

SOVEREIGN

**SUBMISSION TO THE
MINISTRY OF ECONOMIC DEVELOPMENT**

ON

**DISCUSSION DOCUMENT RELATING TO THE FEES REGULATIONS UNDER
THE FINANCIAL SERVICE PROVIDERS (REGISTRATION AND DISPUTE
RESOLUTION) ACT 2008 AND THE FINANCIAL ADVISERS ACT 2008**

13 November 2009

Introduction and summary

1. Sovereign Limited makes this submission to the Ministry of Economic Development (“**MED**”) in response to the discussion document (“**Discussion Document**”) dated October 2009 relating to the fees regulations to be promulgated under the Financial Services Providers (Registration and Dispute Resolution) Act 2008 (“**FSP Act**”) and the Financial Advisers Act 2008 (“**FAA**”).
2. Sovereign is New Zealand’s largest life insurer, protecting the lives of more than 600,000 people through the provision of personal insurance (including life, income protection, disablement, trauma, and major medical policies) and employer sponsored compulsory and voluntary workplace schemes. Sovereign is also New Zealand’s third largest provider of health insurance, New Zealand’s largest non-bank lender and has New Zealand’s sixth largest retail fund with over \$3 billion in funds under management. Sovereign is part of the ASB group of companies, which in turn is part of the Commonwealth Bank of Australia group.
3. Sovereign has a business model under which its products are distributed exclusively through third-party financial advisers, while all policy processing, underwriting, claims management and customer services are provided directly to customers. Sovereign has relationships with over 3,700 advisers, ranging from sole traders through to the employees of large institutions. Sovereign also has a number of employees that will be providing financial adviser services for the purposes of the FAA.
4. Sovereign’s submissions in relation to each category of fees referred to in the Discussion Document is set out below, together with feedback in relation to the specific questions set out on page 13 of the Discussion Document.
5. Sovereign’s contact for matters regarding this submission is:

David Drillien
General Manager, Customers and Markets
Sovereign
T: 09 487 9167
F: 09 487 8026
david.drillien@sovereign.co.nz

Companies Office fees

6. Sovereign acknowledges the statement in the Discussion Document that the Companies Office component of the registration and annual confirmation fees has been set at a rate designed to do no more than recover the costs of establishing and maintaining the register. The fees appear to be relatively high compared to some other fees charged by the Companies Office, such as the fees for incorporating a company under the Companies Act 1993. Further, companies are not required to pay an annual fee. However, Sovereign assumes that the difference in relative fees between registration under the FSP Act and the cost of incorporating of a company reflects the relatively large number of companies that share the costs of maintaining the register of companies (and the fact that such register was established quite some time ago), compared to the number of advisers that will share the cost of establishing and maintaining the register of financial advisers. On that basis, Sovereign generally accepts the proposed approach.
7. Although Sovereign generally agrees with the approach taken by the Companies Office, given the wide range of other costs and expenses that may potentially be incurred by advisers (for example, in relation to joining an approved dispute resolution scheme and, in the case of authorised financial advisers (“**AFAs**”), satisfying competency standards), it may be appropriate for the registration and annual confirmation fees to be reduced from the levels proposed.

Criminal History Checks

8. Sovereign has no comments in relation to the proposed approach in respect of charging for criminal checks as set out in the Discussion Document.

Dispute Resolution Regime

9. Sovereign submits that only those financial service providers that are members of the reserve scheme should be required to contribute towards the costs of that scheme. Members of other approved dispute resolution schemes (who will have to pay to be a member of such other schemes) do not benefit from the reserve scheme and should therefore not be required to fund it.

Securities Commission

QFE and AFA application fees

10. For the reasons discussed in paragraphs 11 to 15, Sovereign considers that the proposed application fees for qualifying financial entity (“**QFE**”) status may not reflect the detailed scrutiny that the Commission has indicated it will apply in assessing QFE applications.
11. The purpose of the FAA is to promote the sound and efficient delivery of financial advice, and to encourage public confidence in the professionalism and integrity of financial advisers. QFEs will play an important role in achieving this purpose. Given the significant responsibilities and frontline compliance role given to QFEs under the FAA (for example, ensuring that a significant number of advisers comply with their obligations under the FAA), it is critical in terms of achieving the purpose of the FAA that any entity granted QFE status is able to meet its obligations under the FAA and the terms and conditions attached to its granting of QFE status. Sovereign therefore agrees that QFE applications should be carefully scrutinised to ensure that QFE status is granted only to appropriate entities.
12. These concepts are recognised by the Commission in its Staff Paper entitled *Regulating and Supervising Financial Advisers* dated 18 June 2009 (“**Supervision Staff Paper**”), where the Commission states at paragraph 58 that “a QFE is responsible for the sound delivery of financial advice by its financial advisers, and encouraging public confidence in the professionalism and integrity of its financial advisers”. Given this, it is vital that QFE status is only granted to appropriate entities. In this regard, the Commission states in the Supervision Staff Paper at paragraph 74 that:

To become a QFE an entity must therefore satisfy the Commission that it can and will ensure appropriate standards are met and maintained. **This is largely a question of capacity – whether there are processes in place to identify training needs and to train and monitor employees and agents, and sufficient resources applied to ensure that those processes are effective. This amounts to whether an entity has the practical and financial capacity to supervise its own advisers.** We envisage this involving an examination of systems and processes on the one hand and the culture of the entity of the other. **(emphasis added)**
13. Sovereign submits that the Commission will be required to commit significant resources to scrutinise QFE applications appropriately in order to ensure that the relevant application criteria for QFE status are satisfied. For example, paragraph 75 of the Supervision Staff Paper provides that a prospective QFE must be able to demonstrate that it has the policies and effective procedure to address and maintain the following:
 - a. competence of employees and agents;
 - b. conduct of employees and agents;

- c. capacity of organisational processes and arrangements;
 - d. compliance and risk management;
 - e. compensation arrangements;
 - f. culture, ethics and governance;
 - g. communication with/disclosure to clients;
 - h. conflicts of interest management; and
 - i. complaints management.
14. A prospective QFE will also need to demonstrate that it has the financial capacity to meet its potential financial obligations resulting from taking responsibility for its advisers and agents. Sovereign anticipates that the Commission's work in respect of processing a QFE application would include, for example, a detailed review of the prospective QFE's policies and procedures and a detailed analysis of its financial position to ensure that it has the financial capacity to be able to meet its obligations (including taking responsibility for breaches by the advisers it is responsible for). It is vital for the integrity of the financial advisers regime that QFEs are financially strong enough to meet their obligations. Sovereign submits that a QFE having professional indemnity insurance in this regard is not sufficient and that the QFE itself should be prepared to (and be able to) stand behind its employees and nominated agents.
15. For the above reasons, Sovereign submits that the proposed application fees for QFEs may be too low given that amount of work that will be required by the Commission to apply the appropriate level of scrutiny to QFE applications. Given the relative amounts of work that Sovereign anticipates would be required to process an AFA application compared to a QFE application, Sovereign would have expected that the difference in application fees for QFEs and AFAs would be greater. However, Sovereign's submission in this regard is based on the expectations set out above in relation to the degree of scrutiny that would be given to QFE applications to ensure that the purpose of the FAA is achieved.
16. However, Sovereign does not consider that the level of the application fee for QFEs should be linked to the number of advisers the QFE is responsible for. This would be inconsistent with the aims of the QFE regime and would not be reflective of the frontline compliance role of, and other responsibilities placed on, QFEs.
17. Sovereign also submits that lower application fees should be payable in respect of AFAs that are employees of a QFE (or a related company of a QFE). This submission is made on the basis that less time and resources are likely to be required by the Commission in connection with the processing of such applications relative to applications from other categories of AFAs.

Renewal fees

18. The Discussion Document contemplates that renewal fees for QFEs and AFAs may be the same as initial application fees. Sovereign submits that, given less work will presumably be required in relation to processing a renewal application compared to an initial application (especially given that the QFE or AFA will have been subject to supervision by the Commission), in most circumstances it would be appropriate for renewal fees to be lower than initial application fees.

Annual supervision fees

19. There appears to be some overlap between the proposed base minimum supervision fee and the levies to be imposed by the Commission under section 155 of the FAA. It

would be helpful if some guidance could be provided in relation to the likely amount of the levy to be imposed under section 155.

20. To the extent that the proposed fees and levies relate to, for example, enforcement activity against a particular QFE or AFA, Sovereign submits that it would be appropriate for the Commission's costs to be recovered from the QFE or AFA concerned rather than being shared by all QFEs and AFAs.

Responses to Questions for Submitters

21. Set out below are Sovereign's responses to the two questions set out on page 13 of the Discussion Document.

(1) *Are our best estimates of financial service providers currently doing business in New Zealand accurate and/or reasonable in the current economic environment?*

22. Sovereign notes that the number of financial service providers falling into each category of provider will depend on a range of matters, including the outcome of proposed changes to the FAA.

(2) *Have all feasible options been considered in respect to how the fees detailed in this paper will be paid and the method of collection?*

23. Sovereign agrees with the proposed approach that all fees be collected by a single agency and further agrees that it would be appropriate for the Companies Office to perform this role.