Summary of goals and key questions

Proposed goals	Key questions for feedback
Goal 1: Consumers have the information they need to find and choose a financial adviser.	Do consumers understand the regulatory framework? Should there be a clearer distinction between advice and sales? How should we regulate commissions and other conflicts of interest?
Goal 2: Financial advice is accessible for consumers.	Does the FA Act unduly restrict access to financial advice? How can compliance costs be reduced under the current regime without limiting access to quality financial advice? How can we facilitate access to advice in the future?
Goal 3: Public confidence in the professionalism of financial advisers is promoted.	Should we lift the professional, ethical and education standards for financial advisers? Should the individual adviser or the business hold obligations?

Regulation of Financial Advice

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

Do consumers understand the regulatory framework?

NO they don't

They do not understand what the designations "Approved" and "Registered" mean. In fact I have heard that some consumers won't deal with advisers who are 'only approved', they want to deal with someone who is registered.

The terms were intended to delineate based on the complexity of the financial products. However, the split was, at best, fairly arbitrary and, at worst, just plain wrong.

We propose a fundamental re-think of the structure ***with the aim of providing total clarity for consumers.***

The restructuring is in 2 parts.

Part 1

Under the current structure, the consumer has absolutely no idea what areas of financial advice an adviser deals in. They may very well contact an adviser for advice on 'life insurance' only to find the adviser works only in investment.

However, if the whole field of "financial advice" is divided into specific disciplines, viz.

- Life Risks Insurance – commonly referred to as life insurance
- General Insurance – commonly referred to as fire & general
- Investments
- Mortgages
- Property Investments might either be a separate designation or be a classification under Investment such as "Investment – property",

"Financial Advisers" would then be classified according to the area/areas they work in, e.g.;

- Investment adviser

Life insurance adviser
Investment and Mortgage adviser etc

This is not necessarily a fully comprehensive list. For example there might be an area for Estate Planning.

This would then make it very clear to the consumer what areas the 'adviser' works in and is competent in (see Part 2).

Part 2

Create **two (**2) totally distinct designations; Adviser and Product Marketer. The distinction needs to be totally clear as would be the case if the following requirements to be an adviser were enforced.

Adviser

Requirements to be classified as an Adviser would be;

1. Totally unrestricted in choosing the companies they place business with. Among other things, this would exclude anyone who;
    I. Is required to put a level of their business with any one company, whether this is by way of an amount or a percentage.
    II. Has only a select number of companies they can place business with.
2. Always put, and be seen to put, the client's interests first. On the basis of "being seen to", this would exclude anyone who;
    I. Is in an employee relationship with a provider of financial products.
3. Personally responsible for the advice they give.
4. Meet prescribed levels of education/competence in the specific discipline(s) they are accredited for. On this point
    I. We believe the current Certificate (Level 5) is unsuitable for this and needs to be replaced appropriate qualifications designed for each specific discipline with commonality in some areas such as the current Standard Set B paper.
    II. Level 5 qualification should be seen as a base-entry point. Higher levels of education/competency would be appropriate but all advisers who do not currently have these must be given a reasonable time to acquire them at a reasonable cost.
    III. As insurance products change on a regular basis, I believe it would be appropriate for all Insurance Advisers to be accredited in the product range of any provider they claim to be able to write business for. This accreditation would need to be renewed at least annually.
5. Meet prescribed levels of ongoing Professional Development specific to the discipline(s) they are accredited for.
6. Provide full disclosure along the lines currently required for AFAs.
7. Belong to an approved Resolution Disputes Scheme.
8. Pay an annual Licence fee & be individually monitored by the FMA.

Under this structure, the adviser would then be referred to as "Licenced" or "Registered"

Product Marketer

This would refer to anyone else either selling product or offering "advice" who does not meet these above requirements. This would include all bank and insurance staff.
Product Marketers would be required to:

1. Advise the client if a level or percentage of their business must be written through any particular company and, if so, what that level or percentage is.
2. Ask the client if the financial product they sell is replacing existing business and, if so, state quite clearly that the product they are selling or recommending may not be as appropriate for the client's needs as the one being replaced.
3. Be suitably trained for the role. If they are an employee or part of an entity currently called a QFE, it is the responsibility of that organisation to ensure they are properly trained and follow all requirements. Failure of a Product Marketer to comply should bring sanctions against the organisation as a whole from requiring immediate retraining of staff to cancellation of the 'licence' for the organisation.
4. Advise the client the name of the entity responsible for their training and ensuring they comply and their dispute resolution procedures.

Qualifying Financial Entity
As the term Qualifying Financial Entity is not understood by consumers and anyone within an existing QFE would not have the designation of Adviser, the term can be removed.

Should there be a clearer distinction between advice and sales?

With the structure outlined above, the distinction between advice and sales is self-evident – only Advisers can advise, Product Marketers sell

How should we regulate commissions and other conflicts of interest?

While it can be considered that any form of commission creates a conflict of interest, full disclosure under the adviser's Disclosure Statement makes the client fully aware of the facts and they can base their decisions with this in mind.

In our opinion, banning commissions in favour of fee-based remuneration is really ***relevant to investment only*** where commission paid, especially an annual commission based either on contribution or fund balance, directly impacts on the net investment return to the client.

Therefore, we see that different rules could apply between investment products and risk products

Considering risk insurance, in general terms, New Zealanders are underinsured. Banning commissions would make the profession untenable for many current advisers which would only make this worse. There is very little appetite by consumers to pay a fee for service and, quite frankly, any fee your standard "mum & dad" might be willing to pay would likely be too small for an adviser to run a viable business. How would these consumers feel about paying a fee which results in advice they don't take up?

