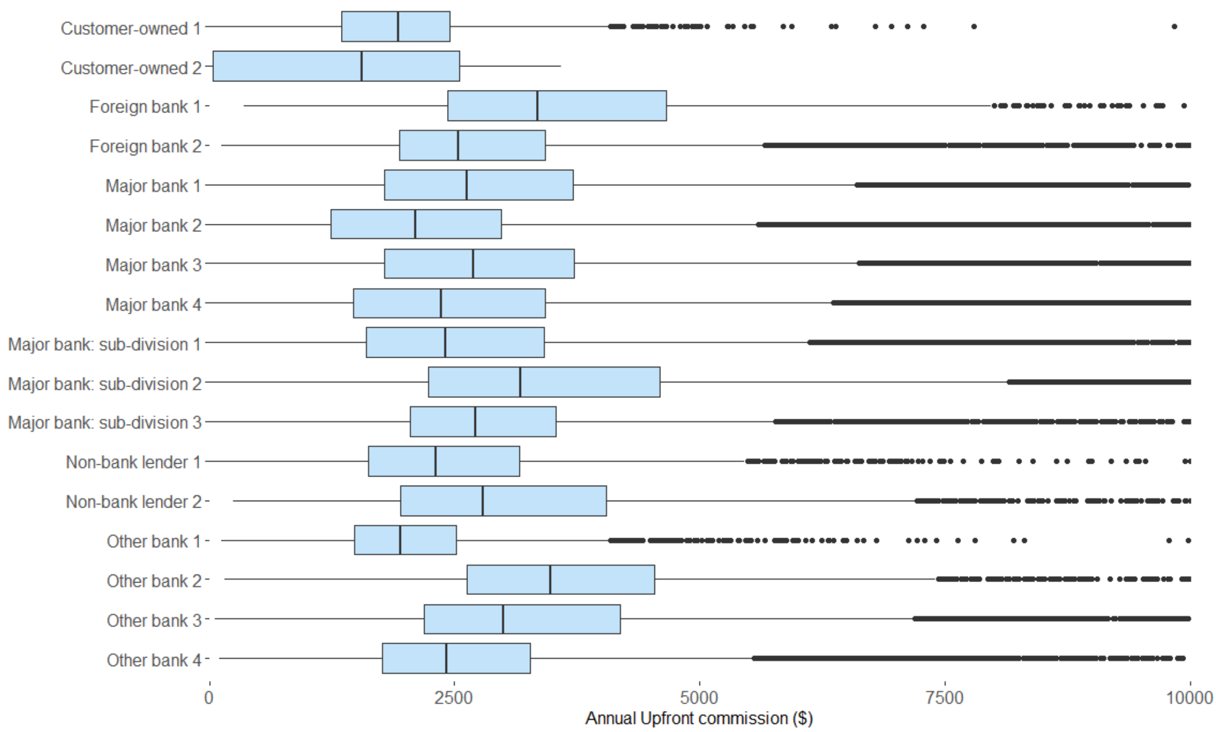
Source: Aggregators' loan flow data

Note: See paragraph 1087 for a description of the trends shown in this figure.

1087 The average per-loan amount of upfront commission received from lenders varied from almost zero to over $5,000. It is important to note that this was the average amount of upfront commission paid on all loans sent by an aggregator's brokers to the lender.

1088 Figure 38 sets out the distribution of the per-loan value of the upfront commission for each lender based on the home loan data supplied by lenders.

Figure 38: Distribution of per-loan values of upfront commission for each lender



Source: Lenders' home loan data

Note: See paragraph 1089 for a description of the trends shown in this figure.

1089 The per-loan amount of upfront commission paid on particular loans by each lender varied widely (as would be expected when the commission depends on the value of the loan). The values ranged from almost zero up to approximately $7,400 at the 95th percentile (which means that, for this lender, 5% of loans paid a commission amount of $7,400 or above).

Note: The dots (which appear as a thicker line) represent individual loans over the 95th percentile. We have cut off this chart at $10,000 so that it is readable.

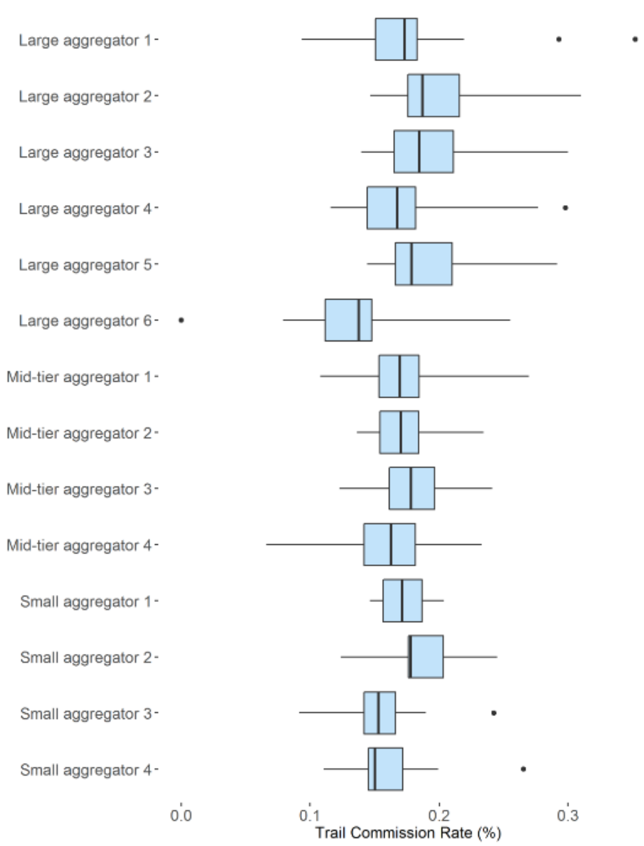
Distribution of rates of trail commission

1090 We also used the data provided by aggregators and lenders to derive information about the rates and value of trail commissions paid by lenders.

1091 From the loan flow data provided by aggregators, we derived an estimate of the average annual rate of trail commission paid by each lender to each aggregator. We did this by dividing the sum of the trail commission paid in each year by the lender by the average outstanding balance of home loans.

1092 Figure 39 sets out the distribution of the average rates of trail commission that each aggregator received from each lender across 2015.

Figure 39: Distribution of average rates of trail commission received by each aggregator from each lender



Source: Aggregators' loan flow data

Note: See paragraphs 1093–1095 for a description of the trends shown in this figure.

1093 The median values of the rates of trail commission ranged from 0.15% to 0.19% of the loan amount, with the industry mean being 0.18%.

1094 Within an aggregator, the difference between the rate at the 5th percentile (i.e. the lowest paying lenders) and the 95th percentile (i.e. the highest paying lenders) ranged between 0.06% and 0.17%.

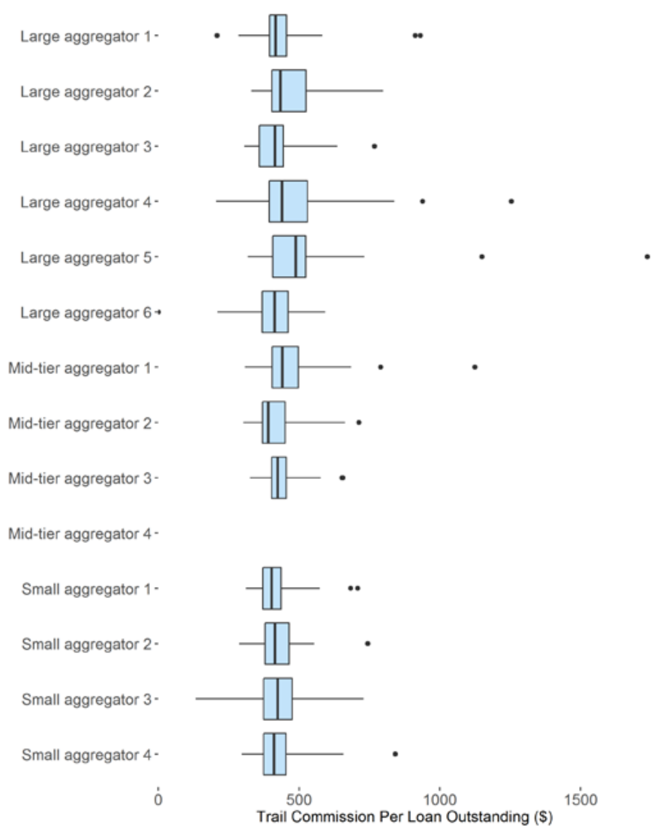
1095 Across all aggregators the lowest average annual rate of trail commission paid by a lender was 0.01% and the highest average rate was 0.35%.

