

**INVESTMENT SAVINGS & INSURANCE ASSOCIATION OF NZ
INC**

Submission

to

**Ministry of Economic
Development**

on the

**Draft Financial Advisers
(Disclosure) Regulations 2010**

9 August 2010



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Investment Savings and Insurance Association of NZ Inc.

1.0 Introduction

- 1.1 The Investment Savings and Insurance Association ("ISI") is the industry association for the companies that issue and manage life insurance, superannuation and managed funds in New Zealand. ISI members are responsible for approximately \$50 billion funds under management. ISI members are also the leading providers of KiwiSaver funds and all six default providers are members of ISI.

A list of members is attached.

- 1.2 We welcome the opportunity to comment on the consultation draft of the *Financial Advisers (Disclosure) Regulations 2010*. These regulations set the practical details for application of the Financial Advisers Act 2008 ("Act") provisions around disclosure and should advance the objective of improving the information given to consumers and their understanding of the relationship with their adviser.

2.0 General Comments

- 2.1 As noted above, the primary objective of financial advisers' disclosure should be to improve the information available to consumers about the adviser with whom they are dealing, and to improve their understanding of the advice relationship.
- 2.2 ISI supports that objective and our comments on the proposals in the August 2009 MED discussion document were made with that in mind.
- 2.3 At the same time, the regulations should provide clear, unambiguous directions on the requirements for adviser disclosure and they should be able to be implemented with minimal compliance difficulties.
- 2.4 It is also important that the regulations apply appropriately to advisers in different distribution channels.

3.0 Further Consultation

We note that the draft regulations do not require disclosure of remuneration or material relationships for registered but not authorised advisers and we understand that there is to be separate consultation on this issue. At this point we reiterate the view given in our August 2009 submission that consumers would benefit from regulations requiring disclosure of remuneration and material interests, relationships or associations by all advisers, other than those giving advice on behalf of their employer.

4.0 Format

- 4.1 The proposed split into a 'primary' and 'secondary' disclosure statement creates the potential for unnecessary confusion. It would be preferable to have all of the information specified in clauses 1 to 11 of Schedule 1 disclosed up front in one statement, with the facility to apply section 22(1)(b) of the Act if it

is not practicable to make some of the disclosures before the service is provided.

- 4.2 For example, it may not be possible to provide certain information in respect of remuneration before the service is provided as the amount of remuneration may be dependent on the decision of the customer at the end of the advice process. The disclosure statement provided up front could include a general description of the basis on which the adviser will be paid for the advice process.

Further details of remuneration (if required) could then be provided once the transaction or contract has been finalised.

- 4.3 Form 1 in Schedule 2 is complicated unnecessarily by the ‘tick-box’ format and we recommend that it be amended to require advisers to disclose only the information that is applicable rather than including all of the options. We also have comments regarding some of the optional statements. Specifically:

How can I help you?

An adviser should never need to tick more than one box so it should be possible simply to select and insert the appropriate statement from the 3 options given.

While we appreciate the simplicity of the statements from a consumer perspective, for certain products it is not clear how many ‘organisations’ are involved in providing them. For example, an investment platform service may be marketed and distributed by one organisation, however, the investment products underlying the platform may be provided by a number of product providers. It is not clear whether each of these providers should be considered an ‘organisation’ for disclosure purposes. Another example is an organisation that sells a number of ‘white labelled’ products from different manufacturers – again, it is not clear whether each of the manufacturers should be considered an ‘organisation’ for disclosure purposes.

How do I get paid for the services that I provide to you?

Only payment types applicable to the adviser should have to be included in the disclosure statement in order to simplify the information for the consumer. For example, if an adviser is paid by fees only it should not be necessary to include the other payment types in the disclosure statement.

The definition of remuneration in clause 7 of Schedule 1 excludes ‘salary or wages of a fixed amount’. While we agree that salaried advisers should not have to disclose the *amount* of salary received, one of the optional statements under this heading should be for an adviser to state that he/she receives a salary from a particular employer.

What else should you know about me?

The tone of the statements in this section is negative. An adviser should only be required to state that he/she has been bankrupt or had a recommendation or order form from the disciplinary committee within the previous 5 years if that is applicable. These statements should not need to be included if they are not applicable. Alternatively, if there is a preference for some form of statement to be made, the adviser should be able to state 'I have never been bankrupted' or 'The disciplinary committee has never made a recommendation or order against me'.

- 4.4 Form 1 for AFAs asks the AFA to list the financial adviser services that they are authorised to provide. There is no word limit. Form 2 for RFAs asks them to list the classes of financial products in which they can give advice and there is a word limit of 200 words. This inconsistency should be addressed. We recommend that in both cases there should be a word limit.

5.0 Telephone Advice

- 5.1 We agree with the problems identified in the Issues Paper on the provision of telephone advice. The problems relate to the timing of disclosure and the requirement for disclosure even when the caller chooses not to go ahead with the financial product.
- 5.2 With regard to timing, section 22(1)(b) of the Act allows disclosure to be made as soon as practicable after providing the service. This provides flexibility to cover scenarios where advice is given other than face-to-face. For this flexibility to apply to authorised financial advisers, clause 5(c) would need to be amended so that the disclosure statement can be provided in accordance with sections 22(1)(a) or 22(1)(b). This would be consistent with clause 6(c) which applies to non-authorised financial advisers. We believe this is appropriate given the primary disclosure required to be made by authorised financial advisers (as set out in clauses 1 to 5 of Schedule 1) is substantially the same as the disclosure required by non-authorised financial advisers under clause 5(2).
- 5.3 With regard to disclosure when the caller chooses not to go ahead with the financial product, we agree that an exemption in respect of advice on category 2 financial products is necessary. We agree with the suggestion in the Issues Paper that the exemption apply when the following circumstances exist:
- The advice is provided by an employee or agent of a financial product provider; and
 - The financial product is subject to a cooling off period; and/or
 - Full written disclosure is provided [an adequate time] before the expiry of the cooling off period if the consumer decides to purchase the product. If the consumer decides not to purchase the product then no disclosure would need to be made.
- 5.4 A further matter to be borne in mind when advising the Minister of Commerce on the design of disclosure requirements applying to the provision of telephone

