

21 May 2009

Manager
Consumer Credit Unit
Corporations and Financial Services Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: consumercredit@treasury.gov.au.

AFG thanks the government for the opportunity to comment on the National Consumer Credit Protection Bill and associated bills and regulations.

AFG is Australia's largest finance broking aggregation company. We provide aggregation services to over 2,500 brokers Australia wide.

AFG has always been a strong supporter of appropriate regulation for the finance industry. We welcome the licensing of credit intermediaries and lenders, and support the thrust of the proposals.

We have been able to review a preliminary draft of the submissions to be made by the Mortgage and Finance Association of Australia (MFAA) and generally support the thrust of those submissions.

As Australia's largest aggregator, AFG takes compliance with all laws very seriously. We have extensive training processes and systems in place to ensure the highest compliance levels. Our comments should be read in that context.

Licensing requirements

We understand that it is intended that the requirements to obtain an Australian Credit Licence will be reasonably obtainable by the majority of mortgage brokers who are currently members of professional associations such as the MFAA.

However, much of LIC170 is lifted from the Corporations Act and mirrors the requirements for obtaining an AFSL.

We are concerned that a regulator or a court when faced with broadly identical language will have difficulty in imposing different standards. This concern is widespread amongst the industry.

If it is difficult to obtain an ACL, many finance brokers will instead need to become credit representatives. This is likely to significantly increase the cost of business and is a substantial change to the way in which the industry currently operates. In WA it is usual for individual loan writers to be licensed.

If only large brokers and aggregators are able to obtain an ACL, there will be a substantial lessening of competition in the industry, because small brokers will effectively be excluded.

In this regard we are particularly concerned about the requirement for a license holder to have in place;

- a plan to maintain competencies
- a training plan for representatives
- An Internal Dispute Resolution process (IDR)
- Systems and a written compliance plan
- And adequate financial and human resources and risk management plan.

Whilst we understand and support what the legislation is trying to achieve, we believe these requirements may be beyond the small broker and may force many otherwise highly competent and honest brokers from the industry. In particular the requirement for an IDR is impractical for a single person operation.

It is also important that the difference between the requirements for an AFSL and an ACL are embedded in legislation to avoid misinterpretation by the courts or regulators.

Role of an aggregator concerning unsuitable loans

Although there are differences between business models, generally aggregators provide support services to brokers and are a conduit from brokers to lenders. Brokers lodge loan applications direct with lenders. Aggregators are not involved in the credit decision.

We read the Exposure Draft to mean that customer facing brokers and lenders will have a responsibility not to arrange unsuitable loans. The legislation does not seek to impose a duty to review the credit or a liability for unsuitable loans upon aggregators. We submit this result is appropriate.

Helping our members assess if a loan is unsuitable

AFG may supply tools to its members to assist members comply with the legislation. These may include tools to assist members assess whether a loan is unsuitable.

Penalties are inappropriate

We object to penalties applying for arranging an unsuitable loan. We accept that a broker should be obliged not to arrange an unsuitable loan – and breach of this obligation on a regular basis should be grounds for disciplinary action. However, the risk of being penalised for isolated errors (especially given that there is no clear distinction between a suitable loan and an unsuitable loan) is wholly inappropriate.

Increased PI costs

The feedback from our PI insurer is that the penalties proposed will increase potential exposure to insurers and increase premiums. This will place an additional and unintended burden on brokers and aggregators.

- While insurers may cover the defence costs in the event of an official inquiry it is highly unlikely they would pay the fine or penalty. It is also highly unlikely many licensees would be able to fund \$220K - \$1.1M;

- Insurers will have difficulty in providing some of the key coverage's. Examples include fraud and run off exposures. Others like EDR awards increasing to \$280K will reduce competition.
- The PI requirements will increase the exposure to insurers and premiums will increase due to the perceived higher risk.

How does a broker assess whether a loan is unaffordable?

AFG brokers currently obtain information from borrowers regarding their financial position, and in particular details of their income and expenses. Based on the information provided by the consumer, our representatives using AFG's sophisticated systems determine what loans they can afford. Our automated software then provides a selection of the most appropriate loans for the customer's circumstances, from which the customer can choose. We submit that calculation of serviceability in this fashion is a sufficient test of affordability. We believe this should be made clearer in the legislation.

Verification of financial position

Lender's requirements and procedures for brokers vary significantly. Some lenders require brokers to obtain evidence of income and assets; others prefer to do that themselves.

In any case, brokers only ever conduct a **preliminary** verification as usually lenders make further enquiries. The broker's verification obligations should be further limited to verification by reference to information **provided by the borrower**, leaving the lender to obtain any verification from third parties considered appropriate. It is often impractical for brokers to conduct any further verification.

Because of the significant education and system change requirements, we submit that assessment of unsuitable loans should be delayed until phase 2 to allow proper and rigorous systems to be established.

