MacKay ON MONEY

BY AUTHORISED FINANCIAL ADVISER CHRIS MACKAY

No one likes filling in forms. I hate them. Looking back I reckon I've filled in thousands over my three decade financial services career.

That's a truck load of insurance proposals, investment and mortgage applications and more recently KiwiSaver plans.

Mind you, because of all these forms, our firm or its Advisers have been instrumental in organising millions of dollars in home loans and in paying out tens of millions in insurance claims, super schemes and investment plan maturities to a ton of happy clients. So that's very good.

Some forms are easy to complete. Some should be, but are diabolical.

Last year, I had to renew some legislative regulation type requirement on line. It should only have taken a few minutes. After completing a section I moved on to the next part and finally was herded nicely to the submit and pay screen. But no, I'd made a blue somewhere so I got bumped back. I fixed the "problem" and pulled out the credit card again. But sorry, still not quite right somewhere. I fixed another "problem". Plastic poised again. Not quite. I hadn't quite nailed it. Five or 10 of these setbacks and half an hour later, the stuffing had been knocked out of me.

I figured it wasn't me. I rang the IT help desk jockey who told me what to do. Didn't work. Tried something else. No good either. And again and again.

The excellent but by now equally frustrated IT guru then got me to give control of my computer to him. Children and luddites, do not try this if some nice person with an accent rings you from some big computer or phone company and tells you they can fix your home computer. My guy works for the Government, so I was quite happy for him to move my mouse all around my screen while I watched in technophobic amazement. I had rung him in the first place too so I figured the chances of him being a Albanian phisher was unlikely.

If he couldn't fill in all the boxes on my renewal form and hasten the transfer of some money from the private to the public sector, no one could.

Well, after another half hour, he too gave up, relinquished control of my mouse and vowed to fix the bug back at HQ. He would get back to me. Which he did and to cut a long story short, it all ended happily ever after with the Government glitch repaired, my renewal renewed and my dough safely in the consolidated fund. A five minute form had turned into a three hour marathon.

If you are an Aussie applying for an old age pension in Australia; if you are an Aussie living in New Zealand or a Kiwi who had lived in Oz for so many years, and want to apply for NZ Super, you will be asked to fill in the Aussie superannuation form. Even if you are going to get NZ Super, you still need to fill in the Australian form. How long? A mere 31 pages. And only 84 questions. So when Quade Cooper comes home, that's what he's up for. [By the way, I hate the booing when Quade comes on in a test match. It's pathetic and it's boorish and it's not the Kiwi way. You know who you are. Give it away eh?]

My elderly mother has gas as well as electricity. So do we. A year or so back, after a number of estimate readings, she got a colossal bill. I sorted it and did a deal with the gas supplier for them to make sure they read her meter regularly. They still screw up and don't do it. But you can "fill in their form" over the phone by ringing the 0800 number and give them your own reading as you know.

This should be easy enough, but on a couple of occasions, the nicely spoken computer at the other end of the phone has told me my actual readings were outside of the range they would allow. So despite trying to enhance their revenue stream, they eschewed my largesse.

And then just recently, they did another estimate which was about five times greater than any previous actual and it resulted in a bill for over $2,100. Yes that's right folks. I figured I had better talk to a real person to get this form filled in correctly, which I did.

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I saw an interesting form last month. This one also from a Government agency. As you have read, I have filled out quite a lot of forms in the past 30 years and I reckon I'm pretty smart at interpreting them. I did some Commercial Law at uni and I can read and understand a contract and indeed, an intelligent and well written form.

For someone (not me) to become a second hand dealer and pawnbroker, one must fill in an application form which results in the dealer being issued with a photo ID card.

The application form requires someone, (lawyer, medical doctor, policemen, J.P.) to authenticate the applicant's identity. But missing from the form (and I read it from cover to cover several times) is the critical information as to on what basis can the authenticator authenticate the authenticatee.

