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ICNZ submission on disclosure requirements in the new financial advice regime

Thank you for the opportunity to submit on the discussion paper *Disclosure requirements in the new financial advice regime* ("discussion paper"). ICNZ represents general insurers which insure about 95 percent of the New Zealand general insurance market, including over half a trillion dollars' worth of New Zealand property and liabilities.

This submission is in two parts:

1. Overarching comments
2. Responses to questions in the discussion paper

Please contact Andrew Saunders (andrew@icnz.org.nz or 04 914 2224) if you have any questions on our submission or require further information.

1. Overarching comments

ICNZ supports robust disclosure requirements and welcomes the introduction of commission/incentive related disclosure. We support disclosure requirements that result in useful information being provided to consumers and are workable for subject entities to provide. As such we generally support quality over volume and note the current QFE disclosure arrangements are generally efficient and streamlined.

In general terms we support a principles-based approach being taken in the new disclosure regulations ("regulations"), which will assist in providing for different advice delivery methods (e.g. face-to-face, over the phone and robo-advice), avoid stifling innovation, and allow organisations to provide disclosure in a way that suits their processes and information systems. Whilst we support a principles-based approach it is important the regulations are clear on what must be disclosed. They should not however be prescriptive as to when and how it is disclosed.

We recognise such an approach will need to be supported by guidance material that more specifically addresses the 'when' and 'how' of disclosure in different situations. This guidance should be

developed by government in consultation with industry and other stakeholders. While flexibility is important we also note that where regulatory expectations are less clear there is a greater risk of some providers being more conservative leading to excessively long and complex disclosures while others may try to exploit the uncertainty to provide little disclosure.

It will also be important that when the regulations are finalised regulators support compliance, and once in force they also appropriately monitor and enforce the requirements.

The discussion paper envisages that both the Regulations and the *Code of Professional Conduct for Financial Advice Services* ("the Code") may include disclosure requirements (refer paragraph 38 of the discussion paper). We consider that ideally the two documents will not both address disclosure requirements, but if they do then it is important to ensure the Code dovetails with the primary requirements in the regulations.

ICNZ welcomes an exposure draft of the regulations being consulted on later in the year. The timing of this needs to be considered in relation to the timing of the planned consultation on the draft of the Code. If, as is envisaged in the discussion paper the Code and the regulations both include disclosure related obligations, it would seem useful for stakeholders to be able to consider the exposure draft of the regulations first so that the planned regulatory requirements are clear at the time the draft of the Code is consulted on.

2. Responses to questions in the discussion paper

1	**Do you agree with the objectives that we have identified? Are there any further objectives that the disclosure requirements should seek to achieve?**
	ICNZ agrees with the content of the objectives outlined on page 10 but considers a few extra matters should be included. Objective 4 relates to different channels but there would also be value in explicitly acknowledging in the objectives the differing nature of advice processes subject to the regulations (e.g. from investment planning to simple single product situations) and the need for the disclosure requirements to work effectively and efficiently for all of these. In regard to objective 5, as well as reducing unnecessary compliance costs for providers, it is also important to ensure disclosure obligations don't discourage providers from providing advice (e.g. due to excessive complexity).
The timing and form of disclosure	
2	**What are your views on the proposal that information be disclosed to consumers at different points in the advice process?**
	It is vital that correct information is disclosed to consumers at appropriate and relevant times during an advice process. It is important to remember though that advice processes can take many forms and so the regulations should not specifically require disclosure at different points in the process. In some cases it will be appropriate for information to be disclosed at different times but in others it may be appropriate for a single upfront disclosure as interactions subsequent will not alter the disclosure required.

