

3 June 2021

Niki De Mel
Strategic Policy Adviser, Strategy Group
ASIC

Via Email: BR.submissions@asic.gov.au

Response to CP340 – draft RG78 and Information Sheet

Dear Niki,

Thank you for the opportunity to provide feedback to Consultation Paper 340: Breach Reporting and related obligations.

In addition to providing our specific feedback to the questions raised in the appendix, we set out some insights below that may assist ASIC in finalising Regulatory Guide 78 and the related obligations to notify, investigate and remediate.

Who are we

In March 2021, Loan Market Australia purchased the Plan, Choice and FAST aggregation businesses and the Australian Credit Licensee, BLSSA Pty Ltd. Combined, the Loan Market Group (which includes Loan Market Australia Pty Ltd and Loan Market Broker Services Pty Ltd as credit licensees and Wealth Market Pty Ltd holding a financial services licence) represents approximately 30% of the broker market and has approximately 5000 brokers using Group services. Approximately half of those brokers are credit representatives of the Group. As aggregators, the Group has contractual obligations to manage its agreement holders and as such will assist and monitor the other 50% of broker firms that hold their own credit licences.

Key themes

The themes that are outlined in this response focus on the newly created *credit* obligations as these represent the majority of the Group's compliance base.

The Group is supportive of the proposed changes and the guidance assisting licensees to comply. However, in short, we consider it would be useful for ASIC to provide the following:

- examples of what would constitute a reportable situation in responsible lending conduct and best interests duty.
- clarity on the scope of serious fraud where it is not clear that the mortgage broker was involved.
- outline expectations for all parties on liability for remediation between a lender and broker.
- Access to breach reports from lenders and licensees to aggregators

Reporting best interests duty breaches

We consider that reporting breaches of best interests duty will require specific examples. A principles based duty (even responsible lending) is by design, specific to each loan. However, without clarifying the boundaries, there is the potential for under or over-reporting. To promote consistent reporting, some examples of scope of reporting would assist. For example:

- A broker undertaking financial inquiries by reviewing one month's statement of account, where the licensee requires 3 months' accounts. While this may require coaching by the licensee, we do not expect this, without more, to be reportable.
- Broker completed a loan application prior to undertaking a preliminary assessment (or no evidence of it). In this instance there is no evidence of inquiry or acting in the best interests of the client. We consider this to be reportable.
- A broker recommends a variable rate loan and there is no indication of other considerations including from the client. The broker then completes an application for a 4 year fixed rate loan. We consider this to be reportable because there is no evidence of a fixed rate loan being in the best interests of the client.
- A broker discusses fixed and variable rate loans with the client who is aware that a fixed rate may be useful from time to time. The broker recommends a product that can be switched from a fixed to variable rate at any time but the initial rate is variable. The rates change and the broker helps the client fix the rate 12 months into the loan. We consider this is not reportable as there is sufficient evidence of the broker conducting inquiries and making a recommendation that is in the best interests of the client.

Material loss and remediation

Our experience with complaints is that clients find it difficult to quantify loss. In addition, *material* loss to a client as against the conduct of a licensee or broker is difficult to determine.

Broadly, a mortgage broker's role is to determine which product is in the best interests of a client. When the lender makes their final credit assessment, the client has obtained an asset in the property at a cost.

Our view is that if the broker directed the client to a product that is not in a client's best interests, the loss *should not be* determined by the difference between the rate the lender gave and a comparable rate for a product that is in the client's best interests for the life of the loan. We consider that the broker should not be responsible for that difference for the entire life of the loan. This is because rates will vary over time depending on market conditions, lender, jurisdiction and product. Further, the broker has no ability to modify an interest rate set by the lender. While each case will turn on its facts, some worked examples are required to ensure client and regulator expectations are clear. For example, an alternative remediation for broker misconduct may be for the broker to cover costs of a refinance to a comparable lender and product. It will then be up to the client to accept that offer. Providing worked examples of loss with respect to broker and lender conduct is, we submit, necessary.

Serious fraud and remediation

Where there is reasonable suspicion of fraud, it is not feasible to investigate all the mortgage broker portfolio. Doing so will impose a significant cost in terms of time and resources. In addition, this effort may result in inconclusive outcomes. Further, if we suspect a third party or client is a participant in a fraud, it is often difficult to prove who was the fraudulent party.

First, our experience is that it is difficult to determine who was involved in a suspected fraud. Often we see clients being blind to conduct or involved in conduct of, for example, a local accountant providing false information to the client in order to assist that client obtain a home loan. Further, we may not have access to that third party information to assess involvement and the client is unlikely to divulge they were complicit.

