

# Summary

## **Objectives**

Under its Terms of Reference, the Task Force is required to consider and report on the regulation of financial intermediaries, and suggest options for reform that will enhance the quality of financial information and advice provided to the public and assist New Zealanders to make the most of their savings.

## **Desirable outcomes**

From these two broad objectives, the Task Force has identified the following specific review outcomes that any reform should positively contribute towards, recognising that any change is likely to take time:

- Providing both the New Zealand public and financial intermediaries with reasonable grounds for participating with confidence in the financial intermediary sector generally;
- Encouraging New Zealanders to increase their use of appropriately qualified financial intermediaries where it is suitable and cost effective to do so;
- An appropriate baseline level of financial intermediary competency and ethical standards;
- Effective disclosure of consumer relevant information about the financial intermediary, in addition to information about the financial products and product generators that the intermediary advises on or promotes;
- Enhancing the general baseline financial literacy of the New Zealand public including the ability to raise questions about the appropriateness of information or advice provided by financial intermediaries and product generators;
- Providing effective mechanisms for addressing poor quality information or advice and unethical or fraudulent behaviour;
- Through the above, contributing to enhanced confidence both by domestic and external investors, in New Zealand's financial markets generally; and
- Having a regulatory regime which is cost effective in achieving the above outcomes.

The Task Force is concerned to ensure that any regulatory reform:

- Facilitates the benefits of choice, innovation and competition; and
- Is effective and proportionate to the issues identified, that the impact of any change can be assessed and that the costs of change are outweighed by the benefits.

The Task Force believes that if it intends structural change in the industry to result from its recommendations, that intention should be explicitly signalled. However, the Task Force is not seeking, as an aim in itself, change in the structure or composition of the industry. The Task Force though is suggesting changes in disclosure and the introduction of industry wide standards, as well as enhanced redress mechanisms, enforcement and sanctions. The Task Force acknowledges that changes in practises in these areas may, directly or indirectly, impact on aspects of the structure and composition of the industry. The Task Force seeks your views on possible impacts.

## **International comparability**

The Task Force believes that international practices and standards, as well as the regulatory approach taken by our closest neighbour, Australia, are relevant considerations. Accordingly, the Task Force has reviewed international standards and comparable jurisdictions' approaches to the regulation of financial intermediaries. The Task Force is guided by the view that any reform of the New Zealand financial intermediary sector should be one that, having regard to both domestic and international considerations, best meets New Zealand's needs.

## **Scope of Task Force focus**

The Task Force's focus is a functional one. Our focus is on the regime under which those who provide financial advice or market a financial product operate, and the position of consumers who deal with them.

A focus on both advice and promotion recognises that in New Zealand, as in many other markets, financial intermediaries can cover three, conceptually distinct, roles, namely:

- Those who undertake a factual information only or execution only role (an “information only” role);
- Those who promote financial products, and provide more than factual information (for example, marketing aspects of the product) but do not advise on the suitability or appropriateness of the product for the consumer’s personal circumstances (“product marketer” role); and
- Those who provide broad financial planning advice or advice on financial products, and implicitly or explicitly advise the consumer on the suitability or appropriateness for the consumer’s personal circumstances (“financial adviser” role).

These roles move along a continuum from least to greatest involvement with the consumer. The Task Force is proposing that different obligations should attach to an intermediary depending on the role the intermediary is undertaking.

Having regard to the objectives and identified outcomes for the review, financial products should be given a wide meaning to include investment (including investment property), risk and credit products.

### **Key Issues**

The Task Force has identified the following broad issues affecting the financial intermediary sector:

- *Consumer information related issues:* a general need to increase consumer financial literacy; greater disclosure around financial intermediary conflicts, financial intermediary obligations and consumer rights; financial intermediary standards, roles and history; and available redress mechanisms for consumers;
- *Financial intermediary standards related issues:* the absence of mandatory minimum industry wide standards; variable quality of financial intermediary advice/service and consumer difficulties in understanding and distinguishing between quality standards; the presence of conflicts of interest and the absence of any consistent approach to managing them; and
- *Consumer redress, sanctions and enforcement issues:* variability of dispute resolution coverage and redress for consumers; difficulties removing negligent or unethical financial intermediaries from the industry; and shortcomings in current

disciplinary, complaints and enforcement mechanisms.