advice is that, rather than being limited specifically to telephone advice, the proposals in respect of the provision of advice over the telephone should be widened to cover all advice provided other than in written form or face-to-face. This would accommodate communication methods that are the result of new technologies, for example, video conferencing.

6.0 Material Relationships

The ISI view is that disclosure of any factor that has a potential to bias the advice given to a customer is more important than merely requiring disclosure of the amount of remuneration the adviser will receive from providing a particular service. Effectively, that would put more emphasis on disclosure of material relationships and any quota arrangements, for instance, rather than just dollar amounts.

This is an essential area of disclosure and we are surprised that there is no requirement for non-authorised advisers to disclose details of material relationships. We believe the consumer needs to know what other relationships may have an impact on the advice that is given. This should also cover relationships with any dealer groups, QFEs and non-QFE entities.

7.0 Disclosure by QFEs

Clause 6 of the regulation refers to disclosure by QFEs under section 25 of the Act.

Clause 6(2)(a) states that the disclosure information must be completed by a QFE adviser on behalf of the QFE. This is inconsistent with section 25 of the Act which requires the QFE to ensure that the prescribed information is disclosed to the client. There will be some situations where the QFE itself completes the disclosure document rather than the adviser. Therefore, we believe this provision should be deleted and reliance should simply remain on section 25 of the Act.

Clause 6(2)(c) states that the disclosure information must be provided by the QFE adviser to the client in accordance with sections 22 (1)(a) or (b) and 24(2)(d) of the Act. However, section 22(2) states that section 22(1) does not apply to a QFE adviser acting in that capacity. It appears there has been a typing error. The reference to 22(1)(a) or (b) should in fact be to 25(1)(a) or (b). Also, clause 6(2)(c) needs to be made consistent with section 25. Therefore the opening reference to “provided by the QFE adviser” should state “provided to the client in accordance with...”. How the QFE arranges for the disclosure to be provided is up to the QFE. Normally it will be through the adviser, but in some cases it may be another employee of the organisation or the responsibility could be contracted out to a third party such as a mailing house.

8.0 Indemnity Insurance

We note that section 23(2) of the Act allows for the regulations to require disclosure of indemnity insurance. However, the draft regulations do not currently include such a requirement and we support that position. Our view is that consumers should be able to see what protection is available in the event

that they receive bad advice and a blanket requirement to disclose professional indemnity insurance may lead consumers to believe they have protection that they do not in fact have.

Professional Indemnity insurance is designed primarily to protect the liabilities of the adviser. Professional Indemnity insurance largely focuses on legal costs incurred in defending a claim brought about by a third party. Many professional indemnity claims are successfully defended with no compensation paid to a consumer.

Requiring indemnity insurance to be disclosed in adviser disclosure statements could potentially create an unreasonable expectation in the eyes of the consumer regarding the potential for compensation. There is the potential risk that such disclosure could mislead consumers to the extent that they may not apply a normal common sense approach to their financial dealings (i.e. they are lulled into a false sense of security).

9.0 Interpretation

Additional definitions are required in order to remove ambiguity from the regulations.

Professional body

It is not clear what the expectation is for this expression and whether there would be a minimum size or standard required for a body to be recognized as a “professional body”.

Conflict of interest

It would be helpful to have some guidance on the meaning of ‘conflict of interest’ in clause 7(c) of Schedule 1.

10.0 Commencement

The regulations are proposed to come into force on 1 July 2011 whereas an adviser may be registered and/or approved as an authorised financial adviser from 1 December 2010. We believe it would be preferable for the disclosure regulations to have effect as soon as an adviser becomes a registered (non-authorised) financial adviser or an authorised financial adviser and to replace the disclosure requirements of the Securities Markets Act.

List of ISI Members

ISI MEMBERS

AIA NZ
AMP Financial Services
Asteron Life Ltd
AXA New Zealand
BNZ Investments and Insurance
CIGNA Life Insurance NZ Ltd
Dorchester Life
Equitable Group
Fidelity Life Assurance Co Ltd
Gen Re LifeHealth
Hannover Life Re of Australasia Ltd
ING New Zealand Ltd
Kiwibank Ltd
Medical Assurance Society NZ Ltd
Mercer
Munich Reinsurance Co of Australasia Ltd
Pinnacle Life
Public Trust
RGA Reinsurance Co. of Australia Ltd
Sovereign Ltd
Southsure Assurance
Swiss Re Life & Health Australia Ltd
TOWER New Zealand
Westpac/ BT Funds Management Ltd

Associate Members

Bell Gully
BNP Paribas
Bravura Solutions
Burrowes & Co
Chapman Tripp
Davies Financial & Actuarial Ltd
Deloitte
DLA Phillips Fox
Ernst & Young
InvestmentLink (New Zealand) Ltd
KPMG
Kensington Swan
Melville Jessup Weaver
Minter Ellison Rudd Watts
Morningstar Research Ltd
PricewaterhouseCoopers
Russell McVeagh
Simpson Grierson