

Submission

From: Independent Development Solutions Limited.

On: MBIE Issues Paper
Review of the FAA 2008 and the FSPA 2008

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Independent Development Solutions Ltd (IDS) appreciates the opportunity to submit a response to the Ministry on this Issues Paper. We believe there is a real opportunity to tidy up what was a hastily implemented regime and one that has brought good and bad in equal measures.

IDS

We believe New Zealanders deserve good financial advice and we believe there are good financial advisers who can help them with their financial needs. The issue is that it is getting harder to run an independent financial advisory business and keep up with all the regulatory requirements. That is why we set up Independent Development Solutions Ltd.

Our goal at IDS is to help financial adviser businesses reduce the risk of non-compliance and help them increase profitability.

We want to help good advisers thrive and help Kiwis achieve their financial goals and we do this by helping them cope with their regulatory requirements and making sure they find efficient ways to deliver their advice.

The key services we provide advice businesses to ensure they are on track are;

Advice Process Reviews and Approval
DIMS and Peer to Peer Lending Reviews
Advice Process Development and Documentation;
Compliance Checking and Support.

In the last four years we have helped over 1000 advice businesses to be more compliant than they were before we were engaged.

FAA Review –IDS submission**1. Do you agree that financial adviser regulation should seek to achieve the identified goals? If not, why not?**

Yes though we think Goal one could be expanded to say ‘Consumers have information to find and choose the appropriate financial advice’. Advice comes in all shapes and sizes and from different entities and technologies. The Financial Advisers Act should really be the Financial Advice act. This could then allow scope for future technologies as well as institutional advice that is not linked to just a person. Also consumers should be able to identify the advice as either Financial Product Information, Financial Product Advice (Currently defined as Financial Advice) or Financial Advice (Currently defined as ‘An Investment Planning Service and could be expanded across a range of services, Insurance, Debt, Property, etc). These three levels of ‘Advice’ cover all the advice situations we have seen being delivered across over 1000 advisers from QFE/AFA/RFA. But currently they are lost in the current definitions and hard to identify for advisers and consumers.

2. What goals do you consider should be more or less important in deciding how to regulate financial advisers?

Consumer Information to easily identify the type of advice or service. Confidence that if the advice is coming from a licensed/authorised/registered source that it is compliant and/or if it goes wrong and it wasn’t compliant the regulator will take action.

Consumer want to know who they can trust for Financial Advice and who will put their interests first. They are also happy to just seek Product Information or Advice from entities who are selling products as well. At the moment though there is no easy way to tell the difference.

3. Does this definition adequately capture what financial advice is? If not, what changes should be considered?

No because the planning services for everything except Investment has been left out.

There are three types of advice consumers want.

Financial Product Information – A Product Provider or Distributor should be able to provide information on their products to assist consumers in making an informed decision on if they wish to purchase the product or not.

Financial Product Advice – A Product Provider or Distributor should be able to assist a consumer in selecting products/benefits/options and help with advice related to the product such as selecting the right level of contributions or sums insured or interest rate to achieve what the client has stated as their reason for wanting the product.

Financial Advice – An Adviser (AFA/Licensed Adviser or entity) is a person/place a consumer can go to and say I want some help planning my needs in the area of (Investment/Retirement/Debt/Mortgage/Insurance/Property) and then based on that advice I also want some Financial Product Advice to achieve that plan. This advice should not come from a Product Provider and should be a separate entity to avoid the natural conflict of interest.

4. Is the distinction in the Financial Advisers Act (FA Act) between wholesale and retail clients appropriate and effective? If not, what changes should be considered?

It is appropriate but not effective. Basically if you own a house in Auckland you could be a Wholesale Client.

We believe the Wholesale definition needs to be lifted higher because people with the current levels are the ones who need the most protection when getting advice and currently they can be excluded by broking and investment houses as wholesale.

