How to have your say

Submissions process

The Ministry of Business, Innovation and Employment (MBIE) seeks written submissions on the questions raised in this document.

- Submissions on the questions in Part 3 of this paper (relating to the Financial Service Providers Register) are due by **5pm on Friday 29 January 2016**.
- Submissions on the questions in Part 1 and Part 2 of this paper are due by **5pm on Friday 26 February 2016**.

Your submission may respond to any or all of these questions. We also encourage your input on any other relevant work. Where possible, please include evidence to support your views, for example references to independent research, facts and figures, or relevant examples.

Please include your name, or the name of your organisation, and contact details. You can make your submission:

- By filling out the submission template online.
- By attaching your submission as a Microsoft Word attachment and sending to ***faareview@mbie.govt.nz***.
- By mailing your submission to:

  Financial Markets Policy
  Ministry of Business, Innovation & Employment
  PO Box 3705
  Wellington
  New Zealand

Please direct any questions that you have in relation to the submissions process to: ***faareview@mbie.govt.nz***.

Use of information

The information provided in submissions will be used to inform MBIE's policy development process, and will inform advice to Ministers on the operation of the Financial Advisers Act 2008 and the Financial Service Providers (Registration and Dispute Resolution) Act 2008.

We may contact submitters directly if we require clarification of any matters in submissions.

Submissions are subject to the Official Information Act 1982. MBIE intends to upload PDF copies of submissions received to MBIE's website at ***www.mbie.govt.nz*** and will do so in accordance with that Act.

Please set out clearly with your submission if you have any objection to the release of any information in the submission, and in particular, which part(s) you consider should be withheld, together with the reason(s) for withholding the information under that Act.

If your submission contains any confidential information, please indicate this on the front of the submission, mark it clearly in the text, and provide a separate version excluding the relevant information for publication on our website.

MBIE reserves the right to withhold information that may be considered offensive or defamatory.

The Privacy Act 1993 establishes certain principles with respect to the collection, use and disclosure of information about individuals by various agencies, including MBIE. Any personal information you supply to MBIE in the course of making a submission will only be used for the purpose of assisting in the development of policy advice in relation to this review.

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Chapter 3 – Barriers to achieving the outcomes

- Do you agree with the barriers outlined in the Options Paper? If not, why not?
  Enter text here.

- Is there evidence of other major barriers not captured in the Options Paper? If so, please explain.
  Enter text here.

Chapter 4 – Discrete elements

- Which options will be most effective in achieving the desired outcomes and why?
  Enter text here.

- What would the costs and benefits be of the various options for different participants (consumers, financial advisers, businesses)?
  Enter text here.

- Are there any other viable options? If so, please provide details.
  Enter text here.

4.1 Restrictions on who can provide certain advice

- What implications would removing the distinction between class and personalised advice have on access to advice?
  Enter text here.

- Should high-risk services be restricted to certain advisers? Why or why not?
  Enter text here.

- Would requiring a client to 'opt-in' to being a wholesale investor have negative implications on advisers? If so, how could this be mitigated?
  Enter text here.

4.2 Advice through technological channels

- What ethical and other entry requirements should apply to advice platforms?
  Enter text here.

- How, if at all, should requirements differ between traditional and online financial advice?
  Enter text here.

- Are the options suggested in this chapter sufficient to enable innovation in the adviser industry? What other changes might need to be made?
  Enter text here.

4.3 Ethical and client-care obligations

- If the ethical obligation to put the consumers' interests first was extended, what would the right obligation be? How could this be monitored and enforced?
  Enter text here.

- What would be some practical ways of distinguishing 'sales' and 'advice'? What obligations should salespeople have?
  Enter text here.

- If there was a ban or restriction on conflicted remuneration who and what should it cover?
  Enter text here.

4.4 Competency obligations

- How can competency requirements be designed to lift capability, without becoming an undue barrier to entry and continuation in the profession?
  Enter text here.

