



**ASIC**

Australian Securities & Investments Commission

**REPORT 526**

# Survey of marketplace lending providers

June 2017

## About this report

This report provides an overview of the marketplace lending industry, based on the findings from ASIC's survey of a limited cross-section of marketplace lending providers in November 2016. This was our first survey on the marketplace lending industry.

This report explains:

- marketplace lending and current regulation;
- how we conducted the survey;
- findings from the survey; and
- our activities relating to marketplace lending.

### About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

**Consultation papers:** seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

**Regulatory guides:** give guidance to regulated entities by:

- 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
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

**Information sheets:** provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

**Reports:** describe ASIC compliance or relief activity or the results of a research project.

### Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

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

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# Executive summary

## Background

- 1 Marketplace lending is a relatively new type of technology-based arrangement that allows investors to invest in loans to consumers and small to medium enterprises (SMEs). Marketplace lending can offer an alternative source of funding for consumers and SMEs to more traditional channels.
- 2 In most cases, marketplace lending arrangements involve the provision of financial services and/or credit activities that are regulated by ASIC.

## Our survey of marketplace lending providers

- 3 As part of our role in regulating marketplace lending, we have engaged with marketplace lending providers to better understand their business models.
- 4 In August 2015, we held a roundtable with the marketplace lending industry where we outlined plans to issue guidance and conduct a periodic industry survey. Following the roundtable and consultation with marketplace lending providers, in March 2016 we published [Information Sheet 213](#) *Marketplace lending (peer-to-peer lending) products* (INFO 213), which gives guidance on the regulatory requirements for marketplace lending providers. In November 2016 we conducted a voluntary survey of a limited cross-section of the marketplace lending industry. This report sets out our findings from that survey.
- 5 This report should be read in the context of the objective of the survey, which was to provide ASIC with a greater understanding of the marketplace lending industry in Australia. The survey asked questions about the business model, level of activities and some risk indicators of each of the surveyed marketplace lending providers.
- 6 The report is based on survey responses from nine entities. One of the respondents was unable to provide responses to the second part of the survey as it had not operated for the full period. While the respondents represent the major portion of the industry, it is important to recognise that the survey was not a census of the entire industry and so the results may not necessarily be reflective of the overall marketplace lending industry in Australia. The report does not cover more traditional investments in loans, such as contributory and pooled mortgage schemes.
- 7 We reviewed the survey results and, where possible, sought clarification with the respondents. However, some questions were interpreted by

respondents differently, which may affect the aggregation and/or comparison of the responses.

- 8 The report highlights the key findings from the survey. This report is not meant to be a comprehensive summary of all responses received. It is also not meant to be a detailed report on every question from the survey.

## Survey findings and observations

- 9 As anticipated, the survey confirmed that marketplace lending business models are diverse. Each of the survey respondents has a different business model and level of activity. Most respondents are in the early stages of their business, with most providers commencing operation in the last two years.
- 10 In the 2016 financial year, the respondents have written \$156 million in loans to consumers and SMEs. The funding of these loans was sourced from retail and wholesale investors, including trustees of self-managed superannuation funds (SMSFs). As marketplace lending is a relatively new product that we are aware is being promoted to SMSFs, we sought information regarding the take up by trustees.
- 11 Most revenue was generated from loan origination, with ongoing fees (such as those linked to loan repayments) making up a much smaller proportion, likely at least partially due to the generally short periods of operation to date. Default levels and numbers of complaints received by providers were generally very low at this stage.
- 12 The business models described in the responses to the survey show some conflicts of interest that marketplace lending providers must manage, including conflicts between:
- (a) the need to continue to originate loans to generate revenue and maintaining an appropriate credit assessment standard to meet responsible lending obligations, if applicable, and acting in the best interests of members of the managed investment schemes they operate;
  - (b) duties towards borrowers, including responsible lending, and duties to investors.

## ASIC's role and related activities

- 13 In addition to conducting the survey, we have undertaken a number of activities in relation to marketplace lending, including:

- (a) granting waivers to a number of marketplace lending providers to facilitate their business model without compromising appropriate protections for investors;
- (b) surveillance activities in relation to advertising and disclosure by marketplace lending providers. We have required operators to make corrective disclosure in some instances to address issues identified, including:
  - (i) inadequate disclosure of the key features and risks of the product;
  - (ii) inadequate disclosure about the withdrawal rights (if any) that are available to investors; and
  - (iii) inappropriate comparisons with banking products or with the products offered by other marketplace lending operators; and
- (c) engaging with providers to ensure that they hold an appropriate Australian financial services (AFS) licence to issue interests in a wholesale scheme in connection with marketplace lending.

14 We have also engaged with 34 potential providers through ASIC's Innovation Hub, since it was established in March 2015 to the end of April 2017, to assist them in understanding the regulations that may apply to their business.

15 As marketplace lending continues to develop and grow, it will remain important for providers to recognise the key risks and potential conflicts of interests that may arise. Our guidance in INFO 213 about the regulatory requirements that apply to marketplace lending, along with the good practice examples, can assist providers in managing their risks and conflicts. While compliance with the regulatory requirements will not remove the risks and conflicts, it will help marketplace lending providers to manage them and deliver the potential benefits of marketplace lending to borrowers and investors.

16 We will continue to monitor industry developments by engaging with marketplace lending providers and other loan-based managed investment scheme providers in the future.

## A Background

### Key points

Marketplace lending involves investment through managed investment schemes or other arrangements in loans made to businesses and individuals.

We published guidance in March 2016 to assist industry participants understand the regulatory requirements for marketplace lending.

### What is marketplace lending?

- 17 Marketplace lending generally describes an arrangement through which retail or wholesale investors, who are seeking to earn a return, invest money that is then lent to borrowers. Those borrowers may be consumers or businesses.
- 18 Marketplace lending is generally the term used to describe arrangements that involve the use of an online platform, usually a website. Investors provide information such as the desired interest rate and loan term and either select the loan/s they wish to invest in or are matched with borrowers by the platform. Borrowers provide certain information to the platform, which determines the level of credit risk, amount of loan(s) and interest rate offered to the borrower.
- 19 The concept of investing in loans is not new. Marketplace lending, however, has seen the emergence of investment in loans that in most cases involves the matching of investors and borrowers facilitated by technology. Marketplace lending can offer an alternative source of funding for consumers and SMEs to more traditional channels.

### Marketplace lending structures

- 20 Through our engagement with marketplace lending providers and potential providers, including through ASIC's Innovation Hub (see paragraphs 146–149), we are aware that different business models may be used to provide marketplace lending products, including:
- (a) managed investment schemes;
  - (b) the issue of derivatives;
  - (c) the operation of a financial market; and
  - (d) the issue of securities.

## Regulation of marketplace lending

- 21 The International Organization of Securities Commissions (IOSCO) conducted a survey of 23 of its nation state members in 2015 about the regulation of crowd-sourced funding, including marketplace lending (referred to as peer-to-peer lending by IOSCO). In its [Crowdfunding: 2015 survey responses report](#) (PDF 0.5 MB), IOSCO observed that the regulatory framework for marketplace lending varies across the 23 surveyed countries.
- 22 There is no bespoke regulatory regime for marketplace lending in Australia. The regulations that apply to marketplace lending depend on how the business is structured, what financial services and products are being offered and the types of investors and borrowers involved. In most cases, we have identified that the provision of marketplace lending products involves the operation of a managed investment scheme, which would require the marketplace lending provider to hold an AFS licence. Where the loans made through the platform are consumer loans (i.e. loans to individuals for domestic, personal or household purposes), an Australian credit licence (credit licence) is also required.

## Relevant ASIC guidance

- 23 Existing regulatory guidance for AFS licensees and operators of managed investment schemes is relevant to marketplace lending providers.
- 24 We have also issued guidance on regulatory requirements for credit licensees, which is relevant to marketplace lending providers that provide consumer loans. This guidance includes:
- (a) [Regulatory Guide 203](#) *Do I need a credit licence?* (RG 203);
  - (b) [Regulatory Guide 205](#) *Credit licensing: General conduct obligations* (RG 205); and
  - (c) [Regulatory Guide 209](#) *Credit licensing: Responsible lending conduct* (RG 209).
- 25 However, in recognition of the need to provide tailored guidance for marketplace lending providers to complement existing guidance, we issued [Information Sheet 213](#) *Marketplace lending (peer-to-peer lending) products* (INFO 213) in March 2016 after consultation with industry.
- Note: INFO 213 describes the regulatory framework for marketplace lending.
- 26 [Regulatory Guide 97](#) *Disclosing fees and costs in PDSs and periodic statements* (RG 97) is relevant to marketplace lending providers that operate registered managed investment schemes.



- 27 We recently issued [Regulatory Guide 259](#) *Risk management systems of responsible entities* (RG 259), which gives specific guidance on how these entities may comply with their obligation under s912A(1)(h) of the Corporations Act to maintain adequate risk management systems. This guide is also relevant to operators of unregistered managed investment schemes.

