MORTGAGE & FINANCE ASSOCIATION OF AUSTRALIA

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Gavin Jones
Director
Competition Exemptions,
Australian Competition & Consumer Commission
Lonsdale Street Melbourne VIC

27 October 2023

By email: exemptions@accc.gov.au

Dear Mr Jones

DRAFT DETERMINATION ON APPLICATION FOR AUTHORISATION AA1000640 – COMMONWEALTH BANK AND ORS INTERESTED PARTY CONSULTATION (THE DRAFT DETERMINATION)

The Mortgage & Finance Association of Australia (**MFAA**) refers to the ACCC's Draft Determination with respect to the Application submitted by the Commonwealth Bank, Westpac Banking Corporation, Australian and New Zealand Banking Group Limited, National Australia Bank Limited and Macquarie Bank Limited (**the Applicants**) regarding the establishment of a voluntary program for mortgage lenders to jointly procure assurance reviews of the compliance systems and standards of participating mortgage aggregators (**Aggregator Assurance Program**). We appreciate the extension of time provided by the ACCC to respond to the ACCC's Draft Determination.

The MFAA is the peak industry body for the mortgage and finance broking industry with more than 14,500 members. Our membership includes mortgage and finance brokers, 10 of the 11 major mortgage aggregators in Australia as well as banks both small and large (including all the Applicants), and non-bank lenders. The MFAA represents the whole of industry in relation to the third-party distribution channel for home loans.

OUR SUBMISSION

Core to the MFAA's role is to facilitate industry dialogue on options to improve processes within the industry. This is so as to enable our members to grow and thrive, and to ensure that competition and choice continues to be preserved for the benefit of our members' customers – being consumers and business owners. As noted in our initial submission to the ACCC dated 22 May 2023 (**Initial Submission**),[1] the MFAA remains strongly supportive of the proposed Aggregator Assurance Program as do our aggregator members. Our position is that:

- there is a strong public benefit to the implementation of the Program in that cost and resource efficiencies to aggregators resulting from the Program will be redeployed by them to supporting small broking businesses for the benefit of consumers and thus enhancing the competition in the home loan market,

[1] MFAA Initial Submission

- the regulatory costs for smaller lenders from current and future assurance activities will be reduced, enhancing the competitive position of these lenders, and
- the program will allow greater participation in assurance activities for a larger number of lenders than currently undertake assurance activities on aggregators, and that can only increase the quality of assurance on aggregators than is currently present.

In preparing our response, we have engaged with our aggregator members to quantify the current and projected costs for each of them individually and collectively in responding to multiple reviews. These aggregators are:

1. REA Group (which includes Mortgage Choice),
2. National Mortgage Brokers (NmB),
3. Connective,
4. Finsure,
5. Lendi Group (which includes Aussie),
6. Astute,
7. Specialist Finance Group (SFG),
8. AFG, and
9. LMG.

There are more than 19,000 brokers in Australia and the vast majority are small broking businesses.[2] Based on our estimates, collectively our aggregator members listed above provide aggregation services to ~93%[3] of brokers in Australia.

On average, aggregators have 52 lenders on panel (including an average of 28 ADIs). Aggregator members who responded to the MFAA's request for data collectively reported a total of 142 audits undertaken in the calendar year 2022. This equated to a total of 4,263 estimated hours of effort responding to lender reviews at an estimated total cost of $723 000 across all aggregator members.[4] This equates to, on average, 16 audits per aggregator (i.e. an average of 34% of lenders on each aggregator panel) at a cost of ~$5,000 per audit. This average does not highlight the variation of audits undertaken. These variations range from full audits (interviews, sample testing and the collection and verification of information on matters ranging from broker onboarding and accreditation to IT system testing and controls) to simple and complex attestations.

