



**THE LAW REFORM COMMISSION
OF WESTERN AUSTRALIA**

Project No 45

Mortgage Brokers

REPORT

SEPTEMBER 1974

The Law Reform Commission of Western Australia was established by the *Law Reform Commission Act 1972*.

The Commissioners are -

Mr. E.G. Freeman, *Chairman*

Mr. B.W. Rowland

Professor R.W. Harding

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**TO: THE HON. N. McNEILL M.L.C.
MINISTER FOR JUSTICE**

TERMS OF REFERENCE

1. The Commission was asked to consider and report on the question whether legislation should be enacted to control the activities of mortgage brokers.
2. A number of businesses act as mortgage brokers in this State, either separately or in association with other businesses such as land agencies. The most common function of a mortgage broker is to arrange, for a fee, loans on the security of mortgages over land, although some brokers arrange loans which are secured on personal property or are not secured at all.
3. Suggestions were made to the Commission during the course of its study on Project No. 37 (Review of the *Land Agents Act*) that mortgage brokers should be subject to statutory control. The Commission considered that this merited further study, and on its recommendation the Attorney General made it a project.

THE WORKING PAPER

4. The Commission issued a working paper on this project on 20 February 1974. Copies of the paper were sent to those persons listed on page 3 of the paper, and to members of the public who answered the Commission's notice in the press inviting comments.
5. A list of those who commented on the working paper is contained in Appendix I. All comments have been taken into account even though not specifically referred to.

A copy of the working paper is attached as Appendix II to this report.

DISCUSSION AND RECOMMENDATIONS

(a) General

6. The Commission defines a mortgage broker as a person who in the course of business as an agent negotiates or arranges loans of money for or on behalf of another for reward. The Commission appreciates that this definition may bring within the ambit of this report categories of persons who would not normally describe themselves as mortgage brokers but as finance brokers.

However, the Commission considers that, if statutory control is to be introduced, it should not be limited to persons negotiating or arranging loans on the security of mortgages of land. Mortgage brokers do not always confine their activity to arranging secured loans (see paragraph 2 above) and the risk of defalcation by the broker exists whether or not the lender intended that the loan be secured. The only categories of persons who should be exempt from any statutory control should be those where the safeguards against defalcation are already adequate.

Accordingly where the Commission makes recommendations in this report with respect to mortgage brokers, such recommendations also extend to finance brokers.

(b) Is statutory control necessary?

7. At present, mortgage brokers may be required to comply with a number of statutory provisions depending on the extent of their activities. For example, where they lend their own money they may have to comply with the *Money Lenders Act 1912*. However when mortgage brokers act as agents in arranging loans they are not required to be licensed and, generally speaking, are not otherwise controlled by statute (see paragraphs 8 to 12 of the working paper).

The Commission expressed the view in the working paper that some statutory control over mortgage brokers was desirable. In particular, the Commission suggested that they should be required to maintain trust accounts which should be subject to annual audits, and that they

should be required to take out a bond with an approved surety or contribute to a fidelity guarantee fund (see paragraph 22 of the working paper).

8. Most commentators agreed that some statutory control over mortgage brokers was necessary. One favoured the Queensland provision where there is a prohibition on the charging of fees for the procuring or negotiating of loans on behalf of other persons (see paragraph 19 of the working paper). A mortgage broker considered that legislation was not necessary, as, in his view, the Mortgage Brokers Association of W.A. endeavoured to protect investors and the majority of mortgage brokers were members of the Association. This commentator said that if the Commission was of the opinion that legislation was necessary, controls similar to those applicable to moneylenders should be introduced.

The Australian Finance Conference, while supporting the introduction of statutory controls for mortgage brokers, considered that the controls should be kept to a minimum.

9. The Commission adheres to its view expressed in the working paper that some statutory control is desirable and recommends that persons acting as mortgage brokers should be required to maintain trust accounts which should be subject to audit in a similar manner to that recommended by the Commission for land agents (see the Commission's *Report on a Review of the Land Agents Act*. Project No. 37, paragraphs 57 to 67).

10. The Commission is of the view that those who deal with mortgage brokers should be given some protection in the case of defalcation, and considers that ideally mortgage brokers should be required to contribute to a fidelity guarantee fund.

