

Submission

to the

Ministry of Business,
Innovation and Employment

on the

Issues Paper - Review of
the Financial Advisers Act
2008 and the Financial
Services Providers
(Registration and Dispute
Resolution) Act 2008

22 July 2015

Submission by the New Zealand Bankers' Association to the Ministry of Business, Innovation and Employment on the Issues Paper – Review of the Financial Advisers Act 2008 and the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (“Issues Paper”)

About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes which contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.
2. The following fifteen registered banks in New Zealand are members of NZBA:
 - ANZ Bank New Zealand Limited
 - ASB Bank Limited
 - Bank of China (NZ) Limited
 - Bank of New Zealand
 - Bank of Tokyo-Mitsubishi, UFJ
 - Citibank, N.A.
 - The Co-operative Bank Limited
 - Heartland Bank Limited
 - The Hongkong and Shanghai Banking Corporation Limited
 - JPMorgan Chase Bank, N.A.
 - Kiwibank Limited
 - Rabobank New Zealand Limited
 - SBS Bank
 - TSB Bank Limited
 - Westpac New Zealand Limited.

Background

3. NZBA is grateful for the opportunity to submit on the Issues Paper.
4. NZBA commends the ongoing commitment to meaningful consultation and engagement and appreciates the invitation to participate in this consultation.
5. The following submission makes some brief comments on the Issues Paper.
6. If you would like to discuss any aspect of the submission further, please contact:

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Executive Summary

7. NZBA members currently employ over 25,000 staff with approximately 20,000 providing some form of advice service, delivered to bank customers within the QFE framework.
8. NZBA members have invested considerable time and resources implementing the FAA and generally view the framework for regulation of financial advisers as having improved the quality of advice for consumers of financial products and services.
9. NZBA notes however that there is a range of areas within the existing framework that could be both simplified and clarified to ensure that the goals of the review are met, i.e.
 - That consumers have the information they need to find and choose a financial adviser
 - Financial advice is accessible for consumers, and
 - Public confidence in the professionalism of financial advisers is promoted.
10. NZBA members will provide their own submissions on the Issues Paper. There is however a broad consensus across the industry that the following areas could be clarified and simplified through the review process to ensure that the goals of the review are met:
 - The current regime is too complex and New Zealand consumers may not be getting access to advice (Questions 35, 36 and 37)
 - QFE regulation (Questions 22, 23, 24 and 25)
 - The regulatory framework for advice needs to encompass emerging technologies (Questions 51 and 52)
 - Issues Paper to lead to the development of a range of policy options.

The current regime is too complex and New Zealand consumers may not be getting access to advice

11. Complexity in the application of the FAA arises from the following:
 - categories of financial advice
 - categories of financial adviser
 - categories of financial product, and
 - compliance requirements for the provision of certain types of financial advice (a written explanation for personalised financial advice).
12. These concepts and categories are not well understood by consumers of financial products and services and the artificial distinctions have resulted in compliance approaches by financial markets participants and advisers that do not achieve what consumers want.

13. Consumers do not understand what information or material they should be requesting or receiving when seeking financial advice. It is common that bank QFE customers are frustrated by not being able to access *product related advice* which they perceive as *financial advice* due to the challenges faced in traversing the various categorisation issues regarding products, advisers, and advice.
14. One of the key drivers of this problem is the complexity the FAA introduced into the financial advice industry, and the way in which industry has tried to implement and deal with that complexity. While the language of the FAA is now well known within the industry a customer does not necessarily know what type of adviser or advice they may need to make an informed decision.
15. For financial markets participants, it is difficult to confidently assess from the FAA what the boundaries of a “class service” are, and where product-related sales advice provided to individual customers (rather than to a class of customers), who have no expectation or requirement for a personalised financial adviser service, fits within the current regime.
16. The complexity and potential liability settings have resulted in service providers limiting the types of services and advice they provide to avoid compliance issues, or not making those services or advice available at all.
17. One of the unintended consequences of the legislation appears to be that New Zealanders now have less access to advice than they did prior to the regime coming into effect. Banks are committed to improving financial literacy for New Zealanders and outcomes for their customers and good quality advice is key to that. The legislative framework needs to make it easier for customers to seek and obtain advice to make appropriate decisions for their financial futures.
18. Uncertainty around the advice categories, as noted above, can mean that advisers (and businesses that employ advisers) adopt a cautious approach to the provision of information about financial products to avoid the risk of crossing into an advice space. Clarification of the distinction between these concepts will provide certainty to institutions around when they are providing advice and what the requirements are, vis-à-vis when they are selling a product. This is likely to improve consumer access to advice.
19. In particular the issue of implied advice is problematic, given the current subjective nature of the test. To help improve certainty for providers in what type of advice they are delivering, the current definition should be replaced with an objective “reasonable consumer in the particular circumstances” test. This would clarify the parameters around what advice is, and how it is to be determined.
20. Resolving this issue would involve refining the current regime in a way that enables the provision of financial products via both the existing licence regime for QFEs and registered product distributors, i.e. through both entities and individuals. This approach recognises that the sale of financial products can occur after information is provided about the product, with an actual or implied recommendation or opinion

about the product, but without assessing the customer's additional personal circumstances or factors.