- Should all advisers be subject to minimum entry requirements (Option 1)? What should those requirements include? If not, how should requirements differ for different types of advisers?
  Enter text here.

4.5 Tools for ensuring compliance with the ethical and competency requirements

- What are the benefits and costs of shifting to an entity licensing model whereby the business is accountable for meeting obligations (Option 1)? If some individual advisers are also licensed (Option 2), what specific obligations should these advisers be accountable for?

Enter text here.

- What suggestions do you have for the roles of different industry and regulatory bodies?
  Enter text here.

4.6 Disclosure

- What do you think is the most effective way to disclose information to consumers (e.g. written, verbal, online) to help them make more effective decisions?
  Enter text here.

- Would a common disclosure document for all advisers work in practice?
  Enter text here.

- How could remuneration details be disclosed in a way that would be meaningful to consumers yet relatively simple for advisers to produce?
  Enter text here.

4.7 Dispute resolution

- Is there any evidence that the existence of multiple schemes is leading to poor outcomes for consumers?
  Enter text here.

- Assuming that the multiple scheme model is retained, should there be greater consistency between dispute resolution scheme rules and processes? If so, what particular elements should be consistent?
  Enter text here.

- Should professional indemnity insurance apply to all financial service providers?
  Enter text here.

4.8 Finding an adviser

- What is the best way to get information to consumers? Who is best placed to provide this information (e.g. Government, industry, consumer groups)?
  Enter text here.

- What terminology do you think would be more meaningful to consumers?
  Enter text here.

4.9 Other elements where no changes are proposed

The definitions of 'financial adviser' and 'financial adviser service'

- Do you have any comments on the proposal to retain the current definitions of

'financial adviser' and 'financial adviser service'?
Enter text here.

Exemptions from the application of the FA Act

- Are those currently exempt from the regime posing undue risk to consumers through the provision of financial advice in the normal course of their business? If possible, please provide evidence.
  Enter text here.

Territorial scope

- How can the FA Act better facilitate the provision of international financial advice to New Zealanders, without compromising consumer protection? Are there other changes that may be needed to aid this, beyond the technological options outlined in Chapter 4.2?
  Click here to enter text.

- How can we better facilitate the export of New Zealand financial advice?
  Enter text here.

The regulation of brokers and custodians

- Do you have any comments on the proposal to retain the current approach to regulating broking and custodial services?
  Enter text here.

Chapter 5 – Potential packages of options

- What are the costs and benefits of the packages of options described in this chapter?
  Enter text here.

- How effective is each package in addressing the barriers described in Chapter 3?
  Enter text here.

- What changes could be made to any of the packages to improve how its elements work together?
  Enter text here.

- Can you suggest any alternative packages of options that might work more effectively?
  Enter text here.

Chapter 6 – Misuse of the Financial Service Providers Register

- Do you agree with our assessment of the pros and cons of the options to overcome misuse of the FSPR?
  Cygnus Law agrees in broad terms with your assessment with some qualifications, as outlined below.

Option 2: Amend the grounds for de-registration

Cygnus Law considers that:

- Providing more grounds for removal potentially increases the risk of unintended consequences rather than reducing them. This reflects the already wide discretion given to the FMA, including that the FMA has a general discretion to determine whether deregistration is "necessary or desirable". So there is no guarantee that this reduces the risk of unintended consequences- it depends very much on the approach taken by the FMA.
- Although not stated it appears that the decision in Vivier and Company Ltd v Financial Markets Authority [2015] NZHC 2337 (judgment released 25 September 2015) may have impacted on the proposal that a ground for deregistration is "where an entity does not provide a substantive amount of services from a place of business in New Zealand option". This approach was not accepted by Brewer J in Vivier as being supported by the current section 18A criteria. Brewer J found that there had to be some evidence of misconduct to support a finding that one of the section 18A criteria is met. However, in the subsequent judgement of Excelsior Markets Ltd v Financial Market Authority (HC, 18 December 2015) Nathan J differed from Brewer J and found that it can be false or misleading if a person registered on the FSPR provides financial services substantially, or wholly, outside of New Zealand, with no requirement for any related conduct (although Nathan J did find that there was evidence of conduct that supported a finding that section 18A criteria had been met). The FMA states on its website that an appeal to Vivier is to be heard on 10 February 2016. It's possible that the Court of Appeal will resolve the conflicting High Court decisions on that point. It would be appropriate that no law change is made before the judgment is released. Regardless of the outcome, Cygnus Law considers the status of an entity (e.g. the extent to which it provides services from New Zealand) is a matter that is best addressed at the time of registration by reference to clear criteria, with a change of status (or untrue statements about status at the time of registration or misleading/deceptive conduct) being appropriate subjects for a deregistration power. This is not to suggest that the outcome of the Excelsior case was wrong in the circumstances including because there was evidence of misconduct that supported deregistration. Please note that Cygnus Law's comments on the Vivier and Excelsior cases are very broad summaries of some findings for the purpose of illustrating key points and shouldn't be taken as a detailed statement of the law arising.
- The key consideration that both judges took into account was that a FSP with a place of business in New Zealand is required to register. Brewer J considered that (in summary) if registration requirements were met it couldn't follow that a FSP could then be deregistered without any additional evidence of misconduct. Nathan J disagreed. The result in Cygnus Law's view is that the effect of the Excelsior is to, in effect, amend the territorial scope provision. This can be given effect either through FMA's powers under sections 15A and 15B to prevent registration and under the equivalent deregistration powers in sections 18A and 18B. So in Cygnus Law's view a prudent registered entity should consider that not only does registration require that a person has a "place of business" (as currently required in section 8A(a)) but that some proportion of the financial services have to be provided from New Zealand. However, the case did not help to clarify what may constitute provision of sufficient services from New Zealand to avoid deregistration, so it arguably increases rather than reduces uncertainty (and FSPs are still in a "Catch-22" situation where they are required to apply to register if they have a place of business in New Zealand but risk deregistration if a certain proportion of the services are not provided from NZ). Cygnus Law considers that there's a risk that legitimate businesses may be less likely to conduct business from New Zealand because of the uncertainty as to what criteria are applied by the FMA in determining when to exercise its powers to prevent registration or to direct deregistration. The policy considerations inherent in the decision to deregister, including the extent to which business needs to be conducted from New Zealand (an issue that crosses into areas such economic development, trade policy and the effect of the internet & use of outsourcing in the financial services industry) are in Cygnus Law's view better considered as part of the process for developing law and regulation, rather being left to be determined in the context of discretionary powers of a regulator.
- Cygnus Law supports making the extent to which services need to be provided from New Zealand an express a criterion for registration together with clarification of what that means (discussed further at question 37).

Option 3: Amend the territorial scope of the legislation to require a legitimate connection to New Zealand
A negative outcome is stated as "It could create other potential loopholes, uncertainty or unintended consequences." However, that is a potential outcome for every option presented, if the policy analysis is not adequate and/or if the wrong mix of options is chosen. In particular it is a potential outcome for option 2, as decisions would be at the FMA's discretion.

Option 4: Require trust and company service providers to register
It's not fully clear from the description how this option would operate and how the benefits would arise. As Cygnus Law understands from media statements many of the off-shore companies that the FMA is concerned about are not subject to AML/CFT obligations, so it's difficult to see how this option will be of substantial help.

- What option or combination of options do you prefer and why? What are the costs and benefits?