In light of increasing demands for assurance, our aggregator members also expect a minimum of a further 54 audits to be conducted by lenders if the Aggregator Assurance Program was not implemented, bringing the total number of audits anticipated for the next calendar year to at least 196 audits. The cost associated with just those additional audits is circa $300, 000 at a minimum. Therefore, on a go forward basis, absent of the Aggregator Assurance Program, based on data supplied by our aggregator members, audits by individual lenders will cost our aggregator members alone an average of approximately $1 million per year.[5] Other industry costs will include lender costs of obtaining the audits, which for smaller lenders in particular can be significant.

OUR RESPONSE TO THE ACCC'S CONCERNS

We acknowledge the concerns raised by the ACCC in its Draft Determination which proposes to deny the authorisation with respect to the Application.

As noted in our Initial Submission, the MFAA remains strongly supportive of the proposed Aggregator Assurance Program. On this point we note also the significant support expressed by respondents

[2] For example, 95% of our members are in businesses of ten or less brokers. See MFAA Industry Intelligence Service Report Edition 15 pg 36.
[3] See Diagram 1 for an analysis of MFAA aggregator member market share responding to the MFAA's request for information.
[4] This is a total of estimated staff costs as well as oncosts which includes rent, technology, and other ancillary costs of running the business.
[5] See Diagram 2 for a snapshot view of the current and projected costs in responding to multiple assurance reviews. This assumes that a minimum of 196 audits would be required annually on a go forward basis.

(including lenders, aggregators, industry associations and professional services firms) to the ACCC's initial consultation on the Application.

Further to the comments in support of the Program set out in our Initial Submission, we have set out our responses to certain concerns raised by the ACCC in its Draft Determination below. These concerns include:

A. The ACCC is not satisfied in all the circumstances that the Aggregator Assurance Program is likely to result in a **public benefit** that would outweigh the detriment to the public as a result of the Program.

B. The Aggregator Assurance Program will lead to a homogenous program, and the ACCC is uncertain as to whether it would lead to higher or lower **quality standards** if some lenders would undertake assurance programs themselves in the absence of the Program.

C. The proposed scope of the Program is high level, and therefore provides significant discretion and **scope** about the nature and scope of the reports.

D. The construct of the Program and current proposed fee structure may favour large lenders over small lenders and therefore will preclude **participation by smaller lenders** in the Program.

A. Public benefit

While the ACCC has suggested that it is not satisfied in all the circumstances that the public benefit will outweigh the detriment, the ACCC has noted at paragraph 5.24 that it considers that the Proposed Conduct is likely to result in some public benefit in the form of efficiencies and cost savings for aggregators and lenders who do participate in the Program. This is because fewer assurance reviews will need to be conducted, reducing the duplication of resources and information required to be reviewed.

Our strong view is that there is a clear public benefit that would result from the Aggregator Assurance Program. In our view, a single independent program would materially lessen the number of audits and assurance activities currently undertaken and experienced by both aggregators and lenders allowing these resources to be redeployed into supporting small broking businesses with compliance, business development and technology infrastructure for the benefit of customers.

As noted in our Initial Submission, brokers utilise the services of aggregators to enable them to conduct their broking businesses, with aggregators providing a range of support services including commission platforms, marketing, and administrative services as well as compliance services. Brokers can be credit representatives of aggregators or are credit licensees, however the services provided by aggregators to brokers are generally consistent across these two licensing arrangements. On this point, we note that aggregators themselves compete against each other in terms of service delivery and quality of technology infrastructure, compliance, and business development support to their brokers.

Firstly, and as noted above, there is currently a very large number of assurance activities by multiple lenders deployed against aggregators ranging from simple to complex attestations and to audit and assurance programs.

The average number of lenders seeking reviews across our aggregator members is 16, but ranges, depending on the aggregator, from 11 to 21 per year. The number of lenders engaging in audit activity of some description is forecast to increase. The breadth of topics is also likely to increase as prudential standards continue to evolve, in particular in relation to the management of information security risks,[6] conflicts of interest which may arise out of third-party compensation arrangements[7] and material supplier risks.[8]

Data provided by MFAA aggregator members highlights the expectation that per aggregator, the average number of audits could increase from 16 to 23[9] and at an average cost of $5,000 per audit per aggregator.

