2 June 2014

ASIC's Deregulatory Initiatives

Introduction

This submission is lodged on behalf of the Mortgage and Finance Association of Australia (MFAA).

The MFAA is the peak national body providing service and representation to over 10,000 professional credit advisers (mortgage and finance brokers, mortgage managers and aggregators) to assist them to develop, foster and promote the mortgage and finance industry in Australia.

We thank ASIC for the opportunity to contribute to deregulatory initiatives. Given the MFAA's remit, our comments are solely focussed on aspects relating to credit, and in particular on the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**).

Our submission is broken into two sections:

- substantive initiatives; and
- fine-tuning initiatives.

Executive summary of our substantive submissions

1. Simplify the disclosure regime for finance brokers and rationalise when disclosure must be given.
2. Remove the duplication in credit assessment.
3. Remove the need for family companies of brokers to be licensed or appointed as credit representatives.
4. Clarify the situation for older borrowers.
5. Permit electronic communications without the need for consent.

Substantive matter 1 Simplify the disclosure regime for finance brokers and rationalise when disclosure must be given

The NCCP Act and the regulations specify a very complex process for disclosure by finance brokers of relatively simple information to prospective borrowers of regulated credit.

The legislation as originally passed has been amended and modified many times by regulation making the current law very inaccessible and unnecessarily complex.

The timing for disclosure and the requirements for disclosure are specified in the following table.

Document	Key purpose	When must the disclosure be made?
Credit Guide by licensees	General information about the licensee's business, including IDR and EDR information	As soon as practicable after it becomes apparent to the licensee that it is likely to provide credit assistance – s113. For consumer leases – s136
Credit Guide by credit representatives	As above	As soon as practicable after it becomes apparent that the credit representative is likely to provide credit assistance – s158. May be combined with the licensee's Credit Guide - r 28L(9).
Quote	Fees payable by the borrower to the credit assistant for brokerage services	Before providing credit assistance – s114. For consumer leases, see s137.
Proposal Disclosure Document (PDD)	Disclosure of commissions paid to the broker by third parties	At the same time as providing credit assistance – s121. For consumer leases, see s144.

It will be seen that in many cases three documents are required when we maintain one would better serve industry and consumers. The disclosure regime for brokers is currently more complex than the disclosure regime for lenders, which seems disproportionate having regard to the role that the parties play.

Change the timing of the application process

Section 123 of the NCCP provides that brokers must not provide credit assistance by suggesting that a consumer apply, or assisting the consumer to apply, for a particular credit contract with a particular credit provider until **after** the broker has conducted a preliminary credit assessment.

However, in practice, brokers will often suggest a particular product with a particular lender **before** conducting a preliminary credit assessment. For example, a broker might complete an application form for Bank A in order to make the required reasonable enquiries and verification. If these enquiries do not result satisfactorily, the application is not lodged. It could be argued that this activity comprises a suggestion or assistance in relation to a specific credit contract with a specific credit provider in breach of section 123.

Accordingly, in practice, a specific loan with a specific lender is usually 'suggested' and 'assistance' commences very early in a finance broker's process. So the suggesting and assisting comes before the preliminary credit assessment and not after – as is the current legal requirement. The requirement should be amended so that brokers must not lodge an application with a lender for a specific loan until the preliminary credit assessment has been conducted. You will see below that we also recommend that the nature of preliminary assessments should change – see Substantive Matter 2.

Rationalise the disclosure documents

Although the law allows the combination of the Credit Guide, Quote, and PDD into a single document, ASIC has in the past expressed doubt as to whether that is possible having regard to the timing specified in the legislation.

In practice, brokers often deal with the whole application process as part of the single meeting.

We suggest a simplified disclosure regime comprising a single document titled 'Credit Guide' which comprises a statement of:

- the licensee's name, contact details, and ACL;
- if applicable, the credit representative's name, contacts details, and CR number;
- the scope of works to be undertaken by the broker;
- the fees payable by the borrower to the broker (if any) and when these fees are payable;
- a list of the broker's panel lenders, but if there are more than six panel lenders, the broker need only list the six with whom the licensee reasonably considers it conducts the most business;
- a description of the types of commission the broker receives. The disclosure should only be in respect of the individual dealing with the consumer or if the person is an employee, the employer of that person, indicating the highest likely commission by dollar amount or by method of calculation;
- a statement that there is a volume bonus arrangement if there is one; and
- details of the broker's IDR and EDR.

This rationalisation of the disclosure documents will:

- simplify the law significantly;
- encourage compliance by brokers;
- assist understanding by consumers; and
- save considerable costs for industry.

