

Regulatory Impact Statement

Financial products exemption from uninvited direct sales requirements

Agency Disclosure Statement

- 1 This Regulatory Impact Statement has been prepared by the Ministry of Business, Innovation and Employment.
- 2 It provides an analysis of options to address the problems that arise when applying the new uninvited direct sales (UDS) provisions of the Fair Trading Act 1986 (FTA) to certain sales of financial products.
- 3 The industry has informed us that as UDS is a new concept, they do not have conclusive quantitative data as to the volume of business that is affected by the problem which the exemption is proposing to address. In the absence of such data, it has been difficult to quantify the costs and benefits of the proposed exemption. We have instead proceeded with our analysis based on qualitative evidence in the form of examples of various everyday scenarios that would be affected by the problem.
- 4 During consultation on the exemption currently proposed, stakeholders have also raised arguments that the proposed exemption should be broader than the regulation-making power allows. For example, it was argued that financial products that are subject to consumer protections under the Financial Advisers Act 2008 but outside the scope of the regulation-making power under the FTA should also be exempt from the UDS provisions. Officials will consider and engage further with stakeholders on whether a broader exemption is warranted following implementation of the currently proposed regulations with the aim of providing certainty to industry before the end of 2014.

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Status Quo

Uninvited direct sales under the Fair Trading Act

- 1 From 17 June 2014, the Fair Trading Act 1986 (FTA) will regulate uninvited direct sales (UDS) to consumers.¹ The UDS requirements were introduced as part of the Consumer Law Reform and replace the provisions of the Door to Door Sales Act 1967. The purpose of the UDS provisions is to protect against the risks of pressure selling.
- 2 An “uninvited direct sale” covers circumstances in which consumers are most vulnerable to unexpected sales pressure, being sale agreements that are negotiated in the consumer’s home, workplace or over the telephone where the consumer has not invited the supplier to come to that place or make the telephone call for the purpose of entering into negotiations relating to the sale.
- 3 Providing contact details to the supplier predominantly for a different purpose does not constitute an “invitation” by the consumer to the supplier to come to their home, workplace or make the call. The UDS provisions will therefore apply in certain situations where suppliers cross-sell other products to existing customers.
- 4 The FTA will not prohibit UDS. Where the UDS provisions apply, suppliers will be required to:
 - a. comply with disclosure requirements which provide that the sale agreement must be clear, legible, in plain language, and set out on the front page specified information including the goods or services supplied, price, the existence of a five working day cooling off period and cancellation rights; and
 - b. provide consumers with a five working day cooling off period during which they can cancel the purchase and receive a full refund.

Offers in the course of ‘unsolicited meetings’ in the Financial Markets Conduct Act

- 5 The Financial Markets Conduct Act 2013 (FMC Act) prohibits offers of financial products² in the course of unsolicited meetings to persons who are not acting in trade. Similar to the FTA, the FMC Act provision is also aimed at protection against pressure selling.
- 6 The general FMC Act prohibition has a number of exemptions, including for offers made through authorised financial advisers (AFAs) and qualifying financial entity (QFE) advisers³ acting in the ordinary course of business as financial advisers, and offers to relatives and wholesale investors. The rationales for the exemptions include that:
 - a. There are certain circumstances where the risks of pressure selling are low, for example, because the offeree is sufficiently experienced in investment or has a relationship with the issuer.

¹ The relevant provisions are currently set out in section 23 of the Fair Trading Amendment Act 2013.

² Being debt securities, equity securities, managed investment products (e.g. KiwiSaver schemes) and derivatives.

³ QFE adviser is defined as an individual who is not an authorised financial adviser and who is (a) an employee of a QFE or any member of a QFE group; or (b) a nominated representative of a QFE or a partner entity. QFEs or ‘qualifying financial entities’ are financial adviser businesses that have obtained QFE status.

- b. AFAs and QFE advisers are already subject to disclosure and other obligations under the Financial Advisers Act 2008 (FAA), which requires them to act with care and take account of client interests. These obligations likely take sufficient account of the risks of pressure selling. Further, there is an expectation in the context of a financial adviser relationship that financial advisers will be selling and advising on a range of products. The nature of financial products and financial advice is that advisers may discuss products other than the ones that the customer initially had in mind.

Fair Trading Act regulation-making power

- 7 The FTA provides a power for regulations to be made exempting from the UDS provisions sales of financial products that are already subject to the exemptions from the unsolicited meetings provisions of the FMC Act. The regulations may prescribe terms and conditions on which an exemption is subject.

Problem Definition

Nature of the problem

- 8 Suppliers of financial products, particularly banks, have provided examples of common scenarios in which they cross-sell financial products in UDS circumstances. For example, a mobile mortgage manager may meet a customer in their home or workplace and discuss other upselling or cross-selling opportunities with the customer. Staff making an outbound call about rolling over a term deposit may identify that opening a savings account would be more suitable for the customer.
- 9 Some suppliers have stated that they train and encourage staff to identify the needs of customers and discuss with customers financial products that may meet their needs. Unlike many other goods and services, consumers may not know that there is a different type of product that meets their needs.
- 10 From 17 June 2014, the status quo will require suppliers of financial products that undertake UDS transactions to ensure that they offer consumers a five working day cooling off period for such transactions and that their product documentation complies with the disclosure requirements in the FTA (in addition to existing disclosure requirements under the FAA and the FMC Act).
- 11 The FTA will not prohibit the sale of financial products in UDS situations. However, a policy decision had been made in the context of the FMC Act that, taking into account the risks and benefits of direct sales of financial products, there are circumstances in which the risks of pressure selling are low such that those circumstances should be exempt from the unsolicited meetings prohibition in the FMC Act. Requiring compliance with the UDS provisions in those circumstances may undermine that FMC Act policy decision and undermine the aim of the FMC Act to create a one-stop shop for regulation of financial products.

