FINANCIAL SERVICES FEDERATION

FSF RESPONSES TO MBIE OPTIONS PAPER QUESTIONS 1 - 35 ABOUT POSSIBLE CHANGES TO THE FINANCIAL ADVISERS ACT

Thank you for the opportunity for the Financial Services Federation ("FSF") to respond to Parts 1 and 2 of the Options Paper addressing the issues relating to the financial service providers register.

While the FSF will respond in its attached submission to some of the questions in the Options Paper, the strongly held view of the FSF and its members is that the fundamental question that requires an answer has not been asked in the Options Paper – that being whether the scope of the Financial Advisers Act 2008 ("FAA") is relevant in the current environment.

The FSF would say in answer to this question that the inclusion of consumer credit as a product that is captured under the FAA is inappropriate and in fact significantly penalises providers of consumer credit as their activities are being regulated twice – once by the FAA and once (and far more relevantly to both their consumers and themselves) by the Credit Contracts & Consumer Finance Act 2014 ("CCCFA").

Further you will be aware that a Memorandum of Understanding exists between the Financial Markets Authority and the Commerce Commission that makes it clear that the dividing line relating to the flow of responsibilities between the two regulators is that the former regulates and enforces issues arising from investment advice and the latter those in relation to debt.

You will also be aware that the CCCFA underwent significant amendment to get to the point of its Current iteration which introduced the concept of Lender Responsibility Principles which came into force on 6 June 2015 and to which every provider of consumer credit is obliged to comply. These Lender Responsibility Principles include (but are not limited to):

- That the lender must at all times exercise the care, diligence and skill of a responsible lender in any advertisement for providing credit, before entering into an agreement to provide credit and before taking a relevant guarantee and in all subsequent dealings with a borrower;
- That the lender must make reasonable enquiries before entering into the agreement with a borrower to be satisfied that the credit provided will meet the borrower's requirements and objectives and the borrower will make the payments under the agreement without suffering substantial hardship;
- That the lender must assist the borrower to reach an informed decision as to whether or not to enter into the agreement and to be reasonably aware of the full implications of entering into the agreement including ensuring that any advertising is not misleading, deceptive or confusing, that the terms of the agreement are expressed in plain language in a clear, concise and intelligible manner, and that any information provided by the lender to the borrower is not presented in a manner that is misleading, deceptive or confusing;
- That the lender must assist the borrower to reach informed decisions in all subsequent dealings in relation to the agreement;

- That the lender must treat the borrower and their property reasonably and in an ethical manner;
- That the lender must ensure that the agreement is not oppressive and that the lender does not induce the borrower to enter into the agreement by oppressive means;
- That the lender has similar responsibilities towards any guarantor providing a relevant guarantee to the lender;
- That the lender has similar responsibilities in relation to relevant insurance contracts.

The Responsible Lending Code also came into force on 6 June 2015 and provides guidance to providers of consumer credit as to how they can meet these and the other Lender Responsibility Principles.

The FSF strongly submits that by adhering to the Lender Responsibility Principles and the Responsible Lending Code, providers of consumer credit are fully discharging their responsibilities to consumers in relation to any advice that may be provided to them with regard to the provision of such credit.

Further the FSF submits that, should any provider of consumer credit be thought to be in breach of their responsible lending obligations to consumers (or not discharging their responsibilities to provide suitable advice about such products) it would be the CCCFA that would be invoked to investigate the breach, enforce compliance or impose any relevant penalties on the provider and not the FAA.

The FSF therefore suggests in the strongest possible terms that the review of the FAA is timely in that it offers policy makers the opportunity to recognise that consumer credit is best addressed outside of the FAA and that consumer protection when it comes to the provision of consumer credit products is adequately provided by the CCCFA.

