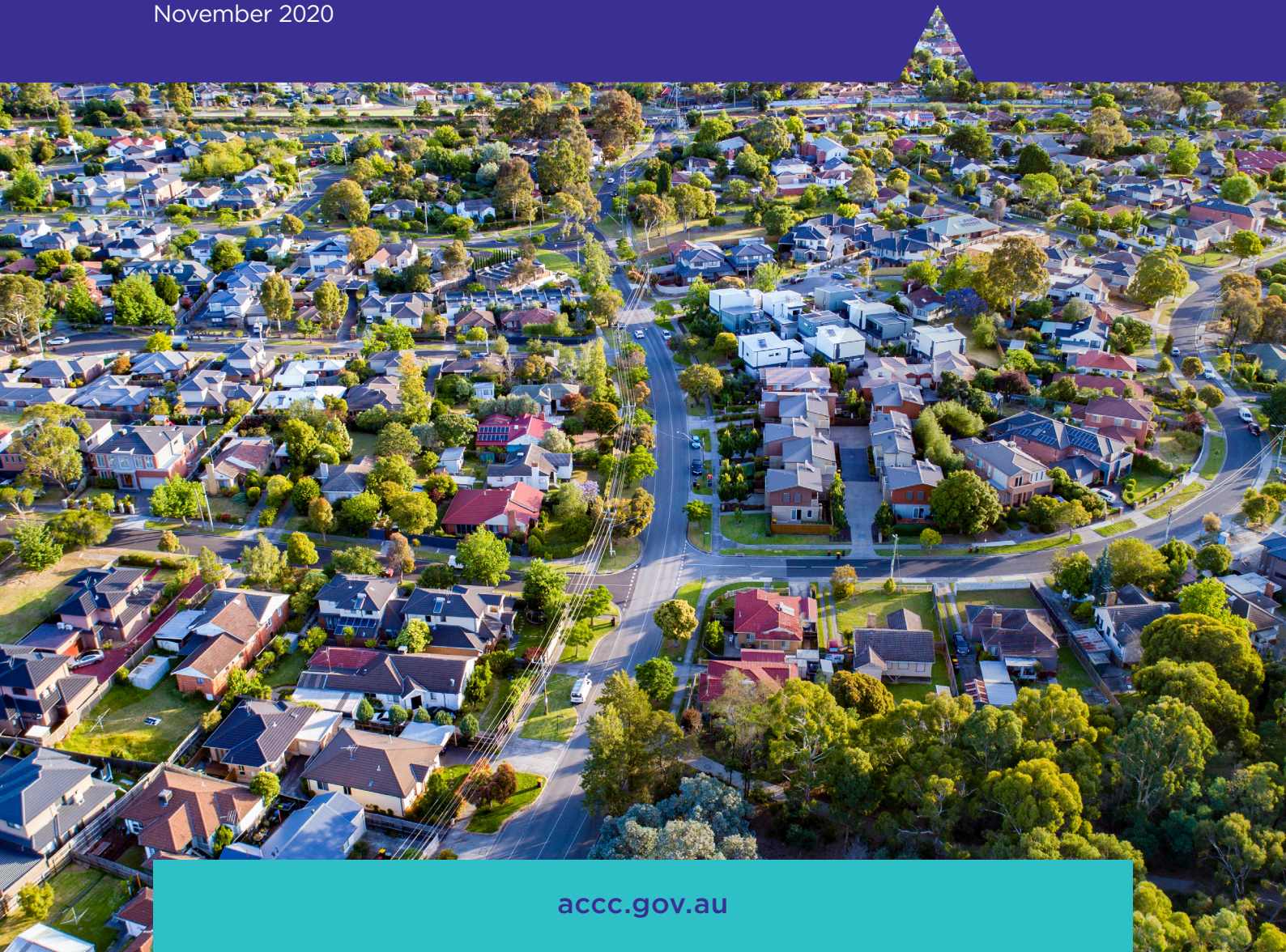




Home loan price inquiry

Final report

November 2020



Australian Competition and Consumer Commission
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Abbreviations and glossary

ACCC	Australian Competition and Consumer Commission
ADI	Authorised deposit-taking institution
ANZ	Australia and New Zealand Banking Group Limited
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
Basic home loan	Home loan products offered without the add-on features available under a standard home loan (defined below).
Basis points or bps	A unit of measure for interest rates. 1 basis point equals 0.01%.
Big four banks	ANZ, CBA, NAB and Westpac.
Cash rate	The interest rate that banks pay to borrow funds from each other in the money market on an overnight basis. The cash rate is calculated as the weighted average interest rate on overnight unsecured loans between banks settled in the Reserve Bank Information and Transfer System.
CBA	Commonwealth Bank of Australia
Consumer Data Right	<p>A digital automation process enabling customers to safely share their data with trusted service providers.</p> <p>In banking, this allows customers to choose to share their existing banking data (for example, their transaction history, interest rate, recurring direct debits and account balances) with a prospective lender or accredited finance-related app or website.</p>
Council of Financial Regulators	<p>The Council of Financial Regulators is the coordinating body for Australia's main financial regulatory agencies, which aims to contribute to the efficiency and effectiveness of financial regulation and promote financial stability.</p> <p>There are four members of the Council of Financial Regulators: the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC), the Reserve Bank of Australia (RBA) and The Treasury.</p>
Discharge Authority form or discharge form	The Discharge Authority form, or discharge form, is a form that lenders require borrowers to complete when they are switching their home loan to a different lender, selling a property, or have fully repaid their home loan, among other reasons.
Discount	A reduction off the headline variable rate. The interest rate paid by the home loan borrower is usually expressed as the headline variable rate (less any discounts granted by the lender). There are two main types of discounts. The first type of discount is those publicly advertised by lenders. The second type of discount is those offered at the lender's discretion on a case-by-case basis to individual borrowers.
Fixed rate home loan	A home loan where the interest rate is set and does not vary over a time period agreed with the borrower and set out in the loan contract (the fixed rate period).

Headline variable rate	The reference rate on which the variable interest rate paid by both new and existing variable rate home loan borrowers is based.
Home loan or residential mortgage product	A loan secured by a mortgage over one or more residential premises.
Loan to value ratio	The amount of a home loan expressed as a percentage of the value of the property being used as security for the home loan.
Macquarie Bank	Macquarie Bank Limited
Mortgage broker	An intermediary between a borrower and lenders. A mortgage broker facilitates access to a range of home loan products from different lenders.
NAB	National Australia Bank Limited
New Payments Platform (NPP)	The NPP is a new payment system infrastructure designed primarily for retail payments, which allows institutions to make funds available in recipients' accounts immediately without settlement or credit risk.
Package	An arrangement under which a customer is eligible for discounts and/or other benefits on a specified range of a lender's products such as transaction accounts, credit cards and home loans. To be eligible for a package a customer may need to maintain specific products with the lender and, in some cases, pay an annual fee.
Price monitoring period	1 January 2019 to 31 December 2019.
Price reduction	Any reduction (borrower-initiated or lender-initiated) in the interest rate or recurring fees granted to an individual borrower after a home loan has been established, other than via a reduction in headline variable rates, and excludes any reductions arising from the borrower switching product or repayment type.
RBA	Reserve Bank of Australia
Standard home loan	Home loan products supplied with a range of add on features. In general these home loan products can, but need not, be taken as part of a package.
Variable rate home loan	A home loan that has an interest rate that can fluctuate over the period of the loan. The interest rate can be changed at any time at the lender's discretion by altering the relevant headline variable rate.
Westpac or WBC	Westpac Banking Corporation

Overview

On 14 October 2019, the Treasurer directed the Australian Competition and Consumer Commission (ACCC) to conduct an inquiry into home loan pricing. The direction required the ACCC to consider two issues:

1. prices charged for home loans since 1 January 2019
2. impediments to borrowers switching to alternative lenders.

Our interim report, published in April 2020, focused on the first issue. It considered prices charged for home loans during the period 1 January 2019 to 31 October 2019. This final report focuses on identifying cost effective recommendations to address specific impediments to borrowers switching lenders.

This report has been completed at a time when there are reforms underway which should assist borrowers in switching between lenders or home loan products. These reforms include the Consumer Data Right, which will help borrowers compare the offers of different lenders and switch.

Within this changing environment, we have targeted our recommendations at impediments likely to persist in the process for switching lenders.

Switching lenders

Switching lenders occurs when a borrower repays their home loan with one lender (the previous lender) using the proceeds of a new home loan obtained from a different lender (the new lender). Switching a home loan from one lender to another is more complex than switching between suppliers of many other products and services. There are over 100 home loan lenders in Australia offering a combined total of nearly 4,000 different home loan products.¹ Switching lenders is also a lengthy process that can take many weeks, or sometimes months, to complete.

We consider that, from the borrower's perspective, the process of switching to a new lender can be broadly categorised into three stages:

- deciding to engage in the home loan market to look for a better offer
- obtaining information on and comparing the offers of different lenders (sometimes referred to as 'shopping around')
- taking action by selecting a new lender and undertaking the steps in the home loan switching process (see figure 1.1).

At each stage in the switching process detailed above, borrowers face challenges or frictions. Our recommendations aim to reduce or remove some of these impediments.

1 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, <https://www.pc.gov.au/inquiries/completed/financial-system/report/financial-system.pdf>, p. 12.

Switching supports competition in the home loan market

Home loan prices have a significant impact on household budgets. For households with a home loan, repayments on that loan are often their largest ongoing expense.² While borrowers incur fees and charges, and must invest time and effort, to switch lenders, the potential gains from switching can be significant. As reported in the interim report and the Residential mortgage price inquiry, the difference in prices paid for new and existing home loans demonstrates that many borrowers could achieve significant savings by switching lenders, or negotiating with their existing lender to receive an interest rate similar to that on offer for new loans.³

In addition to savings for individual borrowers, increased switching in the home loan market could generate demand-side pressure on lenders. Demand-side pressure encourages lenders to innovate and offer better products and lower prices to attract and retain borrowers.

Increased switching could also benefit those borrowers who do not switch. A credible threat of switching can be enough for lenders to improve their product offerings, including by lowering prices, so that their borrowers do not switch, or consider switching, to a different lender.

Evidence of impediments to switching lenders

Since at least 2015, there has been a difference in interest rates paid on new and existing home loans. The gap in interest rates paid on new and existing home loans would not have persisted over time if there were not material impediments to switching. That is because borrowers with existing home loans would seek out, and switch to, a home loan with an interest rate closer to that being paid on newer home loans, and lenders would offer lower interest rates to their borrowers with existing home loans in order to retain those loans.

While there has been a significant increase in the value of home loans being switched between lenders during the first half of 2020, we consider this is likely due to a number of unique circumstances, many of them brought about by the COVID-19 pandemic and unlikely to continue over the longer term. Given the importance of home loan prices to household budgets and the significant benefits to many borrowers of switching, we consider that the recommendations proposed in this report are necessary. Further, these recommendations will support and complement the Consumer Data Right, which will assist borrowers in comparing and switching lenders or home loan products.

2 Based on the most recent census data (2016), more than 2.85 million Australian households (35% of all households) owned a house with a home loan. For these households the median monthly home loan repayment was \$1,755 (or \$21,060 annually) in 2016. Further, based on ABS data, current housing costs were the largest household expense in the 12 months to June 2016, accounting for 20% of household spending. Current housing costs include spending on rent, interest payments on mortgages, rates, home and content insurance and repairs and maintenance. They do not include principal repayments on home loans. Sources: Australian Bureau of Statistics, *2016 Census Quickstats*, Australia, https://quickstats.censusdata.abs.gov.au/census_services/getproduct/census/2016/quickstat/036?opendocument, viewed 3 September 2020. Australian Bureau of Statistics, *6530.0—Household Expenditure Survey, Australia: Summary of Results 2015–16*, September 2017, <https://www.abs.gov.au/statistics/economy/finance/household-expenditure-survey-australia-summary-results/latest-release>, viewed 3 September 2020.

3 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 8. Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, p. 9.

Reducing and removing impediments to switching lenders

Prompting borrowers with older loans to engage in the home loan market

A significant number of borrowers have not switched lenders for several years. As at December 2019, almost half of all variable rate loans were originated at least four years ago.⁴

As borrowers' loans get older, the gap between what they pay and what borrowers with new loans pay widens. For example, as at September 2020:

- borrowers with home loans between three and five years old were, on average, paying around 58 basis points above the average interest rate for new loans
- borrowers with home loans between five and 10 years old were, on average, paying around 71 basis points above the average interest rate for new loans
- borrowers with home loans greater than 10 years old were, on average, paying around 104 basis points above the average interest rate for new loans (see figure 1).⁵

As is evident from figure 1, the significant majority of interest rates paid on older home loans are higher, and in many cases materially higher, than the average interest rate paid on new loans, which is a trend we have observed since 2015. Many of those borrowers with older home loans could achieve significant savings if they switched to a new home loan. For example, if a borrower with a home loan of around \$250,000 switched to a home loan with an interest rate 58 basis points lower than their existing loan, they would save over \$1,400 in interest in the first year. Over the remaining term of the loan that borrower would save over \$17,000 in interest in net present value terms.⁶

4 Loans in the Reserve Bank of Australia's Securitisation Dataset. Reserve Bank of Australia, 'Box C: Do Borrowers with Older Mortgages Pay Higher Interest Rates?' *Statement on Monetary Policy*, February 2020, p. 55.

5 As at September 2020, borrowers whose variable rate owner-occupier loan with principal and interest repayments was between three and five years old were paying an average interest rate of 3.20%, compared to the average interest rate for new owner-occupier home loans with principal and interest repayments, which includes fixed and variable rate home loans, which was 2.62%.

As at September 2020, borrowers whose variable rate owner-occupier loan with principal and interest repayments was between five and ten years old were paying an average interest rate of 3.33%, compared to the average interest rate for new owner-occupier home loans with principal and interest repayments, which includes fixed and variable rate home loans, which was 2.62%.

As at September 2020, borrowers whose variable rate owner-occupier loan with principal and interest repayments was greater than 10 years old were paying an average interest rate of 3.66%, compared to the average rate for new owner-occupier home loans with principal and interest repayments, which includes fixed and variable rate home loans, which was 2.62%.

The average interest rate for new loans is a weighted average for new loans funded in the relevant month based on the Economic and Financial Statistics data collection, which accounts for around 95% of total housing credit outstanding.

Source:

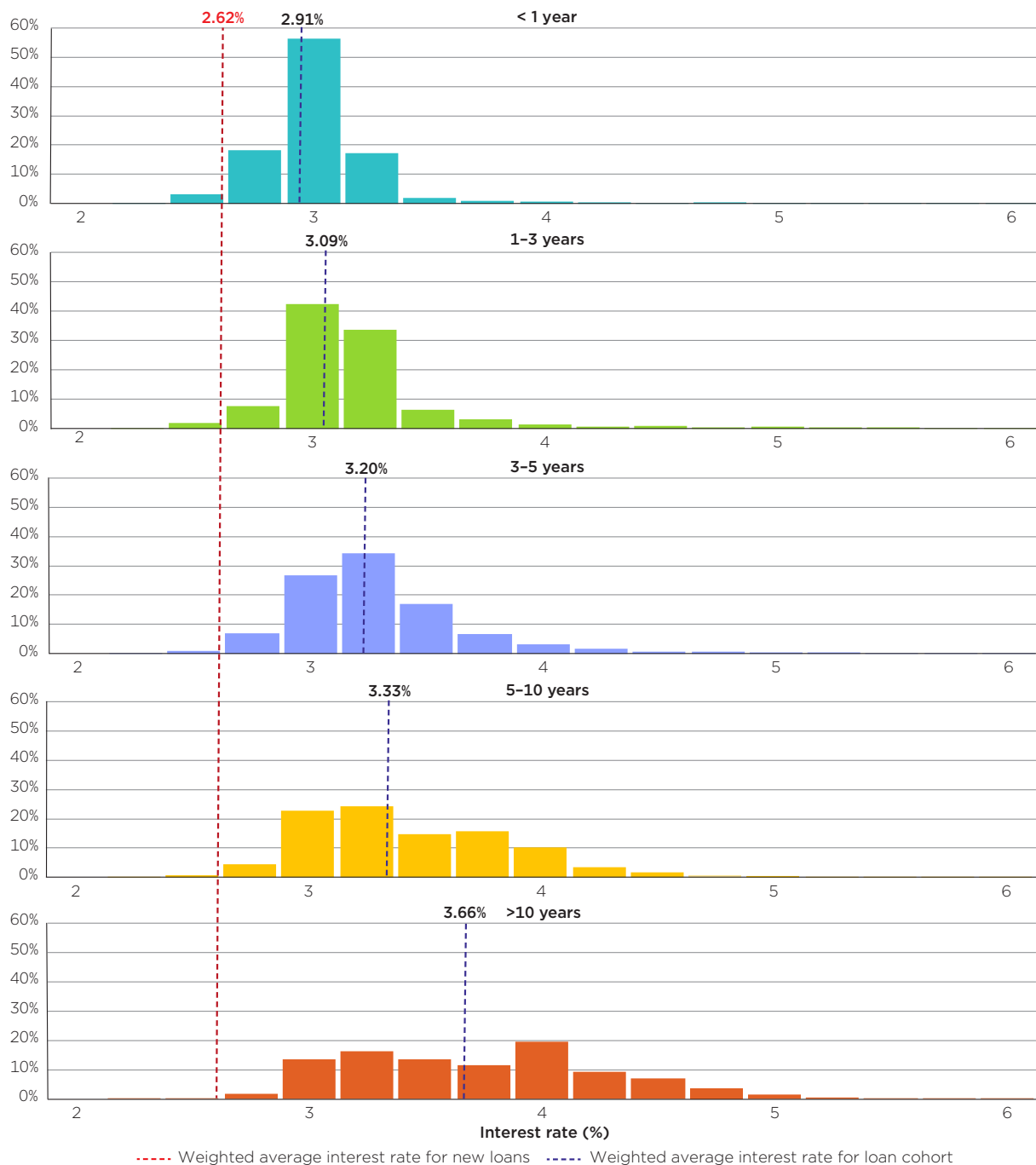
Reserve Bank of Australia, Securitisation Dataset.

Reserve Bank of Australia, Statistical Table F6—Housing Lending Rates, <https://www.rba.gov.au/statistics/interest-rates/>, viewed 6 November 2020.

6 These estimates are based on:

- a (nominal) interest rate for the net present value calculation of 3.20%, which is the weighted average interest rate paid on variable rate owner-occupier loans with principal and interest repayments between three and five years old across all lenders in the Reserve Bank of Australia's Securitisation Dataset as at September 2020
- a remaining term of 25 years.

Figure 1: Distribution of interest rates* on variable rate owner-occupier loans with principal and interest repayments, by loan tenure, September 2020



Note: The proportion of home loans in each interest rate bucket is based on the balance of securitised loans that are eligible as collateral in the Reserve Bank of Australia (RBA)'s domestic market operations. Data from the Securitisation Dataset represents variable rate loans only, whereas the average rate for new loans represents both fixed and variable rate home loans.

The Securitisation Dataset contains data on 2.4 million individual home loans with a combined value of around \$668 billion, or around one-third of the total value of outstanding home loans in Australia. The RBA considers the Securitisation Dataset is reasonably representative of average interest rates in the home loan market. However, the Securitisation Dataset may not be representative of the home loan interest rates in the portfolios of individual lenders. This is because the securitised loans represent only a portion of lenders' portfolios and the type of loans that are securitised may be influenced by (among other things) the way credit ratings agencies assign ratings, the type of lender, investor preferences, and the RBA's repo-eligibility framework.

For more information on the RBA's Securitisation Dataset see: Reserve Bank of Australia, 'The Reserve Bank's Securitisation Dataset', *Bulletin—December 2018*, December 2018.

Source: Reserve Bank of Australia, *Securitisation Dataset*.

Reserve Bank of Australia, Statistical Table F6—Housing Lending Rates, <https://www.rba.gov.au/statistics/interest-rates/>, viewed 6 November 2020.

The fact that many borrowers with older home loans continue to pay interest rates significantly higher than those available on new loans, indicates a lack of engagement in the home loan market among this cohort. If these borrowers were regularly engaging in the home loan market and aware of the significant savings available on new loans, we would expect there to be fewer loans with interest rates significantly higher than the average interest rate for new loans. Instead, many of these borrowers would have switched lenders or home loan products, or asked their existing lender for a price similar to those available for new loans.⁷

The proportion of borrowers who stand to benefit from switching (see figure 1) significantly exceeds the proportion of borrowers who say they intend to switch. For example, survey data held by two of the big four banks shows that over the period September 2014 to September 2019, fewer than one in five borrowers intended to refinance (with their existing lender) or switch their home loan (to a new lender) within the next 12 months.⁸

Deciding to engage in the market to look for a better offer is the first stage of the switching process. As such, a lack of engagement in the home loan market is a significant barrier to borrowers switching lenders. We consider two significant reasons for this lack of engagement to be:

- many borrowers presume that they '*probably won't save much*' by switching lenders⁹
- once a home loan is established, many borrowers are not compelled to consider switching unless they experience a major change in circumstance (for example, moving house). Outside these major changes, many borrowers are not prompted to consider whether they could benefit from switching lenders.¹⁰

To address these issues and encourage borrowers with older home loans, who are generally paying significantly more than borrowers with new loans, to engage in the home loan market, we recommend that lenders provide an annual prompt to their variable rate borrowers with loans greater than three years old (recommendation 1). The prompt should bring the potential benefits of switching to the borrower's attention in a compelling and personalised way. The optimal design of the prompt should be determined through consumer testing and trials.

We recommend that the prompt include a comparison between a borrower's current interest rate and the average interest rate paid by borrowers with similar new home loans across the market. For most borrowers with home loans older than three years, this information would clearly convey that it is worthwhile for them to look for a better home loan offer (see figure 1). Providing the average rate paid for similar new loans will also assist borrowers with looking for a new loan, as they will have a benchmark against which to compare alternative home loan offers.

To further enhance the prompt, it could also include an estimate of the potential interest savings as a dollar figure. For example, it could state what the borrower could potentially save over the first year if they switched to a loan with the average interest rate for new loans, or if their existing interest rate was reduced by 25 basis points. We consider that potential dollar savings over the first year is useful information to help a borrower decide whether it is worthwhile for them, given the costs of taking action (e.g. search and switching costs, such as discharge fees), to engage in the home loan market to see if they could benefit from switching.

Finally, we recommend that the prompt set out the next steps for borrowers to look for a better offer, to give them the confidence to engage in the home loan market to see if they could benefit from switching.

7 We acknowledge that not all borrowers will choose to or be able to switch lenders or home loan products (see chapter 1).

8 The survey question was '*How likely would you be to refinance your mortgage in the next 12 months?*' The share of borrowers reported represents borrowers who said they were '*highly likely*' to do so (8–10 on a scale of 10). For each tranche of the survey from September 2014 to September 2019 there were at least 2,000 respondents. The survey for September 2019 was completed by 2,001 borrowers and was said to be nationally representative by age, gender and location of the respondents.

9 BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, <https://www.customerownedbanking.asn.au/images/stories/media-releases/2017/20170214%20Blackmarket%20Research%20Banking%20Competition%20and%20Switching.pdf>, p. 8.

10 See also: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 163.

Comparing offers

Borrowers who decide to look for a better offer may be deterred from completing their search or may only complete a narrow search because of unnecessarily high search costs created by some lenders' opaque discretionary discounting. In both our Residential mortgage price inquiry and the interim report, we found that borrowers often lack access to transparent and easily understood pricing information about home loans, and that this is primarily caused by the presence of opaque discretionary discounts.¹¹ Discretionary discounts are offered on a case-by-case basis to individual customers, usually after the lender has assessed their application. These discounts also create information asymmetry between lenders and borrowers, as borrowers are not aware of lenders' criteria for discretionary discounts or prices actually paid for new loans.

The potential harm to borrowers from opaque pricing remains a concern for the ACCC. However, between 1 January 2019 and 31 December 2019, we observed two of the big four banks reducing or considering reducing their reliance on discretionary discounting to provide more price transparency to borrowers. A number of lenders, including non-big four banks and non-ADI lenders, also do not offer, or are less reliant on, discretionary discounts.

The move towards greater price transparency has occurred without direct regulatory intervention. Rather, these developments have been primarily motivated by demand-side and other competitive pressures, with these lenders seeking to:

- simplify discounts to benefit the borrower experience
- increase their new lending volume
- adopt pricing structures similar to those that are offered by other lenders.

We consider that these moves towards more transparent pricing, and the existence of demand-side and other competitive pressures, will likely encourage further price transparency from other lenders.

The recommended prompt (recommendation 1) will help reduce some of the search costs and information asymmetry present in the market. By providing variable rate borrowers with the average rate paid for similar new loans, taking into account discretionary discounts, these borrowers will have a benchmark against which to assess their existing loan or other offers.

There are a number of other developments that should also improve price transparency and reduce search costs, including:

- The Consumer Data Right, which will give borrowers the ability to consent to their ADI sharing the data that is held about them with trusted and accredited third parties (data recipients) of their choice.
- The ACCC is also encouraging lenders to display links to key fact sheet calculators clearly and prominently on each webpage where a home loan is advertised, with explanatory text. This may reduce the time and effort required for a borrower to compare the cost of home loans and encourage more transparent pricing.

While we are observing momentum towards greater price transparency, if, in the course of our continued monitoring of competition and prices in the home loan market (recommendation 4), the ACCC observes this momentum stalling and a resurgence of reliance on opaque discretionary discounts, we will consider making recommendations to Government to reduce the resulting consumer harm.

¹¹ Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 8-9.
Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, p. 18.
Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, pp. 7, 21-22.

Making the switch

Once a borrower has compared home loan offers and decided to switch lenders, they need to discharge their home loan from their existing lender. The discharge process should be clear, quick and simple to follow.

The majority of stakeholders the ACCC consulted with raised concerns that the discharge process of many lenders is unnecessarily difficult and lengthy for borrowers.

Commonly reported pain points in the discharge process included:

- unclear and/or complicated steps for borrowers, including Discharge Authority forms that are difficult to access and complete, or administrative hurdles such as lenders requiring in-person contact before processing a discharge request
- uncertainty about how long the discharge process will take and unnecessary delays in the process (including through the use of retention strategies by existing lenders).

We consider that borrowers are less likely to start or complete a switch to a new lender if the process is frustrating or confusing, even if switching would result in a better home loan.

Existing lenders want to retain their borrowers, and are therefore not incentivised to remove pain points from the discharge process (or may even be incentivised to create them). However, pain points in the discharge process impede switching and result in costs to market participants more generally, including lenders, mortgage brokers and borrowers. We consider intervention to remove inefficiencies in the discharge process would result in better outcomes for borrowers and competition. We make two recommendations that we consider would streamline the discharge process and allow borrowers to make better switching decisions that are less affected by pain points in the process:

- Lenders should be required to provide a standardised Discharge Authority form to borrowers, which is easy to access, fill out and submit (recommendation 2).
- Lenders should be subject to a maximum time limit of 10 business days to complete the discharge process, as defined in chapter 4 (recommendation 3).

Continued monitoring of prices and competition in the home loan market

The ACCC's two inquiries into the home loan market have shed light on a range of practices by lenders that detract from price competition in the home loan market and adversely affect consumers. We have recommended interventions to address the consumer harm caused by some of these practices. However, we consider that ongoing monitoring of prices and competition in the home loan market is also warranted given the importance of the home loan market to the Australian economy and the impact of home loan pricing on household budgets (recommendation 4).

The ongoing monitoring of prices and competition in the home loan market is needed to:

- enable the ACCC to continue to provide transparency to the Australian Government and consumers on lenders' pricing practices
- monitor the impact of government initiatives and regulatory reform, including the Consumer Data Right and the recommendations in this report, on home loan prices
- identify persistent or emerging issues that impede price competition.

Where appropriate, the ACCC will make recommendations to remedy these issues and improve competition and consumer outcomes in the home loan market.

Recommendations

► Recommendation 1: A prompt for variable rate borrowers

All lenders should be required to provide borrowers with variable rate loans originated three or more years ago with an annual prompt to encourage borrowers to engage in the home loan market to see if they could benefit from switching lenders or home loan products.

The prompt should:

- be provided directly to borrowers
- communicate the potential benefits of switching in a compelling and personalised way, including a comparison between the borrower's current interest rate and the average interest rate paid for new loans similar to the borrower's loan
- set out the next steps for borrowers to look for a better home loan offer.

Consumer testing and trials should be undertaken to determine the optimal design of the prompt.

► Recommendation 2: A standardised Discharge Authority form

All lenders should be required to provide a standardised Discharge Authority form to borrowers to complete. The form should be easy to access, fill out and submit.

Lenders should adopt an identical standard form template, rather than agreeing to common criteria and continuing to design their own forms, which would still potentially allow them to add fields or make forms unnecessarily complex. The form should only request details from the borrower that are necessary for their discharge request to be processed.

The design and implementation of the form will require further consultation with industry and regulators.

► Recommendation 3: A maximum timeframe for existing lenders to process discharge requests

All lenders should be subject to a maximum time limit of 10 business days to complete the discharge process.

The time limit should cover the period from when the borrower (or a third party acting on their behalf) submits the Discharge Authority form to when the existing lender is ready to begin the settlement process.

While stakeholder consultation has indicated that 10 business days is an appropriate time period for processing discharge requests, further stakeholder consultation will be required on the appropriate time limit, as well as factors including:

- the specific definition of the start and end points in the discharge process to which the time limit should apply
- exemptions to the time limit to account for circumstances in which the existing lender cannot meet the time limit due to factors outside their control.

► Recommendation 4: Continued monitoring of competition and prices in the home loan market

The ACCC should continue to inquire into and monitor competition and pricing in the home loan market, under government direction.

In undertaking this role the ACCC should consider the following matters:

- the difference between prices paid on new and existing home loans
- the difference between the prices advertised for home loans and the prices borrowers actually pay
- the prices charged by, and pricing decisions of, lenders
- the impact of current and future government initiatives and regulatory interventions, including the Consumer Data Right and the recommendations in the Home loan price inquiry final report, on home loan prices, including interest rates, fees and charges
- other emerging issues and lender practices that impede competition or outcomes for consumers that arise during the inquiry period.

The inquiry should focus on the 10 largest lenders in the home loan market and consider other lenders or groups of lenders (such as non-ADIs) as competition issues are identified that involve or impact those lenders.

The ACCC should report to the Treasurer annually over a five year period, providing its first report to the Treasurer by 30 September 2022.

► Action to be taken by the ACCC

We consider that moves by lenders towards more transparent pricing, and continuing competitive and other pressures that are encouraging increased price transparency, mean that further regulatory intervention is not required at this stage.

However, if the ACCC observes through its monitoring under recommendation 4 that momentum towards price transparency has stalled, or if we observe consumer harm associated with a lack of price transparency, we will consider making recommendations to the Government to address this.

Introduction

On 14 October 2019, the Treasurer directed the ACCC to conduct an inquiry into home loan pricing (the inquiry). A copy of the Direction is at Appendix A.