On a go forward basis, the cost impost to aggregators (and by extension their broker members) as a result of multiple assurance programs is significant and will likely exceed $1 million per annum.

Aggregation businesses operate on low gross revenue margins of 1-5% and employ a small number of staff relative to the size of their broker networks. For example, and as noted by one aggregator in its submission to the ACCC's initial consultation with respect to the Application, it employs just 170 people in Australia to a network of 4400 brokers (in essence 1 staff member to 25 brokers).[10]

Notably also the aggregation businesses vary significantly in size, from relatively small businesses with circa 600 brokers to around 4000 brokers. Assurance activity across all aggregators is generally consistent irrespective of size. We noted above that aggregators themselves compete against each other in terms of service delivery and quality of technology infrastructure, compliance, and business development support to their brokers. Therefore, the cost and resource impact on smaller aggregation groups in undertaking multiple assurance reviews will be relatively more significant, impeding their ability to compete with their larger counterparts.

In the absence of the Aggregator Assurance Program, resources and investment that could be directed by aggregators into broker support services (for example, technology, product innovation and compliance support) is instead being directed to multiple assurance programs. Ultimately brokers drive competition between lenders by increasing choice, providing greater access to credit, driving competitive pricing and better overall solutions for customers. The ability for the Aggregator Assurance Program to allow aggregators to redirect their resources and investment into improving their service levels to brokers which in turn will enable brokers to improve service levels to their customers should be considered a public benefit and resultant benefits of the proposed Program.

Putting this another way, under the proposed Aggregator Assurance Program, each aggregator will be subject to one audit. This means the significant reduction in the number of individual assurance reviews undertaken by lenders proposed to be facilitated by the Aggregator Assurance Program will free up cost and resources to enable aggregators to deliver more compliance and business development support to their broker groups. Therefore, the cost savings will allow aggregators to further invest in that service delivery, which will have flow on effects to improving the quality of broker services and ultimately to the benefit of consumers. For example, if aggregators as a result of the Program have more resources and/or can invest in better systems to provide compliance services to brokers, it would assist with improved compliance by brokers of responsible lending and the best interests duty obligations.

B. Quality Standards

The ACCC notes at paragraph 5.80 that it considers that whether the Proposed Conduct is likely to result in assurance reviews being conducted to a higher or lower standard is uncertain. The ACCC considers that the Proposed Conduct is likely to result in a public

[6] See Prudential Standard CPS 234 paragraph 16.
[7] See Prudential Standard CPS 511 paragraph 29(c).
[8] Prudential Standard CPS 230 (paras 48 and 49) requires all APRA regulated entities to identify and maintain a register of its material service providers as well as to manage the material risks associated with using these providers. Material service providers specifically include mortgage brokers.
[9] This analysis is based on additional audits estimated by 7 of the 9 respondents. We have prepared these estimates based on information from our aggregator members and consider this numbers to be a minimum or a floor.
[10] See Connective submission to the Application.

detriment due to the increased risk that assurance reviews under the Program will be performed to a lower standard. To the extent that assurance reviews are performed to a lower standard, this increases the risk of inappropriate lending practices.

The MFAA does not agree that the Aggregator Assurance Program will lead to a lower standard of assurance programs being conducted and we see there is no basis for the ACCC to form this view.

Our observations are that current assurance activity conducted by lenders range from full and comprehensive audits (including sample testing) to complex and simple attestations. The Applicants all perform full reviews which includes meetings with senior members of the respective aggregator, reviewing policies, processes and obtaining evidence that the processes are working as expected.

