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NATIONAL CONSUMER CREDIT PROTECTION AMENDMENT (MORTGAGE  
BROKERS) BILL 2019

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EXPOSURE DRAFT EXPLANATORY MATERIALS



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# ***Glossary***

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The following abbreviations and acronyms are used throughout this explanatory memorandum.

<b><i>Abbreviation</i></b>	<b><i>Definition</i></b>
Credit Act	<i>National Consumer Credit Protection Act 2009</i>
Bill	<i>National Consumer Credit Protection Amendment (Mortgage Brokers) Bill</i>
Final report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry	Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, Volume 1, February 2019.



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# ***Mortgage broker reforms***

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## **Outline of chapter**

- 1.1 Schedule 1 to the Bill amends the Credit Act to
- require mortgage brokers to act in the best interests of consumers; and
  - address conflicted remuneration for mortgage brokers.

## **Context of amendments**

1.2 Mortgage brokers assist consumers to obtain home loans by approaching and negotiating with lenders on consumers' behalf. Mortgage brokers suggest particular loans to consumers based on information about the consumer and various loan products. However, most consumers do not pay mortgage brokers for their services. Instead, lenders generally pay mortgage brokers for their services by way of a fixed commission or a commission based on the size of the consumer's loan. Mortgage brokers also receive volume-based commissions or 'campaign-based' commissions, which are paid on top of the standard commissions. Lenders also provide other 'soft-dollar' or non-monetary benefits, such as training conferences and hospitality.

1.3 The Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry considered mortgage broking in Australia and made recommendations relating to mortgage brokers, including recommendation 1.2 (the best interests duty) and recommendation 1.3 (mortgage broker remuneration). In response to the Royal Commission, the Government committed to a number of reforms in relation to the regulation of mortgage brokers including to:

- introduce a duty for mortgage brokers to act in the best interests of consumers; and
- address conflicted remuneration for mortgage brokers.

1.4 Requiring mortgage brokers to act in the best interests of consumers and addressing conflicted remuneration are intended to strengthen existing protections for consumers who deal with mortgage brokers. In particular, they bring the law into line with what consumers expect – that any advice provided by a mortgage broker serves the consumer's interests first and foremost.

1.5 Within the mortgage broking market, businesses known as ‘aggregators’ act between brokers and lenders by providing technology and administrative support (e.g. facilitating the processing of applications and providing training and professional development programs for brokers). Brokers also rely on aggregators because they have contractual arrangements with lenders, which allow the brokers operating under the aggregator to arrange loans from those lenders.<sup>1</sup>

## Summary of new law

1.6 Schedule 1 to the Bill amends the Credit Act to require mortgage brokers to act in the best interests of consumers and to address conflicted remuneration for mortgage brokers and mortgage intermediaries such as aggregators. These new laws improve consumer outcomes by requiring brokers to act in the best interests of their clients and by reducing the potential for conflicts of interests to arise which may impact the advice consumers receive from brokers.

The key features of the new law are:

- Mortgage brokers must act in the best interests of consumers in relation to credit assistance in relation to credit contracts.
- Where there is a conflict of interest, mortgage brokers must give priority to consumers in providing credit assistance in relation to credit contracts.
- Mortgage brokers and mortgage intermediaries must not accept conflicted remuneration.
- Employers, credit providers and mortgage intermediaries must not give conflicted remuneration to mortgage brokers or mortgage intermediaries.
- The circumstances in which these bans on conflicted remuneration apply are to be set out in the regulations.

## Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Mortgage brokers are required to act in the best interests of their clients and to prioritise their clients’	No equivalent.

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<sup>1</sup> See paragraph 14, ASIC Report 516, Review of mortgage broker remuneration, March 2017.

interests when providing credit assistance.	
Regulations can restrict the circumstances in which conflicted remuneration can be given or received in connection with credit services provided by mortgage brokers and intermediaries.	No equivalent.

## Detailed explanation of new law

- 1.7 Schedule 1 to the Bill amends the Credit Act to
- require mortgage brokers to act in the best interests of consumers; and
  - address conflicted remuneration.

