

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.

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Chapter 3 – Barriers to achieving the outcomes

1. Do you agree with the barriers outlined in the Options Paper? If not, why not?

We agree in principle with the barriers that have been identified. The issue for ideal outcomes to be provided for consumers, is that regulations take account not of the theoretically correct outcomes but those that have practical benefits for consumers. An example of this in the past is the onerous disclosure requirements which resulted in pointlessly lengthy documents that most consumers ignored anyway.

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

There is a structural imbalance in the industry whereby powerful distribution channels, such as the banks, are increasing their market share through what could be perceived as coercive strategies to increase their customers' share of wallet spending via cross selling. In most instances the bank staff are only able to provide one option to the client (the Bank's own product). A continuation of this situation will not lead to optimal outcomes for consumers, rather it will be a return to the pre-regulation era (1991) when the market was dominated by distribution companies selling a single supplier product line to consumers.

We would recommend that NMBIE add a further barrier which is:

Reduction in industry competition and also loss of consumer choice. This could be addressed by ensuring all advisers are required to put the client's needs first which would by implication mean offering more than one suppliers products.

Chapter 4 – Discrete elements

1. Which options will be most effective in achieving the desired outcomes and why?
In order of effectiveness:
 1. Amend restrictions on who can provide what advice. This is of paramount

importance because it removes the artificial and at times ridiculous demarcation between what are supposedly complex products (that only AFAs can sell) and simple products (which RFAs can sell). There is also the existing anomaly whereby QFEs set their own competency standards which further undermines a consumer's ability to assess the relative competency of a potential adviser.

2. Amend ethical and client-care obligations. The options paper consistently refers to situations where an advisers might not be required to put the consumer's interests first. If we want consumers to have confidence in the industry they have a right to expect that no matter what channel or process they utilise, that their needs are the advisers first responsibility (i.e. classifying a transaction as a sale rather than advice should not provide a method for an adviser or business to contract out of the requirement to put the consumers interest first).

3. Increase industry competition and consumer choice. This option is not in the paper but it is an essential component if NMBIE is serious about advisers putting consumer's interests first, then this can best be achieved through a highly competitive market where advisers are required to give consumers choice (e.g. not just 'sell' the products for the bank they work for. There is no structural reason why the manufacture and distribution of financial products needs to be integrated (as in the bank model) other than to restrict consumer choice and maximise bank profitability).

4. Amend regime for ensuring compliance. We are not entirely clear whether each adviser business (of which many, if not most, are single person entities) are going to be asked to be licensed or whether it would be organisations with existing compliance infrastructure (e.g. dealer groups such as Kepa) would undertake this task. Little would be gained if each business entity was required to be licensed because to a large degree this is what already happens. For licensing to be effective it needs to be managed by professional groups that have the expertise and financial strength to provide effective infrastructure.

5. Increase competency requirements. We are not convinced that a wholesale adoption of a level 5 qualification would actually do much to improve consumer confidence given that significant allowances would need to be made for grandfathering existing, experienced advisers and that compulsory level 5 qualifications would act as a barrier to entry for new advisers. However it does seem an oversight that there is currently no compulsory requirement for CPD. We would be in support of compulsory CPD for all financial advisers so that they can demonstrate that they have up-to-date knowledge to consumers.

6. Improve disclosure requirements. The existing system with its differing disclosure requirements has a negative impact on consumers. All advisers should have the same disclosure requirements and a fair way needs to be determined for the bank staff who have sales quotas to have this included in their disclosure information.

7. Allow advice through technological channels. Robo advice should be subjected to the same requirements as 'human' advice.

8. Increase transparency, consistency, and consumer access to disputes resolution. In our previous submission, we highlighted our concerns regarding a lack of competition amongst the disputes resolution schemes. Since then the FSCL annual report has come

out showing that they now have in excess of \$2m in reserves and the ISO \$1.2m. The annual fees for both organisations are broadly similar which does not suggest a high level of competition. These organisations should be required to use some of their reserves to promote their services to the public (\$3.2m would buy a lot of promotion to consumers).

9. Changes to help consumers find advisers. We are unsure that this is an option that many consumers would actually use. Professional associations already have directory services and they receive fairly limited consumer traffic.

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

1. Amend restrictions on who can provide what advice.

The costs of this option are borne by financial advisers (assuming they are self-employed) and businesses. The costs will depend on how they changes are implemented. If all advisers are expected to become the equivalent of AFAs (along with the associated existing requirements) then there will be a significant impost on advisers and businesses through additional education and compliance. Alternatively if advisers are required to comply with the existing Code and undertake CPD (without the requirement to complete the level 5) then the costs would be restricted.

