MFAA
MORTGAGE & FINANCE ASSOCIATION OF AUSTRALIA

Submission Phase 2

28 February 2013

This submission is made by the Mortgage and Finance Association of Australia (MFAA).

The MFAA is the peak national body providing service and representation to over 12 000 professional credit advisers (mortgage and finance brokers, mortgage managers and aggregators) to assist them to develop, foster, and promote the mortgage and finance industry in Australia.

PART 1 – EXECUTIVE SUMMARY

1. The MFAA opposes any further regulation of the finance industry until the impact of the NCCP Act and the Enhancement Act can be assessed.

2. The scope of transactions which can be considered by EDR should be limited to avoid abuse by people who are not really 'consumers'.

3. Making 'private' loans subject to the National Credit Code if arranged by an intermediary will discourage private lenders from using intermediaries, most of whom are licensed finance brokers. This will result in 'private' investors being exposed to greater risk of loss, and encourage the market to operate outside the law. Instead, we suggest a simple regime that intermediaries who arrange private loans must hold an ACL or be a credit representative.

4. We oppose the limited regulation of investment lending both because of our general opposition to any further regulation (see 1 above), but also because of the extremely wide scope of this initiative with possibly unforseen consequences. Our primary concern is that bringing this type of lending within the ACL regime may reduce the availability of finance and reduce competition.

5. We are concerned that regulating investment lending may have the unintended consequence of regulating small business loans. What is an investment and what is a small business loan?

6. If, despite our concerns government decides to proceed with regulating investment lending, it is not appropriate for brokers and lenders to attempt to understand a borrower's risk appetite in relation to protected investment contracts. Instead of making an assessment of whether the customer is prepared to lose ownership of the customer's principal place of residence, there should be a simple prescribed form that borrowers sign evidencing that intention.

7. Generic anti-avoidance provisions are not appropriate for the regulation of finance. These provisions should be made specific or deleted.

PART 2 – GENERAL COMMENTS

Opposition to further regulation

The MFAA as a matter of general policy opposes further regulation before at least 30 June 2016, to allow the existing reforms to be fully implemented and for the results of those reforms to be assessed.

Our comments below are made subject to the general statement above.

The 'EDR' factor

Treasury's discussion proceeds on the basis that investment loans will be subject to 'light touch' regulation. There is a major and fundamental problem with this proposition.

Lenders and brokers are generally required to be members of EDR schemes. The MFAA supports the requirement to be an EDR member. However, we are concerned that being a member applies much of the Credit Code type protections to transactions which are not regulated by the National Credit Code. The potential for abuse by small businesses, investors, and consumers is huge and is proving increasingly costly for the finance industry, reducing the availability of credit, and reducing competition by the withdrawal of participants from this sector.

We believe the vast majority of borrowers and lessees in respect of transactions which are not regulated by the National Credit Code would gladly give up their EDR rights in exchange for a more competitive marketplace and greater availability of finance.

We have identified the following 'Code type' remedies that can be pursued by consumers through EDR schemes in relation to finance that is not regulated by the Credit Code.

- hardship;
- financial loss;
- unjustness;
- unfair and unconscious able conduct; or
- did not meet standards of good practice in the financial services industry; and
- any expression of dissatisfaction about a financial service.

Accordingly, the extension of the NCCP Act to investment loans is not 'light touch' from the perspective of lenders and brokers who are not currently members of EDR schemes. The rules of the EDR schemes should be amended to provide appropriate protections for 'true' consumers.

Current EDR schemes have no limit on the amount of the loan that can be subject to the dispute. Instead, there is a limit on the amount of the claim ($500K) and a limit on the amount of the award ($280K). (These are COSL figures).

The ASIC proposal in CP190 is to limit the jurisdiction of EDR schemes to loans of not more than $5m. If this proposal is implemented, the impact of EDR will be less, but is still very significant. For example, construction finance for a small block of flats could well fall within the jurisdiction.

We submit that it is important that recourse to EDR is limited so that it cannot so easily be abused by people who are not really 'consumers' in the common meaning of the word. This risk could be addressed by:

- setting a maximum loan amount of $2million; and
- excluding 'sophisticated borrowers' from access to the regime. A sophisticated borrower would be a borrower with net assets excluding the principal place of residence and superannuation of more than $500,000.

EDR is not the appropriate jurisdiction for commercial disputes concerning anything other than very small ‘consumer type’ business and investment loans. Because of the stay on enforcement, the jurisdiction can be used to frustrate enforcement by lenders of their appropriate legal rights. We cannot emphasise strongly enough the risk of EDR being used as ‘free run’ abuse of process and as an unfair way of delaying enforcement action. These protections are not suitable except for ‘true consumers’.

PART 3 – COMMENTS ON SPECIFIC PROPOSALS

Schedule 3 – investment lending

We are concerned at the very wide scope of ‘investment’. In short, the proposal seeks to bring within the ACL regime any lending to individuals to strata corporations whatsoever.

