#7

COMPLETE

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PAGE 2: Chapter 3 - Barriers to achieving the outcomes

Q1: 1. Do you agree with the barriers outlined in the Options Paper? If not, why not?

Respondent skipped this question

Q2: 2. Is there evidence of other major barriers not captured in the Options Paper? If so, please explain.

Other barriers include: (1) banks/financial institutions acting in their own interests; (2) there not being a full disclosure of commissions/fees; (3) consumers being limited to 1 Kiwisaver provider (every investment book talks about diversification – and so there should be diversification between fund managers (and not just the funds that they operate as the different funds generally invest in the same underlying investments, just in different proportions) (4) consumers may not be receiving investment advice from people with skin in the game (ie their "financial advisers" are recommending funds (because that is their job) yet, they personally have their money in residential real estate.

PAGE 3: Chapter 4 - Discrete elements

Q3: 3. Which options will be most effective in achieving the desired outcomes and why?

Option 1 is most effective. Use Option 1, and use more meaningful terminolgy (maybe "salesperson", but definetly not "expert"). Add a competency element (such as a test), which doubles as a licence. Depending what you do with the FSP, maybe include licencing – and then a public list of licenced providers. Option 1 should also include a fiduciary standard mandating that the financial adviser act in the best interests of the client. This should also address the "competency" change to options 2 and 3. If the financial adviser must adhere to a fiduciary standard, then as part of that standard the adviser can only advise on the matters that they are competent to advise on. This is different to what is in your summary – that states that an adviser must provide the service that matches the consumer's request. This needs to be changed to be "must provide the service that matches the consumer's request so long as the adviser is competent in that area, and if not, must refer the consumer to another adviser who is". Requiring a fiduciary standard should also help remove the distinction between class and personalised advice – because depending on the nature of the client, and the relevant circumstances, the adviser can make a judgement call on the type of information that they require to advise the client. Without a fiduciary standard, you are essentially passing retail investors into class products on a suitability standard, which does not necessarily take the client's best interests into account.

Q4: 4. What would the costs and benefits be of the various options for different participants (consumers, financial advisers, businesses)?

Respondent skipped this question

Q5: 5. Are there any other viable options? If so, please provide details.

Have you looked at the registration/licencing and competency test regimes in Singapore and Hong Kong?

Q6: 6. What implications would removing the distinction between class and personalised advice have on access to advice?

Respondent skipped this question

Q7: 7. Should high-risk services be restricted to certain advisers? Why or why not?

Yes, high risk services should be restricted to certain skilled advisers. There is clearly a difference between: (a) a person in a bank selling a term deposit or car insurance; and (b) a person operating a fully mandated DIMS.

Accordingly, there should be a separation, or a restriction on who can provide what services. In terms of concerns over whether there is an "advice gap", this is one area, where it should be left to the market to balance out the number of advisers. If there are not enough people providing the financial service, then clearly there is an incentive for another person to enter the market to provide that service. If there are not enough people providing the service, you don't improve outcomes for comsumers by letting less qualified people provide that advice. You would be better off proactively pushing the industry. For example, you (as the Ministry of Business, Innovation and Employment) could publish the numbers of financial advisers and assist independent advisers to sell their services. This would show whether there was room for more people to train to enter the market. Of upmost concern is that you must ensure that you do not create a system where financial advice is only provided by banks and large financial institutions. There are plenty of examples in New Zealand and overseas where such institutions act in their own interest. These include credit rate swaps, high credit card fees, selling CDOs, and distribution of mortgages.

Q8: **8. Would requiring a client to 'opt-in' to being a wholesale investor have negative implications on advisers? If so, how could this be mitigated?**

