Comprehensive submission form: Conduct of Financial institutions review

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Authorised Financial Adviser

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Question 1

Which overarching duties should and should not be included in the regime? Are there other duties that should be considered?

In particular:

- Do you agree with the pros and cons of each duty?
- Do you have any estimates of the size of the costs and benefits of these options?
- Are there other impacts that are not identified?

I am an authorised financial adviser based in Wellington. I am part of SHARE, a nationwide network of 70 advisers, and have been providing advice since 1994.

I have been involved with the changes over the last decade and see that MBIE and the FMA have worked closely with participants to understand and adapt the new environment. Many of the changes have been borne by Authorised Financial Advisers and I am pleased to see with FSLAA and the new Code of Professional Conduct extend, that these are to be extended to other participants.

Overall, I support the thrust of the paper – its right to identify some of the problems and issues with financial service providers in NZ. The options paper though contains some proposals that I believe will create several significantly damaging unintended consequences and in particular it could lead to the disestablishment of intermediated advice as financial services providers restrict access to their products to those people that are either members of their FAP or to employees of their company. This won't enhance access to advice in New Zealand and consumers will have a narrower choice of products and fewer advisers from whom to access financial advice.

I see that this paper is a response to the FMA investigations of the last few years, over laid with the response to the findings of the Australian Royal Commission. However, my concern is that many of the issues identified in this options paper will (and are) being addressed right now. We have seen a progressive change and with FSLAA now enacted, I submit that this should be allowed to settle for at least 24 months to show that an additional overlay proposed by this options paper is not necessary.

Question 2

Do you think the overarching duty for managing conflicts of interest should be general (as it is currently worded) or focus on conflicts of interest that arise through remuneration?

In particular:

- What are some examples of conflicts of interest that arise outside of conflicted remuneration and incentives?

The culture of distribution of financial services has been sales. New business has always been favoured over retention of existing business by product providers (and this has caused conflict between advisers and providers). Almost all incentives (until the last few years) have been around new business production and encouragement to bring new business in the door. Although persistency of a book was reported on, the reward was really in new business, not servicing existing business.

Managing conflicts of interest is a general requirement as it is not always related to remuneration. – and sometimes the adviser may not be aware of a conflict of interest that may operate at a provider level (such as differing reinsurer treaty, revenue share) and sometimes the insurer/provider/fund manager may want the product to be changed – and will not always be transparent around the reasons for the change being recommended. The principles contained in the new Code of Professional Conduct go far to achieve these aims.

There should be an ethical overly to all business.

Question 3

Is a code of practice required to provide greater certainty about what each overarching duty means in practice?

Over the last 10 years AFAs have changed their culture and conduct, as have a number of registered financial advisers. The culture and conduct review, with responses due at the end of June, has seen many of the providers I deal with review their processes, their culture, and certainly announce that they are moving away from sales targets and rewards which are linked to new business production.

Question 4

Which options for improving product design do you prefer and why?

In particular:

- Do you agree with the pros and cons of the options?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?

Option 3 is preferred.

I reinforce the comments made by SHARE in its submission.

In addition to these, the passing back of benefits on newer policies to older policies is critical. At the current time many loyal clients are disadvantaged by improvements on policies which are not 'passed back' to older policies. This does need reinsurer support – and here is the challenge. It would require changes to existing reinsurer agreements, and I expect would involve financial cost to both parties. It would though enhance the outcome for a majority of customers who have 'legacy' policies.

I'd like to see greater oversight in this area and encouragement for the reinsures and existing insurers to review their 'legacy' books and to provide some reassurance that those policy holders' interests can be protected, but also enhanced. Profitability for a product provider comes from a legacy book, not from initial new business. Finding a balance is key – as running a legacy book without new business is not in a clients' best interest either. New business does lead to product innovation and this will come from an executive who is confident and innovative. Overbearing regulation could stifle this innovation.

Question 6

Which options to improve product distribution do you prefer and why?

In particular:

- Do you agree with the pros and cons of the options?
- Are there other impacts that are not identified – such as unintended consequences or
- impacts on particular business models?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?

I prefer Options 1 and 2.

I work very hard for my clients. I moved to a level commission structure 10 years ago. I have high persistency and I use providers where there is a philosophy of passing back any policy enhancements. I advocate strongly for my clients – both at underwriting, and at claim. I work closely with providers to offer perspective and although I am paid by commission from the providers, I very much see that I work for my clients first and absolutely foremost.

I think the commission structure needs to be regulated. The current system does not encourage retention of older policies and incentivises new business production over retention of business in the medium to long term. The sales culture of insurers is profound. However, mortality and morbidity policies are not products that people line up outside my door each day to buy. No one wants to think about dying or being sick or disabled. It does require tenacity, confidence, training, education and support to develop into a professional adviser where you are able to discuss these issues.