Smaller lenders generally rely on attestations (to varying degrees of complexity) to meet their regulatory and prudential obligations and as we understand this is as a result of limited internal compliance resourcing to undertake comprehensive audits. We also understand that there are smaller lenders that currently do not conduct **any** assurance activity whatsoever on the expectation that they expect to benefit from the economies of scale provided by the proposed Aggregator Assurance Program. Respondents to our request anticipate at a minimum an additional 142 audits from this cohort of lenders.

In our view having reviewed the Program Scope, the Program stipulates a much higher standard of review than those that are currently performed by smaller lenders (that tend to rely on attestations rather than full audits). The Program provides the opportunity to all lenders to participate in assurance reviews with access to full audit findings.

In our view therefore, the Aggregator Assurance Program can only have the effect of enhancing the assurance activity of smaller lenders who currently only rely on attestations (or have no program in place) to meet their compliance obligations resulting in a more robust and higher quality oversight regime across the industry.

C. Scope

The ACCC has raised concerns that the Proposed Conduct is likely to lead to more homogenous assurance reviews being undertaken, including due to the proposed appointment of a single assurance service provider.

On the point of proposed scope, and in particular homogeneity raised by the ACCC in paragraph 5.81, we note that the regulatory requirements of both lenders and aggregators are the same and therefore the multiple programs currently in play are already essentially 'homogenous' (i.e. in effect testing for compliance with the same set of regulatory requirements). However, the Program will result in a significant uplift in the quality of the testing for compliance against the regulatory requirements (as discussed above).

As noted in our Initial Submission, observations were made by our aggregator members in relation to current audit and assurance programs that there was similarity and duplication between the multiple programs conducted by different lenders. The main aspects of these reviews related to broker accreditation and onboarding processes, licensing, regulatory requirements with respect to brokers including responsible lending and more recently best interests duty and remuneration reforms. The 'homogeneity' of multiple programs was a main catalyst for the genesis of a single joint Aggregator Assurance Program, and we consider a common sense and pragmatic approach was to implement a single independent coordinated program.

D. Participation of smaller lenders

In the Draft Determination Summary, the ACCC has said that while the Program is intended to be open to all lenders, key decisions about the operation of the Program will be made by the Applicants. This includes decisions about the scope of assurance reviews, where the Applicants will have significant discretion. The ACCC is concerned that this discretion, in the context where other, particularly smaller lenders, will not have a role in making such

decisions, may result in the assurance reviews being conducted in a manner that prioritises the Applicants' requirements, without giving equal consideration to the assurance review requirements of other lenders. The ACCC also considers that all lenders sharing the costs of assurance reviews they participate in equally, as is proposed, may favour large lenders over small lenders. While all lenders who participate appear to be likely to save on costs through joint assurance reviews, the cost saving to larger lenders under an equal cost sharing model, relative to the amount they currently spend on aggregator assurance reviews, are likely to be greater.

We note that COBA has consistently raised concerns about the impact of increasing regulatory costs on its members. In particular COBA notes that these costs impact on the ability of its members to grow by diverting funding away from growth initiatives (resulting in impact to competition, innovation and consumer choice).[11] While the prudential requirements imposed by APRA seek to entrench proportionality in its standards, amongst other things, APRA continues to have an expectation that all banks, large or small have oversight (in the form of assurance) over their material service providers.[12] We understand several smaller lenders propose to respond to material service provider oversight requirements through the proposed Aggregator Assurance Program and as such will benefit from associated regulatory cost savings (and which we would suggest alleviates the regulatory cost burden and improves the competitive position of these lenders in the lending landscape).

In saying this, in our view there remains an opportunity for the Applicants to address the ACCC's concerns in relation to smaller lender participation in the Program through a revised cost structure and participation model.

CONCLUSION

We continue to emphasise our support for the benefits of the program on the expectation that a single independent coordinated program would materially lessen the number of audits and assurance activities currently undertaken and experienced by industry participants. This is expected to lead to corresponding benefits, being a reduction of cost and duplication and an increase in efficiencies across industry.