No. Having an "opt-in" to being a wholesale investor should not have a negative implication on advisers. In fact, havng an opt-in to being a wholesale client is actually benefical to investors that do not qualify as wholesale. Currently, an adviser needs to go through a process to identify whether the client is wholesale or retail before onboarding them. That general onbaording process would not change. Rather, the specifics would change. An investor would instead need to "opt-in" to being treated as wholesale. The current process, generally, is that the investor ticks a box of the wholesale category that they fit into (and, maybe, the adviser takes reasonable steps to confirm that selection). At present, certain advisers only have wholesale clients. This is a busissness decision as it reduces regulatory costs. Generally speaking, the primary reason that a wholesale client is with a particular adviser is because they trust that adviser. From my experience in the industry, investors do not frequently change between wholesale advisers if the adviser is performing. Some investors, including myself and friends, would prefer to put money with the successful advisers that the rich people use – IE the advisers that only have wholesale clients. I can't currently do that because I don't qualify as a wholesale client. Being able to opt-in to wholesale status means that I can access a broader range of investment advisers. Why should some good advisers only be limited to rich people? Why can't I access a good adviser to improve my chances of increasing my funds so I can afford a house? Why do I need to be classed with average person who doesn't understand economics? Most wholesale only advisers have robust systems in place anyway. For example, they tend to use a respected custodian, outsource administration to a specialist, have regular reporting, and annual audits. A wholesale adviser can also voluntarily join a disputes resoution regime (albiet there is the 200K cap). Smart retail investors would not "opt-in" to a wholesale adviser who didn't have robust systems in place. If a wholesale investor invested into a Ross Asset Management, without an audit system in place then that is a stupid decision and they must bear that risk. The majority of retail investors that are not willing to accept the risks (of electing to be wholesale) can stick with the retail providers. You can easily manage the risks of rouge financial advisers getting their retail clients to opt-into wholesale categorisation by prescribing a disclosure that the adviser is not subject to a regulatory regime (or is subject to a minimal one) and advising that other advisers are (subject to a regulatory regime). A reference to the FSP/FMA list of "licenced" or other retail advisers could also be required to be provided. It is then open to the investor to choose that adviser, or chose another one that is subject to the regulatory regime. Whether this process is followed can easily be checked as part of the adviser's AML audit. If you had this opt-in mechanism, you could also require a retail person to seek (or have the opportunity to seek) independent legal advice. This is process that one takes when making other significant financial advice (like providing a guarantee on a mortgage). In any event, I suspect that this would only result in a few wholesale advisers accepting a few retail clients, rather than a large recruiting drive for retail clients. This is because the small advisers have scalablity issues and ususally minimum investment requirements – this is because they run DIMS and don't want to incur disproporationate amount of trading fees in respect of smaller investors. However, having this option would still be beneficial to consumers and to advisers. For example, this is helpful to advisers because currently they are limited as to who they can provide services to. Say for example they only deal with large investors who hold over $5million in assets, but they get approaches from people with only $4million. If there was an "opt-in" then those $4million people can invest with that same adviser. There would be no change to retail focused providers that also offer their services to wholesale. For such wholesale consumers can elect to be retail anyway under the current model. Many retail advisers also treat their wholesale clients as retail for admin and reporting purposes as it is easier administratively for them. While there might not be an easy complusoty disputes mechanism available to a retail investor who uses a wholesale adviser, the retail investor that opts into wholesale would have normal contractual or negligence remedies available – and that is one of the risks that they will knowingly take on by going with a wholesale only adviser. Having an "opt-in" to wholesale would help address the barriers to entry that new providers have, and help prevent the increasing power of the big banks and institutions. To establish an economicial new fund or retail DIMS one essentially needs to get to $10million FUM within a year to start with to break even, and then a minimum of $20million to make a good salary. To target retail clients one needs a distribution network and a supervisor (the numbers of which are decreasing and not taking on new clients unless there is a minimum FUM or guaranteed fee). So, the current system essentially limits retail fund and DIMS offerings to those provided by banks and large financial institutions or others with cash backers. Most financial advisers are aligned to QFEs and so, with a reduction in independent advisers, there is also a reduction in independent funds/DIMS as well. Allowing retail investors to opt out of the FAA would help to

address this uneven playing field and allow boutique providers more of an opportunity to compete with the larger entities if they chose to. Being able to opt in to being treated as a wholesale investor should be a choice available to every investor.

Q9: **9. What ethical and other entry requirements should apply to advice platforms?**

The same ethical obligations should apply to all service providers. Whether that is an individual or an entity providing the service. The obligations on entities can be placed on directors (or equivalent).

Q10: **10. How, if at all, should requirements differ between traditional and online financial advice?**

If making rabo-providers licenced, why not make those that provide a similar service (ie current AFAs) also licensed and call them licensed rather that authorised? That way there is consistency in terminology and obligations.

Q11: **11. Are the options suggested in this chapter sufficient to enable innovation in the adviser industry? What other changes might need to be made?**

In terms of other changes, there should be changes to the KiwiSaver Act to allow kiwisaver funds to be invested with more than 1 provider.