In its submissions on the May 2015 Issues Paper that preceded the current Options Paper, the FSF said this (as part of its response to Q1 of that Issues Paper):

> '*The fact that consumer credit is thus regulated by its own targeted legislation [i.e: the CCCFA] means it is not necessary for it also to be regulated by laws of more general application aimed at products of an entirely different kind, and the FSF strongly submits that the opportunity should now be taken to recognise that the coverage of consumer credit by the FAA was a mistake, is not necessary in a responsible lender environment, and that consumer credit should be removed from the scope of the FAA accordingly.*'

That remains the FSF's position, unchanged by anything in the current Options Paper. If anything, the Options Paper reinforces the FSF's views. Thus, credit contracts are mentioned only once in the entire Options Paper, in the middle of page 21, and even then credit contracts are mentioned only to state the obvious, namely that they are presently category 2 products for the purposes of the FAA.

The fact that credit contracts are mentioned only once and in that way in an Options Paper comprising more than 50 pages further emphasises the FSF's above position, and evidences firstly that issues currently perceived to arise from the FAA have no relevance to consumer credit, and secondly that there are evidently also no issues arising in a consumer credit context that officials felt even warranted a mention in the Options Paper.

To the FSF, that speaks volumes, and confirms that as above, there is neither any need for, nor any useful purpose being served by, the FAA applying to consumer credit, which should accordingly be removed from the scope of the Act.

More broadly, the FSF notes that there is a pattern of wide-ranging legislation such as the FAA and the Financial Markets Conduct Act 2013 (FMC Act) containing appropriately crafted exemptions to prevent this unwanted "doubling up". To give some examples;

- Retirement villages raise a mix of financial and non-financial issues – taking up residence in a retirement village is a major financial commitment for an individual, but also raises care and wellbeing issues. With the passing of the Retirement Villages Act 2003 Parliament recognised the distinctive issues associated with retirement villages and created a tailored regulatory regime for their supervision. Correspondingly the (then) Securities Act 1978 was amended to carve-out matters relating to retirement villages, which has been carried over into the FMC Act.
- The Takeovers Act and Takeovers Code create a specialised regime for the conduct of takeovers, with the Takeovers Panel as enforcement agency when required. The FMC Act carves out conduct in relation to takeover offers under the Takeover Code from general provisions relating to insider trading and market manipulation (as did the former Securities Markets Act 1988). This ensures that any allegations of inappropriate secondary market conduct in connection with a takeover bid are dealt with by the Takeovers Panel as a specialist body, rather than being split between two regulators. In a similar vein the general "fair dealing" provisions in Part 2 of the FMC Act are disapplied for conduct regulated under the Takeovers Code. Even the FAA itself excludes conduct in connection with a Takeovers Code bid, at sections 14(1)(j) and (k).
- The Companies Act provides statutory processes for schemes of arrangement and companies repurchasing their own shares, in each case with appropriate safeguards. These processes are exempted from the relevant aspects of the FMC Act in a similar manner to takeovers – again reflecting the general principal of avoiding unnecessary regulatory duplication.

We mention these examples to reinforce the point that a general regulatory response, where regimes overlap, is to give one precedence and use a statutory exemption to disapply the other. This has already been recognised with the numerous exemptions already contained in section 14 of the FAA, especially those at section 14(1)(i) to (m).

For the reasons noted above it is clear that the protection of borrowers' interests under consumer credit legislation is the Commerce Commission's responsibility, and not that of the FMA. As such, the FSF strongly submits that it is appropriate to exempt relevant services that are provided in connection with a consumer credit contract where the lender is subject to the responsible lending regime in the CCCFA.

Chapter 3 – Barriers to achieving the outcomes

1. **Do you agree with the barriers outlined in the Options Paper? If not, why not?**
   The FSF is not aware of these barriers existing to any material extent in respect of consumer credit. Nor have barriers of this kind been reported by members who are deposit takers with regard to investments offered by them, nor by members involved in the insurance sector.

2. **Is there evidence of other major barriers not captured in the Options Paper? If so, please explain**.
   The FSF is not aware of any such other major barriers either.