An ultimate goal might be to replace current up-front commission models with renewal models. In fact many established life risk advisers operate solely on a renewal commission basis.

However, making this model mandatory for all advisers would make it very difficult to recruit new people into the profession as they would start with no income but some expenses to get Licenced etc then be earning insufficient to make a viable business.

What is probably ***not understood*** by those not directly involved in the profession is the amount of time per case involved in getting an insurance plan implemented – including the time involved with potential clients who ultimately don't proceed.

Is the Towbridge Report relevant in New Zealand?

Let's make it quite clear, the situations in Australia and New Zealand are very different.
In Australia;

- An entity holds a licence to carry out financial services

- Individual advisers come under the umbrella of the licensee
- All commissions are paid to the licensee who then determines any split of those commissions between the adviser and the licensee.
- The licensee can receive a bonus from the supplier based on the volume of business.
- Australia's regulatory regime was far more draconian than New Zealand's.
- Australia has a higher rate of replacement business than New Zealand.
- Australia has a 1-year claw-back of commissions. I.e., once the contract has been in force 12 months, the adviser can rewrite the business with another insurer and there is no write-back of the commissions paid to the licensee.

In New Zealand;

- Individual advisers are 'licenced' to carry out financial services, with the exception of QFEs.
- Commission is, generally, paid directly to the adviser.
- We have a lower level of replacement business than Australia
- Generally, there is a write-back period of at least 2 years.

If we are really concerned with "churn" then, perhaps we should be looking more closely at;

- Insurance companies who offer over-the-top levels of commission, sometimes for a limited time and often with very 'generous' take-over terms. We know of companies who have offered to take over entire sections of business from some advisers just on the signing of a new direct debit in favour of their company.
- Advisers whose method of operation indicates, quite clearly, the regular movement of clients from one company to another once the write-back period has expired.

If these were cracked down on with examples being made of offenders we would see real cases of "churn" minimised with replacement being in line with the intentions of the Act; "in the client's best interest".

Goal 2: Financial advice is accessible for consumers

Does the FA Act unduly restrict access to financial advice?

Investment Advice – YES because a large number of advisers no longer give advice in this area because of the requirements imposed by legislation especially in light of the fall-out from the GFC.

Insurance Advice – probably not significantly.
However, the Act, by defining advice which excludes "selling", allows what the consumer might ***believe*** to be advice to be given without the governance required for advice.

How can compliance costs be reduced under the current regime without limiting access to quality financial advice?

Need to differentiate between what is a true compliance cost and what are additional costs advisers now incur to achieve Best Practice.

Direct costs of compliance would include registration fees, compulsory audits and Complaints scheme costs and, aside from reducing the cost or frequency of these, there is probably little that can be achieved here.

The additional time and software required might be considered as indirect costs of compliance but, again, how much of this is an actual compliance cost and how much is best practice?

Possibly the area where costs can be reduced is in the area of paperwork "required" by compliance when giving advice. We believe there is a real misconception about how detailed the reports, sign-off documents etc need to be so clarifying this so advisers can reduce the paperwork would be a good starting point.

How can we facilitate access to advice in the future?

We don't see this as the responsibility of legislation or the bodies set up to regulate.

What we do believe is that consumers who don't currently use an adviser;

- have confidence in differentiating between who will advise them and who will sell to them.
- have anywhere to go to research potential advisers for their needs.

We believe that the structure we are proposing along with changes to the FSP Register (see below) will go a long way to rectify this.

We also believe that, once the changes are made, there needs to be a comprehensive campaign to educate the public of the structure. This campaign would emphasise the difference between Advisers and Product Marketers.
To date we have seen no real evidence of any attempt to educate the public, other than the Out to Get the Cowboys which did absolutely nothing to instil confidence.

Goal 3: Public confidence in the professionalism of financial advisers is promoted

Should we lift the professional, ethical and education standards for financial advisers?

See our notes on restructure classification of advisers by areas of advice.
Specifically, we recommend the following educational standards for Advisers (not Product Marketers)

Investment Advice

- The current Level 5 Certification is largely based on Licenced Investment Adviser skill-sets and may still be appropriate – though only as an entry-point.
- Perhaps greater emphasis needs to be given to be given to further education including a new Level 6 qualification as well as qualifications like degrees and CFP.

Insurance Advice

- The paper (Standard set D I think) relating to Insurance is a joke. At best it is a very basic introductory paper on the area of risk.
- A more appropriate set of papers must be devised, possibly akin to the old IIAA papers.
- Again, a Level 6 standard

General Insurance

- I believe there are adequate existing papers within IBANZ for this area

Mortgage Advice

- Again, a suitable set of papers could be devised if the Level 5 paper is insufficient

Estate Planning Advice

- ??

On attaining a Level 6 qualification, or higher, the adviser could be classified as "Licenced" rather than Licenced/Registered.

Should the individual adviser or the business hold obligations?

With our recommended restructure this issue largely disappears since an Adviser will, automatically, hold the obligation.

For Product Marketers, the entity to which they belong would hold the obligation
Having said that, we also believe that the failure of one of their product marketers needs to impact significantly on the organisation as a whole.

Financial service provider registration and dispute resolution

Could the Register provide better information to the public?

Yes.

- The FSP Register needs to be;
    1. The 1st web-site listed on a google search.
    2. Must be searchable based on location.
    3. Must be searchable based on area of advice required by the consumer. This would be relatively straightforward under our recommended structure
- The first page accessed on the Register could contain explanations of the various qualifications.
- It would be meaningful for the general details to show other related qualifications (CFP, CLU…..).
- Access to the advisers documentation (Business Statement, disclosure statement etc) should be available via the site
- Possibly some relevant background information to show such as previous roles in the industry, years in the different roles etc.