The MFAA extends its thanks to the ACCC for the opportunity to contribute to this consultation. We propose a meeting with the ACCC to discuss our submission. In the interim, if you require further information, please do not hesitate to contact me at [redacted] or Naveen Ahluwalia at [redacted].

Yours sincerely

[redacted]

Anja Pannek
Chief Executive Officer
Mortgage & Finance Association of Australia

[11] See COBA's submission to the House of Representatives Economics Inquiry into promoting economic dynamism, competition and business formation.
[12] As noted above, CPS 230 requires APRA regulated entities, to amongst other obligations, uplift arrangements with material service providers which specifically includes mortgage brokers.

Annexure A – About the MFAA

The MFAA is the peak industry body for the mortgage and finance broking industry with over 14,500 members. Our members include mortgage and finance brokers, aggregators, lenders, mortgage managers, mortgage insurers and other suppliers to the mortgage and finance broking industry.

Our role as an industry association is to provide leadership and to represent its members' views. We do this through engagement with governments, financial regulators and other key stakeholders on issues that are important to our members and their customers. This includes advocating for balanced legislation, policy and regulation and encouraging policies that foster competition and improve access to credit products and credit assistance for all Australians.

Mortgage and finance brokers play a critical role in intermediated lending, providing access to credit and promoting choice in both consumer and business finance. Mortgage and finance brokers facilitate more than two thirds of all new residential home loans[13] and approximately four out of ten small business loans[14] in Australia and are therefore significantly important to facilitating competition in both the home lending and business lending markets.

[13] MFAA Industry Intelligence Service Report 15th Edition pg 4
[14] Productivity Commission research paper Small business access to finance: The evolving lending market pg 44

Diagram 1 – Market share of aggregators responding to MFAA data request

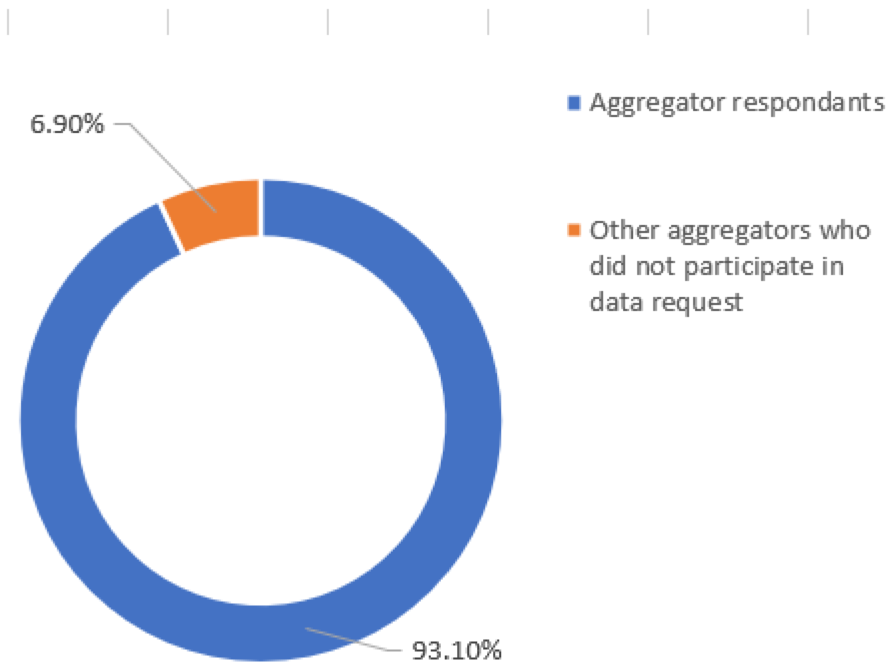

Diagram 2 – Snapshot view of current and projected costs of multiple assurance reviews

Total audits conducted : **142**

Total effort : **4,263 hours**

Total cost : **$722,896**

Extra audits anticipated : **54 minimum**

Extra audits est. cost : **$277,904 minimum**

Ongoing audits est. cost : **$997,800 minimum**