The Direction required the ACCC to consider two issues:

- prices charged for home loans since 1 January 2019, in particular:
 - the difference between advertised interest rates and interest rates paid by borrowers
 - the difference between interest rates paid by borrowers with new loans and borrowers with existing loans
 - lenders' pricing decisions following changes in the Reserve Bank of Australia (RBA)'s target for the cash rate, including why lenders reduced their headline variable rates by as much as they did and how lenders' cost of funds affected these decisions
- impediments to borrowers switching to alternative lenders, in particular:
 - lender practices that create impediments to switching, including product features and bundling
 - consumer behaviour, including decision making, biases and choices
 - the availability of information about prices actually charged for home loans.

The Direction provided that the inquiry should not extend to the conduct of mortgage brokers, the Australian Prudential Regulation Authority (APRA) or the Australian Securities and Investments Commission (ASIC).

The interim report, published in April 2020, focused on the first issue. It considered prices charged for home loans during the period 1 January 2019 to 31 October 2019.

This final report considers the second issue: impediments to switching.

The focus of the final report

This report does not seek to identify and address all impediments to borrowers switching lenders. Rather, following consultation with a range of stakeholders to identify impediments to switching, and building on findings from the interim report, the Residential mortgage price inquiry and the Productivity Commission's inquiry into Competition in the Australian Financial System,¹² the report focuses on identifying cost effective recommendations aimed at addressing specific impediments to switching. Increased switching will enhance competition in the home loan market and improve outcomes for borrowers.

The Ministerial Direction for the inquiry required the ACCC to consider whether product bundling, including through the use of packages, creates an impediment to home loan switching. In relation to home loans, the most common form of product bundling is a home loan package. A home loan package is an arrangement under which a borrower is eligible for discounts and/or other benefits on a specified range of a lender's products such as transaction accounts, credit cards and home loans. To be eligible for a package a borrower may need to maintain specific products with the lender and, in some cases, pay an annual fee.

The inconvenience and search costs associated with switching a home loan that is part of a package may act as an impediment to switching for some borrowers. However, our view is that the relatively low cost of transaction accounts and credit cards,¹³ and the expected implementation of initiatives that will make it easier for consumers to transfer their direct debits and recurring payments to another financial institution, and to compare the individual products in a package, can help to address the inconvenience and search costs (see box 1).

¹² Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018.

¹³ Assuming the full balance of the credit card is repaid each billing cycle.

Given this, we have not focused on product bundling and packages in this report. Further, in our stakeholder consultation, including with non-ADI lenders, packages were seldom mentioned as a significant concern. The ACCC will continue to monitor developments around home loan bundling and packages, including the impact of current and future initiatives, as part of its ongoing monitoring role in the home loan market (recommendation 4).

Box 1: Current and future initiatives can address impediments created by packages

Many lenders, sometimes informed by research into customer behaviour, are aware that customers who hold multiple products with the same financial institution are less likely to switch those products to a different financial institution.¹⁴ This awareness has likely informed the strategies of many lenders who seek to increase the stickiness of their customers by encouraging those customers to hold multiple products with them.¹⁵

Packages are one of the more common methods through which lenders seek to incentivise their customers to hold multiple products with them. The prevalence of those incentives are apparent in the share of borrowers who have taken their home loan as part of a package: about 71% (by number) and 79% (by value) of all home loans outstanding with big four banks and Macquarie Bank were held as part of a package as at 30 June 2018.¹⁶

There appear to be at least two features of packages that are attractive to consumers:

- the convenience of having a number of products with one financial institution; the Productivity Commission found that consumers *'exhibit a strong preference against the ongoing cost of managing affairs with multiple financial institutions'*¹⁷
- the discounts available on products, including home loans, taken as part of package.¹⁸

While packages appeal to many borrowers and deliver certain benefits to those borrowers, they can also create transaction costs when a borrower is seeking to switch their home loan to another lender. However, while potentially inconvenient for switching consumers, these transaction costs do not appear to create a significant impediment to switching to a new lender. Moreover, for the reasons set out below, we expect the size of these transaction costs to reduce over time.

It is relatively inexpensive for customers to hold transaction accounts and credit cards, which commonly are core products receiving discounts under packages, at multiple institutions. The Productivity Commission found this allows consumers to switch through product usage rather than product holdings.¹⁹ This means borrowers can, without undue expense, progressively change recurring payments, such as direct debits, on transaction accounts and credit cards to their new institution when convenient to them. It also means that, while a borrower seeking to switch just their home loan to another lender may lose the package discount on the other products (such as transaction accounts and credit cards), the cost of maintaining those products should not be material, especially compared to the potential savings from switching their home loan.

The Consumer Data Right (further discussed in section 1.3) and the New Payments Platform should, in time, make it easier for customers to change recurring payments. Currently, the time and effort required to change these arrangements likely deters some customers from switching entire packages between lenders.

14 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 66.

15 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 67.

16 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 30.

17 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 157.

18 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 352.

19 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, pp. 151-152.

Developments in the New Payments Platform, including the ability to switch a PayID between financial institutions and the introduction of the Mandated Payments Service, could assist with the transfer of recurring payments.²⁰ PayID allows a consumer to link their transaction account to a unique identifier, such as an email address, mobile number or ABN, and to provide this instead of a BSB and account number to receive a payment.²¹ A PayID can also be transferred to another account at a different financial institution.²² By early 2022, the Mandated Payments Service will enable consumers to authorise third parties to ‘pull’ payments from their PayID-linked transaction accounts, including to pay recurring bills or subscriptions.²³ This means that a switching consumer will only need to change the account their PayID is linked to, rather than notifying all the businesses the consumer has recurring payments with of their new account details.

The Consumer Data Right will give consumers ready access to details of their recurring direct debits. This will aid in the process of migrating those arrangements to a new account where necessary (especially if this process were in some way facilitated by an accredited third party data recipient). The Consumer Data Right will also make it easier for consumers to compare the individual products in a package. This should reduce the search and switching costs arising from, for example, bundling obscuring the price of the individual products within a package, making it difficult for consumers to assess the value of each product.²⁴

Finally, mortgage brokers (who facilitated over half of all home loans settled in the 2018–19 financial year)²⁵ will have a statutory duty from 1 January 2021 to act in the best interests of their customers. This duty will extend to ensuring a home loan taken as part of a package, including switching to or away from a package, is in the best interests of the borrower.²⁶

20 Emilie Fitzgerald and Alexandra Rush, Reserve Bank of Australia, ‘Two Years of Fast Payments in Australia’, *Bulletin—March 2020*, 19 March 2020, <https://www.rba.gov.au/publications/bulletin/2020/mar/pdf/two-years-of-fast-payments-in-australia.pdf>.

See also: New Payments Platform Australia, *New Payments Platform Roadmap 2019*, 28 October 2019, https://nppa.com.au/wp-content/uploads/2019/10/NPP-Roadmap-2019_28-Oct-2019-final.pdf.

New Payments Platform Australia, *Update on the New Payments Platform Roadmap*, 30 April 2020, https://nppa.com.au/wp-content/uploads/2020/04/NPP-Roadmap-April-2020_final.pdf.

21 PayID, ‘Frequently Asked Questions’, <https://payid.com.au/faqs/>, viewed 2 October 2020.

22 PayID, ‘Frequently Asked Questions’, <https://payid.com.au/faqs/>, viewed 2 October 2020.

23 New Payments Platform Australia, *Mandated Payments Service (MPS) Overview Webinar*, June 2020, <https://nppa.com.au/wp-content/uploads/2020/07/MPS-Market-Webinar-website.pdf>, p. 7.

New Payments Platform Australia, *Mandated Payments Service—Enabling third party payment initiation on the NPP*, 30 April 2020, https://nppa.com.au/wp-content/uploads/2020/07/NPP-Mandated-Payments-Service-Overview_final-Apr-2020-min-1.pdf, p. 2.

All participating financial institutions will be required to implement elements of the Mandated Payments Service capability by December 2021, for rollout of services in early 2022.

24 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 352.

25 Mortgage & Finance Association of Australia, *Industry Intelligence Service, 9th Edition*, March 2020, p. 10.

26 Australian Securities and Investments Commission, *Regulatory Guide 273 Mortgage brokers: Best interests duty*, June 2020, <https://download.asic.gov.au/media/5641325/rg273-published-24-june-2020.pdf>, pp. 5, 7, 17, 32–34, 46.

Conduct of the inquiry

The ACCC engaged in a stakeholder consultation process with industry associations, consumer groups and lenders, including non-ADIs, to identify and discuss the impacts of impediments to switching. In addition, we consulted on the recommendations made in this report with:

- government agencies, including the Treasury, ASIC, the RBA, APRA and, in respect of recommendation 1, the Essential Services Commission in Victoria
- the Australian Banking Association, in respect of recommendations 1-3
- the Customer Owned Banking Association, in respect of recommendations 1-3
- FinTech Australia, in respect of recommendations 1-3.²⁷

The ACCC also used its compulsory information gathering powers under section 95ZK of the *Competition and Consumer Act 2010* to obtain information and documents from the big four banks.

²⁷ The prompt recommendation that was consulted on was different to recommendation 1 in several ways, including (1) it was proposed to be sent to all variable rate borrowers and (2) it was proposed to include the first of the potential dollar savings options presented in this report—an estimate of the interest savings in the first year if the borrower switched to a loan with the same interest rate as the average rate for new loans (see box 2.3). The changes made to the prompt recommendation reflect feedback from industry associations and other stakeholders.

1. Home loan switching in Australia

Key findings

- Over 100 lenders supply home loans in Australia, offering a combined total of nearly 4,000 different home loan products. The difficulty for consumers in making a good choice from this multitude of alternatives is compounded by behavioural biases and the opaque prices of some lenders.
- Switching a home loan from one lender to another is more complex than switching between suppliers of many other products and services. It is also a more lengthy process that can take many weeks, or sometimes months, to complete.
- While borrowers incur fees and charges, and must invest time and effort, to switch home loan lenders, the potential gains from switching can be significant. Borrowers, especially those with larger or older home loans, can potentially save thousands of dollars over the remaining life of their home loan by switching lenders or negotiating a better price with their existing lender.

Being able to easily switch between lenders serves the interests of borrowers in two ways. First, it allows them to update their home loan over time to ensure it is suited to their changing needs and circumstances. Second, the demand-side pressure generated through switching, or the credible threat of switching, incentivises lenders to continually innovate and seek to offer better home loan products and lower prices in order to attract and retain borrowers.

Not all borrowers will choose to or be able to switch lenders. There will be some borrowers who periodically evaluate the home loan offerings of different lenders and decide that the home loan and service provided by their existing lender meets their needs. Other borrowers, such as those that are likely to repay their home loan in the short term or those with very small outstanding home loan balances, are unlikely to engage in the switching process as there is little benefit from doing so. Further, there are borrowers, known as mortgage prisoners, who are locked into home loans with their existing lender due to a change in their circumstances since they originally took out their home loan or changes in industry lending practices since that time.²⁸

However, we consider it is much more common that borrowers are either not motivated to look for a better home loan, or they discontinue their search before they secure a better deal due to impediments in the switching process. Impediments to borrowers switching lenders are discussed in the following chapters of this report. This chapter provides context by explaining:

- the process of switching home loan lenders (see section 1.1)
- why ease of switching is important for borrowers (see section 1.2)
- how the Consumer Data Right will assist borrowers to compare home loans and reduce frictions in the home loan application process once a borrower has decided to switch lenders (see section 1.3).

1.1 The process of switching lenders

Switching lenders occurs when a borrower repays their home loan with one lender (the previous lender) using the proceeds of a new home loan obtained from a different lender (the new lender). This section describes the interactions of the borrower, the previous lender and the new lender in this switching process.

28 For example, borrowers may not be able to switch to another lender because:

- they are unable to get a home loan approved at another lender due to a change in their employment status (including reduced income or less stable income) or because of a decrease in the value of the residential property used as security for the home loan
- lenders may be less willing to provide credit to the borrower due to a reduction in risk appetite for borrowers or loans with certain characteristics (such as a high loan to valuation ratio) or because of a change in regulation.

Switching a home loan from one lender to another is more complex and lengthy compared to switching between suppliers of many other products and services. For example, there is generally little to stop a consumer from switching between suppliers of compulsory third party insurance for a motor vehicle when their policy expires. In contrast, the switching process for home loans is complicated by a multi-stage process, including actions such as the borrower needing to obtain a home loan approval from the new lender and the need to transfer collateral (mortgage(s) over one or more residential properties) from the previous lender to the new lender.

The three stages of the process of switching lenders

From the borrower's perspective, the process for switching home loan lenders can be broadly categorised into three stages:

- deciding to engage in the home loan market to look for a better offer
- obtaining information on and comparing the offers of different lenders (sometimes referred to as 'shopping around')
- taking action by selecting a new lender and undertaking the steps in the home loan switching process (see figure 1.1).

Deciding to engage in the home loan market to look for a better offer

Borrowers are prompted to consider switching lenders and engage in the home loan market when they become aware that they may be able to get a better home loan than the one they currently hold. What constitutes a better home loan will vary from borrower to borrower. For many borrowers it will be a cheaper price.²⁹ For others, it may be product features, such as an offset account,³⁰ that better suit their needs and circumstances; better customer service; or improved mobile and online banking services.

A number of things may prompt a borrower to look for better home loan, or be more receptive to alternative offers that come to their attention. For example, dissatisfaction with staff at their previous lender and an unresolved complaint were reported in a 2015 survey as a reason for switching home loan lenders by 20 and 12% of respondents, respectively.³¹ Further, informed by responses to a 2019 survey,³² Deloitte noted the propensity to switch between ADIs in pursuit of better value products can increase when there is a deterioration in the economy and *'more people are struggling to pay bills and there is greater uncertainty around future income levels or stability of employment.'*³³

29 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 147: *'In many instances, the 'best deal' is determined by price. For example, consumers consistently report that price is the most important factor when choosing a home loan (Deloitte 2016a). This implies that the availability of lower-priced products should be a strong motivator of consumer switching.'*

Australian Competition and Consumer Commission, *Residential mortgage price inquiry Final Report*, p. 16.

BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, p. 6: *'Among those considering switching, lower interest rates and lower fees are key factors when considering changing loan providers.'*

30 An offset account is an at-call transaction account, the daily balance of which is 'offset' against the amount outstanding on a home loan for the purpose of calculating the interest payable on that loan.

31 The survey involved self-reported information provided by close to 1,000 Australian adults through an online survey in August-September 2015. The survey's sample was intended to be broadly representative of the Australian adult population. Source: Dr Juliana Silva-Goncalves, Queensland University of Technology on behalf of Heritage Bank, *Australians' switching behaviour in banking, insurance services and main utilities*, September 2015.

32 The survey was undertaken during May 2019 and involved 2,007 Australian retail banking customers. The sample was designed to be nationally representative of Australians aged 18 years and older. It excluded Australians who did not own any financial products.

The survey question informing this observation required respondents to identify the primary reasons that they decided to change the suppliers of their banking products. Participants were able to select as multiple responses and ranked them in order of importance.

Source: Deloitte, *Open Banking: Switch or Stick? Insights into customer switching behaviour and trust*, October 2019, p. 57.

33 Deloitte, *Open Banking: Switch or Stick? Insights into customer switching behaviour and trust*, October 2019, p. 57.

See also:

A survey of 1,114 Australians, conducted by Roy Morgan and commissioned by the Consumer Policy Research Centre, found in May 2020, following the onset of the COVID-19 pandemic and the economic downturn, that 27% of consumers with a home loan reported concerns about their ability to make home loan repayments.

Around 3% of consumers with a home loan reported they attempted to switch to another home loan provider in May, while close to 4% reported they attempted to refinance a home loan with their existing lender during May 2020.

Source: Consumer Policy Research Centre, *COVID-19 and Consumers: from crisis to recovery*, June 2020, pp. 24, 28.

Chapter 2 explains:

- the extent to which borrowers with older home loans pay more than borrowers with new loans, and how this demonstrates a lack of engagement in the home loan market among this cohort
- some of the reasons why borrowers are disengaged and do not consider the benefits of switching
- why a personalised prompt from their lender that outlines the potential benefits of switching is likely to compel many borrowers to engage in the home loan market.

Obtaining information and comparing offers

Once a borrower has decided to look for a better home loan, they need to establish which offers are likely to be available to them. They do this by collecting information on the offers available from different lenders and comparing them to their current home loan.

It can be difficult for consumers to find a home loan that suits their needs and circumstances. This is in part due to what the Productivity Commission has described as a '*blizzard of barely differentiated products*'.³⁴ There are over 100 home loan lenders in Australia offering a combined total of nearly 4,000 different home loan products.³⁵ It is also partly due to the opaque prices of some lenders which make it difficult for borrowers to compare the prices of different home loans.

The complexity of decision-making required to choose a home loan is further compounded by the variety of product features available across different home loans and from different lenders. For example, some of the common choices a borrower needs to make include whether to choose a home loan:

- with principal and interest repayments or interest-only repayments
- with a fixed or variable interest rate, or a home loan split between the two
- as part of a package or as a stand-alone home loan
- with an offset account, redraw facility,³⁶ or both
- with options such as repayment holidays³⁷ or the ability to replace the security property for the home loan with a different property (known as loan portability).³⁸

More generally, consumers can experience cognitive overload when faced with a set of complex choices from a wide array of options. This can cause consumers to overlook important considerations, delay making a decision or, in the extreme, disengage from making a decision altogether. In the case of those borrowers who are considering switching home loans, cognitive overload may be compounded by status quo bias, creating a tendency for consumers to stick with their existing lender even when a better home loan may be available.

As a result, even for the motivated and engaged borrower, the time and effort required to source and compare information from different lenders can deter them from doing so.

Chapter 3 considers the key issues that cause opaque home loan prices and hinder consumers from shopping around and comparing home loans.

34 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 12.

35 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 12.

36 A redraw facility provides the ability to make additional repayments to a home loan and withdraw them at a future date (assuming the loan remains ahead of its scheduled repayments). Additional repayments made into a redraw facility reduce the loan balance and the minimum periodic loan repayment, whereas funds in an offset account only reduce the interest paid on the loan, not the minimum repayment. While a redraw facility allows a borrower to make interest savings in a similar manner to an offset account, unlike an offset account, the funds held under a redraw facility are not guaranteed by the Australian Government under the Financial Claims Scheme.

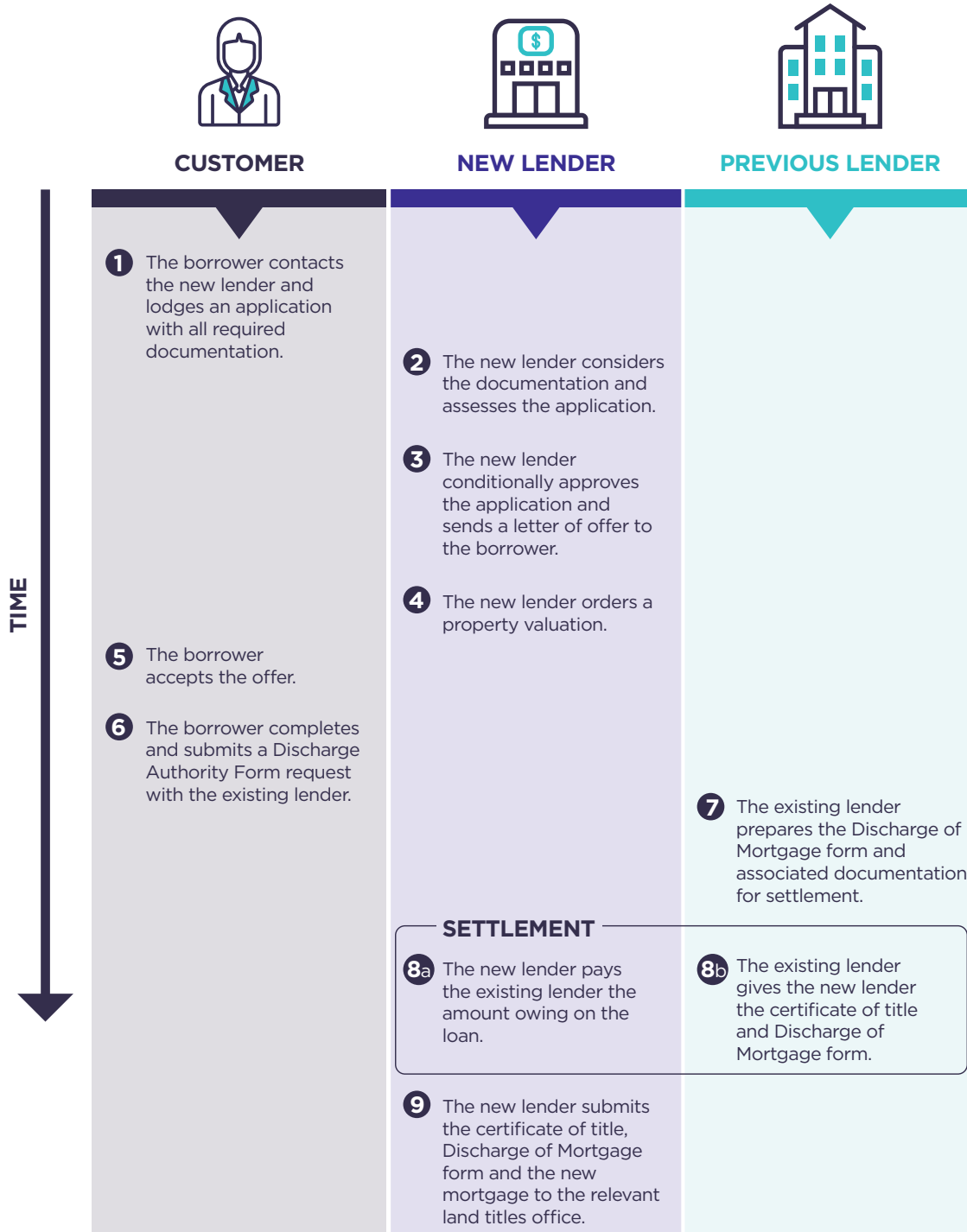
37 Repayment holidays allow borrowers to pause their home loan repayments. Repayment holidays are typically only granted by lenders if the borrower is ahead on their scheduled repayments.

38 Home loan portability allows a borrower to change the property over which the lender holds a mortgage without having to change home loans. It means that in situations where a borrower is selling the security property and purchasing a new property, the new property can be used as security on the existing home loan (subject to a satisfactory valuation, among other things) without the need to close the existing home loan and apply for a new home loan.

Taking action to switch lenders

Having established they can get a better home loan, and identified the lender offering that home loan, the final step for a borrower is to transfer their home loan to that lender. The typical steps in the process of switching home loan lenders are set out in figure 1.1 below.

Figure 1.1: The high level process for switching home loan lenders



Some steps in this process may take a number of days or weeks to complete and can involve multiple interactions between the borrower and the lender. For example, in step 2, the new lender may seek additional documentation (to that supplied in step 1) from the borrower, such as a longer history of transaction account statements to verify the financial position of the borrower and conduct an affordability and credit assessment.

Further, not all of these steps necessarily occur sequentially. Some, such as the ordering of a valuation by the new lender and the borrower obtaining the Discharge Authority form from the existing lender, can occur concurrently. Completing the processes set out in figure 1.1 can take a long time compared to switching between providers of other products and services. A decision to switch between providers of Compulsory Third Party insurance can be implemented within one day whereas the time between submitting a home loan application to the settlement of that loan can be four to six weeks. For certain home loans settled in 2019, it took up to nine weeks.³⁹

As set out in section 1.3, the Consumer Data Right can assist borrowers completing the home loan application process and expedite steps 1–3 in figure 1.1. In addition, in September 2020, the Treasurer, the Hon Josh Frydenberg MP, announced proposed reforms to Australian credit laws, including the removal of responsible lending obligations from the *National Consumer Credit Protection Act 2009*.⁴⁰ If implemented, this may reduce the amount of information borrowers must provide to lenders when seeking approval for a home loan.⁴¹

Steps 6–9 in figure 1.1 are discussed in chapter 4, which includes two recommendations intended to shorten the time and simplify the steps involved in the discharge process. In doing so, these recommendations seek to address the issue of consumers being deterred by the time and effort involved in completing this stage of the switching process.

1.2 Why ease of switching is important for borrowers

While there has been a significant increase in the value of home loans switched between lenders during the first half of 2020 (see figure 1.2),⁴² consumer surveys conducted in recent years indicate there has been relatively less switching of home loans between lenders compared to consumers switching between suppliers of other goods and services.⁴³ The comparatively lower levels of switching in relation to home loans may indicate impediments in the home loan switching process.

39 J Frost, 'Home loans delayed, denied and dearer post-Hayne', *Australian Financial Review*, 23 April 2019, <https://www.afr.com/companies/financial-services/home-loans-delayed-denied-and-dearer-post-hayne-20190422-p51g5h>, viewed 6 August 2020.

40 The Hon Josh Frydenberg MP, *Simplifying access to credit for consumers and small businesses*, 25 September 2020, <https://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/media-releases/simplifying-access-credit-consumers-and-small>, viewed 25 September 2020.

41 The Australian Government, *Consumer credit reforms*, 25 September 2020, <https://ministers.treasury.gov.au/sites/ministers.treasury.gov.au/files/2020-09/Consumer-credit-reforms-fact-sheet.pdf>, viewed 25 September 2020.

42 There are a range of factors that may have contributed to the increase in the number of borrowers switching home loan lenders in the first half of 2020. These include:

- Interest rates on new fixed-rate home loans declined by around 65 basis points from March to June 2020 and in June 2020 the interest rates on new fixed rate home loans were around 60 to 70 basis points below the interest rates on new variable rate loans. This RBA has noted this gap contributed to an increase in refinancing activity as borrowers switched from variable rate to fixed rate home loans.
- Over the first half of 2020, a number of lenders offered cash back offers which ranged from \$1,000 to \$4,000, depending on the lender. Cashback offers pay a specified amount of cash for refinancing an eligible home loan from an existing lender to a new lender. These offers are paid by the new lender to the borrower and aim to cover some or all of the costs involved in refinancing a home loan. The RBA has noted that these cashback offers are consistent with the increase in refinancing activity that has occurred since March 2020.
- As discussed in section 1.1, informed by a 2019 survey, Deloitte have noted that the propensity to switch between ADIs in pursuit of better value products can increase when there is a deterioration in the economy. The contraction in the Australian economy as a result of the COVID-19 pandemic may have contributed to an increase in the number of borrowers switching lenders to seek better value banking products.

Sources:

Deloitte, *Open Banking: Switch or Stick? Insights into customer switching behaviour and trust*, October 2019, p. 57.

D Giannopoulos, 'The lenders giving mortgage holders up to \$4,000 in cash back for refinancing', *Domain.com.au*, 12 June 2020, <https://www.domain.com.au/money-markets/the-lenders-giving-mortgage-holders-up-to-4000-cash-back-for-refinancing-962092/>, viewed 25 June 2020.

Reserve Bank of Australia, *Statement on Monetary Policy—August 2020*, 2020, pp. 69–70.

43 The surveys indicate that around 4 to 6% of home loan borrowers have switched lenders during the survey periods. These surveys also found the rate of switching between home loan lenders is generally lower than the rate of switching between suppliers of other goods and services including insurance, energy, internet and groceries.

Sources:

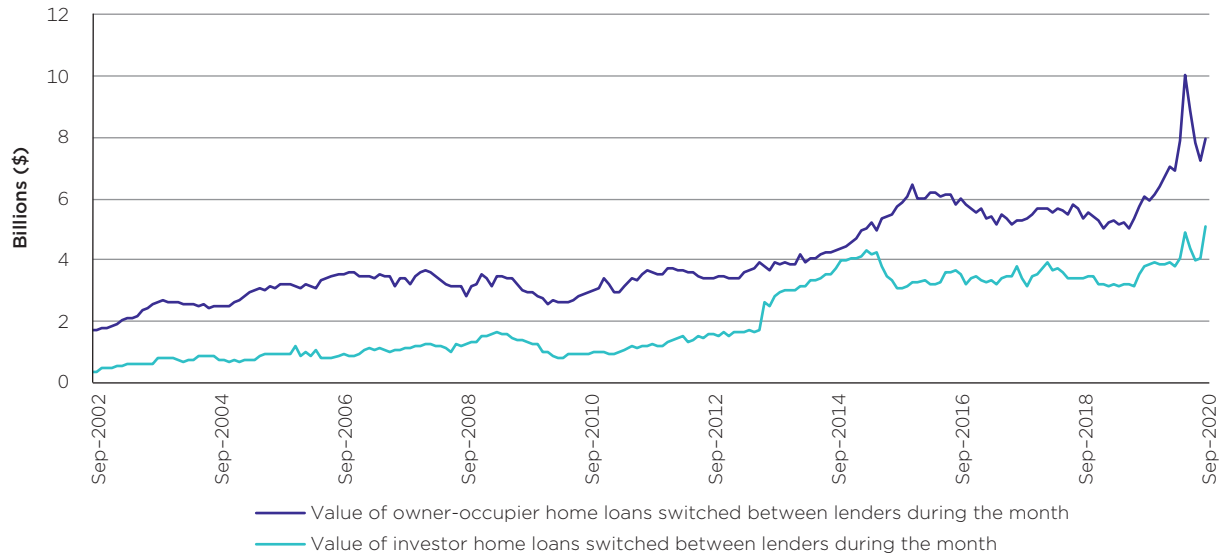
Dr Eugene Chan, University of Technology Sydney on behalf of Heritage Bank, *Australians' Switching Behaviour in Banking and Essential Services*, October 2016.

Deloitte Access Economics for the Australian Banking Association, *Choices in Banking*, 2019.

Deloitte, *Open banking: switch or stick? Insights into customer switching behaviour and trust*, October 2019.

Dr Juliana Silva-Goncalves, Queensland University of Technology on behalf of Heritage Bank, *Australians' switching behaviour in banking, insurance services and main utilities*, September 2015.

Figure 1.2: Value* of owner-occupier and investor home loans switched between lenders



* Seasonally adjusted.

Source: Australian Bureau of Statistics, *5601.0—Lending Indicators*, table 3 and table 13, September 2020.

The more difficult it is for borrowers to search for a home loan that suits their needs or to switch between lenders, the more likely it is that they will not receive the best price, product and service available. Consistent with this, the average interest rate paid across home loans (owner-occupier and investor) originated in 2019 was around 40 basis points lower than the average interest rate for home loans originated in 2015 or earlier.⁴⁴ To put this difference into perspective, it means a borrower with a \$250,000 home loan would pay about \$1,000 in extra interest over one year.

If there were no material impediments to borrowers engaging in the home loan market, comparing offers and moving between lenders, such a difference in interest rates would not be expected to persist over time. That is because borrowers with older home loans would seek out a home loan with an interest rate closer to that being paid on newer home loans, and lenders would offer lower interest rates to borrowers with older home loans in order to retain those loans.

If borrowers can readily obtain and compare information on home loans and can switch lenders, they are better placed to access any improved terms and conditions for their home loan compared to those available when they originally took out their loan. Further, they can benefit without having to switch lenders. A credible threat of switching can be enough for lenders to improve their product offerings so that borrowers do not move, or consider moving, to a different lender. The ways in which a borrower can pursue a better deal with their existing lender are set out in box 1.1.

⁴⁴ Reserve Bank of Australia, 'Box C: Do Borrowers with Older Mortgages Pay Higher Interest Rates?' *Statement on Monetary Policy*, February 2020, p. 55.

