

In Confidence

OFFICE OF THE MINISTER OF COMMERCE AND CONSUMER AFFAIRS

The Chair
Cabinet Economic Growth and Infrastructure Committee

Release of an Issues Paper for the Review of the Financial Advisers Act 2008 and the Financial Service Providers (Registration and Dispute Resolution) Act 2008

Proposal

1. To seek approval to publicly release the attached Issues Paper (see **Annex 1**) for the review of the Financial Advisers Act 2008 (FA Act) and the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act).

Background to the review and developments

2. Access to quality information and advice allows New Zealanders to make informed decisions about participating in financial markets. Investor confidence and participation in these markets provides funding for New Zealand businesses and is a vital tool for individuals in achieving their financial goals.
3. The FA Act and the FSP Act contribute to the regulation of New Zealand's capital markets and are integral in promoting sound investor decision-making:
 - The FA Act regulates professional providers of financial advice in the investment, insurance, mortgage broking and banking industries. It aims to encourage and promote public confidence in the professionalism and integrity of financial advisers and brokers.
 - The FSP Act requires financial service providers to be registered and (where applicable) to belong to a dispute resolution scheme. These requirements are aimed at promoting confident and informed participation of businesses, investors and consumers in fair, efficient and transparent financial markets.
4. The Ministry of Business, Innovation and Employment (MBIE) is required by statute to review and provide recommendations to me on the operation of both Acts over the next 18 months. Given the extensive inter-relationship between the two Acts, they are being reviewed at the same time.
5. In addition to the statutory requirements to review the two Acts, it is a timely opportunity to analyse the role of financial advice, financial service provider registration and dispute resolution in improving financial outcomes for New Zealanders. The review will test and update the objectives of, and rationale for, government intervention in this area.
6. A steering group of senior officials from MBIE, the Treasury, the Financial Markets Authority and the Commission for Financial Capability has been established to oversee the review.

7. In February this year, Cabinet approved the publication of the Terms of Reference for the review [EGI Min (15) 3/9]. The Terms of Reference were published on MBIE's website and provide context on the Acts and developments that have occurred since their implementation. They also outline the scope, objectives and key milestones for the review, including an indication that the Government would release an Issues Paper in May for public consultation.
8. During this initial stage of the review, MBIE has:
 - a. met with industry and consumer groups to discuss how they would like to be involved in the review and their views on the key issues;
 - b. conducted a literature review on financial advice and government regulation in this area;
 - c. held consumer focus groups; and
 - d. surveyed financial advisers.

Issues Paper

9. The attached Issues Paper aims to help identify the key issues and opportunities relating to how the Acts are operating. It outlines MBIE's analysis of the role of financial advice, registration and dispute resolution as well as the role of government and the aims of regulation. It also outlines the key questions that MBIE has identified through its initial engagement with stakeholders. Throughout the Issues Paper, submitters are asked to comment on, correct and challenge this analysis.
10. The Issues Paper does not propose any solutions or legislative changes. Submissions will inform the next stage of the review, which will be an options identification process. Based on this I expect to seek Cabinet approval to release a second formal consultation document, outlining options for regulatory reforms towards the end of the year.

Goals and key questions

11. The Issues Paper identifies three main goals for the regulation of financial advice and raises key questions related to each one:

Goal 1: Consumers have the information they need to find and choose a financial adviser

12. **Do consumers understand the complexities of the regulatory framework?** The Issues Paper identifies that the regulatory framework may be too complex for consumers to understand, undermining their ability to make informed decisions about which type of adviser to use, how to interpret their advice, and may even discourage some from seeking advice altogether. In particular, consumers have noted it is difficult to understand differences between classes of advisers, their different obligations and their ability to advise on different products and give different types of advice. The Issues Paper seeks feedback on any clarifications that could be made to the current regulatory regime to make it easier for consumers to understand.
13. **Should there be a clearer distinction between advice and sales?** The FA Act's definition of financial advice includes many activities that could arguably be more accurately described as "sales". The Issues Paper is interested in stakeholder feedback on whether a clearer distinction between these activities, with appropriate standards for each, would benefit consumers.

14. **How should we regulate commissions and other conflicts of interest?** A number of financial advisers are either partly or wholly paid by commissions paid by product providers. These commissions can create a conflict of interest for the adviser; incentivising them to advise that their client buys a particular product. Though some types of adviser are required to inform their clients of any commissions, there are concerns about the ability of consumers to interpret this information. Internationally, a number of jurisdictions changed regulatory requirements following the global financial crisis to either ban or restrict the use of commissions. The Issues Paper seeks feedback on whether the current disclosure requirements for commissions and conflicts of interest are adequate and how requirements should be applied to the different types of adviser.
15. The ability of consumers to use the Financial Service Providers Register to search for, compare and learn about financial service providers, including financial advisers, (discussed below) is also very relevant to this goal.

Goal 2: Financial advice is accessible for consumers

16. **Does the FA Act unduly restrict access to financial advice?** The Issues Paper is interested in understanding the overall impact that the FA Act has had on consumer access to financial advice. It seeks feedback on the level of competition in the financial adviser market, whether regulatory constraints and boundary issues are adversely impacting on the type of advice available, and the extent to which compliance costs are restricting who can access financial advice. The Issues Paper is particularly interested in information on any specific compliance requirements that are unduly burdensome or are limiting consumers' access to good quality financial advice.
17. **How should the FA Act facilitate access to advice in the future?** The Issues Paper seeks feedback on how the FA Act can deal adequately with a number of potential developments that might affect both the demand for and supply of financial advice. Potential developments include increasing demand for advice as New Zealanders' KiwiSaver balances increase and Financial Markets Conduct reforms come into effect in relation to new investment products such as peer-to-peer lending, and the increasing supply of advice through online platforms. There is a question of whether the FA Act could limit access to advice on these types of new investment products. The Issues Paper seeks feedback on whether any changes to regulation of advice should be considered in response to the Financial Markets Conduct Act changes and the changing investment and advice environment.

