30 June 2017

Ms Ruth Moore
Manager, Financial Services Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Westpac Place
Level 20, 275 Kent St
Sydney NSW 2000
T. 02 8253 4149
westpac.com.au

Per email: consumercredit@treasury.gov.au

Dear Ms Moore,

ASIC REVIEW OF MORTGAGE BROKER REMUNERATION – INVITATION TO COMMENT

The Westpac Group (**Westpac**) appreciates the opportunity to provide comments to the Government's public consultation on the proposals set out in the Australian Securities and Investment Commission's (**ASIC**) Report 516: Review of mortgage broker remuneration (**REP 516**).

Our submission provides commentary on the central themes of the report with feedback on the individual proposals in **Annexure A**. Westpac has also contributed to, and supports, the submission made by the Australian Bankers' Association (**ABA**).

Westpac recognises the importance of getting remuneration frameworks right, given incentives are a key driver of behaviour and culture. We have welcomed the work undertaken by industry, the regulator and the Government to ensure incentives are appropriately designed and calibrated to support positive consumer outcomes.

Demonstrating our commitment to doing the right thing by our customers, Westpac has led industry in making significant changes to our remuneration arrangements. For example, in October 2016 Westpac removed all product related incentives for referrals for the 2,000 tellers in the Westpac branch network with incentives now based entirely on customer feedback. In April 2017 this was extended to include the St. George, Bank of Melbourne and BankSA branches. This means that all tellers across the Westpac Group will only be paid an incentive for providing great service. The remuneration of personal bankers has also been enhanced, product-specific sales targets have been removed and incentive rewards for personal bankers are being changed to equally weight service to customers and sales, with 50 per cent based on customer measures and 50 per cent on financial measures.

Westpac is equally committed to reviewing third party remuneration arrangements and making the changes necessary to support positive consumer outcomes.

Concurrent reviews

In April 2017, Mr Stephen Sedgwick AO completed his review of product sales commissions and product based payments in retail banking in Australia (**the Sedgwick Review**). The Sedgwick Review considered the remuneration arrangements of bank staff and third parties, including payments for selling bank products such as deposit accounts, mortgages and credit cards. The Sedgwick Review was particularly focused on whether the current remuneration arrangements, including commissions, bonuses or other incentives, may result in a misalignment of the interests of bank staff and third parties and the interests of their customers.

Westpac is committed to implementing each of the 21 recommendations articulated in the final Sedgwick Review report. These recommendations address:

- remuneration structures for bank staff;
- governance, culture and performance management; and
- third parties.

There is a strong degree of alignment between Sedgwick's recommendations and the proposals in ASIC's REP 516 regarding third party remuneration. Responding to these recommendations will be complex and will require consultation with the broader industry, brokers and aggregators and the relevant regulatory bodies such as the Australian Competition and Consumer Commission (**ACCC**) and ASIC. It is imperative that any activity by the Government in response to ASIC's REP 516 is mindful of these existing streams of work to prevent any duplicative or contradictory initiatives.

For further Information in relation to any of the matters raised in this submission, please contact Michael Johnston, Acting Head of Government Affairs on (02) 8253 2726 or michaeljohnston@westpac.com.au.

Yours sincerely,

Michael Johnston
Acting Head of Government Affairs

ANNEXURE A

Proposal	Westpac response
Proposal 1: Improving the standard commission model (e.g. reflecting the LVR of the loan)	REP 516 identified that the standard commission model is almost universal, comprising both an upfront and trail commission component. ASIC are concerned that this model may give rise to conflicts of interest, including a product strategy conflict or a lender choice conflict[1]. Given these potential conflicts of interest, ASIC suggests that the standard model could be enhanced to mitigate this risk. As an example, ASIC suggests that lenders could reflect the loan to value ratio (**LVR**) of the loan (and other metrics, such as compliance metrics) in how they calculate these commission payments. Westpac supports initiatives that are seeking to encourage and sustain positive consumer outcomes and believes that the commission model needs to be simple and transparent. It is important to understand, however, that the commission structure is only part of the solution to enhance consumer outcomes. The compliance arrangements and structures surrounding broking practices are equally relevant. Accordingly, steps to change the standard commission model would need to be taken with care to prevent market distortion and unintended consequences. The franchise model will also need to be considered when determining any changes to commission structures, as we understand the franchisee remuneration model is similar to the standard broker industry commission model. *Importance of a level playing field* The process by which industry responds to the Sedgwick and Broker Remuneration Review (**BRR**) recommendations regarding third party remuneration will be important to ensure a level playing field is maintained across all lenders, For instance, if lenders respond individually, there is a risk that each lender may develop different methodologies for the calculation of commission. This could result in lender choice conflict

