

SUBMISSION

**PRODUCTIVITY COMMISSION
INQUIRY INTO COMPETITION IN
THE AUSTRALIAN FINANCIAL
SYSTEM**

**COMMERCIAL ASSET FINANCE
BROKERS ASSOCIATION OF AUSTRALIA**

2017

CAFBA

Commercial Asset Finance Brokers
Association of Australia

Productivity Commission
4 National Circuit
Barton ACT 2600, Australia

15 September 2017

Submission to the Inquiry into Competition in the Australian Financial System

The Commercial Asset Finance Brokers Association of Australia Limited (CAFBA) is a strong voice for issues within the commercial finance sector. This submission was prepared to support the Productivity Commission to gain a deeper understanding of the work of our members and their concerns about competition within the commercial finance sector.

We are pleased that the Productivity Commission is examining competition in the Australian finance sector. CAFBA underscores the need for the Inquiry to maintain a focus on the availability of, and competition in, financial services for small business.

The submission is broken up into a range of small sections covering areas of concern for CAFBA members. The submission focuses on the negative impact of the Point of Sale exemption.

CAFBA members are professional commercial finance brokers committed to providing the best quality service to our business clients. Despite the quality of financial service provided by many commercial finance brokers, some new and unqualified operators have been able to fly 'under the radar' of regulatory bodies through exemptions.

CAFBA believes that while there is currently a discussion about the lack finance options for small businesses in Australia, there are many choices already available. We believe that the Productivity Commission must examine these options to see how they are communicated. In particular, it would be beneficial to analyse how available they are to small businesses and the level of competition between different financial providers.

CAFBA looks forward to continuing to work with the Productivity Commission to improve the quality of financial services availability of finance to small business in Australia. We would welcome an opportunity to discuss our submission with you.

Yours sincerely,

David Gandolfo
President

Kathryn Bordonaro
Vice President

Background on CABFA

Commercial Asset Finance Brokers Association of Australia Limited (CAFBA) is the peak national body of commercial equipment finance brokers, whose prime area of business is the distribution of commercial equipment finance facilities to their clients. With over 700 members, in all states and territories, CAFBA is an important national voice in the Australian finance sector.

CAFBA members are career professionals, with recent studies showing nearly 67% (East & Partners 2017) of new commercial equipment finance is sourced through brokers. Our members and their clients are predominantly small to medium sized businesses and operate in the commercial finance market. The total receivables in the Australian equipment finance market are approximately \$100 billion, so it is an important component of the Australian economy.

CAFBA members know that providing Australian small businesses with access to finance is crucial to economic growth. Although brokers are commonly associated with home loans, CAFBA members work in a complex environment to provide a boutique service. Without the work of CAFBA's professional members, many Australian small business owners would struggle to navigate the complexities involved with commercial equipment finance.

CAFBA embodies the strengths of its members in a unified approach for dealing with financiers and legislators at a national level and regularly seeks the views of members. As an association, CAFBA provides the framework and support to professionally assist our members in their daily activities. This involves education and training, legislative and regulatory updates and forums where the members can interact and exchange ideas with their peers.

CAFBA prides itself on being self-regulating and maintains strict membership standards on probity, continuing professional development, industry experience, and reputation. It is a condition of CAFBA membership that commercial equipment finance brokers must belong to an ASIC-approved External Dispute Resolution Scheme.

CAFBA is a member of the Council for Small Business Australia and works collaboratively with the government, regulators, and business groups.

Availability of Commercial Finance Options for Small Businesses

CAFBA believes that small businesses are vital to Australia's economy for employment, innovation, and productivity. Access to finance is essential to ensure that small businesses succeed and CAFBA members work to enable this.

CAFBA believes that while financial options for small businesses could improve, the current environment does provide choice. Over the past few years, there has been an increase in media of the difficulty for small business to access finance. CAFBA highlights that the finance sector in Australia does provide opportunities for small businesses to access finance. Every day, CAFBA members work to support small businesses to navigate the options and provide them access to finance. Gaining access is not easy, but a quality financial system requires this.

Australia is a leader in the financial services industry due to the quality of regulatory frameworks that govern access to and the provision of finance. CAFBA works to ensure that our small business clients understand and comply with the various requirements to gain and maintain finance. CAFBA members are professionals and work to ensure that financial options are right for the businesses they work for. It is important to remember that access to finance is not a right and that denial of finance is may signify that we have a strong financial sector. Despite this, many hard working small business owners do struggle to gain access to finance and these issues must be addressed.

CAFBA acknowledges that there is a range of challenges that impact the offering of finance to small businesses in Australia. CAFBA believes that there are clear communication gaps between bankers and financial institutions, and small businesses in Australia. Small businesses need opportunities to improve their knowledge and understanding of how to access finance. Banks and financial institutions also need to provide support to small businesses in the form of better explanations of what they needed to do to gain finance. While options are available, many small businesses do not have the time or resources to navigate the complexities of gaining finance. This reduces productivity and combined with the professionalism of CAFBA members, is a driving factor to increasing the contracting of commercial and asset finance brokers in Australia.

