Chapter 3 – Barriers to achieving the outcomes

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

   Generally, we agree with the description of the barriers, particularly the terminology in the legislation which is unclear and confusing.

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

   No response.

Chapter 4 – Discrete elements

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

   We support Options 1 and 3.

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

   No response.

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

   No response.

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?

   No response.

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

   Yes. The range of financial advice services that may be provided is broad, so we do not believe it is practical they are all treated the same in terms of standards of advice and competency requirements. As we noted in our original submission, the key issue is identifying what is or might be a high-risk service in a straightforward way that allows both financial advisers and their clients to know in advance of using the service whether an individual financial adviser is able to provide the advice they want.

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?

   This may have some negative implications for advisers, however, we believe the benefit of having clarity about the basis on which advice is being provided to both the consumer and financial advisers is more important.

4.2 Advice through technological channels

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

   No response.

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

    Specific warnings may be required to ensure the basis on which the advice is provided via platforms is clear so that people using them know how the advice is being generated and the extent to which their personal circumstances are, or are not, taken into consideration.

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

    No response.

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?

    A starting place for defining the ethical obligation to put the consumers' interests first is Code Standard 1 of the Code of Professional Conduct and we suggest this be used.

    As noted in our original submission, we generally see a failure to put consumers' interest first in respect of replacement insurance policies. In this situation, there is a significant risk consumers will find they have no cover (because they had pre-existing conditions or failed to disclose material information), often for minimal or no benefit to the consumer. What we see indicates financial advisers do not routinely make consumers aware of this risk, or that there may be ways of restructuring the existing policy to achieve a similar price reduction. In some situations, it appears financial advisers do not realise the ramifications of changing/replacing policies. Consumers appear to be unaware a financial adviser will usually receive a financial benefit for the replacement of an existing policy.

    Financial advisers currently complete a replacement business form as part of the application process for new policies, which is designed to specify the reasons for the change to the insurer and the consumer. These forms usually provide generic reasons

for replacing policies and we do not believe insurers check them before the new application is processed. We have, for example, seen a financial adviser specify a policy was being replaced to provide the consumer with total disability cover yet, when the new insurer decided not to offer that consumer the cover (because of the consumer's age), no reassessment of whether the replacement cover was in the consumer's best interests occurred. When the consumer later made a claim on the replacement policy, the claim was declined and the policy avoided for non-disclosure. Indications were that a claim under the consumer's original policy would have been accepted.

Given the extent of replacement business, we suggest specific obligations are required about the information and/or warnings that must be provided to consumers.

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

This is a relatively easy distinction to make by definition, but difficult to manage in practice, as it is easy to cross the line from sales to advice.

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

See our response to question 12.

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?

Tailoring competency requirements for different types of advisers to ensure they are relevant would help to stop them acting as a barrier, but may add complexity in respect of monitoring their effectiveness.

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?

We agree all financial advisers should have to meet a basic entry requirement. However, we are not sure it is practical for the requirements to be the same for all types of advisers.

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?

There is merit in this proposal as it makes the relationship and responsibility clear to consumers. It would also remove the confusion sole traders have in terms of their obligation to register on the FSPR and be a member of a dispute resolution scheme.

There are a variety of arrangements between advisers and businesses that would need to be considered, some of which might also logically fit within this model. For example, some businesses provide support services, including all compliance support, to a group of financial advisers. Even though the individual financial advisers may use or include the business's branding, the contractual arrangement treats the financial advisers as individuals and the business takes no responsibility for the activities of those financial advisers.

We believe this option should cover non-employee financial advisers who have contractual arrangements which are sufficiently similar to an employment arrangement as to warrant the business being responsible for those financial advisers. For example, it should include those businesses where the contracted financial advisers only sell through that business.

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

We believe the nature of the industry bodies in New Zealand mean this option would be difficult to implement coherently and/or meaningfully.

Most professional bodies' objective is to raise their members' operating standards. Some financial services professional bodies do this very effectively, but others do not. We believe there is too much inconsistency in professional bodies' roles, requirements and abilities to enforce their standards, for them to play a "formal" role in the regulation of financial advisers.

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 our experience written disclosure is the most effective, because it means consumers have a record they can refer to when required. However, one-off written disclosure requires consumers to keep all documentation and to remember to refer to it. For that reason, we believe there should be multiple points where key information is disclosed.

Most consumers now expect to be able to access information online and we believe that financial advisers' websites should be required to include specified key information, including what to do if their clients have a complaint.

We would also like to see a specific requirement that financial advisers and financial service providers must provide consumers with information about their complaints handling processes when a consumer makes a complaint, regardless of whether that information has previously been provided.