[1] ASIC defines these terms in REP 516 as:

- *Product strategy conflict* – a conflict of interest arising from commission structures in the mortgage broking market where a broker recommends a higher value loan than the customer originally sought or needed to maximise their commission payment. This may also involve recommending a particular product or strategy to maximise the amount that the consumer can borrow.
- *Lender choice conflict* – a conflict of interest arising from commission structures in the mortgage broking market where a broker recommends a loan from a particular lender because the broker will receive a higher commission (whether from that lender generally or for that particular loan product) even though that loan may not be the best loan for the consumer.

Proposal	Westpac response
	where a broker may be encouraged to favour/promote the product of the lender that will deliver a higher commission payment. First mover disadvantage to changing current commission models would also need to be considered to ensure early adopters of a different commission structure, such as one based on LVR or quality metrics, are not adversely affected. Westpac is working with other lenders, relevant industry bodies (such as the ABA and MFAA) and aggregators to determine what may be the appropriate industry level response for such third party remuneration recommendations. . As detailed in the ABA's submission, matters that may be considered by industry include: • Developing a consistent approach to quality measures; • Better defining good customer outcomes; • Considering principles for changing volume based payments and non-monetary (soft dollar) incentives; and • Agreeing a timeframe for implantation of self-regulatory changes. Westpac has appreciated Treasury's participation in these industry level discussions and will continue to engage with Treasury as this work progresses. *Options for enhancing the current standard commission structure* ASIC's suggestion to incorporate an LVR qualifier into the calculations of upfront commission payments would be highly complex and would not necessarily result in better consumer outcomes. In many instances, higher LVR loans have more complex features and the broker needs to spend more time on structuring the loan. The greater effort involved in assisting consumers with these transactions would not necessarily be reflected in a commission payment based on LVR and may result in the broker being disadvantaged if a lower rate of commission was paid on a particular transaction. The segment of the market that would be most affected by such a change would be first home owners who traditionally have higher LVRs. Reducing the commission payable on these types of loans may deter brokers from acting in this space, presenting additional challenges for first home buyers. Another option proposed has been to base the commission payable on loan quality metrics, such as customer feedback and compliance indicators. This could be difficult to apply, as such indicators are prone to being subjective in interpretation and manipulation. Different interpretations of loan quality metrics may also result in inconsistent treatment by lenders, potentially leading to market distortion. Accordingly, some type of framework

Proposal	Westpac response
	would be required to debate and manage different interpretations. Other options would also need to be carefully considered to determine if they result in any unintended consequences. For instance, a flat fee commission structure could prompt an increase in split banking as brokers seek to maximise income by submitting smaller deals. *Regulatory costs* Developing existing, or implementing a new commission structure will result in significant regulatory costs for industry participants. Depending on the metrics feeding into the model, brokers will require very detailed training or knowledge uplift to ensure there is a clear understanding of the factors determining commission payment outcomes. For example, to ensure there is the appropriate transparency, all Recipient Created Tax Invoice (**RCTI**) statements would need to include the loan LVR ratio against every transaction recorded on the statement so the aggregator/broker can determine the commission amount that aligns to each applicable LVR. It may further be necessary for aggregator software to be extensively updated, likely at substantial cost. Additionally, existing contractual arrangements will need to be updated to reflect the new commission structure. Existing contractual obligations, such as the existing obligation on the Franchisor to ensure the franchise commercial model remains a viable business model, would need to be taken into consideration and may require a review for commercial viability being undertaken pre-implementation.
Proposal 2: Moving away from bonus commissions and bonus payments	Westpac supports this proposal, noting that this reflects our current practice. Volume based incentives for our Westpac and St.George brands, over and above upfront commission and trail, have been wound back since January 2015 and sales incentives during campaigns have been fully removed since 2015. For our RAMS business, the current commission structure does not include bonus commissions or bonus payments. A small number of franchises remain on a historic remuneration structure that includes volume-based upfront incentives. This will have been completely phased out by the end of August 2017.
Proposal 3: Moving away from soft dollar benefits	ASIC's REP 516 defines soft dollar benefit as being any rewards or benefits that are not cash and highlights that such benefits risk poor consumer outcomes. Westpac agrees that certain types of soft dollar benefits can present such a risk and have ceased all volume based soft dollar incentives that are tied to sponsorship across all brands. All sponsorship is now tied directly to education and training outcomes and steps are being taken to