Substantive matter 2 Remove the duplication of credit assessment

When the legislation was being workshopped by the Treasury industry working group, the intention was that brokers would conduct a 'preliminary' credit assessment. 'Preliminary' was understood to be something less than a complete duplication of the full credit assessment that lenders are required to undertake.

Over time this interpretation has been completely lost, and brokers are now being required to conduct a full responsible lending assessment. Preliminary has changed from meaning 'light touch' to 'first'.

This is an unnecessary and unwarranted duplication of work, particularly in relation to borrowers whose affairs are not simple (and this includes all non-PAYG earners). We appreciate that lenders are entitled to rely on the due diligence undertaken by brokers, but many don't for various reasons. In particular if lenders do rely on due diligence undertaken by brokers, the lender is still liable if the broker gets it wrong.

There is no commercial or other reason for this duplication. The protection which the legislation seeks to provide to consumers is that they will not enter unsuitable loans. At the end of the day that is the responsibility of the lender, and the objective is achieved by placing the material obligation on lenders.

This second due diligence and assessment creates a number of problems.

1. Significant and unnecessary inconvenience for accountants, employers, and the customer occurs.

2. There are many cases where brokers have rejected applications for responsible lending reasons and subsequently lenders have approved them. The opposite also occurs. This causes significant confusion for consumers, and significant expense for industry.

We recommend that the original concept of preliminary credit assessment should be reinstated and that there should be no need for verification to be undertaken by brokers if that is to be undertaken by lenders. Either the broker or the lender (as agreed between them) should conduct the verification – but not both.

In addition, the law should remove the need for brokers to have a credit policy and conduct a formal credit assessment because that duplicates what lenders do. Rather, brokers should be *reasonably satisfied that the loan is not unsuitable* without the need to hold evidence of that. This change is particularly important for non-prime loans where the current regime scares many brokers away from helping customers who need assistance.

Substantive matter 3 Remove the need for intermediary family companies of brokers to be licensed or appointed as credit representatives

Many brokers operate through family companies. This occurs for:

- taxation purposes;
- image purposes (branding); and
- because lenders and aggregators do not wish to deal with individuals directly in case the individuals are classified as employees.

When the legislation was drafted, the idea behind 'intermediaries' being required to hold a licence was to ensure that aggregators and other service providers were required to be licensed.

It was not realised at the time that the term 'intermediary' would extend to family companies. Accordingly, an outcome quite different from the AFSL regime resulted. Under the AFSL regime family companies are not required to be licensed or authorised. Instead the individual is directly authorised by the licensee.

The need for family companies to be appointed can create additional cost through:

- professional indemnity insurance for the intermediary;
- preparation of appointment documents and notification of appointment to ASIC;
- administrative costs of appointing them;
- EDR membership costs;
- confusion to industry (often the appointment regime is not properly followed).

We submit that intermediary companies who have no active role in providing 'credit assistance' or in the introduction of customers to lenders should not be required to hold a licence or be appointed as credit representatives.

Substantive matter 4 Clarify the situation for older borrowers

Industry remains confused and inconsistent in relation to providing home loans to older borrowers aged, say, 50 years plus. This is because most home loans have terms of 25

years or longer, and that term may expire after the expected retirement age of the borrower.

ASIC's assistance in RG209.105 is helpful, but the problem persists.

The issue arises because of the provision in the NCCP Act that a loan will be presumed unsuitable if it could only be repaid from the sale of the family home. The law should be amended to make it clear that acceptable exit strategies include circumstances when borrowers state that they are prepared to sell their property at an appropriate time. This should not be linked to age – as people may have plans to renovate and sell, or relocate at other times in their life.

Substantive matter 5 Permit electronic communications without the need for consent

Industry increasingly wishes to use electronic communication and consumers increasingly expect it. The law in relation to electronic communications so far as it relates to credit is complex and unnecessary.

In relation to the lending process, written consents are required as specified in the *Electronic Transactions Regulation 2000* (Cth).

Another regime has been established for disclosure documents in Regulation 28L of the NCCP Regulations which has been clarified in turn by ASIC Class Order 10/1230. The result is that a verbal consent can be obtained for disclosure documents. Verbal consents can also be used for pre-contractual statements but this is of limited utility as pre-contractual statements are usually contained in credit contracts and credit contracts cannot be served without written consent.

The requirement for verbal consent and written consent is out of date. The requirement should simply be that the licensee has a reasonable expectation that the recipients will receive the documents.