How can we avoid misuse of the Register by overseas financial service providers?

Only allow financial services providers who are currently actively operating in New Zealand to be registered.

What is the impact of having multiple dispute resolution schemes?

Competition. Advisers able to move to another scheme if they are getting poor service.

Part 2 – Financial Advisers Act

Role and regulation of financial advice

Goals for financial adviser regulation

63. The main purposes of New Zealand's financial markets legislation, set out in the FMC Act and referred to in the FA Act, are to:

a) Promote the confident and informed participation of businesses, investors and consumers in financial markets

b) Promote and facilitate the development of fair, efficient and transparent financial markets.

64. We have developed the following framework for thinking about how regulating financial advice and financial advisers can contribute to these purposes:

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

Fully covered

2: Financial advice is accessible for consumers

Covered

3: Public confidence in the professionalism of financial advisers is promoted

Partially covered.

Once the correct framework around adviser designation and qualification is in place there needs to be education campaign to inform the public about just what these mean and how the consumer can be confident when using the services of an "Area of Expertise" Adviser

69. This goal is clearly reflected in the statutory purpose of the FA Act: "*to promote the sound and efficient delivery of financial adviser and broking services, and to encourage public confidence in the professionalism and integrity of financial advisers and brokers*".

1	Do you agree that financial adviser regulation should seek to achieve the identified goals? If not, why not? Yes
2	What goals do you consider should be more or less important in deciding how to regulate financial advisers?

How is financial advice defined?

70. Section 10 of the FA Act defines **financial advice** as when a person *makes a recommendation or gives an opinion in relation to acquiring or disposing of a financial product*. There are a number of exclusions from this definition, including providing information about a financial product, giving advice about a class of financial products or a process for acquiring or disposing of a financial product, transmitting the advice of another person, and recommending a person consult a financial adviser.

71. Financial advice does not typically capture advice about purchasing physical property, such as land, as this is outside of the definition of a financial product. Property investment schemes that are captured by the FMC Act as managed investment schemes are included as financial products.

3	Does this definition adequately capture what financial advice is? If not, what changes should be considered? See opening comments about restructuring. Selling a property for investment or rental (which is for investment anyway) must be included. Surely this is a very significant "financial product". Sometimes these are advertised as 'the way to financial security', 'wealth acquisition' or 'retirement funding' so, in my opinion, they must be subject to the legislation.

What are the different types of financial advice?

Who can provide financial advice depends on:

1: Who the client is

The majority of requirements in the FA Act only apply to financial adviser services provided to **retail clients**: defined as clients who are not **wholesale clients** (***section 5C*** of the FA Act). Wholesale clients are persons who, due to their assets, size or sophistication, are assumed to be able to effectively choose a financial adviser without much regulatory assistance. The wholesale client definition was recently amended to bring it closer to that in the FMC Act.

2: Whether the advice is personalised

The FA Act applies tighter restrictions on who can provide a personalised financial service i.e. personalised advice that takes into account a client's particular financial situation or goals. A class service is defined as advice that does not come under the definition of a personalised financial service. For the ease of the reader, this paper refers to these types of advice as 'personalised advice' and 'class advice' respectively.

The rationale behind placing higher restrictions on personalised advice is that someone receiving personalised advice has a reasonable expectation that their circumstances have been properly taken into account and that it usually takes a higher level of skill and competence to make this assessment.

3: The product being advised on

The FA Act divides financial products into **category 1** and **category 2** products. Category 1 products have been assessed as being higher risk or more complex and therefore advice on these products is subject to higher regulatory requirements. Category 1 includes investment products such as equity securities and KiwiSaver funds.

Category 2 includes products that have been assessed as being lower risk or less complex (such as most insurance products, credit contracts and many savings products) and are therefore subject to lower regulatory requirements.

4	Is the distinction in the FA Act between wholesale and retail clients appropriate and effective? If not, what changes should be considered? The distinction is inappropriate as I understand Mum & Dad with a family trust is deemed to be a wholesale client which sets the bar too low for 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? Please refer to the opening notes on structure. Personalised service should be where there is a 'face-to-face' discussion that ends to the acquisition or disposal of a financial product. The 'face-to-face' could be by electronic means.
6	Is it appropriate to have different requirements on advisers depending on the risk and complexity of the products they advise upon? No. With the structure proposed, all advisers/sellers would be required to have the prescribed qualifications and be subject to the set of rules appropriate to their area of advice. The existing designation of "higher risk or more complex" and "lower risk or less complex" products is very arbitrary. Is a drip-feed savings that much more complex than a Business Risk Insurance package? Make the distinction between areas of advice and Category 1 & Category 2 debate vanishes
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. See notes above.

Registered Financial Advisers (RFAs)

Becoming an RFA

8	Do you think that the term Registered Financial Adviser 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. Please refer to our recommendation for structure. Then we no longer have Approved and Registered, just "Discipline" Adviser and Product Marketer.

RFA conduct requirements

9	Are the general conduct requirements applying to all financial advisers, including RFAs, appropriate and adequate? If not, what changes should be considered? Yes they are adequate. Our group requires all members' Advice Process to be independently audited at least every 2 years and file checks (randomly selected by the auditor) every alternate year.

RFA disclosure

10	Do you think that disclosing this information is adequate for consumers? Our recommended structure will require ***all*** Advisers to give full disclosure as required currently for AFAs. The current disclosure statement is a joke. It says who they are and who the consumer should contact if they are dissatisfied – as if that's the general outcome of dealing with the adviser. Why can't we have a disclosure document that allows an adviser to list their experience etc? Should RFAs be required to disclose any additional information? While disclosure of commissions on investment products can have a direct bearing on the

	returns the consumer gets, how does the disclosure of *actual* levels of commission on risk products benefit the consumer? In our opinion, it should be sufficient to disclose *how* the adviser will be remunerated (fee, commission, both, fee but rebated if commission paid etc.).

