FinancialServicesCouncil.
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Financial Markets Policy
Building, Resources and Markets
Ministry of Business, Innovation and Employment
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Submission: Disclosure requirements in the new financial advice regime

This submission is from the Financial Services Council of New Zealand Incorporated (**FSC**).

The FSC represents New Zealand's financial services industry having 33 members at 30 April 2018. Companies represented in the FSC include the major insurers in life, disability, income, and trauma insurance, and some fund managers and KiwiSaver providers plus law firms, audit firms, and other providers to the financial services sector.

Our submission has been developed through consultation, and represents the views of our members and our industry. We acknowledge the time and input of all our members in contributing to this submission.

The FSC's guiding vision is to be the voice of New Zealand's financial services industry and we strongly support initiatives that are designed to deliver:

1. Strong and sustainable consumer outcomes;
2. Sustainability of the financial services sector; and
3. Increasing professionalism and trust of the industry.

We therefore agree with the five objectives identified in the consultation paper and broadly support the proposed measures. Our members agree that improved, consistent, consumer-focussed, transparent, disclosure requirements will benefit consumers and the industry.

Given the different business models, diversity and expertise of our members, there are times when there are a range of insights and views. Where this has been the case in relation to this submission we have provided a range of views for further discussion.

Implementation will be a balancing act between ensuring consumers have access to the information they need to make good decisions, and impact on the industry.

There are seven areas which we believe will address potential implementation issues and lead to better consumer outcomes. We expand on these areas overleaf.

I can be contacted on 021 0233 5414 or richard.klipin@fsc.org.nz to discuss any element of our submission.

Yours sincerely
Richard Klipin
Chief Executive Officer, Financial Services Council

Recommendations

1. **Principles-based approach**

   We support the move towards a principles-based environment, and the intent for the regulations to provide flexibility in terms of precisely how information is provided. We agree that this approach has the best chance of providing good consumer outcomes while mitigating the risk of undue compliance costs.

   However, under the Financial Services Legislation Amendment Bill (**Bill**), Financial Advice Providers (**FAPs**) (and others) may be liable for a contravention of the duties relating to disclosure and as such, the regulations must provide Financial Advice Providers and financial advisers certainty as to what is required.

   Certainty is particularly important in order to make disclosure flexible enough to cover a range of advice situations and delivery channels. We recommend that the regulations provide a range of sample templates for guidance, together with clear examples, that the industry can adopt or modify for use. The provision of templates and/or examples may, for some delivery channels, have the added benefit of introducing consistency for consumers, and minimising time and cost for the industry (and hence, ultimately for the consumer). As noted above, we support flexibility and therefore we do not recommend that use of such sample templates is mandatory.

   On the issue of templates, we note that paragraph 38 of the discussion paper proposes that regulations include presentation requirements to ensure consistency with the objectives. The Code of Conduct may also set requirements for how information is given to consumers. We submit that any presentational requirements are not duplicated in different areas of the regime.

2. **Phased disclosure**

   We support phased disclosure, and recommend minor improvements including:

   a) Information about licensing should be made available publicly on request, but should not be required at the time the scope is known.
   b) Acknowledgement that the disclosure of potential material conflicts of interest when the scope is known may lead to restricting scope in order to remove those conflicts.
   c) Consideration of introducing the words 'prominent' or 'easy to find', where relevant, in relation to phased disclosure requirements. For example, if disclosure is made via a website, the information should be easily found on the website, and not hidden. We note that 'prominent' may not work for all products, services or channels.

   While we support phased disclosure, we think it should be clearer that FAPs can combine disclosure/phases and therefore could place more reliance on the publicly available information, particularly where a FAPs business structure is relatively simple or straightforward.

3. **Disclosure of how commission is calculated**

   Our members have a range of views in relation to the three options proposed in the discussion paper. These views are:

   a) To ensure good outcomes for consumers, and consistency in application, the area of commissions is one that needs to be more prescriptive than principles-based (i.e. not Option 3 in the discussion paper).
   b) Given the complexity and range of commission arrangements, we consider a principle-based approach is preferable (Option 3). Disclosure in dollar terms will incur significant compliance costs and accurate disclosure may not be possible at any particular point in time. Consumers could be led to make choices based on fees rather than on what meets their needs.

c) We support disclosure of commission in dollar terms (including use of percentage commission rates). However, this could be by way of an example or a reasonable and temporal estimate. The need to allow reasonable and temporal estimates is due to:
   - The significant operational impact (time and cost) from calculating exact commission amounts.
   - The fact that commission amounts can change throughout the application process. For example, in relation to an insurance application, commission can double if the underwriting of a customer's application results in loadings to the premium.

We are supportive of transparency for consumers, although are concerned about potential compliance costs resulting from repetitive or excessive disclosure. Our members want to work with the Ministry to find the best solution for consumers and the industry. We suggest that real-life examples are used to workshop the best approach to how commissions should be disclosed, and that further specific examples/templates for guidance then be provided.

We support the method proposed in the paper to disclosing clawback, being that those advisers who charge clawback must disclose it as a possible fee, together with dollar amounts at different points in time.

4. Soft commissions

Notwithstanding that our members have a range of views on the use of soft commissions (e.g. overseas trips, professional education and administrative support), we are aligned in our view that soft commissions should be disclosed to consumers.

Soft commission structures can be complex, multiple and varied, so simple disclosure will be difficult. Scenario 2 in the discussion paper (annex 1) is a good example of what disclosure of soft commissions could look like.

We suggest that real-life examples are used to workshop with the industry the best approach to how soft commissions should be disclosed, and that further specific examples/templates for guidance then be created. The real-life examples should include non-monetary incentives both beyond and within organisations. Any resulting guidance should provide the flexibility to make it clear there is a balanced scorecard approach for employees who sell, where payment is not purely based on sales volumes.

5. Replacement Business

Our members have a range of views on replacement business, noting that replacement business is perhaps better handled through the suitability requirements in the Code of Professional Conduct for Financial Advice Services.

Should replacement business be addressed through disclosure requirements then, in general, our members agree that replacement business should have strong disclosure requirements. Notification should include:

a) General risks of replacing a product; and
b) Specific risks to the consumer around the benefits gained and lost, including a like-for-like comparison of existing and new products.

These replacement business requirements should be scalable and depend on the risks related to the type of product. If an adviser is unable to compare products (for example due to lack of information, lack of knowledge or unique features of the product), then this fact should be made clear to the consumer.

6. **Limiting scope to manage conflicts**
   We suggest that both disclosure and managing the scope of advice are ways to manage conflict and we support the disclosure of material conflicts of interest in both general and specific disclosure.

   More scenarios, similar to those already in the discussion paper (annex 1) will help the industry provide consumers with the right information.

7. **Clearer guidance on when regulators will take action**
   Our members support the move for consistent, useful, disclosure and want the ability to innovate, but are balancing this with wariness of regulatory enforcement.

   The current Financial Advisers Act 2008 regime is largely based on criminal offences. The Bill will move enforcement to a mainly civil liability regime. As the civil standard of proof is lower than that for criminal offences, the Bill therefore makes it easier for the Financial Markets Authority to obtain redress for customers. In principle, this is a good thing.

   The wariness of regulatory enforcement may lead to conservative, legalistic, approaches to disclosure. Such approaches are likely to be unhelpful to the consumer and against the objectives set out in the discussion paper. To encourage open and effective disclosure, we recommend that the Financial Markets Authority provide guidance on their approach to enforcing sections 431N and 431O of the Act.