## B Our survey of marketplace lending providers

### Key points

We surveyed a cross-section of marketplace lending providers to:

- better understand their business models and activities;
- identify the risks involved with marketplace lending; and
- enable us to appropriately monitor and respond to these risks.

### Why we undertook the survey

- 28 Marketplace lending is a relatively new technology-based business model in Australia involving the provision of credit and financial services. From our experience in regulating marketplace lending, we have found a great variation in business models, which has an impact on:
- (a) risks that may exist within marketplace lending businesses; and
  - (b) investor and borrower participation and expectations.
- 29 To improve our understanding of the business models and activities of marketplace lending providers, we considered it useful to survey the industry. Insights from the survey will help us to identify the risks involved with marketplace lending business models and enable us to respond appropriately.
- 30 By conducting the survey periodically, we will be able to identify any changes in the level of activity and potential risk indicators (such as the number of complaints and loan defaults experienced during the relevant period), and consider whether marketplace lending providers are managing these risks adequately.
- 31 As the industry develops, we may change the survey questionnaire to ensure that we are collecting information about any emerging risks or new developments.
- 32 Surveying marketplace lending providers is not unique to Australia. The Financial Markets Authority in New Zealand and the Financial Conduct Authority in the United Kingdom conduct similar surveys of marketplace lending businesses in their respective jurisdictions.

## How we conducted the survey

- 33 In September 2016, we consulted with industry on a draft questionnaire to determine whether marketplace lenders:
- (a) readily had the information to respond to the questions;
  - (b) were willing to provide the information voluntarily; and
  - (c) considered that any other questions should be included in the survey.
- 34 In November 2016, we sent the survey to a limited cross-section of marketplace lending providers, and received responses from nine entities.
- 35 The survey questionnaire comprised three parts. The first part included questions about the survey participants' business models, including:
- (a) how investors and borrowers are matched and loans allocated;
  - (b) how credit risk and interest rates are determined;
  - (c) any partnerships, alliances or other arrangements involving equity investment in the business;
  - (d) fee structures and other sources of revenue;
  - (e) cyber security and information technology (IT) security arrangements; and
  - (f) conflicts of interest.
- 36 We expect that this first part of the survey will not need to be completed again by marketplace lending providers, unless there has been a significant change to their business model.
- 37 The second part of the survey will inform us of quantitative trends over time and assist the development of our regulatory response to the industry. The questions in this part of the survey focus on:
- (a) characteristics of the borrowers and investors;
  - (b) characteristics of the loans made, including interest rates, amounts, term, security and default;
  - (c) indicators of operational risk, including complaints, breaches and cyber security threats; and
  - (d) amount of money generated from the key sources of revenue.

Note: In May 2017, the Government announced funding to allow the Australian Prudential Regulation Authority (APRA) to exercise new powers in relation to the provision of credit by lenders that are outside the traditional banking sector (see the Hon Scott Morrison MP, Treasurer, [Building an accountable and competitive banking system](#), media release, 9 May 2017).

- 38            The survey also allows marketplace lending providers to provide their views on current trends and any other matters they consider relevant about their business or the sector.

## C Survey findings and observations

### Key points

Our findings and observations outlined in this report focus on responses relating to the core aspects of a marketplace lending provider's business, including:

- business models (see paragraphs 39–74);
- borrowers (see paragraphs 75–83);
- investors (see paragraphs 84–87);
- loans (see paragraphs 88–107);
- late repayment and default (see paragraphs 108–114);
- compensation arrangements for investors (see paragraphs 115–118);
- IT and cyber security (see paragraphs 119–122);
- conflicts of interest (see paragraphs 123–127);
- complaints (see paragraphs 129–134);
- breach reporting (see paragraphs 135–136); and
- emerging trends and issues (see paragraphs 137–139).

## Business models

### Legal structure

- 39 The marketplace lending sector is relatively new to Australia. The majority of respondents commenced operations between 2014 and 2016 (or intended to commence in 2017).
- 40 All of the respondents operate managed investment schemes. Five respondents operated as schemes registered under Ch 5C of the Corporations Act (registered schemes), and the other four operated as unregistered schemes.
- 41 The regulatory status of the managed investment schemes (i.e. registered or unregistered) largely corresponds to the types of investors—registered schemes where the investors include retail and/or wholesale clients, and unregistered schemes where all investors are wholesale clients.
- 42 All respondents hold an AFS licence. However, the relevant licence authorisations, including the types of financial services that respondents are authorised to provide, vary due to differences in the business models of each respondent.

- 43 All respondents operate via an online platform, although they operate in different loan markets—for example, some focus on consumer loans, some on business loans to Australian SMEs and others lend to particular industry sectors.
- 44 In most cases, it appears the investor is not the lender on record for the loans, which means that the investor does not enter into a contract with the borrower. The loan contract is generally between the marketplace lending provider (as the operator of the managed investment scheme) or their custodian, and the borrower.

### **External service providers**

- 45 As AFS licence holders, marketplace lending providers may outsource key functions relating to the financial services or products they provide. They, however, remain responsible for providing these financial services and products.
- 46 We asked respondents to provide details of their key external service providers. All respondents engage external providers for various services including credit reporting, trustee and scheme custodian services, banking services, identification checks, software development, website hosting services, debt recovery and marketing services.
- 47 While some respondents indicated that a number of service providers are their related parties, many service providers are not related parties of the marketplace lending provider. All respondents monitor their service providers and review their performance on a regular basis, which may involve reviews against service level agreements or the marketplace lending provider's compliance plan, reporting by the service provider and regular liaison with the service provider. One respondent indicated it monitors on an exception basis and would institute a review if performance standards did not meet its expectations.

### **Exposure to loans**

- 48 As marketplace lending providers typically operate through managed investment schemes and each provider's model operates differently, it is important for providers to explain to investors how the arrangement works, and any differences in exposure to loans compared to direct investment.
- 49 Most respondents indicated that investors invest in loans on a fractionalised basis or in the whole loan—that is, an investor has exposure to part of a single loan together with other investors, or to a single whole loan, but not broad exposure to all loans. One respondent indicated its marketplace lending platform provides for investment on a pooled basis, so investors gain

exposure to all loans in proportion to their overall interest in the managed investment scheme.

### **Matching of investors and borrowers**

- 50 We asked respondents how investors and borrowers are matched and loans allocated.
- 51 One respondent indicated that all investment orders are matched on a real time basis and the priority for executing orders is dependent on various factors, including the timing of when an order is placed, and the amounts available to fund loans and interest rate.
- 52 In the case of two respondents that have wholesale investors, the loans that the investor will fund are pre-determined by agreement.
- 53 In some cases, investors are able to select their risk criteria so that they will only be matched with loans that meet these criteria. In one case, there are various categories of borrowers based on their risk grade, each with an interest rate range, which investors may elect to invest in. The final interest rate will depend on the level of demand from other investors and demand from borrowers, which then impacts on the ultimate level of returns that investors will receive.
- 54 One respondent indicated that investors may bid on the platform through live auctions for fractions of available loans based on their risk preferences and preferred loan terms.

### **Investment in loans by the provider or associates**

- 55 We asked respondents whether they, or their associates, invest in any of the loans offered.
- 56 With the exception of two respondents, the providers' officers, employees and shareholders may invest in the loans on the same terms as other investors. Some respondents noted that the loans are on an arm's length basis and are subject to their conflicts of interest policies. One respondent indicated that employees, directors and shareholders who do invest are treated in the same manner as other investors (e.g. charging of management fees, automated bidding process and preparation of investment instructions). In particular, they stated that these parties do not have operational responsibility in relation to the operation of robotic agents used by the platform, the bidding process that determines the interest rate and the loan allocation process.
- 57 One respondent, operating a wholesale investors-only marketplace lending platform, indicated that members of its management team have funded investments in a sizeable percentage of the loans. They would also bid on

loans on their own account, generally at the commencement of a loan listing or towards the end of the period for which the loan is listed.

58 Further findings in relation to conflicts of interest are set out in paragraphs 123–128.

### **Securitisation of loans and third party origination**

59 Most respondents indicated they do not securitise their loans. Two respondents indicated they securitise loans individually or on an aggregated basis. One respondent indicated it has securitised loans to facilitate the issue of notes by another fund. These notes are backed by the loans. More complex securitisation structures may emerge in the future.

60 Most respondents noted they do not sell individual loans to third parties. However, one respondent indicated it may sell individual loans directly to other parties if there is a demand.

61 All respondents indicated they do not acquire loans that were originated by third parties.

### **Affiliations**

62 We asked respondents if they have any partnerships, alliances, or other arrangements with other parties who make an equity investment in the marketplace lending provider's business.

63 A number of respondents indicated that they have a number of equity investors in their business, including banks, credit unions and other institutions. Some respondents indicated that investors simply invest by funding loans to borrowers. One respondent indicated that some of its shareholders also have arrangements under which they refer business to the marketplace lending provider. One respondent indicated that one of its shareholders is a loan broker with which it has referral arrangements.