It would be possible to establish such a fund applicable to licensed mortgage brokers only, although the Commission appreciates that the likely number of licensees initially may be insufficient to establish a fund of a size sufficient to give adequate protection to the public.

Alternatively, a common fund could be established for both land agents and mortgage brokers. Although it might be suggested that this proposal may be inequitable due to the different functions performed by land agents and by mortgage brokers, it may be workable having regard to the fact that many land agents are also mortgage brokers. No doubt a formula

could be devised to bring both classes within the one scheme, perhaps incorporating different rates of contribution.

The Commission recommends that mortgage brokers should, if practicable, be required to contribute to a fidelity guarantee fund, either alone or in conjunction with land agents. However, if neither of the above alternatives for such a fund is practicable, then the Commission recommends that in order to protect the public against defalcation, some other system should be introduced, such as requiring mortgage brokers to take out a bond with an approved surety. The Commission understands that bonding may be more expensive for finance brokers than contribution to a fidelity guarantee fund.

(c) Licensing

11. Most commentators who favoured the introduction of statutory controls over mortgage brokers also considered that a system of licensing should be introduced. The Mortgage Brokers Association of W.A., the Law Society and the Citizens Advice Bureau all suggested that there should be a fitness test as a requirement for licensing, The Institute of Legal Executives went further and suggested an academic qualification.

The Citizens Advice Bureau said that while they considered some form of control was necessary, it was dangerous to introduce legislation so as to form a "closed shop" to anyone subsequently wishing to conduct the business of a mortgage broker.

12. Having considered these views, the Commission considers that a system of licensing is desirable to ensure that only fit and proper persons enter the business of mortgage broking, thereby reducing the likelihood of defalcations and facilitating the administration of the trust account, audit and fidelity guarantee fund provisions. The Commission therefore recommends that persons acting as mortgage brokers should be required to be licensed and that the only qualification requirement should be one of fitness.

(d) Exemptions

13. The Mortgage Brokers Association of W.A. considered that all persons acting as mortgage brokers should be licensed as such, even if already licensed pursuant to some other

statutory requirement, such as is the case with land agents (*Land Agents Act 1922*), moneylenders (*Money Lenders Act 1912*), hire purchase credit providers (*Hire Purchase Act 1959*) and dealers or investment advisers (*Securities Industry Act 1970*). The Association considered that the business of mortgage broking was a distinct function from these other activities and hence required separate statutory controls. On the other hand, most other commentators considered that certain exemptions from any statutory controls would be necessary.

14. The Commission considers that exemption from statutory controls should only apply where adequate safeguards against defalcation exist. The Commission believes that the following classes of persons should be exempted because adequate safeguards already exist with respect to them -

- (a) banks and insurance companies authorised under any law of the Commonwealth to carry on banking or insurance business;
- (b) building and friendly societies authorised to act under any law of the State;
- (c) stockbrokers who are members of an approved stock exchange under the *Securities Industry Act 1970* when dealing in securities within the meaning of that Act;
- (d) trustee companies subject to a private Act of Parliament;
- (e) certificated legal practitioners when acting in the ordinary course of their business as such; and
- (f) such other persons or classes of persons in respect of whom the Minister is satisfied that adequate safeguards already exist against loss by defalcation. The Minister should be empowered to grant an exemption under this subparagraph for such period and upon such conditions as he thinks fit.

15. It can be argued that because it is desirable to have uniformity in the scale of fees charged by all persons acting as mortgage brokers, the controls suggested by the Commission

over mortgage brokerage fees (see paragraph 26 below) should apply to all such persons, whether or not they are exempt from the other provisions of the proposed legislation.

The Commission does not favour this course. To control the fees of persons who are exempt from the other provisions of the proposed legislation may interfere with their established practices as to fees and encourage those whose fees are less than the prescribed scale to increase their charges up to the maximum permitted.

16. There is doubt as to whether the provisions of the *Land Agents Act 1922* extend to a licensed land agent when acting in the capacity of a mortgage broker (see paragraph 12 of the working paper). The Commission considers that a land agent should be required to obtain a mortgage broker's licence before he can act as a mortgage broker. As a consequence he would be required to contribute to any separate fidelity guarantee fund applying to mortgage brokers, in addition to his contribution as a land agent to the Land Agents Fidelity Guarantee Fund (see paragraph 10 above).