3	**Will this approach improve the effectiveness of disclosure by increasing consumers' engagement and understanding of the information they receive? Why or why not?**
	This ability to provide disclosure information at different times where appropriate will improve the effectiveness of disclosure because consumers receive information at the time it is pertinent to their decision making (e.g. at the time they decide who to seek advice from or subsequently whether to accept that advice). It also avoids the need to provide what turns out to be unnecessary and irrelevant disclosure information to consumers early in the process or to repeat information.
4	**Should those giving advice be required to tell consumers that they can access general information about the provider or refer to this general information in advertising material?**
	We support the regulations prescribing what information is to be disclosed in the general publicly available information but not setting the specific form for how this information must be disclosed. We note websites can provide a key role in providing up to date disclosure information to all consumers.
The form of disclosure	
5	**If the regulations were to provide flexibility on the form and timing of disclosure, how can they be drafted in such a way to provide certainty to the industry of what is required?**
	We support the concept of enabling flexibility by setting clear requirements regarding the information that needs to be disclosed without being overly prescriptive in the regulations as to when and how. As outlined above in Part 1 of this submission we see a role for guidance material in providing greater specificity in regard to how and when disclosure is made in different situations.
6	**Should a person who contravenes the presentational requirements under the proposal be subject to civil liability or should it be dealt with by an FMA stop order or similar regulatory response?**
	As with the original implementation of the *Financial Markets Conduct Act 2013*, it would be sensible if the FMA could initially take a constructive approach to enforcement of the new regime. At the outset, we recommend that FMA work with willing compliers to ensure requirements are met over an initial 6 – 12 month period. We would suggest that the FMA should have a number of options available that are proportionate to the nature and severity of the contravention. For example, a minor infraction with no potential for material impact to the consumer, should be addressed through something such as a warning. In contrast, deliberately misleading disclosure should attract much stronger penalties.
What information do customers require?	
7	**Do you agree that information relating to the licence, duties and complaints process should be made available to consumers?**
	Yes.

8	**Do you think that the regulations should provide prescribed text for the disclosure of these pieces of information?**
	Overall as outlined above we support the regulations being clear on what should be disclosed with supporting guidance used to provide greater certainty on when and how in different contexts (e.g. different types of products and advice situations etc).
9	**Should consumers be informed of their ability to access a free dispute resolution service when making a complaint? Should this apply to all financial service providers who provide services to retail clients (in which case it might be implemented via the scheme rules rather than in regulations under the Bill)?**
	ICNZ supports consumers being informed of their ability to access a free dispute resolution service when making a complaint. This should occur within the wider context of information about a providers' dispute resolution process (both its internal and external aspects).
Information about the financial advice	
	Limitations in the nature and scope of the advice
10	**Do you agree with the proposal in relation to the disclosure of nature and scope of advice, as set out on page 19? Why or why not?**
	We generally support the proposal in relation to the disclosure of nature and scope of advice as set out on pages 18 and 19 of the discussion paper. We are unclear exactly what is contemplated in paragraph 52 of the discussion paper in terms of individual adviser level disclosure. With regard to nominated representatives we consider that the level for disclosure sits at the Financial Advice Provider ("FAP") level as the individual nominated representatives operate within the systems and constraints of the FAP.
11	**How can the regulations ensure that consumers receive an accurate indication of the extent of the market that can (and will) be considered?**
	ICNZ agrees it is important consumers have a clear understanding of the type of service that the individual or firm giving advice can provide and the extent of the relevant market that may be actively considered in doing this. We therefore generally support the proposal in relation to the disclosure and scope of advice set out in the three bullet points below paragraph 53. We do however consider the focus of this is better placed on outlining what the scope of advice covers rather than what it doesn't. It is also important to recognise and provide for different contexts. For example, where a consumer phones an insurer with the purpose of securing insurance for a vehicle, the nature and scope of the advice (general insurance and that providers products) are essentially determined by the consumer before the conversation begins. ICNZ supports requiring disclosure of the types of arrangements detailed in paragraph 51 of the discussion paper.

	Costs to client
12	**Do you agree with the proposal in relation to disclosure of costs to clients, as set out on page 20? Why or why not?**
	Yes. We agree it is fundamental consumers are aware of fees that a FAP charges for the advice they give and any expenses that the consumer might be required to pay in the event of a cancellation, including any clawback commissions. It is necessary to recognise though that in some cases it may not be possible to precisely define potential costs, for example explaining (at the time of providing advice) what could be clawed back (and by whom/against whom), in which it may be appropriate to require a fair and reasonable estimate, or the process that would apply.
13	**What role, if any, should the disclosure regulations play in ensuring that consumers are aware of the other fees that they might be charged should they follow the advice (e.g. bank fees, insurance premiums, management fees)?**
	ICNZ supports measures to ensure consumers are aware of all the costs they might incur in following advice. We question the characterisation of "insurance premiums" as an "other fee" in Question 13 as premiums are the price paid for an insurance policy in exchange for the cover the policy provides. An insurance premium is not a type of fee.
	Commission payments and other incentives
14	**Do you agree that commissions and other incentives should be disclosed in more general terms early, followed by more detailed disclosure later in the advice process?**
	ICNZ supports the disclosure of commissions and other incentives. With regard to how and when this disclosure is made, we consider flexibility is important to ensure this can be constructively and efficiently done during the advice process. It is important to recognise the advice process varies, for example it can sometimes involve multiple face-to-face meetings over days/weeks but in others could all take place over the course of a single relatively brief phone call, or online. As the relevant commissions or other incentives, if any, may be identifiable from the beginning of the advice process in some situations then the regulations should not specifically require more detailed disclosure later when it can all take place from the beginning. Please also note our related comments in response to Questions 15 and 16 below.
15	**If the regulations were to include a materiality test that would determine the commissions and incentives that needed to be disclosed, what would an appropriate test be?**
	Whilst ICNZ can see the appeal of including a materiality test as a means for simplifying the information that is disclosed, the subjectivity involved would be problematic in various ways and so we have concerns with using this to determine which incentives have to be disclosed to consumers. Subjectivity is problematic both in the sense that different FAPs might make different judgments on whether to disclose similar information (creating inconsistency) and the more fundamental issue that materiality is very subjective. Whether an incentive is material in practice will depend on both the nature and scale of the incentive and the situation of the