### **Fees and other revenue**

64 We asked respondents to describe their fee structures and other revenue sources.

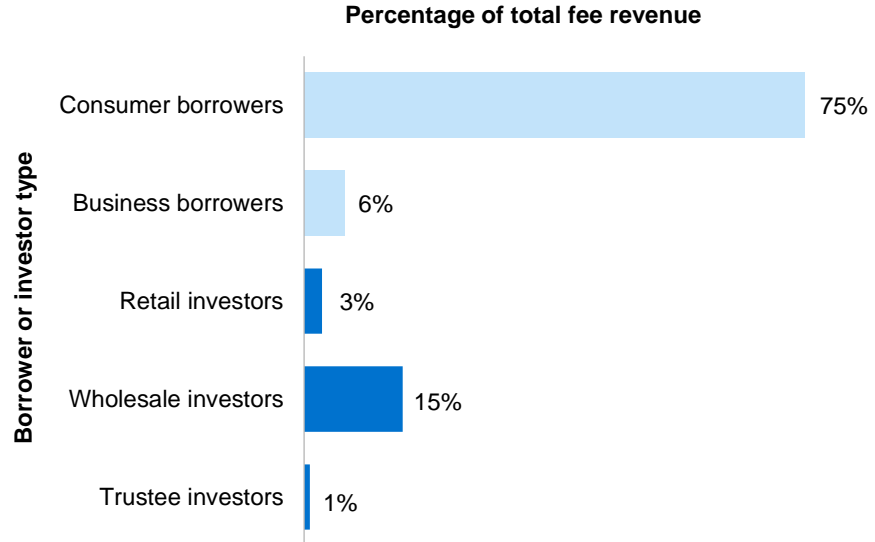
65 All respondents indicated they generate fee revenue from their investors and borrowers. This includes investment management fees charged to investors (which may be calculated as a percentage of the interest earned on the loans, investors' portfolio balances, or funds under management) and an exit fee when investors withdraw monies from their portfolio balance.

66 Respondents primarily earn fee revenue from loan origination, and from consumer borrowers. Figure 1 below shows the distribution of fee revenue



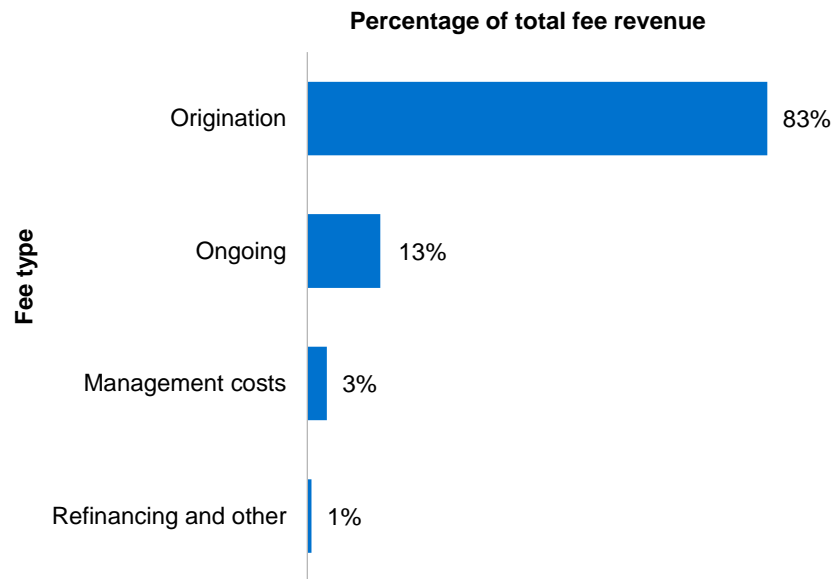
by borrower or investor type, and Figure 2 shows the distribution of fee revenue by fee type.

**Figure 1: Distribution of fee revenue by borrower or investor type**



Note: See Table 1 in the appendix for the data shown in this figure (accessible version).

**Figure 2: Distribution of fee revenue by fee type**



Note: See Table 2 in the appendix for the data shown in this figure (accessible version).

67

Loan origination fees accounted for approximately 83% of total fee revenue and the remainder of the revenue was almost exclusively generated from investors. The high proportion of origination fees may be partly explained by the fact that most providers have not been operating for a long period of time—any fees collected through interest payments may not be fully realised until future years.

- 68 We asked about the source of revenue for marketplace lending providers, as this can be an indicator of potential conflicts; for example, if most of the revenue is generated from loan origination, then the provider might have a stronger interest in origination of loans rather than ensuring existing loans are repaid. This potential conflict may be amplified by the fact that the provider does not necessarily lend its own funds, but is lending the funds of the investors.
- 69 As AFS licensees, marketplace lending providers must appropriately manage this type of conflict. Responsible entities of registered managed investment schemes must also act in the best interests of scheme members and give priority to the interests of members in the case of a conflict with their own interests, when making decisions in their capacity as responsible entities (see paragraphs 123–128 below).
- 70 We note that marketplace lending providers that operate registered schemes need to disclose to investors the fees and costs relating to the product in accordance with Sch 10 of the Corporations Regulations 2001 as modified by [Class Order \[CO 14/1252\]](#) *Technical modifications to Schedule 10 of the Corporations Regulations*. Fees and costs payable out of scheme property can be retained by the responsible entity beneficially only if authorised by the constitution, by a provision complying with s601GA(2) of the Corporations Act. Such amounts may only be retained if the responsible entity is properly performing its duties.

Note: RG 97 provides guidance on the disclosure requirement for fees and costs of managed investment schemes.

### **Promotion to borrowers and distribution arrangements**

- 71 All respondents indicated they employ a range of methods to promote their platform to borrowers. This primarily consists of digital or online promotion (comparison websites, direct emails and social media), although some respondents also use traditional forms of media (TV, radio and outdoor advertising). Some leads are generated by introducers such as loan brokers and licensed advisers.
- 72 We also asked respondents if they have any arrangements with third parties to distribute their products to borrowers. One respondent indicated it has referral partners, being other financial service providers who may refer investors and borrowers, however no payments are made by or to the provider. Another respondent has arrangements with online comparison sites which collect a fee based on activity generated. Three respondents have various relevant agreements, such as with merchants (of non-finance products) that receive a referral fee when they offer the provider's loan financing options to their customers. One respondent noted it relies on third

party introducers to refer borrowers and pays a commission for these referrals. Other respondents do not have referral arrangements.

### Promotion to investors and distribution arrangements

- 73 All respondents indicated they promote their product to investors using various methods such as online (website, social media) and other media (print advertising and radio). Some respondents also undertake direct engagement with professional (institutional) investors, licensed advisers/financial planners who have sophisticated investor clients, and engage in industry conferences.
- 74 Most respondents do not have arrangements with third parties to distribute the marketplace lending product to investors. Some respondents have affiliations with financial advisers, investment platforms and brokers. Not all referral arrangements with third parties involve the payment of remuneration although in some cases, there may be fees agreed on a per-referral basis or on amounts earned by the investor.

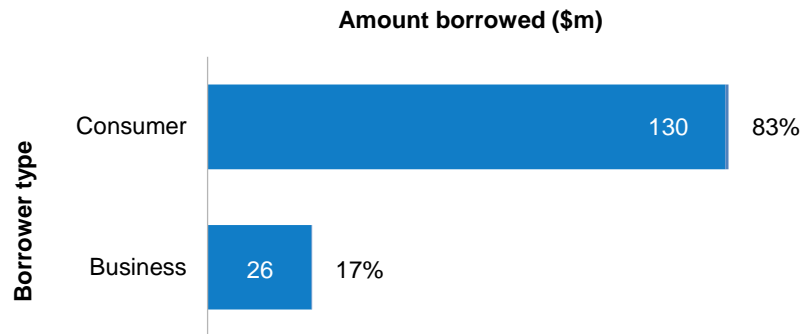
## Borrowers

### Types of borrowers

- 75 Respondents promoted their product to a range of different borrowers, which fell broadly under the category of consumers (i.e. individuals) or non-consumer/business borrowers, such as SMEs, self-managed superannuation funds (SMSFs) and agribusiness.

Note: Where the marketplace lending platform provides consumer loans, the provision of the loans is regulated under the *National Consumer Credit Protection Act 2009* (National Credit Act) and the National Credit Code in Sch 1 to the National Credit Act. These requirements do not apply to business purpose loans and loans to non-consumers (such as corporate entities).

- 76 As at June 2016, the eight entities who responded to the second part of the survey reported a total of 7,448 borrowers, consisting of 7,415 consumer borrowers and 33 business borrowers.
- 77 Figure 3 shows the amount borrowed in the 2016 financial year by type of borrower.

**Figure 3: Amount borrowed by borrower type**

Note: See Table 3 in the appendix for the data shown in this figure (accessible version).

### Credit concentration risk

78 Some respondents indicated that credit concentration risk is not currently a major concern given the small size of their current loan books. Other respondents indicated they regularly assess their portfolios to determine concentration risk. Strategies noted by respondents for managing this risk include:

- (a) undertaking broad-based marketing to reduce the risk of concentration of its borrowers in a geographical location or by demographics;
- (b) allowing investors direct control of their loan selection to build a portfolio suited to their individual risk profile (that is, investors select and self-manage their portfolios); and
- (c) applying a single-loan-per-borrower policy.