Advisers who are good at this difficult role should be rewarded. And those that have good businesses (and in particular many that are more established) do have an advantage here for they are likely more able to absorb changes in remuneration structures. However, I do fear that a large number of advisers will find it hard to adjust to a new environment. Commission is an effective mechanism to remunerate. It should be retained.

Option 4

I do not support Option 4.

Option 5

I agree with this, though I fear the bureaucracy that would be created to manage this – and as such, a risk-based approach must be taken on this. Otherwise the only ones to benefit from this will likely be the large services and audit companies. This would demand more compliance activity from advisers, who will then not be able to service so many clients, and I'm not sure this leads to better customer outcomes.

Question 7

To assist us in comparing the pros and cons of various options, please provide information about remuneration and commission structures currently in use.

In particular:

- What are common structures, average amounts of remuneration/commissions, qualifying criteria etc.?

The majority of my business' revenue is on a level commission basis. This does lead to predictable and sustainable business revenue. It does require confidence though – and if there is a claim 3 years after the policy has started, the predictable revenue has just stopped! However, it also encourages ongoing advice to clients and keeping in touch. The financial impact of losing a client after 5 years is much greater with a level commission basis than an upfront basis (but less focus on new business production means more time can be spent on servicing existing clients). It's a delicate balancing act.

Question 8

What is your feedback on imposing a duty to ensure claims handling is fair, timely and transparent?

In particular:

- Do you agree with the pros and cons?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of this option?

I have found life insurers to be well organised and resourced in claims – perhaps this reflects the type of claims made (as opposed to significant natural disasters and property damage). Employees of insurers are professional and try hard to see that a claim can be made.

Question 10

What is your feedback on requiring the settlement of claims within a set time?

In particular:

- Are there other impacts that are not identified?
- How do you think that exceptions should be designed?
- Should there be different time requirements for different types of insurance?
- Do you have any estimates of the size of the costs and benefits of this option?

It's not just the insurers that participate in the claims process. Often there are many factors that are outside of insurers control – medical certificates, coroner, medical records, financial records, employer information, and perhaps police reports. Although an insurer could request the medical information at the start, this process would extend the period of time for people to be able to get cover – and may restrict healthy people being able to have easy access to obtaining cover. My experience is that insurers work head to pay a claim in life/disability/medical. The extraordinary pressure on claims teams from natural disasters has shown that there are difficulties with mass claims. Finally, I would add that no one expects that they will need to claim – and if they do, it is often when they are vulnerable and in need of personalised assistance. That is when advisers can reassure and assist in the claims process.

Question 11

Do you agree with the option to empower and resource the FMA to monitor and enforce compliance?

In particular:

- Do you agree with the pros and cons?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?

Yes. FMA has the knowledge and experience. I just hope that by one authority doing this, that they are able to achieve scale and thereby reduce the regulatory cost impost on business.

Question 12

What is your feedback on the option to require banks and insurers to obtain a conduct licence?

In particular:

- Do you agree with the pros and cons?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?

The costs associated with entity licensing appear to us to outweigh the additional benefits over and above those proposed in the broad range of regulatory tools noted in the Options Paper. We do not support the entity conduct licensing and this has not proven to be effective in preventing misconduct in other jurisdictions.

Question 13

What is your feedback on the option which discusses a broad range of regulatory tools?

In particular:

- Do you agree with the pros and cons?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?

This option, without conduct licensing, is preferred for the reasons noted above.

Question 17

What is your feedback on the option of regular reporting on the industry?

In particular:

- Do you agree with the pros and cons?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?

This would be a useful way of helping customers to make an informed choice by providing information to allow them (or the intermediary advising them) to compare suppliers. Asking the financial institutions to prepare the information themselves on a standard basis would assist those institutions to focus on what customers would use to compare them.

Question 18

What is your feedback on the role of industry bodies?

In particular:

- Do you agree with the pros and cons?
- Are there other impacts that are not identified?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of the options?
- Who should the conduct regulation apply to?

I am a member of Financial Advice New Zealand. I support the existing purpose of a professional body. I do see that it could become more involved as a useful contributor to assist with conduct and ethics. However, membership is voluntary and so there would be a regulatory cost impost on the professional body – which would mean that fees would increase (though with the current funding model from the government for the FMA there seems to be an inevitable increase in compliance costs – which ultimately is borne by the client).

Question 19

What is your feedback on the options regarding who the conduct regime should apply to?

In particular:

- Do you agree with the pros and cons of the options?
- Are there other impacts that are not identified e.g. do the proposed overarching duties?
- conflict with existing regulation that applies to other financial institutions?
- Are there other options that should be considered?
- Do you have any estimates of the size of the costs and benefits of these options?
- Which options do you prefer and why?

It needs to apply to all participants equally and fairly. And this may mean a proportional cost.

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