individual/s involved. Consumers' perception of the materiality of similar incentives may also differ.

It is also important to recognise the main reason for disclosure of incentives is to reveal conflicts of interest and the context of an intermediary offering varying products with differing incentives attached is different in nature to a salaried employee of a provider offering only that company's products and with a small performance-based component or bonus.

Where an adviser is offering multiple financial product provider's products and directly receiving commissions/incentives - full disclosure of the level of commissions from each financial product provider and any soft incentives is logically required and may only be possible to be disclosed at the point of recommending specific products. On the other hand, where FAP's employ advisers, but the adviser receives no direct commissions or soft incentives from the placement of business – disclosure as to the fact that they are an employee and might receive certain types of incentives would seem appropriate and may be able to occur at the commencement of the process (because it would not change).

If a materiality test was to be included in the regulations the following matters would need to be carefully considered:

- How to provide for the difference contexts of advisers who are not employed by a financial product provider and are able to offer multiple providers' products and advisers who are employees or tied agents of a financial product provider.
- How materiality would be determined at the individual, team/group, and the FAP level in relation to different types of incentives - consumer perceptions of materiality and the advice context also vary substantially.
- Making a materiality test sufficiently clear to avoid inconsistent application.

Please also note our comments below in regard to Question 17.

Options for how to disclose commissions and other incentives

16 **Is it necessary for the disclosure regulations to be prescriptive regarding the disclosure of commissions and other incentives? If so, why?**

ICNZ supports consumers being made aware of the differing commission rates an adviser can receive between different products/providers.

We don't necessarily believe it is necessary for the regulations to be prescriptive regarding the disclosure of commissions and other incentives but they will need to set very clear expectations. This will be necessary to reduce uncertainty of application for subject entities and to ensure consumers receive the information required to help them decide whether to seek advice from a particular person, whether to accept any advice given and whether conflicts are being appropriately managed.

We expect supporting guidance will be required in this area to address the variety of situations that might occur in practice in the different sectors and situations subject to the regime and note the usefulness of the case studies provided in the discussion paper.

17 **Which of the options (as set out in pages 21-22) do you prefer? What are these costs and benefits of the options?**

Consistent with our answer to Question 16 above we consider that taking a principles-based approach to the regulations is the best of the three options outlined on pages 21-22 but

recognise further detailed work will be required. Regulatory requirements in this area need to be sufficiently flexible to account for different arrangements and structures and the evolution of these whilst also being sufficiently clear to avoid under or over compliance. It is important to remember that commissions, soft commissions, referral payments, other incentives and performance targets come in many and varying forms.

Effective disclosure of commissions/incentives so as to enable consumers to understand conflicts of interest may involve an element of all three options. Simply disclosing that commissions might be received seems insufficient, whilst at the other end of the spectrum it could be counter-productive or impractical to specify the exact dollar amount of a commission or the details of all the performance targets that might be relevant to the individual providing the advice, their team, or at corporate level. Some sort of middle ground may most usefully serve the policy objectives of informing consumers whilst being practical for providers, but as noted above in regard to the concept of a materiality test we understand successfully providing for this won't be easy.

Whilst supporting a principles-based approach we recognise that Option 3 runs the risks of being applied in a way that is overly open to interpretation. This could mean that some entities provide insufficient disclosure while others may take a conservative approach (i.e. excessive disclosure) to ensure they are complying, rather than a more pragmatic customer-friendly approach. As outlined above providing supporting guidelines will be important.

Amongst Options 1 and 2, neither would to be suitable in itself and we note that commissions and incentives can be structured in different ways and include elements of percentage rates and specific numbers (i.e. dollar amounts).