5. Is the distinction in the Act between a personalised financial service and a class service appropriate and effective? If not, what changes should be considered?

It is not. The Class Service and latterly defined Class Advice is being used as a short cut around Personalised Advice to sell Products. We suspect in half the cases the consumers would have assumed it was personalised. See suggested changes above.

6. Is it appropriate to have different requirements on advisers depending on the risk and complexity of the products they advise upon?

Yes. Advisers who provide Advice and/or planning services in a particular area should have the relevant knowledge and skill to give advice on the particular products and or services. If you expanded the Definition of Financial Advice as suggest above we would expect to see the code apply to all Financial Advisers and cover Insurance/Mortgages/Property/Etc.

7. Does the current categorisation system accurately reflect the level of complexity and risk associated with financial products? If not, how could it be improved?

No. There is just is much risk when planning insurance debt and property investment as there is in picking an investment portfolio. The categories that split AFA/RFA should be dropped. If you had the advice categories suggested above the advisers can either be a Financial Product Advice who represents Product Providers and can help clients select (Insurance/Mortgage/KiwiSaver/Managed Fund) or they become a Financial Adviser who is licensed/Authorised to provide financial advice in a particular area. i.e. Financial Planning Insurance Investment Planning Debt/Cash Management Property Investment.

8. **Do you think that the term Registered Financial Adviser (RFA) gives consumers an accurate understanding of what these advisers are permitted to provide advice on and the requirements that apply to them? If not, should an alternative term be considered?**

No it doesn't. It implies a higher designation. See Advice types above.

9. **Are the general conduct requirements applying to all financial advisers, including RFAs, appropriate and adequate? If not, what changes should be considered?**

Yes the general conduct requirements are appropriate for those giving Financial Product Information and Financial Product Advice. They also mirror the FMCA and Fair Trading act as well as some license requirements for bank and non-bank lenders. In fact one could make a case that QFE legislation is overkill with all the new legs and regs.

10. **Do you think that disclosing this information is adequate for consumers? Should RFAs be required to disclose any additional information?**

The Current Disclosure Information for all adviser is appalling. The Disclosure requirements from the Investment Advisers Act, which most of the industry had adopted via the professional associations prior to the FAA, was a much better document for consumers.

We spend a lot of time with Advisers and Advice Businesses designing About Us documents to give better consumer information.

The current RFA/QFE and Primary AFA statements have the information that consumers should be able to find on the FSPR. The Disclosure Statements should be standard across all Financial Advisers and should contain relevant information, Who I am, what I do, Areas of specialty, How I get Paid, Which Providers I use, Relevant Qualifications and Experience, Restrictions or limitations to the services.

11. **Are there any particular issues with the regulation of RFA entities that we should consider?**

RFA Advisers get stuck because there services can range from Product Information, class services to full Insurance/Cash/Debt planning services and they can have one provider or many providers yet there are no clear rules or guidelines around Knowledge and Skill required.

If you remove the Product Categories and Changes the Definitions of Financial Advice the RFA question will be answered out the back of those decisions.

We do see RFA advice in areas such as Property and Wholesale clients which we believe is a gap in the current regime.

12. **Are the costs of maintaining an adviser business statement justified by its benefits? If not, what changes should be considered?**

NO. We have had several of our AFA clients who have had monitoring interaction with the FMA and the FMA have not asked for the latest copy of their ABS.

The whole purpose of the ABS was to have a document on hand that the FMA could pick up at any time and refer to when monitoring the adviser or QFE. It is not being used by the FMA therefore it should be replaced by the AFA annual return information and stored in a

database at the FMA and updated annual or when there is a major change in business activities of the AFA.

13. Is the distinction between an investment planning service and financial advice well understood by advisers and their clients? Are any changes needed to the way that an investment planning service is regulated?

NO. Yes see above definition of Financial Advice. The Taskforce had it better defined as a Financial Planning Service but Banks, I mean someone, lobbied and got changed it at the 11th hour. Had that not happened you would have an extra 3000 AFAs today doing Insurance Planning Mortgage Planning Property Investment planning....