### Credit assessment

79 We asked respondents about their process for assessing and approving borrowers to determine their creditworthiness. The assessment of a borrower's creditworthiness will impact on the risk profile of the investment, and is therefore relevant to investors.

Note: In relation to consumer loans, the credit provider is required to comply with requirements in Ch 3 of the National Credit Act (the responsible lending requirements). These requirements are separate obligations for the protection of consumers to ensure that they are not placed in unsuitable loans, and are not focused on the credit risk for the credit provider or investors that fund the loan. The responsible lending obligations include requirements to:

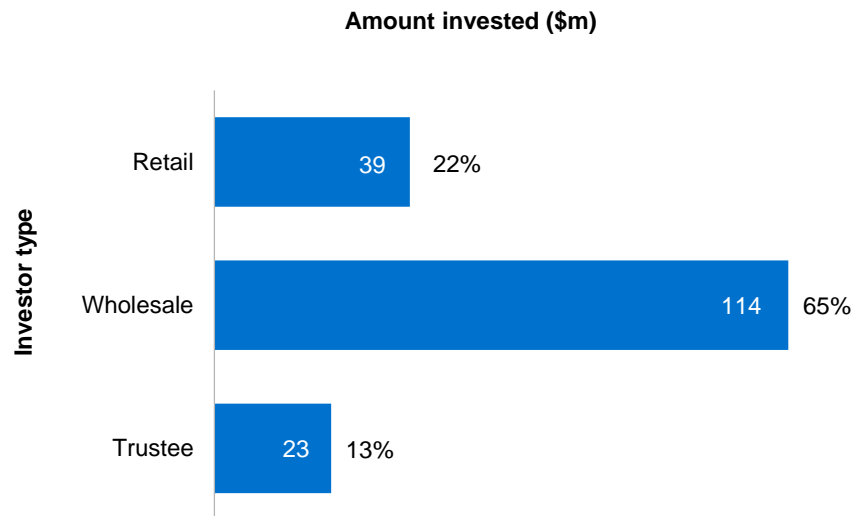
- make inquiries about the consumer's requirements and objectives in relation to the loan;
- make inquiries about, and verify, the consumer's financial situation; and
- using the information obtained through those inquiries, complete an assessment of whether the loan would be unsuitable for the consumer.

- 80 All respondents indicated they collect a wide variety of information about the borrower (such as employment status, income, financial assets and liabilities) and conduct a range of checks (such as identification verification and credit checks). Three respondents noted they also undertake 'due diligence' calls and interviews with applicants. The extent to which the other respondents conduct these types of additional inquiries is unclear. Some indicated they have scoring systems and risk rating assessments.
- 81 We also asked respondents about their methods for verifying information about borrowers. All respondents indicated they undertake a variety of authentication and verification processes, often relying on third party sources and automated systems. Most respondents have procedures for making further inquiries or manual checks if there are inconsistencies or discrepancies.
- 82 It appears that there is heavy reliance on automated processes. Where manual checks are carried out, this is done through direct communication with applicants or by verifying the information provided (such as financial information) using the marketplace lending platform's systems and other tools.
- 83 Respondents indicated they do not routinely review the creditworthiness of borrowers during the loan term unless there is a default or when prompted by the identification of material issues. One respondent indicated reviews depend on such factors as the term of the loan and market conditions. Other respondents indicated they limit their reviews to business borrowers or on a discretionary basis for higher risk borrowers.

## Investors

### Types of investors

- 84 The survey results indicate that both retail and wholesale clients invest in marketplace lending. The majority of the respondents restrict their platforms to investment by wholesale investors only. Of those respondents that provide their services to retail clients, some focus on retail investors only, while others permit both wholesale and retail clients to invest.
- 85 As at June 2016, eight respondents reported a total of 3,201 investors, consisting of 2,664 retail investors, 239 wholesale investors, and 298 trustee investors.
- 86 Figure 4 shows the amount invested in the 2016 financial year by type of investor.

**Figure 4: Amount invested by investor type**

Note: See Table 4 in the appendix for the data shown in this figure (accessible version).

- 87 The survey results indicate that the industry is predominantly comprised of investors that are wholesale clients. However, some respondents that are currently wholesale-only providers have indicated that they intend to broaden their marketplace lending product offering to retail client investors in the future. The fact that many providers operate registered schemes seems to suggest that they may have plans to, or may wish to have the option available to, offer their marketplace lending product to retail client investors in the future.

## Loans

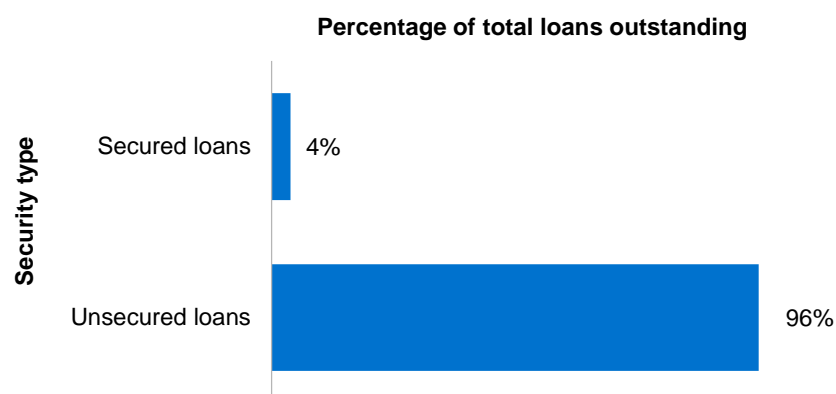
### Loan categories and creditworthiness

- 88 Two respondents indicated they do not categorise their loans before they are made available to investors. One respondent noted that a reason for this is that its marketplace lending platform only has wholesale investors.
- 89 All other respondents indicated their loans are categorised, although the criteria for categorisation varies across the different platforms. The various categories are disclosed to investors, who can take this information into account where given the option to determine their exposure to particular loans or their risk preferences. Each respondent adopts different descriptors in labelling the loan categories. These descriptors appear to be assigned by the provider, rather than a third party, and are designed to reflect the provider's assessment of the risk grade of the available loans.

## Loan security

- 90 Loans available on marketplace lending platforms may either be secured or unsecured. Two respondents provide loans on an unsecured basis only, while one respondent indicated that all its loans are secured (such as by way of a charge against all the borrowers' assets or by registered first mortgage). The remaining respondents indicated their loans may either be secured or unsecured. The security is held for the benefit of the investors.
- 91 Where loans are secured, if the loan security is exercised, the net proceeds from enforcing the security are ultimately paid on a proportionate basis to investors that have exposure to the defaulting loan. One respondent indicated that the proceeds may be paid to the arrangements the provider has in place to offset losses suffered by investors as a result of borrower default or the write-off of loans (see paragraphs 115–118 below) if the investor has already been paid out by these arrangements.
- 92 Figure 5 shows the distribution of outstanding loans (total number) by security type.

**Figure 5: Distribution of outstanding loans (total number) by security type**



Note: See Table 5 in the appendix for the data shown in this figure (accessible version).

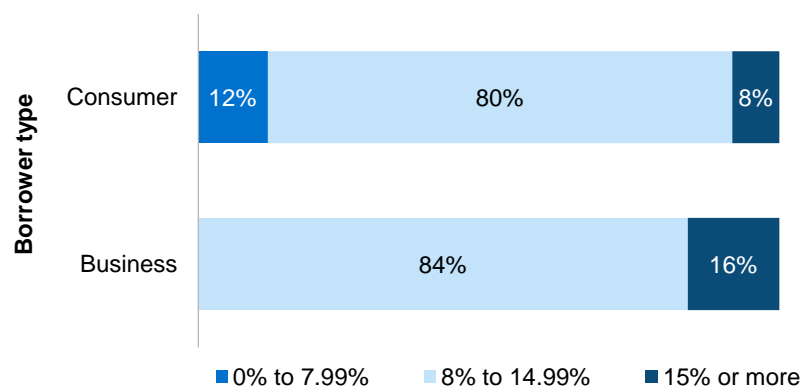
## Interest rates

- 93 We asked respondents how interest rates paid by borrowers and to investors are determined.
- 94 Most respondents indicated that they conduct assessments of potential borrowers to determine which potential loans will be made available on their marketplace lending platform for investors to select or be matched with (where matching or selection is permitted). It appears these assessments are conducted to determine if the borrowers are sufficiently creditworthy before allowing the requests for loans to be made available for investors to select.

In most cases, requests for loans are assessed and assigned a risk grade and interest rate before they are made available for viewing and selection by investors.

