FINANCIAL SERVICES FEDERATION

The Financial Services Federation ("FSF") is grateful for the opportunity to comment on the draft Financial Services Legislation Amendment Bill ("the Bill") and proposed transitional arrangements.

By way of background, the FSF is the industry body representing responsible and ethical finance and leasing providers in New Zealand. The FSF has over fifty members and affiliates providing first-class financing, leasing, and credit-related insurance products and services to over 1 million New Zealand consumers and businesses. The FSF's affiliate members include internationally recognised legal and consulting partners. A list of the current membership is attached to this submission as Appendix "A".

As responsible credit providers, FSF members take their compliance obligations extremely seriously and are always willing to comply with all relevant legislation and regulation in order to ensure that New Zealand has a well-functioning economy and markets and that adequate and appropriate consumer protections exist. However, the FSF believes that regulation should always be developed with the appropriate balance of providing consumer protection and ensuring that business is not over-burdened with unnecessary or competing compliance obligations.

FSF members who are consumer credit contract providers have always believed that the provisions of the Financial Advisers Act ("FAA") applied to them in respect of the way in which they interact with their customers in the provision of credit. The fact that consumer credit is described in the current Act as a category 2 product and that the definition of financial advice is described as making a recommendation or giving an opinion in relation to acquiring or disposing of (including refraining from acquiring or disposing of) a financial product seems to FSF members to make that clear.

FSF members are therefore either Qualifying Financial Entities or they have registered their customer facing staff (RFA's). It is however the FSF's belief that this course of action has not been taken by all credit providers and that there are many consumer credit providers who have taken no action at all under the FAA as it currently stands – and who have suffered no penalty from regulators as a consequence.

The FSF believes that this is an anomaly that could and should be clarified by the Bill by using it as an opportunity to carve out consumer credit providers from the scope of the Bill.

At the time the FAA was enacted the inclusion of consumer credit contracts and the way in which "advice" is provided to consumers around the suitability and affordability of credit was

opposed by the FSF, even if it seemed to others to be reasonable consumer protection. However in the period since then the amended Credit Contracts and Consumer Finance Act 2003 ("CCCFA") introduced the Lender Responsibility Principles in 2015 and provided the guidance to credit providers as to how to meet these through the Responsible Lending Code. The situation now is therefore considerably different and the FSF even more strongly believes that all necessary consumer protections for the way in which "advice" is provided by consumer credit contract providers exists in the CCCFA.

The FSF is therefore disappointed that a consumer credit contract is still included in the draft Bill as a financial advice product and sincerely hopes that this will be rectified before the Bill is enacted.

From discussions with Ministry officials, the FSF understands that the key concern that has led to this continued inclusion is with regard to the situation where a broker has access to a range of consumer credit contract products with which to meet a consumer's need and may be influenced by the level of commission paid for the sale of a particular product rather than meeting the principle of putting the client's interests ahead of his/her own.

The FSF also understands that the Ministry does not necessarily see the provision of consumer credit contracts directly to consumers by a credit provider or lender and the associated activities of their staff as involving the provision of financial advice.

If that were correct then providers of consumer credit contracts and their staff would not be covered within the scope of the new Bill. However, the FSF doubts that this is correct as the Bill is presently drafted and accordingly strongly submits that the position should therefore be made more clear by adding the following to the list of activities in clause 6 of Schedule 5 of the Bill that do not constitute "financial advice":

> *"(a) providing credit under a consumer credit contract;*
> *(b) a person acting as an employee of a provider of consumer credit contracts in respect of credit provided by their employer;"*

Should this suggestion be adopted, the FSF believes that any misunderstanding as to whether consumer credit providers and their staff are providing "advice" to consumers in the course of meeting the lender responsibility obligations will be removed.

However, where consumer credit is being provided to consumers via a broker who may be influenced more by the amount of commission they are receiving to sell a particular product than they might be by putting their clients' interests ahead of their own, under what the FSF has just suggested, it would be clear that the provisions of the new legislation will apply to brokers – they do not provide credit themselves and brokers are not employees of credit providers.