1.8 The objective of the new law is to improve consumer outcomes. It does this in two main ways. Firstly, by requiring mortgage brokers to act in the best interests of their clients. Secondly, by reducing the potential for conflicts of interests to impact the advice consumers receive from mortgage brokers. *[Schedule 1, item 5, section 158K of the Act]*

1.9 The new law expressly clarifies that the obligations it imposes are in addition to any other obligations to which the person is subject under the Act or any other law. This ensures that the new law does not affect existing laws that protect or otherwise benefit consumers. *[Schedule 1, item 5, section 158KC of the Act]*

## Meaning of *mortgage broker* and *mortgage intermediary*

1.10 The new law imposes obligations on mortgage brokers and mortgage intermediaries.

1.11 A mortgage broker, for the purposes of the new law, can be either a licensee or a credit representative of a licensee that carries on a mortgage broking business. In particular the new law defines a mortgage broker as a licensee or a credit representative of a licensee that:

- carries on a business of providing credit assistance in relation to credit contracts secured by mortgages over residential property; and *[Schedule 1, items 3 and 4, subsection 5(1) definition of ‘mortgage broker’ and paragraphs 15B(1)(a) and 15B(2)(a) of the Act]*
- does not perform the obligations, or exercise the rights, of a credit provider in relation to the majority of those credit contracts. *[Schedule 1, items 3 and 4, subsection 5(1) definition of ‘mortgage broker’ and paragraphs 15B(1)(b) and 15B(2)(b) of the Act]*

1.12 Credit assistance is an existing term that is defined in section 8 of the Credit Act. It covers a broad range of conduct engaged in by a person dealing directly with the consumer or the consumer's agent in the course of, as part of, or incidentally to, a business carried on in this jurisdiction and relevantly includes:

- suggesting that the consumer apply for a particular credit contract with a particular credit provider;
- suggesting that the consumer apply for an increase to the credit limit of a particular credit contract with a particular credit provider;
- suggesting that the consumer remain in a particular credit contract with a particular credit provider;
- assisting the consumer to apply for a particular credit contract with a particular credit provider; and
- assisting the consumer to apply for an increase to the credit limit of a particular credit contract with a particular credit provider.

1.13 Credit contracts are contracts under which credit is or may be provided, being credit to which the National Credit Code applies.<sup>2</sup> Sections 5 and 6 of the National Credit Code detail the provision of credit to which the National Credit Code applies, and exclude various types of credit contracts. Some exclusions are relevant in the mortgage broker context. For example, the National Credit Code only applies to credit contracts where the debtor is a natural person or strata corporation.

1.14 For the purposes of the new law a mortgage intermediary is either a licensee or a credit representative of a licensee that acts as an intermediary in relation to mortgages. In particular the new law defines a mortgage intermediary as a licensee or a credit representative of a licensee that:

- carries on a business of acting as an intermediary in relation to credit contracts secured by mortgages over residential property; and [*Schedule 1, items 3 and 4, subsection 5(1) definition of 'mortgage intermediary' and paragraphs 15C(1)(a) and 15C(2)(a) of the Act*]
- does not perform the obligations, or exercise the rights, of a credit provider in relation to the majority of those credit contracts. [*Schedule 1, items 3 and 4, subsection 5(1) definition of*

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<sup>2</sup> Schedule 1 to the Credit Act contains the National Credit Code. The National Credit Code includes regulations made under the Credit Act for the purposes of the National Credit Code and instruments made under Schedule 1 of the Credit Act: see the definition of National Credit Code in section 5 of the Credit Act.

***‘mortgage intermediary’ and paragraphs 15C(1)(b) and 15C(2)(b) of the Act***

1.15 What amounts to acting as an intermediary is currently defined in section 9 of the Act. Under that section a person is acting as an intermediary where, in the course of their business, the person acts as an intermediary (whether directly or indirectly) between a credit provider and a consumer wholly or partly for the purposes of securing the provision of credit for the consumer under a credit contract.

1.16 The definitions of mortgage broker and mortgage intermediary are intended to only capture those businesses that would ordinarily be described as a mortgage broking or mortgage intermediary businesses. In particular, the definitions of both terms are not intended to extend to credit providers where they are providing credit assistance in relation to their own products rather than providing broking or intermediary services. *[Schedule 1, item 4, paragraphs 15B(1)(b), 15B(2)(b), 15C(1)(b) and 15C(2)(b) of the Act]*

***Licensees and credit representatives are liable for the conduct of individual brokers***

1.17 The new law also provides that, where a person is authorised as a credit representative of a licensee by a credit representative that is a body corporate, the secondary representative is taken to be acting within the scope of the secondary representative’s actual or apparent authority from the licensee if the secondary representative is acting within the actual or apparent scope of the authority given by the primary representative to engage in specified credit activities on behalf of the licensee. *[Schedule 1, item 5, section 158KB of the Act]*

## **The new best interests obligations**

1.18 Schedule 1 to the Bill imposes new obligations on mortgage brokers to act in the best interests of consumers. The new obligations apply in relation to licensees that are mortgage brokers, credit representatives that are mortgage brokers, and representatives of credit representatives that are mortgage brokers (all references to mortgage brokers are references to persons to whom the new obligations apply unless indicated otherwise). The obligations are directed at improving outcomes for consumers by legally requiring that mortgage brokers act in their consumer’s best interests and place their consumer’s interests before their own. The new best interests obligations do not affect the existing responsible lending obligations under the Credit Act.