The benefit for consumers with this option is that the theoretical scope for confusion between AFA and RFA and QFE status would be removed. In reality this confusion will only disappear if significant promotion to consumers is undertaken. Had the Securities Commission used the money they allocated to running the "Adviser Cowboy" campaign to educating the consumers on what an AFA and an RFA was there might have been some greater consumer clarity.

2. Amend ethical and client-care obligations.

Consumers are the great winners in this option. Any costs for advisers and businesses in meeting this cost should be regarded as an investment in building a sustainable, consumer centric business model. That is a basic tenet of a successful business and cannot really be viewed as an additional cost.

3. Amend regime for ensuring compliance.

If all advisers are to be subjected to the same requirements (as appears is favoured by NMIE) then a more effective method of ensuring compliance does need to be considered. It is difficult to imagine the FMA staffing up to sufficient levels to ensure compliance if many thousands of existing RFAs are further captured by regulation.

At least in theory, consumers will derive some benefit from a wider scale of compliance and this will be at no additional cost to them except if such changes result in a high number of existing RFAs leaving the industry (which will only exacerbate the existing concerns about gaps in advice). Using dealer groups to ensure compliance (and backing this up with support from professional associations will entail additional costs for advisers and businesses. The magnitude of that cost is largely determinate on the degree of additional compliance that will be required of the existing RFAs.

4. Increase competency requirements.

As previously mentioned we do not think that simply making all advisers complete a qualification such as the level 5 certificate would result in much benefit for consumers. We do however, think that compulsory CPD has benefits for consumers. The cost of compulsory CPD would be shouldered by advisers and the businesses they belong to. However the cost need not be prohibitive. Some professional associations such as the

NZFAA provide 25hours of structured CPD for their members as part of their annual subscription (less than \$600).

5. Improve disclosure requirements.

We remain somewhat sceptical whether consumers actually value disclosure to the same degree as regulators do. If NMIE could provide evidence of a market where disclosure is informative, meaningful and valued by consumers then that would be helpful to us. That said having different forms of disclosure can only undermine what is already a tenuous consumer benefit. A single disclosure requirement that is brief and contains the basic information that a consumer might want to know, can be produced at little cost to the adviser or business.

6. Allow advice through technological channels.

Robo advice is a reality (particularly in the investment field) overseas. It is an important component in the creation of a competitive marketplace and provides benefits to consumers and product suppliers alike. The likely cost in NZ is that of cannibalising some of the lower end investment financial advice although in reality much of that is probably being lost in the existing advice gap.

7. Increase transparency, consistency, and consumer access to disputes resolution.

The disputes resolution schemes have undertaken very little promotion of their services to consumers and this has been to the detriment of consumers. Consumers need to know what the schemes are and how they function. This promotion will come at a cost to the Dispute Resolution schemes but their financial statements demonstrate that they are well placed to fund such promotion themselves.

8. Changes to help consumers find advisers. As previously mentioned, we are unsure that this is an option that many consumers would actually use. It would be easy to spend a great deal of money on this functionality when it is unlikely to actually be adopted by consumers in a meaningful way.

1. Are there any other viable options? If so, please provide details.

Increase industry competition and consumer choice.

Industry competition drives down costs and increases benefits. Term life insurance premiums have almost halved since the de-regulation and demutualisation of life insurance in the early 1990s. The winner in this equation has undoubtedly been the consumer. The banks are a powerful lobbying force and they have been successful in the past in creating competitive advantage through regulation with doubtful consumer benefits e.g. the rather opaque QFE structure. The ongoing product extensions of the major banks mean that consumers are receiving limited choice while the banks are reducing the threat of exposure to competition by their clients. The only additional costs associated with this option are the loss of profits that banks could experience when they are required to provide multiple supplier solutions (as exists in Australia). Their existing competitive advantage is at the expense of consumers. If consumers interests are to be put first then the banks will need to provide consumers with proper choice.

4.1 Restrictions on who can provide certain advice

2. What implications would removing the distinction between class and personalised

advice have on access to advice?

1. The impact on existing RFA numbers would be dependent on the requirements for the existing RFA and QFE advisers. For example a wholesale requirement for all to meet existing AFA requirements (including education) would lead to an increase in the advice gap as a number of existing RFAs would bring forward their retirement decisions.
2. Allowing advisers to provide a more holistic service would have positive benefits on consumers and redressing the advice gap.

Our preference would be for options 1 on the basis that the consumer is selecting the form of service they require e.g. information only, advice based or some specific aspects of a consumer's situation and goals.

