This submission by Tim explains very well the position of many Brokers around the country. I fully endorse Tim's thoughts. Adrian Grant - Stand Fast Finance

1. My name is Tim Gaspar, I am the owner of Hatch Financial Services Pty Ltd (**Hatch**) a mortgage broking business that I established 13+ years ago. In Annexure 1 is a profile of Hatch.
2. I make this submission based on my experience as a mortgage broker (broker), which I believe is representative of many thousands of brokers.
3. The central message in my submission is that while broker misconduct exists, the rate of misconduct is low and does not suggest a systematic issue caused by the commission payment structure. The reform needed is to set appropriate behaviour standards and have a robust compliance and enforcement regime.
4. I wish to make points under 4 headings;
    a. Who do brokers act for?
    b. The impact of remuneration on consumer outcomes
    c. The impact of abolishing commissions
    d. The way forward

Who do brokers act for?

5. I submit that brokers act for clients and clients are clear about this. In my experience, only consumers who have not used a broker see mortgage brokers as the face of the lender.
6. In 2002 broker originated loans made up 25% of all home loans[1], by 2018 that figure was over 55%[2]. This growth reflects the unmet need for advice and service which brokers have provided.
7. The growth is more significant given that 57% of broking businesses are 1-2 broker operations[3] competing against the might and market share of the major banks.
8. Brokers enjoy a Net Promoter Score of 70%[4]. This score reflects that brokers are the trusted adviser to many of their clients and value the service provided.
9. Consumers use brokers for one or more of the following reasons:
    a. ***Service without a fee –*** Meaning brokers can be accessed by consumers easily;
    b. ***To save money –*** this may be through securing lower rates or effective loan structuring;
    c. ***Peace of mind*** – consumer do not feel confident to proceed on their own and are scared that they will make a costly mistake;
    d. ***To* save time** – brokers show clients options across multiple lenders at one time and take care of the loan application process;

[1] ASIC (2017). Report 516: Review of mortgage broker remuneration. Australian Securities & Investments Commission. P49
[2] MFAA (2017b). Exclusive Finance Broker Benchmarking Report, 4e. MFAA Industry Intelligence Service. P15.
[3] MFAA Industry Intelligence Service (Oct 16 – March 17) p30
[4] Aussie and Advantedge report NPS scores of +70

e. ***To avoid hassles*** – by taking care of the loan application process and dealing with lenders, brokers saves clients stress and hassle;

f. ***After service*** – clients will often seek out their broker for ongoing support around their lending needs. In addition, many brokers conduct regular loan reviews with their clients. This may lead to refinancing to another lender but just as often this involves renegotiating rates with the current lender. Much of this service is provided without additional income being earned by the broker unless a new loan is written[5].

10. Many clients will choose to use a broker even if there is no monetary saving. In Annexure 2 is a sample of testimonials from Hatch clients that speak to the value brokers provide.
11. The broker business model is based on the premise that brokers act for, and in the interest of, their clients. While brokers are paid by the lenders, it is the clients that need to borrow money.
12. It is also the clients that will have future borrowing needs and whose family/friends may have borrowing needs. The success of a broker is tied to their ability to deliver a quality broking service and through this win; the loyalty of clients for their future, and referrals to their family/friends.
13. Consequently, behaviours that have a short-term profit centred focus are inconsistent with a brokers' long-term success. I believe that if a broker were to act contrary to the client's best interests the client would see this, if not right away, then at a future time, and at that point the broker would have lost the client and any future referrals. Accordingly, most brokers do business with a clear focus on the long term.
14. Paragraph 7 in Annexure 1 shows that 72% of Hatch's business comes from existing clients and referrals from these same clients. This is typical of many brokers and emphasises the importance of brokers acting in a client's best interests for the brokers own benefit.
15. Whilst brokers' first duty is to their clients, brokers have other obligations. For example, there are obligations under Anti Money Laundering/Counter Terrorism Funding laws as well as to ensure that the information it presents to the bank is accurate.
16. The Royal Commission has also noted that brokers have contractual obligations to lenders. Mostly these do not cause a conflict with the primary duty to clients. The Interim Report highlighted a conflict where CBA requirement that brokers submit a minimum home loan volumes[6]. This was a highly contentious and brokers opposed the requirement for this reason.

[5] Hatch has contacted 135 clients in the last 3 months to do annual reviews.
[6] Royal Commission Interim Report p58.