Goal 3: To promote public confidence in the professionalism of financial advisers

18. **Should we lift the professional, ethical and education standards for financial advisers?** The Issues Paper seeks feedback on the adequacy of the ethical and education standards that apply to different types of financial advisers, which currently differ significantly. There is debate as to whether these standards should be aligned and/or increased. The Issues Paper seeks feedback on what role the various professional bodies could play in lifting these standards.
19. **Should the individual adviser or the business hold obligations?** An important decision when regulating financial advisers is whether to apply obligations to the individual adviser or to the business they represent. The FA Act takes a mixture of these two approaches. The Issues Paper is interested in stakeholder views as to how this is working and whether changes to this approach should be considered.

FSP Act key questions

20. In relation to the FSP Act, the Issues Paper identifies a number of goals for the operation of the Financial Service Providers Register and of dispute resolution. The Issues Paper asks the following key questions:
21. **Could the Register provide better information to the public?** One of the aims of the Financial Service Providers Register is to provide information to the public about financial service providers. The Issues Paper is interested in stakeholder views on whether the Register could be improved to better enable consumers to search for, compare and learn about financial service providers, including financial advisers.
22. **How can we avoid misuse of the register by overseas financial service providers?** A large number of offshore financial service providers have attempted to register in New Zealand in order to give the misleading impression that they are regulated here. While changes have been made to the legislation to address the problem, it does appear to be an ongoing issue. The Issues Paper seeks stakeholder views on the significance of the problem and whether further changes are needed to address it.
23. **What is the impact of having multiple dispute resolution schemes?** There are currently four approved dispute resolution schemes, three of which accept any type of financial service provider as members. The Issues Paper seeks stakeholder feedback on the impact of having multiple schemes, including on the competitive dynamic between the schemes and potential inconsistencies between the rules and approaches of the different schemes.

Next steps: stakeholder engagement and further research

24. Subject to Cabinet approval today, the Issues Paper will be released for public consultation on 27 May for eight weeks. Submissions will close at the end of July. During this time, MBIE plans to engage extensively with industry, consumer and other interested stakeholders. This engagement will take the form of stakeholder meetings, open forums, workshops and attending industry conferences and events. I also expect to speak at some of these events.
25. I am keen to get feedback from a wide range of stakeholders on their experiences and perceptions of the financial services industry. To achieve this, there will be a number of ways the public will be able to provide feedback on the points raised in the Issues Paper:
- By making a formal submission on the Issues Paper through the MBIE website. We expect advisers and industry bodies to predominantly respond through this avenue.
 - By responding to a short online survey based on some of the key questions raised in the Issues Paper. To reach a wider consumer audience, MBIE has developed a more accessible, two-page brochure (which seeks feedback on these key questions.) The brochure will be distributed through various channels, such as industry associations, the banks, the media, and NGOs. We expect consumers and their representative organisations to predominantly respond through this avenue.
 - By attending both industry and MBIE organised events in a number of centres, where the key issues raised in the Issues Paper will be debated.
 - By meeting with MBIE officials.

26. MBIE also plans to conduct a consumer survey aimed at better understanding consumers' perceptions of the financial advice industry. This will supplement the consumer research it has already gathered through previous focus groups.
27. Once submissions on the Issues Paper have closed, I will report to Parliament on the review of the FSP Act by the end of August 2015. Permission will be sought toward the end of 2015 for release of an Options Paper to consult on any proposed changes to the Acts.

Consultation

28. The Treasury, the Reserve Bank, the Financial Markets Authority, the Commission for Financial Capability and the Ministry of Justice have been consulted on the attached Issues Paper.
29. The Department of Prime Minister and Cabinet has been informed.

Financial Implications

30. There are no fiscal implications from the proposals in this paper.

Human Rights

31. There are no human rights implications from the proposals in this paper.

Legislative Implications

32. There are no legislative implications from the proposals in this paper.

Regulatory Impact Analysis

33. Regulatory impact analysis requirements are not applicable to the proposal in this paper.

Publicity

34. The Review has received a moderate level of media interest and I expect this to increase with the release of the Issues Paper. MBIE will publish the Issues Paper, brochure and related resources on its website and will advise stakeholders by email when the paper is released. I will release a media statement to encourage stakeholders to take the opportunity to make a submission.

Recommendations

I recommend that the Committee:

1. **note** that the Financial Advisers Act 2008 and Financial Service Providers (Registration and Dispute Resolution) Act 2008 each include obligations on officials to review the Acts and report to the responsible Minister no later than five years after commencement of the relevant sections of these Acts;
2. **agree** to the release of the attached Issues Paper for public consultation to inform the review;
3. **note** the Issues Paper does not propose any legislative changes but seeks feedback from the public to help identify the key issues with the operation of the Acts;
4. **note** the key areas the Issues Paper focuses on include:
 - a. Consumers have the information they need to find and choose a financial adviser
 - b. Financial advice is accessible for consumers
 - c. There is public confidence in the professionalism of financial advisers
 - d. The Financial Service Providers Register and dispute resolution are effective
5. **note** officials are required to report to me by 15 August 2015 on the operation of Part 2 of the Financial Service Providers (Registration and Dispute Resolution) Act 2008;
6. **note** I will present a copy of that report to the House of Representatives as soon as practicable after receiving it;
7. **note** I expect to seek Cabinet approval to release an Options Paper towards the end of the year.

Hon Paul Goldsmith
Minister of Commerce and Consumer Affairs

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