Distribution of trail commission amounts

1096 From the loan flow data provided by aggregators we calculated the average per loan amount of trail commission paid by each lender in 2015. We did this by dividing the total trail commission paid by each lender by the average monthly number of outstanding home loans.

1097 Figure 40 sets out the distribution of the average per loan amount of trail commission paid by each lender for each aggregator.

Figure 40: Distribution of average annual per-loan values of trail commission paid by each lender to each aggregator



Source: Aggregators' loan flow data

Note 1: See paragraph 1098 for a description of the trends shown in this figure.

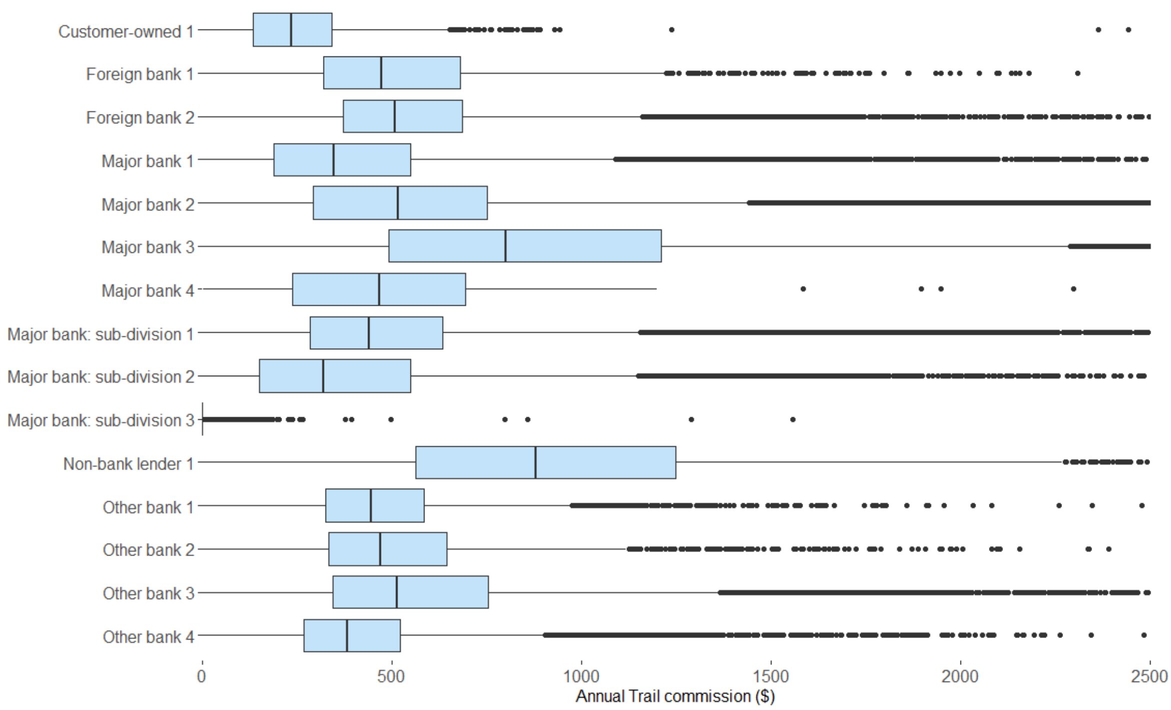
Note 2: Mid-tier aggregator 4 did not provide the number of outstanding loans, which means that we were unable to calculate the per-loan value of trail commission paid.

1098 The average annual per-loan amount of trail commission received from lenders varied from less than $100 to over $750. It is important to note that this was the average annual amount of trail commission paid by the particular lender on all loans sent by an aggregator's brokers to the lender.

1099 From the home loan data provided by lenders we estimated the per year amount of trail commission on a loan-by-loan basis. We did this by dividing the total commission paid on the loan by the length of time the loan was opened: see Figure 41.

Note: We recognise that, on a loan-by-loan basis, it is difficult to derive the average rate of trail commission due to a number of unknown factors that affect the calculation of the trail commission. For those lenders that provided data, we had some of the relevant information (including the total amount of trail commission paid, the period over which the payment was calculated and the closing balance). However, we did not know the opening balance and the month-by-month balance of the account. In addition, we only used data on loans that remained open at 31 March 2016, so we knew how long the loan has been opened.

Figure 41: Distribution of estimated per year amount of trail commission on a loan-by-loan basis



Source: Lenders' home loan data

Note: See paragraph 1100 for a description of the trends shown in this figure.

1100 The per-loan annual amount of trail commission paid on particular loans by each lender varied widely (as would be expected when the commission depends on the value of the loan). The values ranged from almost zero up to approximately $2,200 at the 95th percentile (which means that, for this lender, 5% of loans paid an annual trail commission amount of $2,200 or above).

Note: The dots (which appear as a thicker line) represent individual loans over the 95th percentile. We have cut off this chart at $2,500 so that it is readable.

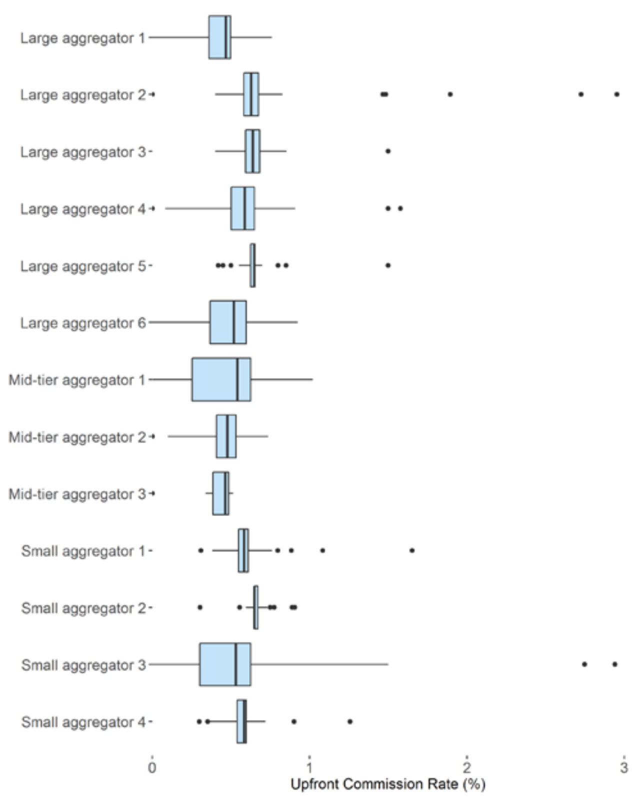
Rates and values of commission paid to brokers

Distribution of rates of upfront commission

1101 From the loan flow data provided by aggregators, we derived the average rate of upfront commission passed on by the aggregator to each broker business from each lender. We did this by dividing the total upfront commission disclosed in a year by the total loan flow from that broker to that lender.

1102 Figure 42 sets out the distribution of the average rates of upfront commission received by broker businesses from various lenders for each aggregator for 2015. Each box plot represents the differing rates of commission that are available for broker businesses within an aggregator.

Figure 42: Distribution of average rates of upfront commission received by broker businesses from each lender for each aggregator



Source: Aggregators' loan flow data

Note: See paragraphs 1103–1105 for a description of the trends shown in this figure.