The use of paper is ecologically unsound and the use of post delays transactions and adds to cost. Consumers are confused when they receive literally hundreds of pages of documents. Consumer's understanding will be assisted if documents are delivered electronically.

Part 2 – Fine Tuning Proposals

These items are listed in no particular order. Some of these proposals overlap the substantive proposals, and may be able to be implemented more easily and quickly.

	Item	Discussion
1	Allow Proposal Disclosure Documents to state that volume bonus commission is unascertainable.	Reg 28G(8) NCCP Regulations currently requires a reasonable estimate of the maximum amount of commission to be stated. Usually this will not be ascertainable.
2	Abandon Key Fact Sheets for home loans.	Lenders report that KFSs are rarely, if ever, requested. Maintaining systems to produce a document rarely asked for and of questionable information value is inappropriate and adds to compliance costs unnecessarily.

3	If KFSs are not abandoned, amend the prescribed form to remove the requirement to delete reference to 'government requirement'.	Paragraph 2.4 of Part 2 of Schedule 5 NCCP Regulations. Removing the reference to 'government requirement' in circumstances when the law doesn't strictly require a KFS is administratively difficult and pointless.
4	If KFSs are not abandoned, amend the prescribed form to more clearly state what happens at the end of a fixed rate term.	
5	Abandon comparison rates.	They are of limited customer value, and can be misleading. The requirement to disclose comparison rates and a prescribed warning makes advertising complex and confusing.
6	If comparison rates are retained, amend the prescribed amounts given inflation since the figures were set.	Change $150,000 for 25 years to $250,000 for 25 years and $300,000 for 30 years
7	Allow finance brokers to disclose all their panel lenders, and not just the six with whom they do the most business.	The 'big six' frequently changes, and so ensuring compliance with this requirement is complex and may be anti-competitive. Providing a list of all panel lenders is more useful to consumers. Both options should be available. This is to confirm a practice which Treasury has previously advised is acceptable, and is widely adopted in the industry.
8	Amend and shorten the Information Statement.	It is long and as a result usually not read – especially in the context of electronic transactions.
9	Create a new Information Statement for SACCs.	The current Information Statement is not suitable for SACCs.
10	Allow verbal consents to be given to the provision of NCCP documents electronically.	Currently, written consent (which itself may be electronic) is required before electronic communications can be used. As the use of post is reducing dramatically, this impediment to the use of electronic communications should be removed, so long as the consent is given clearly, and the form of consent is contained in the first electronic communication (to inform consumers of what they have consented to).
11	Allow finance brokers to obtain credit reports for the purpose of assisting an individual to apply for finance.	Currently brokers are required to obtain this information as an 'access seeker' as agents for individuals. Efficiency would be improved if brokers could obtain these reports once they have been retained by an individual.
12	Allow a combined FSG and Credit Guide for businesses which are authorised to conduct both activities.	Finance brokers may be appointed as a credit representative of an Australian Credit Licensee, and as an authorised representative by a different company holding an AFSL. Combined guides would provide more useful and concise information and reduce business costs.

13	Clarify whether an Australian Credit Licensee can appoint an employee of another Australian Credit Licensee as a credit representative.	The NCCP is silent on this point.
14	Clarify what triggers a hardship application.	ASIC is currently attempting to provide guidance on this topic. The 1 March 2013 amendments read literally mean that every time a borrower fails to pay, a hardship application could be triggered. This was not the legislative intention. The intention was to make it easier for borrowers to apply for hardship relief, but not to create a flood of unnecessary applications.
15	Provide that a hardship application cannot be made after: • a s 88 default notice has expired; • a judgement for debt or possession has been obtained; • the term of the loan has expired.	This is to prevent abuse of the hardship relief provisions.
16	Limit the role of EDRs to loans of $1m or less and financial services of $500K or less.	This change is needed to avoid abuse by individuals and small businesses of this free dispute resolution system. It will free the schemes up to perform better for their target audience – 'real' consumers.
17	Provide that variations of loans without principal increases documented by new credit contracts don't trigger new responsible lending obligations.	The NCCP Act requires a new credit assessment in respect of each 'credit contract' as distinct from each provision of new or additional finance. For systems reasons, some lenders document loan variations (eg switch from variable to fixed or from principal and interest repayments to interest only repayments) by preparing new credit contracts. The use of a new credit contract triggers a requirement for a new responsible lending assessment by brokers and lenders (which is not the intention of the legislation). Finance brokers don't know which method a lender will use, and so don't know whether to conduct a new credit assessment.