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Q12: **12. If the ethical obligation to put the consumers' interests first was extended, what would the right obligation be? How could this be monitored and enforced?**

The right obligation is the fiduciary standard that the US Department of Labour is trying to get passed in the US Congress. Here are 3 short videos on Youtube which explain why a fiduciary standard is necessary – you'll also note that committing to a fiduciary standard can help clarify the problematic distinction between personal and class advice that currently exisits: https://www.youtube.com/watch?v=6YfWDXQdYVw https://www.youtube.com/watch?v=PQQzzLauAdA https://www.youtube.com/watch?v=LxOYO F5JJ4 Why shouldn't someone who is getting paid by a customer (either directly, or their employer is) be required to always provide that service in the best interest of the customer? And why wouldn't a fiducuary standard be mandatory? Is it because the QFEs don't want that standard? This can be enforced through random audit of files in a similar way to an AML audit. I would assume that many customers who go and see an adviser (including QFE advisers) assume that that person is giving them recommendations that are in the customers best interest. I find it odd that the Product Disclosure Statement is required to be written in clear simple English, but then customers are left to determine for themselves whether or not they want to proceed with getting advice from a person who is not required to act in their best interest. One would assume that a financial institution would act in the best interests of the customer in terms of reputational risk considerations. However, if one can legally not act in the best interest of the customer and not need to comply with a fiduciary standard then you are essentially giving the large financial institutions a legal defence to actions of wayward staff chasing targets and incentive bonuses. Indeed, if the adviser is not acting in the customer's best interests, that customer is wasting their time going to see the adviser. Imgaine an ordinary NZ worker who wants to improve their financial situation. They spend their nights looking online to find their local advisers. They consider the options, take an afternoon off work to go and see them – and then, in a meeting, be told (or not told) "sorry I am selling you a product, I am acting in the best interests of my employer/QFE and what I sell to you today may not be appropriate for your needs, but please buy anyways because it helps me meet my sales target." Remember the amount of money that was invested in finance companies and that was lost. A lot of that money was invested in finance companies paying large commissions. The advisers were clearly not acting in the best interests of the clients. Having a legal fiduciary obligation to act in the best interest of the client makes it easier for the client to succeed in a complaint, rather than relying on negligence or breach of contract. In addition, it would also be helpful to place an obligation that is similar to obligations (with regard to investments) automatically imposed on trustees by the Trustee Act. There should be an automatic obligation to exercise the care, diligence, and skill that a prudent financial adviser would exercise in the same circumstances.

Q13: **13. What would be some practical ways of distinguishing 'sales' and 'advice'? What obligations should salespeople have?**

Salespeople should have the same obligations as advisers as both are essentially selling a product. They should also be required to meet a fiduciary standard.

Q14: **14. If there was a ban or restriction on conflicted remuneration who and what should it cover?**

I don't think that there should be a ban or restriction on conflicted remuneration. That would be a total death to "independent" advisers and further consolidation of the provision of financial services to retail clients by an oligarchy of banks and financial institutions. A good compromise would be to take the Swiss approach. In Switzerland, an adviser or financial intermediary is only permitted to accept a commission or trail fee (generally

referred to as a retrocession) where the amount of the retrocession is clearly and expressly disclosed, and the client accepts that the adviser/financial intermediary can accept that commission. The focus is on disclosing the amount (or percentage), and not the fact that there “may” be a commission. This way an adviser that has a range of options for the client, can show the client how much they receive for suggesting a certain product – and what they receive for others. The client is then on notice before accepting the product/recommendation of the amount that the adviser will be paid and can ask the adviser to justify why the recommended product is better than the others. If commissions are banned, this would just lead more consumers to the banks and big financial institutions. If you had $10,000 to invest, why would you pay an independent adviser $2,000 for a plan? You’ve just lost 20% of your capital. Having the adviser derive a small percentage as a trail fee on an on-going basis seems a better compromise. In any event, a trail fee is not usually an additianal cost. It is usually part of the management fee. If commissions were removed – what is the chance that the banks/financial instituion will reduce the management fee? I suspect unlikely. Kiwisaver fees haven’t decreased despite the economies of scale that the banks now have. A ban on commissions would likely also be a futher barrier for millenials investing with an independent adviser, as opposed to baby-boomers that are already established with healthy net worth.

Q15: 15. How can competency requirements be designed to lift capability, without becoming an undue barrier to entry and continuation in the profession?

You can take the Singaporean approach and have a standard test. If the test is passed (at a certain level) then the person is licenced to provide a certain service. If an adviser is not prepared to take a standard test to demonstrate their competence because they fear that they might fail – do you really want that person being available to offer investment advice? Surely that is a similarly damaging to the integrity of New Zealand’s financial markets (which is a test for de-registation under the FSP Act).