RFA Entities

Businesses, rather than individuals, that register to provide financial adviser services are only permitted to provide class advice. This allows entities to take sole liability for published class advice (on a website, for example) and allows the entity's employees to provide class advice directly to clients. At present around 900 entities are registered to provide financial advice.

11	Are there any particular issues with the regulation of RFA entities that we should consider? Our recommended structure covers this

Authorised Financial Advisers (AFAs)

Authorisation

All AFAs must have and keep up to date an adviser business statement (ABS). These statements are written documents that set out what type of adviser business they provide, and what compliance arrangements they have in place. They also explain the systems and procedures the adviser has in place to ensure he or she conducts business professionally.

12	Are the costs of maintaining an adviser business statement justified by its benefits? If not, what changes should be considered? In our opinion, the cost of maintaining an ABS is not significant. We believe this document should be available from the Financial Service Providers register as per our opening comments

Investment planning services

An **investment planning service** (IPS) is defined as the design of a plan for an individual based on an analysis of their current and future overall financial situation, and identification of their investment goals, including a recommendation or opinion on how to realise them. Only AFAs can provide IPS to retail clients, regardless of whether it relates to category 1 or category 2 products. While IPS is a separate authorisation, there are no additional authorisation requirements for this service. As at April 2015, 1,490 advisers had IPS as part of their authorisation scope, but not all are believed to actually provide this service. In June 2014, the AFA return facilitated by FMA revealed that of the 1,490 AFAs who were authorised to provide an IPS, only 835 indicated they were offering this service.

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? Obviously the distinction isn't well understood as we don't see how you can give true financial advice in relation to investments *without* doing an IPS??

Discretionary investment management services

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?
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?

AFA disclosure

AFAs are required to provide two disclosure statements to their clients before providing them with personalised advice, investment planning services or personalised DIMS. The first, known as the primary disclosure statement, is intended to be a relatively short description of the adviser's business which allows prospective clients to compare advisers. It is a largely prescribed document that outlines:

a) The adviser's contact details

b) The services they offer

c) A general description of how they are paid

d) Their disciplinary history (if any)

e) Their complaint procedure.

AFAs are also required to provide one or more secondary disclosure statements that describe the specific nature of the service that the adviser will provide to the client, what it will cost and how the adviser will be paid. This includes detail of any commission that the adviser will receive and any other conflicts of interest. Because this information could vary significantly between advisers there is no set format for secondary disclosures.

16	Are the current disclosure requirements for AFAs adequate and useful for consumers? While they might be adequate, they should be redesigned by a team of advisers and compliance specialists to provide greater clarity for consumers.
17	Should any changes be considered to improve the relevance of these documents to consumers and to reduce the costs of producing them? For relevance, see our comments in 16. Above. Costs are only in maintaining them and printing (if a hard copy is given) which, we believe, is not onerous

Code of Professional Conduct

18	Do you think that the process for the development and approval of the Code of Professional Conduct works well? Seems to??
19	Should any changes to the role or composition of the Code Committee be considered? Should be at least one 'real life' adviser for each "discipline' on the committee. Note that one person could cover a number of disciplines
20	Is the Financial Advisers Disciplinary Committee an effective mechanism to discipline misconduct against AFAs?
21	Should the jurisdiction of this Committee be expanded? **Must** cover all Advisers and Product Marketers as per the terminology used in our opening comments about recommended structure

Qualifying Financial Entities

QFE Conduct Obligations

The bulk of a QFE's obligations are set through the conditions that the FMA places on its approval. The standard conditions that apply to all QFEs are available on the FMA's website and include capacity, reporting and disclosure requirements. These standard conditions require the QFE to ensure that its governance and compliance arrangements and procedures meet the commitments made in the QFE's ABS. Given that a QFE's ABS contains commercially sensitive information the details of these obligations are not publicly available.

22	Does the limited public transparency around the obligations of QFEs undermine public confidence and understanding of this part of the regulatory regime? Probably doesn't

	undermine public confidence but must undermine public understanding. Any time there is a lack of transparency, the public will tend to think the worst.
23	Should any changes be considered to promote transparency of QFE obligations? Under our recommended structure, the term QFE will not exist. However, the body who 'controls' the product marketer **must** be subject to strict penalties when one of their marketers acts contrary to their mandate. When it is found that staff of a QFE breach standards other advisers are required to comply with, for example "Would you like to be able to see your KiwiSaver balances on-line along with your other accounts? Sign here." Then transferring the consumer to their default fund, their 'licence' to operate in that area of 'advice', in this case KiwiSaver, QFE should be either suspended until they are able to demonstrate to the FMA that they have retrained staff or, at least, be given a limited timeframe to retrain pending suspension. The best way to promote confidence would be to make a very public example the first time such an event is detected.

QFE Disclosure

24	Are the current disclosure requirements for QFE advisers adequate and useful for consumers? No. Interesting that AFAs working within a QFE are not required to disclose commission terms in relation to category 2 products whereas AFAs outside a QFE do??
25	Should any changes be considered to improve the relevance of these documents to consumers or to reduce the costs of producing them? The documents must make it very clear that the person is a Product Marketer, dealing only with products from (list of companies) and therefore not comprehensive advice. They should also be required to state that any product they recommend may not be as good as product they may already have or be available elsewhere in the market,

Brokers and Custodians

No Comments

FA Act exemptions

32	Is the scope of the FA Act exemptions appropriate? What changes should be considered and why? Absolutely not appropriate. All persons providing "financial advice" must be bound by the legislation. Two prime examples of exemptions that are wrong are accountants and real estate sales people dealing in rental property. Accountants are often the most trusted professional adviser a person has, especially if that person is a small business owner. Advisers can quote examples of where the accountant personally believes in either minimum or nil personal insurance and 'advises' their client against taking up the recommendations of the adviser. Surely this is contrary to the intention of the legislation. Again that level playing field.