14. To what extent do advisers need to exercise some degree of discretion in relation to their clients' investments as part of their normal role?

The DIMS licensing regime got it wrong. AFA's using wrap accounts and model portfolios via custodians should have been able to be authorised through their current AFA status and not need a license. The AFA who was offering a personalised investment and was handling the investments directly or on behalf of the clients should have been the ones that required a license as they were acting as the adviser and the fund manager. It is a mess really.

15. Should any changes be considered to reduce the costs on advisers who exercise some discretion, but are not offering a funds management type service?

Review Class DIMS by AFAs as a non-licensed activity under the FMCA.

16. Are the current disclosure requirements for Authorised Financial Advisers (AFAs) adequate and useful for consumers?

NO.

The PDS information should be on the FSPR website. The old Investment Adviser Disclosure templates should be reviewed as a starting point of a meaningful consumer document. The Australian FSG's are a good example to look at as well.

Disclosure of Fees and Remuneration should be in the PDS and then actual fees REM and Conflicts of interest specific to the advice should be included in the written advice rather than a separate SDS.

17. Should any changes be considered to improve the relevance of these documents to consumers and to reduce the costs of producing them?

See above.

18. Do you think that the process for the development and approval of the Code of Professional Conduct works well?

Yes

19. Should any changes to the role or composition of the Code Committee be considered?

No

20. Is the Financial Advisers Disciplinary Committee an effective mechanism to discipline misconduct against AFAs?

Yes

21. Should the jurisdiction of this Committee be expanded?

Yes. They should cover all Financial Advisers defined by the act and rule not only on Code related matters but also Conduct related matters for RFA and QFEs (Not QFE adviser individually the QFE themselves)

22. Does the limited public transparency around the obligations of Qualifying Financial Entities (QFEs) undermine public confidence and understanding of this part of the regulatory regime?

Yes

QFEs should be able to give Product Information and Product Advice as described above. But an AFA shouldn't be able to work for a QFE. Code standard one can't be paramount if you want to keep your job. The limitations and natural conflicts don't work.

Consumer are happy to go to a product provider say KiwiSaver and have someone help them work out if they will have enough money for retirement using that KiwiSaver product. This is Financial Product Advice no worries.

But if a consumer wants advice that is in their best interests then they should be able to identify an AFA or Licensed Financial Adviser who doesn't work for a product provider and who is bound by the code to act like a Fiduciary.

23. Should any changes be considered to promote transparency of QFE obligations?

We thought that all QFEs had to follow the Code of Conduct for AFAs anyway and that if they didn't or couldn't meet a code standard they had to state in their QFE ABS 'If not why not?' Therefore they only issue is why in four years have no QFE's been picked up for not meeting this requirement and/or why hasn't it been published?

Confidence would happen if the rules were enforced evenly across the board.

24. Are the current disclosure requirements for QFE advisers adequate and useful for consumers?

No.

25. Should any changes be considered to improve the relevance of these documents to consumers or to reduce the costs of producing them?

Yes.

26. How well understood are the broker requirements in the FA Act? How could understanding be improved?

Not Very. The definition of Broker had multiple means in the industry and to the public. I think the definition and terminology should be reviewed. If the definition was changed then Financial Product Advisers (as defined above) who distribute multiple provider

products could be called Insurance Brokers or Mortgage Brokers.

27. Are these requirements necessary and/or adequate to protect client assets? If not, why not?

No evidence to point to it not being the case.

28. Should consideration be given to introducing disclosure requirements for brokers? If so, what would need to be disclosed and why?

No comment.

29. What would be the costs and benefits of applying the broker requirements in the FA Act to insurance intermediaries?

No Comment.

30. Are the requirements on custodians effective in reducing the risk of client losses due to misappropriation or mismanagement?