The FSF would also take this argument a step further and suggest that the provision of credit-related insurance in the course of providing a consumer credit contract should be treated in the same way. Therefore similar clarification should be made in the new legislation that states that where credit-related insurance is being offered to protect consumers taking on consumer credit (or the asset they are purchasing with that credit), the provisions of the CCCFA and the guidance contained in the Responsible Lending Code with respect to the offering of credit-related insurance should apply rather than the new legislation.

That can best be achieved by also adding providers of credit-related insurance and their staff to the list of exempt activities in clause 6 of Schedule 5 of the Bill as follows:

> *"c) providing cover under a policy of credit-related insurance;*
> *d) a person acting as an employee of a provider of credit-related insurance that is provided by their employer."*

and then adding to the Bill a definition of "credit-related insurance", giving that term the same meaning as in the CCCFA.

A further point the FSF would make before answering the questions raised in the Consultation Paper is that one of the stated objectives of the review of the FAA that has led to the writing of this Bill, is that of removing some of the complexity of the current regime.

Continuing to regulate consumer credit and credit-related insurance providers under this Bill (as well as doing so in different terms under the overlapping requirements of the CCCFA) does nothing to assist in achieving this objective. Instead, it helps to perpetuate the confusion for consumers in determining what legislation applies to consumer credit providers. Effectively consumer credit and credit-related insurance providers will be regulated twice for the same activity which is something that Government and policy makers should be trying to avoid.

Further, the FSF submits that carrying over the inclusion of consumer credit and credit-related insurance providers into the scope of the Bill, risks undermining all the good work carried out by officials on providing adequate and appropriate consumer protections under the CCCFA.

FSF members who are QFE's or who have registered some or all of their employees, believing that they are covered by the current scope of the FAA, also report that they have never had any customer enquiry about their status under the FAA as the public perception is that they are not receiving financial advice from a consumer credit contract or credit-related insurance provider.

With the above submission in mind therefore, the FSF does not propose to answer every one of the questions raised in the Consultation Paper accompanying the draft Bill, but only those which apply directly to the FSF and its members. The FSF will also make comments on points raised in the Consultation Paper that are of concern to the FSF and its members but about which a specific question has not been raised.

3. Do you have any other feedback on the drafting of Part 1 of the Bill?
As previously stated, the FSF strongly submits that the exclusions in clause 6 of Schedule 5 of the Bill need amendment as suggested above to provide clarity that providers of consumer credit contracts and providing cover under a credit-related insurance are not covered by the scope of the Bill – and that only those advisers who advise on a range of consumer credit contracts provided by others would be.

4. Do you have any feedback on the drafting of Part 2 of the Bill?
Other than to repeat that the FSF strongly believes that credit contract and credit-related insurance providers should be exempt from the scope of the Bill and therefore from the licensing requirements, the FSF has no further comment to make on Part 2 of the Bill.

7. Do you support extending the client-first duty to providers who do not provide a retail service (i.e. those who only advise wholesale clients)? Why or why not?
With regard to the duties that apply when the service is not a retail service, the FSF would submit that this is a further area where the provisions of the CCCFA overlap with those of the Bill in an unhelpful way as they apply to consumer credit and credit-related insurance providers. Specifically the Bill is describing a distinction between clients who are retail as opposed to wholesale and the way in which each should be treated.

The CCCFA however distinguishes between consumers and non-consumers and regulates the way in which each should be treated. This is a further area where the two overlapping pieces of legislation create unnecessary complexity and confusion and add no value to consumers. It is also a further reason why consumer credit contract and credit-related insurance providers should be regulated solely by the CCCFA in relation to the way in which they provide advice to their customers.

8. Do you have any other feedback on the drafting in Part 3 of the Bill?
Under the discussion of the key term: when a person gives financial advice, the Consultation Paper talks about the fact that providing discretionary investment management services (DIMS) will no longer be regulated as financial advice as anyone providing DIMS will need to operate under an FMC Act DIMS licence thus avoiding regulating DIMS in two separate ways.