- 95 Most respondents indicated that interest rates are generally set by the provider and investors do not determine or influence the rate. Investors may choose the loans they wish to invest in based on the interest rate and/or risk grade allocated to the loan. One respondent indicated that investors are able to nominate the interest rate at which they are willing to lend. Under this model, the rate is ultimately determined by investors and borrowers according to the level of supply and demand for funds. Another respondent noted that wholesale investors receive a rate that is determined by agreement.
- 96 One respondent also allocates a risk rating to the borrower and relies on a loan auction process to determine a weighted average interest rate for the borrower, which takes into account the various rates and amounts at which different investors will fund the borrower's loan.
- 97 Figure 6 shows the distribution of outstanding loans by borrower type and interest rate.

**Figure 6: Distribution of outstanding loans (total number) by borrower type and interest rate**



Note: See Table 6 in the appendix for the data shown in this figure (accessible version).

## Restructuring of loans

- 98 Most respondents indicated that there is scope to restructure a loan if a borrower experiences hardship. This may involve reduced repayment amounts, repayment holidays or extension of the loan term. Ultimately, it is a matter for the marketplace lending provider to make decisions about the restructure of a loan on a case-by-case basis. Investors do not appear to have any input into the process and any delay in repayments or reduction in the



amounts available for repayment are not funded by the provider, with the focus being on recouping amounts from borrowers. Except in the limited case where investors may have some recourse against compensation arrangements or arrangements where another entity may pay in case of default, it appears the risk of loss is borne by investors.

Note 1: Consumers can seek variation of their loan due to changes in their circumstances that result in hardship. Division 3 of Pt 4 of the National Credit Code contains requirements for handling hardship applications.

Note 2: The compensation arrangements referred to in this paragraph are distinct from the type of arrangements that AFS licensees must have in place to meet the requirements under s912B of the Corporations Act (see paragraph 115).

99 Most respondents indicated that borrowers are not able to refinance their loans—that is, replace their existing loan with a new loan with the provider. However, in limited circumstances, a borrower may be eligible for a loan redraw or enter into a new loan contract to pay out an existing loan with the same marketplace lending provider.

100 All respondents indicated that borrowers are able to repay their loan or exit their loan early without penalty. In some cases, if a borrower wishes to exit early, they must repay the loan in full. One respondent indicated that there is a minimum period (three months) before the borrower may repay ahead of schedule.

Note: Consumers are entitled to pay out a credit contract that is regulated by the National Credit Code at any time: s82 of the National Credit Code. The credit provider cannot limit this right: s192 of the National Credit Code. However, a contract regulated under the National Credit Code may have limitations on making early repayments (other than a full pay out): s26 of the National Credit Code.

101 For investors, most respondents indicated there is no ability to exit the investment early (for example, via a secondary market). One respondent noted they offer a periodic redemption facility which allows regular redemption of units that represent the investor's interest in the scheme over a number of years. Another respondent indicated early exit can occur if a borrower repays early, while another noted that an investor can offer their investment (on their personal dashboard) for purchase by another investor.

### **Loan duration**

102 Each respondent offers different loan terms to borrowers, which can range from three months to 15 years. Most respondents offer loan terms of three or five years. Two respondents further noted that their loans are fully amortising with regular payments.

103 From the investors' perspective, in most cases, these terms correspond with the investment period. However, one respondent indicated that an investor may nominate to invest for one month, where the minimum loan duration is

six months, and another that an investor may invest in an existing loan, in which the investment period is the remaining term of the loan. One respondent, who operates a pooled fund, noted their investors can undertake periodic redemptions over a number of years.

## Loan amounts

104 Loan amounts offered to consumer borrowers typically range from \$5,000 to \$80,000, while for business and other non-consumer borrowers, the amounts range from \$2,001 to \$3,000,000. None of the respondents provide small amount credit contracts or 'payday loans'.

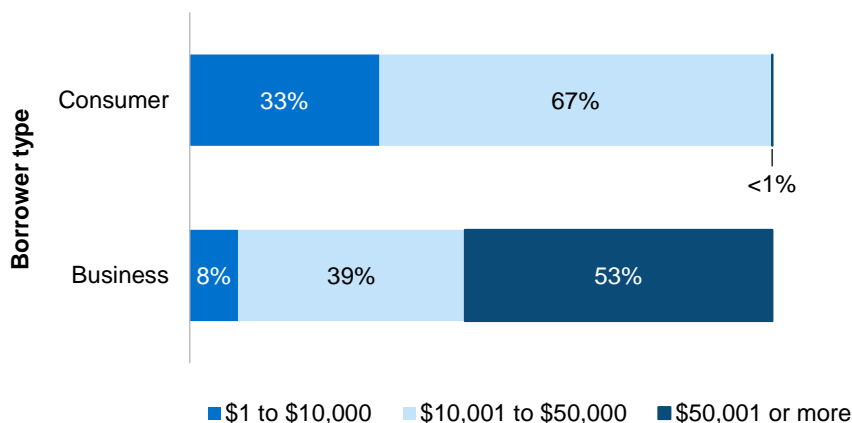
Note: Different regulatory requirements apply to small amount credit contracts, including additional responsible lending requirements (Pt 3-2C of the National Credit Act) and a different cap on the cost of the loan (Div 4 of Pt 2 of the National Credit Code). Interest charges are prohibited for small amount credit contracts (s23A of the National Credit Code).

105 Some respondents indicated that minimum investment amounts are required. These minimums are lower for retail platforms, commencing at a minimum investment of \$10. One respondent that operates a wholesale platform noted that the minimum fractional amount that can be invested is algorithmically determined and increases as the loan funding requirements become higher, to maintain an acceptable level of 'equilibrium' between supply and demand for loan funding.

106 There are no maximum limits on the amounts that may be invested and the amounts are at the investor's discretion. However, one respondent that offers fractional loans indicated that for each loan, there must be a minimum number of investors in the particular loan.

107 Figure 7 shows the distribution of outstanding loans by borrower type and loan amount.

**Figure 7: Distribution of outstanding loans (total number) by borrower type and loan amount**

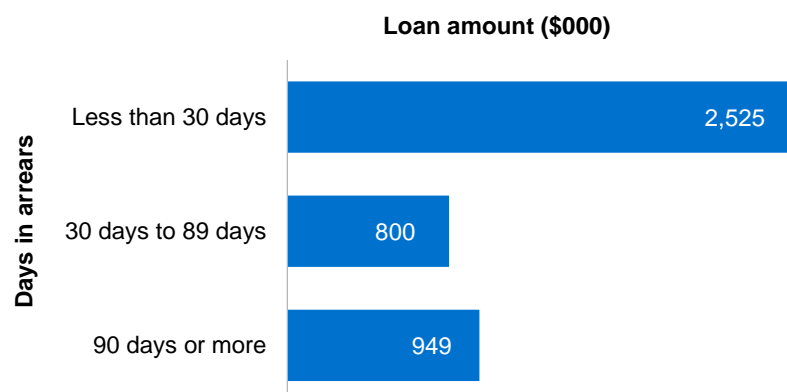


Note: See Table 7 in the appendix for the data shown in this figure (accessible version).

## Late repayment and default

- 108 We asked respondents to describe their procedures for managing late repayments or loan defaults.
- 109 Of the respondents that reported current and historical gross default rates, three respondents reported default rates greater than 0%. These ranged from 0.1% to 3.4% (current default rate at 30 June 2016) and from 0.25% to 12.2% (historical gross default rate).
- 110 When the respondents were asked about their expected default rate for the 2017 financial year, the mean rate was 2.53%, with responses ranging from 0% to 4%.
- 111 Figure 8 shows the distribution of loans in arrears by the number of days in arrears. Loans in arrears represent 3.15% of total loans outstanding (by dollar amount).

**Figure 8: Distribution of loans in arrears (total amount) by days in arrears**



Note: See Table 8 in the appendix for the data shown in this figure (accessible version).

- 112 Most respondents indicated that they provide a grace period for borrowers in the event of missed or late repayments. All respondents indicated that reminders and direct engagement with the borrower are undertaken by the platform provider and that a repayment arrangement may be agreed with the borrower. Referrals to external collections agencies would be made if the loan remained delinquent. In one case, it was noted that recovery action would require the consent of the lenders for the particular loan.
- 113 One respondent noted that problem SME loans require a more tailored process compared to consumer loans.
- 114 Most respondents indicated they do not stress test their loan book, largely due to the relative newness or small size of current loan books which would not produce any meaningful assessment. However, two respondents do undertake some testing.

## Compensation arrangements for investors

- 115 Two respondents indicated that they maintain arrangements to offset the consequences for investors in the event of borrower default or the write-off of loans. These arrangements do not, however, guarantee the recovery of investments.

Note: These arrangements are distinct from the type of compensation arrangements that AFS licensees must have in place to meet the requirements under s912B of the Corporations Act. We provide guidance on these requirements in [Regulatory Guide 126 Compensation and insurance arrangements for AFS licensees](#) (RG 126).