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

    We believe the information in disclosure documents, or at least the headings required to be covered, can be common to all financial advisers.

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

    It can be difficult to disclose remuneration in a relatively simple way, particularly for those financial advisers who can advise on a broad range of products from a number of product providers. To be useful, it needs to provide consumers with sufficient information to allow them to identify advice bias, based on commission.

    There may need to be options for describing remuneration specified depending on the way they are remunerated. For example, by defining a range or by specifying the relevant computation, together with an example of how it is applied.

4.7 Dispute resolution

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

    If nothing is done in New Zealand about competition among multiple schemes, there will be actual evidence of poor outcomes for consumers. That evidence would undermine the stated intention of the legislation. Currently, we must look internationally for comments and, in particular, to Australia, about the detriments of competition among multiple schemes and add it to our own experience; the IFSO Scheme believes that the complexity arising from multiple competing schemes does exist and can hinder a consumer's access to redress, as seen in the following example:

    An enquiry was made by a consumer who had taken out a loan to buy a car with finance company X and, at the same time, purchased loan repayment insurance from insurer Z. The customer rang the IFSO Scheme, because her car was being repossessed. This had happened because she had been sick and unable to work, insurer Z had declined her claim and she had been unable to keep up with the loan repayments. The customer understood that company X was entitled to repossess the car, because she had not made the repayments; however, she strongly believed insurer Z should have paid the claim. Company X was a member of FSCL and insurer Z was a member of the IFSO Scheme. FSCL was contacted to see whether it would be prepared to contact its member, company X, to ask if it would stop the repossession until the complaint against insurer Z had been resolved. FSCL declined to become involved. If company X and insurer Z had both been members of the IFSO Scheme, we may have been able to provide assistance to the consumer. However, the consumer decided not to pursue her complaint against insurer Z because, by that time, even if the complaint had been upheld, the car would have been repossessed by company X.

    In January 2012, a guide was published for The World Bank by David Thomas (formerly the Banking Ombudsman and, later, Principal Ombudsman for the Financial Ombudsman Service, United Kingdom) and Francis Frizon (the French Insurance Mediator), "Resolving disputes between consumers and financial businesses: Fundamentals for a financial ombudsman"("the World Bank report"). The authors discussed the coverage of a financial Ombudsman and the fact that creating an

Ombudsman scheme for a particular sector might be easier to start with. This is of course what happened in the United Kingdom, Ireland, Australia and New Zealand, with the Banking Ombudsman Scheme ("BOS") set up here in 1992 and the ISO Scheme set up in 1995 – both initially as voluntary schemes for banking and insurance respectively.

This was followed by the authors looking at the growing trend of bringing the sectors together into a single financial Ombudsman scheme which "covers all financial services [and] offers economies of scale and flexibility when workload swings between different financial sectors [and it] is also simpler for consumers to understand" (at page 38, the World Bank report).

The authors then specifically commented on competition (at pages 38-39, the World Bank report), as follows:

> "A few countries have the unusual idea of 'competitive' ombudsmen, where - subject to specified minimum standards - the financial industry is able to choose between two or more competing financial ombudsmen.
>
> Such a choice presents severe risks to independence and impartiality - because financial businesses may favour the ombudsman they consider likely to give businesses the best deal.
>
> It overlooks the role of financial ombudsmen as an alternative to the courts and creates one-sided competition - because, unlike the financial businesses, the consumers are not given any choice of ombudsman. See the ANZOA document in annex H."

The "ANZOA document" referred to is the policy statement ("ANZOA's policy statement") endorsed by the Members of the Australian and New Zealand Ombudsman Association ("ANZOA") regarding "Competition among Ombudsman offices" (www.anzoa.com.au).

ANZOA believes that competition among "Ombudsman offices runs counter to [the] principles [of independence, accessibility, fairness, efficiency, effectiveness and accountability]" and ANZOA's position is that "there should be only one external dispute resolution (EDR) Ombudsman's office for any industry or service area", for the following reasons:

> "Competition in Ombudsman offices is most likely to impact on industry Ombudsmen, and is considered inefficient and undesirable on a range of policy levels:
>
> - It is not in the interests of consumers/citizens or their advocates, as it may not be clear where to take complaints or which is the most appropriate service to deal with particular issues.
>
> - It is likely to add unnecessary and inefficient costs to Ombudsman services, e.g. inefficient duplication of infrastructure/resources/services/information systems, mechanisms to establish a 'common door' approach, and the need to provide information to consumers about different offices.
>
> - It may lead to manipulation of dispute resolution services, differing standards, and inconsistencies in decision making which could be adverse for consumers and participating organisations.
>
> - Poor performing organisations may choose to join an alternative office that they believe is not as rigorous in its approach to complaints.