The FSF would question why, if it is considered desirable to avoid double regulation of DIMS providers why does that not also apply to the double regulation of consumer credit contract and credit-related insurance providers? (As above, consumer credit contract and credit-related insurance providers are presently regulated by the FAA and by the CCCFA).

There is considerably more complexity and risk to consumers of being mis-sold or receiving inappropriate advice around a DIMS than there would be in providing a consumer credit contract or credit-related insurance product.

The FSF submits that, if the clarity around consumer credit contract and credit-related insurance providers being excluded from the new legislation is not provided in the way

suggested above, consumer credit contract and credit-related insurance providers will be unduly penalised by being double-regulated in the following ways:

a) Being subjected to the obligations of two separate pieces of legislation for the same function: the new Financial Services legislation and the CCCFA;
b) Being bound by two separate Codes of behaviour for the same function: the new Code to be developed under the new Financial Services legislation and the Responsible Lending Code;
c) Being regulated by two separate regulators for the same function: the FMA under the new Financial Services legislation and the Commerce Commission under the CCCFA (and in the case of credit-related insurance providers, the Reserve Bank of New Zealand).

The FSF believes that this is inherently unfair as well as being inefficient and adding unnecessary costs to affected businesses. Nor is there any benefit to consumers in this double-regulation as they are already adequately protected by the CCCFA but of course they would ultimately bear the burden of the costs being passed on to them.

The FSF suspects that double-regulation of the same activity by consumer credit and credit-related insurance providers was also probably not intended by policy makers or regulators and suggests it is therefore imperative that the clarity sought by FSF is delivered before the draft Bill proceeds further.

Further the FSF would suggest that the two separate regulatory regimes are entirely unnecessary in the context of consumer credit contract and credit-related insurance providers for the following reasons:

a) It is unlikely that any prosecution against such providers about the way in which they were providing advice to consumers would result from the new Financial Services legislation. The way in which this advice should be provided is clearly set out in the Lender Responsibility Principles of the CCCFA and any failure to comply with these would be dealt with under that Act;
b) The way in which consumer credit and credit-related insurance providers are expected to behave when providing advice to consumers is clearly described in the guidance provided in the Responsible Lending Code and the FSF therefore hopes that the new Code written under the new Financial Services legislation would not apply to them as well;
c) The FMA has previously stated publicly that it had no wish to regulate the provision of consumer credit and that they had a clear understanding with the Commerce Commission that any concerns they may have in this area would be passed to the Commission for them to investigate and take enforcement action if required. Further, in the experience of FSF members who are currently QFE's and therefore subject to potential scrutiny of the FMA, none of them have had any material contact from the FMA as to the way in which they operate – possibly because this is outside of the expertise of the Authority.

Finally, the FSF also submits that a precedent exists for appropriate carve-outs of certain sectors from Financial Markets Conduct or securities law. This being the offer and purchase of retirement villages as this is specifically legislated for under the Retirement Villages Act.

9. What would be the implications of removing the "offering" concept from the definition of a broker?
The FSF submits that the removal of the "offering" concept from the meaning of a broker is not of concern.

10. Do you have any other feedback on the drafting of Part 4 of the Bill, for example any suggestions on how the drafting of broker provisions could be simplified or clarified?
The FSF refers to the comments made on page 2 of this submission with regard to the treatment of brokers under the new legislation.

13. Is the designation power for what constitutes financial advice appropriate? Are there any additional/different procedural requirements you would suggest for the exercise of this power?
The FSF is comfortable with the intent of clause 46 in Part 5 of the Bill to allow for the FMA to be granted a mechanism to respond if providers are found to be purposefully avoiding the regulatory perimeter through activities that are advice in substance but not form provided that it is absolutely clear that the "advice" that relates to the provision of consumer credit contracts or credit-related insurance is not within scope of the Bill.