The impact of remuneration on consumer outcomes

17. The Interim Report states that the remuneration model for brokers is "driving different consumer outcomes"[7]. It cites the ASIC conclusion in the *Review of Mortgage Broking Remuneration Report* that broker originated loans typically have higher LVR's, or loan size, than loans established directly with the bank by between 1-4%.
18. A variance of this size is statistically speaking insignificant. However, the explanation of such a difference is likely to be found in two considerations other than broker misconduct:
    a. Consumers who use brokers are different to those that go direct to lenders (more first home buyers, more sophisticated property investors); and
    b. A stronger focus on consumer outcomes by brokers than that delivered by lenders. For example, my experience is that consumers do not want to borrow money but do so as a means to an end (home ownership, wealth creation etc). They certainly do not want to borrow more than they need. The question that brokers and clients need to answer is how much does the client need. The answer will vary from client to client and this is where good conversations and a focus on a client's needs plays a significant role.
19. The move by the Combined Industry Forum to have commissions paid based on the utilised loan amount removes the potential for conflict between broker and client interests regarding loan size.
20. With the assertion that the payment of commission is producing misconduct, I have looked for data to support such a contention. I found no such evidence (beyond the ASIC finding discussed above). I instead found:
    a. Whilst brokers make up 91% of Credit Industry Ombudsmen members, complaints against brokers only make up 1% of complaints;
    b. There were 469 complaints[8] made against brokers through the CIO and FOS in FY2018 while there are estimated to be 17,000 brokers[9]. That equates to one complaint for every 36.25 brokers. For the same period there were 1675 complaints against lawyers in Victoria and there are 22,438 registered lawyers in Victoria[10]. That equates to one complaint for every 13.39 lawyers. Lawyers are paid a fee for service but have more complaints per broker[11].

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[7] Royal Commission Interim Report p60
[8] Numbers taken from CIO and FOS Annual Report
[9] MFAA Industry Intelligence Service 4th edition
[10] Numbers taken for Victorian Legal Services Board Annual Report 2018
[11] I use lawyers as a comparison due the ease of finding data and because they are a professional service. I could not find data on doctors, accountants or financial planners that was easy to understand or break down for the purpose of a similar comparison.

21. Regulatory intervention by APRA in recent years has had a significant impact on consumer outcomes. Examples of this include APRA intervention with respect to investment and Interest Only lending which has led to lenders differentiating between interest rates for investor and interest only loans for practically all lenders. This action has led to the share of Interest Only loans dropping from nearly 40% in 2015 to comfortably below 30% by 2018[12].

Impact of Abolishing Commissions

22. As a broker who has been building my business for 13 years, my income comes equally from upfront and trail commissions. If trail commissions were abolished without any other adjustment, then my net profit/income would drop by over 80% to around $50,000 pa.
23. To earn a viable income that would warrant me remaining a broker I would have to look to:
    a. Make redundant 1 or both staff members and look to offshore labour to do the essential work currently done by my team (reducing labour costs by over 50%);
    b. Forgo an office and work from home;
    c. Slash marketing costs;
    d. Look to replace lost income. The most likely option being to move into commercial broking where clients are not price sensitive or cross sell other products/services.
24. Even doing these things I expect my income to drop by atleast 30%. This may be feasible for an established business, such as Hatch, but the same could not be said for most brokers.
25. MFAA research shows that gross income pa for the average broker is $133,500 comprising $77,000 from upfront commissions and $56,500 from trail.[13] This is before expenses (rent, support staff wages, marketing etc). Removing trail would leave very little net income after costs for brokers earning an average income.
26. Abolishing trail will have flow on consequences. It will damage economic activity as brokers lose their business' and support staff lose their jobs. There will also be the decrease in spending by the remaining brokers as they seek to create a viable business from a lower income base.
27. Diminishing the broker channel will have a serious negative impact on consumers. The damage would include:
    a. A fall in the availability of advice and service for consumers;

[12] Speech by Assistant Governor, Christopher Kent, Reserve Bank of Australia *The Limits of Interest Only Lending* April 2018.
[13] MFAA Industry Intelligence Service, 4th Edition (1 October 2016 – 31 March 2017), p33.

b. Lessening competition in the residential lending market as market share is handed back to majors. (over the last 4 years the Big 4, or lenders owned/aligned to the major banks, has seen their share of residential lending from brokers fall from 74.3% to 66%)[14];

c. A less accessible choice of lenders for consumers (many non-major lenders rely on brokers to reach consumers);

d. Broker access largely being available only to those able to afford to pay – smaller clients/loans would not justify the cost of a brokers' fee

28. If upfront and trail commissions were removed, then brokers would have no business. Research by Deloitte shows that consumers may be prepared to pay a fee of up to $1,000. This is well below the average value of commissions currently paid by lenders per loan[15].

