

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

SUBMISSION

**TO THE
FINANCE AND EXPENDITURE
SELECT COMMITTEE**

ON THE

**FINANCIAL SERVICE PROVIDERS
(REGISTRATION AND DISPUTE
RESOLUTION) BILL**

28 February 2008



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INVESTMENT SAVINGS AND INSURANCE ASSOCIATION OF N.Z. INC.

1.0 Introduction

- 1.1 The Investment Savings and Insurance Association ("ISI") is the industry association representing the companies which issue or manage life insurance, superannuation and managed funds.
- 1.2 ISI has 22 members and 18 associate members who collectively manage over \$60 billion in collective investments on behalf of 1.3 million New Zealanders.
- 1.3 ISI made submissions to the Ministry of Economic Development in 2006 in response to the discussion documents produced from the Ministry's Review of Financial Products and Providers. We note that the Financial Service Providers (Registration and Dispute Resolution) Bill ("the Bill") brings into legislation many of the proposals put forward in the discussion documents: *Overview and Registration of Financial Institutions* and *Consumer Dispute Resolution and Redress*.
- 1.4 ISI is also aware of the Government's commitment to ensuring financial services legislation meets New Zealand's anti-money laundering obligations under the Financial Action Task Force Recommendations.

2.0 General Comments

- 2.1 ISI endorses the intention of the Bill to set up a registration system for financial service providers so that they can be more easily identified and monitored and are not controlled by persons with certain criminal convictions or management bans.
- 2.2 We also support the requirement for all financial service providers to belong to an approved dispute resolution service. All ISI members with retail product offerings are participants in either the Insurance and Savings Ombudsman Scheme or the Banking Ombudsman Scheme.
- 2.3 The success of the new regime will depend on the regulators (Reserve Bank, Securities Commission and Registrar of Financial Service Providers and Financial Advisers) being adequately resourced to enforce compliance by all financial service providers.
- 2.4 This Bill, and the Financial Advisers Bill to which it is closely related, are part of Phase One of legislation flowing from the Review of Financial Products and Providers. We support the intention to create a consistent regulatory framework for the financial services sector and to promote consumer confidence. The magnitude of the task is such that it is being introduced via a number of Bills and

it will be essential to ensure consistency between them and minimise compliance costs and complexity.

- 2.5 We do have some concerns with specific parts of the Bill and they are outlined in the Executive Summary below, and covered in more detail in the following clauses.

3.0 Executive Summary

ISI members support the overall intent of the Bill but key concerns are the possibility of a multitude of dispute resolution schemes and the confusion arising from cross-referencing with the Financial Advisers Bill. Our recommendations are:

- 3.1 Approval of a single dispute resolution scheme, formed either by creation of a new scheme, amalgamation of existing schemes or collaboration of existing schemes behind a single frontage. A reserve scheme would become unnecessary.
- 3.2 Combination of this Bill and the Financial Advisers Bill into one Act.
- 3.3 Urgent drafting of regulations so that they can be considered in conjunction with the Bill during the Select Committee process.
- 3.4 Clarification that financial product providers will not be caught within the definition of ‘financial adviser service’ in the Financial Advisers Bill.
- 3.5 Adequate resourcing of the Companies Office, the Reserve Bank and the Securities Commission to enable the legislation to be enforced.
- 3.6 Appeals against dispute resolution scheme decisions on process grounds to be heard by an independent review authority, rather than the Courts.
- 3.7 A facility for disputes that raise major or novel points of law to be referred to the Courts.

4.0 Discussion

Commencement

- 4.1 The provisions in the Bill for commencement of different parts at different times are confusing. Clause 2 of the Bill sets out that it will come into effect on the day after the date on which it receives the Royal assent, except for clause 44 and Part 2 which will come into force on a date set by Order in Council.
- 4.2 The effect of these provisions is that, although a disputes resolution scheme may apply for approval as an ‘approved dispute resolution scheme’, the requirement for a financial service provider to be a member will not apply until Clause 44 comes into effect. Similarly, the compulsory registration of financial service providers and financial advisers will not apply until Part 2 takes effect.
- 4.3 The Bill’s Explanatory Note states that the reason for Part 2 and Clause 44 being deferred is to enable regulations to be prepared. Clauses 42 and 74 give the Governor-General a wide-ranging power to make regulations and we recognise the benefit of having a facility for matters of detail to be dealt with by regulation. We are concerned, however, that there is no requirement for public consultation on regulations and therefore no opportunity for submissions to be made. As a consequence, significant responsibilities can be imposed on the financial services industry without the opportunity to comment on the impact.
- 4.4 We also note that it is difficult to comment on the adequacy of the implementation timeframes in this Bill when we have yet to see the detail that will be in the regulations. We recommend that regulations should be drafted as a matter of urgency so that they may be considered in conjunction with the Bill. At the very least, a commitment should be made to include consultation with affected parties as part of the development of any regulations under this Bill.
- 4.5 The commencement of Clause 44 is also dependent upon the appointment of a reserve scheme under Clause 66, which effectively defers the commencement of Part 3 of the Bill. In addition, until the Financial Advisers Bill is passed, there is no requirement for an adviser to belong to an approved professional body (“APB”), nor for the APB to arrange for all members to be registered. Until that happens, Part 2 of this Bill would not be able to be fully implemented.