We are concerned that regulating investment lending may have the unintended consequence of regulating small business loans. What is an investment and what is a small business loan? For example, if an individual purchases land on which to conduct a small business, is that an investment loan or a small business loan?

We appreciate that ‘investment’ loans will only be subject to limited regulation, but we are concerned that the requirement for licensing and all that entails may remove some financiers and brokers from the market and reduce competition.

Although all our broker members fall within the ACL regime, we have considered a proposal of regulating brokers but not lenders. However, it would be unfair to regulate part only of the industry.

If despite our objections the proposal is to proceed, we comment as follows.

We are concerned that the legislation is becoming so long and complex that the cost of compliance will increase even further. The numerous provisions also create confusion and the risk of breach. Surely, the proposals for investment lending can be set out without repeating virtually word for word so much of the existing legislation – about 22 pages. Isn’t the proposition simple, namely: ‘if a credit contract is a protected investment contract, instead of ensuring that the borrower can repay without hardship, the licensee must obtain a certificate in the form of Schedule XX’? We contemplate that Schedule X is a certificate in a prescribed form by the mortgagors that they are prepared to lose their home.

Question	Response
No extension to investment leases	We agree that investment leases are rare, but it would be better to regulate them in the same way as investment loans for consistency and to prevent avoidance practices.
133EB(4)(b) - secured over the consumer’s principal place of residence	To make it clear, state wholly or partly secured by a mortgage over the home.
133EB – further restrictions on the definition of ‘unregulated product investment credit contract’	We think that the linked credit transaction provisions in part 7 of the Code is a good model for defining the relevant relationships perhaps with the addition of a relationship existing where a commission is paid by the product supplier/issuer.

Question	Response
133EC - provide a Quote	The obligations should extend to intermediaries as well to prevent avoidance.
133EK - enquiries for protected investment contracts	We consider that the enquiries are appropriate on the basis that Treasury proposes to further limit this category to contracts where there is commission or other financial arrangements creating a risk of conflicted advice. However, it is not appropriate for brokers and lenders to attempt to understand a borrower's risk appetite. Instead of making an assessment of whether the customer is prepared to lose ownership of the customer's principal place of residence, there should be a simple prescribed form that borrower's sign evidencing that intention.

Schedule 4 - Private lending

The proposals go further than simply requiring brokers who arrange 'private' loans to be licensed. They make:

- the credit contract regulated (and all the NCC compliance regime that entails); and
- establish a complex servicing arrangement (similar to the current regime for exempt trustees).

Making 'private' loans subject to the National Credit Code if arranged by an intermediary will discourage private lenders from using intermediaries, most of whom are licensed finance brokers.

If 'private' investors avoid licensed brokers, the investors will be deprived of professional advice and so exposed to greater risk of loss. Instead, we suggest a simple regime that intermediaries who arrange private loans must hold an ACL or be a credit representative.

If despite our submission the law proceeds, we comment as follows.

1. Regulation 9AA(2) allows a 'credit activity investor' to operate without a licence if a licensed intermediary services the loan. A 'credit activity investor' is defined to exclude:

    (a) companies with more than four shareholders;

    (b) companies with corporate shareholders:

    (c) trusts with more than four beneficiaries;

    (d) trusts with corporate trustees;

    (e) trusts with more than four natural person trustees.

    Those excluded private lenders would need to obtain a credit licence to provide Code regulated finance or finance to a small business. This would restrain many:

- family trusts with a wide range of potential beneficiaries;
- family companies owned by a family trust having a corporate trustee; and
- family companies with a more than four family members.

We do not understand the purpose of limiting the exemption in this way. If a large company or trust which is not in the business of lending lends through an intermediary, why should they not be able to access the same regime large securitisation programs can access? The exclusion of these lenders may reduce the availability of finance and limit investment opportunities for many entities as obtaining an ACL would be prohibitive.

2. Regulation 9AA(2) provides for notification of commencement of a servicing agreement. There should be a mechanism for notifying ASIC of a change of servicer and ending of servicing.

Schedule 5 – Consumer Leases

S170A - extension of regulation of consumer leases	The approach is appropriate.

The question states that s170A is intended ‘to include short term leases and indefinite term leases that are currently exempt under subsection 171(2). We do not understand the relevance of s 171(2) to short term and indefinite term leases, as that section relates to the exclusion of goods hired by employees in connection with their employment.

Schedule 6 – Anti-avoidance

As a matter of policy the MFAA opposes non-specific legislation.

We understand that this legislation could address two types of avoidance:

1. credit substitutes (in which case it should be made clear that the issue of guarantee (eg issue of bank guarantee, letter of credit, performance bond guarantee) is not seen as a credit substitute; and

2. ‘artificial’ structures (eg a loan to a company when the ‘real’ borrowers are individuals).

How will a court or tribunal decide whether the arrangement is a ‘genuine’ credit substitute or structure as distinct from an artificial one that is affected by these provisions? In our view this leaves too much to chance, and unless some solution to avoid that risk is found, the provisions should be deleted as they will do more harm than good by reducing commercial flexibility and the availability of different types of financial arrangements.