MORTGAGE & FINANCE ASSOCIATION OF AUSTRALIA

Senate Economics References Committee
Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

5 November 2024

By email: economics.sen@aph.gov.au

Dear Committee Secretariat,

INQUIRY INTO WEALTH MANAGEMENT COMPANIES (INQUIRY)

The Mortgage and Finance Association of Australia (**MFAA**) welcomes the opportunity to make a submission to this Inquiry. The MFAA is Australia's peak industry body for the mortgage and finance broking industry with over 15,500 members. More information about the MFAA and its members can be found in **Attachment A**.

We recognise that this Inquiry focuses on issues related to wealth management companies. In reference to section (i) of the terms of reference—'the implications of the collapse of wealth management companies on the establishment of the CSLR, including design considerations and potential implications for future matters'—we seek to ensure that there are no unintended consequences for the mortgage and finance broking industry arising from this Inquiry.

The mortgage and finance broking sector has a markedly low reliance on the CSLR, with minimal claims and complaint volumes. As such, we believe it is crucial that any adjustments to the CSLR arising from this Inquiry do not inadvertently impose a greater financial or regulatory burden on mortgage and finance brokers.

DETAILED SUBMISSION

For context, we refer to our previous submissions,[1] including those to the Senate Economics Legislation Committee, where we emphasised that the implementation of the CSLR as a consumer protection mechanism must be balanced against the financial impact on small broking businesses.

The CSLR is an initiative designed to provide compensation to consumers and small businesses who have suffered financial loss due to misconduct by financial firms that are unable to pay, typically due to insolvency. The scheme offers compensation of up to $150,000 for eligible claims.

While we support the CSLR's objectives in protecting consumers, it is essential that the scheme's structure and funding do not place undue cost burdens on smaller credit intermediaries.

[1] MFAA submission to the Senate Economics Legislation Committee and submission to Treasury Financial System Division, 7 October 2022.

Like wealth management companies, credit intermediaries constitute a sub-sector within the scope of the CSLR. This legislatively established, industry-funded scheme is designed to allocate costs proportionately based on the claims and compensation payments arising within each sub-sector.

While the Inquiry aims to examine the causes of wealth management company collapses and the implications for the sustainability of the CSLR, we are concerned about potential cross-subsidisation and the increased regulatory cost burden this could place on the credit intermediary sub-sector.

Implications of exceeding sub-sector cap

We note the concerns raised by Finity that the upcoming financial advice levy will exceed the $20 million sub-sector cap.[2]

When compensation claims surpass a sub-sector's levy cap, the CSLR operator must notify the Minister in writing as soon as practicable. This notification includes details such as the number of applications, the total compensation payable, and the portion of unpaid fees attributable to the sub-sector.

Upon receiving the notification, the Minister has the authority to impose a special levy to cover the excess compensation. This special levy can be applied either to the primary sub-sector responsible for the claims or spread across multiple sub-sectors, depending on the circumstances.

Minimal use of scheme by the credit intermediary sub-sector

According to the Australian Financial Complaints Authority (AFCA) Datacube,[3] the mortgage and finance broking industry consistently accounts for less than 0.5% of all banking and finance complaints lodged.

Furthermore, Finity has estimated that credit intermediation will account for just 10 complaints, or 5.1% of the total complaints the CSLR is expected to finalise in its second levy period ending June 2025. There are no indications of an increase in claims for this sub-sector beyond these projections, with uncertainties affecting the levy period primarily attributed to the Financial Advice (i.e wealth management) sub-sector.[4]

Implications of a special levy for broking industry

The credit intermediary sub-sector is predominantly made up of small broking businesses with 80% have 10 or fewer brokers while 41% are solo operators.[5] These businesses play a vital role in facilitating access to credit, empowering consumers and small businesses by providing choice, personalised advice, and guidance through complex lending processes that might otherwise be inaccessible.

If the special levy is distributed across several sub-sectors, entities not directly responsible for excess claims may bear additional financial obligations. This cross-subsidisation can lead to increased costs for sub-sectors with minimal claims on the CSLR, including small broking businesses.

[2] Compensation Scheme of Last Resort 23 October 2024, *Compensation Scheme of Last Resort hosts first financial industry forum*, viewed 4 November 2024, <https://cslr.org.au/news/compensation-scheme-last-resort-hosts-first-financial-industry-forum>.

[3] AFCA datacube, for complaints for period 1 July 2023 to 31 December 2023, viewed 4 November 2024, <https://data.afca.org.au/>.

[4] Finity Consulting Pty Limited March 2024, *1st and 2nd Levy Period Initial Estimates – Compensation Scheme of Last Resort*, viewed 1 November 2024, <https://cslr.org.au/sites/default/files/documents/2024-03/R_CSLR_1st-2nd-Levy-Period-Initial-Estimates_FINAL_FOR_PUBLICATION.pdf>.

[5] MFAA Industry Intelligence Report 17th Edition page 36: <https://cdn.sanity.io/files/t0x3ukgp/production/86ad362f54c8e7ac23ca67a27c6e2bb3c75a0866.pdf>.

Further consultation

If the credit intermediary sector is required shoulder a disproportionate share of additional costs in funding the CSLR, it introduces a moral hazard and raises questions of fairness. Placing a disproportionate financial burden on a sector with minimal claim activity not only challenges the principles of equitable treatment but also risks creating incentives that allow higher-risk sectors to rely on cross-subsidisation rather than addressing risk exposures within that sub-sector.

We welcome the opportunity for dialogue on solutions to address the issue of exceeding the sub-sector cap without imposing additional cost burdens on credit intermediaries and recommend further consultation on this issue.

CLOSING REMARKS

If you wish to discuss this submission or require further information, please contact either me at [redacted] or Stefania Riotto at [redacted]

Yours sincerely
[redacted]

Naveen Ahluwalia
Executive, Policy and Legal
Mortgage and Finance Association of Australia

Attachment A - About the MFAA

Brokers play a critical role in intermediated lending, providing access to credit and promoting choice in both consumer and business finance. Over time, consumers have increasingly sought the services of a mortgage and finance broker with the latest MFAA quarterly market share showing mortgage brokers are writing 74.1% of all new residential home loans[6] and approximately

four out of ten small business loans[7] in Australia.
The MFAA's membership includes mortgage and finance brokers, aggregators, lenders, mortgage managers, mortgage insurers and other suppliers to the mortgage and finance broking industry.

The MFAA's 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.

[6] MFAA media release, *Mortgage brokers remain the first choice for homebuyers*, 30 May 2024.
[7] Productivity Commission research paper Small business access to finance: The evolving lending market pg 44.