In the home loan price inquiry interim report we also found that the big four banks' customers whose existing owner-occupier loans with principal and interest repayment were greater than five years old were paying, on average, 40 basis points above what the big four banks' customers with new loans were paying as at 30 September 2019. Source: Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, p. 65.

Box 1.1: The ways a borrower can obtain a better deal from their existing lender

There are two ways a borrower can get a better deal from their existing lender:

- obtain a better price on their existing home loan
- switch to a cheaper home loan or a home loan with features better suited to their needs with their existing lender.

Getting a better price on an existing home loan

Some lenders will offer a discretionary discount, or an increased discretionary discount, to an existing borrower to dissuade them from switching to another lender. These incremental discounts are sometimes referred to as retention offers and are generally only available for variable rate home loans.

Retention offers are typically extended to borrowers who are looking to switch to a new lender. Lenders can become aware that one of their borrowers is looking to move to another lender when they receive a Discharge Authority form (see step 6 in figure 1.1).

However, borrowers do not need to be about to switch to a new lender or even be looking for a new lender to take advantage of the retention offers that may be available from their existing lender. By researching home loan prices on offer, and asking their lender for a lower price to match or beat the prices available from other lenders, borrowers may be able to access a retention offer.

A price reduction, including through a new or additional discretionary discount, was granted to over 600,000 home loans with the big four banks in the 12 months to 30 September 2019.⁴⁵ While these price reductions resulted in borrowers paying less interest or fees on their home loan, this does not necessarily mean the borrower secured as low a price as they could have by switching to a new lender and obtaining the interest rate available on new loans.

Moving to a cheaper home loan product or a home loan with features better suited to their needs with their existing lender

Borrowers may be able to move to a different home loan product but stay with their existing lender. This can reduce some of the costs, including time and effort, associated with switching, while still delivering the borrower a cheaper home loan or one with features that are better suited to their needs and circumstances. For example, over the period May 2017 to June 2018, when the interest rates on home loans with interest-only repayments were appreciably higher than home loans with principal and interest repayments, the number of home loans with interest-only repayments at the big four banks and Macquarie Bank fell by about 350,000.⁴⁶ Many of these loans appear to have switched to home loans with principal and interest repayments in order to obtain a lower interest rate, generally with the same lender.

Borrowers can save money by switching lenders

The differences in average interest rates paid on variable rate home loans of different ages have persisted since at least 2015 and have become more pronounced over time (see figures 1.3 and 1.4). Based on this trend, many existing borrowers should be able to achieve significant savings by switching lenders or negotiating with their existing lender to receive an interest rate similar to that on offer for new loans (see box 1.1). The size of the potential savings increase with the age of the home loan. For example, as at 30 June 2019:

- a borrower with a \$210,000 home loan from one of the big four banks that was originated five years ago, and paying the average interest rate applying to those loans of 3.95%, could have saved more than \$600 in interest over the year to 30 June 2020 had they refinanced their loan on 30 June 2019

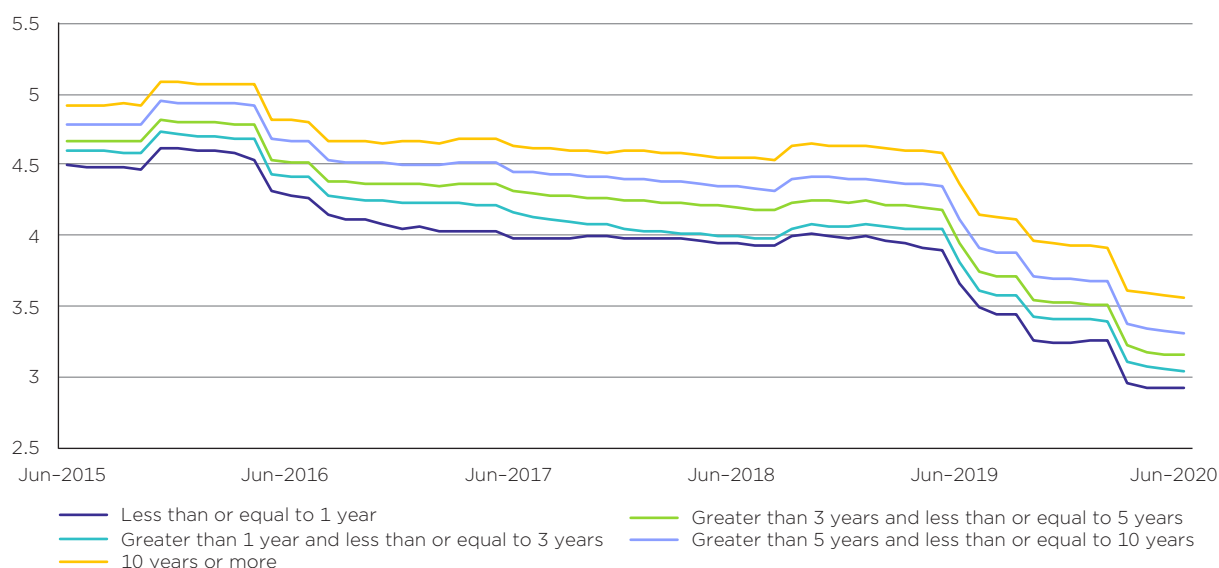
45 Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 63–65.

46 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, pp. 35–37.

to pay the same interest rate as the average for new loans of 3.66%. Over the remaining term of the loan, the borrower could expect to save over \$7,000 in interest in net present value terms.⁴⁷

- a borrower with a \$140,000 home loan from one of the big four banks that was originated ten years prior, and paying the average interest rate applying to those loans of 4.37%, could have saved nearly \$1,000 over the year to 30 June 2020 had they refinanced their loan on 30 June 2019 to pay the same interest rate as the average rate for new loans of 3.66%. Over the remaining term of the loan, the borrower could expect to save over \$9,000 in net present value terms.⁴⁸

Figure 1.3: Weighted average interest rates* paid on variable rate owner-occupier home loans with principal and interest repayments with the big four banks, by age of loan since origination



* The weighted average interest rate is based on the balance of securitised loans that are eligible as collateral in the RBA's domestic market operations.

Source: Reserve Bank of Australia, *Securitisation Dataset*.⁴⁹

47 The estimated savings do not take into account up-front or recurring fees. Aside from the information presented in the scenario, the estimated savings are based on:

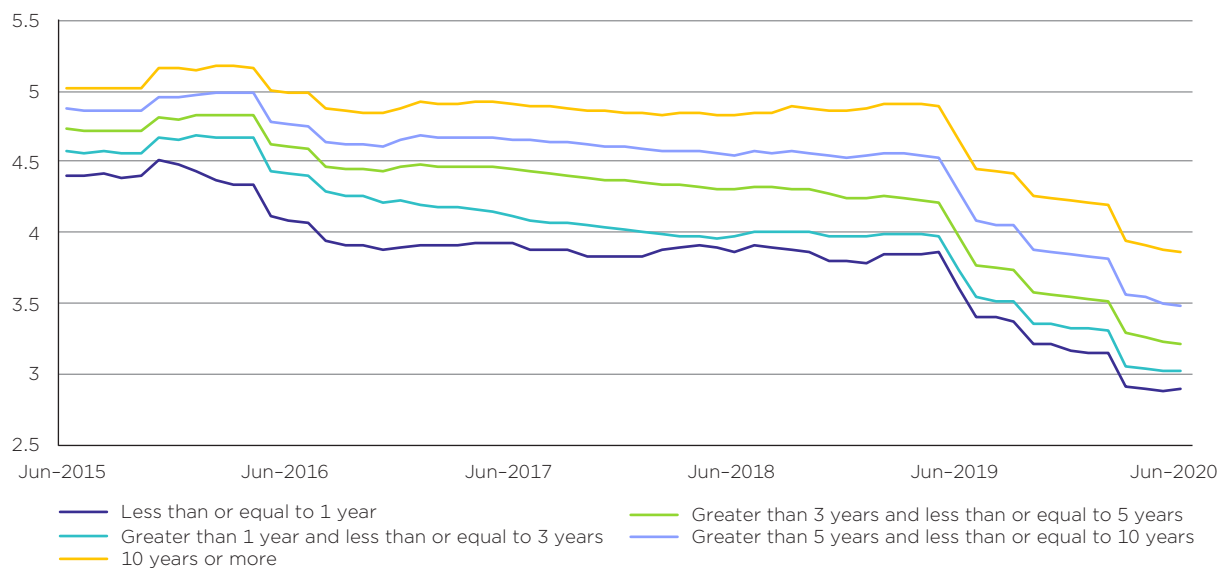
- a loan amount of \$210,000, which is the average size loan, rounded to the nearest \$10,000, across the big four banks for home loans originated five or more years prior to 30 June 2019,
- an assumed remaining loan term of 25 years and minimum monthly repayments
- a (nominal) discount rate for the net present value calculation of 3.95%, which is the weighted average interest rate paid on home loan originated three to five years ago as at 30 June 2019.

48 The estimated savings do not take into account up-front or recurring fees. Aside from the information presented in the scenario, the estimated savings are based on:

- a loan amount of \$140,000, which was the average size loan, rounded to the nearest \$10,000, across the big four banks for home loans originated 10 or more years prior to 30 June 2019
- an assumed remaining loan term of 20 years and minimum monthly repayments
- a (nominal) discount rate for the net present value calculation of 4.37%, the weighted average interest rate paid on existing loans for home loans with the big four banks originated 10 years ago or more as at 30 June 2019.

49 The Securitisation Dataset contains data on 2.4 million individual home loans with a combined value of around \$668 billion, or around one-third of the total value of outstanding home loans in Australia. The RBA considers the Securitisation Dataset is reasonably representative of average interest rates in the home loan market. However, the Securitisation Dataset may not be representative of the home loan interest rates in the portfolios of individual lenders. This is because the securitised loans represent only a portion of lenders' portfolios and the type of loans that are securitised may be influenced by (among other things) the way credit ratings agencies assign ratings, the type of lender, investor preferences, and the RBA's repo-eligibility framework. For more information on the RBA's Securitisation Dataset see: Reserve Bank of Australia, 'The Reserve Bank's Securitisation Dataset', *Bulletin—December 2018*, December 2018.

Figure 1.4: Weighted average interest rates* paid on variable rate owner-occupier home loans with principal and interest repayments with other Australian banks^, by age of loan since origination



* The weighted average interest rate is based on the balance of securitised loans that are eligible as collateral in the RBA's domestic market operations.

^ Other Australian banks are all locally-owned banks excluding the big four banks.

Source: Reserve Bank of Australia, *Securitisation Dataset*.

The potential non-price benefits for consumers from switching lenders

While price is important to most borrowers, it is not the only factor taken into account by many when considering whether to switch to a new lender. There are borrowers that prioritise certain home loan features in deciding which home loan is best for them, including:

- product features, such as offset accounts and loan structuring options
- customer service, including ease of use of borrower-facing technologies such as mobile apps and online banking, and access to services through channels such as physical branches.⁵⁰

Access to better product features and loan structures

Product features, such as offset accounts and redraw facilities, are important considerations for many borrowers when selecting a home loan. Offset accounts and redraw facilities allow borrowers to set aside money in a way that reduces their interest expense but allows them continued access to the money they have set aside. A survey conducted on behalf of Deloitte in 2019⁵¹ found that access to better product features, such as an offset account, was one of the top five reasons why consumers switch between banks.⁵²

A borrower can also value flexibility in how a home loan is structured. This flexibility can manifest in a number of ways, such as:

- the ability to split a home loan into a fixed interest rate loan (or loans) and a variable interest rate loan

50 BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, p. 6.
Dr Eugene Chan, University of Technology Sydney on behalf of Heritage Bank, *Australians' Switching Behaviour in Banking and Essential Services*, October 2016, p. 9.
Deloitte, *Open banking: switch or stick? Insights into customer switching behaviour and trust*, October 2019, p. 57.
Dr Juliana Silva-Goncalves, Queensland University of Technology on behalf of Heritage Bank, *Australians' switching behaviour in banking, insurance services and main utilities*, September 2015, pp. 8–9.

51 The online survey was conducted by Dynata during May 2019. It involved a sample of 2,007 people that was designed to be representative of Australians over the age of 18.

52 The most frequently reported response to why consumers changed providers of their home loan was to seek 'better value'. This was reported by 25% of respondents.
Deloitte, *Open banking: switch or stick? Insights into customer switching behaviour and trust*, October 2019, pp. 57–58.

- the ability to take an extended interest-only repayment period or an extended fixed interest rate period. For example, some lenders were offering a maximum fixed rate term of five years in August 2020 while others were offering a 10 year maximum term. Fixed rate terms of up to 15 years have been available in Australia previously.⁵³

There can be a trade-off between home loan features and price. For example, basic home loans often do not include features such as offset accounts but are commonly promoted by lenders as being a cheaper and simpler option for borrowers compared to standard home loans (which typically include an offset account feature). However, in the Residential mortgage price inquiry, we found that, as at 30 June 2018, across the big four banks and Macquarie Bank, the average interest rate paid on standard variable rate home loans taken as part of a package was generally lower than the average interest rate paid on unpackaged (or basic) home loans.⁵⁴

Better customer service

Customer service has been a significant consideration in the decision-making of many borrowers who have switched lenders. One survey conducted in December 2017 asked borrowers who had switched their home loan to another lender in the last three years what their key reason was for that switch. Nearly one in seven respondents identified *'my lender had poor customer service'* as their key reason.⁵⁵

Dissatisfaction with the customer service of an existing lender can manifest in different ways. Some examples are contained in reasons given for switching between banking products by respondents to a 2019 survey conducted on behalf of Deloitte.⁵⁶ The reasons cited included: *'I was dissatisfied with my old bank'* and *'I didn't trust that my old bank had my best interests at heart'*. In some cases it was because the new financial institution was considered to provide better service by being *'more convenient'* or by having a *'better mobile app or website.'*⁵⁷

The cost of switching can be small compared to the benefits

While borrowers incur a cost of in terms of the time and effort in switching lenders, there is often also a monetary cost. For example, it could have cost upward of \$1,150 in fees and charges to switch a home loan between the big four banks in July 2020 (see Appendix B).

This cost of switching should not be considered by borrowers in isolation. Rather, it needs to be considered in the context of the possible savings (see section 1.2) and other benefits a borrower might gain from switching. It also needs to be considered in light of potential cashback offers, which have been available at times from various lenders. Cashback offers are paid by the new lender to the borrower for refinancing an eligible home loan from an existing lender. These offers are one way for borrowers to be reimbursed for some or all of the fees and charges incurred when switching lenders.

53 W Jolly, 'What Is A 30-Year Fixed Rate Home Loan?', *Canstar*, 23 January 2018, <https://www.canstar.com.au/home-loans/30-year-fixed-rate-home-loan/>, viewed 5 August 2020.

54 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 30.

55 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 17.

56 The online survey was conducted by Dynata during May 2019. It involved a sample of 2,007 people that was designed to be representative of Australians over the age of 18.

57 Deloitte, *Open banking: switch or stick? Insights into customer switching behaviour and trust*, October 2019, p. 57.

1.3 The Consumer Data Right will help borrowers compare the offers of different lenders and streamline the home loan application process

In response to the Review into Open Banking,⁵⁸ the Australian Government announced on 9 May 2018 that it would provide funding for the implementation of the Consumer Data Right in Australia. In the context of home loans, the Consumer Data Right will give borrowers and prospective borrowers the right to safely access data about them that is held by ADIs.

The Consumer Data Right went live on 1 July 2020 with individual customers of the big four banks being able to request that their bank share their data for deposit and transaction accounts, and credit and debit cards. From 1 November 2020, customers of the big four banks were also able to share data relating to home loans, personal loans and joint accounts with accredited third parties. Other ADIs are required to make the equivalent customer data available 12 months after the big four banks, although it is expected some ADIs will opt to make the data available earlier.

Helping borrowers obtain and compare the offers of different lenders

The Consumer Data Right will give borrowers the ability to consent to their ADI sharing data with the trusted and accredited third party data recipient(s) of their choice.⁵⁹ The data recipient may be a service provider that can provide information on the prices that may be available from a range of different lenders given a borrower's characteristics or a lender that can provide the price it would be willing to offer to the borrower. This could assist borrowers in discovering prices available in situations where lenders would otherwise require them to complete a home loan application and provide substantial personal information in order for the lender to assess the borrower's risk profile and determine the interest rate it is willing to offer.

Under the Consumer Data Right, ADIs are also required to make details of their products (including home loans) available in a standard format. This includes information such as interest rates, fees and charges, and eligibility criteria. This data will also assist lenders or service providers to identify the most suitable and best priced products for a borrower's specific needs and circumstances (although it may not contain information on the discretionary discounts offered by some lenders).

Streamlining the home loan application process

In order to obtain a home loan, a consumer must complete a home loan application form and lodge the required documentation with a lender (see steps 1–2 in figure 1.1). Among other things, this documentation typically involves a consumer providing to the lender transaction and savings account statements, credit card and personal loan statements, as well as details of other accounts or loans, that cover a certain period of time (for example, the past three months). These documents have typically been provided by the consumer sending copies of the bank statements to the lender or by the consumer sharing their online banking login credentials (such as their username and password) to companies that 'scrape'⁶⁰ this data and provide it to the lender.

The Consumer Data Right will give consumers the ability to consent to their ADI sharing their data, in a usable, machine readable form, with accredited third party data recipients. This could be, for example, a lender or a third party who aggregates the customer's data and provides it to a lender. This will help to overcome the time and effort associated with manually transferring copies of documents, as well as

58 The Australian Government the Treasury, *Review into Open Banking: giving customers choice, convenience and confidence*, December 2017.

59 The ACCC is responsible for accrediting the entities that can receive data under the Consumer Data Right regime.

60 Screenscraping involves allowing third parties to access bank accounts on a customer's behalf using the customer's access credentials (such as their internet banking username and password). Once access to the customer's account is obtained, data is 'scraped' from the online interface.
For further information on screenscraping see:
The Australian Government the Treasury, *Review into Open Banking: giving customers choice, convenience and confidence*, December 2017, p. 72.

limiting security concerns (and other issues) that can result from screenscraping.⁶¹ An example of how the Consumer Data Right will assist consumers through the home loan application process is in box 1.2.

Box 1.2: How the consumer data right can assist consumers in the home loan application process

Regional Australia Bank, one of the two accredited data recipients as at 1 July 2020, received an online personal loan application on the evening of 1 July, the day the Consumer Data Right went live. Using the Consumer Data Right, the applicant was able to securely share with Regional Australia Bank the details of over 3,000 account transactions as part of their application. According to Regional Australia Bank, the data collection took 21 seconds. The information collected assisted Regional Australia Bank to make its decision on the loan application that same evening.⁶²

61 The Australian Government the Treasury, *Review into Open Banking: giving customers choice, convenience and confidence*, December 2017, p. 72.

62 Regional Australia Bank, 'Regional Australia Bank LinkedIn Post', https://au.linkedin.com/company/regional-australia-bank?trk=organization-update_share-update_actor-text, viewed 28 July 2020.

2. Bringing the benefits of switching to borrowers' attention

Key findings

- Many borrowers with older home loans continue to pay interest rates significantly higher than those available on new loans. The fact those borrowers have not switched to take advantage of potentially significant savings indicates that, among this cohort, there is a lack of engagement in the home loan market and limited awareness of the benefits of switching.
- The proportion of borrowers who stand to benefit from switching significantly exceeds the proportion of borrowers who say they intend to switch.
- Some borrowers may not engage in the home loan market because they presume that there are limited benefits from doing so. Other borrowers can set and forget their home loan and are not compelled to consider switching.
- We consider that many borrowers' willingness to engage in the home loan market to look for a better offer would increase if the potential benefits of switching were brought to their attention in a compelling way. We recommend that lenders provide a prompt to their variable rate borrowers with older home loans.
- Increased engagement in the home loan market, resulting in an increasing number of borrowers switching lenders or home loan products, or obtaining a price reduction on their existing loan, would generate savings for many borrowers and have a powerful effect on competition in the home loan market.

In this chapter, we report on:

- the extent to which borrowers with older home loans pay more than borrowers with new loans, and how this demonstrates a lack of engagement among this cohort
- some of the reasons why borrowers are disengaged and do not consider the benefits of switching
- why a personalised prompt that outlines the potential benefits of switching is likely to compel many borrowers to engage in the home loan market.

2.1 Despite the availability of significant savings, many borrowers go for years without switching

A significant number of borrowers have not switched lenders for several years. The RBA observed that, as at December 2019, almost half of all variable rate loans in the RBA's Securitisation Dataset were originated at least four years ago.⁶³

As borrowers' loans get older, the gap between what they pay and what borrowers with new loans pay widens. For example, as at September 2020:

- borrowers with home loans between three and five years old were, on average, paying around 58 basis points above the average interest rate for new loans
- borrowers with home loans between five and 10 years old were, on average, paying around 71 basis points above the average interest rate for new loans
- borrowers with home loans greater than 10 years old were, on average, paying around 104 basis points above the average interest rate for new loans (see figure 2.1).⁶⁴

As is evident from figure 2.1, the significant majority of interest rates paid on older home loans are higher, and in many cases materially higher, than the average interest rate paid on new loans. As noted in Chapter 1, we have observed this trend since 2015 (see figures 1.3 and 1.4).

63 Reserve Bank of Australia, 'Box C: Do Borrowers with Older Mortgages Pay Higher Interest Rates?' *Statement on Monetary Policy*, February 2020, p. 55.

64 As at September 2020, borrowers whose variable rate owner-occupier loan with principal and interest repayments was between three and five years old were paying an average interest rate of 3.20%, compared to the average interest rate for new owner-occupier home loans with principal and interest repayments, which includes fixed and variable rate home loans, which was 2.62%.

As at September 2020, borrowers whose variable rate owner-occupier loan with principal and interest repayments was between five and ten years old were paying an average interest rate of 3.33%, compared to the average interest rate for new owner-occupier home loans with principal and interest repayments, which includes fixed and variable rate home loans, which was 2.62%.

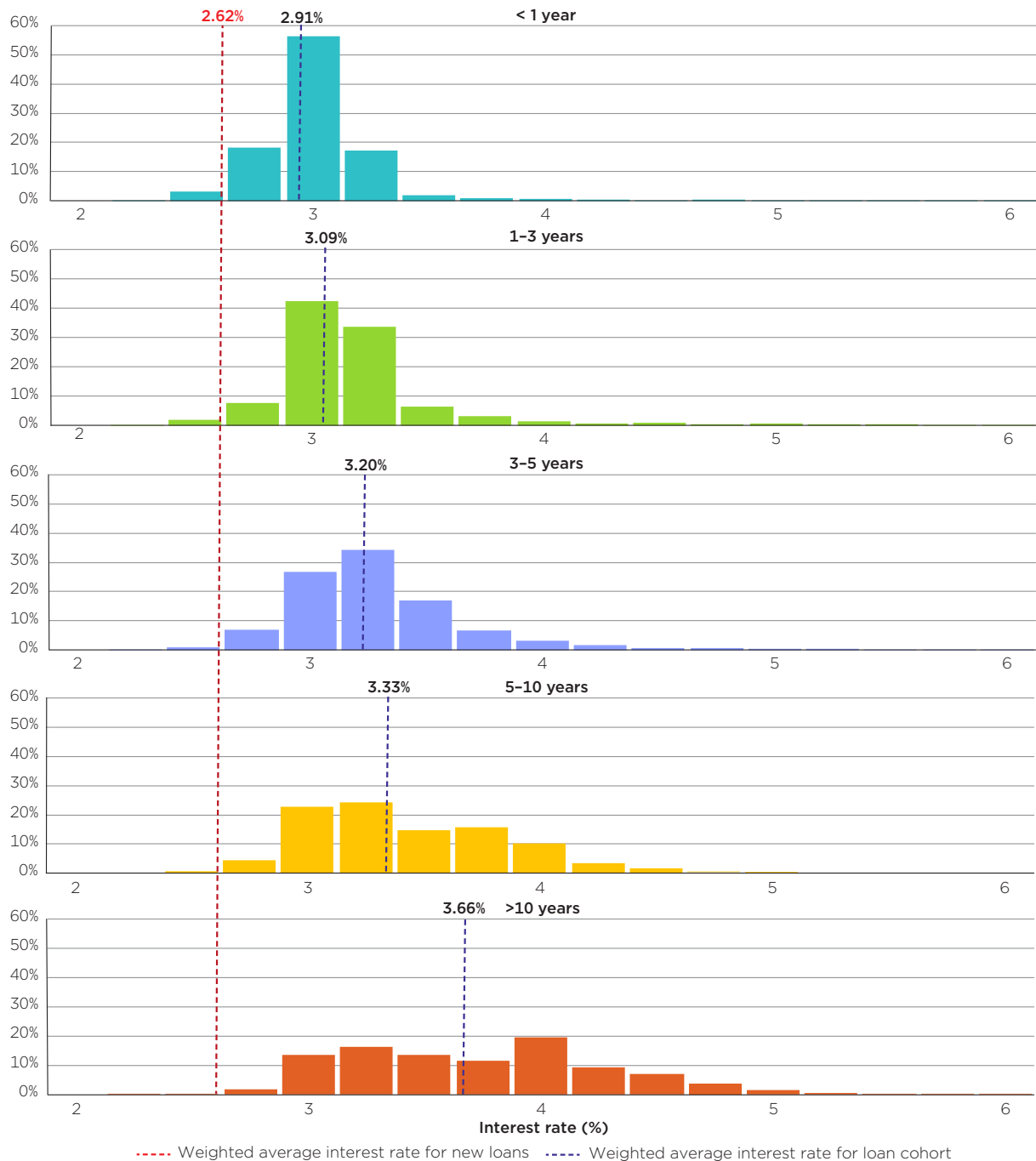
As at September 2020, borrowers whose variable rate owner-occupier loan with principal and interest repayments was greater than 10 years old were paying an average interest rate of 3.66%, compared to the average rate for new owner-occupier home loans with principal and interest repayments, which includes fixed and variable rate home loans, which was 2.62%.

The average interest rate for new loans is a weighted average for new loans funded in the relevant month based on the Economic and Financial Statistics data collection, which accounts for around 95% of total housing credit outstanding. Sources:

Reserve Bank of Australia, *Securitisation Dataset*.

Reserve Bank of Australia, Statistical Table F6—Housing Lending Rates, <https://www.rba.gov.au/statistics/interest-rates/>, viewed 6 November 2020.

Figure 2.1: Distribution of interest rates on variable rate owner-occupier loans with principal and interest repayments, by loan tenure, September 2020



Note: The proportion of home loans in each interest rate bucket is based on the balance of securitised loans that are eligible as collateral in the RBA's domestic market operations. Data from the Securitisation Dataset represents variable rate loans only, whereas the average rate for new loans represents both fixed and variable rate home loans.

The Securitisation Dataset contains data on 2.4 million individual home loans with a combined value of around \$668 billion, or around one-third of the total value of outstanding home loans in Australia. The RBA considers the Securitisation Dataset is reasonably representative of average interest rates in the home loan market. However, the Securitisation Dataset may not be representative of the home loan interest rates in the portfolios of individual lenders. This is because the securitised loans represent only a portion of lenders' portfolios and the type of loans that are securitised may be influenced by (among other things) the way credit ratings agencies assign ratings, the type of lender, investor preferences, and the RBA's repo-eligibility framework.

For more information on the RBA's Securitisation Dataset see: Reserve Bank of Australia, 'The Reserve Bank's Securitisation Dataset', *Bulletin—December 2018*, December 2018.

Source: Reserve Bank of Australia, *Securitisation Dataset*.

Reserve Bank of Australia, Statistical Table F6—Housing Lending Rates, <https://www.rba.gov.au/statistics/interest-rates/>, viewed 6 November 2020.

Many of those borrowers with older home loans could achieve significant savings if they switched lenders or home loan products (see box 2.1).

Box 2.1: Potential savings available to borrowers with older home loans

As set out above, borrowers with home loans between three and five years old were, on average, paying around 58 basis points above the average interest rate for new loans.

If a borrower with a home loan of \$250,000 switched to a home loan with an interest rate 58 basis points lower than their existing loan, they would save over \$1,400 in interest in the first year. Over the remaining term of the loan that borrower would save over \$17,000 in interest in net present value terms.

Borrowers with larger home loans stand to save significantly more. For example, if a borrower with a home loan of \$500,000 switched to a home loan with an interest rate 58 basis points lower than their existing loan, they would save over \$2,800 in interest in the first year and over the remaining term of the loan that borrower would save over \$34,000 in interest in net present value terms.⁶⁵

In our view, the fact that many borrowers with older home loans pay interest rates significantly higher than those available on new loans, is due to a lack of engagement among this cohort. If these borrowers were regularly engaging in the home loan market and aware of the significant savings available on new loans, we would expect there to be fewer loans with interest rates significantly higher than the average interest rate for new loans, as many of these borrowers would have switched lenders or home loan products, or asked their existing lender for a price similar to those available for new loans.⁶⁶

The proportion of borrowers who stand to benefit from switching (see figure 2.1) significantly exceeds the proportion of borrowers who say they intend to switch. For example, survey data held by two of the big four banks showed that over the period September 2014 to September 2019, fewer than one in five borrowers intended to refinance (with their existing lender) or switch their home loan (to a new lender) within the next 12 months.⁶⁷ A survey conducted on behalf of the Customer Owned Banking Association in 2017 showed a similar outcome with nearly two-thirds of respondents saying they were unlikely to consider switching their home loan to a different lender over the next 12 months.⁶⁸

65 These estimates are based on:

- a (nominal) interest rate for the net present value calculation of 3.20%, which is the weighted average interest rate paid on variable rate owner-occupier loans with principal and interest repayments between three and five years old across all lenders in the Reserve Bank of Australia's Securitisation Dataset as at September 2020
- a remaining term of 25 years.

66 We acknowledge that not all borrowers will choose to or be able to switch lenders or home loan products (see chapter 1).

67 The survey question was 'How likely would you be to refinance your mortgage in the next 12 months?' The share of borrowers reported represents borrowers who said they were 'highly likely' to do so (8-10 on a scale of 10). For each tranche of the survey from September 2014 to September 2019 there were at least 2,000 respondents. The survey for September 2019 was completed by 2,001 borrowers and was said to be nationally representative by age, gender and location of the respondents.

68 BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, pp. 3, 5.

The survey was conducted online from 9 to 12 January 2017 and is based on 1,009 Australian adults.

In addition, a CHOICE survey conducted in 2017 evidenced 65% of survey respondents had not switched or considered switching their home loan within the last two years.

Source: CHOICE, *Submission to the Productivity Commission*, September 2017, pp. 7, 14.

The survey was conducted between 15 and 24 September 2017 with 1,029 Australians aged 18+ from a permission-based panel. A nationally representative sample was drawn based on population data sourced from ABS Census 2016, and the final sample was weighed by age group, gender and location.

See also: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, pp. 148-149: 'Once consumers have chosen a product, they do not continue to shop around... In the home loan market, a Queensland University of Technology survey found that 61% of consumers had not considered switching their home loan in a five-year period (Silva-Goncalves 2015 [Dr Juliana Silva-Goncalves, Queensland University of Technology on behalf of Heritage Bank, *Australians' switching behaviour in banking, insurance services and main utilities*, September 2015]).'