Chapter 4 – Discrete elements

3. **Which options will be most effective in achieving the desired outcomes and why**?
   The FSF intends to answer all of Questions 3, 4 and 6 – 8 here, by commenting on each Option as follows:

   Option 1: The FSF sees no need to remove the distinction between class and personalised advice, and is not satisfied that any "gap" of the kind referred to in the Options Paper does exists to any material extent;

   Option 2: So far as consumer credit is concerned, the FSF repeats that a better solution would be to remove it from the scope of the Act altogether. So far as the investments offered by the FSF's deposit taker members are concerned, the FSF would support removing the distinction between category 1 & category 2 in this way, including in the interests of achieving competitive neutrality between bank and NBDT investment products and avoiding any customer confusion there may be between adviser types;

   Option 3: This option and restricting advice on complex products to well qualified advisers makes sense in principle, and as the Options Paper notes, is effectively what the FAA does at present with AFAs. The problem with this approach at present is the category definition. For example, some NBDT investments are presently treated as a "complex" category 1 product, when clearly they are not very complex at all. And as we have said previously, consumer credit is included within the scope of the FAA when it clearly is being regulated by the CCCFA and therefore should be excluded altogether from any of the Options;

   Option 4: The FSF would not support the need for clients only to be considered "wholesale" if they opted into that category. That would add unnecessary complication and the FSF considers it is better to adhere to well considered definitions. The FSF also notes it is plainly desirable for the FAA to be consistent with the FMC Act here.

4. **What would the costs and benefits be of the various options for different participants (consumers, financial advisers, businesses)?**
   See the FSF's response at Q3 above

5. **Are there any other viable options? If so, please provide details**.
   There are none the FSF would suggest, apart from removing consumer credit from the scope of the Act altogether.

4.1 Restrictions on who can provide certain advice

6. **What implications would removing the distinction between class and personalised advice have on access to advice?**
   See the FSF's comments on that possibility at Q3 above

7. **Should high-risk services be restricted to certain advisers? Why or why not**?
   See the FSF's response at Q3 above

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?**
   See the FSF's response at Q3 above

4.2 Advice through technological channels

9. **What ethical and other entry requirements should apply to advice platforms?**
   Some FSF members provide on line loan calculators for the use of clients. Of their nature these are "class" advice and are already adequately regulated as such. The FSF would resist regulating them further.

10. **How, if at all, should requirements differ between traditional and online financial advice?**
    See the FSF's response at Q9 above

11. **Are the options suggested in this chapter sufficient to enable innovation in the adviser industry? What other changes might need to be made?**
    See the FSF's response at Q9 above

4.3 Ethical and client-care obligations

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 FSF does not agree with Option 1 on page 25 and with extending this obligation from AFAs to registered advisers and QFE advisers, as seems to be suggested by this. The FSF disagrees in particular with the comment on page 25 that this may be necessary because the present position is "confusing to consumers."

    That is especially true in the context of credit, where it is apparent to all borrowers that the loan representative with whom they are dealing is indeed selling the lender's product, and not advising on a range of different lenders' products. Any proposal of this kind should accordingly be confined to investment products.

13. **What would be some practical ways of distinguishing 'sales' and 'advice'? What obligations should salespeople have?**
    The FAA already makes exactly this distinction in the section 13 exemption for "incidental" services, which is of particular relevance to FSF members engaged in point of sale finance. Section 13 has worked well in practice and should not be changed.

14. **If there was a ban or restriction on conflicted remuneration who and what should it cover?**
    First, it definitely should not apply to those retailer or dealer employees who are who are presently exempted by Section 13, as they are involved in "sales", not in advisory services. That is well understood by the public at present, and is also reflected in them being exempted from the FAA at present.

    Further regulating "conflicted remuneration" may have something to commend it in respect of DIMs services or perhaps AFAs advising on more complex products, but not in any other areas, especially not in the case of most consumer credit staff, who are typically 'single product sellers' rather than brokers or advisers selling competitive products. It would be unusual for a lender's staff to be remunerated by commissions in any case.