- 116 The arrangements are funded by borrower contributions or interest monies earned on loans. These funds are held in cash deposits in Australian deposit-taking institutions. In the event borrowers default on payment, investors who are exposed to loss may be compensated under these arrangements. However, compensation payments to investors under these arrangements are made at the discretion of the provider.
- 117 These arrangements for investors may offer some investors protection against losses due to default by borrowers. However, it is important to recognise the limitation of these arrangements, including that they are unlikely to provide investors sufficient protection against losses if the default rate is high (for example, due to an economic downturn or poor credit assessment process by the marketplace lending provider). Where these arrangements are offered, their source of funding, limitations and any discretion the provider may have over their use should be disclosed to retail clients.
- 118 The remaining respondents indicated they do not have any specific compensation arrangements of this type.

## IT and cyber security

- 119 We asked respondents about their backup and data recovery arrangements, as well as the IT security arrangements in place to ensure the ongoing operation of the marketplace lending platform and protection of data.
- 120 All respondents indicated they have relevant arrangements in place, often employing the services of third party providers and relying on off-site or cloud-based systems for backups and data recovery. Respondents typically detailed multi-faceted approaches to IT security, including encryption of data, real-time monitoring, physical information security, and business continuity plans.
- 121 Respondents did not identify any cyber security breaches in the 2016 financial year.

- 122 In INFO 213 we identify cyber security as one of the key risks that may impact investors and borrowers using marketplace lending products. We expect that, as part of adequate risk management systems, AFS licensees with businesses that have heavy reliance on IT and the internet will have in place controls to manage cyber security. We have also published [Report 429 Cyber resilience: Health check](#) (REP 429) on managing online fraud and other cyber risks, which we encourage marketplace lending providers to consider.

## Conflicts of interest

- 123 We asked respondents about the key conflicts of interest for their business, and how these are managed.
- 124 Respondents identified the following actual or potential conflicts:
- (a) conflict between the investor's interest in not lowering credit assessment standards and the provider's interest in enabling more borrowers to qualify for loans, which generates additional fees (given providers earn fees from each approved borrower);
  - (b) conflict between the interests of a provider's two sets of customers, being the borrowers and investors;
  - (c) conflict between the interests of the shareholders of the responsible entity and the interests of members of the scheme;
  - (d) conflict between the interests of a provider in commercial relationships with brokers and referral partners, the provider's role as responsible entity and its duties to the members of the scheme and shareholders of the responsible entity;
  - (e) conflicts between the interest of shareholders, directors and employees who are wholesale investors in loans, and other investors where the operator or trustee must ensure that the interests of certain investors are not preferred over other investors; and
  - (f) conflicts resulting from a provider's employees investing in loans, and the need to prohibit employees from bidding in an auction if the loan is fully funded to ensure that other investors do not have to re-bid at a lower interest rate. Also related to employees, conflicts were identified between an employee's interests and the interests of investors as a result of employee bonus arrangements.

- 125 To manage conflicts, all respondents indicated they have a conflicts of interest policy. Methods identified for managing conflicts of interest included:
- (a) employing a fully automated decision-making process, with any exceptions that require manual assessment ultimately directed to a committee for final review and determination;
  - (b) having a multi-level compliance hierarchy, with the combination of a compliance manager, head of compliance and compliance committee to assist in the management of conflicts;
  - (c) staff bonus payments not being volume dependent, and instead being determined by reference to the performance of the business as a whole, rather than by reference to the loans originated or borrowers added to the platform;
  - (d) information barriers between the teams that deal respectively with investors and borrowers;
  - (e) use of a responsible entity independent of the manager to operate the platform business and non-involvement of directors that hold an investment in the business, in the day-to-day running of the business;
  - (f) a requirement that a credit committee approve all loans before they are listed on the platform;
  - (g) prohibiting employees and associates from borrowing via the online platform; and
  - (h) providing the same information to all investors alike.
- 126 Some respondents specifically noted that new conflicts are reported on a quarterly basis and that employee holdings are reported.
- 127 Having adequate arrangements for managing conflicts of interest is an important obligation of AFS licensees. As part of meeting this obligation, AFS licensees are required to identify and appropriately manage any conflicts of interest in providing financial services.
- Note 1: We have issued regulatory guidance on managing conflicts of interest—see [Regulatory Guide 181](#) *Licensing: Managing conflicts of interest* (RG 181).
- Note 2: The duty of AFS licensees to have in place adequate arrangements for the management of conflicts of interest was recently considered in *Australian Securities and Investments Commission v Avestra Asset Management Limited (In Liquidation)* [2017] FCA 497.
- 128 In the context of marketplace lending, it would be appropriate to ensure that any loan investments by employees and officers of the provider (or its associates) are at arm's length and on the same terms and conditions as other investors. Employees and officers should not have an opportunity to invest in loans prior to other investors. It may also not be consistent with doing all things necessary to ensure that the financial services are provided efficiently,

honestly and fairly if such persons have information that may influence other investors but is not provided to them.

## Complaints

- 129 We asked respondents about the number of complaints they had received from borrowers and investors.
- 130 There were five respondents who in aggregate received 25 borrower complaints. Out of these complaints, seven were escalated for resolution via external dispute resolution processes.
- 131 All borrower complaints were resolved, with the exception of one complaint which remained unresolved.
- 132 The common areas that were the subject of borrower complaints included the non-approval of credit applications, alleged non-compliance with responsible lending obligations, and loan fees.
- 133 Other less common areas that were cited as the subject of borrower complaints included customer service, dishonour fees, reporting the borrower to a credit reporting body due to late repayments or default, direct mail marketing material and higher than expected interest rates.
- 134 No investor complaints were reported by the respondents.

## Breach reporting

- 135 We asked respondents how many breaches or likely breaches of their obligations under the Corporations Act were identified during the period.
- 136 Three respondents indicated there were in aggregate seven instances of breaches or likely breaches of the Corporations Act, one of which was notified to ASIC as a significant breach under s912D.

Note: Under s912D of the Corporations Act, an AFS licensee is required to notify ASIC of a breach or likely breach of the financial services laws that is significant. We have issued regulatory guidance to AFS licensee about breach reporting obligations—see [Regulatory Guide 78](#) *Breach reporting by AFS licensees* (RG 78).

## Emerging trends and issues

- 137 We asked respondents if they had identified any emerging trends or issues in relation to marketplace lending. The responses about common trends and issues highlighted:
- (a) lack of uniformity and transparency in the determination of interest rates, which compromises comparability between different products;
  - (b) public awareness and understanding of the industry more generally; and
  - (c) non-application of National Credit Code protections for SME borrowers.
- 138 The issues outlined in 137(a) and 137(b) have been similarly identified by ASIC in our work related to marketplace lending and we have encouraged marketplace lending providers to explain clearly in disclosure documentation and website material how their business model works. As good practice, we have encouraged providers in INFO 213 to:
- (a) refer investors to the marketplace lending information available on our [MoneySmart website](#);
  - (b) provide investors with an appropriately designed risk warning statement. Testing of the risk warning statement may help to ensure its effectiveness;
  - (c) provide investors with an optional ‘knowledge test for investors’ to assess their understanding of the product before they invest; and
  - (d) provide the following information on the website:
    - (i) information about the policies and procedures for managing the selection of borrowers and ongoing monitoring of loans policies (without disclosing commercially sensitive information); and
    - (ii) aggregated information about the loan book such as interest rates, loan amounts, term of the loans and whether loans are secured or unsecured.
- 139 In relation to the issue outlined in 137(c), we note that SME loan contracts are subject to unfair contract provisions in the *Australian Securities and Investments Commission Act 2001* (ASIC Act): refer to paragraphs 172–175.

Note: The National Credit Code does not apply to loans to persons other than consumers (e.g. a loan to a corporate entity is not regulated) and does not apply to loans for business purposes (even if the borrower is an individual). Loans to SMEs are therefore unlikely to be covered. These loans are however a ‘credit facility’ that is regulated under the more general consumer protection provisions in Div 2 of Pt 2 of the ASIC Act. The ‘unfair contract term’ provisions in the ASIC Act apply to consumer contracts and small business contracts.



## D ASIC's role and related activities

### Key points

Marketplace lending providers are generally subject to regulation by ASIC (see paragraphs 140–142). In regulating marketplace lending we have undertaken various activities, including around:

- INFO 213 and MoneySmart material (see paragraphs 143–145);
- ASIC's Innovation Hub (see paragraphs 146–149);
- an internal working group (see paragraphs 150–151);
- AFS licence and relief applications (see paragraphs 152–154);
- surveillance (see paragraphs 155–171);
- unfair contract term protections (see paragraphs 172–175); and
- other compliance observations (see paragraphs 176–179).

As the marketplace lending industry develops, we will continue to engage with providers to help them understand and manage their regulatory requirements, risks and conflicts of interest.

### Our regulatory role

- 140 As marketplace lending products typically meet the definition of a financial product (for example a managed investment scheme), providers of the products are generally subject to regulation by ASIC and are required to comply with the Corporations Act, ASIC Act and, when lending to individual borrowers, the National Credit Act and National Credit Code.
- 141 ASIC's role includes:
- (a) maintaining, facilitating and improving the performance of the financial system and entities in it;
  - (b) promoting confident and informed participation by investors and consumers in the financial system; and
  - (c) enforcing and giving effect to the law.
- 142 In performing this role we have undertaken the following activities in relation to marketplace lending, to assist providers to understand and comply with their obligations, check on compliance with various matters and to ensure adequate consumer protection.