We note that consumer surveys conducted in recent years show that around 4 to 6% of borrowers switched home loan lenders annually (see section 1.2), indicating that many borrowers do not appear to follow through on their intention to switch lenders.

There are many reasons why a borrower may not engage in the home loan market to look for an alternative home loan offer (see examples in chapter 1). We consider two significant reasons for this lack of engagement to be:

- many borrowers presume that they ‘*probably won’t save much*’ by switching lenders⁶⁹
- once a home loan is established, many borrowers are not compelled to consider switching unless they experience a major change in circumstance (for example, moving house). Outside these major changes, many borrowers are not prompted to consider whether they could benefit from switching lenders.⁷⁰

A presumption of limited savings from switching deters borrower engagement

One of the top three reasons provided by respondents to the 2017 Customer Owned Banking Association survey (referred to above) to describe why they were not considering switching lenders was that they ‘*probably won’t save much*’.⁷¹ This is consistent with the Productivity Commission’s finding that:

*For many financial products, consumer responses to variations in price and service are limited. Consumers lack meaningful transparent information and face switching barriers; and they **perceive insufficient ongoing difference between providers and product offerings to make the process worthwhile** (emphasis added).⁷²*

We consider that opaque discretionary discounts, which make it difficult for borrowers to discover the best prices offered (see section 3.1), may be one factor affecting borrowers’ assessment of the benefits of switching.⁷³

A presumption that there are limited benefits from switching, when combined with the real or perceived difficulty of switching,⁷⁴ likely explains why many borrowers have expressed the view that it is ‘*not worth the effort/paperwork*’.⁷⁵ Our recommendation in section 2.2 seeks to address these issues by providing a prompt with personalised potential savings. This is designed to lead borrowers to question their presumptions by engaging in the home loan market to see if there may in fact be better offers available to them that will generate meaningful savings.

69 BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, p. 8.

70 See also: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 163: ‘...consumers often require a ‘trigger’ to prompt them to search for an alternative. These triggers usually take the form of external events, rather than being built into a regular schedule.’

71 BLACKMARKET research, *Project: Switch—Financial/Banking Institution Survey*, January 2017, pp. 3, 8. The survey question, which only ‘non-considerers of switching’ were asked to provide a response to, was: ‘Which of the following reasons best describes why you are not considering changing your home/investment loan provider?’. The available reasons were ‘Happy with current provider’, ‘Probably won’t save much’, ‘Not worth the effort/paperwork’, ‘All banks are the same’ and ‘Just could not be bothered’. The survey was conducted online from 9 to 12 January 2017 and is based on 1,009 Australian adults.

72 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 164 (Finding 5.1).

73 See also: Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 7.

74 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 163: ‘Consumers can also be deterred from switching [financial products] because they **perceive** the process to be costly or difficult... These perceptions are not always accurate, as consumers often overestimate the cost or difficulty of switching. According to Fraser (2011, p. 4), ‘the perceived hassles involved in these processes by prospective switchers are usually greater than the problems experienced by people actually making switches’ (original emphasis).

75 BLACKMARKET Research, *Project: Switch—Financial/Banking Institution Survey*, January 2017, pp. 3, 8. The survey question which only ‘non-considerers of switching’ were asked to provide a response to, was: ‘Which of the following reasons best describes why you are not considering changing your home/investment loan provider?’. The available reasons were ‘Happy with current provider’, ‘Probably won’t save much’, ‘Not worth the effort/paperwork’, ‘All banks are the same’ and ‘Just could not be bothered’. The survey was conducted online from 9 to 12 January 2017 and is based on 1,009 Australian adults. See also: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 156: ‘Consumers have limited resources (in terms of time, money and energy) to allocate to a variety of tasks and responsibilities. According to CHOICE, many consumers do not switch because the cost of doing so is too high... 36% of people who had not switched said switching was ‘too much hassle’...’.

Most borrowers are not regularly prompted to consider switching lenders

Most borrowers are not regularly prompted to consider whether they would benefit from switching lenders.⁷⁶ Many borrowers can ‘set and forget’ their home loan once it is approved and automatic repayments begin.⁷⁷

We consider this is more likely to occur among borrowers with variable rate home loans, in particular with principal and interest repayments, which is the most common type of home loan in Australia.⁷⁸ In contrast, the end of a fixed rate term, or interest-only term, can be a prompt for a borrower to reassess the suitability of their loan and the possibility of there being better offers available. For example, the big four banks contact their fixed rate borrowers, in some cases on multiple occasions and via multiple channels, prior to the expiry of their fixed rate term, alerting the customer that their fixed rate will automatically ‘roll over’ to a variable rate upon expiry. In addition, three of the four big four banks set out alternative options that the borrower could take up on the expiry of their fixed rate, such as taking out another fixed rate period. The United Kingdom’s Financial Conduct Authority attributes the ‘high level of engagement in the [United Kingdom] mortgage market’, in part, to the fact that most borrowers have fixed rate home loans and therefore receive a prompt to consider switching as they approach the end of their fixed rate term.⁷⁹

This is not to say that other borrowers are never prompted to consider whether they could benefit from switching lenders. Seeing a better advertised price or incentive such as a cashback offer, an unsolicited offer of a better deal, dissatisfaction with their existing lender, a lender not fully ‘passing on’ a cut to the cash rate or an ‘out of cycle’ rate increase (particularly if accompanied by press coverage) could all act as prompts for borrowers to consider switching (or to ask their existing lender for a better deal) (see section 1.1).⁸⁰ However, for many borrowers, these events may not be observed or not be sufficiently compelling to prompt action. Further, for borrowers who have been disengaged for some time, these irregular external events could be seen as not directly affecting their home loan, and therefore do not prompt them to take action. The remaining large proportion of borrowers with older home loans, despite the increase in switching in the first half of 2020, indicates this is the case for many borrowers.

Our recommendation in section 2.2 seeks to address the lack of compelling prompts for variable rate borrowers, particularly those who are disengaged, by mandating a prompt designed to encourage borrowers with older home loans to consider whether they would benefit from switching.

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- 76 Australian Securities and Investments Commission, *Productivity Commission Inquiry into competition in the Australian financial system: Submission by the Australian Securities and Investments Commission*, September 2017, p. 74: ‘The long-term nature of many financial products and services means there is often no clear prompt for consumers to regularly review or compare their current product with others on the market (e.g. home loans).’
Customer Owned Banking Association, *Submission to Productivity Commission Inquiry into Competition in the Australian Financial System*, 15 September 2017, p. 35: ‘Factors that affect customers’ awareness and capacity to switch include the lack of natural trigger points to look around and the perception that the benefit of switching is minor, particularly compared to the costs.’
Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 163.
- 77 Behavioural Economics Team of the Australian Government, Department of the Prime Minister and Cabinet, *Credit when it’s due: Timely reminders help consumers reduce their credit card debt*, March 2019, pp. 7–8: ‘In finance, many consumers benefit from “set and forget” payments such as direct debit, which allow them to make regular payments without having to remember to do so every time. While this can be beneficial in many ways, the tendency to stick with our usual course of action can also mean consumers miss out on benefitting from changes’.
- 78 Variable rate home loans with principal and interest repayments account for about 55% of all home loans.
Source: Reserve Bank of Australia, ‘Box D: Distribution of variable housing interest rates’, *Statement on Monetary Policy*, November 2019, p. 59.
See also: S&P Global Ratings, *An Overview of Australia’s Housing Market And Residential Mortgage-Backed Securities*, 14 November 2019, p. 28.
- 79 Financial Conduct Authority, *Mortgages market study: interim report*, pp. 44, 47–48.
- 80 See also:
Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 64–65.
Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 163.
Australian Bankers’ Association Inc, *Inquiry into Competition in the Australian Financial System*, 15 September 2017, p. 66.
Deloitte, *Open banking: Switch or Stick? Insights into customer switching behaviour and trust*, October 2019, p. 57.

2.2 Variable rate borrowers with older home loans need a compelling prompt to engage in the home loan market

The behaviour of borrowers, and in particular their level of engagement in the home loan market, plays an important role in imposing a competitive constraint on lenders. In particular, if a borrower is disengaged and remains on their current home loan without exploring alternative options available in the market, their existing lender is not incentivised to compete for them.⁸¹

As discussed in chapter 1, increased switching could result in savings for individual borrowers, and generate demand-side pressure on lenders. Demand-side pressure encourages lenders to innovate and offer better products and lower prices to attract and retain borrowers. Increased switching could also benefit those borrowers who do not switch. A credible threat of switching can be enough for lenders to improve their product offerings, including by lowering prices, so that their borrowers do not switch, or consider switching, to a different lender (see section 1.2).

Lenders profit when their existing borrowers have limited incentives to shop around.⁸² We expect that lenders generally have little, if any, incentive to prompt their existing borrowers to consider whether they could benefit from switching lenders. Prompting borrowers to do so could result in them switching to a different lender and result in lower revenue for the existing lender.

As it does not appear feasible to rely on all lenders to provide a meaningful prompt to their variable rate borrowers to consider whether they could benefit from switching to another lender, we consider a regulatory intervention is required to mandate that lenders provide prompts to these borrowers with older home loans. To ensure such an intervention is effective in encouraging engagement in the home loan market, the prompt must be compelling enough to cause borrowers to question any presumption of limited savings from switching or that engaging in the home loan market is not worth the effort.

We recommend that the prompt:

- be provided directly to borrowers
- communicate the potential benefits of switching in a compelling and personalised way, including a comparison between the borrower's existing interest rate and the average interest rate paid for new loans similar to the borrower's
- set out the next steps for borrowers to look for a better home loan offer.

Consumer testing and trials should be undertaken to determine the optimal design of the prompt in order to achieve these objectives.

The prompt should be provided to variable rate borrowers with loans originated three or more years ago on an annual basis. As discussed above, many borrowers with loans originated three or more years ago are paying significantly higher interest rates than borrowers with new loans and would benefit from receiving a personalised prompt.

We do not recommend that the prompt be provided to borrowers with a fixed rate loan, including borrowers with a home loan split between a fixed and variable rate. As noted above, borrowers with fixed rate loans are prompted at the end of the fixed rate term to consider their home loan options, for example by being notified that their fixed rate will automatically 'roll over' to a variable rate upon expiry (see section 2.1 above). Further, there may be significant break fees for borrowers with fixed rate loans who refinance before the end of the fixed rate term.

81 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, pp. 8, 33. See also: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, pp. 146-147.

82 See also: Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 6.

The prompt should be provided directly to borrowers with variable rate home loans

For products lacking natural review points, where consumers often go ‘for many years without ever being prompted to make a conscious choice about whether to continue or switch provider’, evidence suggests that a prompt containing salient information incentivising them to review their current arrangements and consider switching is an effective way to increase consumers’ willingness to engage.⁸³ For this reason, we recommend that lenders provide their borrowers with variable rate home loans older than three years with a prompt.⁸⁴

We consider that providing the prompt to all eligible borrowers at the same time of year (i.e. during the same month) would facilitate effective messaging from regulators and associated media coverage about why borrowers are receiving the prompt and the benefits of engaging in the home loan market. Regulators will have an important role to play, at least initially, in raising borrowers’ awareness of the new prompt, the reasons why borrowers are receiving it and how borrowers should interpret and use the information in the prompt. In particular, regulators explaining that borrowers are receiving the prompt due to a regulatory or government initiative could help to ‘provide context and reassurance about the reason for the prompt’ and to ‘convey the notion of impartiality and independence’.⁸⁵ We suggest the prompt itself should also include an explanation of why the borrower is receiving it.

Consultation with industry should be conducted to understand the impact that the timing of the prompt (the same time of year for all borrowers or, alternatively, loan anniversary dates) would have on lenders, in particular smaller lenders.

We suggest that lenders be required to provide the prompt to borrowers in the same way they send home loan statements, for example via internet banking, email or post, but provide it separately to those statements. We note that consumers are generally most responsive to receiving prompts via channels that provide credibility and also reflect how they tend to engage with their banking affairs.⁸⁶

The prompt should communicate the potential benefits of switching in a compelling and personalised way

The information in the prompt needs to be compelling to attract borrowers’ attention. Some consumers pay little attention to periodic communications received from their bank.⁸⁷ Further, the prompt will need to compete for borrower’s attention among a ‘constant barrage of information from a wide variety of different sources [in relation to various aspects of their life]... or risk being drowned out and hence not having the anticipated benefits’.⁸⁸ A prompt is likely to be compelling to a borrower if it contains

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- 83 Competition and Markets Authority, *Retail banking market investigation final report*, 9 August 2016, p. xxxix. See also: Decision Technology Limited prepared for the Financial Conduct Authority, *FCA prompts and alerts design: Behavioural evidence*, April 2018, <https://www.fca.org.uk/publication/research/fca-prompts-and-alerts-design-behavioural-evidence.pdf>, p. 31. Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 163.
- 84 Research indicates that a consumer’s existing supplier is perceived as ‘the most relevant, trusted and expected sender’ of a prompt, and assurance of the prompt’s origin increases the likelihood that consumers will engage with the prompt. Source: Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, https://assets.publishing.service.gov.uk/media/56dd710ded915d0376000008/Qualitative_report_of_findings_prepared_by_Optimisa.pdf, pp. 6, 23.
- 85 Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, pp. 6-7.
- 86 Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, pp. 46-47.
- 87 Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, p. 38.
- 88 Financial Conduct Authority and the Competition and Markets Authority, on behalf of the UK Competition Network, *Helping people get a better deal: Learning lessons about consumer facing remedies*, October 2018, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/744521/UKCN_consumer_remedies_project_-_lessons_learned_report.pdf, p. 25. See also: Australian Securities and Investments Commission and Dutch Authority for Financial Markets, *REP 632 Disclosure: Why it shouldn’t be the default*, 14 October 2019, p. 20.

personalised insights that clearly show the potential benefits the borrower could derive from engaging in the home loan market and reassessing their choice of home loan.⁸⁹

Although borrowers choose their home loan, and will choose to stay with their existing lender for a number of reasons, price is generally the primary motivation for a borrower to switch home loans.⁹⁰ All of the big four banks hold evidence that price is a major motivator when borrowers switch. For example, an internal document of one of the banks records that 75% of borrowers who switched away from the bank were 'price driven'. Another bank informed the ACCC that '*the principal measure used by the Bank to improve consumers' willingness or ability to [s]witch to the Bank is by making changes to [the Bank's] Headline Interest Rate*'. Given this, and to make the prompt compelling to as many borrowers as possible, we recommend that the prompt include an interest rate comparison (as interest rates are generally the most significant component of the price of a home loan). We recommend that the prompt provide the borrower with details of:

- their current interest rate
- the average interest rate paid for new loans similar to the borrower's loan.

The average interest rate paid for new loans based on loan-type (owner-occupier or investor) and repayment-type (principal and interest or interest-only) is currently available on the Moneysmart Mortgage calculator (see box 2.2).⁹¹

89 See also: Decision Technology Limited prepared for the Financial Conduct Authority, *FCA prompts and alerts design: Behavioural evidence*, April 2018, p. 31.

90 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 147, '*In many instances, the 'best deal' is determined by price. For example, consumers consistently report that price is the most important factor when choosing a home loan (Deloitte 2016a). This implies that the availability of lower-priced products should be a strong motivator of consumer switching*'.
Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 16.
BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, p. 6: '*Among those considering switching, lower interest rates and lower fees are key factors when considering changing loan providers*'.

91 See: Moneysmart, 'Mortgage calculator', <https://moneysmart.gov.au/home-loans/mortgage-calculator>, viewed 29 October 2020.

Box 2.2: The average interest rate for new loans on the Moneysmart Mortgage calculator

In March 2020, the Moneysmart Mortgage calculator was enhanced to include information on average interest rates for new loans across loan and repayment types. To access the average interest rate, a consumer inputs a loan type (owner-occupier or investor) and a repayment type (principal and interest or interest-only) and the calculator reports the average interest rate for new home loans in the most recent available month with those characteristics. The average interest rates for new loans is also currently available on the Moneysmart 'Switching home loans' web page.

Figure 2.2: The Moneysmart Mortgage calculator*

The screenshot shows a web interface titled "My interest rate". Below the title, it says "Choose your loan and repayment types to see the average interest rate for new home loans in September 2020". There are three input fields: "Loan type" with a dropdown menu showing "Owner occupier", "Repayment type" with a dropdown menu showing "Principal and interest", and "Avg interest rate September 2020" which displays "2.62%".

* Consumers can select a loan type and repayment type from the drop-down boxes provided.

Source: Moneysmart, 'Mortgage calculator', <https://moneysmart.gov.au/home-loans/mortgage-calculator>, accessed 12 November 2020.

The average interest rates are weighted averages based on the Economic and Financial Statistics data collection, which accounts for around 95 per cent of total housing credit outstanding.⁹² The average interest rate data are also currently published on the RBA's website.⁹³

The Council of Financial Regulators and the ACCC developed the enhancements to the Mortgage calculator following the Productivity Commission's recommendation that ASIC develop an online calculator that reports median interest rates for loans issued according to different combinations of loan and borrower characteristics.⁹⁴ The purpose of the recommendation was to address the lack of transparency around interest rates actually paid by borrowers, as the '*absence of readily available data on interest rates paid by borrowers in relation to their mortgages had been highlighted as one factor impinging on competition in the Australian financial system*'.⁹⁵

Given the gap between interest rates on new loans and loans older than three years (see section 2.1 above), we expect that a comparison between a borrower's existing interest rate and the average interest rate paid for similar new loans would convey that it is worthwhile for them to engage in the home loan market to see whether they could benefit from switching.

92 Megan Garner, Reserve Bank of Australia, 'Insights from the New Economic and Financial Statistics Collection', *Bulletin—September 2020*, <https://www.rba.gov.au/publications/bulletin/2020/sep/pdf/insights-from-the-new-economic-and-financial-statistics-collection.pdf>, p. 51.

The data is collected from all ADIs (including banks, building societies and credit unions) and APRA registered financial corporations.

Source: Australian Prudential Regulation Authority, Modernised economic and financial statistics, July 2019, <https://www.apra.gov.au/modernised-economic-and-financial-statistics>, viewed 29 October 2020.

93 See: Reserve Bank of Australia, 'Lenders' Interest Rates', <https://www.rba.gov.au/statistics/interest-rates/> (Statistical Table F6—Housing Lending Rates), viewed 29 October 2020.

94 See: Megan Garner, Reserve Bank of Australia, 'Insights from the New Economic and Financial Statistics Collection', *Bulletin—September 2020*, p. 53.

95 Megan Garner, Reserve Bank of Australia, 'Insights from the New Economic and Financial Statistics Collection', *Bulletin—September 2020*, p. 53.
Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, chapter 12.

Many consumers are also responsive to what they perceive as unfair pricing or the concern that they are being ripped off.⁹⁶ In addition, social comparisons, such as what an identifiable peer group has compared to the consumer, can drive consumer behaviour.⁹⁷ We expect that providing borrowers with details of the average interest rate paid by borrowers with similar new loans would prompt many borrowers to engage in the home loan market and look into whether a better offer is also available to them (or at least call their existing lender to ask for a better offer).

Consumer testing and trials could identify the most compelling way to present this comparison information to borrowers. For example, infographics, such as a thermometer or traffic lights, could be used to visually present how the borrower's existing rate compares to the average rate paid for similar new loans.⁹⁸

We expect that a comparison between the borrower's existing interest rate and the average interest rate paid for similar new loans would be compelling to many borrowers. However, a further enhancement, in particular for those borrowers who presume there are limited savings from switching, could be the inclusion of an estimate of potential savings as a dollar figure. This would more clearly demonstrate for many borrowers that it is worthwhile for them to engage in the home loan market to see if a better offer is available. We recommend that three potential options for expressing dollar savings be consumer tested for inclusion in the prompt:

- the interest savings in the first year if the borrower switched to a loan with the same interest rate as the average rate for new loans (see box 2.3)⁹⁹
- the interest savings in the first year if the borrower's current interest rate was reduced by 25 basis points (or a similar round number that borrowers can, relatively easily, use to infer what savings might apply in their personal circumstances), assuming all other conditions of the loan remained the same
- generalised examples of potential savings available based on the average loan size across the market e.g. 'a typical borrower with a \$250,000 loan could save over \$600 in the first year if their interest rate was 25 basis points lower'.

Other options for presenting potential savings could also be developed during consumer testing.

We consider that the potential dollar savings over the first year is useful information to help a borrower decide whether it is worthwhile for them, given the costs of taking action (e.g. search costs and, potentially, switching costs, such as discharge fees), to engage in the home loan market.¹⁰⁰ As part of consumer testing, consideration should also be given to whether including an estimate of switching fees (for example, based on average discharge and establishment fees in the market) would assist borrowers with making a decision to engage in the home loan market to look for a better offer.

The potential savings information would be compelling for those borrowers who, because of the complexity of the calculation or a lack of awareness of available tools, such as the Moneysmart

96 Lan Xia, Kent B. Monroe and Jennifer L. Cox, *The Price Is Unfair! A Conceptual Framework of Price Fairness Perceptions*, <https://www.jstor.org/stable/pdf/30162012.pdf>, pp. 6, 7: '...perceived price unfairness increases buyers' price consciousness' and 'When buyers believe that an inequality in an exchange is unacceptable and are upset, disappointed, or regretful (if they believe that there is a better option), they may choose to complain, ask for a refund, spread negative word of mouth, and/or leave the relationship, depending on their assessment of which action is most likely to restore equity with the least cost. In addition, they may search for additional information to assess the potential switching costs or to assess their power to renegotiate with the seller.'

97 Behavioural Insights Team, *Applying behavioural insights to reduce fraud, error and debt*, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/60539/BIT_FraudErrorDebt_accessible.pdf, p. 22.

98 National Consumer Protection Service, *Redesigning the Mortgage Statement and its Impact on Consumers Mortgage Purchase Decisions: Experimental Evidence*, May 2020, pp. 12-13.
Decision Technology Limited prepared for the Financial Conduct Authority, *FCA prompts and alerts design: Behavioural evidence*, April 2018, p. 31.

99 We acknowledge there is the potential for a lag to occur between the date at which the average interest rate for new loans is calculated and the date on which lenders are able to deliver the prompt to borrowers. This could potentially skew the potential savings calculation contained in the prompt, for example in a scenario where headline interest rates change across the market. To mitigate the risk of this happening, we consider it would be prudent if lenders were required to issue the prompt as at a particular date with a minimal time lag from when the average interest rate for new loans is calculated.

100 See also: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 147 'The decision to shop around and switch products is motivated by whether the expected benefits of switching (such as financial gain or improved services) exceed the expected costs (such as search costs and the implicit and explicit costs of switching).'

Mortgage switching calculator,¹⁰¹ may otherwise struggle to transform interest rate differentials into tangible dollar savings. These borrowers may not otherwise comprehend the significance of potential savings available to them.¹⁰² Providing the potential savings would allow borrowers to immediately see what a lower interest rate could mean for them. Research suggests that highlighting costs and savings in dollar terms makes disclosures significantly more comprehensible for consumers, and more effective in influencing consumer behaviour, than providing interest rates alone.¹⁰³

Box 2.3: Example of how the potential interest savings could be calculated

We suggest that the estimate of the potential interest saved if the borrower switched to a loan with the average interest rate for new loans could be calculated by comparing:

- the projected interest the borrower would have paid, based on their current interest rate, over the year following the issuance of the prompt
- the interest the borrower would pay if the average interest rate for new loans were applied.

To simplify the calculation, it could be based on the following assumptions:

- the borrower makes only the minimum contracted repayments and the repayments are made on the contracted due date
- the loan repayments are adjusted to those necessary to repay the loan over its remaining term under the scenario where the borrower is assumed to be paying the average interest rate for new loans
- the borrower does not have an offset account and any redraw balances are not drawn down by the borrower
- interest is calculated in the same manner as it is calculated for the borrower's existing loan
- fees (switching fees and ongoing fees) are not included as part of the calculation.

We recognise that these assumptions are not tailored and will not apply to the circumstances of all borrowers. However the purpose of the prompt is not to convey the actual or guaranteed savings available to each individual borrower. Rather, the purpose is to compel action by providing an example of potential savings. We consider the assumptions above to be a reasonable basis for a calculation of potential savings. We suggest that the prompt include guidance for the borrower on how to interpret the average rate for new loans and the potential savings, including that these figures do not include any fees. As discussed above, as part of consumer testing, consideration should be given to whether including an estimate of switching fees (based on average discharge and establishment fees in the market) would further enhance the prompt.

Where a borrower is already paying an interest rate lower than the average interest rate for new loans, it would not be necessary to provide a calculation of the potential interest saved if the borrower switched to a loan with the average interest rate for new loans. We expect this scenario would only apply to a small proportion of borrowers with loans greater than three years old. We suggest that the prompt include guidance to the effect that a lower interest rate may still be available to these borrowers.

101 See: Moneysmart, 'Mortgage switching calculator', <https://moneysmart.gov.au/home-loans/mortgage-switching-calculator>, viewed 29 October 2020.

102 Australian Securities and Investments Commission, *Report 638: Consumer testing of the fees and costs tools for superannuation and managed investment schemes*, 29 November 2019, p. 7: Consumer testing found some people 'had very little experience working with information presented as percentages. The more percentages there were, the more confused they became. These readers needed concrete examples to make these percentages make sense'.

See also:

Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, p. 55.

The Behavioural Insights Team for Citizens Advice, *Applying behavioural insights to regulated markets*, 26 May 2016, p. 20.

103 The Behavioural Insights Team for Citizens Advice, *Applying behavioural insights to regulated markets*, 26 May 2016, p. 20.

Examples of prompts to encourage consumer engagement and switching that include potential better offers can be found in the Victorian energy market and the Irish home loan market (box 2.4). Another example can be found in Chile, where changes are proposed to mortgage statements to encourage consumer engagement and switching.¹⁰⁴ In respect of the most recent Irish reforms, which are prompts based on changes to the loan-to-value ratio, we consider that a comparison based on the average interest rate for new loans would be a more compelling prompt for Australian borrowers. There are a number of factors that can determine an Australian borrower's interest rate, in addition to loan to value ratio.

104 The Chilean National Consumer Protection Service (SERNAC) has recommended redesigning the *'Mortgage Statement'* (a statement designed by the regulator to reduce information asymmetries, which financial institutions must send to their customers every three months). The purpose of redesigning the Mortgage Statement is to *'motivate consumers on quoting, switching options and [facilitate] the understanding of the information provided in the financial market'*. SERNAC recommended that the redesigned statement include, among other things:

- a disclaimer that *'the information is forwarded by the financial institution in compliance with legal obligations, and that it was designed by SERNAC and the Ministry of Economy'* (this is to *'strengthen confidence in the message'*)
- *'a thermometer that indicates the distance between the average market interest rate -reported by the Central Bank in the month before the statement's issue date- and the interest rate applied to the debtor'* (this part of the 'nudge' *'considers the relevance of reference points or anchoring to stimulate decision-making'*)
- *'the amount in pesos that the person could save if s/he renegotiate their mortgage and manage to reduce their current interest rate by one percentage point, keeping all other loan conditions constant'* (this part of the nudge *'considers the power of loss aversion as an explanation for decisions'*)
- a *'step by step guide to compare and search for better mortgage offers'* (the objective of including this is to *'facilitate the use of the statement during the mortgage quoting process, allowing consumers to consider the next steps and encourage them to follow them'*).

An online survey experiment testing the effects of the redesigned statement *'suggested an increase of 23.3% (between 18.3–28.4% considering the marginal error) in the probability of quoting new loan offers in comparison to those exposed to the current statement'*. We note the SERNAC reported that *'a relevant part of the impact on the predisposition to quote is guided by the thermometer that reflects the distance between the interest rate on the consumers' loan and the average interest rate of the market. Nonetheless, it does not imply that the information on how much to save will not have an impact, but rather that the most significant impact occurs when the distance on the thermometer is larger.'*

Source: National Consumer Protection Service, *Redesigning the Mortgage Statement and its Impact on Consumers Mortgage Purchase Decisions: Experimental Evidence*, May 2020, pp. 2, 3, 4, 7–8 and 12–13.

Box 2.4 Example prompts to encourage engagement and switching

‘Best offer’ message on energy bills in Victoria

In 2018, the Victorian Government introduced reforms requiring electricity and gas retailers to provide their domestic and small business customers with ‘*genuinely helpful assistance in finding the most suitable energy deal for them*’.¹⁰⁵ The reforms came after an independent review highlighted that Victorian consumers had not been ‘*gaining the benefits of a competitive retail market*’.¹⁰⁶

Effective 1 July 2019, the reforms were intended to ‘*hold energy companies responsible for rebuilding customer trust, by requiring them to do more to help customers understand, compare and switch energy plans*’.¹⁰⁷

One of the reforms, known as the ‘*best offer*’ message, was designed to help customers assess the suitability of their energy plan. The best offer message includes requirements for energy retailers to tell customers, at least quarterly for electricity bills and at least every four months for gas bills, whether they are on one of the retailer’s best energy plans based on their usage and, where applicable, how much the customer could save by switching to the best energy plan with their retailer.¹⁰⁸ Where the customer is already on one of the retailer’s best energy plans,¹⁰⁹ the retailer is obliged to ensure it is clear to the customer that they are on one of the retailer’s lowest cost customer retail contracts,¹¹⁰ and to also include a link to a government price comparison website¹¹¹ so the customer can access offers from other retailers.

105 Essential Services Commission, ‘Energy regulator says energy reforms ‘a game changer’’, 30 October 2018, <https://www.esc.vic.gov.au/media-centre/energy-regulator-says-energy-reforms-game-changer>, viewed 10 August 2020.

106 Engage Victoria, ‘Independent Bipartisan Review of Electricity and Gas Retail Markets (background)’, <https://engage.vic.gov.au/review-electricity-and-gas-retail-markets-victoria>, viewed 10 August 2020.

107 Essential Services Commission, ‘Once-in-a-decade reforms to help engage customers find the best deal’, transcript, 30 October 2018, <https://www.esc.vic.gov.au/media-centre/once-decade-reforms-help-energy-customers-find-best-deal>, viewed 10 August 2020.

108 *Energy Retail Code*, Version 17, 1 October 2020, Division 4, sections 70R(1)–(4), pp. 87–88.

109 If the customer would save less than or equal to \$22 by switching, they are considered to already be on one of their retailer’s best energy plans. If the customer would save greater than \$22 by switching, they are considered not to be one their retailer’s best energy plans.
Source: *Energy Retail Code*, Version 17, 1 October 2020, Division 4, sections 70Q(1)–(3), p. 87.

110 *Energy Retail Code*, Version 17, 1 October 2020, Division 4, sections 70S (3)(a), p. 89.

111 The website is an independent Victorian Government energy price comparison site.
Source: State Government of Victoria, Department of Environment, Land, Water and Planning, ‘Welcome to Victorian Energy Compare’, <https://compare.energy.vic.gov.au/>, viewed 10 August 2020.
See also: *Energy Retail Code*, Version 17, 1 October 2020, Division 4, sections 70S (3)(b), p. 89.
See also: *Energy Retail Code*, Version 17, 1 October 2020, Part 1, Division 1, section 3, p.11 and Part 2A Division 4, sections p. 11 70S(3)(b), p. 89.