Should this sensible premise not prevail and the provision of consumer credit contracts or credit-related insurance is not removed from the scope of the Bill, the FSF would absolutely not support the FMA having that power over such providers. The FSF does not believe that the FMA has sufficient expertise in the regulation of such providers to be able to exercise it appropriately.

15. Do you have any other feedback on the drafting of Part 5 of the Bill?
The FSF has no feedback on the drafting of Part 5 of the Bill other than to say that clarification is required to ensure that the provision of consumer credit contracts and credit-related insurance is not a financial advice service whether or not they are provided to retail or other types of clients.

16. Does the proposed territorial application of the Act set out above help address misuse of the FSPR? Are there any unintended consequences? How soon after the passing of the Bill should the new territorial application take effect?
The FSF supports the proposed territorial application of the Act to help address misuse of the FSPR and can see no unintended consequences of applying this. On the basis that the proposed changes have been signaled well in advance of the Bill being enacted, the FSF can see no reason why this should not take immediate effect upon enactment.

All FSF members who are required under the law to be so are registered on the FSPR.

17. Do you support requiring further information (such as a provider's AML/CFT supervisor) to be contained on the FSPR to help address misuse?
The FSF would support a requirement for the FSPR to also include a provider's AML/CFT supervisor to help address misuse.

18. Do you consider that other measures are required to promote access to redress against registered providers?
The FSF fully supports the concept of providing access to dispute resolution for New Zealand retail customers dealing with providers who may not have a place of business in New Zealand.

The FSF is aware of online consumer credit providers based in Australia and other jurisdictions for example, offering such products to New Zealand consumers without either being registered on the FSPR or belonging to a disputes resolution service. Apart from the lack of protection this affords to New Zealand consumers, particularly to vulnerable borrowers, FSF members are also concerned about the inequity of providers being able to offer products into New Zealand without having to comply with the same legal obligations as New Zealand-based providers.

The FSF is unsure whether there is any benefit to anyone least of all consumers in the legislation providing that dispute resolution schemes may refuse or terminate membership if a provider is not engaging with the scheme as required or if the scheme is not satisfied that the provider will engage with the scheme. It would seem that this is unnecessary given that the disputes resolution schemes are themselves licensed and all have constitutions that describe how they should be run including how they might terminate membership and providing for them to refuse membership to a provider at their discretion.

20. Do you support clarifying that schemes must provide information to the FMA if they believe that a provider may be involved in conduct that constitutes breach of relevant financial markets legislation?
The FSF supports this clarification in principle with the proviso that, with regard to the provision of consumer credit contracts, any such apparent breaches should be referred to the Commerce Commission rather than to the FMA.

23. Do you have any other feedback on the drafting of Schedule 1 of the Bill?
The FSF notes with extreme concern that expressions of interest in positions on the new Code Working Group have already opened and will close by 7 April which is long before this Bill is likely to be enacted. It is likely that the Code Working Group might therefore commence work on the new code of conduct before the Bill is passed, particularly if the scope of the Bill at that stage still included providers of consumer credit and credit-related insurance contracts. Should such providers not receive the exemption the FSF believes is right and proper, it would be of significant concern that a Code Working Group was developing a code of conduct for the way in which they provide "advice" to their customers without any representation on such a

Committee from anyone experienced in the responsible provision of consumer credit contracts and credit-related insurance products or an understanding of how advice is provided to consumers in these instances.

The FSF strongly submits that consideration of the composition of the Code Working Group should not be decided until the Bill has passed and it is absolutely clear to whom the Bill will apply.

Further, and independently of that, it would also be a concern that the Code Working Group might be engaged on a Code that applied to consumer credit contracts or credit-related insurance when there is of course a perfectly good and recently written such Code in existence already – namely the Responsible Lending Code under the CCCFA.

25. We understand that some lenders consider that they may be subject to the financial adviser regime because their interactions with customers during execution-only transactions could be seen to include financial advice. Does the proposed clarification in relation to execution-only services help to address this issue?