Even without the unsuitable loan provisions, the legislation provides significant consumer protection by ensuring that consumers have access to EDR and that lenders and intermediaries need to be licensed and registered. The additional imposition of testing unsuitability in a formal way and being liable to a penalty if that task is not performed properly, is unwarranted from a commercial perspective (given the lenders will have this obligation) and not capable of being implemented within the time allowed.

Information for aggregators

It is likely we will adopt a model where most if not all of our members are licensed in their own right. In order to discharge our obligations to lenders and other members, it is important that we know if one of our members is being investigated or is the subject of complaint or censure.

It is also important that ASIC is obliged to inform the licensee if one of its representatives is being investigated or is the subject of complaint or censure.

The Exposure Draft does not require ASIC to provide that information to a licensee's aggregator. We submit that such an obligation is essential for the proper running of the industry.

Commission disclosures

R130 – Credit guide of credit assistance providers

R130 requires an intermediary to provide a credit guide soon after ‘it is likely to provide credit assistance’.

Under R130(2)(e) the credit guide is required to provide:

- (i) commissions expressed in their dollar value;
- (ii) the amounts of those commissions, or the range of those amounts; and
- (iii) the method for working out those amounts.

These three paragraphs conflict with each other. What is intended?

At the time a credit guide is provided, the loan product will usually not have been selected and so it will be impractical to disclose commissions other than in very general terms. The credit guide should only give a **generic description** of how the intermediary is paid.

Disclosure of specific commission amounts (other than those payable by the consumer) is usually not useful information for consumers. We understand the intent of such disclosure – that is, to assist the consumer identify whether a product is being favoured by the broker because the commission is higher. However, we wonder whether consumers can identify that issue. Even if the consumer does identify the issue, we suspect that brokers can present plausible explanations that dismiss any concern. We consider consumers are better protected by a broker’s obligation to act honestly and fairly. We submit that disclosure of specific commission payable other than by the consumer should be deleted from the proposals.

If despite our submission to the contrary, it is decided to require **specific commission disclosure**, it is important to recognise that it will usually never be possible to express commission in dollar terms because:

- trail commission is payable on the variable monthly balances of the loan account (so this amount is unascertainable); and
- Many lenders pay bonuses to aggregators having regard to factors such as service levels and performance of the portfolio. The amount of these bonuses can only be ascertained well after the loan has settled.
- Most lenders have upfront commission clawback provisions in place that extend out to 18 months if the loan is repaid in this time frame. This impacts the amount of commission the broker ultimately receives.

Instead, we suggest a regime under which commission is disclosed in bands, and specific commission disclosure is never required. Disclosure in bands is more useful to the consumer as it facilitates comparison. A suggested regime appears below.

Range	Lenders
Upfront commissions (% of loan amount)	
0.0% to 0.3%	[name each lender falling in each band]
Over 0.3% to 0.6%	
Over 0.6% to 1.0%	
Over 1.0%	
Trail commissions (%pa of loan balance)	
0.0% to 0.3%	
Over 0.3% to 0.6%	
Over 0.6% to 1.0%	
Over 1.0%	

Provision of credit assessment

R170 requires brokers to provide consumers with a written copy of the preliminary credit assessment conducted by the broker.

Provision of credit assessments should be abandoned or postponed to Stage 2

There are significant systems issues involved in arranging for borrowers to be provided with a copy of the credit assessment. Some of the difficulties are discussed under the next two headings.

We submit that this requirement should be deleted in full or at least postponed until Phase 2. If this submission is rejected, we press for the changes described under the next two headings.

Provide credit assessment only if credit is provided

The note forming part of R170 states that the licensee is only required to provide a copy of the credit assessment if credit assistance is provided. Under DEF7, an intermediary can provide credit assistance even if a loan is not arranged. We submit that the obligation to provide the credit assessment should only apply if a loan is actually made. This recognises that the purpose of providing the credit assessment is to allow a consumer who finds themselves in difficulty a way to investigate whether the intermediary or the lender acted improperly in arranging or making the loan.

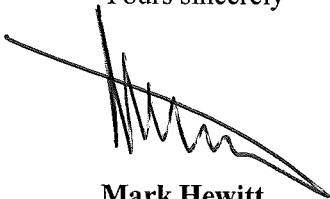
Specify what amounts to a credit assessment

What amounts to a copy of a credit assessment is unclear. Particularly for lenders, a credit assessment could be very lengthy and deal with things such as policies relating to geographic areas, socio-economic groups, and other sensitive commercial information that should not be made available. The legislation needs to make it clear that the copy of a credit assessment that must be provided is limited to a demonstration of loan serviceability based on the customers declared income and expenses..

Standard templates

Our experience with the WA regulations has been that that a great deal of confusion has been generated by the lack of a standard template for disclosure documents being provided by the regulator. This leaves some parts of the legislation open to individual interpretation. It is our strong recommendation that that standard or base documents be developed and provided by the regulator as part of this legislation.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Mark Hewitt', with a long horizontal stroke extending to the left.

Mark Hewitt

General Manager Sales & Operations

Australian Finance Group