Irish mortgage reforms

In 2016, the Central Bank of Ireland introduced a number of information requirements for lenders to provide to their mortgage customers. These requirements include a summary of the lender's other mortgage products that could provide savings for the customer, a statement that the customer should keep their mortgage arrangements under review and a link to the relevant section of the Irish Competition and Consumer Protection Commission's website relating to switching lenders or changing mortgage type.¹¹² The website allows consumers to compare potential savings available from other lenders.¹¹³

In June 2018, the Central Bank introduced several further reforms to provide additional transparency and to facilitate mortgage switching.¹¹⁴ The reforms followed findings by the Central Bank that some customers were unaware that cheaper interest rates can become available to them as their loan-to-value ratio changed.¹¹⁵

The reforms included a requirement for lenders to notify their customers with variable rate mortgages every year as to whether they can, or cannot, move to a lower interest rate as a result of a move in their loan-to-value interest rate band, subject to the provision of an up-to-date valuation and any other requirements that may apply.¹¹⁶

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- 112 Central Bank of Ireland, *Addendum to Consumer Protection Code 2012*, July 2016, Chapter 6, Post-sale information requirements, provision 6.5 (g).
Central Bank of Ireland, Introduction of additional consumer protection measures for variable rate mortgage holders, 21 July 2016, <https://www.centralbank.ie/news-media/press-releases/additional-consumer-protection-measures-variable-rate-mortgage-holders> accessed 3 November 2020.
- 113 Competition and Consumer Protection Commission, 'Mortgages' (mortgage comparison tool), <https://www.cccp.ie/consumers/money-tools/mortgage-comparisons/>, viewed 25 September 2020.
- 114 Central Bank of Ireland, 'New Requirements Introduced to Provide Additional Transparency and Facilitate Mortgage Switching', 20 June 2018, <https://www.centralbank.ie/news/article/mortgage-switching-20-June-2018>, viewed 25 September 2020.
- 115 Central Bank of Ireland, 'New Requirements Introduced to Provide Additional Transparency and Facilitate Mortgage Switching', 20 June 2018, <https://www.centralbank.ie/news/article/mortgage-switching-20-June-2018>, viewed 25 September 2020.
Central Bank of Ireland, *Enhanced Mortgage Measures: Transparency and Switching Consultation Paper CP112*, August 2017, <https://www.centralbank.ie/docs/default-source/publications/consultation-papers/cp112/cp112-enhanced-mortgage-measures--transparency-and-switching.pdf?sfvrsn=2>, p. 6, 'While it is likely that a consumer's LTV [loan-to-value ratio] will change over the lifetime of their mortgage, consumers may not know if they can move between interest rate bands as their LTV changes, and what their lender's policy is on movement between bands.'
- 116 A consumer may not be permitted to receive a cheaper interest rate if the lender's policy does allow for movement between loan-to-value bands.
Source: Central Bank of Ireland, *Enhanced Mortgage Measures: Transparency and Switching Consultation Paper CP112*, August 2017, p. 7.
If the customer is permitted to move between loan-to-value interest rate bands, the lender is to invite the customer to contact them to discuss further. If the customer is not permitted to move between loan-to-value interest rate bands, the lender is to provide a notification to the customer that lower loan-to-value interest rate bands may be available from another lender.
The requirement does not apply to 'tracker' interest rates.
Sources:
Central Bank of Ireland, *Addendum to the Consumer Protection Code 2012*, June 2018, Chapter 6, Post-sale Information Requirements, Amendment to Provision 6.5, p. 7.
Central Bank of Ireland, 'New Requirements Introduced to Provide Additional Transparency and Facilitate Mortgage Switching', 20 June 2018, <https://www.centralbank.ie/news/article/mortgage-switching-20-June-2018>, viewed 25 September 2020.

Why an average interest rate for new loans is a good basis for the prompt

The purpose of including the average interest rate for new loans is to compel action, not to forecast or represent exactly what interest rate an individual borrower would be eligible for, or to suggest that the borrower consider switching to a particular lender or product. The average rate for new loans, which is currently available on the Moneysmart Mortgage calculator, is well suited to the intended purpose for a number of reasons:

- it utilises data that has '*greatly enhanced the transparency of interest rates paid by borrowers*' (see box 2.2)¹¹⁷ and is therefore likely to be a compelling prompt for those borrowers with older home loans paying interest rates well above those available on new loans (see section 2.1 above)
- it should support competition through switching by giving borrowers an insight into what may be available to them across all lenders, and a range of different products, not just from their existing lender
- using the average interest rate for new loans, rather than the lowest rate available for new loans, reduces the risk of a 'race to the bottom' among lenders, which could result in lenders focusing on offering the lowest price at the expense of offering other product or service features that borrowers value. It also reduces the risk of borrowers being prompted to only consider a particular product or lender
- having the information on the average rate actually paid for new loans to hand may help borrowers negotiate with their existing lender, or other lenders, as borrowers will have an idea of the actual rates in the market and how their rate compares.¹¹⁸

As part of the ACCC's ongoing monitoring role (recommendation 4), the ACCC would monitor whether the introduction of the prompt and the use of the average interest rate for new loans in the prompt is having any unintended consequences on prices, such as lenders' offers converging around the average rate for new loans or lenders reducing interest rates, but increasing fees.¹¹⁹

Feedback from industry associations on the use of an average interest rate for new loans and the potential savings

The Australian Banking Association and the Customer Owned Banking Association¹²⁰ do not consider that a comparison to an average rate for new loans is informative for borrowers or results in good consumer outcomes as there are many factors that need to be considered for a 'like for like' comparison between interest rates to be made.¹²¹ We note that the purpose of the prompt is not to provide a strictly 'like for like' comparison, as the prompt is not intended to recommend that borrowers switch to a particular alternative product. As discussed above, the purpose of the prompt is to compel action

117 Megan Garner, Reserve Bank of Australia, 'Insights from the New Economic and Financial Statistics Collection', *Bulletin—September 2020*, pp. 51, 53.

118 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, pp. 348, 356.

119 We note that FinTech Australia raised concerns that if '*a simple headline rate is used (and not comparison rates) consumers may be misled and some lenders may 'game' the system by quoting rates that understate the true cost of credit*'.

120 As set out in the Introduction, the ACCC consulted with the Australian Banking Association, the Customer Owned Banking Association and FinTech Australia in respect of a prompt recommendation. The prompt recommendation that was consulted on was different to the currently recommended prompt in several ways, including (1) it was proposed to be sent to all variable rate borrowers and (2) it was proposed to include the first of the potential dollar savings options presented in this report—an estimate of the interest savings in the first year if the borrower switched to a loan with the same interest rate as the average rate for new loans (see box 2.3). The changes made to the prompt recommendation reflect feedback from industry associations and other stakeholders.

121 For example, the Australian Banking Association stated that '*[t]here are many factors other than an interest rate that need to be considered for a like-for-like comparison to be made, such as the size of the loan, features of the product offered (e.g. offsets), or other factors such as lender policies or solutions (e.g. bridging loans, parental leave policies, borrowing capacity). Asking customers to compare their loan interest rate to an average interest rate for new loans may result in customers not considering the full value or other benefits they are receiving from their current product (which extends beyond price)*'.

For example, the Customer Owned Banking Association stated that '*COBA members say the notion that variable rate loans should be bucketed together using only two criteria, owner-occupier or investor and P&I or interest-only, is overly simplistic and will lead to unnecessary confusion for borrowers as they compare 'apples with oranges'*'.

We note that similar arguments ('*it was suggested that the information produced by a calculator would be too much of an aggregate rate to benefit consumers and potentially be misleading*') were made by stakeholders in response to the Productivity Commission's draft recommendation that ASIC develop an online calculator that reports median interest rates for loans issued according to different combinations of loan and borrower characteristics.

Source: Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 2018, pp. 359–360.

by encouraging borrowers to engage in the home loan market to see whether they could benefit from switching lenders or home loan products. Further, providing the average rate for new loans will provide transparency to borrowers around interest rates actually paid on new loans and assist borrowers in making more informed choices about their home loan.¹²² Borrowers having greater visibility over actual interest rates paid may also encourage lenders to present their best prices more readily (see section 3.3). Further, it may also encourage lenders to proactively offer better prices to borrowers with older home loans to reduce the risk of them switching to another lender.

The Australian Banking Association and the Customer Owned Banking Association each raised a number of additional concerns about the prompt, including considering that:

- the prompt would be misleading as borrowers might interpret the average interest rate, or associated savings estimate, as a 'guaranteed' figure, or even an offer from their existing lender¹²³
- *'[p]roviding a nudge or guidance to customers solely on price, and not cognisant of other product features that may suit (or offer greater value to) the customer's individual circumstances, may in fact be financially detrimental to the customer'*¹²⁴
- the prompt does not take into account the potential impact of fees should the borrower choose to switch, or the availability of offset accounts.¹²⁵

FinTech Australia members, including lenders, support an annual prompt for variable rate borrowers provided by lenders. However, FinTech Australia advocated for the use of comparison rates, which include fees, in the prompt.¹²⁶ For the reasons set out above, the ACCC's position is that an average interest rate for new loans is well suited to the intended purpose of the prompt—to encourage borrowers to engage in the home loan market to see if they could benefit from switching. Further, the average interest rate information is already being collected and is currently publicly available (see box 2.2).

We recognise that the average interest rate for new loans will not indicate the best interest rate available for all borrowers. Some borrowers, depending on their characteristics and choice of product, would be able to obtain a rate lower than the average rate and others, due to their risk profile, would only have access to loans with a higher interest rate. This creates a risk that:

- some borrowers may be prompted to begin looking for a new offer but become disengaged again if they are unable to find a better offer or an offer with a rate as low as the average rate for new loans
- other borrowers, who are already paying a rate close to or below the average for new loans, may see the average rate in the prompt as confirming that they are already on a good rate or that they *'probably won't save much'* by switching lender.¹²⁷ These borrowers may therefore be deterred from engaging in the home loan market. However, we expect that most borrowers with loans greater than three years old will be paying a rate higher than the average rate for new loans.

122 See also: Megan Garner, Reserve Bank of Australia, 'Insights from the New Economic and Financial Statistics Collection', *Bulletin—September 2020*, pp. 51, 53. *'The EFS [Economic and Financial Statistics] collection has greatly enhanced the transparency of interest rates paid by borrowers in Australia, which assists consumers in making better informed choices about their finances. The absence of readily available data on interest rates paid by borrowers in relation to their mortgages had been highlighted as one factor impinging on competition in the Australian financial system (Productivity Commission 2018).'*

123 For example, the Australian Banking Association stated that it was *'concerned that the [prompt] has the likelihood of confusing and misleading consumers. It is in a prescriptive form which implies that a consumer is in fact entitled to and can switch to the new product at the average rate or price' and 'members are concerned that their customers may receive the annual nudge and expect that they are entitled to the 'average rate''*. For example, the Customer Owned Banking Association stated that the prompt *'could mislead borrowers into thinking they are being made an offer' and 'Providing borrowers with an estimate of the interest they would save if they switched to a lower-rate home loan implies they are entitled to that lower-rate home loan. This may not be the case.'*

124 Quote from Australian Banking Association.

125 For example, the Australian Banking Association stated *'[the potential savings calculation does not] take into account a range of other relevant factors that could significantly impact any savings that might arise, including for example, differences in fees between the products or the availability of features such as offset accounts...'*

126 FinTech Australia advocated for the use of comparison rates in the prompt *'to ensure informed decisions by borrowers in their interest rate decisions and prevent lenders from hiding the true cost of credit in fees and charges or via introductory rates that later increase' and to avoid the prompt causing borrowers 'to switch to a supposedly lower rate which is not actually in their best interests because of fees that are not reflected in the rates disclosed'*.

127 BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017, p. 8.

To manage these risks and the risks identified by the industry associations, we recommend that the prompt contain guidance for borrowers on:

- how to interpret the average interest rate and potential savings, including that:
 - the prompt is not an offer for a new loan or discount
 - not all borrowers will be eligible for a home loan with a lower rate than their existing loan or able to obtain the potential savings, as the total cost of a loan and a borrower's eligibility for a loan or interest rate depends on many factors, including the type of loan and the borrower's risk profile
 - borrowers who are already paying a rate lower than the average rate for new loans may still be eligible for a home loan with a lower interest rate¹²⁸
- next steps to look for a better home loan offer, including that borrowers should consider interest rates, product features and fees, including switching fees, when comparing home loans and before deciding to switch.

These messages will need to be consumer tested to ensure they are easily understood and do not inadvertently undermine the potential benefits of switching or deter borrowers from engaging in the home loan market.¹²⁹

The prompt should set out the next steps for borrowers

For the prompt to be effective in compelling borrowers to engage in the home loan market to see if they could benefit from switching, it needs to clearly set out what a borrower needs to do after they have read the prompt and encourage them to take action.¹³⁰ Research has found that '*[w]hen people are informed of the benefits or risks of engaging in certain actions, they are far more likely to act in response to that information if they are simultaneously provided with clear, explicit information about how to do so.*'¹³¹

Research has shown that the likelihood that consumers follow through on their intention to search for or switch financial products increases if they are provided with details of what sources they can consult for further information and reassurance around the switching process itself.¹³² We suggest that including the following information in the prompt would help borrowers to take action:

- a link to the Moneysmart website, in particular to the site's '*Switching home loans*' page.¹³³ Providing a link means that borrowers can access further information and guidance on switching at a time that is suitable for them
- encouragement for borrowers to contact their existing lender to ask them for a better rate. This will likely be a less daunting, and less costly, first step for a borrower than looking for another lender. If an existing lender does not offer the borrower a better rate, the borrower can then embark on a broader search to assess what other deals are available in the market. A lender not agreeing to

128 We note that FinTech Australia expressed a view that '*receiving the notification (even if their rate is lower than the average new loan rates) would assist borrowers to remain engaged and know how competitive their rate is*'.

129 The Australian Banking Association stated that it '*considers the number of assumptions required and associated disclaimers that will need to be attached to the proposed annual ACCC nudge, may overwhelm and confuse customers and negate the original purpose of the nudge*'. We note that consumer testing and trials are proposed to mitigate the risk that borrowers do not engage with the prompt as intended.

130 Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, p. 7. See also: Timmons, S. et al, *Official advice improves mortgage-holders' perceptions of switching: experimental evidence*, Behavioural Public Policy, p. 1. Decision Technology Limited prepared for the Financial Conduct Authority, *FCA prompts and alerts design: Behavioural evidence*, April 2018, p. 18.

131 Cass R. Sunstein, Empirically informed regulation, *The University of Chicago Law Review*, 78(4), 1352: <https://chicagounbound.uchicago.edu/cgi/viewcontent.cgi?article=5551&context=uclev>.

132 Optimisa Research prepared for the Competition and Markets Authority, *Informing the development of communication tools designed to increase consideration of switching among PCA and SME customers*, March 2016, p. 7.

133 This page provides a short overview of what borrowers should consider before switching and advice for borrowers about asking their existing lender for a better deal. See: Moneysmart, 'Switching home loans', <https://moneysmart.gov.au/home-loans/switching-home-loans>, viewed 29 October 2020. We note that 90% of users reported taking action on their finances after visiting the Moneysmart website. Source: Australian Securities and Investments Commission, *Annual Report 2017-18*, p. 24.

provide a better offer may also act as a further prompt for the borrower to engage in the switching process. The prompt could also encourage borrowers to contact their mortgage broker

- references to the experience of borrowers who have switched. For example, '*X% of consumers rated switching banks as 'easy' in survey X*'.

These suggestions will need to be consumer tested, to ensure that the information is useful to and understood by borrowers, and does not have any unintended consequences, such as causing confusion, undermining the potential benefits of switching lenders or deterring borrowers from engaging in the home loan market.

Ensuring the prompt does not create an undue regulatory burden

Although the final form of the prompt has not yet been determined (as consumer testing and trials are required), we note that both the Customer Owned Banking Association and the Australian Banking Association raised concerns about the compliance burden it would create.¹³⁴ On the other hand, FinTech Australia noted that the prompt would be '*simple and practical and can readily be implemented*'.

► Recommendation 1: A prompt for variable rate borrowers

All lenders should be required to provide borrowers with variable rate loans originated three or more years ago with an annual prompt to encourage borrowers to engage in the home loan market to see if they could benefit from switching lenders or home loan products.

The prompt should:

- be provided directly to borrowers
- communicate the potential benefits of switching in a compelling and personalised way, including a comparison between the borrower's current interest rate and the average interest rate paid for new loans similar to the borrower's loan
- set out the next steps for borrowers to look for a better home loan offer.

Consumer testing and trials should be undertaken to determine the optimal design of the prompt.

¹³⁴ As set out above, the prompt recommendation that was consulted on was different to the currently recommended prompt in several ways, including (1) it was proposed to be sent to all variable rate borrowers and (2) it was proposed to include the first of the potential dollar savings options presented in this report—an estimate of the interest savings in the first year if the borrower switched to a loan with the same interest rate as the average rate for new loans.

For example, the Customer Owned Banking Association stated that '*The ACCC's proposal... would impose significant compliance costs...*' and '*Implementation costs and ongoing compliance costs implied by [the prompt] recommendation include changes to IT systems, processes, communications and staff training. These costs are also opportunity costs because they divert resources away from other priorities*'.

The Australian Banking Association stated that '*the ABA is concerned about the cost and complexity involved and compliance burden placed on lenders should they be required to calculate the interest each customer would potentially save in the first year assuming they switched to a product with the average interest rate for new loans*'.

3. Being able to ascertain and assess home loan prices

Key findings

- The ability to ascertain, compare and assess home loan prices is an important stage in a borrower's switching journey. However, discretionary discounting practices among lenders mean that borrowers often lack access to transparent and easily understood home loan price information.
- The use of discretionary discounts creates an information asymmetry between lenders and borrowers about how actual prices are determined. Borrowers do not have access to the same information as lenders about the factors that determine discretionary discounts, and ultimately determine the final price that will be offered. This is, at least in part, because lenders do not publish their respective discretionary discounting eligibility criteria and the potential size of the discounts available pursuant to this criteria.
- The opaque nature of discretionary discounts means that borrowers incur significant search costs to discover a given lender's home loan price. Before discovering a lender's price, borrowers are usually required to submit a home loan application and have the application assessed and approved by a lender. To obtain multiple price quotes, this process must be repeated with each lender.
- The existence of information asymmetry and unnecessarily high search costs reduces the likelihood that borrowers will obtain the best price for their circumstances.
- The potential harm to borrowers from opaque pricing remains a concern for the ACCC. However, over the price monitoring period (from 1 January 2019 to 31 December 2019), we have observed two of the big four banks reducing or considering reducing their reliance on discretionary discounting to provide more price transparency to borrowers. This move towards greater price transparency has occurred without direct regulatory intervention.
- We consider that the recent moves by some lenders towards more transparent pricing means that further direct regulatory intervention is not required at this stage. Other market developments (including the prompt recommended in chapter 2 and the Consumer Data Right, which will reduce search costs) will also facilitate greater price transparency.
- If, during continued monitoring of competition and prices in the home loan market (recommendation 4), we find that the momentum towards price transparency stalls or we observe consumer harm associated with a lack of price transparency, we will consider making recommendations to Government to address this.

In this chapter, we report on:

- the difficulty borrowers face in accessing simple and transparent home loan price information
- the potential for borrowers to pay higher prices as a result of unnecessarily high search costs and information asymmetry
- recent developments towards greater price transparency, which we consider will, if they continue, reduce the harms currently associated with opaque home loan prices
- the proposed regulatory interventions that the ACCC could consider recommending if we find that momentum towards price transparency has stalled.

3.1 Borrowers cannot easily access simple and transparent home loan price information

In both our Residential mortgage price inquiry and the interim report, we found that borrowers do not have easy access to transparent pricing information about home loans, and that this is primarily caused by the presence of opaque discretionary discounts.¹³⁵

The Productivity Commission expressed a similar view, noting that '*actual home loan interest rates and the discounts offered on the SVR [standard variable rate] are generally not easily and simply made available to consumers*'.¹³⁶

Discretionary discounting is a feature of the home loan pricing practices of many lenders, including the big four banks (see box 3.1).

Box 3.1: Advertised and discretionary discounts in home loan interest rates

There are two types of discounts offered by home loan lenders: advertised discounts and discretionary discounts.

- Advertised discounts are generally published on the lender's website and are relatively easy for borrowers to discover. The discount available to borrowers when they take their home loan as part of a package¹³⁷ is one of the more common advertised discounts available from the big four banks.
- Discretionary discounts (also referred to as unadvertised discounts) are offered by lenders at their discretion and on a case-by-case basis to individual borrowers. As a result, discretionary discounts are less easily discovered by borrowers compared to advertised discounts.

Not all borrowers will be eligible for a discount, nor will all borrowers be willing to agree to the terms on which a lender offers a discount.

The history of advertised and discretionary discounts

Advertised and discretionary discounts have not always been a feature of home loan pricing by the big four banks.¹³⁸ The ACCC understands that the advertising of discounts associated with a home loan package arose during the late 1990s. Such packages were generally targeted at high-income professionals such as those in the accounting, legal and medical sectors, and high-wealth individuals. Advertised discounts offered as part of a package were generally available for people who qualified, and were not discretionary in amount. By the mid-2000s, packages, including advertised discounts, were targeted towards the wider public, with the big four banks aiming to consolidate all the products a consumer may need into one bundle.

135 Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 8–9.
Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, p. 18.
Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, pp. 7, 21–22.

136 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 347.

137 Packages will often have discounts on a suite of the lender's products such as transaction accounts, credit cards and home loans. The borrower often has to pay an annual fee for the package and, in turn, receives reduced (or waived) fees on their home loan, credit card and transaction account as well as a discount on the interest rate applying to their home loan.

138 Reserve Bank of Australia, 'Box B: Variable Interest Rates on Housing Loans', *Financial Stability Review*, March 2005, p. 39.

The practice of discretionary discounting appears to have commenced in the early 2000s, with some lenders increasing the discount offered on their standard home loan rate to new borrowers beyond the advertised rate.¹³⁹ Lenders have been open about the existence of discretionary discounts since the mid-2000s.¹⁴⁰ The ACCC understands that, while discretionary discounts were initially more limited in scope and amount, their use significantly increased during the 2010s. The RBA has noted that discretionary discounting '*enabled banks to slow the repricing of their loan books because only new or refinancing borrowers benefited from the discounts, whereas changes to their standard variable rate immediately flowed through to all borrowers.*'¹⁴¹

More widespread discretionary discounting also appears to have coincided with the implementation of Basel II in Australia in 2008. Basel II is a set of international banking regulations which requires financial institutions to incorporate the credit risk of assets held by them to determine regulatory capital ratios against individual loans, commensurate with the risk of those loans. The implementation of Basel II saw the cost of funding home loans become more closely aligned to the risk of those loans.

More recently, competition from new lenders has also contributed to the use of discretionary discounts by the big four banks. Discretionary discounting has enabled the big four banks to compete with new entrants by allowing the big four banks to price for the types of customers they want to obtain—for example, borrowers seeking less risky loans, such as those with a larger loan size but with a lower loan to value ratio, would generally receive a higher discount.¹⁴²

As discussed later in this chapter, there are some signs that discretionary discounts are now becoming less prevalent.

The scale and extent of discretionary discounting varies from lender to lender. In addition to observing two of the big four banks reducing, or considering reducing, their reliance on discretionary discounting (as discussed further below), the ACCC is also aware of some other lenders, including non-big four banks and non-ADI lenders, who do not offer, or are less reliant on, discretionary discounts. These lenders either do not offer discretionary discounts at all, or only offer them in limited cases, such as where they are trying to retain a customer.

The ACCC considers that these developments towards more transparent pricing are important because the presence of opaque pricing caused by the use of discretionary discounts can result in detriment. This detriment arises as opaque pricing:

- means borrowers face unnecessarily high search costs in determining the actual price lenders charge for home loans, which may be one factor affecting borrowers' assessment of the benefits of switching and their level of engagement in the home loan market (see chapter 2)
- creates an information asymmetry between lenders and borrowers in relation to available actual home loan prices, which puts borrowers in a weaker negotiating position when dealing with lenders.

Consequently, the existence of opaque prices has the potential to harm borrowers, causing them to pay more than they otherwise would.

The significant majority of borrowers receive discounts off the headline rate

The interest rate a borrower pays on their home loan is the headline interest rate (sometimes referred to as the reference rate) less a discount granted by their lender.

139 Guy Debelle, '*The State of the Mortgage Market*', Address to Mortgage Innovation Conference, 30 March 2010, <https://rba.gov.au/speeches/2010/sp-ag-300310.html>, viewed 25 September 2020.

140 Guy Debelle, '*The State of the Mortgage Market*', Address to Mortgage Innovation Conference, 30 March 2010, <https://rba.gov.au/speeches/2010/sp-ag-300310.html>, viewed 25 September 2020.

141 Guy Debelle, '*The State of the Mortgage Market*', Address to Mortgage Innovation Conference, 30 March 2010, <https://rba.gov.au/speeches/2010/sp-ag-300310.html>, viewed 25 September 2020.

142 M. Bergmann and M. Tran, Reserve Bank of Australia, '*The Distribution of Mortgage Rates*', *Bulletin—March 2018*, March 2018, p. 2.

In the interim report, we found that as at 31 October 2019, close to 90% of the big four banks' borrowers receive discounts off the headline variable rate.¹⁴³ The discount a borrower receives off the headline rate (which can be an advertised discount, a discretionary discount, or a combination of both) will amount to the difference between the headline rate and the rate the borrower actually pays.

For example, if the lender's headline interest rate is 4.00% and the lender grants a 0.75% (75 basis points) discount, the actual interest rate paid by the borrower is 3.25%.

The presence of discretionary discounts leads to opaque prices and information asymmetry

The presence of discretionary discounts makes actual home loan prices opaque and leads to information asymmetry between borrowers and lenders.

Discretionary discounts allow lenders to price based on the risk that a borrower's characteristics and loan features (including loan type and purpose) pose to the lender. However, discretionary discounts also allow lenders to price discriminate and charge borrowers with the same risk profile different prices for the same product.

Discretionary discounts are offered on a case by case basis. Their eligibility criteria are unpublished and vary from lender to lender. As observed in the Residential mortgage price inquiry interim report, *'lenders know the size of discounts they are prepared to offer and the type of borrowers they are prepared to offer them to but this information is not publicly available.'*¹⁴⁴ Accordingly, it is almost impossible for a borrower to determine the size of a potential discretionary discount available to them based on publicly available information. Across lenders, the discretionary discount potentially available to a borrower can vary depending on factors such as the:

- borrower's risk profile as assessed by the lender
- location of the security property
- loan to value ratio
- loan size
- purpose of the loan: owner-occupier or investor
- repayment type: principal and interest or interest-only
- type of loan: standard features or basic features
- value of the borrower to the lender given the products they hold, or will hold, with the lender
- lender's desire to win the borrower's business
- borrower's willingness to pay, including how hard the borrower pushes for a discount and how informed the borrower is of the ability to attain discounts.

Even if a borrower is able to identify the potential factors that a lender may take into account in determining discretionary discounts, the relative weighting of these factors is not transparent.

In addition to knowing the qualifying criteria for and degree of their own discretionary discounts, many lenders also appear to monitor and estimate discretionary discounts and actual prices of other competing lenders. For example, the ACCC's review of internal documents of the big four banks and Macquarie Bank in the Residential mortgage price inquiry suggested that these banks have visibility over the (other) big four banks' prices and discounts.¹⁴⁵ There are a number of ways these lenders could have sourced this information, including through relationships with mortgage brokers and from potential borrowers presenting competing offers for them to match.¹⁴⁶ Equipped with this knowledge,

143 As at 31 October 2019, the gap between the headline variable rate and the average interest rate paid on standard owner-occupier loans with principal and interest repayments across the big four banks ranged from 123 to 131 basis points. Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 8, 51, 55.

144 Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, p. 18.

145 Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, p. 18.

146 Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, p. 18.

lenders may be in a stronger position than borrowers to know what constitutes a reasonable or fair price for a borrower with certain characteristics and loan features to pay.

The opaqueness of discretionary discounts unnecessarily raises borrowers' search costs

The lack of visibility that borrowers have over discretionary discounts means that it can be unnecessarily difficult and time consuming for borrowers looking for a cheaper home loan to determine the prices available to them across lenders. The ACCC has previously observed that there is an '*unnecessarily high cost of price discovery*'.¹⁴⁷ This view has been shared by other regulators, including the RBA which noted in its submission to the Productivity Commission that '*a customer will have difficulty determining the competitive price without incurring large search costs*'¹⁴⁸ and ASIC, which observed that borrowers '*may be reluctant to refinance due to the cost, time and inconvenience involved*'.¹⁴⁹

As explained later in this chapter, we have observed two of the big four banks reducing, or considering reducing, their use of discretionary discounts. We are also aware of a number of other lenders, including some non-big four banks and non-ADI lenders who do not offer or are less reliant on discretionary discounts. However, for lenders that still rely on discretionary discounts, it can be difficult for a borrower considering their options to determine the actual price that these lenders will charge for a home loan. These lenders generally require borrowers to lodge a home loan application before confirming any discretionary discount and the actual price available to them.¹⁵⁰ If a borrower would like to obtain price quotes from multiple lenders, they will need to lodge an application with each of those lenders.

As part of the home loan application process, lenders generally require an applicant to provide multiple documents to verify their identity, income (for example, three months of salary, payslips, and employment contracts), expenses and financial position (including details of all assets and liabilities).¹⁵¹ Further, some lenders require copies of contract of sales, transfer of land documents, superannuation details and copies of vehicle registrations. Each lender has a different process which means that lodging one application does not lower a borrower's search costs for subsequent applications.¹⁵² Navigating each application process adds considerably to the time and effort a prospective borrower must expend to discover accurate interest rate offers.

Comparison websites and mortgage brokers cannot fully address unnecessarily high search costs caused by opaque prices

While intermediaries such as comparison websites and mortgage brokers have an important role in reducing search costs more broadly, we consider that they cannot completely address the unnecessarily high search costs that are caused by opaque pricing.

147 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 6.

148 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 349.

149 Australian Securities and Investments Commission, *Report 516: Review of mortgage broker remuneration*, 2017, p. 21.

150 Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, p. 79.

Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 21.

Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, p. 6.

151 See for example:

Australia and New Zealand Banking Group Limited, 'The documents you need for your home loan application', <https://www.anz.com.au/personal/home-loans/get-started/documents-home-loan-application/>, viewed 6 August 2020.

Commonwealth Bank of Australia, 'What you'll need when applying for a home loan', <https://www.commbank.com.au/home-loans/applying-for-a-home-loan.html>, viewed 6 August 2020.

National Australia Bank Limited, 'Home loan application form', <https://www.nab.com.au/content/dam/nabrwd/documents/forms/loans/home-loan-application-form.pdf>, viewed 6 August 2020.

Westpac Banking Corporation, 'How to apply', <https://www.westpac.com.au/personal-banking/home-loans/how-to-apply/>, viewed 6 August 2020.

152 See for example:

Australia and New Zealand Banking Group Limited, 'The documents you need for your home loan application', <https://www.anz.com.au/personal/home-loans/get-started/documents-home-loan-application/>, viewed 6 August 2020.