1103 The median values of the derived rates of upfront commission passed through to broker business from aggregators ranged from 0.46% to 0.65% of the loan values, with the industry mean being 0.54%.

1104 Within an aggregator, the difference between the rate at the 5th percentile (the lowest paying lenders) and the 95th percentile (the highest paying lenders) ranged between 0.13% and 0.70%.

1105 Across all aggregators, the lowest average rate of upfront commission passed on to a broker business was 0.00% and the highest average rate was 3.23%.

1106 Table 25–Table 38 set out the range of rates of upfront commission paid to individual broker businesses reported on by the aggregators for home loans funded by the ADIs in the review. We have included each broker business that originated more than 100 loans through those ADI lenders in 2015. The tables set out the median, minimum and maximum average rates of upfront commission received by the broker businesses. In addition, the tables out the values at the 5th and 95th percentile.

Note: Commission is calculated as a percentage of the loan amount.

1107 Overall, even when limiting the range of lenders to include only ADIs, the variations in the average rate of upfront commission received by brokers were still considerable. Variations tended to be at least 0.10% (i.e. $500 of upfront commission on a $500,000 loan), while variations of over 0.30% were not uncommon.

Table 25: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 1

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.00%	0.49%	0.53%	0.53%	0.53%	0.53%	1,455
B2	0.36%	0.42%	0.49%	0.54%	0.56%	0.20%	0.13%	1,422
B3	0.35%	0.38%	0.49%	0.53%	0.61%	0.27%	0.16%	1,321
B4	0.36%	0.37%	0.49%	0.53%	0.56%	0.20%	0.16%	1,159
B5	0.37%	0.44%	0.50%	0.55%	0.76%	0.39%	0.12%	1,091
B6	0.00%	0.00%	0.45%	0.51%	0.54%	0.54%	0.51%	1,024
B7	0.00%	0.00%	0.46%	0.50%	0.54%	0.54%	0.50%	763
B8	0.36%	0.40%	0.46%	0.49%	0.57%	0.22%	0.09%	484
B9	0.00%	0.15%	0.33%	0.46%	0.85%	0.85%	0.31%	374
B10	0.00%	0.02%	0.43%	0.50%	0.70%	0.70%	0.48%	242
B11	0.15%	0.22%	0.39%	0.47%	0.73%	0.58%	0.25%	143

Table 26: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 2

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.11%	0.47%	0.62%	0.70%	0.70%	0.59%	0.22%	10,654
B2	0.21%	0.48%	0.63%	0.70%	0.71%	0.50%	0.23%	8,789
B3	0.47%	0.53%	0.61%	0.70%	0.71%	0.24%	0.17%	8,480
B4	0.38%	0.47%	0.63%	0.70%	0.70%	0.33%	0.23%	8,226
B5	0.47%	0.52%	0.61%	0.70%	0.71%	0.24%	0.18%	3,309
B6	0.35%	0.41%	0.57%	0.70%	0.79%	0.44%	0.29%	167

Table 27: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 3

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.50%	0.52%	0.64%	0.70%	0.76%	0.26%	0.18%	7,595
B2	0.47%	0.49%	0.62%	0.70%	0.70%	0.23%	0.21%	4,475
B3	0.47%	0.52%	0.64%	0.70%	0.70%	0.23%	0.18%	3,119
B4	0.47%	0.48%	0.60%	0.68%	0.70%	0.23%	0.21%	1,964
B5	0.50%	0.53%	0.64%	0.70%	0.73%	0.23%	0.17%	1,707
B6	0.59%	0.60%	0.65%	0.70%	0.71%	0.12%	0.10%	1,685
B7	0.47%	0.48%	0.61%	0.70%	0.72%	0.24%	0.22%	1,222

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B8	0.45%	0.50%	0.58%	0.70%	0.70%	0.25%	0.19%	495
B9	0.43%	0.50%	0.65%	0.70%	0.70%	0.27%	0.20%	320
B10	0.45%	0.47%	0.61%	0.70%	0.70%	0.25%	0.23%	222
B11	0.37%	0.41%	0.58%	0.70%	0.71%	0.35%	0.29%	140
B12	0.40%	0.41%	0.52%	0.70%	0.80%	0.40%	0.29%	140
B13	0.45%	0.50%	0.58%	0.63%	0.64%	0.19%	0.13%	123

Table 28: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 4

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.25%	0.58%	0.70%	0.91%	0.91%	0.45%	7,053
B2	0.00%	0.00%	0.59%	0.70%	0.74%	0.74%	0.70%	4,110
B3	0.07%	0.23%	0.56%	0.72%	0.76%	0.70%	0.48%	3,869
B4	0.25%	0.29%	0.61%	0.69%	0.72%	0.47%	0.40%	3,708
B5	0.00%	0.16%	0.60%	0.68%	0.70%	0.70%	0.52%	1,156
B6	0.17%	0.21%	0.54%	0.79%	0.85%	0.68%	0.58%	195
B7	0.08%	0.30%	0.63%	0.70%	0.71%	0.62%	0.40%	151

Table 29: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 5

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.35	0.50	0.65	0.70	0.70	0.35	0.20	4,810
B2	0.39	0.51	0.64	0.70	0.72	0.33	0.19	2,804
B3	0.58	0.58	0.65	0.70	0.80	0.22	0.11	2,159
B4	0.58	0.59	0.65	0.74	0.80	0.22	0.15	639
B5	0.58	0.60	0.65	0.69	0.70	0.12	0.09	303
B6	0.50	0.50	0.62	0.70	0.70	0.20	0.20	133
B7	0.50	0.57	0.64	0.66	0.67	0.17	0.09	109

Table 30: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 6

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.06%	0.38%	0.51%	0.61%	0.82%	0.76%	0.23%	4959
B2	0.45%	0.47%	0.57%	0.67%	0.77%	0.32%	0.19%	3663
B3	0.37%	0.40%	0.56%	0.66%	0.68%	0.31%	0.27%	3231
B4	0.37%	0.45%	0.55%	0.64%	0.66%	0.29%	0.19%	3180
B5	0.49%	0.50%	0.60%	0.67%	0.76%	0.27%	0.16%	1256
B6	0.30%	0.40%	0.56%	0.66%	0.68%	0.38%	0.27%	641

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B7	0.19%	0.24%	0.53%	0.66%	0.68%	0.49%	0.42%	498
B8	0.38%	0.49%	0.66%	1.30%	1.57%	1.19%	0.81%	282
B9	0.20%	0.30%	0.47%	0.55%	0.55%	0.35%	0.25%	150

Table 31: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 1

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.01%	0.12%	0.59%	0.70%	0.70%	0.69%	0.57%	4,209
B2	0.01%	0.05%	0.18%	0.62%	0.65%	0.64%	0.57%	1,937
B3	0.35%	0.44%	0.54%	0.69%	0.76%	0.42%	0.25%	1,101
B4	0.57%	0.58%	0.65%	0.91%	1.02%	0.45%	0.32%	456
B5	0.04%	0.24%	0.54%	0.63%	0.66%	0.61%	0.39%	363
B6	0.11%	0.22%	0.57%	0.65%	0.80%	0.69%	0.43%	190
B7	0.45%	0.47%	0.56%	0.59%	0.60%	0.15%	0.12%	170
B8	0.20%	0.29%	0.56%	0.62%	0.63%	0.43%	0.33%	112