New and Emerging Finance Providers

CAFBA recognises the important role that new and emerging finance providers can play in creating more competition in the Australian finance sector. In particular, the rise of financial service providers using and innovating with emerging technologies is pleasing. This has the potential to provide businesses with a range of new choices; however, this must be regulated and managed appropriately.

The members of CAFBA believe that it is important to ensure ownership and or control of emerging companies that provide finance is diverse. While Australia's finance sector is

served well by major banks in many ways, it is important that new “fintech” companies are not dominated by these finance providers.

Consistency and Standardisation in AML/CTF Policy in the Finance Sector

CAFBA believes that the Productivity Commission must focus on areas where red tape can be reduced in the financial sector. The onerous requirements, associated paperwork, and confusing interpretations by lenders regarding Anti-Money Laundering (AML)/Counter-Terrorism Finance (CTF) reform are causing challenges for small businesses. Reducing burdens of red tape like this in both in government and business is essential to delivering on the current government’s agenda of economic growth through innovation.

A clear productivity gain that could improve how small businesses and brokers access credit is to provide greater consistency in AML / CTF compliance processes. There is a range of AML / CTF compliance forms required to be completed by small businesses when applying for loans. If a business is rejected for the loan and goes to a separate financial institution, they will likely have completely different forms and information required to meet their AML / CTF process.

AML/CTF legislation has not stopped identity fraud. Professional brokers and financiers are burdened by the cost and administration of the regulation, which has not stopped criminals finding ways around it.

CAFBA acknowledges that there is a level of fraud in the equipment finance industry, as there is in other industries; however, it is not a favoured means of money laundering or raising funds for terrorism. Lenders acknowledge that equipment finance is a “low-level risk” for CTF, but it is still bound by the same requirements as “high-level risk” products like cash deposits. The target of AML/CTF legislation largely falls outside the equipment finance space and fraud is generally minimised by normal due diligence. While identification of borrowers/guarantors and verification of financial information is of critical importance, it is superfluous to extend this to the extent of locating and certifying Trust Deeds and verifying beneficiaries. Some of these Trust Deeds have been in place for decades, but are required to finance assets such as a motor vehicle to be used in the normal course of business.

In the equipment finance sector, borrowers receive assets, not cash. The security position of financiers should be strengthened by PPSR which identifies and secures assets, and reduces the need for overlaid protections under AML/CTF.

CAFBA believes that there is a need to standardise the way that major banks apply current AML / CTF compliance policies. There must be improved consistency in basic processes to increase productivity for both small businesses and brokers. Policies can be widely different and include unnecessary information that may be focused on market research rather than compliance with the legislation.

Quality of Financial Services Available to Businesses

Professional finance brokers are essential for improving productivity. Brokers reduce the time that businesses spend on gaining access to finance and allow them to spend their valuable time on growing and improving their businesses. CAFBA has a strong commitment to ensuring that all our members are professional and receive and engage in regular professional development to ensure they comply with national standards and regulations.

CAFBA would like to underscore to the Productivity Commission the difference between personal, home, and commercial finance brokers. We recognise that brokers have been under pressure in the media through the poor practice by some in other sectors. Despite this, commercial and asset finance brokers are highly regarded in Australia due to their professional conduct. It is essential that we work to maintain this.

CAFBA members arranging business finance as licensees, must meet specified standards and comply with ongoing obligations as follows:

- Meeting general conduct standards, including acting fairly and honestly and managing any conflicts of interest so as not to disadvantage businesses;
- Maintaining their organisation's competence to engage in credit activities, including having responsible managers and adequately trained representatives;
- Maintaining adequate financial resources and risk management systems;
- Meeting responsible lending conduct obligations, including ascertaining and verifying a businesses' financial situation, and assessing whether the credit contract is suitable; and
- Belonging to an ASIC approved EDR scheme and lodging an annual compliance certificate with ASIC.

It is CAFBA's position that where a business is providing financial services to businesses, staff engaged in this process should be required to:

1. hold an Australian Credit Licence; or
2. be appointed as a credit representative of a licensee;

This would place those individuals who act as credit intermediaries in the same position as CAFBA members and others engaged in the finance industry providing similar services.

We believe the adoption of consistent regulation across the industry is necessary, not only to create a level playing field but also provide adequate business protection. For obvious reasons, consistency of credit legislation has been a key aim of the reform process for many years, and the removal of the current exemption will assist in achieving this.

The Productivity Commission should be aware that the current professionalism and quality of commercial and asset finance services provided to businesses is at risk, particularly due to

emerging and unregulated financial service providers. While a well-developed broker market that caters to small business lending could increase competition, we must ensure that standards are maintained.

Car Retailers Finance

CAFBA believes that the Productivity Commission should have a focus on the negative impact that unregulated competition can have in relation to car sale finance.

Prior to the commencement of the National Consumer Credit Protection Act in 2010, the previous Labor Government exempted point of sale (POS) vendor introducers from the requirements of the Act. The exemption thus applied to those who engage in credit activities at the point of sale. The specific exemptions included excluding those POS vendor introducers from the credit licensing regime and the responsible lending obligations. This exemption has remained in place for almost a decade and is an area of broken policy from the previous government that remains in need of repair.