29. Given the impact that abolishing commissions will have on brokers I submit that this step can only be supported where there is incontrovertible evidence that commissions are the source of misconduct and that the misconduct can only eliminated by removing commissions.

The way forward

30. Many brokers operate to a standard above the minimum level required by law.

31. At the same time, I would welcome raising the standards around home loan lending. The Combined Industry Forum (CIF) has led the way in this area.

32. In addition to implementing the CIF recommendations I would also:

   a. Require the disclosure to all clients of:

      i. The lenders that a broker is accredited with;

      ii. The commissions payable for each lender;

      iii. Data on the lenders used by a broker in the last 12 months;

      iv. The projected total cost of loan over the loan term and a breakdown of that figure between interest and other costs;

   b. More active supervision of and enforcement of regulations.

33. The solution to arriving at better consumer outcomes lies in education, regulation and enforcement. Commission is not the primary cause of bad consumer outcomes.

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[14] MFAA Industry Intelligence Survey 4th Edition p 18

[15] Deloitte 2016, *Customer Experiences of Using Mortgage Brokers*, market research report prepared for the MFAA, p5.

Annexure 1: Profile for Tim Gaspar and Hatch Financial Services

Profile – Hatch Financial Services

1. Hatch comprises myself and 2 staff. One a full-time loan processor/customer service officer and the other 0.75 FTE admin/marketing person. I am the sole mortgage broker licensed to provide credit assistance.
2. I was recently recognised by my Aggregator (Connective) as the Best All Round Broker of the Year in Victoria.
3. I was a finalist for Customer Services awards with Connective (2018) and The Adviser Better Business Awards (2014 & 2018).
4. Hatch has a Net Promoter Score (NPS) – 80%[16].
5. We have an external provider audit our business and compliance. Over 25% of all files are audited as part of this process.
6. Here is some basic data about the home loans settled by Hatch for its customers over the last decade:

	Fy08	**Fy13**	**Fy18**
Total Settlements	$26.45M	$45.38M	$49.5M
Biggest Lender by $ value	ANZ ($7.12M)	CBA ($14.67M)	Macquarie ($11.8m)
2nd biggest lender by $ value	Westpac ($4.91M)	ING ($12.02M)	CBA ($7.63M)
3rd biggest lender b $ value	ING ($4.58M)	ANZ ($7.7M)	ING ($6.9M)
Total No of Loans	80	101	86
Total No of Lenders Used	12	9	18

7. The table below shows Hatch's source of settled loans for the last 2 years:

	FY18	FY17
Existing clients (new borrowing needs)	36.32%	54.89%
Referrals from clients	36.21%	24.96%
Personal networks	8.5%	8.9%
Business networks	17.76%	8.89%
Other	1.21%	2.36%

[16] Based on research conducted by Fusion Insights in 2017.

Annexure 2: Client Testimonials

The testimonials below are presented to demonstrate the extent of the value that brokers provide consumers:

"As young investors, Tim and Jimmy translated financial jargon into conversation that was easy for us to understand. We felt that through Hatch's guidance we were able to make a well-informed decision that suited us. As first-time buyers we had a lot of questions which were answered promptly and honestly."

"Tim's value-add beyond pure mortgage broking advice was crucial to us securing our dream home in less than 3 weeks…he gave us bidding tips that may just have been the deciding factor in our win."

"We just completed our second mortgage through Tim…While it was 12 years between the two, we would have been in contact with Tim more than a dozen times in between, asking for advice, considering different property options, learning about the market…so when it came time to finally get our next property, it was a simple decision to use Tim…I cannot express strongly enough how working with Tim took the stress out of the process, making it easy… "

"Incredibility helpful in finding loan options tailored to my situation, with the support of Hatch I felt confident to walk the path for the first time."

"When it comes to a mortgage broker it is so much more than just interest rate. The team at Hatch spend the time to truly understand your needs and goals. Tim had the patience we were looking for and was a pleasure to deal with."

"Was great to have Tim…taking the scary, or who should we trust part, out of the finding a mortgage …It was great to have a true unbiased account of what to expect from the whole process too."

"Finding a new home loan was always a hassle to me. When I used Hatch to organise refinance options, it was a pleasure. Easy, fast, with great communication and efficient. "

"Tim and the Hatch staff were efficient and easy to deal with…even when there were a few "hiccups"…Tim did everything in his power to rectify this quickly and with minimum stress to us."

Tim and his team…assessed our needs and responded promptly…their ability to provide their clients with a range of home loan options from various lending institutions makes Hatch a great choice for anyone wanting home loan advice.