Q16: 16. Should all advisers be subject to minimum entry requirements (Option 1)? What should those requirements include? If not, how should requirements differ for different types of advisers?

There should be minimal entry requirements which are a test. Getting a degree in advising is no sure way of ensuring that a person would be a good adviser.

Q17: 17. What are the benefits and costs of shifting to an entity licensing model whereby the business is accountable for meeting obligations (Option 1)? If some individual advisers are also licensed (Option 2), what specific obligations should these advisers be accountable for?

Respondent skipped this question

Q18: 18. What suggestions do you have for the roles of different industry and regulatory bodies?

Respondent skipped this question

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Q19: 19. What do you think is the most effective way to disclose information to consumers (e.g. written, verbal, online) to help them make more effective decisions?

Written.

Q20: 20. Would a common disclosure document for all advisers work in practice?

It would at least allow consumers to easily compare advisers as the information would be in a consistent form.

Q21: 21. How could remuneration details be disclosed in a way that would be meaningful to consumers yet relatively simple for advisers to produce?

Disclose the amount (or percentage) of commission that is paid. The consumer can then sign their contract with the adviser acknowledging that they are aware of the commission/fee schedule. If the adviser does not disclose (and get the acknowledgement) then they should hold any undisclosed commissions/fees on constructive trust for the client. I have seen wholesale disclosures that disclose the percentage of all fees to investors – ie what brokerage and FX conversion costs, plus commissions from funds. In retail disclosures I have seen “we may be paid” wording. Some AFA’s state that they are paid a salary and a bonus. I don’t care what they are paid by their employer. I want to know specifically what the adviser/firm is taking from me for fees – and I want to know what others are charging so that I can compare providers. I want to know how much of the management fee is actually a trail fee to the adviser. It seems odd that despite the amount of change to the regulatory environment wholesale advisers voluntarily disclose more pertinent information to investors than that which statute requires to be disclosed to retail investors.

Q22: 22. Is there any evidence that the existence of multiple schemes is leading to poor outcomes for consumers?

Is the more relevant question, is there a public set of decisions so that retail investors are confident that there is consistency in decision making?

Q23: 23. Assuming that the multiple scheme model is retained, should there be greater consistency between dispute resolution scheme rules and processes? If so, what particular elements should be consistent?

Yes – the whole point is to allow consumers to have easy redress. However, the providers pick the dispute resolution scheme. So, on the current set up, it is the provider that has the ability to pick the scheme that they may find more friendly to their interests.

Q24: 24. Should professional indemnity insurance apply to all financial service providers?

Yes. All of the "Offshore Financial Centres" including Samoa and the Cook Islands require indemnity insurance as a condition of gaining a licence in those countries.

Q25: 25. What is the best way to get information to consumers? Who is best placed to provide this information (e.g. Government, industry, consumer groups)?

Probably all 3. But if you want to help the industry grow and be more transparent, you should have a government list of providers and list to contact details. This doesn't need to be a register. It just needs to be a list of all (licenced) providers. This can be the same as the FMA lists for licenced providers. That way, when I get cold calls from the US I can check the list to see whether the person is legit, or whether they are just a scam.

Q26: 26. What terminology do you think would be more meaningful to consumers?

Any terminology should be meaningful and consistent with the legislation so that there can be an easy cross-check against the obligations in the Act. It would also be very helpful to more clearly use the terms custodian and broker in the Act. I really don't like the proposed use of "expert" as a statutory term. An expert has a common usuage meaning – that usually incorporates some form of recognition as an expert. By using the term you are effectively giving a statutory declaration that a certain adviser is an expert. There is obviously a lot of scope here for misleading the public. One starts to wonder which clever interest group suggested the use of "expert" as an appropriate term. Why not use something like a Level/Class A (or Category 1) adviser and a Level/Class B (or Category 2) adviser. This at least indicates to consumers that there are 2 levels of advisers and that if they are dealing with a B/2 adviser, there is someone who is more experienced/better qualified that they can talk to. You can have "independent" and "[name of QFE] adviser" or "[name of QFE] employee". If a person is not aligned with 1 particular QFE and fully discloses their commissions they should be able to use the term "independent".

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Q27: 27. Do you have any comments on the proposal to retain the current definitions of 'financial adviser' and 'financial adviser service'?

Respondent skipped this question

Q28: 28. Are those currently exempt from the regime posing undue risk to consumers through the provision of financial advice in the normal course of their business? If possible, please provide evidence.