Table 32: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 2

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.27%	0.33%	0.51%	0.80%	1.37%	1.10%	0.47%	2,369
B2	0.17%	0.28%	0.53%	0.74%	1.05%	0.88%	0.46%	2,241
B3	0.23%	0.24%	0.47%	0.57%	0.61%	0.38%	0.33%	1,972
B4	0.00%	0.27%	0.47%	0.60%	0.68%	0.68%	0.33%	1,678
B5	0.13%	0.29%	0.49%	0.60%	0.64%	0.51%	0.31%	1,064
B6	0.17%	0.31%	0.46%	0.56%	1.04%	0.87%	0.25%	715
B7	0.00%	0.41%	0.53%	0.62%	0.63%	0.63%	0.21%	398
B8	0.00%	0.00%	0.40%	0.76%	0.94%	0.94%	0.76%	358
B9	0.20%	0.27%	0.45%	0.59%	0.74%	0.54%	0.32%	302
B10	0.30%	0.32%	0.45%	0.53%	0.62%	0.32%	0.21%	265
B11	0.00%	0.34%	0.44%	0.53%	1.18%	1.18%	0.19%	201
B12	0.16%	0.23%	0.47%	0.53%	0.76%	0.76%	0.30%	131
B13	0.13%	0.19%	0.39%	0.47%	0.49%	0.36%	0.29%	118

Table 33: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 3

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.46%	0.47%	0.52%	0.52%	0.52%	0.05%	3,470
B2	0.00%	0.40%	0.46%	0.49%	0.49%	0.49%	0.10%	2,336
B3	0.00%	0.42%	0.43%	0.49%	0.49%	0.49%	0.06%	2,219
B4	0.00%	0.46%	0.47%	0.51%	0.51%	0.51%	0.05%	2,014
B5	0.00%	0.45%	0.48%	0.50%	0.50%	0.50%	0.04%	1,746
B6	0.00%	0.43%	0.46%	0.46%	0.46%	0.46%	0.04%	1,462
B7	0.00%	0.44%	0.45%	0.48%	0.18%	0.48%	0.04%	1,044
B8	0.40%	0.40%	0.43%	0.44%	0.44%	0.05%	0.05%	851
B9	0.00%	0.25%	0.38%	0.44%	0.44%	0.44%	0.19%	306
B10	0.00%	0.36%	0.39%	0.42%	0.42%	0.42%	0.05%	295
B11	0.00%	0.31%	0.39%	0.44%	0.44%	0.44%	0.14%	247
B12	0.32%	0.32%	0.35%	0.38%	0.38%	0.06%	0.06%	150

Table 34: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 4

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.14%	0.50%	0.63%	0.68%	0.70%	0.56%	0.18%	1,152
B2	0.41%	0.44%	0.60%	0.73%	0.78%	0.37%	0.30%	974
B3	0.25%	0.47%	0.62%	0.68	0.70%	0.45%	0.21%	954
B4	0.41%	0.46%	0.58%	0.66%	0.69%	0.28%	0.20%	892
B5	0.47%	0.53%	0.62%	0.69%	0.88%	0.41%	0.16%	791
B6	0.41%	0.47%	0.60%	0.67%	0.72%	0.30%	0.19%	320
B7	0.50%	0.50%	0.64%	0.70%	0.70%	0.20%	0.19%	122

Table 35: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 1

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.40%	0.44%	0.58%	0.70%	0.75%	0.35%	0.26%	7,169
B2	0.37%	0.42%	0.56%	0.65%	0.65%	0.28%	0.23%	3,155
B3	0.39%	0.42%	0.57%	0.66%	0.74%	0.35%	0.23%	2,727
B4	0.05%	0.42%	0.55%	0.66%	0.74%	0.69%	0.24%	1,802
B5	0.30%	0.39%	0.57%	0.68%	0.71%	0.41%	0.29%	1,493
B6	0.46%	0.46%	0.53%	0.61%	0.65%	0.19%	0.15%	203

Table 36: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 2

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.33%	0.47%	0.63%	0.70%	0.73%	0.41%	0.23%	737
B2	0.40%	0.46%	0.63%	0.70%	0.80%	0.40%	0.24%	732
B3	0.50%	0.54%	0.65%	0.72%	0.82%	0.33%	0.19%	487
B4	0.48%	0.50%	0.65%	0.69%	0.70%	0.22%	0.19%	341
B5	0.30%	0.50%	0.65%	0.76%	0.83%	0.52%	0.26%	314
B6	0.50%	0.50%	0.65%	0.72%	0.75%	0.25%	0.22%	250
B7	0.56%	0.57%	0.65%	0.85%	1.04%	0.48%	0.28%	179
B8	0.30%	0.50%	0.65%	0.73%	0.91%	0.61%	0.22%	1069
B9	0.32%	0.50%	0.60%	0.70%	0.78%	0.46%	0.20%	103

Table 37: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 3

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.01%	0.50%	0.67%	1.64%	1.64%	0.66%	1,285
B2	0.00%	0.15%	0.55%	0.67%	0.74%	0.74%	0.53%	1,141
B3	0.00%	0.06%	0.47%	0.65%	0.73%	0.73%	0.59%	1,017
B4	0.00%	0.09%	0.54%	0.72%	1.35%	1.35%	0.62%	858

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B5	0.00%	0.11%	0.46%	0.68%	0.70%	0.70%	0.57%	760
B6	0.10%	0.34%	0.59%	0.65%	0.77%	0.68%	0.31%	369
B7	0.00%	0.16%	0.49%	0.65%	0.67%	0.67%	0.49%	357
B8	0.26%	0.26%	0.52%	0.65%	0.65%	0.39%	0.39%	277
B9	0.00%	0.06%	0.52%	0.70%	0.84%	0.84%	0.64%	207
B10	0.32%	0.45%	0.61%	0.98%	1.50%	1.18%	0.53%	131
B11	0.00%	0.15%	0.52%	0.65%	0.71%	0.71%	0.50%	120
B12	0.00%	0.02%	0.54%	0.68%	0.70%	0.70%	0.67%	108

Table 38: Variation in rates of upfront commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 4

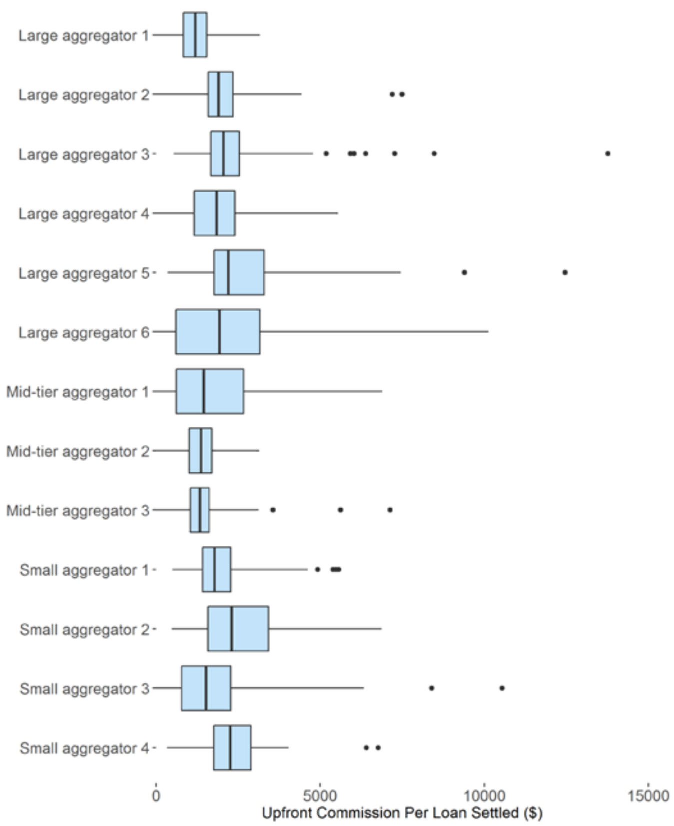
Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.45%	0.46%	0.56%	0.60%	0.61%	0.16%	0.14%	539
B2	0.51%	0.51%	0.62%	0.72%	0.76%	0.25%	0.21%	290
B3	0.50%	0.52%	0.60%	0.69%	0.74%	0.24%	0.16%	258
B4	0.14%	0.18%	0.37%	0.63%	0.64%	0.51%	0.45%	202
B5	0.33%	0.37%	0.55%	0.65%	0.72%	0.39%	0.28%	103

Distribution of upfront commission amounts

1108 We also derived the average per-loan amount of upfront commission passed on to the broker business by the aggregator from the aggregators' yearly loan flow data.