  With regards to the issues that have led to proposals for law change, the Options Paper states that:
  - "misuse remains an ongoing challenge and the de-registration powers have not proven to be fully effective"
  - "some offshore-controlled firms have sought to register on the FSPR in order to take advantage of New Zealand's reputation as a well-regulated jurisdiction. These firms then misrepresent that they are licensed or actively regulated in New Zealand."
  - "Given the risk of damage to New Zealand's reputation as a well-regulated jurisdiction and the reputation of legitimate New Zealand-based financial service providers…"

  However, the Options Paper does not refer to the following additional matters noted in the Report on the operation of Part 2: Registration ("FSP Report") (the report is undated but Cygnus Law understands it was published in August 2015):
  - Whilst this risk was seen as a matter of priority by those who submitted on the related question in the Issues Paper, the number of fraudulent cases is small.
  - Increased risk profiling and integrity checking by the FMA and Companies Office and new powers to prevent registration and to de-register has reduced the numbers of FSP applications from offshore entities in recent months.
  - As at 22 July 2015 the FMA has directed the Registrar to remove 40 entities, three others voluntarily deregistered after receiving a Notice of Intention to deregister, and two were deregistered due to their dispute resolution scheme membership being cancelled post the FMA issuing a Notice of Intention to issue a direction to the Registrar.
  - The FMA has taken action to prevent 34 entities registering as FSPs - 20 by direction to the Registrar, along with five withdrawn and nine expired without renewal during the period of FMA's consideration of their applications.

  Public information since that date states that the number of deregistrations now exceeds 100 and the number of registrations prevented is over 40. No information has been provided to support the statement that the deregistration powers have not proven fully effective. Rather, the information indicates a very significant degree of success. Appeals are to be expected when there is new law that has a significant impact. Typically there are far fewer appeals once the law has been tested and key precedents are established. Cygnus Law accepts that there may be issues with the deregistration powers but, in the absence of a qualitative assessment of those issues in the Options Paper, it's difficult to assess the extent to which the proposed amendments address the issues issue and are appropriate.

  Cygnus Law considers that there are further factors that support a conclusion that there has been a significant degree of success in addressing what is a genuine issue:
  - The issues that the FMA has faced likely represented a "high water mark", following several

years where such perimeter issues were not given a lot of priority (possibly because the powers to act were limited).
- The relevant registrations mostly occurred at a time when there was no requirement for a New Zealand company to have a director living in New Zealand. That changed last year and is likely in itself to have an impact.
- The FMA's actions are very likely making registration in New Zealand a less attractive option so the number of registrations may reduce over time for that reason alone. This conclusion is supported by the reference in the FSP Report to voluntary deregistrations and to the fact there have been fewer applications. That also reflects the FMA's experience with "low ball" unsolicited offers - these were a significant cause of concern and there was much negative media commentary. However, following new regulations designed to address the issue and significant FMA oversight, few if any issues are now reported in that area.
Also, banks have stated publicly that they will not open accounts for money remitters and derivatives issuers because of AML/CFT concerns, two key categories of off-shore providers (although this approach is currently being challenged in proceedings brought by E-Trans International against Kiwibank).

Cygnus Law cannot identify strong grounds for strengthening the FMA's deregistration powers on the information available, particularly where they relate to status rather than conduct. Rather, as noted at question 36, Cygnus Law considers that reform should be focused on clarifying and extending the requirements for registration, with less room for discretionary decision making (deregistration powers would then be secondary to the registration requirements). This is consistent with the recommendations made in the FSP Report, which recommended the following actions to "Ensure offshore providers cannot misuse the Register" (and made no reference to extending deregistration powers):
- Amending the territorial scope and registration requirements of the FSP Act to clearly exclude providers that do not offer a financial service either to or from New Zealand, do not provide a financial service to New Zealanders, or that do not provide a substantive amount of their services from a place of business in New Zealand may help reduce fraudulent financial activity.
- Changes to the territorial scope of the Act and the inclusion of registration criteria could provide both the Registrar and applicants with clear criteria regarding which providers are not able to register in New Zealand. This would provide for an efficient registration process and would minimise the impact of misuse on the Registrar, and FMA and DIA resources.
Any concerns about unintended consequences could be addressed by giving the Registrar and/or the FMA an “exemption” power to allow registration in meritorious cases where the criteria are not met.