1.19 The obligations apply in relation to credit assistance provided by mortgage brokers in relation to any credit contract. This ensures that when mortgage brokers deal with consumers in relation to mortgages, the broker must act in the best interests of the consumer not only in relation to the

mortgage but also in relation to any other credit contracts for which they provide credit assistance. Examples of other credit contracts in relation to which a mortgage broker may provide credit assistance include credit cards and personal loans that are packaged with the mortgage as well as unsecured credit for home renovation. *[Schedule 1, item 5, subsection 158L(1) and sections 158LA, 158LD and 158LE of the Act]*

1.20 The duty to act in the best interests of the consumer in relation to credit assistance is a principle-based standard of conduct that applies across a range of activities that licensees and representatives engage in.<sup>3</sup> As such, what conduct satisfies the duty will depend on the individual circumstances in which credit assistance is provided to a consumer in relation to a credit contract. Consistent with the recommendation of the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, the duty does not prescribe conduct that will be taken to satisfy the duty in specific circumstances. It is the responsibility of mortgage brokers to ensure that their conduct meets the standard of ‘acting in the best interests of consumers’ in the relevant circumstances. *[Schedule 1, item 5, section 158KA of the Act]*

1.21 By way of illustration, a consumer could be provided with credit assistance by a mortgage broker in a variety of ways. For example, the credit assistance could consist of a broker recommending one or more home loan products out of a selection of home loan products and then assisting the consumer to apply for the product the consumer selects. The content of the duty ultimately depends on the circumstances in which such credit assistance is provided and would include a failure to do certain things. Examples of such content that might arise under certain circumstances are:

- prior to recommending any home loan product or other credit contract to a consumer based on consideration of that consumer’s particular circumstances, it could be expected that the mortgage broker consider a range of such products (including the features of those products) and inform the consumer of that range and the options it contains;<sup>4</sup>
- any recommendations made could be expected to be based on consumer benefits, rather than benefits that may be realised by the broker (such as commissions);

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<sup>3</sup> The new law also aims to ensure a broad interpretation of what constitutes an ‘act’ for the purposes of the new obligations, and also includes an omission or failure to act in the best interests of a consumer. In particular, the new law clarifies that for the purposes of the new law, a reference to doing an act or thing includes a reference to causing or authorising the act or thing to be done.

<sup>4</sup> Similar considerations would apply where a mortgage broker suggests that a consumer apply for an increase to the credit limit in a particular credit contract.

- in cases where critical information is not obtained when inquiring about a consumer's circumstances, the broker could be expected to refrain from making a recommendation about a loan where there is a consequent risk that the loan will not be in the consumer's best interests;
- a broker would not suggest a white label home loan that has the same features as a branded product from the same lender, but with a higher interest rate, because it would not be in the best interests of the consumer to pay more for an otherwise similar product; and
- during an annual review, a broker would not suggest that the consumer remain in a credit contract without considering whether this would be in the consumer's best interests.

1.22 In addition to the new best interests obligation, the new law also requires a mortgage broker to resolve conflicts of interests in the consumer's favour. In particular, if the mortgage broker knows, or reasonably ought to know, that there is a conflict between the interests of the consumer and the interests of the broker or a related party<sup>5</sup>, the mortgage broker must give priority to the consumer's interests. This requirement is based on section 961J of the Corporations Act, which places an equivalent obligation on financial advisers. *[Schedule 1, items 1 and 4, subsection 5(1) definition of 'associate' and section 15A of the Act]*

1.23 As noted, a mortgage broker may be a licensee or a credit representative. Where the mortgage broker is a credit representative:

- the obligations only apply where the broker is acting within the scope of the credit representative's actual or apparent authority from the licensee; and
- the licensee is required to take reasonable steps to ensure that the representative complies with the obligations requirement. *[Schedule 1, item 5, sections 158LB and 158LF of the Act] [Schedule 1, item 5, subsection 158L(2), section 158LD and subsection 158LE(2) of the Act]*

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<sup>5</sup> These include an associate of the mortgage broker, a representative of the broker, an associate of a representative of the broker and, where the broker is a credit representative of a licensee, also includes any other representative of the licensee and their associates. For the purposes of this obligation, the law defines *associate* by reference to the definition of associate in subsection 204(2) of the National Credit Code (which includes related bodies corporates, suppliers in respect of whom the credit provider is a linked credit provider, and the officers, agents and employees of the credit provider or any such related body corporate or supplier). The regulations may also prescribe additional circumstances in which a person is an associate of another.