1109 Figure 43 sets out the distribution of the average per-loan value of the upfront commission passed onto the broker business by the aggregator from each lender for 2015.

Figure 43: Distribution of average per-loan value of upfront commission received by broker businesses from each lender for each aggregator



Source: Aggregators' loan flow data

Note: See paragraph 1110 for a description of the trends shown in this figure.

1110 The average per-loan amount of upfront commission passed on to broker businesses by each lender varied from $0 to over $10,000.

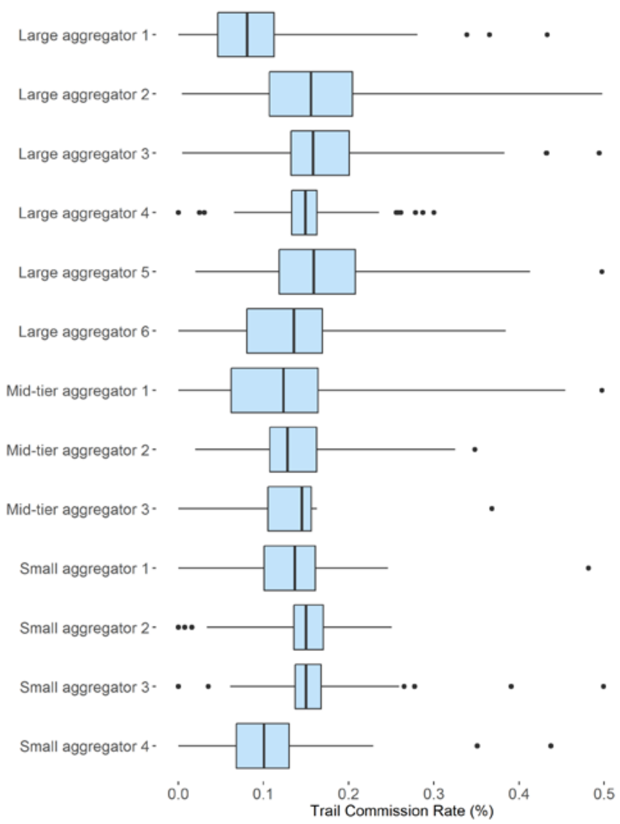
Distribution of rates of trail commission

1111 We also used the yearly loan flow data from aggregators to derive information about the rates and value of trail commission that was passed on to broker businesses by the aggregator.

1112 We derived an estimate of the annual trail commission rate passed on to each broker business by the aggregator for each lender. We did this by dividing the total trail commission for each year by the outstanding balance of home loans disclosed by the aggregator. We note that, as we did not have the month-by-month balance of outstanding home loans (which is used as the basis of calculating trail commission), this rate is an estimate only.

1113 Figure 44 sets out the distribution of those rates in 2015.

Figure 44: Distribution of average rates of trail commission received by broker businesses from each lender for each aggregator



Source: Aggregators' loan flow data

Note: See paragraphs 1114–1116 for a description of the trends shown in this figure.

1114 The median values of the derived rates of trail commission passed on to the broker business from the aggregator ranged from 0.08% to 0.16% of the loan values, with the industry mean being 0.14%.

1115 Within an aggregator, the difference between the rate at the 5th percentile (the lowest paying lenders) and the 95th percentile (the highest paying lenders) ranged between 0.11% and 0.28%.

1116 Across all aggregators, the lowest average annual rate of trail commission passed on to a broker business was 0.00% and the highest average rate was 0.73%.

1117 Table 39–Table 52 set out the range of rates of trail commission paid to individual broker businesses reported on by the aggregators for home loans funded by the ADIs in the review. We have included each broker business that originated more than 100 loans through those ADI lenders in 2015. The tables set out the median, minimum and maximum average rates of trail commission received by the broker businesses. In addition, the tables set out the values at the 5th and 95th percentile.

Note: Commission is calculated as a percentage of the loan amount.

1118 Overall, even when limiting the range of lenders to include only ADIs, the variations in the average rate of trail commission received by brokers are still considerable. Variations tended to be between 0.05% and 0.15%.

Table 39: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 1

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.00%	0.09%	0.12%	0.32%	0.32%	0.12%	1455
B2	0.00%	0.02%	0.07%	0.12%	0.14%	0.14%	0.09%	1422
B3	0.01%	0.03%	0.11%	0.15%	0.25%	0.24%	0.12%	1321
B4	0.01%	0.03%	0.11%	0.16%	0.20%	0.19%	0.13%	1159
B5	0.00%	0.00%	0.05%	0.09%	0.17%	0.17%	0.09%	1091
B6	0.00%	0.00%	0.09%	0.12%	0.12%	0.12%	0.12%	1024
B7	0.00%	0.00%	0.09%	0.15%	0.17%	0.17%	0.15%	763
B8	0.00%	0.00%	0.06%	0.10%	0.11%	0.11%	0.10%	484
B9	0.02%	0.04%	0.08%	0.12%	0.18%	0.16%	0.08%	374
B10	0.00%	0.00%	0.07%	0.12%	0.16%	0.16%	0.12%	242
B11	0.02%	0.04%	0.07%	0.10%	0.13%	0.11%	0.06%	143

Table 40: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 2

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.09%	0.18%	0.25%	0.38%	0.38%	0.17%	10654
B2	0.08%	0.12%	0.17%	0.26%	0.29%	0.22%	0.14%	8789
B3	0.05%	0.11%	0.18%	0.29%	0.63%	0.58%	0.17%	8480

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B4	0.07%	0.08%	0.16%	0.32%	0.59%	0.52%	0.25%	8226
B5	0.06%	0.08%	0.13%	0.18%	0.26%	0.19%	0.10%	3309
B6	0.09%	0.10%	0.13%	0.21%	0.27%	0.18%	0.11%	167

Table 41: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 3

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.08%	0.10%	0.16%	0.25%	0.31%	0.23%	0.16%	7959
B2	0.03%	0.09%	0.13%	0.19%	0.27%	0.24%	0.10%	4475
B3	0.09%	0.11%	0.16%	0.29%	0.31%	0.22%	0.18%	3119
B4	0.02%	0.10%	0.15%	0.32%	0.44%	0.42%	0.21%	1964
B5	0.01%	0.10%	0.18%	0.26%	0.28%	0.27%	0.17%	1707
B6	0.03%	0.04%	0.07%	0.13%	0.19%	0.16%	0.10%	1685
B7	0.01%	0.11%	0.20%	0.27%	0.29%	0.28%	0.15%	1222
B8	0.09%	0.12%	0.16%	0.22%	0.25%	0.16%	0.09%	498
B9	0.01%	0.10%	0.16%	0.26%	0.27%	0.26%	0.16%	320
B10	0.04%	0.06%	0.15%	0.20%	0.26%	0.22%	0.15%	222
B11	0.03%	0.08%	0.18%	0.36%	0.50%	0.47%	0.28%	140

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B12	0.05%	0.08%	0.17%	0.27%	0.28%	0.23%	0.19%	140
B13	0.04%	0.06%	0.12%	0.23%	0.37%	0.33%	0.17%	123

Table 42: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 4

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.07%	0.11%	0.15%	0.20%	0.28%	0.21%	0.09%	7053
B2	0.00%	0.00%	0.13%	0.15%	0.15%	0.15%	0.15%	4110
B3	0.06%	0.08%	0.14%	0.16%	0.22%	0.16%	0.08%	3869
B4	0.00%	0.06%	0.15%	0.17%	0.17%	0.17%	0.11%	3708
B5	0.00%	0.03%	0.13%	0.15%	0.15%	0.15%	0.12%	1156
B6	0.07%	0.10%	0.15%	0.20%	0.21%	0.14%	0.10%	195
B7	0.00%	0.00%	0.13%	0.15%	0.15%	0.15%	0.15%	151