17. The Commission does not consider that accountants should be exempted from the proposed legislation. Although most accountants are members of and are subject to the rules of private professional associations, they are not subject to statutory controls with respect to trust accounts or audit, nor are they required to contribute to a fidelity guarantee fund.

18. The controls in the *Money Lenders Act 1912*, and the *Hire Purchase Act 1959*, in so far as they apply to persons acting as agents, do not contain any requirements for the maintenance of trust accounts and their audit, and the establishment of a fidelity guarantee fund. In these circumstances the Commission does not consider that licensed moneylenders and licensed hire purchase credit providers should be exempted from the proposed legislation.

In so far as moneylenders and hire purchase credit providers lend their own money, the proposed legislation would not apply to them.

19. The Commission also considered whether corporations exempted under s.3(f) of the *Money Lenders Act 1912*, should be exempted from the proposed legislation. The Commission has decided against such a recommendation, because the considerations to be

taken into account in granting an exemption under the *Money Lenders Act* are not necessarily the same as those applicable to the business of arranging loans as agent.

20. The Commission is aware that some mortgage brokers or their related companies borrow from and lend money to the public other than as agents, for example, where they borrow funds at fixed rates of interest for reinvestment. Such activities may presently be subject to legislative controls as follows -

- (a) the schemes of some mortgage brokers may come within the "interest" provisions of Division 5 of Part IV of the *Companies Act 1961*, and a person dealing in "interests" must also be licensed under the *Securities Industry Act 1970* - see *Corporate Affairs Commission v. M.G. Securities Australasia Ltd.* [1974] Australian Corporate Affairs Report, 27,761, Supreme Court of N.S.W.;
- (b) a mortgage broker who comes within the definition of a "money lender" in the *Money Lenders Act 1912*, is required to be licensed and is subject to other controls under that Act (see paragraph 9 of the working paper); and
- (c) a mortgage broker who makes a false or misleading statement in relation to his services may be committing an offence under the *Trade Descriptions and False Advertisements Act 1936-1973* (see paragraph 8(f) of the working paper).

It may be that additional statutory requirements are necessary to control adequately the activities of mortgage brokers borrowing and lending money other than as agents, but the Commission considers that any problems arising from any such activities are not unique to mortgage brokers and should not be controlled by legislation specifically dealing with them.

(e) Licensing and disciplinary authority

21. Both the Mortgage Brokers Association of W.A. and the Law Society considered that the Court of Petty Sessions should be the licensing authority for mortgage brokers, although the Society suggested that in the absence of objections, a Registrar of Mortgage Brokers should be able to grant renewal of licenses.

The Mortgage Brokers Association of W.A. considered that a disciplinary board for mortgage brokers should be established comprising a representative of the Crown Law Department, the Registrar of Companies and the Association.

The Law Society considered that the Court of Petty Sessions should be vested with any disciplinary functions upon referral to it by the Registrar of Mortgage Brokers.

One other commentator suggested that the Registrar of Companies should be the licensing and disciplinary authority for mortgage brokers, while another commentator suggested that these functions should be performed by the same authority as for land agents.

22. The Commission recommends that a supervising authority for mortgage brokers be established. It should comprise the members for the time being of the proposed supervising authority for land agents (see the *Report on a Review of the Land Agents Act*, Project No. 37, paragraphs 9-11), except that a licensed mortgage broker, appointed by the Governor, should take the place of the two land agent members. The proposed supervising authority for mortgage brokers would therefore comprise -

- a legal practitioner as chairman, with a minimum of eight years practice;
- an accountant/auditor;
- a licensed mortgage broker; and
- one other person.

If a common fidelity guarantee fund is established for land agents and mortgage brokers (see paragraph 10 above), it would be desirable in addition to retain one land agent member on the authority, preferably the land agent member elected by the general body of licensed land agents.