Monitoring and enforcement of the FA Act

33	Does the FA Act provide the FMA with appropriate enforcement powers? If not, what changes should be considered? Yes
34	How accessible and useful is the guidance issued by the FMA? Are there any improvements you would like to see?

Key FA Act questions for the review

These are discussed at the start of this paper.
The specific questions will be listed for completeness but will be commented on only if further comments are warranted.

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

Do consumers understand the regulatory framework?

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 initial comments

Should there be a clearer distinction between advice and sales?

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? Consumers probably don't understand the difference very well – hence the suggestion that the distinction be eliminated.
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 previous comments

How should we regulate commissions and other conflicts of interest?

Comment (other than earlier comments on commission)
Fire & General Advisers receive a commission from the insurance companies they place business with but there doesn't seem to be a perception of conflict of interest nor of being less trustworthy. This might be because commission is pretty standard and is a level % every year.

Eliminating up-front commissions and volume-based bonuses to individual advisers could go a long way to overcome the negative perception but a significant number of current advisers would probably no longer have a viable business and it would certainly restrict the number of new advisers who could enter the profession.

Perhaps one step could be to eliminate up-front commission on business that is transferred from one insurer to another but this could also potentially have unseen –ve consequences.

Box 3: Churn
"Churn" is the practice of advisers persuading clients to move from one financial product to another for the purpose of receiving a high up-front commission. The FMA has identified churn in relation to some types of insurance and KiwiSaver as a key strategic risk.
Switching insurance policies, for example, can be a positive indication of a competitive market and can be driven by consumer expectations rather than by advisers. However, it is important that advisers ensure that the new policy meets the client's needs and that the client understands any differences in policy coverage. Similarly, it is important that there is a strong competitive dynamic in the KiwiSaver market, but incomplete or inaccurate advice motivated by upfront commissions has the potential to cause significant harm to investor outcomes.

Does information disclosure solve conflicts of interest?

Unfortunately Insurance Companies are very bad at not distinguishing between churned business as defined above and genuine replacement business based on client needs.
In our opinion, real churn is;

- restricted to a limited number of advisers
- generally known of by insurance companies
- either actively or discretely promoted by a limited number of insurance companies, some offering special terms on transfer of books of business
- also, see comments recently on the subject in Good Returns article "Churn debate: AMP surprised click here,

38	Do you think that current AFA disclosure requirements are effective in overcoming problems associated with commissions and other conflicts of interest? Yes but…. document must be consumer-friendly or it will be brushed over. See Issue Paper's own comment that disclosures are seldom read by consumers.
39	How do you think that AFA information disclosure requirements could be improved to better assist consumer decision making? As above

Should all advisers be required to disclose potential conflicts?

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 – the same rules must apply for all. In our terminology, Product Marketers must also be required to provide this information, including targets they are required to meet or levels at which they are rewarded By delineating advisers by area of business (investment, life insurance, etc.) means the disclosures could be different for the different areas of advice. For example, it might be appropriate for Licenced/Registered Life Insurance Advisers to declare they will receive a commission (if that's how they operate) and only disclose how much if it is in excess of the industry standard. Likewise they *must* be required to declare what level of business must be placed with any particular insurer. This refers to 'aligned' advisers, advisers within a company etc.

Should commissions be banned or restricted?

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? 2 distinct areas for discussion; <u>Investment</u> A strong case could be made for banning commission or creating standardised commission terms for classes of investment. Note that I am unaware of any true churn concerns over investment products. The instances referred to in relation to the GFC could well have been influenced by the commission levels but what % of investment in these areas on the advice of financial advisers, what directly influenced by 'recommendation' by a well-known figure and what % by direct advertising of high returns? <u>Life Insurance, F&G Insurance, Mortgage "Broking"</u> The industry needs to retain the current bases of commission payments for the adviser base to not be decimated. However, a partial solution might be a mix of; • Legislated maximum up-front commissions • No up-front commission on replaced business – though how you police this is questionable since it relies on the adviser's/client's honesty on whether the business replaces another contract. However, reviews like the one currently being undertaken by the FMA should be able to highlight this and, where found, there should be severe penalties for the "adviser" concerned. • Requiring insurance companies to only accept business with a full application and fully underwritten. • Requiring insurance companies to inform the FMA whenever they suspect churning

Goal 2: Financial advice is accessible for consumers

Does the FA Act unduly restrict access to financial advice?

Level of competition in the market for financial 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)? No. The artificial split between AFAs and RFAs and the existence of QFEs means that, overall, the quality standards need improvement. Also, the GFC has meant that many advisers who have the current designation of AFA, are reluctant to give advice in investments
43	What changes could be made to increase the levels of competition between advisers? We think the concept of competition is misleading. Are we looking for cut-rate deals? Surely the idealistic goal should be to do everything possible to align the consumer with the adviser that's best for them. This means a total re-jig of the FSPR to allow a consumer to be able to select by location and by areas of advice required. For example, you need to be able to enter Licenced Investment Adviser, Wellington and be provided with a list of all advisers on the Register who fit these criteria. As stated before, there also needs to be more pertinent detail on the register such as other qualifications, time in the profession, website link etc.