## Conflicted remuneration

1.24 Schedule 1 to the Bill enables restrictions to be made on conflicted remuneration relating to mortgage broking. In particular, it allows regulations to provide circumstances under which conflicted remuneration cannot be given or accepted.

1.25 Conflicted remuneration means any benefit, whether monetary or non-monetary, that is:

- given to a licensee, or a representative of a licensee, who provides credit assistance to consumers that, because of the nature of the benefit or the circumstances in which it is given, could reasonably be expected to influence the credit assistance provided (including, therefore, the choice of credit contract or choice of credit provider); or *[Schedule 1, items 3 and 5, subsection 5(1) definition of 'conflicted remuneration' and paragraph 158N(a) of the Act]*
- given to a licensee, or a representative of a licensee, who acts as an intermediary and because of the nature of the benefit of the circumstances in which it is given, could be reasonably expected to influence whether or how the licensee or representative acts as an intermediary. *[Schedule 1, items 3 and 5, subsection 5(1) definition of 'conflicted remuneration' and paragraph 158N(b) of the Act]*

1.26 This definition of conflicted remuneration is in substance drawn from the definition of conflicted remuneration in Part 7.7A of the Corporations Act.

1.27 The regulations may also prescribe:

- circumstances in which a benefit given to a licensee or representative of a licensee is not conflicted remuneration; and *[Schedule 1, items 3 and 5, subsection 5(1) definition of 'conflicted remuneration' and paragraph 158NA(b) of the Act]*
- circumstances in which a benefit given to a licensee or a representative of a licensee is conflicted remuneration. *[Schedule 1, items 3 and 5, definition of 'conflicted remuneration' and paragraph 158NA(a) of the Act]*

1.28 The ability to prescribe by regulation what is and is not conflicted remuneration provides flexibility for the regime to efficiently and effectively respond to changes in industry practice and to ensure that the new regime operates for the benefit of consumers.

1.29 Regulations also give effect to the ban on conflicted remuneration. This provides flexibility to provide for the circumstances in which conflicted remuneration is banned.

1.30 The ban has two aspects: a prohibition on accepting conflicted remuneration and a prohibition on giving conflicted remuneration. In particular, in relation to accepting conflicted remuneration:

- a licensee must not accept conflicted remuneration in circumstances prescribed by the regulations if the licensee is a mortgage broker or mortgage intermediary; and *[Schedule 1, item 5, section 158NB of the Act]*
- a credit representative of a licensee must not accept conflicted remuneration in circumstances prescribed by the regulations, if the credit representative or the licensee is a mortgage broker or mortgage intermediary. The licensee must also take reasonable steps to ensure that its credit representative complies with this requirement. *[Schedule 1, item 5, section 158NC of the Act]*

1.31 Under the existing sections 324 and 325 of the Act, a licensee or credit representative will also be liable for the conduct of its agents, employees and other persons acting at the direction or with the consent or agreement (whether express or implied) of an official of the licensee. This means that if an employee or representative of a licensee who is a mortgage broker accepts conflicted remuneration in circumstances prescribed by the regulations, the licensee may be liable for breach of these provisions.

1.32 In relation to giving conflicted remuneration:

- an employer of either a licensee or a representative must not give the licensee or representative conflicted remuneration in circumstances prescribed by the regulations if the licensee or representative is a mortgage broker or mortgage intermediary; *[Schedule 1, item 5, section 158ND of the Act]*
- a credit provider must not give a licensee or representative conflicted remuneration in circumstances prescribed by the regulations if the licensee or representative is a mortgage broker or mortgage intermediary; and *[Schedule 1, item 5, section 158NE of the Act]*
- a mortgage intermediary must not give a licensee or representative conflicted remuneration in circumstances prescribed by the regulations if the licensee or representative is a mortgage broker or mortgage intermediary. *[Schedule 1, item 5, section 158NF of the Act]*

## Anti-avoidance

1.33 Schedule 1 to the Bill includes a prohibition on schemes to avoid the obligations imposed under the Bill. In particular, a person must not,

either alone or with other persons, begin to carry out or carry out a scheme if:

- it would be concluded that they did so for the sole purpose or for a purpose (that is not incidental) of avoiding the obligations in the Bill; and
- the scheme or a part of the scheme has or would achieve that purpose (but for the prohibition). [*Schedule 1, item 5, section 158T of the Act*]

1.34 The prohibition is necessary to support the effective operation of the obligations in the Bill. It is based on anti-avoidance provisions that apply in relation to financial advice obligations in Part 7.7A of the *Corporations Act 2001*.<sup>6</sup>

### Civil penalties

1.35 A contravention of each obligation in Schedule 1 to the Bill is a civil penalty. The maximum penalties applicable to each obligation are detailed in the following table.