- An office may focus more on participating organisations rather than on complainants or consumers in order to keep or grow its membership.

- Where offices are subject to regulatory approval and/or other regulatory mechanisms, regulators may need to set up separate reporting and communication systems for different offices, potentially about the same issues.

- The value of the Ombudsman's office as a source of information and analysis to contribute to the ongoing improvement of an industry or service area will be diluted, to the detriment of consumers, service providers and the wider community."

In May 2012, The Navigator Company Pty Limited (a company based in Melbourne, Australia, which has extensive experience of reviewing Ombudsman schemes in Australia, New Zealand and Canada) published the "Independent Review Credit Ombudsman Service Limited [('COSL')] Report" ("COSL report"), in which observations were made about competition in financial dispute resolution in Australia (at pages 16-17, COSL report), as follows:

> "The first challenge is to properly understand the nature of competition in this particular multi-stakeholder environment.
>
> First, this is not competition as it is normally thought of as applying in a free market. In industry EDR, there are three 'customers': the funder (member); the consumer; and the public interest (voiced through the regulator). Each of whom has clearly distinct interests and conceptions of quality.
>
> Second, there is also only one funder, the member firm, and in the normal course of day-to-day business only the member firm has the free market option of weighing up price and quality and optimising their outcomes through choice.
>
> Individual consumers must accept whichever EDR service their financial services provider chooses. The risk for consumers is that competition will result in the 'winner' being the EDR service provider that costs financial services providers the least (in fees, administration and in recommended compensation). But an EDR service provider that 'wins' on these terms also incurs substantial risks - the risk that frequent users of the services such as financial counsellors and legal aid lawyers will air their dissatisfaction publicly and with the regulator, undermining the scheme's reputation and position.
>
> We do not think these are trivial or remote risks. Ultimately, the regulator will have no choice but to impose greater and more specific regulatory standards, or in a more extreme case, force a merger of the competing schemes or swallow both schemes into a statutory scheme like that in the UK. (We note that competition in EDR is not universally supported. It has recently been criticised by the World Bank and by the Australian and New Zealand Ombudsman Association (ANZOA) and the Consumer Submission to the COSL Review includes argument that one scheme would be preferable to the current two scheme environment.)
>
> ...
>
> It should also be noted that these are not only long-term issues. The presence of competition is a powerful influencer of organisational behaviour - often in

> subtle and unacknowledged ways."

In August 2014, the Australian Securities and Investments Commission ("ASIC") made submissions on the Financial System Inquiry interim report (at pages 47- 48) as follows:

> "ASIC has played a key role in establishing and shaping the dispute resolution system in financial services industry. Over the period since the Wallis Inquiry, having set standards through regulatory guidance for both internal dispute resolution (IDR) processes and EDR schemes, ASIC approved a total of eight schemes. ASIC does not consider that competition between different schemes enhances consumer outcomes. ASIC has worked with industry to reduce the number of schemes, with resulting improvements in economies of scale and efficiency, the removal of uncertainty for consumers and financial investors, and the reduction in jurisdictional boundary issues. Following the merger of five EDR schemes into the Financial Ombudsman Service (FOS) in 2008 and 2009, there are now two ASIC-approved EDR schemes in Australia."

In March 2014, Consumer Action (an independent, not-for-profit, campaign-focused policy organisation which provides free legal advice and representation to vulnerable and disadvantaged consumers across Victoria, Australia and is the largest specialist consumer legal practice in Australia) referred to its submission to the Commonwealth Consumer Affairs Advisory Council ("CCAAC") review of the benchmarks for industry-dispute resolution schemes (at page 4), as follows:

> "In our submission to the CCAAC inquiry, we supported the position of the Australian and New Zealand Ombudsman Association that it is not desirable to have multiple ombudsman schemes operating in the same industry area. In the finance sector, there are two schemes operating: the Financial Ombudsman Service (FOS) and the Credit Ombudsman Service. We do not see that competition among ombudsman services in the one industry sector operates in the interests of consumers or efficient market outcomes. Rather than creating incentives for schemes to provide better service for consumers (that is, complainants), EDR schemes will be competing for the business of industry members who will be interested in paying lower fees (which may reduce resources available per compliant received) and more industry-friendly processes."

Based on international experience and submissions about multiple schemes operating in the financial sector, poor outcomes for New Zealand consumers are undesirable and, at this stage, still preventable.