The FSF refers to everything that has been said previously in this submission in support of its contention that the Bill should make it absolutely clear that lenders (or providers of consumer credit contracts) and credit-related insurance providers are not covered by the scope of the Bill as the "advice" that is provided in the course of providing a consumer credit contract or a credit-related insurance product is regulated by the CCCFA.

The FSF further strongly contends that the provisions of the CCCFA mean that if a consumer credit contract or credit-related insurance product were provided on an "execution-only" basis that would be in breach of the Lender Responsibility Provisions of the CCCFA.

In the opinion of the FSF, an "execution-only" transaction is one where a product is presented to a consumer with no advice as to its suitability for that particular consumer and the consumer makes up his or her own mind as to whether or not to take it.

Further it is not possible for consumer credit contracts or credit-related insurance products to be provided on this basis as the Lender Responsibility Principles of the CCCFA require providers of such products to ensure that the product being provided meets the consumer's goals and objectives, can be repaid without causing substantial hardship and that the consumer is making an informed decision before taking the product. To not do so, would result in a breach of that piece of legislation.

As the FSF has previously stated, however, there are many consumer credit providers who do not believe that they provide "advice" when offering such contracts and who therefore have chosen not to comply with the provisions of the FAA. To the FSF's knowledge they have done so without incurring any penalty for having failed to comply with the FAA.

In order to address that anomaly, the FSF submits in the strongest possible terms, that given there is no such thing in the FSF's opinion, as an "execution-only" consumer credit contract (or indeed a credit-related insurance) transaction, the Bill must provide absolute clarity that the provision of consumer credit contracts or credit-related insurance is not within the scope of the Bill.

If regulators believe that the way in which consumer credit contracts or credit-related insurance products are provided whilst still meeting provider obligations under the CCCFA does constitute an "execution-only" transaction and is therefore not "financial advice", the FSF submits that rather than leave this to the very real prospect of misinterpretation, then absolute clarity that this is the case should be included in the Bill. This could be achieved by including consumer credit contracts and credit-related insurances as exclusions in clause 6 of the new Schedule 5 of the FMC Act, as has been suggested on page 2 of this submission.

29. Does the wording of the required minimum standards of competence, knowledge and skill which "apply in respect of different types of advice, financial advice products or other circumstances" adequately capture the circumstances in which additional and different standards may be required?

The FSF submits that most individual loans staff working for consumer credit contract providers learn the skills and judgment required to become a good lender in-house. Each provider has its own credit policy for example which defines the level of risk they are prepared to take when considering consumer credit applications, what criteria consumers have to meet in order to have an application for consumer credit approved and what discretion (if any) the individual lender holds within this policy (among other things). These skills and competencies can only be learned in an in-house situation.

Therefore the FSF would have some concern, should consumer credit providers not be explicitly carved out of the scope of the Bill, if the FMA were to be the arbiter of whether these programmes are sufficient to meet whatever code standards might exist around the provision of consumer credit contracts. With the greatest of respect to both the FMA and the Code Working Group, neither of these bodies is likely to be competent to decide what an individual lender's credit policy should look like.

What is relevant here is whether individual lenders working for a consumer credit provider meet their employer's requirements for discharging their obligations under the CCCFA. If anyone was to determine whether this is the case, the FSF submits that this should be the Commerce Commission but certainly not the FMA.

At the risk of repetition, the real point here is that it is simply not necessary for this proposed Code to address these subjects in relation to consumer credit or credit-related insurance: they have already been fully and recently addressed by the Responsible Lending Code under the CCCFA, and it is plainly not desirable for two statutory Codes to address the same subject.

In any event it is virtually impossible for FSF to make any meaningful comment as to what the Code may have to say with regard to required minimum standards of competence, knowledge and skill before the Code is actually written.

