Submission to the

Ministry of Economic Development

on the

Draft Financial Advisers (Disclosure) Regulations 2010

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SUBMISSION BY THE NEW ZEALAND BANKERS' ASSOCIATION TO THE MINISTRY OF ECONOMIC DEVELOPMENT ON THE DRAFT FINANCIAL ADVISERS (DISCLOSURE) REGULATIONS 2010

1. Thank you for the opportunity to comment on the draft Financial Advisers (Disclosure) Regulations 2010 (regulations), and for meeting with us to discuss our views on the regulations and the issues paper you circulated on the application of the disclosure obligation to the provision of telephone advice (issues paper). We appreciate the willingness of the Ministry of Economic Development (MED) to meet with the New Zealand Bankers' Association (NZBA) to discuss the workability of the disclosure regime.

2. This submission is the collective view of the NZBA, being the following nine member banks:
    - ANZ New Zealand Limited
    - ASB Bank Limited
    - Bank of New Zealand
    - Citibank, N.A.
    - Hongkong and Shanghai Banking Corporation Limited
    - Kiwibank Limited
    - TSB Bank Limited
    - Rabobank New Zealand Limited
    - Westpac New Zealand Limited.

3. In reviewing the regulations and issues paper, we have focused on areas of greatest concern for NZBA member banks: practical concerns about the regulations, specific issues relating to telephone advice, and disclosure requirements for qualifying financial entities (QFEs).

PRACTICAL CONCERNS ABOUT THE REGULATIONS

General points

Disclosure should be clear and not duplicate information

4. Overall, NZBA considers that the disclosure requirements in the regulations and the prescribed forms in the Schedules to the regulations do not always fit well together and may be unclear or duplicate information. For example, a statement on fees is required in the primary disclosure statement for authorised financial advisers (AFAs) in Schedule 2, Form 1 under the heading "How do I get paid for the services that I provide you?", and is also required in the AFA secondary disclosure statement in Schedule 1, clause 6.

5. NZBA suggests the requirements and forms should be closely reviewed to ensure clarity. Unnecessary duplication of information only adds to the amount of information consumers will receive without adding to the quality of that information and should also be avoided.

Disclosure statements could have a more positive focus

6. The prescribed forms contain some information which is negatively focused. While it is accepted that disclosure should address what a consumer can do if something goes wrong, some of this information may not always be useful. Under the heading "What else should you know about me", questions are asked about whether an adviser has been bankrupt, has had a recommendation or order made against him or her by a disciplinary committee or has been expelled from a professional body. Consideration could be given to requiring this information only where there is an adverse event to report. This would also shorten the prescribed form, which is currently unlikely to comply with the stated government policy that disclosure statements should not to exceed two A4 pages in length. (To this end we would also recommend removing other surplus information in prescribed disclosures and question whether the declaration section serves any purpose.)

7. If the question on bankruptcy is to remain, we note that a negative answer to the statement “I have been bankrupt within the previous 5 years”, could possibly lead a client to question what happened before that. This could be avoided by rephrasing the statement to read “I have not been adjudged bankrupt”. This is the approach used for current disclosure.

8. NZBA member banks have noted that current financial adviser disclosures are written in a more personal tone than is anticipated in the Schedule 2 forms. This allows advisers to introduce themselves to customers in their disclosure statements. NZBA submits that consideration be given to allowing the inclusion of a small amount of optionally disclosed information in disclosure statements, such as the adviser's qualifications, experience and professional memberships. This would allow for a more comprehensive picture of the adviser to be presented, and balance the more negatively focused compliance requirements of the prescribed form.

Specific matters

Disclosure of complaints information

9. Schedule 1, clauses 1 and 2 and the prescribed forms in Schedule 2 currently require the provision of a contact name and fax number for the AFA's internal complaints process and dispute resolution scheme. The provision of a single name is not always practicable given that complaints and disputes are often dealt with by a range of staff. We submit it would be more useful to include the name of the relevant role or team within an organisation. It is also noted that some organisations enable complaints to be made online. In such cases, consideration could be given to whether provision of the relevant website link would suffice.

