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National consumer credit regulatory reform — the impact on credit advisers

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Background

On 1 July 2010, a new national regulation over the credit industry commenced — the National Consumer Credit Protection Act 2010 (Cth) (NCCP Act), which regulates lenders, credit advisers and everyone in between. In response to the *Financial Services and Credit Reform* green paper,[1] released in June 2008, Treasury introduced this uniform licensing and responsible lending regime under the NCCP Act to address — specific to credit advisers — the apparent differentiation of broker regulation from jurisdiction to jurisdiction in Australia, which it said allowed dishonest practices by some brokers in lower regulated jurisdictions.

For the mortgage broking industry, Treasury's key objective was to remove unscrupulous and rogue brokers (brokers are referred to as credit advisers), and more closely regulate and monitor the rest. Now regulated by the Australian Securities and Investments Commission (ASIC), many of Treasury's objectives under the NCCP Act have been successful. However, the NCCP Act has also had far-reaching implications for the mortgage broking industry, with some unintended negative consequences. In this article, we explore how the introduction of the NCCP Act has changed the face of the mortgage broking industry, and hear the views of Tim Brown of the Mortgage Finance Association of Australia (MFAA) regarding the true impacts on credit advisers.

Introduction of the NCCP Act

Before the NCCP Act regime was introduced, credit advisers had very little regulation. Western Australia had the most robust system in Australia, followed by New South Wales, Victoria and the Australian Capital Territory — all required a finance broking contract to be entered into between the customer and broker, but little more. South Australia, the Northern Territory, Tasmania and Queensland, on the other hand, had no government regulation. In introducing the NCCP Act, Treasury sought to address this gap in consumer credit regulation and bring consistency across the country.[2]

The NCCP Act now requires licensing of credit advisers with relevant disclosure, conduct and responsible lending in place, as well as coverage of dispute resolution schemes and compensation methods for customers. The Act regulates any dealings relating to the provision of credit to natural persons or strata corporations for:

(i) personal, domestic or household purposes; or
(ii) to purchase, renovate or improve residential property for investment purposes; or
(iii) to refinance credit that has been provided wholly or predominantly to purchase, renovate or improve residential property for investment purposes.[3]

For credit advisers, this now means that they must hold an Australian credit licence[4] (ACL) in order to conduct credit assistance (also called credit advice), which is the act of suggesting or assisting a customer into a particular credit or lease product with a particular credit or lease provider[5] (Credit Assistance). Along with licensing also came new responsible lending obligations, requiring both lenders and credit advisers to conduct reasonable enquiries into the financial health of the customer to ensure that the customer can repay the loan without hardship, as well as to assess that the requirements and objectives in applying for consumer credit are met. Before providing Credit Assistance, the mortgage broker must conduct this preliminary assessment to ensure that the credit product is not "unsuitable"[6] for the customer.

Before and at the time of providing a customer with Credit Assistance, credit advisers must also provide certain prescribed disclosure documents[7] to make customers aware of who the broker is, what the broker will be paid and by whom, how the customer can complain about them, and details of the credit product for which the customer is applying. Finally, a credit adviser now has extensive general conduct obligations[8] to comply with in order to keep their ACL current, such as having appropriate compensation methods and being a member of an external dispute resolution body, as well as onerous ongoing training requirement each year — particularly for credit advisers providing Credit Assistance into third-party credit providers.[9]

Positive impacts on credit advisers

When asked about the positive impacts that the NCCP Act has had on credit advisers, Tim Brown believes that the most significant benefit has been a better reputation for the mortgage broking industry in general. Now that brokers must hold licences and be vetted by ASIC before being granted their ACL, the industry is attracting the "right kind of people" as credit advisers and consumers are placing more trust on their brokers. With the NCCP Act now firmly in place, Mr Brown believes that consumers in every state in Australia now have a better understanding of whom they are dealing with and that their broker is a reputable, well informed, appropriately educated, ethical and highly regulated credit adviser.

In stark contrast to pre-NCCP Act days, credit advisers now have compliance frameworks in place with supporting policies and procedures, as well as appropriate compensation methods for customers and internal dispute resolution processes. These have all had a very positive impact on the mortgage broking industry, says Mr Brown. Rogue brokers are being squeezed out.