It just seems odd to allow some people to provide "financial advice" and not go through the same registration, accreditation and disclosure requirements as "financial advisers" merely because they are an accountant or lawyer. (But I guess it depends on what advise they are giving. Tax advice could be regarded as financial advice, but it doesn't necessarily involve a financial product.) But then again, there are lots of odd exemptions in financial services legislation – like their being exemptions for lawyers, accountants, real estate agents and gold storage providers from the AML/CFT Act. Even AML auditors are saying that the easiest way to launder money in NZ is to overpay your legal/accounting fees, buy real estate or buy gold.

Q29: 29. How can the FA Act better facilitate the provision of international financial advice to New Zealanders, without compromising consumer protection? Are there other changes that may be needed to aid this, beyond the technological options outlined in Chapter 4.2?

I guess this depends on where you are looking to accommodate the financial advice from. Why wouldn't foreign advisers be subject to the same requirements as NZ advisers.

Q30: 30. How can we better facilitate the export of New Zealand financial advice?

You could provide a summary of the key obligations in other jurisdictions so that financial advisers here can have a little bit of an idea on jurisdictions that they wish to target to provide services. They can then get further legal advice, but a general overview would provide the initial information. You could also impose the fiduciary standard so that overseas clients knew that the adviser had an obligation to act in the client's best interest.

Q31: 31. Do you have any comments on the proposal to retain the current approach to regulating broking and custodial services?

The definitions are confusing when working with them in a practical sense. Many people just read broker with an ordinary commercial meaning of the term. The terms broker and custodian should be split out into the Act and used with their common meaning.

PAGE 7: Chapter 5 - Potential packages of options

Q32: 32. What are the costs and benefits of the packages of options described in this chapter?

With respect to option 2 and 3, I am struggling to understand how the “competence” regime is going to work if you remove the distinction between class/personalised and category 1 and category 2. If it is complusory to provide a service (eg full advisory) within your area of competence (eg MIS and equity financial products) how are you meant to do this if you are a new financial adviser? How do you determine whether one is competent? I also think that your comparison with the legal profession is not quite right. Compentency varies a lot between lawyers. Also, most advice in a large law firm is provided by the Partner who has compentency. A junior does not sign off the advice, but works for the partner. Are you imagining a system where all junior financial advisers must have the advice approved by someone regarded as competent?

Q33: 33. How effective is each package in addressing the barriers described in Chapter 3?

Respondent skipped this question

Q34: 34. What changes could be made to any of the packages to improve how its elements work together?

Option 1 needs: (1) a government list of financial advisers to help clients identify where to seek financial advice from. (2) more meaningful terminolgy (maybe “salesperson”, but definetly not “expert”). (3) a competency element (such as a test), which doubles as a licence. (4) a fiduciary standard mandating that the financial adviser act in the best interests of the client. This should also address the “competency” change to options 2 and 3. If the financial adviser must adhere to a fiduciary standard, then as part of that standard the adviser can only advise on the matters that they are competent to advise on. This is different to what is in your summary – that states that an adviser must provide the service that matches the consumer’s request. This needs to be changed to be “must provide the service that matches the consumer’s request so long as the adviser is competent in that area, and if not, must refer the consumer to another adviser who is”. Requiring a fiduciary standard should also help remove the distinction between class and personalised advice – because depending on the nature of the client, and the relevant circumstances, the adviser can make a judgement call on the type of information that they require to advise the client. Without a fiduciary standard, you are essentially passing retail investors into class products on a suitability standard, which does not necessarily take the client’s best interests into account.

Q35: 35. Can you suggest any alternative packages of options that might work more effectively?

Respondent skipped this question

PAGE 8: Chapter 6 - Misuse of the Financial Service Providers Register

Q36: 36. Do you agree with our assessment of the pros and cons of the options to overcome misuse of the FSPR?

Respondent skipped this question

Q37: 37. What option or combination of options do you prefer and why? What are the costs and benefits?

Respondent skipped this question

Q38: 38. What are the potential risks and unintended consequences of the options above? How could these be mitigated?

Respondent skipped this question

Q39: 39. Would limiting public access to parts of the FSPR help reduce misuse?

Respondent skipped this question

PAGE 9: Demographics

Q40: 1. Enter your name and/or the name of the group of people, business, or organisation you are providing this submission on behalf of.

anonymous

Q41: 2. Enter your email address or other contact details

anonymous

Q42: 3. Are you providing this submission:

- As an individual

Q43: 4. Please select if your submission contains confidential information:

Respondent skipped this question