## Information Sheet 213

- 143 We released INFO 213 to assist providers of marketplace lending products and others providing financial services in connection with these products. INFO 213 covers:
- (a) what is marketplace lending;
  - (b) key risks in providing marketplace lending products;
  - (c) key obligations that may apply to marketplace lending business models and applications for relief;
  - (d) advertising of marketplace lending products; and
  - (e) good practice examples.
- 144 We encourage marketplace lending providers to have regard to the guidance in INFO 213.

## MoneySmart material

- 145 To assist investors and borrowers, we have provided some guidance on marketplace lending and relevant risks on our [MoneySmart website](#). We encourage investors and borrowers to review this material before they invest or borrow money through marketplace lending.

## Innovation Hub

- 146 In March 2015, ASIC established the Innovation Hub. One objective of the Innovation Hub is to help fintech start-ups to navigate the regulatory requirements that may apply to their business.
- 147 If an entity meets the eligibility criteria for assistance from the Innovation Hub, it may submit a request for assistance. The eligibility criteria and request for assistance form are available on the [Innovation Hub webpage](#).
- 148 Marketplace lending is a relatively new and innovative fintech business, which generally means that new providers are eligible to seek assistance from the Innovation Hub. The Innovation Hub has assisted a number of entities interested in becoming marketplace lending providers to understand their regulatory obligations and navigate the process of obtaining an AFS licence.
- 149 Since its commencement, the Innovation Hub has engaged with 34 potential marketplace lending providers.

Note: In May 2017, ASIC released [Report 523](#) *ASIC's Innovation Hub and our approach to regulatory technology* (REP 523) which, in addition to covering current

initiatives underway in relation to regtech and proposed next steps, also gives an update on the work of ASIC's Innovation Hub.

## Internal marketplace lending working group

- 150 We have an internal working group for marketplace lending, comprising staff from across relevant teams within ASIC, including those with regulatory oversight of AFS licensing, investment management, credit and credit licensing, and markets.
- 151 The marketplace lending working group meets regularly to discuss ASIC's work in this space, and emerging trends and issues.

## Assessment of AFS licence and relief applications

- 152 To operate a managed investment scheme for marketplace lending, the providers must hold an AFS licence. We have assessed 14 applications from marketplace lenders, and have granted 10 AFS licences.
- 153 In some circumstances, marketplace lending providers have applied to ASIC for relief from compliance with requirements under the Corporations Act. We have assessed applications for relief in relation to six marketplace lending platforms.
- 154 Some examples of relief that we have granted to marketplace lending providers from requirements under the Corporations Act are set out below:
- (a) Relief from the withdrawal requirements (s601GA(4) and Pt 5C.6 of the Corporations Act), to facilitate withdrawal of cash by members while the scheme is illiquid, was granted in circumstances where each member had a separate portfolio that comprised a separate class of interest. For additional information see [Report 420](#) *Overview of decisions on relief applications (June to September 2014)* (REP 420).
  - (b) Relief was granted from the requirement to seek registration of a separate managed investment scheme for each loan entered into through the marketplace lending platform.
  - (c) Relief was granted from the requirement to treat the underlying assets of a provision fund operated in connection with the lending platform as scheme property of the scheme. For additional information see [Report 435](#) *Overview of decisions on relief applications (October 2014 to January 2015)* (REP 435).

## Surveillance

155 As part of our role, we regularly undertake inquiries and surveillance work in relation to our regulated populations. This has included assessment of some marketplace lending providers' compliance with the Corporations Act and the ASIC Act. Some of our surveillance work has been in response to complaints and referrals we have received.

156 Where we identify non-compliance, the action taken will depend on the circumstances of each case, including the seriousness of the contravention and its consequences. We will also take into account whether the non-compliance was promptly identified and reported to ASIC, whether the provider is willing to work with us to ensure the matter is promptly rectified and whether there have been similar breaches by the same provider in the past.

157 Below is a summary of some of our surveillance work, and issues of non-compliance that we identified. We have worked with the providers to rectify these issues.

### Product Disclosure Statement content

158 We have conducted reviews of some marketplace lending providers' Product Disclosure Statements (PDS).

159 If retail investors will be acquiring the marketplace lending product, a PDS needs to be prepared by a marketplace lending provider and given to investors before they make an application to invest in the product. Marketplace lending providers must ensure that the PDS complies with the content requirements of the Corporations Act and ASIC Act (see Pts 7.9 and 7.10 of the Corporations Act and Pt 2 of the ASIC Act).

160 In our review of PDSs, in some instances we identified inadequate disclosure about:

- (a) key features of the relevant marketplace lending product offered (e.g. how the product operates, who is the provider of the product, how borrowers and investors are matched, how interest rates are determined, and how borrowers' creditworthiness is assessed);
- (b) risks associated with investing in the marketplace lending product;
- (c) withdrawal rights (if any) that are provided to investors;
- (d) the potential impact of responsible lending obligations, including but not limited to the potential for a borrower to not only vary its loan contract but to have it set aside in certain circumstances, including, for example, where the marketplace lending provider lends irresponsibly.

161 We required the relevant marketplace lending providers to revise the disclosure in PDSs to address the above issues, which has resulted in additional disclosure being made.

### **Advertising and promotional material**

162 We have conducted reviews of some marketplace lending providers' advertising and promotional material, including website material.

163 The content of advertising and promotional material also needs to comply with the content requirements of the Corporations Act and must not include any material that is misleading or deceptive (see s1018A, s1018B and Pt 7.10 of the Corporations Act and Pt 2 of the ASIC Act).

164 [Regulatory Guide 234](#) *Advertising financial products and advice services (including credit): Good practice guidance* (RG 234) contains good practice guidance to help promoters understand their legal obligations.

165 In our review of advertising and promotional material, in some instances we identified:

- (a) inappropriate comparisons of the investment by investors in marketplace lending products with banking products, when the products are not similar and have very different risk profiles;
- (b) over-emphasis of the potential benefits of the marketplace lending product without appropriate balanced disclosure about the relevant risks of the product;
- (c) inappropriate comparisons of the marketplace lending product with the products offered by other marketplace lending providers;
- (d) citing of references by others (such as customer testimonials or the media) which include potentially misleading statements or inappropriate comparisons.

166 We required the relevant marketplace lending providers to make amendments to advertising and promotional material to address the above issues.

167 Marketplace lenders must also ensure that advertising and promotion material made available to prospective borrowers is not misleading. In particular, lenders must ensure that the advertising of interest rates using the form, 'rates from X% p.a.' does not misrepresent the availability of the stated rate (i.e. where the rate offered to the consumer in practice is based on the credit risk profile of the consumer and, potentially, the demand from investors). This is likely to require the lender to regularly monitor the rates being offered to consumers.

## Failure to hold an AFS licence

- 168 We have identified some marketplace lending providers operating without an AFS licence in contravention of the Corporations Act (see s911A of the Corporations Act).
- 169 Generally, a marketplace lending provider, including a provider that is operating a wholesale scheme, will need an AFS licence that covers any financial product advice, dealing, or custodial or depository financial services undertaken in relation to the scheme, unless an exemption applies.
- 170 We identified some business models where the marketplace lending product was structured as a managed investment scheme offered to wholesale investors and the provider:
- (a) was relying on a corporate authorised representative authorisation by another AFS licensee to operate the scheme—we do not consider it is possible to operate a managed investment scheme in reliance on an intermediary authorisation, such as a corporate authorised representative arrangement; or
  - (b) did not hold an AFS licence or an authorisation to operate the scheme—as outlined above, generally an AFS licence is required to be held by the provider.
- 171 We raised concerns with these operators about their unlicensed conduct, and they obtained their own AFS licence with appropriate authorisations to operate the scheme.

## Unfair contract term protections

- 172 The unfair contract term protections for consumers were extended to cover standard form small business contracts entered into, or renewed, on or after 12 November 2016. In the context of small business loans, the unfair contract term protections apply to loans of up to \$1 million to small businesses employing fewer than 20 staff.
- 173 ASIC and the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) have publicly expressed concerns that the following kinds of clauses are at high risk of not complying with the unfair contract term laws (see [Media Release \(17-056MR\)](#) ASIC and ASBFEO join forces to ensure bank lenders meet unfair contract laws (9 March 2017)):
- (a) *unilateral variation clauses*—terms that give lenders a very broad discretion to unilaterally vary terms and conditions of the contract;
  - (b) *non-monetary default clauses*—terms that provide for loan ‘default’ in a very broad range of circumstances, rather than where the borrower has materially defaulted on their obligations;

- (c) *entire agreement clauses*—terms that absolve the lender from responsibility for conduct, statements or representations that the lender makes to borrowers outside of the contract; and
- (d) *indemnification clauses*—terms that too broadly indemnify the lender against losses, costs, liabilities and expenses.
- 174 The big four banks have committed to making comprehensive changes to ensure all small business loans (under \$1 million) entered into or renewed from 12 November 2016 will be protected from the terms noted above (see [Media Release \(17-139MR\) ASIC and ASBFEO hold banks to account on unfair contract terms](#) (16 May 2017)). This followed extensive work with the banks, including a roundtable on 10 May 2017.
- 175 ASIC and ASBFEO will continue to work with lenders, including marketplace lending providers, to ensure that small business loan contracts do not contain unfair terms.