Yes

31. Should any changes to these requirements be considered?

No Comment

32. Is the scope of the FA Act exemptions appropriate? What changes should be considered and why?

Property and Property Investment Advice should be included.

33. Does the FA Act provide the Financial Markets Authority (FMA) with appropriate enforcement powers? If not, what changes should be considered?

We would suggest considering allowing the use of the Disciplinary Committee to handle Conduct under the act issues rather than just Code Conduct issues for Financial Advisers.

34. How accessible and useful is the guidance issued by the FMA? Are there any improvements you would like to see?

It is a mixed bag and at times extremely frustrating.

DIMS is a good example. The rules changed right up until the 11th hour after consultation. This meant that people who 6 months ago had they known about the new changes would have proceeded with a license application.

Guidance is also launched sometime on the website sometime by email and sometime I don't know how. We have had to hire a person to track the changes to regulations, legislation, website updates, guidance notes etc from the FMA as there is no one clear definitive channel of communication.

Some of the guidance notes themselves are excellent and provide good information for a principals based regime.

35. What changes should be considered to make the current regulatory regime simpler and easier for consumers to understand? For example, removing or clarifying the distinction between AFAs and RFAs.

See suggested changes to Financial Advice Definitions above.

Consumers understand if they go directly to a product provider they should be able to get product information and product advice.

The current regime makes it difficult for consumers to identify what an RFA or AFA does.

Therefore the regime should state who are the Financial Advisers who can give Financial Advice in certain areas of expertise and will under the code.

Therefore Entities or Individual should be able to license/authorise as Financial Advisers for Insurance/Investment/Cash/debt management/property

Advisers who want to give Financial Product Advice only could register either via a product provider or via a Licensed/Authorised entity or individual and they should have responsibility for the adviser to ensure they meet conduct requirements under the act as well as have them listed on the FSPR as an adviser specializing in ?

36. To what extent do consumers understand that some financial advisers primary roles may be selling financial products, rather than solely acting as an unbiased adviser to their clients?

We think consumers who approach a product provider for advice understand the relationship. The RFA and AFAs who are non-provider aligned it is less clear.

37. Should there be a clearer distinction between sales, information provision, and advice? How should such a distinction be drawn? What should or should not be included in the definition of financial advice?

See definitions above for Financial Advice.

38. Do you think that current AFA disclosure requirements are effective in overcoming problems associated with commissions and other conflicts of interest?

The SDS is.

39. How do you think that AFA information disclosure requirements could be improved to better assist consumer decision making?

Yes see earlier comments.

40. Do you support commission and conflict of interest disclosure requirements being applied to all financial advisers? If so, what requirements are appropriate for different adviser types?

Yes they should all disclose the revenue they and their associated entity gets for the Financial Product Advice they give.

There is No difference – All advisers including QFEs have conflict of interest when recommending products.

If a client has an existing KiwiSaver with ASB then a QFE adviser will tell them to move to their products because of a (insert generic reason). If they don't sell enough KiwiSaver (or mortgages or insurance) the QFE adviser will lose 100% of their income when they are let go for non-performance. (or their manager is)

Same for AFAs or RFAs – if your KiwiSaver is with ASB I recommend XYZ because I can be your adviser. Which means I get a trail commission from XYZ, but don't from ASB.

So yes disclosure of revenues from advice is important.

41. Do you think that commissions should be restricted or banned in relation to financial advice, and if so, in what way? What would be the costs and benefits of such an approach?

No. We have seen some fantastic financial advice given by commission paid advisers and we have seen some terrible advice given by advisers charging fees. The method of remuneration has no direct correlation to the quality of the Financial Advice.

Stick to applying the conduct and code obligations as they are the best tools the regulator needs for handling bad advice.

42. Has the right balance been struck between ensuring advisers meet minimum quality standards and ensuring there is competition from a wide range of providers (and potential providers)?

