



Submission to the Financial System Inquiry – Round 2

Attached for your consideration is a submission prepared by Flongle.com.au Pty Ltd (“flongle”) in regard to the Financial System Inquiry.

About Us

flongle is an Australian company delivering the world's first fully independent mortgage contest platform. Borrowers or their advisers use flongle to gather and anonymously publish their finance requirements and capacity, where an open market of banks, mortgage brokers and non-bank lenders can then, while fulfilling responsible lending obligations, tender suitable products and pricing in a sealed bid contest.

flongle's match and price engine then ascertains a match factor and Total Individual Cost for that borrower for each product across a range of user selected exit points and repayment amounts. Flongle's Top Deals filter identifies the best matching bid for each product that delivers the lowest Total Individual Cost based on the borrower's settings. Borrowers can also disable filtering to see all bids made for their contest and at their discretion connect directly with one or more bidders.

The platform is totally unbiased within the meaning of section 160B of the National Consumer Credit Protection Act.

flongle can be used standalone by borrowers over secure internet connection, or with online, end to end human help of an independent professional, or by the borrowers own independent mortgage adviser.

Horizontal Integration

As the Inquiry is aware, the Rudd Gillard Federal Government introduced the Future Of Financial Advice reforms (**FOFA**) which despite recent review by the current Abbott Government have by and large, left unaltered particularly with respect to the provision to consumers of financial advice. While it would belittle the overall effect of FOFA to single out particular concerns and reforms, it is painstakingly obvious that three key reforms are the skills based improvement of the quality of advice, the best interests test and the banning of conflicted remuneration.

Indeed, the Financial System Inquiry, in its Interim Report published July 2014 supports the essence of the Ripoll Report in making the observation that improving standards of adviser competence and removing the impact of conflicted remuneration can improve the quality of advice.

Slightly prior to the commencement of FOFA reforms, a series of both small scale and large scale horizontal integrations commenced between the financial services and mortgage broker sectors. The most notable examples of this include Mortgage Choice and Yellow Brick Road, both of which in themselves, also suffer Vertical Integration Risk to some extent or another.

Convergence Risk

While there may be compelling reasons for both the benefit of consumers and also advice professionals to integrate mortgage advice into a financial advice practice, the

sector has recently made significant progress in regaining consumer trust and recognition as professional advisers, rather than as mere product sellers. Conversely, the mortgage industry continues to operate a substantially conflicted product sales model in which it is virtually impossible to prioritise the interests of the client above their own.

Horizontal integration of conventional mortgage broker businesses with any financial advice practice creates a situation whereby conflicted remuneration has again been reintroduced by companies and individual Licensees or authorised representatives of an Australian Financial Services Licensee.

Although mortgage products are specifically excluded from the Financial Services Reform Act 2001 ('FSRA'), the Corporations Act and therefore FOFA, this distinction is not commonly understood by the general public.

Notwithstanding, it is a somewhat confused message and an unreasonable expectation for a consumer to rely on independent advice in their best interest on one strain of product from one part of a business and not be safe in expecting the same standard of professional care when dealing with its mortgage advice department or the planners referral partner.

It is worthwhile noting that mortgage broker remuneration is neither insignificant nor dissimilar to the conflicted remuneration received by financial advisers pre-FOFA. It includes five of the six forms of remuneration identified by ASIC¹ in its submission to the 2009 Inquiry into financial products and services in Australia ('**Ripoll Report**') that were subsequently banned under FOFA including:

- (a) up-front commissions;
- (b) trail commissions;
- (c) soft-dollar incentives;
- (d) volume bonuses; and
- (e) rewards for achieving sales targets.

Summary

While it makes sense to retain the current legislative separation and approach between credit and financial advice, integration between Financial Services and mortgage broker or similar business defies the spirit of FOFA, the best interests of the consumer and harms current progress toward the development of professional advice sectors for both financial advice and mortgage advice. It marks the deliberate reintroduction of conflicted remuneration into financial services through the exploitation of a small legislative loop hole.

¹ Parliamentary Joint Committee on Corporations and Financial Services Inquiry into financial products and services in Australia Report November 2009, Page 116.

While mortgage broker remuneration is quite established and accepted, horizontal integration, like FOFA and the NCCP is relatively young. As such, the two previously and still mostly separate industries, have not had the opportunity to develop deeply intertwined commercial dependencies which would otherwise make the basic return to separate, vertical sectors either difficult or costly.

We respectfully suggest that it would be a missed opportunity if the inquiry did not in the very least consider extending the ban on conflicted remuneration to any AFS Licensee or representative regardless of the type of product they are recommending. We also respectfully suggest a ban on any form of horizontal integration where the AFS Licensee and their representatives and/or the Australian Credit Licensee and their representatives provide advice on products other than their own.

Thank you for receiving this submission and considering its evidence.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Michael Lee". The signature is written in a cursive, flowing style.

Michael Lee
Founder

flongle.