Cross-referencing

- 4.6 Understanding of the Bill is complicated by the extent of cross-referencing to the Financial Advisers Bill and commencement of the Bill needs to be aligned with the effective date of the Financial Advisers Bill in order for the cross-references to be workable.

- 4.7 Clause 5 of the Bill lists the financial services covered by the definition and specifically excludes those provided ‘in the context of a financial adviser service’. ‘Financial Adviser Service’ and ‘financial adviser’ are not defined in the current Bill, but appear in the Financial Advisers Bill. Uncertainty about the effect of the phrase ‘not provided **in the context of** a financial adviser service’ (emphasis added), particularly pending enactment and taking effect of the Financial Advisers Bill, potentially creates a loophole to avoid registration.
- 4.8 Further, the extent of ‘in the context of a financial adviser service’ in the Financial Advisers Bill appears so wide that it would, presumably inadvertently, capture some financial service providers. For example, a financial service provider that would come within the definition of ‘Manager’ in the Securities Act may be deemed to be providing a financial adviser service because of the breadth of that definition in the Financial Advisers Bill. Paragraph (b) of the definition of financial adviser service refers to ‘*the receipt, handling, payment or investment of money or other property in the course of business if that receipt, handling, payment or investment is connected to, the result of, or performed in anticipation of, a financial decision...*’. A manager receives and handles the payment and investment of money in the course of business as a result of financial decisions. We recommend clarification of this point and propose to make a recommendation to that effect in our submission on the Financial Advisers Bill. We have copied the proposed wording of that recommendation here, in recognition of the interlinking of these Bills:

“On the assumption that paragraph (b) of the definition of financial adviser service in Clause 5 is intended to cover financial advisers handling client money on behalf of the financial product provider, Clause 7 should be amended to exclude a financial product provider. The exclusion should also be consistent with exclusions currently in the definition of ‘investment adviser and adviser’ in the Securities Markets Amendment Act 2006. That is, it should exclude the entities described in paragraph (c) of that definition i.e. an issuer or a promoter or a trustee or a statutory supervisor. We would also recommend exclusion of an administration manager and an investment manager otherwise they will be inadvertently captured by the broad definition of financial adviser service in Clause 5.”

- 4.9 It is essential that there is no confusion in the coverage of this Bill and the Financial Advisers Bill and, to that end, it may be preferable to combine the two Bills. We note that the author of Bills Digest 1599 also recommended that the two Bills should form one Act.

Enforcement to be adequately resourced

- 4.10 Clause 5 gives a very wide meaning to ‘financial service’ and it is essential that all financial service providers caught by the definition are required to comply with the Bill. The effectiveness of the legislation will depend on its enforcement. It

would be inequitable if compliance with the Bill were to be enforced for large (visible) service providers but not in respect of others who may be smaller but have a major impact on the financial well-being of their clients. We recommend that the Regulators be adequately resourced to ensure that the legislation is able to be enforced.

Application for registration

- 4.11 Clause 14 (2) requires an application for registration by a licensed provider to be accompanied by ‘any prescribed information required to obtain an appropriate licence.’ Legislation is planned that will require insurance companies to be licensed by the Reserve Bank. In order to avoid duplication of effort, we recommend that an application for registration should be required only to notify the Registrar of an existing licence and the Registrar should be empowered to obtain relevant information direct from the licensing authority.
- 4.12 We also recommend that the Registrar be required to automatically register all licensed insurance companies on notice from the Reserve Bank of a licence being granted (in much the same way as the Registrar will be required to register financial advisers on notice from an Approved Professional Body). Deregistration of insurance companies under the Bill should also be more discretionary and linked in with the withdrawal of a licence by the Reserve Bank and/or the Registrar should be required to consult with the Reserve Bank before deregistering an insurance company so as to not undermine the objectives of the prudential supervision regime for insurance companies.