4.4 Competency obligations

15. **How can competency requirements be designed to lift capability, without becoming an undue barrier to entry and continuation in the profession?**
    The FSF considers there is no need to seek to increase any existing competency requirements. The requirements for an AFA qualification are high enough already, and as the FSF has already noted above the problem at present is more about definition of the categories to which the AFA qualification relates. See further the comments on Option 3 at Q3 above about that.

    If, despite the FSF's views, the FAA will continue to apply to credit products, then additional competency requirements very definitely are not necessary for, and should not be added in respect of, "category 2" advisers on credit products. If such a suggestion were ever to be pursued further by MBIE, the FSF would ask to be consulted about it.

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?**
    The FSF has nothing to add to its above response to Q15.

4.5 Tools for ensuring compliance with the ethical and competency requirements

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?**
    The FAA's present QFE concept is a type of entity licensing model, and in the experience of those FSF members who are QFEs, it has worked well thus far, and there is no apparent need to change it. Nor is there any need to force it upon those credit providers who have chosen not to be QFEs, but who have chosen instead to have staff who are registered advisers, as that too has worked well for the FSF members in that category and needs no change.

    If officials believe there are grounds for imposing entity licensing on entities other than credit providers, what that may again reflect is that credit is sufficiently different in nature from other products to which the FAA relates to make the sensible solution to remove credit from the scope of the FAA altogether.

    As regards the possibility of an industry body such as the FSF having some compliance role, the FSF is definitely not set up to perform such a role, and neither the FSF nor its members would want this to occur. The FSF strongly opposes this suggestion.

    With regard to Option 4 and banning commissions, for reasons already stated above the FSF is pleased to see that the Options Paper states that "This is not currently a preferred option." It would certainly need much greater study than it is given in the Options Paper if this were to be considered seriously as an option.

18. **What suggestions do you have for the roles of different industry and regulatory bodies?**
    The FSF has nothing to add to its above response to Q17.

4.6 Disclosure

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?**
    In those areas of the Act's application that are principally relevant to FSF members (namely consumer credit, NBDT investment products and insurance that is often sold at point of sale) the FSF totally disagrees with the paragraph that appears in the middle of page 32 to the effect that existing FAA disclosure requirements "can be misleading to consumers." That has not been the experience of FSF members.

    It may well be the case in other areas, where the FSF can see that the differences between say an AFA and a registered advisers may not be widely appreciated, but once again that further emphasises that it does not make sense to regulate consumer credit by the FAA in the same way as those other areas, especially not when other (sometimes overlapping) disclosures are already required by other legislation such as the CCCFA.

    As to the 3 options put forward in pages 32 and 33:

    Option 1: The FSF strongly opposes the suggestion that all advisers should have the same disclosure requirements. It would not be at all sensible for, say, consumer loans staff to have the same disclosure requirements as AFAs, as was recognised in 2008 when the Act was passed, and that remains true today;

    Option 2: The first bullet point under this heading is already addressed by QFE and registered adviser requirements, so this would add nothing to existing requirements. As regards the remuneration and commission aspects, see what the FSF has already said above, such as at Q14: in the areas most relevant to FSF members, there is neither any need nor any point in requiring this further disclosure;

    Option 3: It is not possible to address this option without knowing what "further information" officials envisage might be added to what is already required to be on the FSP Register. The FSF would add that it doubts that Register is much used by consumers as an information source in any case.

20. **Would a common disclosure document for all advisers work in practice?**
    The FSF has nothing to add to its above response to Q19

21. **How could remuneration details be disclosed in a way that would be meaningful to consumers yet relatively simple for advisers to produce?**
    The FSF has nothing to add to its above response to Q19, except to reiterate that there is no need to consider requiring disclosures in respect of the remuneration of credit staff to customers, and no benefit would come from doing so –as already noted above, such staff are typically not remunerated by commissions.