Table 43: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 5

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.08%	0.12%	0.20%	0.32%	0.38%	0.30%	0.20%	4810
B2	0.11%	0.13%	0.18%	0.37%	0.57%	0.46%	0.25%	2804

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B3	0.03%	0.05%	0.13%	0.28%	0.42%	0.38%	0.22%	2159
B4	0.01%	0.02%	0.05%	0.11%	0.12%	0.11%	0.10%	639
B5	0.04%	0.04%	0.05%	0.06%	0.06%	0.02%	0.02%	303
B6	0.02%	0.10%	0.16%	0.24%	0.28%	0.26%	0.14%	133
B7	0.04%	0.10%	0.15%	0.23%	0.30%	0.26%	0.13%	109

Table 44: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Large aggregator 6

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.07%	0.11%	0.15%	0.28%	0.72%	0.65%	0.17%	4959
B2	0.00%	0.00%	0.06%	0.18%	0.26%	0.26%	0.18%	3663
B3	0.03%	0.10%	0.15%	0.21%	0.27%	0.25%	0.11%	3231
B4	0.02%	0.12%	0.16%	0.26%	0.57%	0.55%	0.15%	3180
B5	0.02%	0.06%	0.20%	0.57%	0.74%	0.72%	0.51%	1256
B6	0.05%	0.10%	0.16%	0.31%	0.42%	0.37%	0.21%	641
B7	0.02%	0.12%	0.16%	0.20%	0.21%	0.19%	0.09%	498
B8	0.12%	0.12%	0.25%	0.35%	0.38%	0.27%	0.23%	282
B9	0.11%	0.12%	0.15%	0.27%	0.28%	0.17%	0.15%	150

Table 45: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 1

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.01%	0.06%	0.12%	0.15%	0.15%	0.12%	4209
B2	0.00%	0.00%	0.03%	0.08%	0.12%	0.12%	0.08%	1937
B3	0.00%	0.11%	0.16%	0.25%	0.27%	0.27%	0.14%	1101
B4	0.01%	0.02%	0.06%	0.08%	0.09%	0.08%	0.06%	456
B5	0.03%	0.06%	0.11%	0.17%	0.18%	0.14%	0.10%	363
B6	0.00%	0.01%	0.10%	0.21%	0.23%	0.23%	0.20%	190
B7	0.00%	0.00%	0.08%	0.16%	0.17%	0.17%	0.16%	170
B8	0.04%	0.08%	0.16%	0.24%	0.39%	0.35%	0.15%	112

Table 46: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 2

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.01%	0.09%	0.14%	0.35%	0.48%	0.47%	0.26%	2369
B2	0.03%	0.05%	0.13%	0.22%	0.25%	0.22%	0.17%	2241
B3	0.01%	0.10%	0.16%	0.24%	0.35%	0.34%	0.14%	1972
B4	0.02%	0.06%	0.12%	0.20%	0.54%	0.52%	0.14%	1678
B5	0.02%	0.04%	0.11%	0.21%	0.29%	0.27%	0.17%	1064

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B6	0.02%	0.03%	0.12%	0.21%	0.23%	0.20%	0.18%	715
B7	0.01%	0.03%	0.09%	0.15%	0.16%	0.14%	0.11%	398
B8	0.02%	0.07%	0.14%	0.22%	0.35%	0.33%	0.15%	358
B9	0.00%	0.06%	0.11%	0.17%	0.30%	0.30%	0.11%	302
B10	0.06%	0.07%	0.12%	0.18%	0.27%	0.21%	0.10%	265
B11	0.06%	0.09%	0.17%	0.24%	0.43%	0.37%	0.15%	201
B12	0.01%	0.03%	0.13%	0.17%	0.21%	0.20%	0.14%	131
B13	0.04%	0.07%	0.15%	0.23%	0.28%	0.24%	0.16%	118

Table 47: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 3

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.16%	0.16%	0.16%	0.16%	0.16%	0.01%	3470
B2	0.00%	0.11%	0.16%	0.16%	0.16%	0.16%	0.05%	2336
B3	0.00%	0.11%	0.16%	0.20%	0.20%	0.20%	0.09%	2219
B4	0.00%	0.15%	0.15%	0.16%	0.16%	0.16%	0.01%	2014
B5	0.00%	0.14%	0.15%	0.15%	0.15%	0.15%	0.01%	1746
B6	0.00%	0.14%	0.15%	0.15%	0.15%	0.15%	0.02%	1462

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B7	0.00%	0.16%	0.17%	0.18%	0.18%	0.18%	0.01%	1044
B8	0.11%	0.11%	0.11%	0.12%	0.12%	0.01%	0.01%	851
B9	0.00%	0.07%	0.07%	0.11%	0.11%	0.11%	0.04%	306
B10	0.00%	0.05%	0.09%	0.09%	0.09%	0.09%	0.04%	295
B11	0.00%	0.06%	0.10%	0.14%	0.14%	0.14%	0.08%	247
B12	0.00%	0.04%	0.05%	0.05%	0.05%	0.05%	0.00%	150

Table 48: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Mid-tier aggregator 4

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.02%	0.04%	0.10%	0.15%	0.16%	0.14%	0.11%	1152
B2	0.10%	0.10%	0.16%	0.27%	0.33%	0.23%	0.16%	974
B3	0.00%	0.07%	0.15%	0.19%	0.31%	0.31%	0.12%	954
B4	0.03%	0.09%	0.14%	0.26%	0.56%	0.54%	0.17%	892
B5	0.00%	0.01%	0.07%	0.13%	0.14%	0.14%	0.12%	791
B6	0.03%	0.04%	0.11%	0.17%	0.27%	0.24%	0.13%	320
B7	0.00%	0.02%	0.12%	0.16%	0.18%	0.18%	0.14%	122

Table 49: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 1

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.01%	0.03%	0.11%	0.15%	0.19%	0.17%	0.12%	7169
B2	0.01%	0.10%	0.15%	0.23%	0.26%	0.25%	0.13%	3155
B3	0.01%	0.08%	0.16%	0.23%	0.23%	0.22%	0.14%	2727
B4	0.02%	0.05%	0.16%	0.22%	0.49%	0.47%	0.17%	1802
B5	0.01%	0.07%	0.13%	0.22%	0.26%	0.25%	0.16%	1493
B6	0.07%	0.10%	0.14%	0.23%	0.28%	0.21%	0.13%	203

Table 50: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 2

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.00%	0.08%	0.16%	0.24%	0.25%	0.25%	0.16%	737
B2	0.10%	0.14%	0.16%	0.25%	0.25%	0.15%	0.11%	732
B3	0.13%	0.14%	0.15%	0.25%	0.25%	0.12%	0.11%	487
B4	0.00%	0.03%	0.14%	0.15%	0.56%	0.56%	0.12%	341
B5	0.00%	0.00%	0.13%	0.15%	0.15%	0.15%	0.15%	314
B6	0.00%	0.00%	0.12%	0.15%	0.15%	0.15%	0.15%	250
B7	0.00%	0.00%	0.12%	0.15%	0.15%	0.15%	0.15%	179

Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B8	0.02%	0.12%	0.18%	0.24%	0.25%	0.23%	0.12%	169
B9	0.00%	0.05%	0.15%	0.18%	0.22%	0.22%	0.13%	103