Commonwealth Bank of Australia, 'What you'll need when applying for a home loan', <https://www.commbank.com.au/home-loans/applying-for-a-home-loan.html>, viewed 6 August 2020.

National Australia Bank Limited, 'Home loan application form', <https://www.nab.com.au/content/dam/nabrwd/documents/forms/loans/home-loan-application-form.pdf>, viewed 6 August 2020.

Westpac Banking Corporation, 'How to apply', <https://www.westpac.com.au/personal-banking/home-loans/how-to-apply/>, viewed 6 August 2020.

Comparison websites

Comparison websites have a useful role in aggregating several sources of information into a single platform. In the context of home loans, insofar as they reduce the time spent by borrowers in navigating several lenders' websites to determine those lenders' advertised or headline rates, they will reduce search costs for borrowers to some extent.

However, comparison websites cannot readily reduce search costs caused by opaque home loan pricing arising from lenders' discretionary discounting practices. Comparison websites merely aggregate publicly available information. Given information about discretionary discounts is not publicly available, the use of a comparison website cannot reduce the search costs that a borrower will ultimately have to incur to ascertain a lender's actual price (including the cost in preparing and lodging a home loan application).

The usefulness and effectiveness of comparison websites may also be limited by the breadth of their market coverage and the influence of commercial arrangements they have with third parties. The Productivity Commission noted that:

Comparison sites are only as good as the input they use. The commercial arrangements (such as ownership, commission or advertising revenue) between comparison websites, the issuers and distributors of financial and credit products may mean that consumers are accessing information that only covers a portion of the market. For example, only products from commercially-related parties may be included in search comparisons...¹⁵³

The Productivity Commission also noted that 'commercial arrangements may also affect the way information is framed or presented, in order to influence consumer choices in a particular direction...'¹⁵⁴ For example, a comparison website's top results may prioritise products for which the website operator will receive a commission or referral fee over the best value products.

The ACCC is aware of these concerns regarding the distorting influence of commercial arrangements (both in banking and elsewhere). These issues have prompted the ACCC to develop and release guidance on comparison websites, and monitor their conduct in certain contexts (see box 3.2).

¹⁵³ Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 355.

¹⁵⁴ Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 355.

Box 3.2: ACCC's consideration of comparison websites

The ACCC monitors and provides guidance to industry, consumer groups and regulators on the use of comparison websites and their impact on competition and consumer welfare.¹⁵⁵ Most notably, the ACCC has published guidelines for comparison websites and service providers to encourage compliance with Australia's competition and consumer protection laws.¹⁵⁶ These guidelines note that comparison websites should:

- facilitate honest, like-for-like comparisons, including presenting results in a way that best matches consumers' needs, and making accurate representations of savings
- be transparent about commercial relationships
- clearly disclose who and what is being compared, including the nature and extent of the comparison service and market coverage.¹⁵⁷

The ACCC has taken enforcement action against several comparison websites including:

- litigation against iSelect (2019), Trivago (2018) and Energy Watch (2012)
- issuing infringement notices to Finder (2017) and Compare the Market (2014) for misleading consumers.

Mortgage brokers

Like comparison websites, mortgage brokers also cannot completely address the unnecessarily high search costs of price discovery, resulting from the use of discretionary discounts. Mortgage brokers can help borrowers generally navigate the market and can provide borrowers with more granular insights regarding the factors lenders consider in determining discretionary discounts, as they may have access to some information (that is not publicly available) about lenders' discretionary discounting policies.

However, ultimately these discounts are determined by lenders on a case-by-case basis, having regard to several unique characteristics of an individual borrower and their loan. While a broker can use their professional judgement to estimate the price a lender would quote having regard to all of these characteristics, they generally cannot provide an exact final figure, which only a lender can quote after considering a borrower's home loan application.

Therefore, in most instances, consumers will still need to go through the process of applying for a home loan with a lender to determine the actual home loan price, although each application process is likely made easier with the assistance of a broker. This is consistent with the findings of the Productivity Commission, which noted that *'brokers in discussion with the Commission confirmed that consumers are generally only able to be certain of the actual size of their 'discount' once they have formally had their home loan application assessed.'*¹⁵⁸

As with comparison websites, there have also been concerns about how commercial arrangements can influence brokers' incentives and the home loan recommendations they make to consumers. The best interests duty was legislated by the Australian Government following a recommendation of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. This duty will require brokers to act in the best interests of consumers, and where there is a conflict,

155 See for example: ACCC website guidance which assists consumers with use of comparison websites—Australian Competition and Consumer Commission, 'Comparator websites', <https://www.accc.gov.au/consumers/online-shopping/comparator-websites>, viewed 18 August 2020.

Australian Competition and Consumer Commission, *Comparator websites: A guide for comparator website operators and suppliers*, August 2015.

156 Australian Competition and Consumer Commission, *Comparator websites: A guide for comparator website operators and suppliers*, August 2015, p. 2.

157 Australian Competition and Consumer Commission, *Comparator websites: A guide for comparator website operators and suppliers*, August 2015, pp. 2–4.

158 Productivity Commission, *Competition in the Australian Financial System Inquiry Report*, 29 June 2018, p. 352.

to prioritise consumers' interests when providing credit assistance.¹⁵⁹ This duty comes into effect from 1 January 2021, and may mitigate some of these concerns around the improper influence of commercial arrangements on brokers' recommendations.

3.2 Unnecessarily high search costs and information asymmetry may result in borrowers paying higher prices

Opaque pricing, by creating unnecessarily high search costs and information asymmetry, reduces the likelihood that borrowers will obtain the lowest priced product for their circumstances. In our Residential mortgage price inquiry we observed that:

[t]he lack of transparency in discretionary discounts makes it unnecessarily difficult and more costly for borrowers to discover the best price offers. This adversely impacts borrowers' willingness to shop around, either for a new residential mortgage or when they are contemplating switching their existing residential mortgage to another lender. It is likely a key reason many borrowers do not obtain more than one or two quotes when looking for a residential mortgage, despite this being the most significant financial commitment over many years for most borrowers.¹⁶⁰

..By deterring borrowers from seeking more than one or two price offers, these costs reduce the likelihood that borrowers will find the best offer available or even an interest rate close to the best offer available to them in the market.¹⁶¹

In addition, as noted above, the opaque nature of home loan prices means that lenders have greater visibility than borrowers over what constitutes a reasonable or fair market price for a borrower with certain characteristics and loan features. This may hinder borrowers' ability to assess price quotes that they receive from lenders, and to negotiate in response. In other words, even once a borrower has spent time and effort to seek one or more price offers, they may lack sufficient information to assess whether these offers represent a reasonable or fair price for someone in their circumstances to pay. In the absence of this information, borrowers may not be able to know when they are being quoted a high price, and may not be in a strong position to negotiate a lower price.

3.3 Continued developments towards greater price transparency will reduce the harms currently associated with opaque home loan prices

While opaque pricing resulting from discretionary discounting (and its consequential harm to borrowers) remains a concern for the ACCC, we have observed that there are a number of lenders that either do not rely on discretionary discounts, only rely on them in limited cases, or have taken steps during the price monitoring period to reduce their reliance on them.

Steps taken by lenders to reduce their reliance on discretionary discounts have been driven (in part) by demand-side competitive pressures, and are improving price transparency. A number of other market developments and tools (including information on the Moneysmart Mortgage calculator, the prompt recommended in chapter 2, the Consumer Data Right and the use of key fact sheets) may also encourage lenders to continue to price more transparently.

Given these existing and coming developments, we do not consider it is necessary, at this stage, to introduce further regulation to directly require lenders to price more transparently.

159 Australian Securities and Investments Commission, *Regulatory Guide 273 Mortgage brokers: Best interests duty*, June 2020, <https://download.asic.gov.au/media/5641325/rg273-published-24-june-2020.pdf>, p. 4.

160 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 7.

161 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 22.

However, if the ACCC observes, during ongoing monitoring of the home loan market (recommendation 4), that momentum towards price transparency has stalled or if we observe consumer harm associated with a lack of price transparency, we will consider recommending that the Government take action to address this (as discussed in section 3.4).

Lenders' voluntary moves to more transparent pricing means that further regulatory intervention is not required at this time

Based on documents and data obtained from the big four banks, we have observed that over the price monitoring period, some of the big four banks took steps towards more transparent pricing structures. This included initiatives such as simplifying advertised discounts (for example reducing the number of discount tiers on home loan packages), and more notably, two of the big four banks reducing, or considering reducing, their reliance on discretionary discounts.

In our interim report, we observed '*Westpac offering higher advertised discounts in the second half of 2019, in order to improve the transparency of discounts and reduce its reliance on discretionary discounts*' in its packaged home loan product.¹⁶² For example, Westpac currently advertises a discount of 129 bps on variable rate loans as part of its Premier Advantage Package, while the advertised discount for this equivalent product as at 1 March 2019 was between 60 bps and 90 bps.¹⁶³

We have observed another big four bank considering a move to increase its advertised discount on its packaged home loan product, while reducing its degree of discretionary discounting to increase transparency. If this lender implements this change, it should result in a convergence between its advertised price and the price the borrower actually pays. Initiatives like this will apply further competitive pressure for other lenders, in particular, the two remaining big four banks, to reduce their reliance on discretionary discounts and advertise prices that more closely reflect the actual prices borrowers pay.

These moves towards more transparent prices have occurred without direct regulatory intervention. Rather, we understand that these developments have been motivated by these banks seeking to:

- simplify discounts to benefit the borrower experience
- increase their new lending volume
- adopt pricing structures similar to those that are offered by other lenders.

In addition to these initiatives taken or considered by the two big four banks, we are also aware of some non-big four banks and non-ADI lenders who do not offer or are less reliant on discretionary discounts.

The ACCC encourages lenders to continue to move towards more transparent pricing structures. This will reduce the unnecessarily high search costs borrowers currently face in determining actual home loan prices and the difficulties that borrowers face in assessing home loan offers.

On the basis of these recent developments, and the continuing demand-side and other competitive pressures that are encouraging lenders to move to more transparent pricing, we are of the view that supply-side regulatory intervention is not required at this time.

Other developments will also support competition and increased price transparency

As outlined below, the ACCC considers that other market developments and tools may encourage lenders to continue to move to more transparent pricing.

162 Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, p. 54.

163 Westpac Banking Corporation, 'Premier Advantage Package - Conditions of Use', 29 July 2020, https://www.westpac.com.au/content/dam/public/wbc/documents/pdf/pb/PAP_ConditionsofUse.pdf, p. 8.

Moneysmart Mortgage calculator

As outlined in chapter 2, following a recommendation by the Productivity Commission aimed at improving interest rate transparency for home loans, the Moneysmart Mortgage calculator was enhanced to display the average interest rate for new loans with a selected loan type (owner-occupier or investor) and repayment type (principal and interest or interest-only) for the most recent month for which data is available (see box 2.2).

In chapter 2, we recommend that lenders should be required to provide borrowers with loans originated three or more years ago with an annual prompt that should include a comparison between the borrower's current interest rate and the average interest rate paid for new loans similar to the borrower's loan.

The availability of average interest rate information reduces information asymmetry by providing transparency around the *actual interest rates paid for new loans*. This provides borrowers with a benchmark against which they can compare their existing interest rate or offers from lenders. This benchmark will assist borrowers in assessing their own rate, or other lenders' rates and will enhance their ability to negotiate with lenders.

If borrowers have more visibility over actual interest rates for similar loans (and in particular if this information is included in the prompt recommended in chapter 2), this may encourage lenders to present their best prices more readily to borrowers, which may support increased price transparency.

Consumer Data Right

The Consumer Data Right, as outlined in chapter 1, gives borrowers the ability to consent to their ADI sharing the data that is held about them with accredited third parties (data recipients) of their choice. The data recipient may be another lender, or it may be a third party that may aggregate information on the prices available for a borrower based on their characteristics from a range of different lenders. As outlined in chapter 1, this could assist borrowers in discovering prices available in situations where lenders would otherwise require them to complete a home loan application and provide substantial personal information in order to assess the borrower's risk profile and determine the interest rate they are willing to offer.

Since 1 October 2020, non-major ADIs (as data holders under the Consumer Data Right) are also progressively publishing generic product data. Although this generic product data may not include information about the discretionary discounts that are offered by some lenders, its publication will still enhance borrowers' ability to compare the headline rates and features of home loan products.

We expect the Consumer Data Right will reduce the costs borrowers incur to search for, discover and compare prices from a range of lenders, and will (in conjunction with other measures taken by lenders to reduce opaque discretionary discounts) increase price transparency for home loans.

Key fact sheets

Key fact sheets were introduced in 2011 as part of a package of legislative reforms aimed at improving consumer outcomes in the home loan market by making it easier for borrowers to identify, compare and switch to cheaper home loans.¹⁶⁴ Under these reforms, credit licensees that offer home loans are required to display on their website, and make available on request, a key fact sheet.¹⁶⁵ This sets out important home loan information in a standardised format, including:

- the interest rate
- fees
- monthly repayments

164 On 1 July 2010, the Australian Government also introduced a ban on exit fees for new home loans. This was designed to increase competition and encourage borrower switching.

165 The requirement to provide a key fact sheet only applies to principal and interest, fixed or variable home loans. The requirement does not extend to interest-only home loans or split home loans.
National Consumer Credit Protection Act 2009 (Cth).
National Consumer Credit Protection Regulations 2010 (Cth).
National Consumer Credit Protection Amendment Regulations 2011 (No. 5) (Cth).

- how much a borrower will repay per dollar of credit borrowed
- a personalised comparison rate.¹⁶⁶

Certain consumer research has indicated that when key fact sheets are provided to borrowers, it can improve their ability to select the cheapest loan.¹⁶⁷ This research also found that the benefits of key fact sheets have been limited in the home loan market as many consumers are not aware of their existence.¹⁶⁸ We consider that this may be due, in part, to some lenders not providing easily accessible links to key fact sheet calculators on their websites or an explanation of how consumers can use key fact sheets.¹⁶⁹

The ACCC encourages lenders to display links to key fact sheet calculators clearly on each webpage where a home loan is advertised, and include text explaining to consumers how to use key fact sheets.¹⁷⁰

As key fact sheets only incorporate advertised or headline interest rates, they do not provide borrowers with information about potential discretionary discounts that they may be eligible for. Therefore, in isolation, their increased use and accessibility is unlikely to address opaque pricing caused by discretionary discounts.

Nevertheless, the increased accessibility and use of key fact sheets could reduce some of the time and effort required to compare the headline rates and features of home loans across multiple lenders. Increasing borrowers' visibility over advertised rates and facilitating easier comparison of these rates, may encourage lenders to reduce their reliance on opaque discretionary discounts in order to ensure that their advertised rates are competitive to those offered by lenders that do not rely on these discounts.

3.4 The ACCC will consider recommending regulatory intervention if momentum towards price transparency stalls

The ACCC's preference is to strengthen competition between lenders to address the harms to borrowers and competition caused by opaque discretionary discounting, rather than using further direct regulatory intervention.

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- 166 Schedule 5, National Consumer Credit Protection Regulations 2010 (Cth). Comparison rates reflect the total cost of credit per annum, arising from interest charges and any other prescribed credit fees and charges. The National Credit Code (which is Schedule 1 of the *National Consumer Credit Protection Act 2009*) requires comparison rates to be calculated on the basis of an assumed loan size of \$150,000 and a loan term of 25 years. Comparison rates only take into account advertised or headline interest rates and do not provide borrowers with information about discretionary discounts that they may be eligible for.
- 167 Gavin Nicholson, Ross Skelton and Julie-Anne Tarr, *An exploratory study of regulatory failure in the Australian home mortgage market*, Journal of Consumer Affairs: Volume 53 Issue 1, 2019, <https://eprints.qut.edu.au/123536/8/123536.pdf>, p. 137.
- 168 Gavin Nicholson, Ross Skelton and Julie-Anne Tarr, *An exploratory study of regulatory failure in the Australian home mortgage market*, Journal of Consumer Affairs: Volume 53 Issue 1, 2019, <https://eprints.qut.edu.au/123536/8/123536.pdf>, p. 137.
- 169 In September 2020, we conducted a desktop review of the websites of 50 ADIs, who collectively accounted for around 99% of home loan credit outstanding as at 31 August 2020. We consider that for more than 2 out of 3 ADI websites we reviewed, it was difficult to locate the key fact sheet. This is because a link to a key fact sheet calculator was not available on the pages in which home loans were advertised, or the key fact sheet calculator was only available in a hyperlink in the terms and conditions text at the bottom of the webpage. In 1 in 10 cases, there was no key fact sheet calculator available or it was only accessible through directly searching for the term 'key fact sheet' in the ADI's website search bar.
- 170 Of the 50 ADIs reviewed, the ACCC considers that one in three of these ADIs provide key fact sheet calculators clearly and prominently on each webpage a home loan is advertised. See for example:
 86,400, 'Own home loan', <https://www.86400.com.au/own/>, viewed 30 September 2020.
 AMP, 'Home loans', <https://www.amp.com.au/home-loans>, viewed 30 September 2020.
 Community First Credit Union, 'Home loans', <https://www.communityfirst.com.au/personal/home-loans>, viewed 30 September 2020.
 Credit Union Australia, 'Achieve Variable Home Loan', <https://www.cua.com.au/loans/home-loans/achieve-variable>, viewed 30 September 2020.
 HSBC, 'Home Value Loan', <https://www.hsbc.com.au/home-loans/products/home-value/>, viewed 30 September 2020.

As outlined in chapter 5, we are recommending that the ACCC continue monitoring prices and competition in the home loan market to enable continued transparency to consumers and the Government on lenders' pricing practices. We consider that this ongoing monitoring role will support competition and improve consumer welfare.

As outlined above, actions taken by some lenders to reduce reliance on opaque discretionary discounts (which may be supported by other market developments and tools) are improving price transparency. Accordingly, we consider that further regulatory intervention is not required at this stage.

However if, during ongoing monitoring, we find that this momentum towards price transparency has stalled or if we observe consumer harm associated with a lack of price transparency, there are a number of regulatory interventions the ACCC could consider recommending to the Government.

These regulatory options for improving price transparency could include:

- requiring lenders to provide consumers with tailored indicative price quotes delivered through lenders' websites (similar to tailored quotes for other complex financial products that price for risk, such as insurance)
- prescribing that lenders be required to present their prices to consumers in a way that details the multiple factors that contribute to these prices (taking into account discretionary discounts where the lender uses them).

Tailored price quotes that include discretionary discounts

The ACCC could consider recommending that lenders be required to provide prospective borrowers with tailored indicative price quotes, including discretionary discounts, in advance of the borrower lodging a home loan application.

It is likely this could be effectively delivered through a lender's website, similar to tailored quotes for other complex financial products, such as insurance, that are priced depending on a number of factors and consumer characteristics. This would allow a prospective lender to seek risk characteristics and other information from the prospective borrower and use its pricing models (or a variant thereof) to calculate an indicative price *inclusive* of any potential discretionary discounts.

In addition to parallels with other complex financial products that have a price based on a number of factors and characteristics, much of the information required for such a calculator is information that is already provided by prospective borrowers when they use a lender's other online tools, such as borrowing power and home loan repayment calculators. This information includes income, expenses, assets, liabilities, number of dependents and whether the home loan is jointly held.

Through an online platform, lenders should be able to take into account other factors that may influence the offering and size of discretionary discounts, including those that are outlined above in section 3.1.

While the quote provided would be indicative only, it would still have utility for a prospective borrower. A broadly indicative quote would be useful for borrowers to determine which lender is likely to give them the lowest price, even if the price itself does not factor in all considerations. Further, the indicative nature of the online price quote could be made clear to borrowers at the time they obtain the quote.

Prescribing how lenders present their prices to consumers

Alternatively, the ACCC could recommend that lenders be required to present their prices to consumers in a way that details the most salient factors that contribute to their prices (taking into account discretionary discounts where the lender uses them).

Publication of this material would provide more transparency over lenders' actual prices and the criteria to qualify for discretionary discounts, as well as the size of those discounts. For example, prescribing that potential loan prices be presented in the form of a table or tables containing indicative actual prices that lenders would charge, taking into account the most salient determinants of these prices and discretionary discounts (for example, loan to value ratio, loan size, repayment type and loan type), may help consumers with price discovery.

We note that any such standardised presentation of prices would need to be extensively consumer tested to ensure it provides consumers with clear and accurate information at the time they need it. It would also require consultation with lenders to ensure the most salient determinants of prices are captured.

Box 3.3: Action to be taken by the ACCC

We consider that moves by lenders towards more transparent pricing, and continuing competitive and other pressures that are encouraging increased price transparency, mean that further regulatory intervention is not required at this stage.

However, if the ACCC observes through its monitoring under recommendation 4 that momentum towards price transparency has stalled, or if we observe consumer harm associated with a lack of price transparency, we will consider making recommendations to the Government to address this.

4. Pain points in the discharge process impede switching

Key findings

- Once a borrower has compared offers in the market and decided to switch lenders, they need to discharge their home loan from their existing lender.
- Existing pain points in the discharge process have introduced inefficiencies in the switching process. Commonly reported pain points in the discharge process include:
 - opaque and difficult steps for borrowers to complete, such as Discharge Authority forms that are difficult to access and complete, or lenders requiring in-person contact or multiple points of contact before processing a discharge request
 - delays in existing lenders processing discharge requests, or uncertainty regarding the length of the discharge process.
- The majority of stakeholders that the ACCC consulted with raised concerns that the discharge process of many lenders is opaque, challenging, and inefficient for borrowers to complete. This reflects the incentives of the existing lender, who has an interest as a profit-maximising business to retain borrowers for as long as possible. While lenders may or may not intentionally create pain points, they have little motivation at the individual level to remove pain points from the discharge process.
- Borrowers are less likely to start or complete a switch to a new lender if the process is frustrating or confusing, even if switching would result in them obtaining a better home loan. Pain points affect consumers' ability to make and give effect to decisions that benefit them, and result in costs to lenders more generally by impeding the competitive process.
- We have made two recommendations that we consider would streamline the discharge process, make it easier for borrowers to switch lenders and drive better consumer outcomes and competition in the home loan market:
 - All lenders should be required to provide a standardised Discharge Authority form to borrowers, which is easy to access, fill out and submit (recommendation 2).
 - All lenders should be subject to a maximum time limit of 10 business days to complete the discharge process, as defined in this chapter (recommendation 3).

In this chapter, we report on:

- commonly reported pain points in the discharge process
- how pain points in the discharge process can cause inefficiencies that result in harm through:
 - borrowers not starting, or failing to complete, a switch to a new lender
 - new lenders incurring costs or not being able to secure new borrowers based on the merits of their offers
- the ACCC's recommendations targeted at making the discharge process clearer and quicker for borrowers to complete, and improving competition and consumer outcomes.

For the purposes of this chapter, our discussion and recommendations on the 'discharge process' focus on those components of the process that are within the control of existing lenders, rather than attributable to state and territory regulations. Box 4.1 below sets out our definition of the 'discharge process' in this chapter. The ACCC considers that increased digitisation and technological improvements in conveyancing and across all stages of the switching process between lenders (as illustrated in figure 1.1) will also make the overall process more efficient and easier for borrowers to complete (see box 4.3).

Box 4.1: What do the discharge and settlement processes involve?

The discharge process

When a borrower is switching lenders, the new lender first assesses the borrower's circumstances and issues the borrower with a letter of offer for a new home loan. The borrower must then ask their existing lender to discharge their existing mortgage, which involves obtaining and completing the Discharge Authority form¹⁷¹ ('discharge form') and submitting it to the existing lender to begin the discharge process.

For the purposes of this chapter, the 'discharge process' includes the steps taken by the existing lender once the borrower has made a discharge request up until they are ready to arrange settlement with the new lender (steps 6–7 in figure 1.1). Some of the key actions undertaken by the existing lender before arranging settlement with the new lender include:

- verifying the identity of the borrower seeking to discharge their home loan
- processing the borrower's discharge form (each lender has their own version of a discharge form, and different requirements regarding how their discharge form is accessed or submitted)
- calculating the home loan payout figure and receiving the borrower's agreement to the payout figure
- retrieving the property's certificate of title (Title)¹⁷² documents in some cases, such as for paper-based Titles.

This chapter does not focus on the subsequent steps taken by both the existing and new lenders to complete the settlement process and discharge the existing mortgage under state and territory regulations (steps 8–9 in figure 1.1).¹⁷³ However, a brief explanation of the settlement process is also provided below.

The settlement process and electronic conveyancing (e-conveyancing)

The settlement process begins once steps in the discharge process (as defined in this chapter) are completed, and refers to the process of transferring the Title from the existing lender to the new lender. To do this, a 'Discharge of Mortgage' form must be lodged with the relevant state or territory land titles office to 'discharge' or remove the old mortgage from the Title. The Discharge of Mortgage form used by land titles offices is distinct from the Discharge Authority form submitted by borrowers earlier in the discharge process, and which this chapter refers to as the 'discharge form'.

To complete the settlement process, the new lender generally meets (physically for paper-based settlements and virtually for electronic settlements) the borrower's existing lender to pay the amount outstanding on the home loan, arrange for the Title to be exchanged and register a new mortgage over the borrower's property. The Title, Discharge of Mortgage form and new mortgage are then submitted to the relevant land titles office.

171 The Discharge Authority form (or discharge form) is required by lenders when a borrower is switching their home loan to a different lender, is selling or has sold a property, or has fully repaid their home loan, among other reasons. The discharge form is required to release the security property provided for a home loan, where the security property is an item or sum of money as protection for the lender in the case of the borrower being unable to repay the home loan. For example, the security property may be the property which the home loan is used to purchase.

172 The certificate of title is an individual's record of interests and rights affecting their land. For borrowers with a home loan, the existing lender holds the certificate of title until the loan is repaid.

173 The discharge and settlement processes are similar to the steps required when a home loan is fully repaid, or if the property is sold. Similarly, switching a home loan to a new lender is effectively the same process as acquiring a new home loan and will share many identical steps.

For most states and territories in Australia, the settlement process can be done electronically via an Electronic Lodgment Network.¹⁷⁴ Electronic settlement and e-conveyancing can be done via an Electronic Lodgment Network Operator (ELNO) such as Property Exchange Australia (PEXA) and, more recently, Sympli in some jurisdictions. The ACCC has been involved with work regarding the competition issues in relation to the introduction of e-conveyancing.¹⁷⁵

Finally, the borrower is notified once settlement is complete and begins to repay their new home loan to the new lender.

4.1 The discharge process can be unnecessarily difficult and lengthy for borrowers

Lenders' discharge processes can contain a number of pain points, or the potential for pain points, which make it unattractive or difficult for borrowers to start or complete a switch to a new lender.

The commonly reported pain points in the discharge process can be broadly categorised into two issues:

- Uncertainty about the length of time that the discharge process will take, and unnecessary delays in the process (including due to the use of retention strategies by existing lenders).
- Unclear and/or complicated steps for borrowers to complete during the discharge process.

While these pain points may appear minor,¹⁷⁶ they can have a significant impact on consumers. A discharge process that is unclear, lengthy and/or difficult for borrowers to follow can deter or prevent them from switching, resulting in costs (financial or otherwise) if they are unable to switch to a better suited home loan. New lenders will also incur costs if they are unable to secure new customers or gain their business efficiently.

Accordingly, pain points in the discharge process have the potential to cause consumer harm and harm to competition more broadly. However, despite this potential harm, existing lenders are not incentivised at the individual lender level to remove (and may even be incentivised to create) these pain points (see section 4.2 below).

174 As of 6 August 2020, e-conveyancing is currently available in all states and territories except for Tasmania, the Australian Capital Territory and the Northern Territory. E-conveyancing is mandatory for New South Wales, South Australia, Victoria and Western Australia. The requirements for paper-based or electronic Titles also vary by jurisdiction.

Sources:

NSW Land Registry Services, 'eConveyancing in NSW', 7 May 2020, <https://www.nswlrs.com.au/eConveyancing>, viewed 6 August 2020.

Business Queensland, 'Electronic conveyancing', 19 May 2020, <https://www.business.qld.gov.au/industries/building-property-development/titles-property-surveying/titles-property/elodgement-conveyancing/econveyancing>, viewed 6 August 2020.

Land Services SA, 'Mandating of eConveyancing in South Australia', 17 April 2020, https://www.landservices.com.au/_data/assets/pdf_file/0017/5822/NTLP-228-Mandating-of-eConveyancing-in-South-Australia.pdf.

State Government of Victoria, Department of Land, Water and Planning, '100% electronic lodgment program', 10 July 2020, <https://www.propertyandlandtitles.vic.gov.au/forms-guides-and-fees/electronic-lodgment/100-electronic-lodgment-program>, viewed 6 August 2020.

Landgate, Western Australian Land Information Authority, 'Electronic conveyancing', 11 May 2020, <https://www.landgate.wa.gov.au/for-individuals/legislation-and-reform/electronic-conveyancing>, viewed 6 August 2020.

175 On 2 December 2019, the ACCC released its report on e-conveyancing market reform. In the report, the ACCC highlighted the need to implement a pro-competition market model for e-conveyancing to avoid entrenching a monopoly provider and identified interoperability as its preferred approach to facilitating competition. On 7 September 2020, all states and territories supported the principle of requiring interoperability between ELNOs, with New South Wales, Queensland, South Australia and Western Australia agreeing to develop technical and regulatory regimes for legislation to be in place by mid-2021. The ACCC's report is available at <https://www.accc.gov.au/about-us/consultations-submissions/accc-submissions>.

176 Nobel Laureate Richard Thaler coined the term 'supposedly irrelevant factors' to refer to factors that should not influence the thinking of a rational person, according to traditional economic theory. These factors can include the way that an option is framed, the design of a form, or minor steps in an administrative process. In practice, these supposedly irrelevant factors can have a significant impact on consumer choice.

Source: Richard Thaler, *Misbehaving: The Making of Behavioral Economics*, W. W. Norton & Company, 2015.

Borrowers face uncertainty about how long the discharge process will take, the process may involve lengthy delays

The majority of stakeholders consulted with during this inquiry raised concerns about the harm caused by existing lenders taking lengthy periods of time to process discharge requests. When delays occur in this processing, there is little that the borrower or new lender can do to expedite the process. In particular, existing lenders are not required to discharge home loans within any particular timeframe. Many stakeholders raised concerns that the lack of a standardised timeframe for a lender to process a discharge request allows significant and unnecessary delays to occur frequently. For example:

- One lender said that there is a large variance in discharge times and the length of the process can deter borrowers from switching. They considered that introducing a mandatory time limit to process a discharge form would be greatly beneficial in outlining the expectation for all parties and requiring them to meet it.
- One market participant complained that there is no standardised timeframe to process a discharge form, with each lender setting their own timeframe, creating uncertainty for borrowers around how long it will take to switch. This participant also said that providing more certainty about the length of the process will encourage borrowers to switch.
- Another market participant identified that a difficult part of the discharge process for borrowers was not knowing how long a lender will take to process the discharge form.

Box 4.2 outlines public information and stakeholder feedback regarding the time that existing lenders typically take to discharge home loans.

Box 4.2: How long does discharging a home loan take?

