

**Submission to:**

Financial Markets Policy
Ministry of Business, Innovation and Employment

26 February 2016

Subject:

Options Paper: Review of the Financial Advisers Act 2008 and the Financial Service Providers (Registration and Dispute Resolution) Act 2008

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Background

Citizens Advice Bureau New Zealand (CABNZ) Ngā Pou Whakawhirinaki o Aotearoa welcomes the opportunity to be involved in the review of legislation relating to financial advisers.

The purpose of our organisation is to:

- Ensure that individuals do not suffer through ignorance of their rights and responsibilities or of the services available; or through an inability to express their needs effectively — Me noho matāra kia kua te tangata e mate i tāna kore mōhio ki ngā āhuatanga e āhei atu ana ia, ki ngā mahi rānei e tika ana kia mahia e ia, ki ngā ratonga rānei e āhei atu ana ia; i te kore rānei āna e āhei ki te whakaputu i āna hiahia kia mārama mai ai te tangata.
- Exert a responsible influence on the development of social policies and services, both locally and nationally — Kia tino whai wāhi atu ki te auahatanga o ngā kaupapa-ā-iwi me ngā ratonga-ā-rohe, puta noa hoki i te motu.

We support the principle of partnership reflected in the Treaty of Waitangi. E tautoko ana Ngā Pou Whakawhirinaki, i te mātāpono nohotahi (hononga), e whakaatahia ana i roto i te Tiriti o Waitangi.

We work to empower individuals to resolve their problems and to strengthen communities. The person-to-person service provided by over 2,400 Citizens Advice Bureau (CAB) volunteers is unique in New Zealand. From 83 locations around New Zealand, the CAB provides individuals with a free, impartial and confidential service of information, advice,



advocacy and referral. In the 2014/2015 financial year we had 530,000 interactions with clients, including over 200,000 in-depth enquiries where we offered information, advice and support across the gamut of issues that affect people in their daily lives.

We use our experience with clients to seek socially just policies and services in Aotearoa New Zealand.

1.0 Outcomes – keep consumers at the centre

Citizens Advice Bureau New Zealand regards the outcomes listed in the Options Paper as an improvement on the goals proposed in the earlier Issues Paper, which we also responded to. In our opinion, the goals did not adequately reflect the fact that the primary reason for regulating the financial advice services industry is to increase the chances of consumers being given good financial advice - advice that matches the client's financial position and risk profile and puts their interests first. This is now acknowledged by the second outcome the review seeks to achieve: *Advice improves consumers' financial outcomes.*

As we said in our response to the Issues Paper, we must not lose sight of the fact that the suite of legislation regulating the financial advice industry came into being because consumers needed protection from advisers who were being unscrupulous or negligent. In reviewing this legislation the focus must be on how best to protect the consumer, not on what is most convenient for the industry, or cheapest for government to implement and monitor.

In our earlier submission we pointed out that the current purpose statement of the Financial Advisers Act (FAA) is indirect about the need for consumer protection:

The purpose of this Act is to promote the sound and efficient delivery of financial adviser and broking services, and to encourage public confidence in the professionalism and integrity of financial advisers and brokers.

We continue to believe that the FAA purpose statement should be amended to put consumer protection front and centre. For example:

The purpose of this Act is to create the conditions that will give consumers the best possible chances of obtaining financial advice which is sound and puts their interests first.

2.0 Measures to reduce complexity and confusion

We agree with the proposal in section 4.8 of the Options Paper that the Ministry work with consumers and advisers to identify terminology that would make it easier to distinguish between the different categories of adviser and the different categories of advice.

We also wonder whether complexity and confusion could be reduced by simply having fewer categories of adviser – see 2.1 below.

2.1 RFA's

As stated in our earlier submission, we are in favour of doing away with the term Registered Financial Adviser (RFA). This designation is misleading, and in no way conveys the fact that, under the current regime, the bearer:

- is restricted to providing a limited range of advice
- does not have to meet minimum competency standards
- does not have to put the consumer's interests first
- does not have to disclose conflicts of interest

These restrictions and limitations increase the risk to the consumer, and the new designation must somehow convey this. It is important to get this right, given that so many financial advisers currently fall into the RFA category.¹

We also agree with the suggestion in section 4.5 of the Options Paper that RFA's should be subject to a licensing or approval process over and above the requirement to register.

An alternative approach could be to do away with the RFA category altogether, and require all advisers who are not Brokers or working for Qualifying Financial Entities (QFE's) to become Authorised Financial Advisers (AFA's). This could lift the standard of service provided to consumers while at the same time resolving much of the current confusion about the different types of advisers and the variation in ethical and competency standards.

2.2 QFE's

We agree with the proposal to amend the term 'QFE adviser' to include the name of the business that adviser is working for.

Unless changes are made to QFE standards, it also needs to be made clear to consumers that advisers in the QFE category are not always required to put the consumer's interests first, only have to disclose if asked to do so by the client, and may be operating to in-house competency standards.