32. Do you have any other feedback on the drafting of Schedule 2 of the Bill?
With regard to enforcement and penalties against consumer credit contract or credit-related insurance providers not discharging their obligations to consumers to provide the appropriate advice as to product suitability, ability to repay without incurring substantial hardship and to help them make an informed decision about entering into the loan agreement, the FSF submits that these are adequately already covered by the CCCFA in Part 4 of that Act.

To subject consumer credit contract and credit-related insurance providers to the possibility of further disciplinary proceedings and penalties via the financial services legislation would, in the opinion of the FSF, place consumer credit contract and credit-related insurance providers in a situation of double jeopardy. This is of course highly unfair and unnecessary and would be eliminated by the clear exemption of consumer credit contract and credit-related insurance providers from the scope of the Bill.

It should further be noted that under the Financial Service Providers (Registration and Dispute Resolution) Act 2008, all consumer credit contract and credit-related insurance providers are registered and belong to an approved disputes resolution scheme which provides consumers with a means to make a complaint against them if their internal disputes resolution process fails to reach a resolution of the customer complaint. Therefore the FSF submits that the consumer protection mechanism for making a complaint to an independent disputes resolution scheme already exists for consumer credit contract and credit-related insurance providers.

35. Is six months from the approval of the Code of Conduct sufficient time to enable existing industry participants to shift to a transitional licence?
The FSF submits that it is impossible to say whether six months from the approval of the Code of Conduct would provide existing industry participants with sufficient time to shift to a transitional licence (were they required so to do) without having first seen and understood the implications on providers of the contents of the Code of Conduct.

In any event, as has been said in everything that goes before this, consumer credit contract and credit-related insurance providers should not be included in the scope of the Bill and would therefore not have any transition to undergo.

48. Do you have any other comments or suggestions regarding the proposed transitional arrangements?
The FSF has no comment to make about the proposed transitional arrangements (other than what has already been said in answer to question 35 above), because the FSF repeats its central position that consumer credit contract and credit-related insurance providers should not be covered by the scope of this legislation and, on the basis that this sensible premise prevails,

consumer credit contract and credit-related insurance providers would not be part of the transition process.

The FSF would be pleased to provide any further comment or input that would be helpful in the process of formulating this legislation. Please do not hesitate to contact us if we can be of any further assistance.

Thank you again for the opportunity for the FSF to submit on this Bill.

Lyn McMorran
EXECUTIVE DIRECTOR

Appendix "A"

FSF Membership List as at 1st November 2016

Debenture Issuers - (NBDT) Non-Bank Deposit Takers	Vehicle Lenders	Finance Company Diversified Lenders	Credit Reporting Other	Insurance	Affiliate Members
<u>Rated</u> Asset Finance (B) Fisher & Paykel Finance (BB+) <u>Non-Rated</u> Mutual Credit Finance Gold Band Finance Limited	BMW Financial Services Branded Financial Services Community Financial Services Go Cars Finance Ltd European Financial Services Mercedes-Benz Financial Services Motor Trade Finance Nissan Financial Services NZ Ltd Onyx Finance Limited Toyota Finance NZ Yamaha Motor Finance <u>Leasing Providers</u> Custom Fleet Fleet Partners NZ Ltd LeasePlan NZ Ltd ORIX NZ SG Fleet	Advaro Limited Avanti Finance Caterpillar Financial Services NZ Ltd Centracorp Finance 2000 Finance Now Future Finance Geneva Finance Home Direct Instant Finance John Deere Financial Latitude Financial Personal Finance Ltd South Pacific Loans The Warehouse Financial Services Group Thorn Group Financial Services Ltd Turners Finance Limited	VEDA Advantage <u>Debt Collection Agencies</u> Baycorp (NZ) Consumer Credit Management Limited Dun & Bradstreet (NZ) Limited	Autosure Protecta Insurance Provident Insurance Corporation Ltd Southsure Assurance	American Express International (NZ) Ltd AML Solutions Buddle Findlay Chapman Tripp EY Finzsoft KPMG PWC SimpsonWestern (Total : 53 members)