23. When dealing with the proposed supervising authority for land agents in the Commission's *Report on a Review of the Land Agent Act* (Project No. 37 paragraphs 14 to 22) there was a divergence of views among the members as to whether the licensing and disciplinary functions should be dealt with by the proposed authority in all cases (the majority view) or only in the absence of objections and otherwise by a court (the minority view). The member of the Commission who took the minority view in that project is of the same view

with respect to mortgage brokers. The other two members of the Commission consider that licensing and disciplinary functions with respect to mortgage brokers would be best performed by the proposed supervising authority in all cases.

The Commission is, however, unanimous that if either of these views is adopted, the functions and powers of the proposed supervising authority for mortgage brokers should be similar to those for land agents.

(f) Written appointment

24. The Mortgage Brokers Association of W.A. and all others who commented on the question as to whether a written appointment of a mortgage broker should be a prerequisite to payment for their services (see paragraph 23(f) of the working paper) agreed that such a prerequisite was desirable.

The Commission agrees with this view. It suggests that for purposes of uniformity, any such requirement should be the same as is adopted for land agents. It therefore recommends that before a mortgage broker can recover or retain his fees, his appointment should be in writing although not necessarily before the performance of his services (see paragraph 42 of the *Report on the Review of the Land Agents Act*). The Commission appreciates that this may cause difficulty in some areas of mortgage broking particularly in respect of short term loans, but considers that a written appointment is desirable to prevent possible abuses.

(g) Fees

25. Several commentators considered that the fees charged by mortgage brokers should be controlled. The Law society suggested that this should be done by regulations made by the Governor in Council, while the Institute of Legal Executives considered that they should be controlled by the Land Agents Supervisory Committee. The Mortgage Brokers Association of W.A. suggested that the fees should be prescribed by their Association, although the Citizens Advice Bureau opposed this.

26. The Commission considers that the maximum fees charged by mortgage brokers should be controlled, and recommends control in a similar manner to that proposed for land

agents, that is, the power to prescribe fees should be given to the proposed supervising authority for mortgage brokers, subject to disallowance by Parliament (see paragraph 44 of the *Report on Review of the Land Agents Act*).

The Commission also recommends that it should be an offence -

- (a) for a person to charge a fee in respect of a mortgage broking transaction unless he is licensed as a mortgage broker or is exempt from licensing; and
- (b) for a licensed mortgage broker to charge more than the maximum prescribed fee.

(h) Advertising and canvassing

27. In answer to the question whether advertising and canvassing by mortgage brokers should be controlled (see paragraph 23(i) of the working paper), the Mortgage Brokers Association of W.A. suggested that mortgage brokers should be required to state their name, street address and the telephone number of their business in any advertisement. The Law Society did not see a need for statutory control of advertising by mortgage brokers.

Since the issue of the working paper, the Commission has been informed of statutory changes in two States of Australia that are, amongst other things, designed to control advertising and canvassing by mortgage brokers (N.S.W. *Money-lenders and Infants Loans (Amendment) Act* No. 85 of 1973, Victorian *Money Lenders (Advertisements) Act* No. 8454 of 1973). Both Acts regulate the information that may be contained in advertisements by mortgage brokers, including a requirement that where an interest rate is mentioned it must be expressed in terms of the formula contained in the principal Act.

28. The Commission is of the view that advertisements by a person acting as a mortgage broker should be sufficiently specific to enable a reader to identify the broker concerned, in the same way as has been recommended for land agents, and recommends accordingly (see paragraph 41 of the *Report on a Review of the Land Agents Act*).

The Commission also recommends that it should be an offence to mention an interest rate in any such advertisement unless it is expressed at a rate calculated in accordance with a uniform formula. Formula that might be considered for adoption are contained in the Schedule to the *Money Lenders Act 1912* and the Fifth Schedule to the *Hire Purchase Act 1959*, as amended in 1973. However any breach of such a provision by a broker should not result in the avoidance by a borrower of any contract entered into by a lender as a consequence of such an advertisement.

29. The Commission considers that there is no need to, have separate statutory provisions dealing with false and misleading advertisements by mortgage brokers, as there is already a general offence for making such advertisements in s.8 of the *Trade Descriptions and False Advertisements Act 1936* (see paragraph 20(c) above and see also the *Commonwealth Trade Practices Act 1974*, Part V). The Commission does, however, recommend that it should be an offence for a person to hold himself out by way of advertisement or otherwise as being in the business of a mortgage broker if he is not licensed as such.