18	Allow interest in advance to be paid when a loan switches to an investment loan.	Interest cannot be paid in advance in respect of most consumer finance, but can be paid (and debited) in advance in respect of loans for residential real estate investment. If a borrower decides to change the use from being the borrower's principal place of residence to an investment property, the NCCP Act does not currently allow interest to be paid in advance. Reg 78 deals with an investment loan that becomes a personal domestic or household loan, but not vice versa.
19	Amend Reg 28H(3)(c) to provide that the maximum interest rate appears on the manager's website (instead of the lender or lessor).	This is to reflect the intention of the regulation as previously advised by Treasury, and is widely adopted in the industry.
20	Amend s13A of the National Credit Code to better describe a reverse mortgage.	Section 13A(2) provides that one of the conditions for a loan to be a reverse mortgage is for '*the debtor's total liability* [to] *exceed* [the amount lent] *without the debtor being obliged to reduce that liability'.* This is difficult to understand given the debtors are required to repay the loan if they sell, vacate, die, or certain other events occur.
21	Amend s84A of the National Credit Code which limits the amount a lender can recover under a reverse mortgage.	If a property has been damaged, the amount the lender can recover should be the market value plus the loss of value caused by the deliberate damage. The section should specify that the lender can select the valuer (currently there is no statement as to who chooses the valuer).
22	Review point of sale exemption, especially as it applies to motor vehicle dealers	The MFAA seeks total removal of this exemption.
23	Amend responsible lending obligations on credit assistance providers so that the test is less prescribed.	Currently brokers are required to conduct a 'preliminary credit assessment' which is exactly the same as required of lenders. This causes confusion when a consumer passes the assessment of either the broker or the lender but is declined by the other. 'Preliminary credit assessment' should be reworked to remove the requirements for a credit policy and a formal assessment, and become a true *preliminary* or *incomplete* assessment, with brokers having an obligation not to provide credit assistance in respect of a loan which has been reasonably reviewed and found not unsuitable. Consumers are protected because the final decision whether credit is provided still lies with the lender.

24	Brokers and managers who sell only one credit provider's products should not be required to comply with the qualification and CPD requirements of a 'third party home loan assistant'.	RG206 has been interpreted by ASIC to require these brokers to comply with the higher standard applicable to brokers who offer a range of home loans. This places artificial and unnecessary barriers on outsourcing.
25	Section 144 NCC provides that insurance must not be financed for more than one year. Amend s144 NCC to remove the unfair consequence which occurred in relation to tyre and rim insurance where consumers kept the insurance but lenders had to refund the insurance premiums.	
26	Amend s17(8) NCC to limit the requirement to show total fees to loans that would be paid out within seven years.	This is to conform with the limitation on showing total interest charges and total repayments in s17(6) and 17(7). Showing the total for longer terms is misleading as the vast majority of loans do not run for longer than seven years.
27	ASIC could outsource minor complaints about credit licensees and their representatives	We suspect that ASIC receives a substantial number of complaints about credit industry participants. Dealing with these minor matters can be time consuming and may divert ASIC resources from more important matters. ASIC should have the power to refer matters to self-regulatory bodies such as the MFAA. There could be an MOU on such issues with the MFAA which would require issues to be referred back to ASIC if warranted. The MFAA would be obliged to inform ASIC on the outcomes of all referred matters.
28	Amend service provisions to allow a single envelope to be used when serving a credit contract on joint borrowers who co-habit, and allow a single copy to keep to be given.	Section 194(3) NCCP Act provides that joint nominations do not apply to pre-contractual statements. However, s194(3) has been modified by regulation 28L and CO 10/1230 such that pre-contractual statements can be given in other ways. In particular, clause 6(d) of the class order provides that *'(d) If a disclosure document is not given to a debtor personally, or to a person acting on debtor's behalf, the credit provider must be reasonably satisfied that the debtor has received the disclosure document before engaging in further credit activities in relation to the debtor's credit contract. A person is not acting on the debtor's behalf if the person is engaging in credit activities.'*

		Usually pre-contractual statements are included in credit contracts. The class order does not extend to credit contracts and so each borrower still has to be served in separate envelopes a copy of the credit contract, the terms and conditions incorporating in the credit contract, the mortgage, and mortgage common provisions to keep. The use of separate envelopes and the provision of separate copies complicates matters for consumers and reduces understanding. It adds cost for industry. Joint nominations should be allowed for pre-contractual statements for joint borrowers who co-habit, or better still the class order should be expanded to relate to service of credit contracts and mortgage documents.