21. For example, NZBA members frequently receive requests from customers seeking a recommendation or opinion relating to a particular product or products in situations where the customer does not want a comprehensive assessment of their financial situation or goals to be undertaken prior to the provision of the recommendation or opinion. Customers want their bank to provide enough information relating to the advantages/disadvantages of the product in question by reference to a general factual situation for them to be able to make an informed decision about whether to buy (or dispose of) the product.

QFE regulation

22. NZBA disagrees with the view espoused by some advisers, and which is reflected in the Issues Paper, that QFEs are lightly or inadequately regulated. This is simply wrong, and is a view which arises out of a lack of understanding of the admittedly complex regulatory framework in which QFEs operate.
23. QFEs play an important role in ensuring accessibility of advice. The QFE regime was designed to reduce the compliance costs of institutions with large numbers of advisers while ensuring they had appropriate regulatory coverage. While we strongly support the QFE framework and can understand the level of regulatory scrutiny over existing QFEs, in many respects these savings in compliance costs haven't been realised. It is unfortunate that there is a perception of transparency issues and that lower standards apply to QFEs.
24. In reality QFEs are subject to rigorous compliance and consumer protection obligations, at a standard that is on par or higher when compared to other market participants who perform similar services. This includes greater accountability and more intensive supervision by the regulator. Banks take their compliance responsibilities extremely seriously, investing considerable resources into education and monitoring. This inaccurate perception should not be used as a driver for change. In addition, QFEs play an important role in introducing new advisers into the industry which supports the accessibility objective.
25. The regime does allow some flexibility to allow QFE's to apply a different standard to their QFE advisers on their own category 1 products. We understand that this was intended to take account of the fact that the product range of a QFE adviser would often be limited in scope – e.g. to only 1 product type, in which case the qualifications of the Code and standards related to planning etc might be less relevant. In practice, we understand that this flexibility has only limited application as:
 - QFEs often have AFAs who are able to advise on a range of category 1 products from outside the QFE group. QFEs often use these AFAs to advise on their own category 1 products rather than using QFE advisers. As the

Issues Paper notes, QFEs actually account for 35% of the AFAs in New Zealand so QFEs have the capacity to do so.

- Information about whether QFEs utilise QFE advisers for category 1 products is available in their QFE disclosures. Many bank QFEs do not use QFE advisers to provide personalised advice on category 1 products.
26. In order to address the inaccurate and erroneous perception that QFEs are somehow less transparent or more lightly regulated than other advisers we have provided a comparison of the relevant QFE obligations vis-à-vis RFAs and AFAs below.
27. QFEs are required to provide disclosure under the Disclosure Regulations. The prescribed content of the QFE disclosure is comparable with that for RFAs with limited additions, and some additional expectations set by FMA in the explanatory note. QFE disclosure attracts additional obligations in relation to Category 1 products which are equivalent to those for AFAs.
28. The other QFE obligations under the FAA are contained in the Standard Terms and Conditions for QFEs and the Reporting and Notifications Standard Conditions for QFEs. The Terms and Conditions require a QFE to maintain appropriate governance and compliance arrangements. The FMA's guidance on these arrangements is set out in the QFE ABS Guide.
29. The FMA publishes the Terms and Conditions and its QFE ABS Guide on its website in exactly the same manner as the Standard Terms and Conditions for AFAs (<http://www.fma.govt.nz/compliance/role/qfes-and-qfe-advisers/your-on-going-obligations/>). AFAs are not required to provide copies of their ABS publicly – nor are QFEs. There is no equivalent suggestion of a lack of transparency for AFAs in the Issues Paper although they do not make their ABSs publicly available.
30. The Issues Paper appears to assume that QFE ABSs contain obligations under the FAA which should be publicly available. This is not the case. All the obligations on QFEs are contained in the FAA, its associated regulations and the Standard Terms and Conditions for QFEs issued by the FMA. An individual QFE's ABS merely describes its internal arrangements for meeting the expectations – its internal processes and controls. These would be of little use to a consumer and may be commercially sensitive.
31. The Standard Terms and Conditions for QFEs do not give the QFE ABS more binding force than an AFA ABS (and therefore a greater obligation to disclose). The Standard Terms and Conditions for QFEs require QFEs to:
- “1.2 . . . at all times maintain procedures to:
- i) Ensure that retail clients receive adequate consumer protection, including clients of the QFE, any member of the QFE Group and its nominated representatives;
 - ii) For personalised services provided by QFE advisers to retail clients in relation to category 1 products, ensure that consumer protection is of a similar standard to that

provided by advisers who are subject to the Code of Professional Conduct for Authorised Financial Advisers taking into account the scope of category 1 products for which the financial adviser service is provided;

iii) Train employees of the QFE and the QFE Group and nominated representatives;

iv) Set standards for employees of the QFE and the QFE Group and nominated representatives.”

