Submission

By

To

The Ministry of Economic Development

On

Proposed fee and levy changes for the Financial Markets Authority External Reporting Board New Zealand Companies Office Insolvency and Trustee Service

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1. Introduction

The Insurance Brokers Association of New Zealand Inc (IBANZ) is pleased to make this submission to the Ministry of Economic Development (MED) on the discussion document issued in June 2011 regarding the **Proposed fee and levy changes for the Financial Markets Authority (FMA), External Reporting Board (XRB), New Zealand Companies Office (NZCO), and Insolvency and Trustee Service (ITS)**.

1.1 About IBANZ

IBANZ is New Zealand's professional body representing the interests of fire and general insurance brokers, risk managers and consumers in New Zealand.

We have 160 member firms employing in excess of 2,200 staff many of whom are financial advisers and therefore would be subject to the proposed FMA and FAA levies. Members write $2.3 billion of premiums annually out of a gross market premium of approximately $3.5 billion.

The organisation advises members, government, consumer groups and other stakeholders on key insurance issues and provides training, technical advice, guidance on regulation and business support.

1.2 Release of information

We have no objection to the public release of any information contained in this submission.

2. Executive Summary

The following are the key issues we have with the discussion document.

2.1 Market distortion

The purpose of the proposed FMA levy is to fund the FMA's general monitoring, supervision, surveillance and investigation of financial markets as well as general regulation of financial markets participants (FMP). In the absence of measures/statistics to fairly apportion the costs of regulatory effort across different classes of FMPs, reliance solely on an apparently arbitrary per capita FMA levy imposed only on a subset of FMPs is unfair, creates financial and structural market distortion encouraging behaviour contrary to the objectives of the Financial Advisers Act.

The charging regime should in no way distract from the primary purpose of the Act. Distortionary aspects of the discussion document's preferred option clearly promote structures that will detract from this purpose.

A fairer approach is a small per capita charge imposed on a wide population, such as all companies, which indirectly benefit from operating in a well-

regulated financial market. We suggest two alternative approaches for doing this while ensuring advisers pay their fair share – see 3.2 below.

Under the preferred option (option one) as outlined in the discussion document the bulk of the FMA funding will end up being paid by about 7,000 AFA and RFA Advisers with QFEs paying far less. Financial service providers will restructure businesses as a result of these costs producing structures reflecting regulatory charging rather than regulatory intent. Ultimately as a consequence of financial advisers restructuring their businesses there will be a significant reduction in fees/levies collected. A less distortionary option should be adopted.

The cost on a per financial adviser basis does not recognise the difference in risk for the differing groups of market participants. The FAA levy should reflect the risks associated with the complexity of product advised upon and the fact that QFEs require a higher degree of regulatory oversight than individual advisers.

2.2 Double charging

There is substantial overlap between the activities of the regulator that are funded by the FMA levy and those that are funded by the FAA levy. For example, both levies cover surveillance and enforcement activities, so in effect advisers are being double charged, first for FAA-related surveillance and enforcement and then for surveillance and enforcement conducted by the FMA on non-adviser work.

In addition, we recommend that care be taken to avoid double imposts in situations where advisers work within corporate structures, where the company and the adviser were both being levied. For example with organisations which are not QFEs but employ and pay for the regulatory fees of their advisers, they now face the significant double costs in relation to the FAA and FMA levies. This is particularly pronounced in relation to the FMA levy.

2.3 Financial impact on advisers

The magnitude of the proposed levies will significantly impact on financial advisers. These costs need to be seen in the total picture of regulatory costs. Financial advisers also have significant costs in belonging to an external dispute resolution scheme. Additionally the competence requirements impose substantial training costs which are ongoing through the need to undertake continuing professional development.

2.4 Impact of FAA/FMA levy funding on consumers

The fundamental objectives of the legislation are focused on the consumer. There is limited information in the discussion document as to what analysis has been carried out regarding the effect of these fees and levies on the consumer.

Ultimately the consumer will end up bearing additional regulatory costs imposed on advisers, further reducing the affordability of professional advice. With these levies, there will almost certainly be a reduction in the numbers of advisers,

particularly independent advisers which is clearly not in the consumer's interest as well as increased charges to consumers.

Ideally the levies should be structured to minimise the impact on consumers.

2.5 Public versus private funding

We note that subsequent to the release of the discussion document, you have made available parts of the Cabinet Paper supporting the imposition of an FAA levy on industry. While this confirms Cabinet's decision, it sheds little light on the rationale for recovering some of the FMA's costs from industry. We do not oppose the principle of partial funding of the regulator by industry particularly as it relates to regulation under the FAA. However, we believe decisions about how the levies should be raised (including those relating to the questions in your discussion document) would be far clearer if there existed a statement of principles regarding industry funding.

Furthermore, although the regulator must be able to operate in an independent and unfettered manner, we suggest that some form of reporting back and/or industry liaison arrangements by the FMA would be desirable, so that industry received some indication of how their levy had been spent. Normal accountability mechanisms are one thing: giving levy-funders some ownership and interest in the regulator goes a step further, offering potential benefits to the regulator, industry and – most importantly – to a strengthened relationship between them.

3. Comments

We make these comments in response to the questions posed in the discussion document.

3.1 Financial Markets Authority

1. Which is your preferred option?

We prefer Option 4. (We assume that the payee covers not just the wide range of entities listed in the discussion document but also all financial service providers, including individuals.) This option is the least distortionary, fairest in the absence of information, most pragmatic and most likely to achieve the objectives of the Financial Advisers Act.