Our review of a sample of lenders' websites showed that only a small number of these lenders provide guidance on their websites regarding how long the discharge process will take. Of those that did provide guidance, the estimated timeframe for processing a discharge varied to some degree. For example:

- CBA's website states that *'it will take up to 14 business days'* to process a completed discharge form¹⁷⁷
- NAB's website advises borrowers to submit completed discharge forms *'at least 10 business days before [their] preferred settlement date'*¹⁷⁸
- the non-ADI lender, Pepper, indicates on its website that it requires *'a minimum of 10 business days'* upon receipt of a completed discharge form before settlement can be booked.¹⁷⁹

During consultation, several stakeholders said that discharge timeframes are often too long, and provided different estimates of how long lenders typically take in practice to complete the discharge process (or the discharge and settlement processes combined). For example:

- The Mortgage and Finance Association of Australia said that it has *'received reports that many lenders take 15 business days or longer to be ready to discharge a mortgage when a loan is being repaid or refinanced'*, and that in some cases, it has heard of lenders taking up to 40 days.

177 Commonwealth Bank of Australia, 'Discharge/Refinance Authority Form', <https://www.commbank.com.au/digital/home-loan-forms/mortgage-discharge/start>, viewed 13 August 2020.

178 National Australia Bank, 'Mortgage discharge authority form checklist', <https://www.nab.com.au/personal/home-loans/manage/mortgage-discharge-form-checklist>, viewed 1 October 2020.

179 Pepper Money, 'How do I discharge from a Pepper loan?', <https://www.pepper.com.au/lending/help-centre/customer-service/pepper-loan-discharge-process>, viewed 7 September 2020.

- One smaller lender noted that there is an (unwritten) standard industry expectation that lenders will process discharge forms within 15 business days of receipt, but in most cases it takes lenders longer to do so. This lender provided indicative monthly data from March to June 2020, which showed that, for borrowers switching to them from another lender, it took on average 25 to 45 business days for their mortgage to be discharged (including settlement), depending on the month and existing lender type (small, mid-tier or large lenders).
- One market participant estimated that over the 12 months to 30 April 2020, existing lenders took 16 business days on average to process a discharge request and be ready to book settlement, with the discharge time being 5 business days at best and 21 business days at worst.
- One mid-tier lender said that, *'due to varying service levels set by banks, we find that some banks review the discharge agreement & set a settlement date within a few days of [lender name] uploading the discharge agreement whilst with others, we have to constantly follow up and delay settlement'*.

Impact of the COVID-19 pandemic on discharge times

Several stakeholders acknowledged that the COVID-19 pandemic has affected discharge processing times recently, for example because of the redeployment of staff to meet more immediate consumer needs (such as loan repayment deferrals) or its impact on offshore processing centres. Lenders have also been handling a higher volume of switching requests (see figure 1.2).¹⁸⁰

While the impact of COVID-19 may be resulting in longer than usual discharge times, we consider that the stakeholder evidence indicates that delays in the process have existed and persisted prior to COVID-19.¹⁸¹ The Mortgage and Finance Association of Australia said that *'our members have been complaining for many years about the time taken for existing lenders to be ready to release their mortgage'*. One small lender also said that the *'discharge process has changed little in the last 30 years, most likely because there is no business case or incentive for [lenders] to change.'*

Retention strategies used by the existing lender can contribute to significant delays

After receiving a discharge request, existing lenders typically employ retention strategies to persuade the borrower to stay, for example by offering them a lower rate, cashback or frequent flyer points. While competitive retention offers made in a timely manner can result in borrowers getting a better deal, the lack of a timeframe for processing a discharge creates the potential for the existing lender to unnecessarily prolong process times to continue making additional retention offers in an attempt to retain a particular customer. The uncertainty and frustration caused by delay and the cognitive load of engaging with multiple retention communications can make it difficult for consumers to make the best decision when choosing between the new lender's offer and any retention offers from the existing lender. This could result in consumers not completing a home loan switch which would have been more beneficial to them.

Stakeholders had mixed views on the use of retention strategies. While most stakeholders expressed frustration about the extent to which retention strategies contribute to delays or other pain points in the discharge process, some of them also noted the potential for retention offers to benefit borrowers. For example, the Customer Owned Banking Association said that if a retention offer allowed the borrower to obtain a better deal than the alternatives, then that was a good consumer outcome. The Australian Banking Association considered, on a more general level, that *'switching between lenders (external refinancing) is not the only way that a consumer can receive the best outcomes'*. It said that if borrowers shop around and ultimately stay with their existing lender because they are offered a better interest rate or more suitable product, then that was evidence of healthy competition.

180 See also, for example, D Hughes, 'Record numbers of borrowers refinancing property', *Australian Financial Review*, 15 May 2020, <https://www.afr.com/property/residential/record-numbers-of-property-borrowers-refinancing-20200515-p54tcj>, viewed 20 August 2020.

181 See also, for example, N Bendel, 'Discharge times slammed as 'absolutely ludicrous'', *The Adviser*, 11 November 2014, <https://www.theadviser.com.au/breaking-news/31072-discharge-times-slammed-as-absolutely-ludicrous>, viewed 20 August 2020.

Administrative hurdles in the discharge process (discussed further in the section below) may facilitate the use of retention strategies by existing lenders. For instance, an existing lender may not provide discharge forms or instructions, or commence processing discharge requests, until borrowers receive multiple ‘save calls’ or are redirected to retention teams. The Mortgage and Finance Association of Australia said that certain existing lenders may require borrowers to visit a branch to obtain a discharge form because it provides them with a face-to-face opportunity for a repricing discussion. The Mortgage and Finance Association of Australia and several market participants considered that existing lenders create delays in the discharge process to maximise the opportunity to make retention offers.

It is likely the borrower will not have received a final payout figure for their current home loan at the time when retention offers are being made, making the total financial cost of the discharge somewhat uncertain. This final payout figure includes interest payments, bank fees and government fees. In the context where a borrower is fatigued by delay and multiple contacts from their existing lender, they may perceive that the switching process will involve too much hassle and cost (see also section 1.2), and therefore be less inclined to take action to carefully compare offers and more inclined to take the path of least resistance.

Two smaller lenders said that even if the existing lender’s retention offer rate is the same or slightly higher than that of the new lender, borrowers can be persuaded to stay because of the ‘hassle’ of switching. Three other stakeholders said that the existing lender may offer short-term incentives, such as cashback offers and temporary discounts, to persuade the borrower not to switch, even if these incentives save the borrower less money in the longer run than the new lender’s price offer. We note that short-term incentives (which will be beneficial to customers at least in the immediate term) are also used by new lenders to attract new borrowers (see section 1.2 for a discussion of cashback offers in the context of their use by new lenders). Short-term incentives can be effective because many consumers display ‘present bias’, where they over-value small immediate gains relative to larger long-term gains. Borrowers with a strong ‘present bias’ may be particularly disinclined to engage with a process involving time and effort, especially since the benefits of switching tend not to be felt immediately.¹⁸²

The ACCC acknowledges that retention offers may allow borrowers to obtain a lower home loan price or more suitable product than they otherwise would have (by either staying on their current product offering or switching to a new lender). We are not seeking to unnecessarily restrict the ability of lenders to make retention offers, given that these efforts are a natural feature in many markets and they can result in positive consumer outcomes. However, we consider retention strategies should not result in unnecessary delay or turn into an obstacle to a borrower switching efficiently to a new lender.

Steps involved in the discharge process may be unclear or unnecessarily difficult

Numerous stakeholders expressed concern that steps involved in the discharge process can be unclear and unnecessarily difficult for borrowers to navigate, further adding to inefficiencies and impediments in the process. The problems experienced by borrowers include:

- difficulty accessing discharge forms
- discharge forms being unnecessarily complex
- further administrative and process hurdles, including unclear or unnecessarily difficult steps to submit the discharge form, and a lack of assistance from existing lenders regarding their process requirements.

These problems are discussed in the sections below.

182 See: Behavioural Economics Team of the Australian Government, Department of the Prime Minister and Cabinet, *Credit when it’s due: Timely reminders help consumers reduce their credit card debt*, March 2019, p. 7. See also: Amelia Fletcher, University of East Anglia—Norwich Business School, Norwich, UK, *Disclosure as a tool for enhancing consumer engagement and competition*, September 2019, pp. 5–6.

Borrowers can face difficulties obtaining a copy of their existing lender's discharge form

Numerous stakeholders raised concerns that it can be difficult for borrowers to access many lenders' discharge forms, creating inefficiencies in the discharge process. Discharge forms are often unavailable or difficult to locate on a lender's website, meaning that borrowers need to directly request a copy of the discharge form from their existing lender. For example, one market participant gave the example of borrowers being required to call a particular lender's generic customer service line to request the form to be emailed to them. Some lenders may require borrowers to physically visit a branch before they receive a discharge form. One small market participant was of the opinion that the lack of easy accessibility amounted to a '*professional blocking tactic*' by the existing lender. Other stakeholders shared similar sentiments that existing lenders create such pain points in the discharge process as a deliberate tactic to deter borrowers from switching.

A mid-tier lender said that, in their experience, making copies of the discharge form publicly available caused issues of version control when third parties (such as solicitors) offered outdated copies on their websites for their clients to use. They said that if a borrower submits an outdated version of the form that has since been updated, they would then need to repeat the process of obtaining, completing and submitting the correct version. Nevertheless, this lender acknowledged that standardising the form across lenders (recommendation 2) could assist in resolving issues of version control (see section 4.3 below).

The Mortgage and Finance Association of Australia considered that discharge forms are not necessary for existing lenders to process a discharge request. It stated that '*[t]here is no need for any form, and a simple request to arrange for the full repayment of the loan and discharge of the mortgage should be sufficient. If mortgagees insist on a form, it should be a readily available industry standard form so as to not to add [to] the time taken.*'

We reviewed a sample of discharge forms and processes for a small selection of 10 different lenders, including the big four banks, mid-tier and smaller lenders. Our review showed the variety of different processes that lenders have for accessing discharge forms. At the easier access end, we found two lenders allowed borrowers to access the discharge form on their websites, and that three of the big four banks assisted borrowers in filling out the discharge form by requiring the use of an online questionnaire that guided them to input their details and generated a form with those fields already completed. At the more difficult access end, we found that three lenders directed borrowers to call the lender or visit their local branch to obtain a discharge form, while the remaining two lenders did not provide any information or instructions on their websites regarding how borrowers could access the form or complete the discharge process.

The discharge form provided by the existing lender may be unnecessarily complex

Though all forms require certain common information, we observed significant variance between different lenders' discharge forms. Each lender has their own version of a discharge form, and different requirements regarding how their discharge form is submitted. In our review of sampled discharge forms, we found that their design varied, despite requiring broadly similar information from borrowers.

When completing a discharge form, the information that the borrower is typically required to provide includes:

- personal contact details
- contact details of the borrower's representative, if any
- reason for the discharge (for example: property sale, refinance, early payout)
- information about the security property to be released
- signature and date to authorise the discharge.

The sampled discharge forms varied in their layout, user friendliness and the type or complexity of the terminology used. Furthermore, lenders referred to their version of the discharge form by different names, including variously calling the form a 'discharge authority', 'discharge request form' or 'security release authority'.

Several stakeholders raised concerns regarding lenders' ability to create their own versions of the discharge form, including the concern that it enables some lenders to design forms so that they are unnecessarily difficult for borrowers to follow. For example, one smaller lender noted that *'[L]enders will frame a question or instruction on the form in a confusing way, meaning the customer is more likely to make an error on the form.'* They considered that the level of complexity of some form requirements indicates it is a tactic by the existing lender to make switching difficult, rather than an authentic safety measure. Some stakeholders also reported that lenders may include unnecessary fields in their version of the form, or regularly update the form with immaterial changes (such as formatting updates) but still require borrowers to use the latest version.

If the borrower subsequently makes an error on the discharge form or submits an incorrect version, the lender may require them to repeat the process of completing and submitting it. Three market participants said that if there is an issue or error with a submitted form, the existing lender may significantly delay or reset the discharge processing time. For example, one lender said that in one instance, it took two months for a borrower to switch to them because the existing lender did not communicate to the borrower that they were required to fix a small error made on their discharge form.

Borrowers can face further administrative hurdles during the discharge process

Borrowers may face further administrative hurdles during the discharge process, such as needing to navigate complicated procedures to submit the discharge form or meet particular requirements that involve extra time or effort (for example, providing physical paperwork or supplying a 'wet signature' rather than an e-signature on the form). Stakeholders reported a variety of administrative hurdles that borrowers may experience. For instance:

- A market participant said that some lenders expect borrowers to find, print off and then scan to submit a discharge form, and considered that this was unreasonable when the process can be fully digitised (this topic is discussed further below in box 4.3).
- More generally, this market participant observed that discharge process requirements vary between lenders, ranging from the most straightforward to the most *'antiquated with the greatest number of pain points'*. They considered that the number of times a borrower (or their representative) has to contact some lenders to progress their discharge request ('touch points') costs the borrower unnecessary time and effort in switching. They observed that, in their experience, borrowers engage in five touch points on average with their existing lender, and nine touch points in the worst cases, to progress the discharge of their home loan. If the new lender or another representative contacts the existing lender on behalf of the borrower to progress their discharge, then they also expend time and effort.
- One smaller lender said that the existing lender may keep changing the method by which a discharge form must be submitted, or refuse to accept a form submitted by a third party on the borrower's behalf (such as their new lender, solicitor or settlement agent). They considered that these were techniques employed by the existing lender to hinder the discharge process or delay discharging the borrower.
- As discussed earlier, if the borrower makes an error on the discharge form or submits an incorrect version, the lender may then require them to repeat the process of completing and submitting it, and reset the discharge processing time. While one mid-tier lender said it was reasonable for the existing lender to take time to ensure forms are error-free for security reasons, this lender was also exploring ways to reduce error rates and improve the discharge process by training staff and digitising processes. We consider that the standardisation and simplification of discharge forms would likely reduce the incidence of errors (recommendation 2).
- Borrowers may find that the steps involved in the discharge process are generally unclear or difficult to determine due to a lack of information or assistance from existing lenders. Two stakeholders said that it is often difficult for borrowers to reach staff at their existing lender for help with queries regarding the discharge process, which would further hinder borrowers' ability to determine what steps to take and complete the process correctly and efficiently.

4.2 Pain points in the discharge process can cause consumer harm and impede competition

The pain points that currently exist in many lenders' discharge processes can prevent borrowers from making or following through on decisions that benefit them. In particular, borrowers may be deterred from switching lenders due to the experience or expectation of pain points, even if the new lender is offering a better home loan than the existing lender.

Behavioural economics research shows that consumers exhibit certain behavioural preferences or biases that may affect their switching decisions. For example, borrowers may:

- exhibit 'present bias' and be less likely to switch if the benefits from switching are not experienced immediately¹⁸³
- suffer from cognitive overload, where borrowers become overwhelmed by the difficulties in the process of switching and drop out of the switching process¹⁸⁴
- overestimate the costs of switching, if they are unsure about how the switching process will play out in practice and/or perceive that it takes too long or it is too difficult to switch.¹⁸⁵

A survey conducted on behalf of the Financial Conduct Authority in the United Kingdom also found that one barrier for borrowers who have not switched home loans, but could benefit from switching, was that they believed they were lacking important information about the switching process that would help them make the decision to switch, including an understanding of how long the process would take.¹⁸⁶

If borrowers do not start or complete the process of switching lenders due to the pain points that they anticipate or experience, this can distort the competitive process, as borrowers are less likely to select offers based on their true merits. For example, if the borrower is frustrated by the delays and uncertainties of the discharge process, or prefers a quicker financial gain, they may accept a retention offer rate that is slightly higher than the new lender's rate.

A number of stakeholders specifically noted that borrowers drop out of the switching process because of pain points or retention offers from the existing lender. For example:

- A small market participant estimated that, from the refinancing applications between lenders it facilitates per month, up to 30% are withdrawn by borrowers because of the inconvenience of the discharge process, frustrations with delays, or the existing lender's retention offers.
- A small lender estimated that, of the borrowers that made applications to switch to them, a number equivalent to nearly 15% of their loan book dropped out prior to settlement. This included borrowers who had already submitted all the evidence required to receive unconditional approval for their new home loan. This lender also considered that drop-outs were mainly due to delay tactics and retention offers from the existing lender.

Even when borrowers decide to complete a switch to a new lender for a cheaper or more suitable product, they will still incur a cost, financial or otherwise, for each day of delay during the discharge process.

183 See: Behavioural Economics Team of the Australian Government, Department of the Prime Minister and Cabinet, *Credit when it's due: Timely reminders help consumers reduce their credit card debt*, March 2019, p. 7.

See also: Amelia Fletcher, University of East Anglia—Norwich Business School, Norwich, UK, *Disclosure as a tool for enhancing consumer engagement and competition*, September 2019, pp. 5–6.

184 Deloitte, *Open Banking: Switch or Stick? Insights into customer switching behaviour and trust*, October 2019, p. 50.

See also: Amelia Fletcher, University of East Anglia—Norwich Business School, Norwich, UK, *Disclosure as a tool for enhancing consumer engagement and competition*, September 2019, pp. 10–11.

185 A consumer survey from 2017 also cited in chapters 1 and 2 identified that the effort involved in switching lenders was one of the top three reasons provided by respondents for why they were not considering changing lenders. The survey was conducted online from 9 to 12 January 2017 and is based on 1,009 Australian adults.

Source: BLACKMARKET research, *Project: Switch, Financial/Banking Institution Survey*, January 2017.

186 Savanta: ComRes, research commissioned by the Financial Conduct Authority, *Mortgage switching research*, 3 March 2020, pp. 6, 33.

Removing inefficiencies in the discharge process would result in better outcomes for consumers and competition

The current issues in the discharge process reflect the incentives of the existing lender as a profit-maximising business, with an interest in holding on to revenue from customers for as long as possible. While existing lenders may or may not intentionally create hurdles, they are at least incentivised not to remove them, as they financially benefit from the borrower being delayed in making, or not completing, a switch to a new lender.

At the same time, the new lender or mortgage broker facilitating the switch incurs costs, as they invest time to help borrowers manage pain points in the discharge process, experience uncertainty or delay themselves, or lose prospective borrowers that do not end up switching.

We consider that, once a borrower has decided to switch to a new lender, the discharge process should be clear, quick and simple to follow. While this may not be in the immediate interest of the existing lender in that individual case, a more efficient discharge process would enhance overall outcomes for market participants, including lenders, mortgage brokers and borrowers. In particular, once the borrower has compared offers in the market and decided that they would prefer to switch to a new lender, a clearer and quicker discharge process would result in the following outcomes:

- It would encourage more borrowers to start or complete the discharge process, as they would expect and experience fewer pain points or inefficiencies in the process.
- It would enable borrowers to more accurately compare the new lender's offer with any retention offer from their existing lender, as their decision would not be affected (or at least be less affected) by frustration or confusion with the discharge process. Therefore, whether they ultimately choose to remain with their existing lender or switch lenders, their decision would be more likely based on their best interests, and they would be able to move to a more competitive offer and obtain the resulting benefits or financial savings more quickly.
- Given that borrowers would be able to more accurately compare offers between the existing and new lenders, and act on their decision without excessive hurdles, it would drive lenders to offer more competitive home loan prices and allow them to gain customers through more effective competition in the home loan market.

Given the incentives of individual lenders to retain customers, we consider regulatory intervention would assist in reducing inefficiencies in the discharge process and achieving the above outcomes.

4.3 A time bound discharge process and standardised discharge form will help address pain points

We consider that the following two recommendations will make the discharge process clearer, easier and more efficient:¹⁸⁷

► Recommendation 2: A standardised Discharge Authority form

All lenders should be required to provide a standardised Discharge Authority form to borrowers to complete. The form should be easy to access, fill out and submit.

Lenders should adopt an identical standard form template, rather than agreeing to common criteria and continuing to design their own forms, which would still potentially allow them to add fields or make forms unnecessarily complex. The form should only request details from the borrower that are necessary for their discharge request to be processed.

The design and implementation of the form will require further consultation with industry and regulators.

► Recommendation 3: A maximum timeframe for existing lenders to process discharge requests

All lenders should be subject to a maximum time limit of 10 business days to complete the discharge process.

The time limit should cover the period from when the borrower (or a third party acting on their behalf) submits the Discharge Authority form to when the existing lender is ready to begin the settlement process.

While stakeholder consultation has indicated that 10 business days is an appropriate time period for processing discharge requests, further stakeholder consultation will be required on the appropriate time limit, as well as factors including:

- the specific definition of the start and end points in the discharge process to which the time limit should apply
- exemptions to the time limit to account for circumstances in which the existing lender cannot meet the time limit due to factors outside their control.

The design and implementation of both recommendations will require further consultation with industry and regulators. We consider that these recommendations should be implemented as soon as practicable, allowing for constraints due to the COVID-19 pandemic.

187 Similar policy reforms to our recommendations have been made in the superannuation industry, where regulated superannuation funds and approved deposit funds are required to adhere to a maximum time limit (currently 3 business days under the *Superannuation Industry (Supervision) Regulations 1994*) to process customer requests to transfer their account balance to a different fund and provide a standardised form for customers to use to reduce errors and make the transfer process more efficient. Customers can also opt to use a form provided by the Australian Taxation Office (ATO) or transfer their balance through myGov. The time limit only begins once the customer has provided all necessary information, and is subject to certain exemptions. Our discussion regarding recommendations 2 and 3 below refers to similar considerations in determining their design elements.
Sources:
The Australian Government the Treasury, *A plan to simplify and streamline superannuation*, May 2006, p. 51.
L Parker, 'Delays on super transfers to stop', Sydney Morning Herald, 13 June 2007, <https://www.smh.com.au/business/delays-on-super-transfers-to-stop-20070613-gdqd1o.html>, viewed 4 November 2020.
Australian Taxation Office, 'Rollover initiation request to transfer whole balance of super benefits between funds', 26 April 2017, <https://www.ato.gov.au/Forms/Rollover-initiation-request-to-transfer-whole-balance-of-superannuation-benefits-between-funds/>, viewed 4 November 2020.
Australian Prudential Regulation Authority, 'SuperStream—frequently asked questions', 4 July 2017, <https://www.apra.gov.au/superstream-frequently-asked-questions>, viewed 4 November 2020.
Moneysmart, 'Consolidating super funds', <https://moneysmart.gov.au/how-super-works/consolidating-super-funds>, viewed 4 November 2020.

We consider that, by streamlining the discharge process, our recommendations would improve the ability of borrowers to make switching decisions more efficiently based on a truer comparison of home loan offers between the new and existing lenders, because their decision-making would be less affected by pain points in the process. This, in turn, would generate additional demand-side pressure, incentivise lenders to compete more vigorously on the basis of their product pricing and offerings, and allow borrowers to move more quickly to more competitive offers and obtain the resulting benefits. Lenders would also benefit (as the new lender) by securing new borrowers more promptly and efficiently through competitive offers, and from a lower rate of borrowers dropping out during the switching process.

A maximum time limit for lenders to process a discharge request (recommendation 3) would also limit the time available to existing lenders to conduct retention strategies and encourage them to make their best retention offer earlier on. The borrower would then be able to compare the existing lender's most competitive offer to the new lender's offer, and make decisions more efficiently.

Recommendation 2: Require the use of a standardised discharge form that is easy for borrowers to access, fill out and submit

Lenders should be required to adopt a standardised discharge form and simplified processes for borrowers to make a discharge request. This will address the potential for unnecessary complexity and confusion in discharge processes (and associated delays). The form should only request details from the borrower that are necessary for their discharge request to be processed. Lenders should also ensure that the form is readily accessible (for example, on their website) and provide clear instructions to borrowers regarding how to complete and submit the form. Effective form and website design can have a major impact in terms of engaging consumers, shaping their decisions and assisting them to complete a task.¹⁸⁸

The ACCC considers that introducing a standardised discharge form among lenders is achievable based on our review of different lenders' discharge forms (see section 4.1). Notwithstanding the variations between forms across lenders (in terms of specific content, design and layout), our review indicates that their substantive requirements are consistent.

Furthermore, several stakeholders considered that discharge forms can be standardised, or that the fields can be simplified, to improve the switching process. For example, one smaller lender said introducing a standardised discharge form would simplify the discharge process and ensure the form only contained necessary fields, making it easier for borrowers to fill out correctly in the first instance. They also said that lenders can source at least some of the information currently requested in discharge forms from the existing information they have about the borrower. FinTech Australia supported the introduction of a standardised discharge form for individual borrowers, and listed the information fields that they considered could be included.

We consider it preferable that lenders adopt an identical standard form template, rather than agreeing to common criteria and continuing to design their own forms, which would still potentially allow them to add fields or make forms unnecessarily complex. An identical template across lenders will ensure that the form is simple and clear in all instances, provide additional clarity to borrowers, and resolve version control and accessibility issues (as borrowers will be able to access the template from multiple sources, rather than only from their existing lender, and be less likely to use an incorrect version of the form). We consider that the form should only request necessary information and documentation, and use plain language where possible. We also consider that the requirement to have this form should be drafted in a technology neutral way to take into account different consumer preferences for dealing with lenders.

We also recommend that lenders adopt similar, easy and clear processes for borrowers to access, complete and submit the discharge form. This includes, for example:

188 Field experiments have shown that modest design changes can influence consumer decision-making, and that enhanced form and website design is more likely to lead to consumer behavioural change.
Source:
S Benartzi and S Bhargava, 'How Digital Design Drives User Behavior', *Harvard Business Review*, 3 February 2020, <https://hbr.org/2020/02/how-digital-design-drives-user-behavior>, viewed 16 September 2020.

- providing borrowers with clear instructions at the start of the discharge process regarding what it will involve, and allowing them to complete all steps electronically (if they prefer to do so). For example, lenders should provide open access to the discharge form on their websites and allow for the electronic submission of discharge forms¹⁸⁹
- removing unnecessary requirements such as wet signatures and the physical submission of paperwork, where possible
- allowing for appropriately authorised third parties (for example, a settlement agent, mortgage broker or new lender) to complete and submit discharge forms on borrowers' behalf.

We understand that there is a broader industry shift towards the increased digitisation of transactions (see box 4.3 below). Many stakeholders are supportive of digital enhancements to speed up the switching process between lenders, as noted in box 4.3. We consider that this is a relevant environmental consideration that will, alongside our recommendations, make the overall switching process quicker and easier for borrowers to complete.

Box 4.3: Digitisation to improve the switching process between lenders

Transactions are becoming increasingly digitised, resulting in the greater use of e-signatures, remote ID verification and electronic, rather than paper-based, document production. We consider that these are positive steps that will, alongside our recommendations, increase the efficiency of the overall switching process (see figure 1.1).

A considerable number of stakeholders expressed their support for increased digitisation, or noted how borrowers benefit from or prefer digital processes, helping to break consumer inertia. In a media release from June 2020, the Australian Banking Association said that a number of associations, including themselves, were advocating for the temporary digitisation of transactions in response to the COVID-19 pandemic to *'be made permanent to save time, money and hassle for Australian customers'*.¹⁹⁰ In its interim report released in September 2020, the Senate Select Committee on Financial Technology and Regulatory Technology recommended that legislation and regulations be amended to allow for e-signatures, remote witnessing and the electronic execution of legal documents.¹⁹¹ The Government's Digital Business Plan similarly focuses on measures to support the transition towards a digital economy.¹⁹² A number of jurisdictions in Australia have mandated e-conveyancing (as opposed to paper-based conveyancing), and it is currently available in all states and territories except for Tasmania, the Australian Capital Territory and the Northern Territory.

The ACCC expects that switching timeframes will naturally reduce as steps in the process become increasingly digitised and automated, given the above developments. We also consider that Open Banking and the Consumer Data Right will help expedite the switching process (see section 1.3). We expect that these technological shifts, alongside our recommendations, will assist in reducing cumulative consumer fatigue over the entire switching process.

We recognise that paper-based options should remain available alongside electronic processes for vulnerable consumer groups or consumers that do not have ready access to computers or the internet. We also note consideration will need to be given to the cybersecurity and fraud risks arising from the increased digitisation of transactions.

189 In its submission in response to the ACCC's proposed recommendations, FinTech Australia noted that its members suggested *'that there should be a standardised delivery mechanism for discharge authorities. Ideally, all lenders should nominate a single email address to which all discharge authorities should be sent, instead of those authorities having to be directed to particular branches or lenders in charge of the switching borrower's facility.'*

190 Other associations included the Customer Owned Banking Association, the Business Council of Australia, the Australian Institute of Company Directors and the Financial Services Council, among others.

Source:

Australian Banking Association, 'Electronic transactions and mortgages should be here to stay', 18 June 2020, <https://www.ausbanking.org.au/electronic-transactions-and-mortgages-should-be-here-to-stay/>, viewed 14 August 2020.

191 See recommendations 3 and 4, The Senate, Select Committee on Financial Technology and Regulatory Technology, *Interim Report*, September 2020, pp. 208–209.

192 Prime Minister of Australia, 'Digital Business Plan to Drive Australia's Economic Recovery', 29 September 2020, <https://www.pm.gov.au/media/digital-business-plan-drive-australias-economic-recovery>, viewed 29 October 2020.

Recommendation 3: Implement a maximum time limit of 10 business days for lenders to complete the discharge process

We consider that there should be a maximum time limit for all existing lenders to complete the discharge process (as defined in box 4.1). We consider that this will encourage lenders to adopt more efficient discharge processes.

The time limit should cover the period from when the borrower (or a third party acting on their behalf) submits the discharge form to when the existing lender is ready to begin the settlement process. As a starting point for further consideration, and based on our consultation with stakeholders (see box 4.4 below), our view is that the maximum time limit should be 10 business days. However, we consider that further stakeholder consultation is required, including on the specific definition of the start and end points in the discharge process to which the time limit should apply. In determining this, careful consideration will need to be given to which components of the discharge and settlement processes are the responsibility of the existing lender and are visible to third parties. This will ensure that the time limit is practical to follow, monitor and enforce. There may be scope to allow for additional time for paper-based property transfers (as compared to electronic transfers).

We accept that there may be legitimate circumstances in which the existing lender cannot meet the time limit due to factors outside their control. These may include, for example, widespread system outages, natural disasters, and events similar to the COVID-19 pandemic. Stakeholder consultation would be required to determine the necessary exemptions for such scenarios. Exemptions may also apply for specific categories of discharge applications that are more complex, such as, for example, where the loan is covered by a guarantee or the borrower has other debt also secured by the property due to be released. While exemptions may be required for certain scenarios, we consider that a time limit should generally apply to the majority of discharge applications made by borrowers.

In addition to exemptions, there may be scope to restart or pause the time limit if the borrower (or their representative) is responsible for any errors or delay. We note that the use of a standardised discharge form and simplified processes for its completion (recommendation 2) will assist borrowers in completing and submitting forms correctly and efficiently in the first instance.