Contra this with the passport application which spells out the authenticator must know the applicant for at least 12 months. Simple. These things shouldn't be hard. Investment companies are also required to establish client identity. But they spell out exactly what type of documentation or combination is required, be it certified copies of a passport, NZ Driver's License, NZ Gun License, utilities bill, bank statement, whatever.

I rang the Second Hand Dealers and Pawnbrokers Licensing Authority to check out the rules. First time I was directed to the person who may be able to help but she turned out to be a voicemail. Second time, after explaining to the operator I had just been forwarded to a voicemail, I ended up at the same voicemail. Being tenacious I tried one more time. This time the first answerer let me ask him the question. He didn't know but would get someone to call me back. Well, "someone" also didn't know the answer but was going to pass on my comments to "someone else". I double checked again while writing this article and spoke to a good guy at the Authority who read through the official Regulations while I waited on the phone. Guess What? There is nothing in the Regulations to spell out the process. Who drafts the Regulations? Turns out it's Parliament so I don't suppose I should be in the least surprised.

When you build a house or even do alterations these days you need to file a building consent form (and possibly a resource consent). If it's outside the standard building code (3604) then it requires an engineer to design the structure. There's a greater degree of compliance and information necessary these days before any building consent is issued. The Council has 20 working days from when the application form is submitted (or ready to be processed) to produce a building consent. More often than not there are often cases where further information is required which delays the process even further.

During building, heaps more forms are required to be filled by the builder and all licensed subcontractors. There are regular inspections by the Council of the building, plumbing and drainage where Council forms are produced at the end of each inspection. Then the engineer has to monitor and inspect the structural work he has designed and produces a PS4 form which goes to the Council along with all the warranties and guarantees from all the subcontractors. This is then compiled into a code compliance certificate (CCC) application form which the Council then processes and if OK, they do a final inspection of building work and then issue the owner with a CCC. That's a lot of forms!

Under the new Anti Money Laundering and Countering of Terrorism Act 2009 which came into being on July 1 2013, there are a whole lot of new rules and forms.

If you have bought any investments, opened a bank account or joined a KiwiSaver scheme since then you will understand. There's a ton of information one needs to provide in order to satisfy the investment company you are who you say you are. There is also a classification known as a "politically exposed person" or PEP and these people must pass a more rigorous test.

According to Wikipedia, "in financial regulation, [a] 'politically exposed person' (PEP) is a term describing someone who has been entrusted with a prominent public function, or an individual who is closely related to such a person….

Heavy fines have been imposed on financial institutions such as Riggs Bank [for most of its history, the largest bank in Washington D.C.] for conducting business with PEPs without following adequate Know Your Customer procedures and enhanced due diligence processes. PEP-specific compliance legislation underlines the link between corrupt politicians, money laundering and the financing of terrorism. Since September 11, 2001, more than 100 counties have changed their laws related to financial services regulation, with the fight against political corruption playing a fundamental role. Despite attempts at regulation, certain political leaders like Muammar Gaddafi and Hosni Mubarak have made news for having assets [frozen] in US banks that did not follow these processes for these individuals.

The designation 'Politically Exposed Person" dates back to the late 1990s [to] what was known as the "Abacha Affair".

Sani Abacha was a Nigerian dictator who organised (with his family members and associates) a network of massive theft of assets from the Government of Nigeria. It is believed several billion dollars were stolen, and the funds were transferred to bank accounts in the United Kingdom and Switzerland.

In 2001, in an effort to recover the money, the Nigerian Government that succeeded the Abacha regime lodged complaints with several European agencies, including the Federal Office of Policy (FOP) of Switzerland which, in turn, investigated close to 60 Swiss banks. In this investigation the concept of "Politically Exposed Person" emerged, which was later included in the 2003 United Nations Convention against Corruption."

That's why forms and identity requirements surrounding new investments are more rigorous than in the past.

Our company provides a mortgage broking service. The guys lending the money (the mortgagees) require a plethora of forms and documentation. They want to know the borrower (mortgagor) is in paid employment, has and will have more money coming in than going out, has good credit history (pays their bills) and the property is worth more than the mortgage. (The Reserve Bank of NZ, in order to dampen down the property market, has recently told the banks borrowers need to have 20 per cent of the house value as a deposit.) Why should a bank want a buffer? If the borrower defaults, then they know they can recover their loan plus overdue interest plus costs.

