

## **Submission to the Senate Economics Inquiry Post GFC Banking Sector**

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I refer to the evidence provided to the Committee on August 8th 2012 by Ms Denise Brailey of the Banking and Finance Consumers Support Association (Inc) and wish to put Ms Brailey's Submission to the Committee and her evidence in the correct historical prospective.

I have been a mortgage broker in the West Australian market for the past 25 years and previously worked as property finance lending officer for national finance company. I have served as WA State President of the Finance Brokers Association of Australia for three years up to February 2003, was then CEO of the FBAA in 2003/04, I served as WA state Councillor of the Mortgage & Finance Association of Australian from 2005-2007 and I served a total of eight years as an Industry Representative on the former WA State Government Finance Brokers Supervisory Board.

I am currently a lecturer in the Diploma of Financial Services (Finance & Mortgage Broking Management) with a Registered Training Organisation and from 1992-1997 was a lecturer in the finance broking course delivered by the Perth College of TAFE. I am currently a Director and Responsible Manager of two companies that hold an Australian Credit Licence that are restricted to finance broking activities.

As a result of my position of Industry Elected Representative on the WA Finance Brokers Supervisory Board in 2000/01 I was a Witness at the Gunning Committee of Inquiry, the Temby Royal Commission and the State Parliamentary Upper House Select Committee of Inquiry into the finance broking profession held during this period. These Inquiries related primarily to activities of lenders, borrowers, brokers, valuers and solicitors engaged in the private mortgage sector of the finance market and were not concerned with the mortgage market generally, as it relates to bank lending or the provision of regulated LoDoc, LiteDoc or NoDoc loans to individual borrowers.

However, as a result of general lending practices and concerns about tax evasion by the Federal Government, measures were included in the 2010 NCCP legislation to effectively put an end to true LoDoc, LiteDoc and NoDoc lending to individual borrowers. The NCCP does not regulate lending to company borrowers or any lending that is predominantly for investment purposes with the exception of investment in residential real estate by individuals.

Although there are lending products still promoted as LoDoc or LiteDoc loans, unlike the period prior to July 1st 2010, lenders are now required under the NCCP regulations to obtain some form of substantiation of a borrower's incomes. This type of lending is essential if the self employed are to obtain housing finance, but do not at the time of applying for credit have the most recently completed financial year's tax return.

Bear in mind that the self employed generally are not required to lodge their business and personal tax returns for up to 10 months after the end of a financial year. The most common reason for this delaying in finalising tax returns relates to the availability of Accountants and Tax Agents to complete this work given the large number of self employed people and companies seeking their service post June 30th each year.

Under the provisions of the NCCP regulations, lenders of regulated credit, which encompasses all forms of credit for personal use, including owner occupied and investment housing loans to individuals, are obligated to assess a borrower's ability to service a loan from income. For self employed borrowers, income verification can be achieved by means other than the most recent financial year's tax return. This type of loan is referred to as a LoDoc loan.

The three common alternative means of income verification are:-

- Business bank statements covering a 3-6 month period.
- The last four quarterly Business Activity Statements (BAS) printed from the ATO Tax Agents Online Portal.
- A letter from the borrower's Accountant or Registered Tax Agent certifying that the borrower's statement of income is realistic and in line with the Accountant's expectation (given that they have access to the borrowers bookkeeping records for the previous financial years).

While Ms Brailey's statement's to the Committee about LoDoc lending have relevance to the period prior to introduction of the NCCP, particularly those States that had no effective broker laws prior to July 1st 2010, they are significantly less relevant in today's lending market.

This assertion is supported by information already provided by others to the Committee that there is no unusual trend in arrears associated with LoDoc lending compared with fully income verified loans (Full Doc Loans).

As Government backed RMBS issues have very strict criteria governing the credit assessment standards and lending ratios on loans packaged up in these securitised issues, it would be incorrect to say that there are high risks attached to this form of Government investment in the mortgage market. Most LoDoc loans that exceed 60% lending ratio, up to a 80% maximum, are mortgage insured at the borrower's expense and therefore do not present a significant risk to the lender or RMBS investor.

Denise Brailey stated that there are 39 credit providers that engage in LoDoc lending that require the borrower to hold an Australian Business Number (ABN) for only one day. As a practicing broker I know of only one such lender in the current market and, as a result of the introduction of the NCCP, they require verification of sufficient income to service a proposed loan.

In regard to loan serviceability calculators, which I use on a daily basis to access a client's borrowing capacity, they are developed by lenders to ensure that borrowers do not over commit themselves and this can easily be demonstrated by any lender to the Committee. Again, these calculators are designed to ensure the lenders compliance with NCCP.

The suggestion that lender's Business Development Managers advise brokers how to use serviceability calculators to assess the income a borrower needs to declare to qualify for a LoDoc loan is no longer possible, because lenders now require some form of verification of income. While it was possible prior to the NCCP for dishonest borrowers and unscrupulous brokers to make up a figure, so long as it meet the minimum amount required in the serviceability calculator to qualify for the loan, the new regulatory environment and practice standards introduced by lenders minimises this type of loan fraud.

The recent Basel III liquidity standards imposed on banks has further required banks tighten up their lending standards, as a consequence of weaknesses in the overseas banking sector post the GFC.

Denise Bealey refers to problems in the credit market that were evident during the credit boom from 2000 to 2008 but I believe other evidence this Committee will hear during its sittings will confirm that the dodgy broking and lending practices of the past have largely been eradicated since the implementation of the NCCP in 2010. I suspect that the disaffected borrowers to which Ms Brailey refers have loans taken out prior to July 2010.

I also do not subscribe to Denise Brailey's "big bang theory" regarding the introduction of LoDoc lending in the late 1990's. From my observation at the time, as a practicing mortgage broker, the concept of LoDoc loans was introduced by non-bank lenders with funding sourced from the USA. Such loans enabled the self employed to obtain a home loans when their Accountant was unable to complete the most recent financial year's tax return at the required time.

Other lenders, including the major banks, gradularly extended their lending products to meet this growing market, while still requiring applicants to meet the same credit standards as regular, fully verified income loans. Most banks eventually introduced tighter standards for LoDoc loans by reducing the loan to valuation ratio requirements and requiring mortgage insurance on loans in excess of 60% of valuation.

I will conclude by saying that despite the implementation of the NCCP, it won't achieve the desired results if it is not effectively policed by ASIC. The failure of the former WA Finance Brokers Control Act 1975 to protect private mortgage investors was primarily due to:-

- A) Failure of successive Governments to heed the industry's call over 20 years for updates to make the regulation relevant to changing practice standards.
- B) Failure to act swiftly on complaints that would have revealed systemic problems with some brokers, lenders and valuers.
- C) Failure by the regulator to employ properly trained staff, familiar with industry practice standards, to investigate complaints in sufficient depth to reveal irregularities.

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