¹ The following numbers were provided in the MBIE Issues Paper of May 2015:

- 1900 Authorised Financial Advisers (AFA's)
- 56 Qualifying Financial Entities (QFE's) which employ 23,000 non-AFA's
- 6200 Registered Financial Advisers (RFA's)

2.3 Sales vs Advice

We are recommending that conflicted remuneration be phased out (see 5.0 below), but if this does not come to pass, the next best thing is to completely ‘divorce’ sales from advice. This is a crucial distinction to make, and one that is often not clear to consumers, who may think they are receiving advice when in fact what they are being given is a sales pitch which takes no account of their best interests.

We therefore support the idea of creating a designation specifically for people who are selling financial products (and possibly receiving commissions or bonuses as a result), instead of advising clients and exploring options with them in a neutral fashion. We do not believe that such a person should be permitted to call themselves a financial adviser.

Any Ministry-led campaign to help consumers distinguish between sales and advice could also take the opportunity to make it clear to consumers that even the advice of an ‘independent adviser’ may be limited by the range of products that person has access to.

3.0 One-stop-shop for consumers looking for a financial adviser

We support the idea of establishing a portal to assist consumers to find an adviser to suit their needs although we have doubts about whether the Register of Financial Service Providers could serve this purpose. It would certainly need to be significantly re-designed.

As mentioned in our earlier submission, we find the Register to be decidedly unhelpful as a means of obtaining information about providers and comparing them. We recommend that it be re-built to reflect what non-expert consumers need to know and what they say they would find useful.

4.0 Competency levels

It is of real concern that RFA’s are not required to meet a minimum competency standard “despite advising on financial products which can have a significant impact on consumers’ financial wellbeing” (Options Paper p.27). We see this as an anomaly that needs to be corrected and believe that all financial advisers should be required to demonstrate that they have met the present minimum competency standard before providing financial advice. Again, this could be achieved by requiring all RFA’s to upskill to become AFA’s.

In answer to the concern that raising the bar may cause some to leave the industry and/or increase the cost of advice, we say that this is an acceptable price to pay for ensuring that advice received by consumers meets a minimum standard. It is more important to have competent advisers than many advisers.

5.0 Managing conflicts of interest

We find it unacceptable that “there is currently no across-the-board requirement [for financial advisers] to put consumers’ interests first or to disclose conflicts of interest to consumers” (Options Paper p.17) and we doubt that many consumers are aware that this is the case.

These two gaps seriously undermine the capacity of the current regime to deliver effective consumer protection and effective advice. We think the solution is a combination of Options 1, 2 and 4 suggested in section 4.3 of the Options Paper.

We agree with the proposal to extend ethical requirements to all providers of financial advice services (Option 1) so that all have the obligation to put the consumer's interests first and to manage any conflicts of interest that may influence the advice provided. As already stated, we also agree with the need to distinguish between sales and advice (Option 2).

Most importantly, however, we consider it essential to phase out conflicted remuneration (Option 4). The Options Paper makes no secret of the fact that commissions and other conflicted remuneration create a conflict of interest that stands in the way of advisers acting in the best interests of their clients:

Remuneration arrangements (such as commissions) and sales targets are incentivising some advisers to provide advice which may not lead to the best outcome for the consumer.[...] This includes consumers being churned between insurance policies and sold replacement products, when this is in the interest of the adviser rather than the consumer. (Options Paper p.17)

Given the detrimental effect this situation is having on consumers, we are disappointed to see that a ban on conflicted remuneration is not the Ministry's preferred option. We are aware that the Ministry favours disclosure as a means of addressing conflicts of interest but we believe it is unrealistic to assume that consumers will have the skills to evaluate advice in the light of a disclosed conflict of interest.

The solution is to regulate to eliminate the conflict of interest and thereby give consumers the best possible chance of getting financial advice that puts their interests first. The result may be an increase in upfront fees, but this is preferable to the situations described above.

6.0 Disclosure

We are in favour of the proposal to require all advisers to disclose the same information, and in a form that is meaningful for consumers. This information must include a description of how the adviser will be remunerated (fees, commissions etc) and alert the client to any other conflicts of interest.

However, we reiterate our caveat that disclosure alone cannot remove the risks to consumers associated with conflicted remuneration. Consumers will not necessarily know how to use the disclosed information to assess the financial advice they are being given and in some cases the disclosure may give the consumer a false sense of security, rather than acting as a warning.

Disclosure of information is an important element of consumer protection, and we wish to see it used to the best possible effect. However, we continue to believe that the surest way



to protect consumers against conflicts of interest arising from payment structures such as commissions is to regulate to prohibit the conflict.

7.0 Dispute resolution

We are disappointed that the Ministry is not persuaded of the need to replace the current multiple scheme model with a single scheme.

We are of the opinion that the current arrangement disadvantages consumers because the schemes are set up to provide a service for their members - financial service providers - not for the complainant. This creates a conflict of interest.

We therefore once again recommend that the four competing schemes be replaced with one neutral disputes resolution body tasked with dealing with all disputes between consumers and Financial Service Providers.

Thank you for this opportunity to comment. Please contact me if you have any questions, or want any clarification about our submission.

Yours sincerely

A handwritten signature in black ink, appearing to read "Kerry Dalton".

Kerry Dalton
Chief Executive