32. QFEs are required to monitor their compliance with these obligations. The ABS provides the FMA with information about how each QFE addresses the obligations in 1.1, 1.2 and 1.3 of the Standard Terms and Conditions for QFEs in relation to governance and compliance arrangements.
33. The QFE ABS then acts as a benchmark for the notification of material changes to a QFEs adviser business or governance arrangements alongside other direct notification obligations.
34. The specific content of a QFEs ABS is not a set of obligations on the QFE. There is a QFE obligation to comply with the terms and conditions of its grant of QFE status under s46(1) of the FAA which is enforceable under s129 of the FAA. The obligation on QFEs in s46(1) FAA is absolutely identical to the AFA obligation under s45(1) FAA and its equivalent offence under s126.
35. There is no offence for a breach of a QFE or AFA ABS and consequently no requirement in the Reporting and Notifications Standard Conditions for QFEs or AFAs to report “breaches” of a QFE or AFA ABS.

QFE disclosure to customers

36. The QFE disclosure information provided to customers needs to be reviewed. The existing QFE disclosure could be simplified so that the relevant information is readily accessible online and the information handed to customers is better targeted to their needs.
37. AFA disclosure ought to be reviewed to ensure that customers are getting only the information that is specifically relevant to help them assess the adviser and their suitability to provide the service.
38. QFEs have extensive disclosure obligations many of which have been set by the FMA under the Standard Terms and Conditions for QFEs. The Standard Terms and Conditions for QFEs require a lot of information about the range and types of services because of an underlying assumption that a customer wants to know the range of adviser services available as they are choosing an adviser.
39. In practice the intended purpose of QFE disclosure is not necessarily related to the purpose of QFE customers. For example, consumers going to a bank for deposit or lending products do not think that they are choosing an adviser. People going to a

bank for deposit or lending products think they are choosing a bank. The QFE disclosure statement is artificial for customers in this context.

40. QFE disclosure statements are also complex and include FAA jargon. This is because QFEs must provide different information for different FAA categories of products and types of services under standard 4 of the Standard Terms and Conditions for QFEs. It is very difficult to do this without using the FAA jargon.
41. Customers are not ordinarily familiar with the types of financial adviser services under the FAA and do not find the information helpful.
42. Banks' QFE disclosures are usually lengthy as they must provide information about a wide range of products that are not relevant to the advice being given. Customers are usually not interested in all these products at the time they receive the QFE disclosure. There is also significant double up where a customer is receiving QFE disclosure and then both primary and secondary AFA disclosure when dealing with a bank AFA. This complex and detailed disclosure does not assist the consumer to make their decision, and in fact is more likely to undermine investor confidence in the advice being given if it is prefaced with what may be perceived as a lengthy 'disclaimer'.
43. Simplification of the disclosure requirements, particularly by category 2 QFE advisers, could be done in conjunction with increasing consumer financial capability.

The regulatory framework for advice needs to encompass emerging technologies

44. The current regime limits the giving of advice to an individual and this excludes entities from being able to give advice online. The regime should be amended to allow entities to give advice, which would recognise the shift towards customers (in particular young consumers) accessing online products and services, including advice. Enabling delivery of online financial advice presents an opportunity to provide financial advice to a large number of consumers.
45. The pace of change in the financial services landscape is fast and the risk of disruption high. Increasingly competition is coming from non-traditional sources, especially in the digital technology space. Policy and regulatory settings need to accommodate and encourage innovation and facilitate the use of new technologies, while effectively safeguarding consumers.
46. The regime should be neutral as to the delivery channel for advice and avoid bias of one over the other. The right settings will allow flexibility and bring about framework durability to enable new technology to provide new channels of advice delivery with customers. This will present opportunities and greatly increase access to advice, and will incentivise institutions to be proactive in developing technology that will lower costs and increase customer accessibility and convenience. Technology should help

overcome issues of small adviser numbers and the concerns around low numbers entering the financial advice industry.

47. Regulatory settings also need to be able to accommodate new models (such as peer-to-peer and crowd funding), while also ensuring a level compliance playing field.

Issues Paper to lead to development of a range of policy options for consideration

48. NZBA suggests that the first phase of this review is concluded with the provision of a range of policy options for discussion and consideration by key industry stakeholders as the next step.