Proposal	Westpac response
	give greater transparency on what would qualify a broker to receive such benefits. Particularly, Westpac is currently exploring how qualifiers could be structured so as not to trigger the broker choice conflict. Such qualifiers will be based on a balanced scorecard approach and developed in consultation with aggregators. Broker training is a key pillar in ensuring the skills of industry participants meet compliance, risk and conduct requirements. Consumer outcomes are enhanced when customers are served by professional, well skilled brokers who have been trained not only in their regulatory requirements, such as responsible lending obligations, but also in the specific processes and policies of the lender. Not only is the customer experience enhanced, as the timeliness of decisions is improved, but compliant customer outcomes are also achieved. Westpac is also reviewing its hospitality practices with the broking industry and limits have been put into place based on spend per function. Transparency and monitoring of broker attendance will be gained through a register recording attendance at events. To ensure a level playing field, it would be beneficial for the transition away from soft dollar payments to be supported by clear definitions of what constitutes a soft dollar benefit. Particularly, whether ASIC's recommendation stemmed from a concern about the type or volume of soft dollar benefits being paid. The importance of brokers being provided with appropriate training at regular intervals to ensure they have and retain the necessary skills to undertake their role, as well as to keep up-to-date with regulatory expectations or changed legislative requirements, cannot be understated. Any response to ASIC's recommendation regarding soft-dollar benefits should acknowledge and reflect the importance of regular broker education. Industry should also be required to make this transition away from soft dollar benefits within a defined timeframe.
Proposal 4: Clearer disclosure of ownership structures	ASIC found that competition in the home loan market is affected by lender ownership of, or financial interest in, aggregators and the limited ability of smaller lenders to access and remunerate brokers in the same way as larger lenders. As demonstrated through our response to ASIC's review, Westpac does not have a direct financial interest in any aggregators but we acknowledge that lender ownership may have an impact on competition in the industry. We also acknowledge that it is beneficial for consumers to know if there is a relationship of ownership between the aggregator that their broker is accredited with and the lender with which they may obtain a loan. Accordingly, we support the principle of informing the consumer of such a relationship.

Proposal	Westpac response
Proposal 5: A new public reporting regime, to disclose the average pricing of home loans (brokers and lenders)	Westpac supports reforms to increase transparency in the mortgage broking market. ASIC's report suggests that consumer outcomes could be improved by establishing a new public reporting regime of consumer outcomes and competition in the home loan market. To achieve these outcomes, it is important to consider what information will assist consumers making informed choices and how, and in what format, this information will be conveyed to them. Any reporting must also appropriately protect the confidentiality of commercial data. For instance, any data should be published on an anonymised basis and not be capable of identifying any particular lender. Westpac anticipates that the Government and/or ASIC will consult extensively on the design and operation of such a regime.
Proposal 6: Improve governance and oversight to place greater importance on fostering a consumer-centric culture	Westpac views strong governance and risk management practices as essential to achieving our vision to be one of the world's great service companies. We have robust governance and oversight structures, which capture our third party and intermediary channels to ensure they meet our compliance, risk and conduct requirements. These structures are underpinned by our firm commitment to do the right thing and critically, to do the right thing for our customers. Promoting conduct and a consumer-centric culture remains a critical theme as we continue our practice of enhancing our governance and oversight structures. Westpac is fully engaged in industry discussions on how existing governance, oversight and assurance practices can be improved and enhanced. We will continue to support our industry partners as they review and consider their own governance and oversight structures in order to enhance conduct and ensure the progression of great customer outcomes.