#### Penalties concerning obligations

<i>Obligation</i>	<i>Penalty</i>
Failure of a licensee to act in the best interests of the consumer	5,000 penalty units
Failure of a licensee to give priority to the consumer’s interests	5,000 penalty units
Failure of a credit representative to act in the best interests of the consumer	5,000 penalty units
Failure of a licensee to take reasonable steps to ensure that the credit representative acts in the best interests of the consumer	5,000 penalty units
Failure of a credit representative to give priority to the consumer’s interests	5,000 penalty units
Failure of a licensee to take reasonable steps to ensure that credit representatives give priority to the consumer’s interests	5,000 penalty units
Licensee accepting conflicted remuneration	5,000 penalty units

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<sup>6</sup> See Division 6 of that Part.

<i><b>Obligation</b></i>	<i><b>Penalty</b></i>
Credit representative accepting conflicted remuneration	5,000 penalty units
Failure of licensee to take reasonable steps to ensure that credit representatives do not accept conflicted remuneration	5,000 penalty units
Employer of licensee giving licensee conflicted remuneration	5,000 penalty units
Employer of licensee giving representative conflicted remuneration	5,000 penalty units
Credit provider giving licensee conflicted remuneration	5,000 penalty units
Credit provider giving representative conflicted remuneration	5,000 penalty units
Mortgage intermediary giving licensee conflicted remuneration	5,000 penalty units
Mortgage intermediary giving representative conflicted remuneration	5,000 penalty units
Engaging in avoidance scheme	5,000 penalty units

1.36 The existing enforcement regime in the Credit Act also applies in relation to contravention of the obligations. For example, the ability of courts to provide a range of remedies under Part 4-2 of Chapter 4 of the Act, including injunctions, compensation orders, and other orders, could apply to contraventions of the above obligations.

## Consequential amendments

1.37 The Bill makes a number of consequential amendments that ensure that all provisions of the Act that currently apply in relation to ‘commissions’ also apply in relation to ‘conflicted remuneration’. The affected provisions generally relate to information that must be disclosed to consumers in particular circumstances or the conditions that must be met if certain words such as “independent”, “impartial” or “unbiased” are to be used in connection with a credit service. *[Schedule 1, item 2, subsection 5(1) (definition of ‘commission’) of the Act; Schedule 2, items 1 to 23, subsection 5(1) definition of ‘indirect remuneration’, paragraph 92(e), section 111, subparagraphs 113(2)(g)(i), 113(2)(g)(ii), 113(3)(b)(i) and 113(3)(b)(ii), Division 5 of Part 3-1 of Chapter 3 (heading), Section 121 (heading), paragraphs 121(2)(b), 121(3)(a) and 121(3)(b), section 134, subparagraphs 136(2)(g)(i), 136(2)(g)(ii), 136(3)(b)(i) and 136(3)(b)(ii), Division 5 of Part 3-3 of Chapter 3 (heading), section 144 (heading), paragraph 144(2)(b), 144(3)(a) 144(3)(b), subparagraphs 158(2)(g)(i), 158(2)(g)(ii), 158(3)(b)(i) 158(3)(b)(ii), and 160B(2)(a)(i), and paragraph 160B(2)(d) of the Act]*

## **Application and transitional provisions**

1.38 Application provisions apply in relation to both the new best interests obligations and the ban on conflicted remuneration. In particular, the Bill amends the *National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009* to provide for the following arrangements:

- the obligations relating to the best interests obligations apply in relation to the provision of credit assistance to a consumer after 1 July 2020, whether or not the assistance was sought, or commenced being provided before that day; and *[Schedule 1, item 6, items 1 and 2 of Schedule 9 to the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009]*
- the obligations relating to the ban on conflicted remuneration apply in relation to conflicted remuneration given after 1 July 2020, subject to regulations being made prescribing the circumstances in which the ban applies. *[Schedule 1, item 6, items 1 and 3 of Schedule 9 to the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009]*

1.39 The ban on conflicted remuneration applies to benefits given after 1 July 2020, regardless of whether any arrangement under which those benefits are given was in place prior to 1 July 2020.