Yes

43. What changes could be made to increase the levels of competition between advisers?

None.

44. Do you think that the Code of Professional Conduct for AFAs strikes the right balance between requiring them to understand their clients and ensuring that consumers can get advice on discrete issues?

Yes it does, though definitions elsewhere of Class Service, Class Advice, Limited Advice confuse the issue. If the Financial Advice definitions and types are defined better, the Code will work better in practice.

45. To what extent do you think that the categorisation of types of advice and advisers is distorting the types of advice and information that is provided?

It has driven the evolution of the whole industry for the last four years and has in fact reduced access to advice in some areas and missed areas of risk (Property Investment).

46. Are there specific compliance requirements from the FA Act regulation that have affected the cost and availability of independent financial advice?

The AFA requirements and costs are over the top and they have impacted a lot of adviser's

decisions not to Authorise and stick to Category Two advice only. The IFA has done some great analysis on the costs. It needs to be reviewed.

47. How can regulatory requirements be made less onerous without reducing the quality and availability of financial advice?

- Reduce the reporting requirements.
- Outsource Reviews and Audits so it doesn't double up with FMA monitoring.
- Review AML/CFT reporting entity status for Financial Advisers
- Remove the ABS requirements.
- Allow advice by other means other than written advice.

48. What impact has the Anti-Money Laundering and Countering Finance of Terrorism Act had on compliance costs for advisers? How could these costs be minimised?

The IFA has completed an analysis of the costs and they seem ball park to us.

Remove Reporting entity status from Advisers who don't take monies. Require them to follow the Product and Service Providers requirements and have all advisers required to report suspicious transactions and request across all financial transactions not just investments.

49. What impact do you expect that KiwiSaver decumulation will have on the market for financial advice in New Zealand? Are any specific changes to regulation needed to specifically promote the availability of KiwiSaver advice?

It will increase demand for Financial Product Information, Financial Product Advice and Financial Advice in the future. No specific changes required other than those suggested to tidy up the current definitions.

50. What impact do you expect that the introduction of the Financial Markets Conduct Act (FMC Act) will have on the market for financial advice in New Zealand? Should any changes to the regulation of advice be considered in response to these changes?

Our belief is that the FMCA and licensing of non-banks lenders, insurance companies and changes to the Fair Trading Act and CCFA should have all happened prior to the implementation of the FAA. Then you could have just added a Financial Advice licence to the FMCA for Financial Advisers as defined above, and all the Product Providers could have had sections in their relevant FMCA or Reserve bank license covering Financial Product Advice and Distribution and no need for QFEs.

51. Do you think that international financial advice is likely to increase? Is the FA Act set up appropriately to facilitate and regulate this?

Yes, international financial advice into and out of New Zealand will continue to increase. No, the FA Act is not set up to appropriately facilitate and regulate this.

52. How beneficial are the current arrangements for trans-Tasman mutual recognition of qualifications? Should further arrangements be considered?

Not very. It is a minefield.

53. In what ways do you expect new technologies will change the market for financial advice?

New Zealanders are DIY in nature and will use the internet to find answers. That is why we would expand the Financial Advisers Act to be The Financial Advice Act.

54. How can government keep pace with technological developments to ensure that quality standards for advice are maintained, without inhibiting innovation?

Make the Websites or entities bound by the same rules.

55. Are the minimum ethical standards for AFAs appropriate and have they succeeded in fostering the ethical behaviour of AFAs?

Yes

56. Should the same or similar ethical standards apply to all types of financial advisers? Based on our definitions of Financial Advice above all Financial Advice should be to the same standard.

57. What is an appropriate minimum qualification level for AFAs?

The bar should be raised to Diploma level within the next 5 – 10 years, but competence testing and reviews should also confirm could also confirm Re-Authorisation rather than going back to school.

58. Do you think that RFAs (for example insurance or mortgage brokers) should be required to meet a minimum qualification relevant to the area of advice they specialise in? If so, what would be an appropriate minimum qualification?