Dispute Resolution

- 4.13 We endorse the objective of a “simple and low-cost avenue for consumers to seek redress”. The two ombudsman schemes to which ISI members belong currently provide such a service at **no cost** to consumers.
- 4.14 We are strongly opposed to the facility for more than one dispute resolution scheme to be approved by the Minister. Approving a range of dispute resolution schemes will be contrary to the objectives of accessibility and effectiveness set out in clause 43.
- 4.15 In all of the consultation leading up to the Bill we have recommended a single Financial Services Ombudsman Scheme and that is still our preference. A single dispute resolution scheme would provide a number of benefits:
- greater consistency of decisions
 - removing the possibility of complainants ‘scheme shopping’ and possibly approaching more than one scheme
 - avoiding demarcation issues and conflict over jurisdiction

- facilitating management of historical disputes against advisers (jurisdictional problems may arise if the adviser has changed scheme since the act or omission complained about.)
- 4.16 In order to achieve the objective of accessibility it is essential that consumers can easily identify where they can take their complaints about financial services and a single, high-profile body is the answer. That may be achieved by creating a new scheme or it may also be done more easily by creating a high-visibility Financial Services Ombudsman frontage behind which existing schemes could continue in their specialist roles with the addition of new clauses for those areas (such as advisers) which are not adequately covered at present.
- 4.17 We endorse the intention to limit Government involvement to approving schemes, receiving reports and having the power to request information and we do not recommend a statutory dispute resolution service. We do, however, believe that a multiplicity of dispute resolution schemes would be confusing for consumers and would not achieve the potential improvements in skill-utilisation and cost-effectiveness that could come from a single scheme.
- 4.18 As noted, under clause 44 (b) the requirement for any financial service provider to join a dispute resolution scheme only applies if a reserve scheme has been established and clause 66 (2) (b) requires the reserve scheme to be ‘capable of resolving disputes relating to all types of providers of all types of financial services and financial adviser services’. That objective could most easily be achieved by approving an amalgamation of existing schemes behind the banner of a single Financial Services Ombudsman scheme.
- 4.19 The size of the financial services market in New Zealand is too small to bear the cost that would be involved in the duplication of dispute resolution schemes. We note that in the United Kingdom there is a single Financial Services Ombudsman and there are moves in Australia towards aggregation of their dispute resolution schemes. Both of those markets are considerably bigger than New Zealand.

Criteria for approval of dispute resolution schemes

- 4.20 Clause 47 sets out the ‘mandatory considerations’ that the Minister must have regard to when considering an application for approval of a dispute resolution scheme. We are concerned that some of the ‘considerations’ are vague and existing schemes may incur unnecessary expense demonstrating that they have complied. For example, clause 47 (1) (b) refers to whether the applicant has undertaken ‘appropriate’ consultation with representatives of consumers. It is difficult to know how far that requirement should be taken, particularly in instances where there is no obvious representative of a specific group of consumers or a scheme has been operating successfully for a number of years. We recommend that clause 47 (1) (b) should be amended to require ‘reasonable’ consultation, which is more readily interpreted as an objective standard.

Reserve Scheme

- 4.21 Some clarification is needed regarding the establishment of a reserve scheme. As noted above, the requirement for a financial services provider to join a dispute resolution scheme will not apply until a reserve scheme has been established and clause 66 (2) (b) requires the reserve scheme to be capable of resolving disputes for all types of financial services and providers.
- 4.22 We are not aware of any scheme currently in existence that would qualify for appointment under clause 66. Consequently, such a scheme would need to be established, or an existing scheme would need to be expanded to fit the criteria, before the requirement for financial service providers to join a dispute resolution scheme would commence.
- 4.23 We acknowledge that some lead time would be required for existing schemes to combine under the brand of 'Financial Services Ombudsman' but we cannot see the value of establishing a comprehensive reserve scheme at the same time and deferring the requirement for financial services providers to join a scheme where one already exists.
- 4.24 As the terms 'complaint' and 'dispute' are both used in Part 3 of the Bill we believe it would be beneficial for them to be defined. We recommend the following definitions:
"complaint" means an expression of dissatisfaction conveyed to the company or an **adviser** about a product, **advice** or service offered or provided coupled with a request to remedy it.
"dispute" means an unresolved **complaint**.

Appeals

- 4.25 The section in the Bill regarding appeals is potentially confusing for consumers. On the one hand, it is an improvement on some current dispute resolution processes (where reviewers review their own process) to have a clear path to follow if the complainant is dissatisfied with the process. On the other hand, there is the potential for consumers to mistakenly believe that, by appealing to the District Court, they will get a different decision, when in fact all that happens is the matter is sent back to be reheard.
- 4.26 However, the District Court can be a daunting forum for many people and that is at odds with the accessibility objective of a dispute resolution scheme. It would be preferable to have a 'dispute resolution expert' review the process, as in the United Kingdom where there is an independent reviewer who is appointed by the board for the Financial Ombudsman Service. A further right of appeal should be available to the District Court on process grounds, at the appellant's expense.

4.27 We recommend that there should also be a facility in the legislation for a member of an approved dispute resolution scheme to have a dispute, prior to a binding ruling by the decision maker, referred from the scheme to the District Court if the dispute involves:

- an issue which has important consequences for the business of the member or members generally; or
- an important or novel point of law.

The member will provide notification to the decision maker and an undertaking that if either party to the dispute commences proceedings within six months then the member will pay the costs. On receipt of the notification, the decision maker will cease further consideration of the issue.