## Other compliance observations

- 176 Through our work in this area, we have also identified the following issues, which we bring to providers' attention to ensure ongoing compliance.

### References to credit reporting agencies

- 177 We understand that some providers may seek to include in the PDS for a marketplace lending product references to reports and credit scores prepared by credit reporting agencies.
- 178 Under s1013K of the Corporations Act, a PDS may only include a reference to a statement made by a person if the person has consented to the statement being included in the PDS and the PDS states the person has given the consent. Accordingly, if any references are made in the PDS to the material prepared by the credit reporting agency, we consider that it is necessary to obtain the consent of the agency to include the content and for this to be stated in the PDS.

### Compliance with other relevant guidance

- 179 Some marketplace lending platforms structured as managed investment schemes may also meet the definition of a mortgage scheme. For operators of these schemes, it will be necessary to consider the disclosure benchmarks and principles in [Regulatory Guide 45 Mortgage schemes: Improving disclosure for retail investors](#) (RG 45).

Note: For the purposes of RG 45 a mortgage scheme is a managed investment scheme that has, or that is likely to have, at least 50% of its non-cash assets invested in

mortgage loans and/or unlisted mortgage schemes. Mortgage loans are loans secured by a mortgage over real property (including residential, commercial, industrial or retail property, or vacant land).

## Next steps

- 180 Marketplace lending in Australia is still developing. While it shares many features of other managed investment schemes that offer investors an exposure to loans, including mortgage funds, it appears to rely more heavily on automation and technology than these traditional loan-based funds. This has implications for the way investors and borrowers interact with the product and on the types of risks, how they are managed, and operational dependencies faced by the provider.
- 181 The survey responses highlight the diverse nature of marketplace lending business models, which makes it more important to ensure that providers help consumers and investors understand their particular model. While risks and potential conflicts of interest will continue to exist around marketplace lending, they can be managed by providers meeting their AFS licence and other compliance obligations. Our regulatory guidance will assist providers in understanding and meeting these obligations.
- 182 As part of our regulatory role we are keen to continue engaging with marketplace lending providers to ensure that we keep abreast of developments, including overseas regulatory and industry developments. We will also continue to assist marketplace lending providers, including new providers, understand the regulatory requirements that apply.



## Appendix 1: Accessible versions of figures

183 This appendix is for people with visual or other impairments. It provides a text description and/or the underlying data for each of the figures included in this report.

**Table 1: Distribution of fee revenue by borrower or investor type**

Borrower or investor type	Percentage of total fee revenue
Consumer borrowers	75%
Business borrowers	6%
Retail investors	3%
Wholesale investors	15%
Trustee investors	1%

Note: This is the data contained in Figure 1.

**Table 2: Distribution of fee revenue by fee type**

Fee type	Percentage of total fee revenue
Origination	83%
Ongoing	13%
Management costs	3%
Refinancing and other	1%

Note: This is the data contained in Figure 2.

**Table 3: Amount borrowed by borrower type**

Borrower type	Amount borrowed (\$ million)	Percentage of total amount borrowed
Consumer	130	83%
Business	26	17%

Note: This is the data contained in Figure 3.

**Table 4: Amount invested by investor type**

Investor type	Amount invested (\$ million)	Percentage of total amount invested
Retail investors	39	22%
Wholesale investors	114	65%
Trustee investors	23	13%

Note: This is the data contained in Figure 4.

**Table 5: Distribution of outstanding loans (total number) by security type**

Security type	Percentage of total loans outstanding
Secured loans	4%
Unsecured loans	96%

Note: This is the data contained in Figure 5.

**Table 6: Distribution of outstanding loans (total number) by borrower type and interest rate**

Borrower type	0% to 7.99% interest rate	8% to 14.99% interest rate	15% or more interest rate
Consumer	12%	80%	8%
Business	0%	84%	16%

Note: This is the data contained in Figure 6.

**Table 7: Distribution of outstanding loans (total number) by borrower type and loan amount**

Borrower type	\$1 to \$10,000 loan amount	\$10,001 to \$50,000 loan amount	\$50,001 or more loan amount
Consumer	33%	67%	<1%
Business	8%	39%	53%

Note: This is the data contained in Figure 7.

**Table 8: Distribution of loans in arrears (total amount) by days in arrears**

Days in arrears	Loan amount (\$ thousand)
Less than 30 days	2,525
30 days to 89 days	800
90 days or more	949

Note: This is the data contained in Figure 8.

## Key terms

Term	Meaning in this document
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries on a financial services business to provide financial services  Note: This is a definition contained in s761A.
AFS licensee	A person who holds an AFS licence under s913B of the Corporations Act  Note: This is a definition contained in s761A.
ASIC	Australian Securities and Investments Commission
ASIC Act	<i>Australian Securities and Investments Commission Act 2001</i>
associate	Has the meaning given in Div 2 of Pt 1.2 of the Corporations Act
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
current default rate	Total number of loans in default divided by total number of outstanding loans on issue at a point in time
default	A failure by a borrower to make a repayment when it is due on a loan, for a period of 90 days or more
fintech	Financial technology
historical gross default rate	Number of loans classified as in default as a percentage of the number of gross loans written since commencing operations
managed investment scheme	Has the meaning given in s9 of the Corporations Act
National Credit Act	<i>National Consumer Credit Protection Act 2009</i>
National Credit Code	National Credit Code at Sch 1 to the National Credit Act
registered scheme	A managed investment scheme that is registered under s601EB of the Corporations Act
REP 420 (for example)	An ASIC report (in this example numbered 420)
responsible entity	A responsible entity of a registered scheme as defined in s9 of the Corporations Act
retail client	A client as defined in s761G of the Corporations Act and Div 2 of Pt 7.1 of the Corporations Regulations
RG 166 (for example)	An ASIC regulatory guide (in this example numbered 166)

<b>Term</b>	<b>Meaning in this document</b>
wholesale client	A client who is not a retail client as defined in s761G of the Corporations Act and Div 2 of Pt 7.1 of the Corporations Regulations

## Related information

### Headnotes

borrower, INFO 213, investor, loan, managed investment scheme, marketplace lending provider

### Class orders

[Class Order \[CO 14/1252\]](#) *Technical modifications to Schedule 10 of the Corporations Regulations*

### Regulatory guides

[RG 45](#) *Mortgage schemes: Improving disclosure for retail investors*

[RG 78](#) *Breach reporting by AFS licensees*

[RG 97](#) *Disclosing fees and costs in PDSs and periodic statements*

[RG 126](#) *Compensation and insurance arrangements for AFS licensees*

[RG 166](#) *Licensing: Financial requirements*

[RG 181](#) *Licensing: Managing conflicts of interest*

[RG 203](#) *Do I need a credit licence?*

[RG 205](#) *Credit licensing: General conduct obligations*

[RG 209](#) *Credit licensing: Responsible lending conduct*

[RG 234](#) *Advertising financial products and advice services (including credit): Good practice guidance*

[RG 259](#) *Risk management systems of responsible entities*

### Information sheets

[INFO 213](#) *Marketplace lending (peer-to-peer lending) products*

### Legislation

ASIC Act, Pt 2 Div 2

Corporations Act, s601GA, Ch 5C Pt 5C.6, s911A, s912A, s912B, s912D, s1013K, s1018A, s1018B, Ch 7 Pt 7.10

National Credit Act, Ch 3 Pt 3-2C

National Credit Code, s23A, s26, Pt 2 Div 4, Pt 4 Div 3, s82, s192

## Cases

*Australian Securities and Investments Commission v Avestra Asset Management Limited (In Liquidation)* [2017] FCA 497

## Reports

[REP 420](#) *Overview of decisions on relief applications (June to September 2014)*

[REP 429](#) *Cyber resilience: Health check*

[REP 435](#) *Overview of decisions on relief applications (October 2014 to January 2015)*

[REP 523](#) *ASIC's Innovation Hub and our approach to regulatory technology*

## Media releases

[Media Release \(17-056MR\)](#) *ASIC and ASBFEO join forces to ensure bank lenders meet unfair contract laws* (9 March 2017)

[Media Release \(17-139MR\)](#) *ASIC and ASBFEO hold banks to account on unfair contract terms* (16 May 2017)

## Non-ASIC documents

IOSCO, [Crowdfunding: 2015 survey responses report](#) (PDF 0.5 MB), report, December 2015

The Hon Scott Morrison MP, Treasurer, [Building an accountable and competitive banking system](#), media release, 9 May 2017