Table 51: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 3

Broker	Min. commission	*5th percentile commission*	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.06%	*0.11%*	0.15%	0.17%	0.21%	0.15%	0.06%	1285
B2	0.02%	*0.09%*	0.14%	0.17%	0.20%	0.18%	0.09%	1141
B3	0.01%	*0.10%*	0.14%	0.18%	0.19%	0.18%	0.08%	1017
B4	0.07%	*0.08%*	0.14%	0.17%	0.21%	0.15%	0.09%	858
B5	0.00%	*0.02%*	0.14%	0.16%	0.17%	0.17%	0.14%	760
B6	0.02%	*0.06%*	0.14%	0.15%	0.16%	0.14%	0.09%	369
B7	0.00%	*0.04%*	0.14%	0.17%	0.19%	0.19%	0.13%	357
B8	0.01%	*0.05%*	0.14%	0.17%	0.18%	0.16%	0.12%	277
B9	0.00%	*0.00%*	0.15%	0.18%	0.19%	0.19%	0.18%	207
B10	0.00%	*0.00%*	0.13%	0.15%	0.15%	0.15%	0.15%	131
B11	0.00%	*0.02%*	0.14%	0.18%	0.19%	0.19%	0.16%	120
B12	0.13%	*0.13%*	0.15%	0.15%	0.16%	0.03%	0.02%	108

Table 52: Variation in rates of trail commissions paid to brokers, between lowest paying and highest paying ADIs (2015)—Small aggregator 4

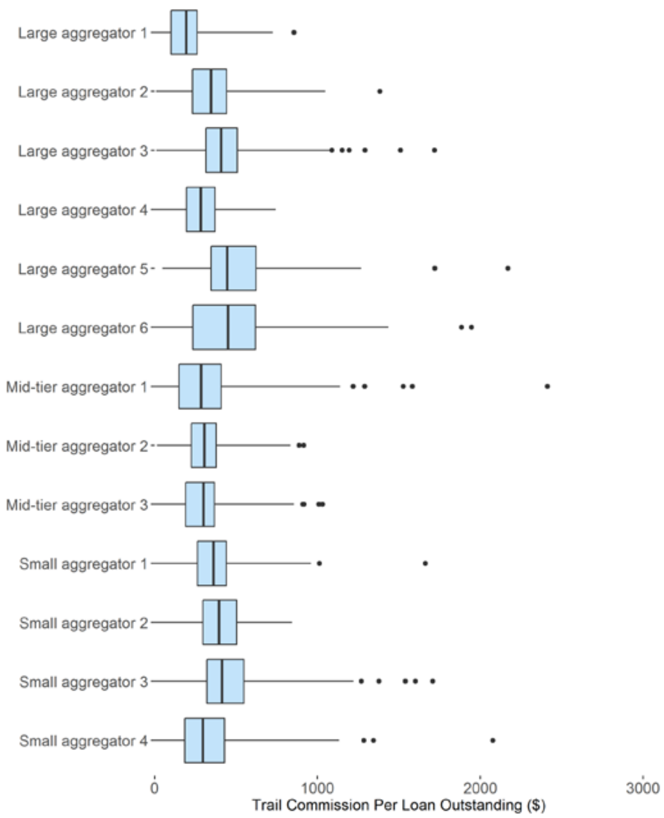
Broker	Min. commission	5th percentile commission	Median commission	95th percentile commission	Max. commission	Difference (max.–min.)	Difference (95%–5%)	Total loans sold by broker
B1	0.05%	0.05%	0.09%	0.20%	0.44%	0.39%	0.15%	539
B2	0.00%	0.00%	0.07%	0.17%	0.23%	0.23%	0.17%	290
B3	0.00%	0.00%	0.03%	0.12%	0.12%	0.12%	0.12%	258
B4	0.00%	0.00%	0.04%	0.15%	0.18%	0.18%	0.15%	202
B5	0.01%	0.04%	0.10%	0.17%	0.17%	0.16%	0.13%	103

Distribution of trail commission amounts

1119 From the yearly loan flow data from aggregators, we calculated the average per-loan amount of trail commission passed on by the aggregator to each broker business from each lender in 2015.

1120 Figure 45 sets out the distribution of those values in 2015.

Figure 45: Distribution of average annual per-loan value of trail commission received by broker businesses from each lender for each aggregator



Source: Aggregators' loan flow data

Note: See paragraph 1121 for a description of the trends shown in this figure.

1121 The average annual per-loan amount of trail commission paid to broker businesses by individual lenders varied from $0 to over $1,000.

Key terms

Term	Meaning in this document
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
accelerated rate of commission	A higher rate of commission (including a flat bonus amount of commission) that is paid on residential mortgages, at a volume-based or non-volume based rate, subject to certain criteria being satisfied. An accelerated rate of commission may be paid as a separate payment to the base rate of commission (e.g. it may be paid annually rather than every month)
accelerator	A feature of a commission structure (either with an aggregator or another type of intermediary) that results in a higher amount of commission per sale (either a higher per sale flat commission amount or a higher percentage commission) based on certain criteria being satisfied
ADI	Authorised deposit-taking institution
AFC	Australian Finance Conference
AFM	Autoriteit Financiële Markten (Netherlands)
AFS licence	Australian financial services licence
aggregator	A business which provides aggregation services to a broker business or broker and with which a lender a direct contractual relationship. It does not include a broker business or broker which does not provide aggregation services, even if there is a direct contractual relationship with the lender. If a lender has a contractual arrangement with an entity for aggregation services and a related party of that entity provides the aggregation services to a broker business or broker, then the two entities are treated as one aggregator
APRA	Australian Prudential Regulation Authority
ASIC Act	*Australian Securities and Investments Commission Act 2001*
balanced scorecard	A tool for measuring an employee's performance in which the variable remuneration (e.g. a bonus) is based on information from a range of measures, including financial/sales, customer feedback, internal business processes, and learning and development. Use of a balanced scorecard means there is a less direct connection between the sale of a product and the remuneration that is actually paid

Term	Meaning in this document
base rate of commission	The rates of upfront and trail commission that apply assuming the broker or other intermediary does not meet the criteria for an accelerated rate of commission
broker business	A sub-aggregator/franchise business or other broker business
broker club	A service offered by the lender under which a broker is given a special status (e.g. a 'gold broker'), subject to meeting certain criteria, which provides benefits to the broker
campaign-based commission structure	A commission structure, potentially including special upfront, trail or accelerated rates of commission, which applies for a short, defined period only
churning	Recommending to a consumer to refinance a loan to obtain commissions, rather than to meet the consumer's requirements and objectives
CIO	Credit and Investments Ombudsman
clawback	See 'commission recovery'
COBA	Customer Owned Banking Association
commission recovery	To take back an upfront or trail commission that has been paid to an intermediary such as a broker
comparison website	A website or other channel through which consumers can compare interest rates (and other features) of home loans and which may give the consumer the ability to contact a lender or go to a lender's website
credit licence	An Australian credit licence
credit licensee	The holder of an Australian credit licence
credit representative	A person who is authorised to engage in specified credit activities by a credit licensee
cross-selling	The practice of selling other products to consumers alongside the principal sale (e.g. selling home and contents insurance with a home loan)
customer-owned banking institutions	Includes mutual banks, credit unions and building societies
EDR	External dispute resolution
FBAA	Finance Brokers Association of Australia
FCA	Financial Conduct Authority (UK)
FOFA	Future of Financial Advice
FOS	Financial Ombudsman Service

Term	Meaning in this document
franchise	A broker business that, under a franchise agreement, provides sub-aggregation services to other broker businesses and brokers under a common brand. It does not include a business that has lender–aggregator agreements directly with lenders
FSG	Financial Services Guide
home insurance	General insurance over a home and contents
home loan	A mortgage loan secured by residential property, not including: • loans for business or commercial purposes; • reverse mortgages; • loans for business or commercial purposes; or • loans to self-managed superannuation funds
introducer	See 'referrer'
lender	Includes a person who has a servicing agreement with a special purpose funding entity
lender–aggregator agreement	The agreement under which the lender agrees to receive applications for residential mortgages originated through the aggregator. It includes any side agreements (e.g. marketing or business support-related agreements). It does not include any agreement (or part of an agreement) between the lender and aggregator where the lender agrees to: • provide a white-labelled residential mortgage product using a brand of the aggregator, or • appoint the aggregator as a mortgage manager
lender choice conflict	A conflict of interest arising from commission structures in the mortgage broking market where a broker recommends a loan from a particular lender because the broker will receive a higher commission (whether from that lender generally or for that particular loan product) even though that loan may not be the best loan for the consumer
lender's mortgage insurance	Insurance to protect the lender against financial loss if a borrower defaults on a home loan and the proceeds from the sale of the security property do not cover the unpaid loan balance and related expenses
LMI	Lender's mortgage insurance
LVR	Loan-to-valuation ratio
MFAA	Mortgage & Finance Association of Australia