These issues may in turn be impacting on overall market confidence in the financial intermediary industry. There are obvious overlaps between these issues, and it is the mix of issues that may have the most significant impact.

The Task Force has not been able to assess the magnitude of some of these issues, nor the significance of particular risks and harms that might arise in relation to a number of them. Because of this, the impacts of any regulatory response need to be carefully considered. Nonetheless, the Task Force does believe there is a case for change.

### **Proposed reform**

The Task Force has identified three broad areas of potential reform:

- *Reform proposal 1:* Enhanced consumer information. This would be achieved through enhanced consumer education initiatives, enhanced intermediary disclosure obligations and, though ultimately outside the strict scope of this review, through enhanced product generator disclosure requirements;
- *Reform proposal 2:* Enhanced redress and enforcement mechanisms and effective sanctions; and
- *Reform proposal 3:* Enhanced ethical and conduct standards.

The Task Force is seeking your views on each of the reform proposals.

### **Reform Proposal 1: Enhanced consumer information**

Enhanced consumer information can make a positive contribution on a number of levels, including enabling an individual consumer to make better decisions about an intermediary or financial product and make comparisons across intermediaries and financial products. It can also encourage greater competition between intermediaries and product generators and contribute to poor performing intermediaries and/or product generators exiting the market, and good quality intermediaries and/or product generators increasing their business, with the overall effect of increasing levels of performance.

### ***Reform Proposal 2: Enhanced redress, enforcement and sanctions***

The Task Force considers that effective and comprehensive dispute resolution procedures are crucial to promoting consumer confidence in the financial intermediary industry. It recognises that under current arrangements, there are some gaps in coverage of self-regulatory dispute resolution mechanisms.

In addition, enhanced disclosure, well understood and consistently applied intermediary minimum standards (see below), and effective and comprehensive dispute resolution procedures need to be backed up with effective enforcement mechanisms and sanctions, including the ability to remove negligent and/or unethical participants from the industry.

### ***Reform Proposal 3: Enhanced standards***

The Task Force preference is for baseline standards to be consistently applied across intermediaries performing similar functions. The Task Force believes this would make a positive contribution to increasing overall quality of financial advice and information for consumers, and facilitating more effective management of conflicts. Some standards will vary depending on the intermediary's function, for example, whether they act in an "information only" capacity, as a product marketer, or as a financial adviser.

### ***Implementation design options***

These reform proposals can be implemented through a range of mechanisms from least to greatest intervention.

- *Option 1: General legal standards:* Under this implementation option, minimum disclosure, redress, ethical and conduct standards would be made mandatory and set out in industry-specific legislation. A variation on this could be a combination of statutory requirements with industry to determine the detail.
- *Option 2: Registration (in addition to Option 1):* A registration regime would require intermediaries to register their details with a governing body. Entry into the industry would be restricted to registered intermediaries.

- *Option 3: Restriction of occupational designations (in addition to Option 1 and possibly Option 2):* Under this option, practicing as a financial intermediary would not be restricted, but the ability to use certain titles would be prohibited unless the person wishing to use the title adhered to certain standards and gave notice through public registration of certain details. A title that might be reserved under this option would be "financial adviser".
- *Option 4: Licensing:* A licensing regime would explicitly prohibit all but licensed people or organisations from offering financial intermediary services. Entry would be dependent upon the person or organisation meeting minimum standards and there would be ongoing competency and conduct requirements. The continuation of the licence would depend on the licensee meeting its ongoing requirements.

We refer to these in this paper as the implementation options. The Task Force seeks your views on these options, including their effectiveness in achieving the outcomes, their costs and benefits, and on aspects of the design you think need addressing.

### ***Transitional arrangements***

Under some or all of these options, consideration would need to be given to what transitional arrangements would be adopted.

Your feedback will contribute significantly to our assessment of the most appropriate responses to the issues we have identified.