With regard to Option 1, commission rates are easily understood by consumers and would often be more straightforward and workable to communicate for entities (i.e. it could be standardised if shown in % terms.) than disclosure in dollar terms as per Option 2. Percentages could potentially be shown in ranges rather than specific numbers but these ranges would need to be sufficiently narrow to be useful (e.g. "20% - 30%" might be useful information for a consumer whereas "0% - 100%" wouldn't be).

While Option 2 would likely provide the most easily understandable information to the consumer it would be complex to apply in practice. For instance, with an insurance product it might not actually be known until the sum insured was confirmed (or later), making it more challenging and complex to apply than Option 1. There also seems to be a risk that providing specific dollar values of incentives functions as a distraction for some consumers and potentially risks introducing confusion with other dollar values being discussed with regard to the advice or financial product/s.

Other conflicts of interest and affiliations

18	**Do you agree that those giving financial advice should be required to disclose all relevant potential conflicts of interest?**
	Yes. It would be inconsistent and incomplete to require disclosure of commission/incentive whilst not requiring disclosure of other sorts of conflicts or affiliations.

19	**Are there any additional factors that might influence financial advice that should be disclosed?**
	In the insurance space, brokers often operate under binding authorities but may not have authority to provide advice on behalf of the insurer. In this context it would seem appropriate for the adviser to disclose that while it may provide some services to the product provider (in the insurance context, limited underwriting services), it does not provide financial advice on the product provider's behalf. This would help provide clarity to the consumer on where their rights of recourse sit, and from the advisers' perspective would help them manage their duty to prioritise clients' interests.
20	**Should these factors be disclosed alongside information about the conduct and client care duties that financial advice will be subject to (as discussed on page 17)?**
	We don't have specific comments to make on this aspect but note that when disclosure of these factors is relevant/appropriate may vary depending on the advice process.
Information about the firm or individual giving advice	
	Details of relevant disciplinary history
21	**Do you agree with the proposed requirement to disclose information relating to disciplinary history and bankruptcy or insolvency history? Why or why not?**
	We agree that that nominated representatives should not be required to disclose relevant insolvency or bankruptcy issues as, unlike AFAs, they are following the FAP's processes and limitations and so a nominated representative's recent insolvency or bankruptcy history should not be relevant to how much confidence a consumer should place on the advice. We also consider that in relation to disciplinary issues, an FAP should not have to provide the relevant disciplinary history of an individual nominated representatives if they are employed by a FAP. In contrast, we consider that in the case of AFAs it may make sense for them to, as they currently do, disclose information relating to their personal history in terms of disciplinary action, bankruptcy or insolvency. Thought may need to be given as to exactly what is relevant for disclosure and whether a threshold for this would be appropriate. Overall for corporate entities it is appropriate and much more workable for corporate level disclosure rather than potentially an individualised level for each employee. FAP's are responsible for the activities and actions of their nominated representatives and so it is appropriate for disclosure to occur at that level. We note the approach we advocate could require a distinction between investment planning and financial advice. This would nonetheless be consistent with the approach being contemplated for the Code.

22	**Should the disclosure of information relating to disciplinary history and bankruptcy or insolvency history also apply to the directors of a financial advice provider?**
	We note that directors subject to the *Insurance (Prudential Supervision) Act 2010* are already required to meet "fit and proper" standards issued by the Reserve Bank of New Zealand. The added value of requiring the proposed disclosure is not clear in this situation but may be appropriate in situations where there is no independent authority already monitoring Directors on a fit and proper basis.
23	**Should financial advice providers also be required to disclose if they have been found to have contravened a financial advice duty?**
	We would suggest that this may have a place but the imposition of this sort of requirement needs to be carefully considered in terms of the value it would provide and whether it would be proportional. For example we would question whether it would be appropriate to require a minor one-off infraction to be disclosed. In contrast, in the case of a sustained history of infractions or deliberately misleading disclosure, this may be appropriate for disclosure.
Additional options	
	A prescribed summary document
24	**Do you think that a prescribed template will assist consumers in accessing the information that they require?**
	As outlined above we generally advocate a more principles-based, rather than prescriptive, approach. There may be a role for more specific presentational expectations to be set through guidance material, whilst still allowing flexibility and innovation in implementation. We are also cognisant of the limitations of this noted in the discussion paper in relation to online robo-advice or advice over the phone.
25	**How could a prescribed template work in situations when advice is not provided in person (i.e. if it is provided over the phone or via an online platform)?**
	As noted above we don't considered a prescribed template would be a good approach in relation to advice provided over the phone or online. We recommend keeping the requirements principles based and where necessary providing more specific examples in guidance that are tailored to different advice settings.
	Requirements for disclosure provided through different methods
26	**Should the regulations allow for disclosure to be provided verbally? Why or why not?**
	Yes, this is amongst other things necessary to facilitate advice being able to be provided over the phone, which is a key delivery model for providers and consumers.