Regulatory constraints on advice and boundary issues

"Confusion about how the regulatory regime works may also be artificially preventing consumers from accessing the best type of advice for their circumstances. For instance, restrictions on the products RFAs and QFEs can advise on necessarily lead to their recommending the purchase of financial products that they are permitted to provide advice on. However, regulatory complexity may mean consumers interpret these as a recommendation on the best overall product for them, rather than the best product the adviser is permitted to give a recommendation about. In these situations it may be more appropriate for the consumer to seek the advice of an AFA, but poor understanding about the distinctions between advisers may stop this from happening."

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? In general we believe it does
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? We believe the current categorisation makes it extremely difficult for a consumer to know when they can expect 'advice' and when just a promotion for a sale of product. Our recommended structure would, if not eliminate, at least lessen the opportunity for confusion.

How can compliance costs be reduced under the current regime without limiting access to quality financial advice?

46	Are there specific compliance requirements from the FA Act regulation that have affected the cost and availability of independent financial advice? We believe there is a lack of understanding of just what a client report needs to contain resulting in over-long reports being delivered which are too involved for most clients to digest. This not only results in a cost in terms of time but also in printing and storage.
47	How can regulatory requirements be made less onerous without reducing the quality and availability of financial advice? A more pragmatic approach as to when the requirements are needed
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? Our members believe the application of this Act to basic KiwiSaver is unwarranted, especially

	when the client can open one at the bank or go into a default scheme at work without the paperwork required from an AFA

How can we facilitate access to advice in the future?

KiwiSaver withdrawals

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?

Introduction of the Financial Markets Conduct Act

50	What impact do you expect that the introduction of the 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?

Internationalisation

51	Do you think that international financial advice is likely to increase? Is the FA Act set up appropriately to facilitate and regulate this?
52	How beneficial are the current arrangements for trans-Tasman mutual recognition of qualifications? Should further arrangements be considered?

Opportunities and challenges of technological change

53	In what ways do you expect new technologies will change the market for financial advice?
54	How can government keep pace with technological developments to ensure that quality standards for advice are maintained, without inhibiting innovation?

Goal 3: Public confidence in the professionalism of financial advisers is promoted

Should we lift the professional, ethical and education standards for financial advisers?

Please refer to our opening recommendations on structure; i.e. the concept of removing the AFA and RFA designations and replacing them with Licenced Investment Adviser, Licenced Life Insurance Adviser etc would mean that ***all*** advisers could/should be brought under the same ethical and education standards **appropriate to their area of advice.**

Ethical requirements

55	Are the minimum ethical standards for AFAs appropriate and have they succeeded in fostering the ethical behaviour of AFAs? Has probably made the adviser maintain better documented records of discussions and advise. With investment and the transparency on commissions it *might* gave removed some "cowboys"
56	Should the same or similar ethical standards apply to all types of financial advisers? See our opening comments on Structure.

Qualification requirements

Relevant points from the Issue Paper:

"We have heard that the minimum qualification requirements have made some progress in creating a more professional advice market for AFAs. Many stakeholders have argued that similar, if not the same, requirements should apply to all financial advisers, including RFAs."

Firstly, we believe it is a flawed concept to believe that qualification implies professionalism.

Qualification is about acquiring knowledge, professionalism is about behaviour.

We don't necessarily agree that it has created a "more professional advice market". Most people I have talked to felt the cost in dollars and time to get the required standard was a waste as they learnt little or nothing in the process.

We have, however, heard from a number of stakeholders that the current minimum qualification for AFAs is broadly inadequate for investment advice and that it should be increased, for example to a Level 7 qualification such as a Graduate Diploma. The Code Committee has previously noted that it considers it likely that these minimum standards would be raised in the future. Others within the industry have expressed concern that many aspects of the qualifications regime are not fit for purpose."

Please refer to our comments at beginning regarding classification and qualification

57	What is an appropriate minimum qualification level for AFAs? Please see our opening comments which includes details on possible qualification standards for each area of advice. For investment advice, we believe it could depend on the specific area of investment advice. For mum & dad who want to drip-feed for late spending, be it retirement or other, there possibly doesn't need to be a very high level of qualification. If the bar is set too high then who will give KiwiSaver clients advice – especially if commissions were removed? Probably would be hard to get advisers involved in this and these will just be picked off by the banks into their default funds which isn't in the client's best interest and goes against the intent of the legislation. However, more complex situations could easily require a higher level of skill/qualification. How do you legislate that?

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? See notes on adviser classification & qualification at the beginning.
59	How much consideration should be given to aligning adviser qualifications with those applying in other countries, particularly Australia? Why align with Oz? We were smart enough not to follow them on the current legislation, making ours not nearly as draconian and, I would argue, we have had a far better outcome than they have had. Perhaps it is time we stopped considering ourselves the younger sibling and decide on what is righty for us, then asking Oz to copy us.

The role of professional bodies

60	How effective have professional bodies been at fostering professionalism among advisers? In my experience, very little. Also, with the FA Act etc, many advisers couldn't see any relevance in belonging to a professional body with yet another layer of expense and have cancelled their membership.
61	Do you think that professional bodies should play a formal role in the regulation of financial advisers and if so, how? They could but, unless you had one body for each area of advice, how would you ensure they had comparable standards etc? The +ve side would be there would be a far better understanding of the situation from an adviser perspective so any "rules" would likely produce a better result.

Should the individual adviser or the business hold obligations?

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? See our opening notes; individuals to hold obligation but, if part of a company (read QFE) then any breach by the individual results in "suspension" of QFE for the area of advice (or given limited time to retrain etc)
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? Most definitely not. Anecdotally some of the ***worst*** behaviour comes from within QFEs (rolling KiwiSaver, replacing good financial products with not so good etc.) and I am sure consumers don't appreciate they are being sold down the river. Individual areas of advice and relevant qualifications for each with no separation of "sale" and "advice" should go a long way to resolving this.