Second, licensees are often dependent on lenders providing information in respect to suspected fraud. In our experience lenders are inconsistent in their approach to sharing information to assist a licensee's investigation. This can impact a licensee's ability to promptly identify, report and address misconduct.

In terms of an *investigation* of a suspected fraud, our view is that unless there is evidence to the contrary, the investigation should be directed to, in our example, those clients that used that accountant rather than the broker's entire portfolio. We would appreciate clarification on this point.

However, while we agree these instances are reportable, it is not clear what the expectation is on the credit licensee with respect to *remediation* where there is doubt about whether the client was involved in the fraud. Our proposal is that where there is *evidence* of client involvement, remediation should not be awarded.

Access to reports

Aggregators provide an intermediary function between lenders and brokers. As a result, they have contractual obligations to monitor broker conduct. However, as set out above, not all brokers are the aggregators' credit representatives and not all aggregators are credit licensees.

A lender may report on the misconduct of a mortgage broker and provide the report to that broker's licensee. Part of the aggregator's role when this occurs is to facilitate discussions and, sometimes, conduct its own investigations on that brokers conduct. Without access to the report from the lender or other licensee, the aggregator may not be aware of the scope of the activities or be able to effectively investigate for the purposes of fulfilling those contractual obligations. Our view is that in order to do so aggregators will require access to those brokers and other licensees that report or are being reported on. We are aware that this request may require legislative change. However, short of that, we request some reference to the free flow of information between lenders and aggregators to assist in the operation of the regime.

If you have any questions or require any further information, please do not hesitate to contact John Evangelista on [REDACTED]

[REDACTED] or David McQueen on [REDACTED]
[REDACTED]

Yours sincerely

John Evangelista
Head of Regulation and Governance
For the Loan Market Group

Appendix -Specific feedback to the questions raised in CP340.

B1 We propose to give consistent guidance for AFS licensees and credit licensees on how they can comply with the breach reporting obligation, with examples of how the obligation applies in particular situations.

<p>B1Q1 Do you agree with our proposed approach? If not, why not?</p>	<p>Yes.</p>
<p>B1Q2 Are there differences in the structure or operation of credit licensees that require specific guidance on how the breach reporting obligation applies?</p>	<p>Yes. We consider that there are important differences that need consideration when including examples in the regulatory guide.</p> <p>Unlike financial advice, a credit assistance provider broadly recommends a product and lender that is in the best interests of a client. The lender will then undertake their responsible lending obligations and approves the loan.</p> <p>In our view this impacts on questions relating to who reports, who is responsible for what breach, and what is the scope of remediation.</p>

B2 We propose to include case studies and scenarios to supplement our general guidance and help illustrate key principles as they might apply to different licensees, industries and business models.

<p>B2Q1 Are there any specific issues, incidents, challenges or areas of concern you think we should include as examples, case studies or scenarios? If so, please provide details and explain why they should be included.</p>	<p>As set out above, we would welcome examples where ACL holders have conducted investigations that have found one of the following outcomes:</p> <ul style="list-style-type: none">- Customer led fraud (no fault of broker)- Broker led fraud- Inconclusive findings- No breach however some gaps in NCCP processes (eg, failure to follow licensee procedure)
---	---

B3 Draft RG 78 identifies where the existing breach reporting obligation (as in force immediately before 1 October 2021) continues to apply to AFS licensees: see draft RG 78.14–RG 78.18.

<p>B3Q1 Should we include further guidance to help AFS licensees understand how the existing breach reporting obligation under s912D of the Corporations Act (as in force before 1 October 2021) applies? If so, please provide details.</p>	<p>No comment.</p>
--	--------------------

B4 We propose to provide high-level guidance to help AFS licensees and credit licensees identify what they must report to ASIC, including guidance on:

- (a) what is a ‘reportable situation’ (see draft RG 78.19–RG 78.25);
- (b) whether a breach or likely breach of a core obligation is significant (see draft RG 78.26–RG78.45);
- (c) when an investigation is a reportable situation (see draft RG 78.46–RG 78.57);
- (d) what are ‘additional reportable situations’ (see draft RG 78.58–RG 78.60); and
- (e) what are reportable situations about other licensees (see draft RG 78.61–RG 78.67).