Term	Meaning in this document
mortgage manager	An intermediary between the funder/lender and the consumer. The key characteristic of a mortgage manager is that the manager presents itself as a product distributor rather than a broker
mortgage manager who also acts as an aggregator/broker business	A business that acts as a mortgage manager for particular residential mortgages, but which predominantly provides [aggregation/broking] services
National Credit Act	*National Consumer Credit Protection Act 2009*
National Credit Regulations	National Consumer Credit Protection Regulations 2010
non-volume based	Something that is dependent on criteria other than sales (or referrals) of residential mortgages (e.g. quality criteria such as the conversation rate of applications into loans)
non-volume based accelerated rate	An accelerated rate of commission that is dependent on non-sales based criteria being satisfied (e.g. quality criteria such as the conversion rate of applications into settled loans). The accelerated rate may be paid for mortgages settled when the criteria for the rate were met or for all mortgages during a certain period
non-white label loan	Residential mortgages issued under a brand of the lender
offset account/facility	A transaction account that is linked to a loan account so that some or all of the balance in the transaction account ‘offsets’ the loan principal. Interest is then calculated on the loan principal minus the offset account balance. This includes similar facilities offered by non-ADI lenders
other broker business	A broker business that is not a franchise business or sub-aggregator
omnibus survey	A method of quantitative market research where data on a wide variety of topics is collected during the same interview, allowing multiple clients to share the cost of conducting research
other deposit product	A basic deposit product offered by an ADI, other than a transaction account. This includes term deposit accounts and online savings accounts
package	A home loan package with a discounted interest rate and possibly including other non-mortgage benefits such as a credit card. Packages often have a package fee structure distinctly different from the fee structure on standard loans
premium loan	A fully featured home loan that includes an offset facility, including after a loan ceases to be a fixed rate loan

Term	Meaning in this document
product strategy conflict	A conflict of interest arising from commission structures in the mortgage broking market where a broker recommends a higher value loan than the consumer originally sought or needed to maximise their commission payment. This may also involve recommending a particular product or strategy to maximise the amount that the consumer can borrow
product recommendation software	Any software program that is provided to brokers to assist with the process of choosing a loan to recommend to a consumer
professional services business	Accountants, lawyers, tax agents, financial advisers, migration agents, real estate agents and similar business offering professional services. It does not include property developers, retail businesses or businesses offering personal services (e.g. hairdressers, doctors)
RBA	Reserve Bank of Australia
reg 27 (for example)	A regulation of the National Credit Regulations (in this example numbered 27), unless otherwise specified
referrer/introducer	A person who, under agreement with the lender or a referrer aggregator, identifies potential sales opportunities for a lender and, without making any recommendation about the loan to the consumer, either: • tells the consumer how they may contact the lender or referrer aggregator; or • obtains and provides the consumer's details to the lender or referrer aggregator. Unless the person is in the business of making referrals, the referrer/introducer is likely to rely on the licensing exemptions in the National Credit Regulations (and is sometimes known as a 'mere referrer')
s47 (for example)	A section of the National Credit Act (in this example numbered 47), unless otherwise specified
senior management	Managers who have significant influence over or control of the operation of a business
soft dollar benefits	Any rewards or benefits that are not cash
staff	This includes: • any employee of the lender; • any person (whether an employee or not) who operates under the lender's own brand and only sells, or provides customer services for the lender's own residential mortgages (e.g. product advisers who operate under a franchise model with the lender); and • mobile lending or branch staff who operate under a franchise model with the lender (regardless of the contractual or licence situation)

Term	Meaning in this document
standard commission structure	The commission structure that ordinarily applies under the lender–aggregator agreement (although it may be changed from time to time) and which is not offered on a short-term, campaign basis. It includes base rates of upfront and trail commission, accelerated rates of commission and commission recovery provisions
sub-aggregator	A business that provides aggregation services to a broker business or broker where there is no direct contractual relationship
term sheets	Written documents setting out the agreed terms between lenders and aggregators or brokers. These documents include contracts and letters of variation
threshold	Minimum criteria (either volume-based or non-volume based) that must be satisfied for any commission to be paid
trail commission	A regularly recurring commission to an intermediary, such as a broker. The commission is normally a small proportion of the current or average loan balance
transaction account	A basic deposit product offered by an ADI that is intended to be used for day to day purchases and other transactions
upfront commission	An initial commission to an intermediary, such as a broker, which is generally once-off and paid after settlement. The commission is normally a proportion of the settled amount, drawn amount, or a portion of the approved limit
volume-based	Something that is dependent on sales (or referrals) of residential mortgages
volume-based rate	An accelerated rate of commission that is dependent on the total sales of residential mortgages in a defined period of time. The accelerated rate may be paid for mortgages settled when the criteria for the rate were met or for all mortgages during a certain period
white label loans	A residential mortgage issued by the lender under a brand owned or controlled by someone else (e.g. an aggregator or broker business)
white label agreement/ relationship	An agreement/relationship with someone else (e.g. an aggregator or broker business) under which the lender issues white label loans. Compared to a mortgage manager relationship, the other party (e.g. aggregator or broker business) is not usually responsible for underwriting or managing the loans

Related information

Headnotes

ADIs, aggregators, bonus payments, borrower characteristics, broker businesses, campaign-based commissions, comparison websites, conflict of interest, consumer credit, credit licence, credit representative, customer-owned banking institutions, governance, home loans, lenders, loan flow data, mortgage brokers, mortgage broking market, non-ADIs, non-volume based incentives, ownership, referrers, remuneration, soft dollar benefits, trail commissions, upfront commissions, volume-based commissions

Regulatory guides

RG 203 *Do I need an Australian credit licence?*

RG 205 *Credit licensing: General conduct obligations*

RG 206 *Credit licensing: Competence and training*

RG 209 *Credit licensing: Responsible lending conduct*

Legislation

ASIC Act, Pt 2, Div 2

Australian Consumer Law

Corporations Act, Ch 7

National Credit Act, s5, 29, 31, 47, 113, 121, 158, 180A

National Credit Code, s16, 17(14), 204

National Credit Regulations, reg 25, 26, 26A(2)–(3), 27, 27A, 27B, 28G, 28H, 28P, 72

Responsible Lending Code (NZ)

UCCC

Consultation papers and reports

REP 19 *A report to ASIC on the finance and mortgage broking industry*

REP 330 *Review of licensed credit assistance providers monitoring and supervision of credit representatives*

REP 445 *Review of interest-only home loans*

REP 493 *Review of interest-only home loans: Mortgage brokers' inquiries into consumers' requirements and objectives*

Information sheets

INFO 146 *Responsible lending disclosure obligations—Overview for credit licensees and representatives*

Non-ASIC documents

APRA, *Quarterly authorised deposit-taking institution property exposures* June 2016 (released 30 August 2016)

APRA, APG 223 *Residential mortgage lending*

CHOICE, *Mortgage broker shadow shop*

Deloitte, *Australian mortgage report 2016*

Ernst & Young Australia, Observations on the value of mortgage broking: Prepared for the Mortgage & Finance Association of Australia

FCA, FS16/3 *Feedback statement on call for inputs on competition in the mortgage sector*

FCA, MS16/2 *Mortgages market study*

MFAA, *Inquiry into competition in the banking and non-banking sectors: Submission by the Mortgage and Finance Association of Australia* (PDF 465 KB)