30. The Commission is not aware of any malpractices which would require statutory provisions controlling canvassing (other than by way of advertisement) by persons acting as mortgage brokers. If any problem did arise in this regard, it could be dealt with by an appropriate enactment at that time.

SUMMARY OF RECOMMENDATIONS

The Commission recommends that persons acting as mortgage brokers, that is, those who in the course of their business as agents negotiate or arrange loans of money for or on behalf of other persons for reward, should be subject to statutory control. The form such control should take is set out in the following summary -

- (1) Persons acting as mortgage brokers should be required to maintain trust accounts which should be subject to audit in a similar manner to that recommended by the Commission for land agents.

(see paragraph 9 above)

- (2) If practicable, mortgage brokers should be required to contribute to a fidelity guarantee fund either alone or in conjunction with land agents. If neither of these alternative is practicable, some other system should be introduced, such as requiring mortgage brokers to take out a bond with an approved surety.

(see paragraph 10 above)

- (3) Persons acting as mortgage brokers should be required to be licensed and the only qualification requirement should be one of fitness.

(see paragraph 12 above)

- (4) The following persons should be exempt from all the provisions of the proposed legislation-

- (a) banks and insurance companies authorised under any law of the Commonwealth to carry on banking or insurance business;
- (b) building and friendly societies authorised to act under any law of the state;
- (c) stockbrokers who are members of an approved stock exchange under the *Securities Industry Act 1970* when dealing in securities within the meaning of that Act;

- (d) trustee companies;
- (e) certificated legal practitioners when acting in the ordinary course of their business as such; and
- (f) such other persons or classes of persons in at respect of whom the Minister is satisfied that adequate safeguards already exist against loss by defalcation. The Minister should be empowered to grant an exemption for such period and upon such conditions as he thinks fit.

(see paragraph 14 above)

- (5) A supervising authority for mortgage brokers should be established, comprising the members for the time being of the proposed supervising authority for land agents, except that a licensed mortgage broker, appointed by the Governor, should take the place of the two land agent members.

If a common fidelity guarantee fund is established for land agents and mortgage brokers, it would be desirable in addition to retain one land agent member on the proposed supervising authority for mortgage brokers, preferably the land agent member elected by the general body of licensed land agents.

(see paragraph 22 above)

- (6) The functions and powers of the proposed supervising authority for mortgage brokers should be similar to those for land agents.

(see paragraph 23 above)

- (7) Before a mortgage broker can recover or retain his fees, his appointment should be in writing.

(see paragraph 24 above)

- (8) The fees charged by mortgage brokers should be prescribed by the proposed supervising authority for mortgage brokers, subject to disallowance by Parliament.

(see paragraph 26 above)

(9) It should be an offence -

- (a) for a person to charge a fee in respect of a mortgage broking transaction unless he is licensed as a mortgage broker or is exempt from licensing; and
- (b) for a licensed mortgage broker to charge more than the maximum prescribed fee.

(see paragraph 26 above)

(10) Advertisements by persons acting as mortgage brokers should be required to be sufficiently specific to enable the reader to identify the broker concerned.

(see paragraph 28 above)

(11) It should be an offence to mention an interest rate in any advertisement by a mortgage broker unless it is expressed at a rate calculated in accordance with a uniform formula. However any breach of such provision by a broker should not result in the avoidance by a borrower of a contract with a lender entered into as a consequence of such an advertisement.

(see paragraph 28 above)

(12) It should be an offence for a person to hold himself out by means of advertisement or otherwise as being in the business of a mortgage broker if he is not licensed as such.

(see paragraph 29 above)

E.G. Freeman
Chairman

B.W. Rowland
Member

R.W. Harding
Member

20 September 1974

APPENDIX I

List of persons who commented on the working paper

Associated Banks in W.A.

Australian Finance Conference

Citizens Advice Bureau of W.A. Inc.

Deputy Registrar (Legal), Companies Office

G.W. Sansom Pty. Ltd. (mortgage brokers)

Institute of Legal Executives (Western Australia) (Incorporated)

Morgan Priddy & Keogh (chartered accountants)

Mortgage Brokers Association of W.A.

Stock Exchange of Perth Limited

The Law Society of Western Australia Inc.

Vine, K.J.