10. It also seems unnecessary to require the inclusion of fax numbers in disclosure statements. This form of communication has become increasingly outmoded. It should be sufficient to provide postal address, phone number and email contact details (but to allow for the optional inclusion of fax numbers).

Schedule 2, Form 1

11. In Schedule 2, Form 1 under "How can I help you?" the aim of the first tick box appears to be to identify tied agents that only provide services in respect of 'own products', i.e. products provided by their employer or a corporate group with which they are associated. If so, it may be clearer to disclose this directly, i.e. "financial

products provided by the [x] group of companies" in the primary disclosure statement, rather than in the secondary disclosure statement pursuant to clause 10 of Schedule 1. That would avoid duplication with two disclosures on the same topic and give potential clients more information at the outset about the scope of service their adviser can provide.

12. The distinction between advisers who provide services in respect of financial products provided by 2 to 5 organisations as opposed to more than 5 organisations is arbitrary. A more relevant distinction may be between advisers who provide services in respect of financial products provided by a limited number of organisations, and advisers who provide services in respect of financial products from the whole market. In the case of the former, the standard wording could also include a prompt to "Ask me for a list of the organisations whose financial products I will be able to [give you advice/make recommendations/make financial decisions on your behalf] about".

13. Under "How do I get paid for the services that I provide you?" there is an assumption that all commissions will be retained. In fact, the full value of a commission may be passed on to the client, i.e. by reducing fees, reducing product charges, increasing the investment amount or by way of a refund. This could be addressed by adding an extra tick box for commissions that are passed on in full; or amending the first fees tick box to include commissions that are passed on in full.

14. The amount of the payment does, as stated, depend on the decisions the client makes. However, it could also depend on how much the client invests, the term of the investment and the client's age. We recommend consideration is given to adding to the generic statement proposed along the lines of the following: "The amount of that payment depends on the decisions you make, for example the amount you invest and for how long; and can also depend on factors like your age and personal circumstances."

15. AFAs may offer different payment options, and may therefore tick more than one box. Standard text such as “I offer different payment options, which I will discuss and agree with you” could be appropriate in these circumstances.

16. Under “What else should you know about me?” the third tick box requires disclosure of expulsion from any ‘professional body’. This term is undefined, and could be defined to clarify that the expulsion must be from a professional body associated with the provision of financial adviser services (see for example s41B(c) of the Securities Markets Act 1988). The definition of ‘professional body’ in the Code of Professional Conduct for AFAs may be appropriate.

Secondary disclosure statement

17. NZBA submits that the fees, commissions and benefits disclosure requirement under Schedule 1, clause 7 is too wide. Disclosure should only be required where there is a sufficient relationship between any benefit and the advice given. This could be overcome by including reference to any benefit “reasonably likely to materially influence the financial adviser”, as included in clause 8 in respect of interests.

Schedule 2, Form 2

18. The notes at the end of Schedule 2 Form 2 should be headed “Notes for other financial adviser…” rather than “Notes for authorised financial adviser…” .

PROVISION OF ADVICE BY TELEPHONE

19. NZBA supports the proposed exemption for advice provided by telephone in relation to category 1 financial products. This would exempt advisers from making full disclosure before giving advice by telephone to a member of the public, provided limited disclosure was made and followed up by full written disclosure within five working days.

20. NZBA also supports an exemption for category 2 financial products but submits that the proposed exemption is not practicable. This is because the exemption relates to the provision of advice that ‘does not result in a sale’. The fact of whether or not a sale occurs is not the appropriate trigger. In practice, it is not always possible to know whether a call will or will not result in a sale. It is common for a customer or prospective customer to telephone a bank for information which does not result in an immediate sale. The customer may then call back some time later to purchase the product about which they originally enquired.