Part 3 – The Financial Service Providers (Registration and Dispute Resolution) Act 2008

Role of financial service provider registration and dispute resolution

Why do we have a financial service provider registration regime?

Before the introduction of the FSP Act in 2010, there was no comprehensive way to identify or monitor financial service providers, which caused issues for policy makers, regulators and consumers. In particular:

a) Policymakers could not identify the number of people who could be affected by any regulatory actions being contemplated.

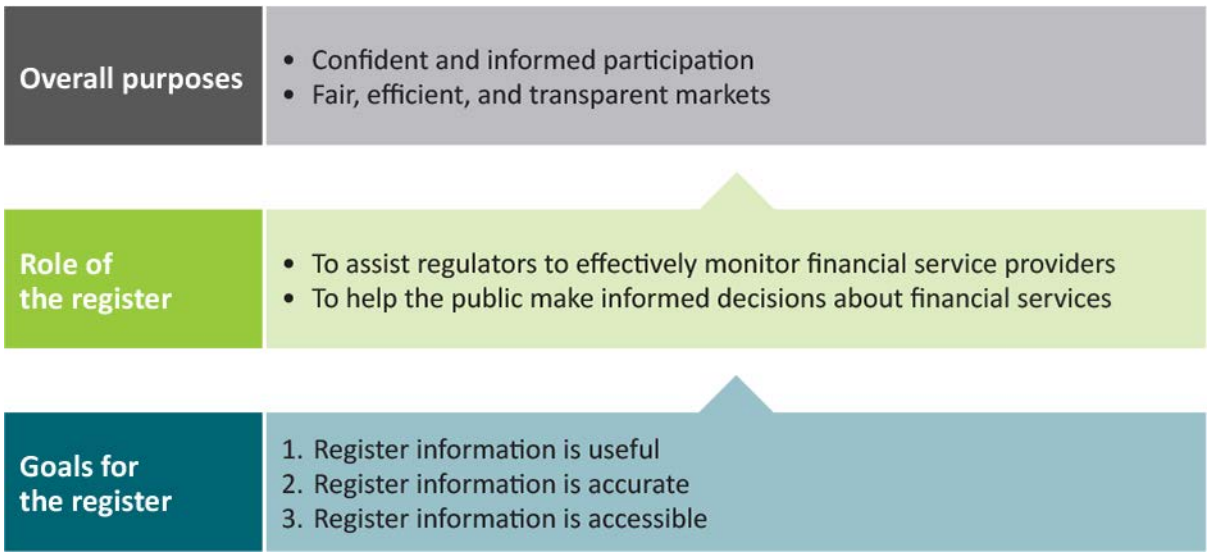
b) Regulators found it difficult to identify the regulated population.

c) No public record existed of who was permitted to provide certain types of financial services, potentially giving rise to public confusion and uncertainty.

The Register was introduced to address these issues. It also satisfies New Zealand's obligations under the FATF Recommendations by allowing AML-CFT supervisors to identify financial institutions with obligations under the AML-CFT Act.

Goals for an effective registration system

We have developed the following draft framework for assessing the effectiveness of the financial service provider registration regime. This framework is based on the original policy intent for and statutory purposes of the Register. It identifies three goals for the Register which, if met, will mean it is fulfilling its intended role and in turn contributing to Government's broader policy objectives for financial markets:



1: Register information is useful

Not very useful for the public;

- Is Jo Bloggs even aware of it?
- Can only use it to check if the name of the 'service provider' is known.
- Insufficient relevant information to compare individual 'service providers'.

2: Register information is accurate

3: Register information is accessible

64	Do you agree that the Register should seek to achieve the identified goals? If not, why not? Yes
65	What goals do you consider should be more or less important in reviewing the operation of the Register? They are all equally important

Framework for an effective dispute resolution regime

We have developed the following draft framework for how dispute resolution can contribute to the Government's broader financial markets goals. This framework is based on the original policy intent and statutory purposes of dispute resolution in the FSP Act. It also takes into account the following internationally accepted principles of effective dispute resolution:

a) Accessibility

b) Independence

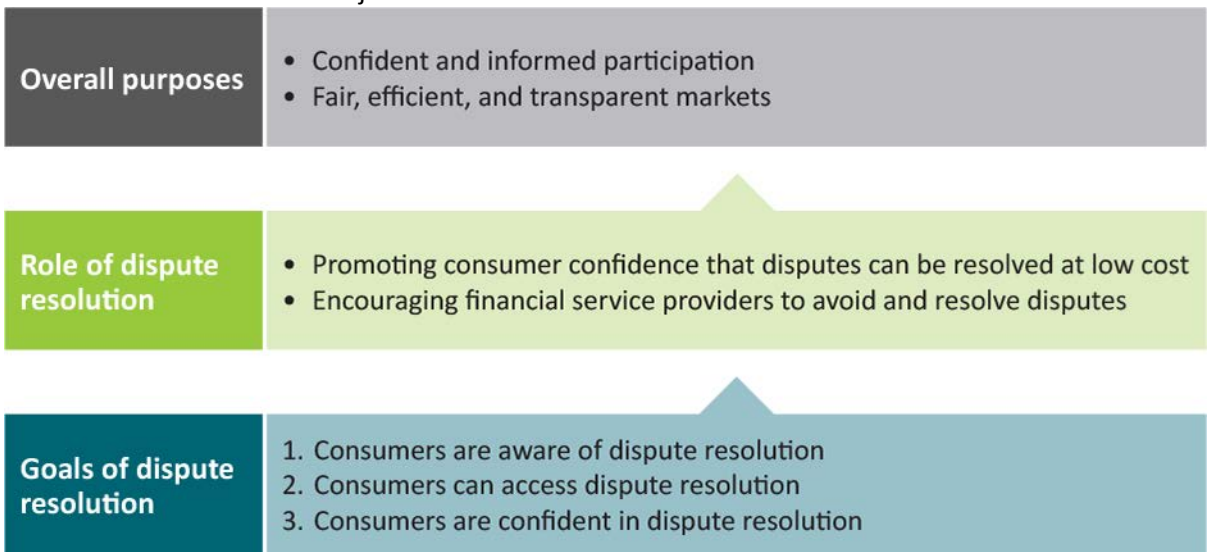
c) Fairness

d) Accountability

e) Efficiency

f) Effectiveness

The draft framework identifies three goals for dispute resolution, which if achieved will contribute to the Government's broader objectives for financial markets.



1: Consumers are aware of dispute resolution

Possibly not aware of it if they haven't used the services of a 'financial adviser'

There seems to have been very little education of the public which, I thought, was one of the major goals of the FMA.

There would need to be an ongoing campaign to educate the public on

- Our recommended structure with new designations & what they mean

- The required level of qualifications required for each area of advice
- The required ethical standards required
- The system that is available to consumers to resolve any issues

2: Consumers can access dispute resolution

Well obviously. Would be pretty stupid if they couldn't access it!

This goal needs to read "Consumers can ***readily*** access dispute resolution"

3: Consumers are confident in dispute resolution

It is vital for the consumer to have total confidence in the dispute resolution system.

Even if it goes against them they must feel they have been treated fairly.

66	Do you agree that the dispute resolution regime should seek to achieve the identified goals? If not, why not? Yes – with the exception of the wording of goal 2
67	What goals do you consider should be more or less important in reviewing the dispute resolution regime? All are equally important

How the FSP Act works

Registration

From the FSP Act

> Every person who knowingly breaches subsection (1) commits an offence and is liable on conviction,—
>
> (a) in the case of an individual, to imprisonment for a term not exceeding 12 months or to a fine not exceeding $100,000, or to both; or
>
> (b) in the case of a person who is not an individual, to a fine not exceeding $300,000.

68	Does the FMA need any other tools to encourage compliance with FSP registration? If so, what tools would be appropriate? Above should be sufficient
69	What changes, if any, to the minimum registration requirements should be considered?

Dispute resolution

70	Does the requirement to belong to a dispute resolution scheme apply to the right types of financial service providers? I think so – provided we do away with the distinction between sales and advice and place primary obligation with the adviser
71	Is the current framework for the approval of dispute resolution schemes appropriate? What changes, if any, should be considered?
72	Is the current framework for monitoring dispute resolution schemes adequate? What changes, if any, should be considered? It would appear so
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? Might be appropriate to have different maximum levels for each area of advice

75	Should additional requirements to ensure that financial service providers are able to pay compensation to consumers be considered in New Zealand? I don't believe so **BUT** surely, in the interest of fairness, an adviser should be able to appeal a scheme's order

Key FSP Act questions for the review

Goals for the Register: The Register information is useful, accurate and accessible

Could the Register be used to provide better information to the public?

76	What features or information would make the Register more useful for consumers? Searchable on; • Location • Area of advice (Investment Life Insurance, General Insurance, Mortgage Broking…) Information • As below - qualifications & disciplinary record (if none than clearly state NONE) • History of service in the industry/profession including positions held • Disclosure statement (in new format which allows more information about the adviser • Website address
77	Would it be appropriate for the Register to include information on a financial adviser's qualifications or their disciplinary record? Yes

How can we avoid misuse of the Register by overseas financial service providers?

78	Do you consider misuse of the Register by offshore financial service providers is a significant risk to New Zealand's reputation as a well-regulated jurisdiction and/or to New Zealand businesses? What is significant? If it causes the New Zealand consumer to lose trust in the register – especially when it revamped so it is useful – then such misuse would, in my opinion, be "significant".
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? As they have to belong to a Complaints Scheme, then there are 2 separate entities checking (or should be checking) on the 'residential' status of the applicant. Having said that, people who set out to deceive can usually invent ways around.

Goals for dispute resolution: Consumers are aware of, confident in, and can access dispute resolution

What is the impact of having multiple dispute resolution schemes?

80	What are the effects of (positive and negative) competition between dispute resolution schemes on effective dispute resolution? We have no 1st-hand knowledge of this – probably best left to companies such as IDSL & Strategi to answer form their experience. My one concern is the perception that a consumer might get different results from different schemes. There need to be 'rules' developed (either legislated or by round table discussion & agreement between the schemes) to ensure this doesn't occur. I believe the Banking Ombudsman should cover solely bank issues and duties relating to 'financial adviser' left to one of the other schemes.

81	Are there ways to mitigate the issues identified without losing the benefits of a multiple scheme structure? See above
82	Are the current regulatory settings adequate in raising awareness of available dispute resolution options? How could awareness be improved? See thoughts on improving the FSP Register and FMA embarking on a campaign to educate consumers.

Demographics

*83. Please provide your name and/or the name of the group of people, business, or organisation you are providing this submission on behalf of:

Planet Financial Services Limited

*84. Please provide your contact details:

[redacted]

85. Are you providing this submission:

☐ On behalf of an organisation

Please describe the nature and size of the organisation:

Planet is an organisation which provides support and services to its members who are either AFAs or RFAs

86. If submitting on behalf of an organisation:
How many people are in the organisation, or work in the organisation, that you are providing this submission on behalf of?

20-49