Cygnus Law does not support all of the specific recommendations in the FSP Report but considers that the general approach of focusing on registration criteria is the best option. Accordingly, Cygnus Law considers that Option 3 is the most appropriate measure to address the underlying concerns on a long term basis. Cygnus Law does not support a criterion for registration that services are provided to clients in New Zealand, at least without significant further consideration of the likely impact. Also, it seems contrary to the general policy of supporting export industries in New Zealand. Cygnus Law considers that there are significant benefits in that approach, if properly implemented, including that it creates greater certainty for market participants (as noted in the FSP Report). Potential approaches to increase certainty include:
- The approach taken in the Companies Act 1993 with regard to establishing whether an overseas company is "carrying on business" (section 332) in order to determine whether it must be registered. A definition is not provided but two examples of activities that will comprise carrying on business are, together with a long list of activities and events that will not.
- However, while Cygnus Law thinks this approach may be of limited assistance it, it does not consider it will to provide sufficient certainty and suggests assistance in developing positive criteria could be obtained from the FMA's licensing guides, which list the operational infrastructure that various licensed financial services business are expected to have.
- Requiring registration with the IRD. This was one initiative that has been implemented to

address concerns about off-shore purchases of houses in New Zealand. It may deter entities that do not genuinely want to operate from New Zealand.

Cygnus Law acknowledges that any detailed registration criteria regarding the extent to which financial services must be provided from New Zealand will lead to attempts to implement minimum required presence. However, this is always going to occur regardless of the standards set and it does not automatically follow that leaving the criteria to be established on a case-by-case basis is a better outcome. It also provides for certainty, which should reduce costs for financial services businesses who may need to register. The key to implementing option 3 will be ensuring that the criteria give sufficient confidence that the business is genuinely being conducted from New Zealand, at least in part. This will give the FMA greater ability to monitor conduct and to take action.

Cygnus Law is not convinced that the warning suggested by Option 2, or a similar warning, is the appropriate response. Key considerations in relation to option 2 are:
- Cygnus Law queries whether it is appropriate to say that any entity is not subject to active supervision. This suggests that regulators can choose to not comply with their mandate to regulate conduct. It potentially compounds the potential issues by creating a perception that the regulator will "turn a blind eye" to misconduct or simply isn't monitoring at all.
- All exporters need to comply with the law of the countries they export to. Cygnus Law is not aware of any exporters in other sectors who have to warn the consumers about how they are regulated. Cygnus Law suggests that the requirements for registration, and regulator oversight, be sufficiently strong that warning statements should not be required. Otherwise, it raises questions about the integrity of New Zealand's registration process as well as the registered entities. And it potentially prejudices legitimate financial services businesses if they have to provide a warning.

Also:
- While Cygnus Law accepts that it is not possible or appropriate to closely monitor activities off-shore, this being better addressed by the authorities in the relevant jurisdictions, there is room for greater regulator engagement. This is not different in principle from the role of MPI, which is actively involved in supporting exporter compliance in other jurisdictions. While accepting the context is very different, Cygnus Law thinks that it should not be assumed that the regulator cannot or should not play a role in this area.
- Cygnus Law does not support assertions that the off-shore activities of unlicensed New Zealand financial service providers are "unregulated" and that registration on the FSPR is an "administrative" process. As the FSP Report notes, the intention of the FSPR was that "the Registrar be responsible for carrying out negative assurance checks on the controlling shareholders, directors and senior managers of financial service providers, and individual financial service providers. Those providers which do not meet the checks would not be registered and therefore unable to provide financial services." Accordingly, in Cygnus Law's view, registration is more than an "administrative process" and does and is intended to provide a limited level of comfort to recipients of financial products and services regarding the providers. Either those checks should be removed or there should be acceptance that New Zealand law does give a level of legitimacy to registered FSPs, and a perception they are regulated, regardless of what the FSPR is called or whether or not it is public. This supports a clearer and more robust registration process to filter out FSPs that may act inappropriately.
- The effect of the definition of "restricted communication" in section 464 of the Financial Markets Conduct Act 2013 (FMC Act) means that the FMA has power to regulate the conduct off-shore by New Zealand companies, including where they provide few if any relevant services from New Zealand. A "restricted communication" includes "a form of communication that directly or indirectly refers to an offer, or intended offer, of financial products or the supply, or possible supply, of a financial service … that is authorised or instigated by, or on behalf of, the offeror, the issuer, the service provider … that is to be, or has been, distributed to a person". And a restricted communication includes an advertisement (section 464(3)). Section 33 of the FMC Act addresses the territorial scope of sections 19 to 23 of the FMC Act (relating to fair dealing). Section 33(2) states that "Sections 19 to 23 also apply to a restricted communication