21. NZBA member banks deal with a very large volume of telephone calls each day. In terms of training staff, it is significantly simpler to apply a rule (to disclose or not to disclose) all the time, or none of the time, than it is to require a judgment to be on disclosure for each call (which would be likely to result in a decision being made to ‘over disclose’). NZBA member banks would therefore prefer an exemption which would require a brief verbal disclosure for all telephone enquiries concerning category 2 financial products.

22. NZBA would welcome the opportunity to work with MED about the specific requirements for the proposed limited disclosure.

DISCLOSURE BY QUALIFYING FINANCIAL ENTITIES

Disclosure under the proposed regulations

23. The absence of prescribed forms for QFE disclosure or guidance about what will be required for inclusion in the terms and conditions of a grant of QFE status may lead to a lack of clarity and comparability among disclosure documents. While we understand that the terms and conditions for each QFE will necessarily be different in other respects, we consider that disclosure must be comparable and any variance between disclosure provided by QFEs may be potentially misleading. This could be avoided by including minimum standards in a prescribed form in the regulations for QFE disclosure. NZBA would be happy to assist with the development of a template form for QFE disclosure.

24. For the sake of completeness, we note clause 6(2)(a) of the draft regulations would require the disclosure of specified information by the QFE adviser on behalf of the QFE. We understand that this clause will be amended so that the disclosure requirement falls on QFEs and not their advisers. NZBA supports this change. As acknowledged, this would be consistent with the policy rationale advanced for the QFE model. QFEs could then, for example, provide the information required by clause 6(1) in brochures and signs displayed in customer relations areas.

Transitional arrangements sought for QFE disclosure to existing customers

25. NZBA member banks have raised significant concerns about the provision of disclosure statements to existing customers at the commencement of the new financial adviser regime. Section 25 of the Financial Advisers Act 2008 requires that a QFE ensures that it makes disclosure to each of its retail customers before a personalised service is provided. For NZBA member banks a very large number of customers will be required to be provided with this disclosure as at the commencement of the operation of the Act.

26. Apart from the key unknown, which is what will be required in terms of disclosure under the regulations and the terms and conditions of the grant of QFE status, the logistics of meeting the initial disclosure obligation will be difficult to manage, due to sheer volume. Of particular concern to banks is how they can 'ensure' disclosure is made. NZBA submits that consideration should be given to providing for deemed receipt in circumstances where disclosure has been provided in a reasonable fashion. Tracking receipt of disclosure would be extraordinarily difficult and costly to manage.

27. If written disclosure were to be required, NZBA estimates the costs of printing and posting disclosure to be millions of dollars. When Kiwisaver was introduced, member banks report having to make special arrangements with mail centres to accommodate the volume of mail. To reach a majority of existing clients this way most economically would suggest mailouts be combined with bank statements or other mailings. This could take more than a month and would not ensure all customers were reached, as some customers elect not to receive paper

statements. In addition to compliance difficulties, we also query whether a mailout is the best way of ensuring customer awareness of QFE disclosure.

28. If brief disclosure could be given over the telephone to all customers, directing them to a website for full disclosure, this would be helpful. However, this would still require systems changes and the requirements to test, implement and train staff. Even if a recorded message could be utilised at the start of incoming calls, some systems changes would still be required for outbound calls.

29. NZBA member banks have indicated six months is a fairly minimal lead time for this kind of change. This is because internal bank processes must be observed. Such processes would usually require a business case to be prepared and approved, which could take around six weeks. Then, design approval for an information technology systems change would need to be sought and approved. Systems would then need to be built and tested. Staff training time would also need to be factored in. In terms of implementation, there may also be delay. Banks commonly have ‘change windows’ which require systems changes have to be booked in advance, to ensure that risk is properly managed . Accordingly, it is critical to ensure that banks have certainty over disclosure requirements as soon as possible, so that compliance timetables are able to be met.