CAFBA members, who are professional equipment finance brokers are not exempt and are bound by the Act when arranging finance for businesses, providing protection for businesses and sector-wide standards for brokers of business finance. This is something that CAFBA supports for the benefit of all, but in particular to ensure that businesses in Australia are protected.

The outcome is brokers of business finance fall into 2 broad classes; those who are required to be licensed and those who are not, simply because they are vendor introducers. In our view, a broad-based vendor exemption for business finance introduced at the point of sale is no longer tenable. It was intended to be an interim exemption for 12 months to allow the Government to consider the market and processes in greater detail. It is now approaching 7 years, with deep and distinct business and competitive disadvantages.

The negative consequences of this policy are that the exemption provides an opportunity for high-risk commercial finance to be provided to consumers. It opens a window of opportunity for inexperienced individuals with limited training to provide low-quality services to businesses. This is concerning

Businesses providing financial services with a POS exemption:

- Are not required to meet any entry standards and ASIC is also unable to exclude vendor introducers from the credit market
- Can select, recommend or propose credit products without having to conduct an assessment as to whether the product is suitable for the consumer, or meets their financial requirements or objectives.

- Limit the ability of consumers to access remedies for the conduct of vendor introducers.

These characteristics are at odds with the requirements of finance brokers, such as many CAFBA members who are licensed to arrange consumer finance, complying with the Act and applying responsible lending practices. The alternative to licensing is for brokers to act under the licence of a broker or a credit provider/lessor by being appointed its credit representative.

The exemption, therefore, does not provide any means of adequately regulating or controlling the activities of POS vendor introducers who may cause loss or damage to consumers, despite their linked credit providers/lessors being responsible for their conduct.

Consumers rely on their financial provider to give them a high-quality service when making any purchase. The variety of pressures placed on the staff of car retailers, combined with varying experience, or inexperience, in providing financial service can negatively impact on consumer experiences.

The risk of harm is more likely where the POS vendor introducer has selected the financier on the basis of the commissions they will receive if finance is approved, where those commissions increase the cost of finance paid by the consumer. The exemption also means that there is a lack of competitive neutrality between POS vendor introducers and other businesses, like licensed CAFBA members, which are performing similar functions.

How well-informed a consumer is about their car purchase and financial options should not depend on the practices of dealers involved. All dealers that are involved with providing finance options for car sales at the point of sale/ time of sale should be experienced professionals and be trained in providing services specific to their client's needs.

Of concern to CAFBA is the way some consumers may misunderstand the protections available to them when accepting finance from POS vendors. Car buyers may believe that they have full protections when they obtain dealer finance and, through a lack of awareness of POS policy and legislation, they place unwarranted faith in what they are told by car dealers which makethem even more vulnerable than the exemption itself and even easier prey for unscrupulous operators.

The Competitive and Consumer Act (C&C Act) promotes competition and fair-trade markets to benefit consumers, businesses, and the community. CABFA holds the strong view the current vendor introducer exemption to the NCCP Act is at odds with objectives of the C&C Act. Conduct by businesses in an Australian market is meant to be such that does not have a substantially adverse impact on competition or detriment to the broader consumer interest. The only occasions on which conduct should run counter to this is if the law believes it is the public interest to do so. The Australian Competition & Consumer Commission, the Australian Competition Tribunal and the courts are arbiters of the public

interest.

CAFBA understand specific laws, such the POS vendor introducer exemption, can override the essential tenets of the C&C Act. Despite this, the continuation of that exemption cannot be sustained in the public interest. The anti-competitive effect of continuing the exemption is the significant financial and compliance investment by licensed brokers in meeting their licensing and responsible lending obligations and in maintaining them over the longer term.

By comparison, POS vendor introducers merely have to follow what their linked credit providers /lessors train them in and instruct them to do. There is no investment in POS standards, consumer protection or consumer disclosure. And, at its worst, the structural issues can result in a significant disadvantage by consumers paying more for their finance than they may have otherwise, resulting in potentially a significant financial benefit to the POS vendor introducer.

The anti-competitive consequences of the current POS vendor introducer exemption are very real to the consumer finance broker market. It is, to our mind, bad public and competition policy to have different regulatory models and outcomes for the same processes/ services unless it is demonstrably in the public interest to do so. CAFBA does not see competition law public benefit in keeping the current POS vendor introducer exemption.

Conclusion

This submission highlights CAFBA's desire to ensure that the Productivity Commission has a focus on the financial options and competition for small business finance within the finance sector. We also want to ensure that there is a deep understanding of and appreciation for the professionalism of commercial equipment finance brokers.

While there are many finance options available to small businesses in Australia, brokers play a crucial role in facilitating their access. New and emerging finance providers through "fintech" can and will play an important role in increasing competition, but high standards must be maintained. Consistency and standardisation of AML/CTF policy within the finance sector would increase efficiency and productivity. Professionalism and quality of services provided by all providers within the finance sector is crucial to provide both value for money and maintain productivity.

CAFBA would welcome an opportunity to discuss any aspect of this submission with the Productivity Commission.