Comparison Rates:

We write as an industry organisation that supports ongoing commitment to the Compulsory Comparison Rate initiative. Tools such as comparison rates can be very useful when product pricing is complex – however it is important to design these tools in a way that is most useful to consumers.

Rather than abolishing the Compulsory Comparison Rate, we encourage Government to consider ways that the Compulsory Comparison Rate could be much more useful. Implementation of a few simple and practical steps within the current framework could facilitate a better outcome for consumers by providing a more accurate yardstick of comparison and minimise the current opportunity to manipulate Compulsory Comparison Rates.

<u>Relevant Length of Loans (Loan Terms)</u>

As competition has increased and consumers have become better informed, we no longer see residential mortgage loans running for 25 years with the same lender. This is becoming increasingly less likely over time and renders 25 year Compulsory Comparison Rates ineffective. Various statisticians suggest the average life of loan to be as low as 2 years to as high as 7 years.

It is a reasonably straightforward process to provide a Compulsory Comparison Rate based on a 3 Year Exit, 5 Year Exit and 25 Year Exit. These figures would be more in line with the consumer reality and less reliant on long-term assumptions such as the time cost of money.

By calculating the term as an Exit cost, buried extras such as deferred establishment fees, early exit penalties, discharge fees, and settlement fees can be included in the Compulsory Comparison Rate.

Break costs for Fixed Rate loans exceeding the exit intervals should be noted as an additional fee not included in the calculation of the Compulsory Comparison Rate. Alternatively, Fixed Rate Loans could be excluded from this requirement where the Fixed Rate Term exceeds the applicable Exit Interval.

<u>Declaration of Impending Changes to Variable Rates.</u>

This section only applies to Variable Rate Loans.

Although rarely applicable to the banking sector, several non-bank lenders (one of which is a subsidiary of a bank) have actively held back rate rises to allow them to advertise a significantly lower rate for up to 120 days after the Reserve Bank has lifted the Target Cash Rate.

Known as “Holding Back”, this practice deliberately widens the consumer perception of rate differences between lenders and affects the accuracy of both the advertised rate and the Compulsory Comparison Rate. However, the reality is that by the time an application is lodged and the loan is settled some 42 to 60 days later, the consumer realises only a very minor advantage, if any, over, more responsive lenders.

This loophole misleads the consumer and penalises honest and responsive lenders.

Lenders must not advertise any rate that does not factor an impending change in interest rate to the consumer.

Legislation should require mandatory adjustment for the unabsorbed portion of the rate change for both advertised rate and the Compulsory Comparison Rate where the lender does guarantee absorption of a rate change for the life of the loan in their standard form loan contract and pre-approval documentation.

Application to all products

Rather than exclusion of products such as Lines of Credit, application of Compulsory Comparison Rates should be broadened to all Residential Mortgage Products and calculated assuming the facility is fully drawn down and minimum monthly repayments are made.

Inclusion of Average Cost

Lenders are prone to creation of costs that are ‘not ascertainable’ at the time of advertising or may not be payable by some borrowers and as such, are not currently included in the Compulsory Comparison Rate.

With the exception of Lenders Mortgage Insurance, it is reasonable that lenders are able to identify fees that are paid by the majority of borrowers. Similarly, it is also reasonable that where fees are paid by the majority of borrowers, an averaging of variable fees should be included in the calculation of the

Fixed Rate Loans – Warning and Disclosure.

Unless otherwise arranged, the applicable rate for Fixed Rate Loans during the Fixed Rate period is not set until the day the loan is settled.

This creates a situation where a consumer makes an application with a lender based on an attractive fixed rate, but by the time the loan settles several weeks and sometimes months later, may end up with an applicable rate substantially higher than the advertised and Compulsory Comparison Rate. If the lender was also holding back, a ‘cheap’ loan can easily become the most expensive option.

However, some lenders lock or cap the applicable rate on application or on approval.

All Fixed Rate loan promotional and advertising material should carry a clear warning that the actual rate that applies for the fixed rate may vary from the currently advertised rate.

Advertising and promotion for Fixed Rate loans where a rate is promoted should also include a disclosure of the whether:

1. You can cap the rate; the cost; what day the rate is capped and for how long.
2. You can lock the rate; the cost; what day the rate is locked and for how long.
3. You cannot lock or cap the rate.

Advertising Standards

Clear definition of the standard wordings, spacing, location, and typeface and point size as a percentage of the largest print in the relevant advertising reduces the ability to create hidden or confusing disclosure.

Current and common practice is to develop a large, finely honed message from the lender with lengthy footnotes, in small print font that actively discourages consumers from getting the message. Effort should be invested in simplifying and standardising these messages, improving the visibility of these messages and ensuring that they are clearly displayed, much like those utilised in the anti-smoking campaigns.

Broker Regulation

Although regulation of the mortgage brokering industry may assist in ridding some of the worst excesses, it may not resolve many real issues facing the consumer.

Active public discussion and implementation must be vigorously pursued to enable focus on solution development and keep the risks and issues in the forefront of the industry and consumers minds.

Discussion papers we have seen regarding regulation seem rather lengthy, onerous and unlikely to result in a simple measurable mechanism that protects the consumer and assists in identification of a qualified, ethical mortgage broker. We do not consider this a particularly complex issue and are puzzled and disappointed that there seems to have been little, if any progress.

Above all, we consider it critical that regulation is effective in consistently raising the professional standard of this industry as a whole. Optimistically this would include direct and measurable improvements in the quality of advice given to the consumer and necessary protection measures and arbitration mechanisms when that advice falls short.