3. Should high-risk services be restricted to certain advisers? Why or why not?
We are unsure what evidence there is that there is an existence of high risk services. Unless there is a burning need, then creating another level of service will only continue the existing issues with consumers confusing RFA, AFA and QFE services.
4. Would requiring a client to 'opt-in' to being a wholesale investor have negative implications on advisers? If so, how could this be mitigated?
Not really but it does have a positive impact in that the wholesale investor is actively aware of his or her status. Is it a level of complexity that has material benefits to investors?

4.2 Advice through technological channels

5. What ethical and other entry requirements should apply to advice platforms?
We support the platforms having the same requirements that apply to advisers. If advisers are to be licensed then the same would be applied to platforms.
6. How, if at all, should requirements differ between traditional and online financial advice?
None
7. Are the options suggested in this chapter sufficient to enable innovation in the adviser industry? What other changes might need to be made?
Yes.

4.3 Ethical and client-care obligations

8. 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?
We favour option 1 (extend ethical requirements to all financial services). If the aim of regulation is to create more informed and confident consumers, they need to know that their interests are being put first.
9. What would be some practical ways of distinguishing 'sales' and 'advice'? What obligations should salespeople have?
We do not support the separation of sales and advice. All advisers (and robo-advice) should be bound by the same requirements to place the consumers interests first

10. If there was a ban or restriction on conflicted remuneration who and what should it cover?

We don't support a ban or restriction on 'conflicted remuneration'. The cost of remuneration is built into most products. A complete removal would only result in a price reduction of approximately 15% and advisers would need to be remunerated through other means such as fees (paid for by consumers).

New Zealand is not a particularly sophisticated market and therefore any move from commission to fees is only going to exacerbate the advice gap.

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?

This could be undertaken using a staggered approach such as: all advisers must complete 25 hrs structured CPD per annum, grandfathering provisions for existing advisers, supervision of new entrants via dealer groups and professional association mentor schemes (which would have to be developed).

1. 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?

As above

4.5 Tools for ensuring compliance with the ethical and competency requirements

2. 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?

If option 1 does not include the option for dealer groups to take over the licensing for advisers then we think this option is of extremely limited utility. The FMA would simply have transferred the compliance monitoring to businesses) most of which are one band bands with limited resources to undertake their own compliance. If that was the case we would prefer to remain with the existing FMA monitoring

1. What suggestions do you have for the roles of different industry and regulatory bodies? Regulatory bodies should set the standard, professional associations should provide CPD opportunities and Dealer groups (and businesses with more than 10 advisers) should monitor ongoing compliance.

4.6 Disclosure

1. 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?

Written but supported by verbal offer to explain further any items that a consumer may require further clarification on.

2. Should all advisers have the same format for disclosure statements?

Yes (option 1).

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

Life insurance as a % of annual premium.

Investments as a % of FUM.

Mortgages a % of the mortgage being sought.

4.7 Dispute resolution

2. Is there any evidence that the existence of multiple schemes is leading to poor outcomes for consumers?

As we have previously mentioned our main issue with the current schemes is that they have accrued very large reserves in a short space of time and have not significantly reduced their membership fees or invested in promotion of their services to consumers. To have \$3.2m sitting as reserves between the ISO and FSCL is not a sign of an efficient market. What exactly are they reserving for?

3. 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?

We agree with all of the components outlined in option 1 (page 35)

4. Should professional indemnity insurance apply to all financial service providers?

Most suppliers already require advisers who have an agency with them to have P.I. insurance. If one of the aims of regulation is to increase consumer confidence, then mandatory P.I. cover would seem a logical decision.

4.8 Finding an adviser

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

The utility of this option varies with the type of advice being tendered. Some product groups (e.g. mortgages) are largely driven by an initial enquiry by a consumer (and thus would benefit from a 'finding an adviser' facility) while others such as risk insurance are predominately initiated by the adviser. Assuming professional association membership was to be mandatory, the associations are best placed to create such a register (through inter-organisation co-operation). If that does not occur then our preference would be option 1.

6. What terminology do you think would be more meaningful to consumers?

Not sure of the exact term to reference but if a single standard was adopted then the referenced should refer to that e.g. Authorised/unauthorised. Similarly with the type of

sale it could be advice/no advice. Using a single reference standard should reduce the scope for consumer confusion.

4.9 Other elements where no changes are proposed

The definitions of ‘financial adviser’ and ‘financial adviser service’

7. Do you have any comments on the proposal to retain the current definitions of ‘financial adviser’ and ‘financial adviser service’?
Need to ensure that non-human advice e.g. Robo Advice is encompassed in the definition (at the moment the definition refers to a ‘person’).