<p>B4Q1 Do you agree with our proposed approach? If not, why not?</p>	<p>Yes</p>
<p>B4Q2 Should we include further guidance on what constitutes a ‘core obligation’? If so, please provide details.</p>	<p>Yes. In particular, for how this relates to obligations under BID (see main response) will enable us to report in a consistent manner.</p> <p>Clarity also provides the licensee (and aggregator) the opportunity to curate relevant training and education tools to help brokers (those giving credit assistance).</p>
<p>B4Q3 Should we include further guidance on how to determine whether a breach or likely breach of a core obligation is ‘significant’? If so, please provide details.</p>	<p>Yes, See our response to B4Q2.</p>

<p>B4Q4 Should we include further guidance on reporting an ‘investigation’ to ASIC? If so, what should be clarified? Please provide examples of scenarios (where relevant).</p>	<p>No</p>
<p>B4Q5 Should we include further guidance on what constitutes ‘material loss or damage’? If so, what are the challenges licensees face in determining whether loss or damage is material? Please provide examples of how you consider questions of material loss or damage.</p>	<p>Yes, see main response.</p>
<p>B4Q6 Should we include further guidance on reportable situations involving serious fraud or gross negligence? If so, what are the challenges licensees face in identifying when serious fraud or gross negligence has occurred?</p>	<p>Yes. see main response.</p>
<p>B4Q7 Should we include further guidance on reportable situations about other licensees? If so, please provide details.</p>	

B5 We propose to include guidance in draft RG 78 about the obligation for licensees to report to ASIC within 30 days after they first know that, or are reckless with respect to whether, there are reasonable grounds to believe a reportable situation has arisen: see draft RG 78.68–RG 78.81.

<p>B5Q1 Should we include further guidance to help licensees understand when to report to ASIC? If so, please provide details, including what guidance would be helpful and why.</p>	<p>Reasonable Grounds: The majority of brokers are small businesses, sole operators or 1-2 staff, so providing a ‘scaled’ example will help to</p>
--	---

	provide better effective training on what each means.
B5Q2 Should we include further guidance on what may amount to 'knowledge', 'recklessness' and 'reasonable grounds'? If so, please explain what specific guidance would be helpful and why.	Yes. Providing examples of what representatives of a licensee may find (ie, sales staff, someone doing a review on a credit representative) or an administrative support person in the broker's office will help identify self-reporting examples -particularly for smaller ACL holders.
B5Q3 Should we include any additional or alternative guidance to help licensees provide reports to ASIC in a timely manner? If so, please give details.	

B6 We propose to provide general guidance on the types of information we will include in the prescribed form that licensees must use to provide reports to ASIC: see Table 8 in draft RG 78

B6Q1 Do you have any feedback about the types of information we propose must be included in the prescribed form? If so, please provide details, and identify any issues.	Our feedback here is to make those forms easy for a small business owner to complete - without the need for legal advice.
B6Q2 Should we include any other information in the prescribed form? If so, please provide details.	Potentially -there should be the ability to ensure that a licensee can include all relevant information about any third party that may be involved in a breach.
B6Q3 Do you have any concerns about the types of information in the prescribed form and whether this information can be provided within the prescribed 30-day time period? If so, please provide details.	

B7 We propose to provide high-level guidance on compliance systems for breach reporting to help licensees comply with the breach reporting obligation: see Section D of draft RG 78.

B7Q1 Do you agree with our proposed approach? If not, why not?	Yes.
B7Q2 Are there any other specific areas that we should consider including in our guidance? If so, please provide details.	
B7Q3 Are there any challenges that you would face in applying our guidance to your specific circumstances (i.e. the nature, scale or type of your business)? If so, please provide details.	Loan Market Group is sufficiently resourced to manage reporting obligations. However, we point out that credit licensees that are small businesses may struggle due to the nature of their business.

C1 We propose to provide guidance for AFS licensees who are financial advisers and credit licensees who are mortgage brokers. The new obligations require these licensees to notify, investigate and remediate affected clients in certain circumstances. We have set out our proposed guidance in an information sheet: see draft INFO 000 in Attachment 2 to this paper.

C1Q1 Do you agree with our proposed approach? If not, why not?	Yes.
C1Q2 Should the guidance we provide on the new obligations be provided in the form of a separate information sheet, or be incorporated into RG 256? Please provide details.	
C1Q3 Should we include further or more specific guidance on the circumstances in which licensees must: (a) notify affected clients of a breach of the law; (b) investigate the full extent of that breach; or (c) remediate affected clients?	Yes. As set out in the main response, clarification on the scope of investigation and what is the expectation on the licensee to remediate customers who may be complicit in the breach (when it relates to misconduct).

If so, what other information would be helpful in determining how these obligations apply?	
--	--

C2 We propose to give high-level guidance to AFS licensees and credit licensees about the types of information we consider should be included in the notices that must be given to affected clients: see in Actions 1 and 3 of draft INFO 000 in Attachment 2 to this paper.

C2Q1 Do you agree with our proposed approach? If not, why not?	Yes.
C2Q2 Should the form of the notices referred to in Actions 1 and 3 of the information sheet be approved by ASIC? If so, what information, or types of information, should be mandatory, and what should be left to the discretion of the licensee?	We consider that the respective licensee could draft the notices to include the guidance provided by ASIC.