that is distributed or to be distributed to a person outside New Zealand by any person resident, incorporated, registered, or having a principal place of business in New Zealand.". The background to this provision was referred to in the report of the Commerce Committee on the Financial Markets Conduct Bill, which stated that "We consider that the territorial scope of the bill needs to be extended to allow the regulation of the conduct of New Zealand residents and businesses in respect of their offshore activities in limited circumstances." To take an example, a website regarding financial services directed to overseas persons, and operated by a New Zealand company that provides few if any financial services in New Zealand, is likely to be subject to New Zealand law (and hence regulator oversight), by virtue of the company being incorporated in New Zealand and/or registered on the FSPR. The FMA has powers it can exercise in the event of breach, including issuing stop orders. Regardless of the proposals that come out of this consultation, Cygnus Law suggests that this area is revisited to avoid potential inconsistencies between it and the updated registration regime.

With regard to Option 1 Cygnus Law considers that:
- This would provide only limited ability for the FMA to prevent "fraud". The FMA/Registrar would be relying on the statements of the applicant regarding where it planned to provide services. If fraud was intended then it can be expected that the information provided would not be correct but the FMA or the Registrar may not be able to identify that.
- If FSPs are providing services to wholesale clients (or their equivalent) off-shore, then they may not be required to be licensed (as would be the case for some financial services and products supplied within New Zealand) - it would likely be difficult for the FMA to confirm the validity of such claims.
- Bonding does not address what Cygnus Law understands is the primary issue, which is the activities of "offshore controlled providers" who are purporting to operate from New Zealand but do not have New Zealand clients.

With regard to Option 4 it's not clear that it will be of significant benefit in resolving the issues being considered. For example:
- If the issue is that registration does not equate with regulation, how does the registration requirement for trust and company services providers allow the FMA regulate such providers?
- If trust and company service providers are acting as directors then they are subject to the Companies Act (which the FMA already has jurisdiction over for FSPs).
- Nominee shareholders are very common in many situations. The law supports this by permitting the creation of trusts, including bare trusts to hold assets, including shares (though these are not permitted to be recorded on the share register of a New Zealand company). This is addressed in AML/CFT Act, the Companies Act and other legislation by requiring disclosure of ultimate beneficial owners. It should be evident if a known agent incorrectly claimed that the agent is the ultimate beneficial owner.

- What are the potential risks and unintended consequences of the options above? How could these be mitigated?
  Please see the response to question 37.

- Would limiting public access to parts of the FSPR help reduce misuse?
  Please see the response to question 37. Cygnus Law does not consider it would prevent misuse and that this approach would only address a symptom rather than addressing the cause of the issue.

Demographics

1. Name:
   Enter your name and/or the name of the group of people, business, or organisation you are providing this submission on behalf of here.

2. Contact details:
   Enter your email address, or other contact details here.

3. Are you providing this submission:
   ☐As an individual
   ☐On behalf of an organisation

   (Describe the nature and size of the organisation here)

4. Please select if your submission contains confidential information:

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Reason: Enter text here.