Exemptions from the application of the FA Act

8. 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.
The exemption for some professions is a weakness in the Act. For example, accountants are able to provide advice on A.C.C. cover but in our experience many have a very limited understanding of the cover options available to their clients (but don’t like to admit their lack of knowledge). Incorrect occupational codes assigned to clients are also quite common. This type of error is rudimentary and should be picked up by the accountant at renewal time but often A.C.C. renewals are given little more than a cursory glance by accountants.
ACC is a form of income protection and incorrect or non-existent advice can be extremely damaging for a client. Having this work undertaken via exempted advisers is unsatisfactory and this loophole should be closed.

Territorial scope

9. 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?
We have no opinion on this.
10. How can we better facilitate the export of New Zealand financial advice?
See above.

The regulation of brokers and custodians

11. Do you have any comments on the proposal to retain the current approach to regulating broking and custodial services?
No

Chapter 5 – Potential packages of options

12. What are the costs and benefits of the packages of options described in this chapter?

1. How effective is each package in addressing the barriers described in Chapter 3?

Option 1. – Overall effectiveness – low/medium

It is hard for consumers to know who to seek advice from - low (changing the designations will not have any impact unless followed up with considerable promotion to consumers)

Certain types of advice aren't being provided – low (this option doesn't have any levers to change the existing advice gap)

Consumers may be receiving advice from people without adequate knowledge, skills and competence – low (no change to existing environment)

Certain conflicts of interest maybe leading to suboptimal outcomes for consumers- high (disclosure will address this)

Consumers don't always understand the limitations of different types of advice- medium/high (disclosure should address this)

Option 2. – Overall effectiveness at overcoming barriers – medium/high

It is hard for consumers to know who to seek advice from – medium

Certain types of advice aren't being provided – medium (removal of AFA/RFA and QFE distinctions would improve this to some extent)

Consumers may be receiving advice from people without adequate knowledge, skills and competence – high (new competence requirements address this)

Certain conflicts of interest maybe leading to suboptimal outcomes for consumers- high (disclosure will address this)

Consumers don't always understand the limitations of different types of advice- high (limitations will be driven by the consumers request and also outlined in the disclosure process)

Option 3. – Overall effectiveness at overcoming barriers– low/medium

It is hard for consumers to know who to seek advice from – low (the use of areas of competence will continue the problems of confusion that currently exist with RFA vs AFA vs QFE)

Certain types of advice aren't being provided – low (requirement for areas of competence will not free this up)

Consumers may be receiving advice from people without adequate knowledge, skills and competence – high (competence requirements will improve this)

Certain conflicts of interest maybe leading to suboptimal outcomes for consumers- medium (the concept of delineating between sales people and advisers limits the scope of disclosure to influence this factor)

Consumers don't always understand the limitations of different types of advice – low (replacing RFAs with Salespeople will do little to address this issue)

2. What changes could be made to any of the packages to improve how its elements work together?

Option 1.

So many areas of this option fail to address the identified barriers that it would be

pointless attempting to modify each of the elements to make the option work better. We would prefer starting with either option 2 or 3 as the basis for potential modification.

Option 2.

Licensing should be available to dealer groups and businesses with more than 10 advisers (i.e. not to stand alone advisers or small businesses who will usually lack monitoring infrastructure)

We don't think the term 'expert adviser' is very useful. Most professions (e.g. medicine, engineering, accounting, legal) would refer to such people as specialists. We are also not convinced that there is a need to be a high level 'quality mark'.

Execution only service should be renamed 'no advice'.

Option 3.

Execution only service should be referred to as no advice.

If sales vs advice distinction is to be made (and we don't see the benefits of this) then refer to the components as advice and no advice rather than advice and sales.

Include requirement for all advisers to put the client's needs first (i.e. do not give salespeople/no advice people a watered down version of this)

Licensing entities to include dealer groups

3. Can you suggest any alternative packages of options that might work more effectively? These three options provide a reasonable spread of options to be considered.

Chapter 6 – Misuse of the Financial Service Providers Register

4. Do you agree with our assessment of the pros and cons of the options to overcome misuse of the FSPR?
No comment to make on this.
5. What option or combination of options do you prefer and why? What are the costs and benefits?
No comment to make on this.
6. What are the potential risks and unintended consequences of the options above? How could these be mitigated?
No comment to make on this.
7. Would limiting public access to parts of the FSPR help reduce misuse?
No comment to make on this.

Demographics

1. Name:
Jeff Page, CEO, Kepa
2. Contact details:

Redacted

3. Are you providing this submission:

As an individual

On behalf of an organisation

(Describe the nature and size of the organisation here)

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