Box 4.4: Stakeholder views on how long it should take to discharge a home loan

There was a widely held view among stakeholders that the time currently taken by lenders to discharge a mortgage is too slow. Of the stakeholders that provided views on how long the discharge process should take, most considered that around 10 business days or less was sufficient for both paper-based and digital property transfers. Most of them also considered that the time required for paper-based property transfers should be approximately the same or slightly more than that for digital property transfers. More generally, a number of stakeholders noted that discharge timeframes should naturally reduce as processes become increasingly digitised (for example, due to the adoption of e-signatures, e-conveyancing and electronic Titles). Stakeholder views on discharge timeframes are summarised below:

- The Mortgage and Finance Association of Australia said that lenders should process discharge forms and be ready to book settlement within 10 business days, and that this '*should be a maximum period (not a target)*'. They considered that '*15 business days or more [for a lender to complete the discharge process] is unreasonable and causes consumer harm and expense to small businesses*'.
- One mid-tier lender considered that it should take 14 business days from when lenders receive discharge forms to settlement, while another mid-tier lender considered that it should take 10 business days, provided the lender receives correct information. A third mid-tier lender considered that lenders should generally be able to complete the entire end-to-end process of discharging a mortgage (including settlement) within 10 business days (assuming that the new lender is also ready for settlement).
- One market participant considered that it should take 2 business days from when a borrower requests a discharge to when the existing lender is ready to book settlement.
- One smaller lender considered that lenders should be able to process a discharge form in as quickly as one day and complete the discharge and settlement processes in far less than 15 business days. Another small market participant considered that lenders should be able to process discharge forms and be ready to book settlement within 2 business days for digital property transfers, and within 7 business days for paper-based transfers.
- FinTech Australia said its members had provided varying timeframes for how long lenders should take to process discharge forms and be ready for settlement, ranging from 2 to 8 business days for digital property transfers, and 4 to 11 business days for paper-based transfers.

Implementation considerations

The ACCC considers that the proposed recommendations should be mandated through regulatory intervention. Government regulation will allow for the necessary level of precision and clarity in designing the proposed requirements, and ensure that lenders are subject to uniform requirements and compliance mechanisms.

Regulation will also ensure that the requirements apply to all lenders in the home loan market. When consulted regarding the proposed recommendations, the Australian Banking Association and the Customer Owned Banking Association, who govern the Banking Code of Practice and the Customer

Owned Banking Code of Practice respectively,¹⁹³ expressed the view that any new obligations should apply equally to all lenders and not just to industry code subscribers.

The regulations will need to contain appropriate compliance and enforcement mechanisms. The ACCC acknowledges that such mechanisms can apply an uneven burden across lenders and that careful consideration is required to minimise the impact of regulatory burden.

In relation to recommendation 3, it may also be effective to make lenders publicly accountable regarding their compliance with the maximum time limit through reporting obligations. We note that a public reporting mechanism has been used to encourage compliance with regulatory timeframes in relation to the COVID-19 Early Release Scheme,¹⁹⁴ where APRA publishes weekly data on application processing times for the early release of superannuation payments.¹⁹⁵ For recommendation 3, lenders could similarly be required to publicly report discharge processing times. This may involve, for example, the average number of days taken to process discharge requests over a given period or the proportion of discharge requests processed on time. These statistics could be measured against compliance targets to ensure that lenders generally meet the expected standard. More serious enforcement mechanisms, such as penalties, could then be pursued in cases of repeated or persistent non-compliance.

193 The Australian Banking Association's membership is comprised of 22 banks from across Australia. Australian Banking Association members include the big four banks, regional banks and international banks with an Australian banking licence. Australian Banking Association members are required to subscribe to the Banking Code of Practice as a condition of membership to the Australian Banking Association.

The Customer Owned Banking Association represents Australian customer owned banking providers, and is owned by 63 member institutions including 34 credit unions, 27 mutual banks and 1 building society. Customer Owned Banking Association members are not required to subscribe to the Customer Owned Banking Code of Practice, however the Customer Owned Banking Association Code Compliance Committee website states that '*most credit unions, mutual banks and mutual building societies in Australia subscribe to the Customer Owned Banking Code of Practice*'.

Sources:

Australian Banking Association, 'The ABA', <https://www.ausbanking.org.au/about-us/the-aba/>, viewed 20 August 2020.

Australian Banking Association, 'New Banking Code of Practice will be compulsory, binding and enforceable', 26 March 2018, <https://www.ausbanking.org.au/new-banking-code-of-practice-will-be-compulsory-binding-and-enforceable/>, viewed 20 August 2020.

Customer Owned Banking Association, 'Who we represent', <https://www.customerownedbanking.asn.au/about-coba/who-we-represent>, viewed 20 August 2020.

Customer Owned Banking Code Compliance Committee, 'Code Subscriber register', <https://www.cobccc.org.au/code-of-practice/code-register/>, viewed 20 August 2020.

194 The COVID-19 early release of superannuation scheme allows individuals financially affected by the COVID-19 pandemic to access some of their superannuation early. Eligible citizens and permanent residents have been able apply once in each of the 2019-20 and 2020-21 financial years to access up to \$10,000 of their superannuation.

Source:

Australian Taxation Office, 'COVID-19 early release of super', 25 September 2020, <https://www.ato.gov.au/individuals/super/in-detail/withdrawing-and-using-your-super/covid-19-early-release-of-super/>, viewed 25 September 2020.

195 APRA has provided guidance for how long stages in the early release of superannuation scheme should take. Applicants for the early release of superannuation must first submit their application to the ATO, which can take up to four business days to be processed before the application is forwarded to the superannuation fund for payment. APRA has set a five business day guidance period for superannuation funds to make payments to applicants after the receipt of applications from the ATO, but also acknowledges that these timeframes may extend slightly due to a high volume of applications and that delays may also occur in exceptional circumstances.

Over the period from the start of the scheme on 20 April 2020 to 25 October 2020, superannuation release payments have been made to eligible members in an average of 3.3 business days after receipt by funds of the application from the ATO, and 95% of payments have been made within five business days.

Sources:

Australian Prudential Regulation Authority, 'APRA publishes weekly data on the superannuation early release scheme', 21 September 2020, <https://www.apra.gov.au/news-and-publications/apra-publishes-weekly-data-on-superannuation-early-release-scheme>, viewed 25 September 2020.

Australian Prudential Regulation Authority, 'COVID-19 Early Release Scheme—Issue 27', 2 November 2020, <https://www.apra.gov.au/covid-19-early-release-scheme-issue-27>, viewed 4 November 2020.

5. Continued monitoring of prices and competition in the home loan market

Key findings

- The ACCC's two inquiries into the home loan market have shed light on a range of pricing practices by lenders which detract from competition and adversely affect consumers. While certain lenders have taken action to remedy some of these issues, the persistence of these issues continues to inhibit price competition in the home loan market.
- The ongoing monitoring of prices and competition in the home loan market is needed to continue to provide transparency to the Australian Government and consumers on lenders' pricing practices, to monitor the impact of government initiatives and regulatory reform on home loan prices, and to identify emerging or persistent issues that impede price competition. Where appropriate, the ACCC will make recommendations to remedy these issues and improve competition and consumer outcomes in the home loan market.

This chapter sets out why the ACCC continuing to monitor and report on prices and competition in the home loan market is necessary to continue to support competition and improve consumer outcomes.

The \$1.8 trillion home loan market plays a vital role in the Australian economy.¹⁹⁶ It enables many Australians to purchase their first home, to move between homes as their needs and circumstances change, and for some, to invest in residential property.¹⁹⁷ Home loan prices also have a significant impact on household budgets. For households with a home loan, repayments on that loan are often their largest ongoing expense.¹⁹⁸

In the 2017–18 Budget, the Australian Government announced additional funding for the ACCC to establish a dedicated unit to undertake regular inquiries into specific financial system competition issues. The Government said it would facilitate greater and more consistent scrutiny of competition matters in the economy's largest sector, which had been lacking to date.¹⁹⁹

196 The figure of \$1.8 trillion refers to the stock of housing credit outstanding with financial institutions operating in Australia. It does not include cross-border and non-intermediated lending. Reserve Bank of Australia, *Statistical Tables—Lending and Credit Aggregates—D2*, <https://www.rba.gov.au/statistics/tables/>, viewed 3 September 2020.

197 The home loan market also enables investors to provide rental accommodation for many Australians. Based on data from CoreLogic, in June 2016, investors owned 27% of Australian dwelling stock by number of properties and 24% by value. Source: CoreLogic, *Profile Of The Australian Residential Property Investor*, June 2016, https://www.corelogic.com.au/resources/pdf/reports/CoreLogic%20Investor%20Report_June%202016.pdf, p. 4.

198 Based on the most recent census data (2016), more than 2.85 million Australian households (35% of all households) owned a house with a home loan. For these households the median monthly home loan repayment was \$1,755 (or \$21,060 annually) in 2016.

Further, based on ABS data, current housing costs were the largest household expense in the 12 months to June 2016, accounting for 20% of household spending. Current housing costs include spending on rent, interest payments on mortgages, rates, home and content insurance and repairs and maintenance. They do not include principal repayments on home loans.

Sources:

Australian Bureau of Statistics, *2016 Census Quickstats*, Australia, https://quickstats.censusdata.abs.gov.au/census_services/getproduct/census/2016/quickstat/036?opendocument, viewed 3 September 2020.

Australian Bureau of Statistics, *6530.0—Household Expenditure Survey, Australia: Summary of Results 2015–16*, September 2017, <https://www.abs.gov.au/statistics/economy/finance/household-expenditure-survey-australia-summary-results/latest-release>, viewed 3 September 2020.

199 The Commonwealth of Australia, *Budget 2017, Banking and Financial Services—A more accountable and competitive banking system*, https://archive.budget.gov.au/2017-18/glossies/factsheets/FS_Banking.pdf, p. 3.

See also:

The Commonwealth of Australia, *Budget 2017–18, Budget Paper 1: Budget Strategy and Outlook*, <https://archive.budget.gov.au/2017-18/bp1/bp1.pdf>, pp. 1–24.

The Honourable Scott Morrison MP, 'Budget Speech 2017–18 delivered on 9 May 2017 on the second reading of the Appropriation Bill (No. 1) 2017–18 by the Honourable Scott Morrison MP Treasurer of the Commonwealth of Australia', https://archive.budget.gov.au/2017-18/speech/Budget_speech.pdf, p. 9.

Since 2017, the Treasurer has directed the ACCC to undertake two home loan price inquiries.²⁰⁰ These inquiries have shed light on a range of pricing practices by lenders which detract from price competition in the home loan market and adversely affect consumers (see box 5.1). While there have been actions by certain lenders to remedy some of these issues,²⁰¹ their persistence continues to inhibit competition in the home loan market.

Box 5.1: Pricing practices identified in the Residential mortgage price inquiry and the Home loan price inquiry

- **A lack of price transparency:** while there has been some movement toward more transparent home loan prices since the ACCC's Residential mortgage price inquiry, some lenders' continued use of opaque discretionary discounts makes product comparison unnecessarily difficult, lessens consumers' willingness to shop around and stifles price competition (see chapter 3).²⁰²
- **A difference between the prices paid on new and existing home loans:** lenders' focus, in particular the big four banks, on attracting new home loan customers through offering increasingly large discounts, has created a significant gap between the average interest rate on new loans compared to existing loans.²⁰³ That price gap tends to increase with the age of a home loan, and disproportionately affects borrowers who do not switch or who are unable to switch (see figure 1.3, figure 1.4 and figure 2.1).
- **Oligopolistic behaviour:** the big four banks, who account for close to 80% of the home loan market (by value of housing credit outstanding), have exhibited signs of oligopolistic behaviour and demonstrated a lack of vigorous price competition when setting their home loan interest rates. For example, at times, when setting variable interest rates, the big four banks have been accommodative and focused on each other, giving little regard to smaller lenders.²⁰⁴
- **Reductions in the cost of funds not flowing through to interest rates paid by borrowers:** reductions in the headline interest rate and average interest rate on owner-occupier home loans with principal and interest repayments at the big four banks were smaller than the reduction in their respective cost of funds over the period January 2018 to October 2019. This was also the case for investor home loans with interest-only repayments for three of the big four banks.²⁰⁵

Given the importance of the home loan market to the Australian economy, the impact of home loan pricing on household budgets, and the ongoing pricing practices by lenders that impede price competition and adversely impact consumers, the ACCC should continue to monitor and report on prices and competition in the home loan market for a five year inquiry period, reporting annually from 2022.

A Direction from the Treasurer to the ACCC to undertake such an inquiry into competition and pricing in the home loan market, will enable the ACCC to use its compulsory information and document gathering powers under section 95ZK of the *Competition and Consumer Act 2010*. The ACCC will be able to require lenders to provide information and produce documents, including information and documents explaining any changes or proposed changes to their prices (interest rates, fees and charges). Access to this material will allow the ACCC to undertake an in-depth examination of pricing decisions to identify pricing practices that are having an impact on competition (and therefore on outcomes for consumers).

200 See:

Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*.

Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*.

Australian Competition and Consumer Commission, *Home loan price inquiry interim report*.

201 For example, in the *Home loan price inquiry interim report*, we found that in the second half of 2019, Westpac was offering higher advertised discounts, in order to improve the transparency of discounts and reduce its reliance on opaque discretionary discounts.

Source: Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 54–55.

202 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, pp. 7, 21–22.

203 Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, pp. 7–8.

Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 58–62.

204 Australian Competition and Consumer Commission, *Residential mortgage price inquiry interim report*, pp. 6–8.

205 Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 41, 49–50.

The continued annual monitoring of prices and competition should focus on the 10 largest home loan lenders²⁰⁶ and report on:

- the difference between prices paid on new and existing home loans
- the difference between the prices advertised for home loans and the prices borrowers actually pay, including the prevalence and size of discretionary discounts
- material changes in the interest rates charged by lenders, and whether, for example, they reflect movements in the cost of funds
- material changes in the fees and charges charged by lenders.

It would also be appropriate for the ACCC's ongoing monitoring to also consider the pricing decisions of other lenders or groups of lenders, such as non-ADIs, as price and competition issues are identified that involve or may impact those lenders.

The ongoing monitoring and reporting on prices across the largest 10 lenders would enable the ACCC to:

- understand whether previously identified impediments to price competition persist across the broader home loan market²⁰⁷ and recommend whether government or regulatory intervention is required (see, for example, potential future recommendations discussed in chapter 3)
- identify trends, emerging issues and price movements that require further examination and explanation.

Monitoring and reporting on the pricing decisions of lenders would also allow the ACCC to examine and report on whether government initiatives and regulatory reform designed to increase price transparency, consumer engagement and switching, including the Consumer Data Right, and the recommendations in this report, are impacting prices and competition.

In addition, regular reporting on lenders' prices and pricing decisions by the ACCC will provide additional transparency to the Government and regulators, and help support evidence-based policy decisions about any future interventions in the home loan market. As the Australian economy recovers from the COVID-19 pandemic,²⁰⁸ it will be particularly important to identify whether the temporary

206 As at 30 June 2020, the 10 largest lenders held \$1.6 trillion in housing credit outstanding and accounted for over 90% of housing credit outstanding with ADIs.
Source: Australian Prudential Regulatory Authority, *Monthly authorised deposit-taking institution statistics June 2020*, 31 July 2020. <https://www.apra.gov.au/monthly-authorised-deposit-taking-institution-statistics>, viewed 3 September 2020.

207 The Residential mortgage price inquiry focused on the pricing of residential mortgage products by ADIs subject to the Major Bank Levy—that is the big four banks and Macquarie Bank.
The *Home loan price inquiry interim report* focused on the prices of home loans of the big four banks.
As at 30 June 2020, the big four banks held \$1.38 trillion in residential housing credit, which is 78% of the stock of residential housing credit outstanding (by value).
Sources:
Australian Competition and Consumer Commission, *Residential mortgage price inquiry final report*, p. 4.
Australian Competition and Consumer Commission, *Home loan price inquiry interim report*, pp. 12–13.
Australian Prudential Regulatory Authority, *Monthly authorised deposit-taking institution statistics June 2020*, 31 July 2020, <https://www.apra.gov.au/monthly-authorised-deposit-taking-institution-statistics>, viewed 3 September 2020.

208 The Australia economy contracted 7% in the June quarter 2020. The RBA estimates that over the 2020 calendar year the Australian economy will contract by 4% as a result of the COVID-19 pandemic.
Source: Reserve Bank of Australia, *Statement on Monetary Policy—November 2020*, 2020, pp. 37, 80.

measures, including home loan repayment deferrals²⁰⁹ and initiatives to lower funding costs,²¹⁰ have a lasting impact on pricing and competition in the home loan market.

Further, regular reporting by the ACCC would continue to raise consumer awareness of pricing issues, such as the difference between the prices paid on new and existing loans and opaque pricing practices, and may promote greater consumer engagement in the home loan market. As an example of the impact of the ACCC's home loan inquiries and associated media coverage, one of the big four banks identified that:

'Regulatory reviews such as the ACCC's Residential Mortgages Inquiry have urged customers to consider switching providers to obtain the best possible price. The effects of this have been enhanced by statements from politicians and extensive media coverage encouraging consumers to do the same. This has led to increased public awareness that switching providers is:

- *an option consumers have available to them to pursue best possible rates; and*
- *may be less arduous than the customer realised.'*

We recognise that the ongoing monitoring of pricing and competition issues in the home loan market would create an additional reporting burden for some lenders. However, the ACCC's experience in undertaking inquiries into the home loan market, the use of standardised reporting templates the ACCC has developed over the course of two home loan price inquiries, and the use of data held by other agencies,²¹¹ would all help to minimise the reporting burden.

The ongoing monitoring of prices and competition in the home loan market would be in addition to other inquiries into specific financial system competition issues, as directed by the Treasurer.

209 Over \$192 billion (11%) of home loans have had their repayments deferred as at 9 July 2020.

Source: Australian Prudential Regulatory Authority, *Temporary loan repayment deferrals due to COVID-19*, 9 July 2020, <https://www.apra.gov.au/temporary-loan-repayment-deferrals-due-to-covid-19-0>, viewed 5 October 2020.

210 There have been a number of measures implemented in 2020 to lower the funding costs of Australian lenders to encourage credit growth, in particular business lending. These include:

- In March 2020, the RBA lowered the cash rate target to 0.25%, introduced a target of 0.25% for the 3-year Australian Government bond yield and implemented a three-year term funding facility (TFF) at a cost of 0.25% for ADIs. Further, in March 2020, the Australian Government introduced a \$15 billion structured finance support fund, administered by the Australian Office of Financial Management, to make targeted investments in structured finance markets used by smaller lenders that provide consumer and business finance by investing in rated term securitisations and in rated and unrated securitisation warehouses.
- In September 2020, the RBA increased the size of the TFF and extended the time period for entities to access this funding.
- In November 2020, the RBA lowered the cash rate target to 0.1%, reduced the target for the yield on 3-year Australian Government bonds to 0.1%, and reduced the interest rate on new drawings under the TFF to 0.1%.

Source:

Reserve Bank of Australia, *Statement on Monetary Policy—August 2020*, 2020, p. 4.

Australian Office of Financial Management, *Structured Finance Support Fund*, March 2020, <https://www.aofm.gov.au/sfsf>, viewed 5 October 2020.

Reserve Bank of Australia, *Statement on Monetary Policy—November 2020*, 2020 p. 4.

211 For example, the ACCC's previous inquiries into the home loan market have published data from the Economics and Financial Statistics collection which is administered by APRA on behalf of the ABS and RBA, and the RBA's Securitisation Dataset to minimise the reporting burden on lenders.

For further information on the Economics and Financial Statistics collection, see: Australian Prudential Regulatory Authority, *Economic and financial statistics—frequently asked questions*, 17 September 2020, <https://www.apra.gov.au/economic-and-financial-statistics-frequently-asked-questions>, viewed 5 October 2020.

For further information on the RBA's Securitisation Dataset, see: Reserve Bank of Australia, 'The Reserve Bank's Securitisation Dataset', *Bulletin—December 2018*, December 2018.

► **Recommendation 4: Continued monitoring of competition and prices in the home loan market**

The ACCC should continue to inquire into and monitor competition and pricing in the home loan market, under government direction.

In undertaking this role the ACCC should consider the following matters:

- the difference between prices paid on new and existing home loans
- the difference between the prices advertised for home loans and the prices borrowers actually pay
- the prices charged by, and pricing decisions of, lenders
- the impact of current and future government initiatives and regulatory interventions, including the Consumer Data Right and the recommendations in the *Home loan price inquiry final report*, on home loan prices, including interest rates, fees and charges
- other emerging issues and lender practices that impede competition or outcomes for consumers that arise during the inquiry period.

The inquiry should focus on the 10 largest lenders in the home loan market and consider other lenders or groups of lenders (such as non-ADIs) as competition issues are identified that involve or impact those lenders.

The ACCC should report to the Treasurer annually over a five year period, providing its first report to the Treasurer by 30 September 2022.

Appendix A Competition and Consumer (Price Inquiry—Home Loans) Direction 2019



Competition and Consumer (Price Inquiry— Home Loans) Direction 2019

I, Josh Frydenberg, Treasurer, give the following direction to the Australian Competition and Consumer Commission.

Dated 14/10/2019



Josh Frydenberg
Treasurer

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Part 1—Preliminary

1 Name

This instrument is the *Competition and Consumer (Price Inquiry—Home Loans) Direction 2019*.

2 Commencement

- (1) Each provision of this instrument specified in column 1 of the table commences, or is taken to have commenced, in accordance with column 2 of the table. Any other statement in column 2 has effect according to its terms.

Commencement information		
Column 1	Column 2	Column 3
Provisions	Commencement	Date/Details
1. The whole of this instrument	The day after this instrument is registered.	

Note: This table relates only to the provisions of this instrument as originally made. It will not be amended to deal with any later amendments of this instrument.

- (2) Any information in column 3 of the table is not part of this instrument. Information may be inserted in this column, or information in it may be edited, in any published version of this instrument.

3 Authority

This instrument is made under the *Competition and Consumer Act 2010*.

4 Definitions

Note: Expressions have the same meaning in this instrument as in the *Competition and Consumer Act 2010* as in force from time to time—see paragraph 13(1)(b) of the *Legislation Act 2003*.

In this instrument:

Australian credit licensee has the meaning given by the *National Consumer Credit Protection Act 2009*.

authorised deposit-taking institution has the meaning given by the *Banking Act 1959*.

exempt supply has the meaning given by subsection 95A(1) of the Act.

goods has the meaning given by subsection 95A(1) of the Act.

home loan means a loan secured by a mortgage over one or more residential premises.

inquiry has the meaning given by subsection 95A(1) of the Act.

Part 1 Preliminary

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price has the meaning given by subsection 95A(1) of the Act.

residential premises has the same meaning as in the *A New Tax System (Goods and Services Tax) Act 1999*.

services has the meaning given by subsection 95A(1) of the Act.

State or Territory authority has the meaning given by subsection 95A(1) of the Act.

supply has the meaning given by subsection 95A(1) of the Act.

the Act means the *Competition and Consumer Act 2010*.

Part 2—Price inquiry into the supply of home loans

5 Commission to hold an inquiry

- (1) Under subsection 95H(1) of the Act, the Commission is required to hold an inquiry into the market for the supply of home loans. The inquiry is *not* to extend to any of the following:
 - (a) the supply of a good or service by a State or Territory authority;
 - (b) the supply of a good or service that is an exempt supply;
 - (c) the conduct of the Australian Prudential Regulation Authority or the Australian Securities and Investments Commission;
 - (d) the conduct of a mortgage broker.

Note: The matters referred to in paragraphs (c) and (d) fall within scope of other inquiries.
- (2) For the purposes of subsection 95J(1), the inquiry is to be held in relation to goods and services of the following descriptions:
 - (a) home loans supplied by authorised deposit-taking institutions;
 - (b) home loans supplied by Australian credit licensees;
 - (c) home loans supplied by a person who would be covered by paragraph (a) or (b) apart from an exemption in force under the *Banking Act 1959* or the *National Consumer Credit Protection Act 2009*.
- (3) Under subsection 95J(2), the inquiry is *not* to be held in relation to the supply of goods and services by a particular person or persons.

6 Directions on matters to be taken into consideration in the inquiry

Under subsection 95J(6) of the Act, the Commission is directed to take into consideration all of the following matters in holding the inquiry:

- (a) the prices charged, since 1 January 2019, by suppliers covered by subsection 5(2) for providing home loans, including:
 - (i) differences between the prices advertised and the prices actually charged or paid, with particular regard to interest rates published by suppliers and the interest rates paid by customers; and
 - (ii) differences between the prices charged to, or paid by, existing customers as compared to new customers; and
 - (iii) supplier pricing decisions following changes in the Reserve Bank of Australia's target for the cash rate (which is the overnight money market interest rate), including:
 - (A) the extent to which any resulting price changes were due to changes in suppliers' access to, and costs of, finance; and
 - (B) the timing of suppliers' announcements of price changes and their implementation of those changes; and
- (b) the extent and existence of supplier practices and strategies that create an impediment to existing home loan customers refinancing to an alternative supplier (commonly referred to as 'switching'), including impediments resulting from product features and the effect of product bundling; and

Part 2 Price inquiry into the supply of home loans

Section 7

- (c) other impediments to existing home loan customers refinancing to an alternative supplier, with particular regard to:
 - (i) consumer behaviour, including consumer decision-making, biases and choices; and
 - (ii) the availability to the public of information about prices actually being charged, or paid, for home loans.

7 Directions as to holding of the inquiry

Under subsection 95J(6) of the Act, the Commission is directed to do the following in holding the inquiry:

- (a) have particular regard to the activities of those with the largest shares of outstanding home loans by market value; and
- (b) give to the Treasurer an interim report on the inquiry by 30 March 2020.

8 Period for completing the inquiry

For the purposes of subsection 95K(1) of the Act, the inquiry is to be completed, and a report on the matter of inquiry given to the Treasurer, by no later than 30 September 2020.

EXPLANATORY STATEMENT

Issued by authority of the Treasurer

Competition and Consumer Act 2010

Competition and Consumer (Price Inquiry–Home Loans) Direction 2019

Section 95H of the *Competition and Consumer Act 2010* (the Act) provides that the Minister may require the Australian Competition and Consumer Commission (ACCC) to hold an inquiry into a specified matter or matters.

The *Competition and Consumer (Price Inquiry–Home Loans) Direction 2019* (the Direction) is made under subsection 95H(1) and provides a direction to the Chairperson of the ACCC requiring the ACCC to hold a price inquiry into the market for the supply of home loans.

The inquiry will support the Government’s commitment to promoting competition and good consumer outcomes in the home loan market, including by bringing more transparency to the pricing practices of the banks. As such, the Treasurer is requesting the ACCC hold a price inquiry into the market for the supply of home loans.

Part 1 of the Direction provides the machinery provisions of the instrument, including the definitions.

Part 2 of the Direction provides the terms of reference for the inquiry and guidance on the matters to be taken into consideration. The ACCC must have particular regard to the activities of those with the largest shares of outstanding home loans by market value.

The ACCC must give the Treasurer an interim report on the inquiry by 30 March 2020 and provide a report to the Treasurer by no later than 30 September 2020.

In accordance with section 17 of the *Legislation Act 2003*, the ACCC has been consulted on the terms of this Direction.

The Direction is a legislative instrument for the purposes of the *Legislation Act 2003*. However, the instrument is not disallowable and does not sunset (see *Legislation (Exemptions and Other Matters) Regulation 2015*).

The Direction commences the day after the instrument is registered.

A statement of Compatibility with Human Rights is at Attachment A.

ATTACHMENT A

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Competition and Consumer (Price Inquiry–Home Loans) Direction 2019

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

Section 95H of the *Competition and Consumer Act 2010* (the Act) provides that the Minister may require the Australian Competition and Consumer Commission (ACCC) to hold an inquiry into a specified matter or matters.

The *Competition and Consumer (Price Inquiry–Home Loans) Direction 2019* (the Direction) is a direction to the Chairperson of the ACCC to hold a price inquiry into the market for the supply of home loans.

The Direction sets out the terms of reference for the inquiry.

Human rights implications

This Legislative Instrument does not engage any of the applicable rights or freedoms.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.

Appendix B The fees and charges to switch lenders

In addition to the time and effort involved in switching lenders (see chapter 1), borrowers typically incur monetary costs. For example, the fees and charges involved in switching a home loan²¹² from one of the big four banks to another in June 2020 included:

- a discharge and/or settlement fee of \$320–350, depending on which bank was the existing lender. This fee applies when a home loan is repaid and the mortgage over the security property is released (see table B.1)
- a loan establishment fee of \$395–600 depending on which bank was the new lender and whether the home loan was taken as a package (see table B.2)
- land titles office charges in the order of \$220–\$400 in total, depending on the state or territory in which the security property was located. These charges relate to the registration of the discharge of the existing lender’s mortgage and the registration of the new lender’s mortgage over the security property.²¹³

Depending on their circumstances, borrowers may have to pay other costs to switch lenders.

- Fixed rate borrowers may also have to pay a break fee to their lender if they repay their home loan before the expiry of their fixed rate contract. The amount of this break fee will depend on how interest rates have changed since the borrower locked in their fixed rate, the remaining fixed rate period and the home loan balance.
- Depending upon the amount of the home loan and the value of residential property offered as security, the borrower may need to pay a lenders mortgage insurance²¹⁴ premium at the new lender. Lenders mortgage insurance is often required where the home loan amount exceeds 80% of the value of the residential real estate offered as security for the loan. The size of the premium will depend on the amount of the home loan and the value of residential property, and could be thousands of dollars.
- Borrowers may also be required to pay government stamp duty as part of their refinance.²¹⁵

Table B.1: Mortgage discharge and settlement fees: 30 September 2020

	ANZ	CBA	NAB	WBC
	\$	\$	\$	\$
Mortgage discharge ^a /production fee ^b	160	350 ^c	350	350
Settlement fee	160	—	—	—

- a The fee includes the preparation of a discharge of mortgage and the bank’s attendance at settlement for CBA, NAB and WBC. The fee is referred to as ‘discharge settlement fee’ at CBA.
- b ANZ does not charge a discharge fee. ANZ charges a ‘production fee’ of \$160 for each certificate of title or other security document produced as a result of a customer switching home loan lender or paying out their home loan.
- c The fee does not apply to residential mortgages taken under the bank’s ‘No Fee’ products.

212 For the purpose of this example, the home loan is assumed to have been secured by a single residential property.

213 The range of fees is based on the fees disclosed on the websites of the land titles offices for the eight Australian states and territories. The sites were visited either on 5 August 2020 or 7 August 2020, depending on the jurisdiction.

214 Lenders mortgage insurance is insurance that protects the lender from loss in the event that the borrower defaults and the lender is unable to recover the outstanding loan balance, including through the sale of the security property.

215 Moneysmart, ‘Switching home loans’, <https://moneysmart.gov.au/home-loans/switching-home-loans>, viewed 6 August 2020.

Table B.2: Establishment fees for standard home loans:* 30 September 2020^

	ANZ	CBA	NAB	WBC
Loan establishment fee	\$600 ^a	\$600 ^b	\$600	\$600
Annual package fees	\$395	\$395	\$395	\$395

* Standard home loans are those supplied with a range of add-on features.

^ Establishment fees reported are those applying to unpackaged standard variable rate home loans for owner-occupiers under the bank's main brand. Depending on the bank, 'establishment fees' are referred to as establishment fees (CBA and WBC), application fees (NAB), or loan approval fees (ANZ).

a A lodgment fee of \$160 is also payable on the registration of each mortgage security.

b CBA does not charge a loan establishment fee for home loans taken as part of a package. The fee increases to \$800 for residential properties purchased from off the plan.



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