27	**If disclosure was provided verbally, should the regulations include any additional requirements?**
	Verbal disclosure can an effective form of communication but we recognise following it up with written disclosure could be appropriate and convenient for some consumers. In situations where disclosure is provided over the phone then customers should be able to request it in writing, particularly if it is not available on a website, ensuring certainty of disclosure by FAPs, particularly if the verbal disclosure is not scripted or pre-recorded.
	Requirements for financial advice given through different channels
28	**Should the regulations provide for any additional requirements that would apply when advice is given via a robo-advice platform or over the phone?**
	Whilst phone-based advice is not face-to-face, it still involves a consumer directly dealing with a person and so whilst recognising the context it can potentially be treated in much the same way as offering advice face-to-face. A robo-advice platform is fundamentally different as there is no direct person-to-person interaction. Notwithstanding these differences and regardless of the channel/s used, the matters that are required to be disclosed should be the same, but the regulations must allow flexibility in how to recognise the use of one or more of these channels during an advice process.
29	**Do consumers require any additional information when receiving financial advice via an online platform?**
	Note our comments in relation to Question 28 above.
	Disclosure when replacing a financial product
30	**Should those advising consumers to replace financial products be required to provide a prescribed notification? If so, what should a prescribed notification contain?**
	We don't consider there is a general need for a prescribed notification in all situations involving the replacement of a financial product. Should such a requirement be imposed, it should only be in those situations where particular risks associated with the replacement of that type of financial product justify it. For short-tail insurance products (e.g. general insurance[1]) we do not see a rationale for regulations to impose a prescribed notification associated with replacement. For long-tail products (e.g. life, disability, health insurance) where there is a clear risk of the consumer being put in a worse position by changing products, we agree there is a rationale for requiring a specific notification in relation to replacement (as noted in paragraph 80).
31	**Should this apply to the financial advice given on the replacement of all financial advice products?**
	As outlined above in relation to Question 30 we do not consider this should apply to the financial advice given on the replacement of all financial advice products.

[1] For example home and contents, motor or liability insurance.

	Information to existing financial advice clients
32	**Should the regulations provide for reduced disclosure requirements for existing clients? If so, in what situations should it apply and what information should consumers receive?**
	As part of efforts to ensure disclosure is not unnecessarily burdensome for consumers or FAPs we see merit in the concept of reduced disclosure requirements for existing clients as an option. We also recognise that general insurance contracts are renewable on anywhere from a monthly to annual basis and so if there are any material changes these can be communicated at the time of renewal. Existing customers could be referred to the FAP's website to see the latest version of the disclosure information. We also recognise choosing to undertake full disclosure for existing clients could be more straightforward for some FAPs.
33	**Should there be a limit on the length of time that this relief would apply?**
	Repeating the same information appears to have little value although we agree there is a need to update consumers when previously disclosed information has changed or the scope of advice is meaningfully different. We haven't identified any particular time period that would be appropriate.
	Transitional requirements
34	**Is it necessary for the disclosure regulations to provide a transitional period for the industry to comply with the new requirements beyond this nine-month period?**
	Many of our members have indicated comfort with the proposed nine-month transition period although some have suggested a longer period would be appropriate.
35	**Should the regulations include specific transitional provisions for AFAs authorised to provide personalised DIMS under the FA Act?**
	No comments – not relevant to general insurers.
	Disclosure to wholesale clients
36	**Should the regulations require the provision of additional information regarding the wholesale designation in some circumstances? If so, when would it be appropriate for this to take place?**
	We agree it is important for wholesale clients, and FAPs, to be clear as to whether a client is being treated as such. Notwithstanding this in our view any provision of additional information regarding the wholesale designation in some circumstances needs to be focussed on addressing a specific issue, and be straightforward to comply with, to avoid imposing unnecessary complexity and cost. We would recommend that any requirements of this kind should to be required to be carried out on a one-off basis at the outset of the relationship and at the entity level (if dealing with a corporate client, for example).

37	**Do you have any alternative suggestions for how the regulations could ensure that wholesale clients are aware of what it means to be deemed a wholesale client?**
	No additional comments beyond those made above in relation to Question 36.

Conclusion

Thank you again for the opportunity to submit on the discussion paper. If you have any questions, please contact our Regulatory Affairs Manager on (04) 914 2224 or by emailing andrew@icnz.org.nz.

Yours sincerely,

Andrew Saunders
Regulatory Affairs Manager