As per our definitions above for Financial Advice Yes.

59. How much consideration should be given to aligning adviser qualifications with those applying in other countries, particularly Australia?

If we want cross boarder advice then it must be considered.

60. How effective have professional bodies been at fostering professionalism among advisers?

Excellent!

61. Do you think that professional bodies should play a formal role in the regulation of financial advisers and if so, how?

Only if there is one, they could be considered as a replacement for the Code Committee in setting the Code Requirements. What have three or four different codes of conduct. The body would have to be able to match the code to the different types of advice and advisers, which is possible and something IDS would happily get involved with as we work with all the associations currently.

62. Should any changes be considered to the relative obligations of individual advisers and the businesses they represent? If so, what changes should be considered?

At the moment there is a vague reference to A representing B for advice therefore B is responsible for the advice too. If you allowed entities to License for Financial Advice and then list who they employ then you shouldn't need separate license's for individuals as well.

63. Is the QFE system achieving its goals in terms of consumer protection and reducing compliance costs for large entities? If not, what changes should be considered?

No to consumer protection Yes to reducing compliance costs per adviser compared to AFAs.

QFE's who are product providers should just be product providers who can give Financial Product Information and Financial Product Advice without being licensed separately for that. However they should also not be Licensed as Financial Advice Entities for Financial Advice Service either.

64. Do you agree that the Register should seek to achieve the identified goals? If not, why not?

Agreed.

65. What goals do you consider should be more or less important in reviewing the operation of the Register?

The register should be a repository for regulatory information that can be searched and transparent and provide valuable information. It should replace basic disclosure requirements such as AFA PDS.

66. Do you agree that the dispute resolution regime should seek to achieve the identified goals?

If not, why not?

Agreed

67. What goals do you consider should be more or less important in reviewing the dispute resolution regime?

ACCESS and AWARENESS first,

68. Does the FMA need any other tools to encourage compliance with financial service provider (FSP) registration? If so, what tools would be appropriate?

The FMA could look to license external auditing firms to provide two yearly reviews of Licensed or Authorised Advisers to save on direct monitoring costs.

69. What changes, if any, to the minimum registration requirements should be considered?

No comment.

70. Does the requirement to belong to a dispute resolution scheme apply to the right types of financial service providers?

Yes

71. Is the current framework for the approval of dispute resolution schemes appropriate? What changes, if any, should be considered?

Yes

72. Is the current framework for monitoring dispute resolution schemes adequate? What changes, if any, should be considered?

No. The FMA should have a role that reviews or moderates the DRS providers to ensure they are providing similar levels of protection for consumers.

73. Is the existence of multiple schemes and the incentive to retain and attract members sufficient to ensure that the schemes remain efficient and membership fees are controlled?

Yes

74. Should the \$200,000 jurisdictional limit on the size of claims that dispute resolution schemes can hear be raised in respect of other types of financial services, and if so, what would be an appropriate limit?

No comment

75. Should additional requirements to ensure that financial service providers are able to pay compensation to consumers be considered in New Zealand?

No

76. What features or information would make the Register more useful for consumers?

Current Basic Disclosure Information for Financial Advice Businesses.

77. Would it be appropriate for the Register to include information on a financial adviser's qualifications or their disciplinary record?

Yes

78. Do you consider misuse of the Register by offshore financial service providers is a significant risk to NZ's reputation as a well –regulated jurisdiction and/or to NZ businesses?

Yes

79. Are there any changes to the scope of the registration requirements or the powers of regulators that should be considered in response to this issue

No Comment

80. What are the effects of (positive and negative) competition between dispute resolution schemes on effective dispute resolution?

No comment

81. Are there ways to mitigate the issues identified without losing the benefits of a multiple scheme structure?

No comment

82. Are the current regulatory settings adequate in raising awareness of available dispute resolution options? How could awareness be improved?

No comment