Mr Brown explains how credit advisers are now the number one choice for consumers who are seeking a home loan or to refinance their existing loan. Credit advisers work with customers to determine their borrowing needs and ability and select a loan that is suitable to the customer, given their circumstances, and then work with the customers to assist with the management of their application through to the settlement of their loan. This distribution method for lenders is now highly established and is an integral part of a lender's sales model. Credit advisers now make up to 50% of the current distribution of all new home loans lent in Australia, making them a key asset to the mortgage finance industry generally.

Along with directing more attention on credit advisers, the NCCP Act has also resulted in more support to brokers from ASIC and from industry bodies such as the MFAA. Mr Brown explains how, since the introduction of the NCCP Act, the MFAA has developed a system called "Pathways" to assist credit advisers with further education, business development and ongoing communication regarding the continuous changes to legislation. Given that all credit advisers must complete 30 hours of relevant industry training annually, Pathways has become a central point of reference for a range of courses and events from providers vetted by the MFAA, as well as options offered by the MFAA itself. It allows credit advisers to select from webinars and interactive learning, or simply ordering CDs and books, or registering for a seminar or workshop. Credit advisers who are MFAA members also have online access to many legal and compliance resources. Extensive and easily accessible resources and support are a direct and positive response to the overly regulated industry.

Negative impacts on credit advisers

Mr Brown explains how the MFAA was one of the strongest supporters of the introduction of the NCCP Act in the lead-up to enactment. The idea that customers would only be exposed to "responsible lending" was definitely worthy of being enshrined in legislation. However, the resultant NCCP Act and NCCP regulations, plus various subsequent ASIC Regulatory Guides released by ASIC, have produced literally hundreds of pages of details, which effectively seek to micro-manage each business in the consumer credit sector.

For the mortgage broking industry, Mr Brown believes that this creates overly onerous compliance obligations and concerns, and unreasonably high costs and time pressure for many credit advisers — most of which are small-to-medium enterprises. For example, the requirement for credit advisers to produce three disclosure documents to consumers (a Credit Guide, a Credit Quote and a Credit Proposal) is time consuming if done manually and costly to automate from a systems perspective, and creates timing and cost issues for brokers. The MFAA is of the view that the previous requirement for a Finance Broking Contract, which combined all essential elements in the current NCCP Act disclosure regime, worked well.

Mr Brown also describes the requirement for credit advisers to conduct a preliminary assessment for all potential borrowers before recommending finance, when the lender then has to carry out their own assessment before deciding to lend, is duplication and is onerous for credit advisers. In particular, credit advisers do not have access to all the information that lenders have access to, and do not (and should not) carry out their own credit reports or verification checks. It is therefore difficult for a mortgage broker to determine that a loan might be suitable for a client in those preliminary stages of the client engagement process. In relation to the preliminary assessment requirement on brokers, Mr Brown questions whether the NCCP Act demonstrates any benefit to the consumer, or whether it simply adds compliance time and cost for credit advisers, and added documentation and frustration for customers.

A further negative impact that the NCCP Act has had on credit advisers is the ban on the use of the word "independent", which has had the unintended negative impact on restricting brokers from advertising themselves as being "independently owned". In the current day, an independently owned mortgage broker is a rare and positive message, given the numerous takeovers and

mergers of banks, non-bank lenders, aggregators, mortgage managers and brokers during and after the global financial crisis (GFC). While using the words "independently owned" in the context of a privately owned corporation does not mislead customers as to the broker's independence from other lenders and aggregators, the use of this word in advertising by brokers has strictly been banned in all instances.

Finally and not surprisingly, the ban on lenders charging exit fees has negatively impacted credit advisers as well as non-bank lenders. According to Mr Brown, the moment lenders could not recover upfront and trail commissions paid to credit advisers out of deferred establishment fees paid by customers on early termination of their home loan, the lenders reduced mortgage broker commissions to make up for some of those lost upfront costs. Clawback of commissions on early discharge of a customer's home loan is also now currently prominent in the market. Non-bank lenders with higher upfront cost, higher borrower churn and more reliance on third-party distribution than the major four Australian banks could not adequately recover those costs to remain competitive.

Financial System Inquiry

The Financial System Inquiry is currently in consultation with the banking and finance industry, after an interim report[10] was released by Treasury in July 2014. The intension of the Financial System Inquiry is to establish a direction for the future of Australia's financial system, given that it has been 16 years since the last financial system inquiry. The interim report tackles issues relevant to credit advisers, such as the substantial regulatory reform agenda, new competitive dynamics in the banking sector, and the impact of the GFC.