4.7 Dispute resolution

22. **Is there any evidence that the existence of multiple schemes is leading to poor outcomes for consumers?**
    The FSF is not aware of anything to suggest that the existence of multiple schemes is leading to poor outcomes for consumers, nor of anything that might substantiate some of the surprising suggestions about that which are noted in the middle of page 34. The FSF thinks that the Options Paper is correct to state that there is a "lack of evidence" of such negative outcomes.

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?**
    The FSF definitely considers that the multiple scheme model should be retained. In principle the FSF also considers that consistency between dispute resolution scheme rules and processes is desirable, but is not aware of any evidence of material inconsistencies between schemes either existing or causing issues at present.

24. **Should professional indemnity insurance apply to all financial service providers?**
    The FSF does not see any need to make professional indemnity insurance mandatory for all financial service providers.

4.8 Finding an adviser

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)?**
    Both questions 25 and 26 address what the Options Paper refers to as "barriers to consumers knowing where to seek advice from". If such barriers exist, they are unlikely to be relevant to the activities of most FSF members, as most of their staff who are 'advisers' fall within that term because of their involvement in consumer credit, and the FSF is clear that the public generally has no problem finding or dealing with staff in that category.

    Nevertheless, the FSF does note with concern the related suggestions (on pages 36 and 37) that QFE advisers and registered advisers might be renamed. Although the FSF's preference would be that those statuses would cease to be relevant to many FSF members by removing consumer credit from the scope of the FAA as submitted above, if that does not occur then the FSF would oppose any renaming of the QFE adviser and registered adviser roles. Most relevant staff of the FSF members who employ 'advisers' fall into one of those two categories, and FSF members have had to make a significant investment in documentation and compliance systems that use those descriptions. There is nothing to suggest that any benefits that might result from renaming those roles would justify the significant costs that doing so would cause to industry participants.

26. **What terminology do you think would be more meaningful to consumers?**
    The FSF has nothing to add to its above response to Q25.

4.9 Other elements where no changes are proposed

The definitions of 'financial adviser' and 'financial adviser service'

27. **Do you have any comments on the proposal to retain the current definitions of 'financial adviser' and 'financial adviser service'?**
    The FSF has no issue with retaining the current definitions of 'financial adviser' and 'financial adviser service', but that comment does not detract from the FSF's strongly held view that each term should cease to apply to consumer credit, by removing consumer credit from the definition of a "category 2" financial product.

Exemptions from the application of the FA Act

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.**
    The exemptions for lawyers, accountants and estate agents are not directly relevant to FSF members, and given the lack of evidence that they are causing risk to consumers, the FSF is comfortable with those exemptions continuing.

    The FSF also notes that retailers' or dealers' staff who are involved in point of sale finance are also effectively exempted at present by section 13, and that should continue to be the case.

Territorial scope

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?**
    Issues about the provision of international financial advice are not relevant to FSF members.

30. **How can we better facilitate the export of New Zealand financial advice?**
    The FSF has nothing to add to its above response to Q29.

The regulation of brokers and custodians

31. **Do you have any comments on the proposal to retain the current approach to regulating broking and custodial services?**
    This issue is also of limited relevance to FSF members, and the FSF accordingly has no comment to make.

Chapter 5 – Potential packages of options

32. **What are the costs and benefits of the packages of options described in this chapter**?
    The FSF has nothing that it wishes to add here to its specific responses above, except that it will be evident from those responses that if credit is to remain subject to the FAA, of the options presented in the paper, the FSF would favour a 'minor change' option, such as "Package 1".

33. **How effective is each package in addressing the barriers described in Chapter 3?**
    As per Q32 above

34. **What changes could be made to any of the packages to improve how its elements work together?**
    As per Q32 above
35. **Can you suggest any alternative packages of options that might work more effectively?**
    As per Q32 above