The NZ banks and home loan lenders have been relatively responsible over the past decade.

Contrast this with what caused the Global Financial Crisis (GFC). If you are interested, pick up a copy of "A Colossal Failure of Common Sense – The Incredible Inside Story of the Collapse of Lehman Brothers" by Larry McDonald. It's a great read.

This is it in a nutshell. In the early part of the century, Americans were sold the story house prices in the US had never gone up by less than five per cent since the Great Depression. They were told it's more like 10 per cent or 20 per cent at the moment. This will go on forever. There's a shortage of houses. The US Government wants poorer people owning their own home. Low interest rates make credit easy. Let's not worry about borrowers having any deposit. The house will go up by at least 10 per cent next year so if the borrower defaults, who cares; we'll sell the house for more than they paid and the mortgage lender will get its money back and there will even be some left over for the defaulting mortgagor. Do we need to fill in lots of forms? Well not really. Can the borrower fog a mirror? They are alive aren't they? Have they got a job? Well they almost got one last week. What sort of income? They get some welfare benefits. How much in the bank? Well none really. Any existing debts? Some credit card balances. Well, let's tidy those up too. Look why would you stay with your in-laws in this cramped apartment paying rent when you could move into a beautiful new home in a brand new subdivivision? Heck, it only costs $300,000, but we'll lend you $330,000 to tidy up your credit cards and allow you to buy some new furniture and maybe a holiday to Disney World for the family. The repayments are less than your current rent. We'll only charge you two per cent interest for the first couple of years and yes it will go up after than, but don't worry because the house will be worth $400,000 by then. If you can't afford it, then you can sell it and make a huge profit. Any forms to fill in? Not really – just sign here. These were the famous "Ninjna" loans. No income, no job, no assets. Sub prime mortgages – here we come!

The mortgage sales guys didn't care. They got a huge commission for selling the mortgage and I suppose the house too. If the borrower defaulted, it wasn't their problem. These ex pizza delivery boys and now "mortgage originator executives" were all making a fortune and there was no downside.

The companies providing the money also wouldn't care if the mortgages were dodgy because they would package up say a thousand of these mortgages, make it sound sexy by calling it a collateralized debt obligation (CDO), ring Lehmans or Merrill Lynch (John Key's old company) and flog the dog in disguise off to them.

Larry goes on:

"The investment banks used a technique called asset swaps to in effect provide immediate returns to investors, even though some of the mortgages started paying just the teaser rate of two per cent for the first couple of years."

Lehmans would add on a large margin, slice up the big CDO into million dollar chunks and on sell these to some other bank in Washington, UK, Japan or even Iceland.

"The final holder of the bond, the distant bank or fund, also held the deeds to the original houses which meant a homeowner in sunlit California could be sitting in a house that was owned by a couple of Eskimos out on the ice floes chasing polar bears, six thousand miles away."

The eventual owner may have even believed that they were "insured" through some specialised product known as a credit default swap. Second richest American, Warren Buffet, termed these complex derivative whizbangers, "financial weapons of mass destruction" and they were.

Even NZ got sucked in. ING who morphed into OnePath (now ANZ Investments) had a couple of retail funds invested in CDOs, possibly sourced from Lehmans. Who knows?

Anyway, it all turned to custard as you know. Mortgage repayments went up. Borrowers defaulted. They did runners in the middle of the night and left the house keys in the letter box or posted them back to the bank (known as jingle mail). House prices plummeted when the banks needed to sell them to recover their advances. Those parcels of sub prime loans, flogged off all around the world obviously dropped in value too. Overseas banks' capital disappeared over night. Lehmans couldn't on sell the most recent packages they had bought. Bankruptcy loomed, a bail out was a possibility, but in the end the US Treasury allowed Lehmans to go broke and then the fun started!

All because of slack process, greed, forgetting fundamentals and crappy application forms.

Feel informed? I hope so.

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