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?

Certain scheme rules and processes must comply with the FSP Act and, therefore, they should already be consistent e.g. in terms of monitoring, the FSP Act requires that an annual report be provided to the Minister and 5 yearly independent reviews are undertaken.

However, if important aspects required of a DRS are not set out in the statute,

variations can emerge that create distinctions between the approved schemes e.g. monetary jurisdiction; while all the schemes now have the same limits, FSCL was originally approved with a lower cap of $100,000 which reduced its members' liability to pay consumers' complaints.

It is also important the approved schemes are all seen to be substantially the same in terms of structure. In particular, it is to be noted that ANZOA supports a "not for profit" model of DRS and not all of the schemes are the same e.g. FDR is a Crown owned entity and a "for profit" scheme, which is a different operating model and, with a focus on making money from complaints, is likely to lead to different organisational behaviour.

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

We believe professional indemnity insurance should apply to all financial service providers. However, we note that coverage under professional indemnity ("PI") insurance may vary and, in our experience of insurance products, the fact a financial service provider has it in place does not mean it will cover every situation.

We understand that, in Australia, all licensees must have a dispute resolution system, which includes an IDR procedure, membership of an ASIC-approved EDR scheme and arrangements for compensating consumers for loss or damage due to breaches of the financial services or credit laws. The law requires that unless the licensee is exempt (i.e. because they are prudentially regulated) they must generally hold adequate PI insurance cover. A licensee's PI insurance cover must be adequate for the licensee's business. ASIC's guidance also requires that a licensee's PI insurance must cover EDR scheme awards.

Our concern is that PI insurance is designed to protect licensees against business risk, and not to provide compensation directly to investors and financial consumers. It is a means of reducing the risk that a licensee cannot pay claims because of insufficient financial resources, but has some significant limitations, including where there are insolvency issues or multiple claims against a single licensee.

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)?

Using clearer and more meaningful terminology would be a useful start in assisting consumers to find and choose the right financial adviser.

We believe we need a combination of sources of consumer information. We see the government and industry as being best placed to get information to consumers. This needs to be supported by well informed consumer groups who can ensure consumers know who can assist if things go wrong.

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

We do not have a firm view on what terminology would be more meaningful to

consumers and support the proposal to consult with them to determine this. Using terminology that has traditionally been used in the industry in the way it is still commonly used would also be sensible, e.g. the term “Broker” which has been used in the FA Act to mean something entirely different to how it is commonly used in the industry.

We agree that the reference to “Registered” suggests a financial adviser has met a particular standard required to be registered and we believe that is potentially misleading and confusing for consumers.

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’?

In our experience these terms work reasonably well in practice.

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.

We are not aware of any issues in respect of those who are currently exempt.

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?

We appreciate that allowing consumers to access financial advice and products from overseas providers has some advantages. However, from a dispute resolution perspective dealing with financial service providers that do not have a meaningful presence in New Zealand can be difficult. For that reason, we support the tightening of the territorial scope of the legislation to require that financial service providers have a place of business in New Zealand. I refer to our submission of 29 January 2016 on the operation of the FSPR that provided more detail about this.

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

No response.

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?

    We do not receive complaints or enquiries about brokers and custodial services and are not aware of any specific issues in respect of them.

Chapter 5 – Potential packages of options

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

    We are not in a position to comment on the industry costs for each package. We anticipate package 2 would deliver sufficient benefits to outweigh the costs associated with the industry implementing it.

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

    No response.

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

    No response.

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

    No response.

Chapter 6 – Misuse of the Financial Service Providers Register

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

    I refer to our submission of 29 January 2016 on the operation of the FSPR that provided more detail about this. I also note that allowing overseas providers to use the NZ system simply to gain credibility for their international operation is fundamentally undermining the legislation and needs to be stopped; those overseas providers should not be allowed to register on the FSPR.

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

    I refer to our submission of 29 January 2016 on the operation of the FSPR that provided more detail about this.

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

I refer to our submission of 29 January 2016 on the operation of the FSPR that provided more detail about this.

39. Would limiting public access to parts of the FSPR help reduce misuse?
I refer to our submission of 29 January 2016 on the operation of the FSPR that provided more detail about this.

Demographics

1. Name:
Insurance & Financial Services Ombudsman Scheme Incorporated.

2. Contact details:

Redacted

3. Are you providing this submission:

☐~~As an individual~~

☐On behalf of an organisation

The IFSO Scheme is an approved dispute resolution scheme with a staff of 17 and over 4,000 members.