It is the view of Mr Brown and the MFAA that the mortgage broking industry could certainly have a break from new regulatory reform, with the MFAA contributing a submission[11] that competition in the lending sector needs to be enhanced by a strong securitisation market to enable a vibrant and innovative non-bank and small lender sector. The MFAA also put forward its view that regulation must be either competition enhancing or, at least, competitively neutral in its impact on the various players in the lending market.

The NCCP regulations introduced over the last five years, with their many requirements and high compliance cost, apply equally to a small mortgage broker as to a large bank. This has resulted in an inequity across the sector, with smaller credit advisers and non-bank lenders struggling to keep up with the regulatory costs that can be better absorbed by the big banks.

This imbalance of cost versus share of market, coupled with the GFC, which saw large banks swallow non-bank lenders and mortgage aggregators, has had the unintended effect of reducing competition in the lending sector. Mr Brown and the MFAA submission[12] express a desire for any new regulation to enhance competition, rather than decrease it. Mr Brown explains the MFAA's view that, before Treasury considers introducing any further regulatory reform that impacts credit advisers, it should first examine the proposed reforms to ensure that they are competitively neutral across all players in the market.

Conclusion

While the introduction of the NCCP Act has had many positive impacts on the mortgage broking industry — most important of which has been the intended weeding out of rogue and unscrupulous credit advisers — it is the unintended negative impacts that see the brokers struggling to keep up with the constant reform and compliance obligations. The NCCP Act itself saw subsequent extensive National Consumer Credit Protection Regulations 2010 (Cth) released, and thereafter iterations and variations to the laws, as well as regulatory guides, information sheets and regulatory impact statements. In essence, Mr Brown believes that regulation should be principles based rather than an attempt to micro-manage business. Credit advisers could do with a breather from new regulation or, at the very least, from regulation that detracts from rather than enhances competition in the lending market.

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About the author
Leonie Chapman's *experience extends to banking and finance, consumer credit and mortgage lending, contract negotiation, trade practices and fair trading legislation, intellectual property and trade marks, and corporate and financial services. After completing her Bachelor of Laws and Bachelor of Commerce in 2002, Leonie went on to work both in private practice and as senior in-house lawyer supporting a specialist lender, and then for six years with Macquarie Bank Ltd. Having achieved a Master of Laws in 2009 specialising in banking and finance law, Leonie's main focus now as Principal of LAWYAL Solicitors is on regulation and compliance for banking and financial institutions.*

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About the author
***Tim Brown** is the President of the Mortgage Finance Association of Australia. He has worked in the banking and finance industry for over 30 years and has held senior management positions in organisations such as Macquarie Bank, LJ Hooker, Suncorp, Aussie Home Loans and AVCO Finance (now GE Capital). Tim's industry experience has seen him successfully establish and own LJ Hooker Home Loans as a master franchise which was acquired by LJ Hooker in 2003. Tim is currently the CEO of Vow Financial, Australia's sixth largest mortgage aggregator. He has an MBA and also completed a Diploma in Mortgage Lending and Business Management and a Diploma in Financial Planning.*

Footnotes

1. Treasury *Financial Services and Credit Reform: Improving, Simplifying and Standardising Financial Services and Credit Regulation — Green Paper* Australian Government, June 2008, available at http://archive.treasury.gov.au.
2. Above, n 1.
3. NCCP Act, Sch 1 (National Credit Code), s 5.
4. Above, n 3, s 29(1).
5. Above, n 3, s 8.
6. Above, n 3, s 116.
7. Above, n 3, s 113 (Credit Guide), s 114 (Quote) and s 121 (Credit Proposal).
8. Above, n 3, s 47.
9. ASIC Regulatory Guide 206: *Credit licensing: Competence and training* July 2014 and ASIC Regulatory Guide 207: *Credit licensing: Financial requirements* June 2010 at [207.77], available at www.asic.gov.au.
10. Treasury *Financial System Inquiry: Interim Report* Australian Government, July 2014, available at www.fsi.gov.au.
11. Submission by the Mortgage Finance Association of Australia in response to Financial System Inquiry, March 2014.
12. Above, n 11.