We note that Option 4 is not necessarily optimal because, as you state in paragraph 39 of the discussion document: "distributing the costs of FAA regulation across a broader group does not reflect the objective that: those benefiting from regulatory functions provided, or contributing to risks that warrant a regulatory response, should bear the costs of those regulatory functions."

We do not support Options 1 or 3 because costs of regulating **financial markets participants** are (a) imposed on a subset of that population, namely **financial service providers** and (b) levied on a per capita basis with no adjustment to reflect the size or regulatory risk of each business paying the levy. We note that the per capita cost would be, for many of our members, a very significant business cost.

Given the range of business models in which financial adviser services are provided in New Zealand, we believe either of these options would distort the market, most notably imposing significantly more cost on a registered financial adviser (and their employers) than on a QFE adviser. We believe these options encourage behaviour contrary to the objectives of the Financial Advisers Act, for example by effectively incentivising non-advice selling (as advice gets increasingly expensive) and discouraging advisers from aspiring to AFA status (because the costs are too great).

While we support spreading of the FMA levy across the broad range of those who benefit from the FMA's regulatory functions our preference is not Option 2 as set out in the discussion document. This is because the proposed FMA levy primarily relates to the non-adviser work of the FMA. Imposition of Option 2 in addition to an FAA levy amounts to double charging the adviser sector – once for their regulatory costs and once for the costs of regulating others in the market. We would support this option if it were not accompanied by a separate FAA levy (see our Alternative B below).

2. Is there an alternative you would prefer?

We propose two alternatives.

We acknowledge that there are no easy, reliable methods for determining the size of an advisory business or its degree of regulatory riskiness. However, a per capita allocation of all the FAA costs results in distortions, no matter how they may be apportioned between QFEs, RFAs and AFAs.

EITHER Alternative A: Our preferred alternative is a hybrid approach that offers a pragmatic way of not unfairly burdening smaller advisory businesses. We suggest all the FMA costs **and a portion of the FAA costs** be apportioned to the population described in Option 4, to result in a levy of around $30 (for all financial service providers, companies, limited partnerships, building societies, credit unions, industrial and provident societies, friendly societies, and contributory mortgage brokers.). The balance of FAA costs could then be attributed to advisers on a basis similar to that proposed by you, noting that the per capita costs will reduce and thus lower the chances for material market distortions occurring.

OR Alternative B: Impose the FAA levy as proposed by you on advisers but exempt advisers from payment of any FMA levy.

3. Why have you chosen your preferred option?

Because as discussed above it is the only option that avoids material market distortions and does not undermine the fundamental objectives of the legislation.

3.2 FMA Levy

4. Which types of entities should be required to pay the Financial Markets Authority (FMA) levy?

A broad range of entities benefit from a well regulated market and therefore we would support the imposition of at least some of the FMA levy on all financial service providers companies, limited partnerships, building societies, credit unions, industrial and provident societies, friendly societies, and contributory mortgage brokers. However, we acknowledge that subsets of that population – such as advisers – contribute risks that warrant a greater regulatory response – and so should bear a greater share. The challenge is to find a fair way of doing so that is neither a disincentive to giving good advice nor distorts the costs paid by the end client. It should also recognise the fact that they may pay some form of additional FAA levy. Our suggested alternatives attempt to address this challenge.

5. Is it desirable to vary the amount of the FMA levy applied to different groups?

Yes, for the reasons stated above. We support the attribution of at least some of the FAA costs only to the advisory industry. One of the principle reasons we suggest that **not all** FAA costs should be imposed solely on the advisory industry is that there is no easy, reliable method for doing so. That being the case, we recommend that the bulk of the regulator's costs (FMA plus some FAA) should be spread evenly over the population that directly benefits from a well-regulated market.

6. How could this be achieved, given the limited information available for structuring such tiers?

See our suggested alternatives.

3.3 FAA Levy

7. Are the Financial Adviser Act 2008 (FAA) levy tiers appropriate?

Yes. We suggest an activity test should be applied so that the levy is not payable in respect of advisers who are inactive (i.e. do not provide any financial adviser service) in a given period. This would be based on a declaration by the adviser, or in the case of QFE advisers, by the QFE.

8. Should any other financial service providers pay the FAA levy e.g. brokers?

Yes; note our suggestion above that some of the FAA costs should be apportioned across the broad population for these reasons (a) everyone benefits from a well-regulated market, including a well-functioning adviser sector and (b) this is the fairest way of avoiding levy-induced market distortions.

IBANZ has no comment on the following sections as they do not have a material impact on our members:

- **Auditor Regulation**
- **External Reporting Board (XRB)**
- **New Zealand Companies Office**
- **Insolvency and Trustee Service**

IBANZ notes that it has canvassed opinion from all of its membership, which consists of 160 general insurance broker companies with around 2,200 employees. We have received overwhelming support for this submission.

BrokerWeb, a consortium of 38 independently owned and operated general insurance broker companies are presenting a submission fully in support of the IBANZ submission.

Allied Insurance group, a consortium of 30 independent general insurance broker companies have given their total support to the IBANZ submission.

IBANZ members Aon, a significant company with over 600 staff, have asked to have their submission attached to our response. They are in total agreement with the comments expressed in our submission.

The Professional Advisers Association representing over 850 financial advisers also lends their support to our submission.