- 12 Aside from any consideration of the separate policy decisions that have already been made, the status quo would likely involve material costs and difficulties:
- a. There are practical difficulties with applying the cooling off rights to financial products:
 - i. Where a financial product has a fluctuating price, there would be an incentive on consumers to “game” the system by exercising their cancellation rights to avoid losses due to movement in the value of the product. For example, if the value of a managed investment product that has a fluctuating unit price suddenly fell in value due to wider market conditions, a consumer may choose to exercise their cancellation right.
 - ii. Until the end of the cooling-off period, deposits would need to be categorised as “at call” for the purpose of prudential requirements. This would adversely impact banks’ liquidity requirements.
 - iii. The process for joining KiwiSaver schemes would need to be altered to either delay the processing of applications until the expiry of the five working day period or to implement procedures between the scheme provider, Inland Revenue and any transferring provider to enable the unwinding of membership.
 - b. There would be material costs associated with implementing documentation changes across suppliers’ product ranges and carrying out compliance training for staff. Those costs are not unique to suppliers of financial products. However, due to other existing legislative obligations that apply to sales of financial products, in some situations the UDS provisions would confer little additional benefits such that the costs are not justified.
- 13 Due to the costs and difficulties of complying with the UDS requirements, suppliers may:
- a. pass on the increased compliance costs to customers through lower interest rates or higher fees; or
 - b. discontinue the sale of financial products in circumstances that may amount to an UDS. Such an outcome would be contrary to client expectations of certain financial adviser-client relationships and could result in identified financial needs or risks remaining unaddressed to the detriment of consumers. It would also undermine the FMC Act exemption.

Size of the problem

- 14 The industry has informed us that as UDS is a new concept, they do not have conclusive quantitative data as to the volume of business that is affected by the problem which the exemption is proposing to address. We have therefore been unable to quantify the size of the problem
- 15 Submitters have instead provided us with examples of various everyday scenarios that would be affected by the problem, including sales made where upselling or cross-selling opportunities are identified:
- a. when a mobile mortgage manager meets a customer in their home or workplace, a commercial manager visits a customer at their place of business, a rural manager meets a customer on their farm; or
 - b. when outbound calling staff call customers about an annual review or rolling over of term deposit.

Withheld

- 17 In summary, while the size of the problem is uncertain, there are circumstances where the costs of complying with the UDS provisions for sales of financial products appear disproportionate to the incremental consumer protection benefit of the provisions. There is a risk that the costs of compliance may lead to suppliers discontinuing certain cross-selling practices in circumstances where such cross-selling would be beneficial to consumers.

Objectives

- 18 The objectives are to protect consumers from the risks of pressure selling in a way that:
- a. minimises compliance costs; and
 - b. does not unnecessarily restrict suppliers' ability to sell (and consumers' ability to obtain) financial products through UDS circumstances.

Regulatory Impact Analysis

- 19 We consider below each of the exemptions from the unsolicited meetings prohibition set out in the FMC Act and consider whether the same exemption should be made from the FTA UDS provisions.
- 20 In some cases, an exemption exists in the FMC Act because a complete prohibition on those unsolicited offers would not be justified, but disclosure and a cooling off rights under the UDS provisions remain appropriate such that the exemption should not be replicated in the FTA.

Offers through AFAs or QFE advisers

- 21 The FMC Act provides an exemption for offers of financial products through an AFA or QFE adviser who is acting in the ordinary course of business as a financial adviser.⁴

Option	Protects consumers against pressure selling	Minimise compliance costs	Remove unnecessary restrictions on UDS selling
Retain the status quo	Yes	No	No
Exempt offers through AFAs or QFE advisers <i>(Recommended option)</i>	Yes. Other legislation will continue to protect against the risks of pressure selling, albeit not in the same way.	Yes	Yes

⁴ Section 34(2)(b) of the FMC Act.

Status quo

- 22 Under the status quo, consumers would be protected against the risks of pressure selling for offers through AFAs and QFE advisers through:
- a. the UDS provisions which requires the supplier to comply with disclosure requirements and provide consumers with a five working day cooling off period during which they can cancel the purchase and receive a full refund; and
 - b. requirements on AFAs and QFE advisers to exercise care, diligence and skill in the FAA; obligations in the Code of Professional Conduct for AFAs; standard conditions for QFEs; and disclosure requirements in the FAA and FMC Act.
- 23 The problems with retaining the status quo are set out in paragraphs 10-13 above.
- 24 The costs and difficulties identified could potentially be avoided if suppliers obtained customer consent to being contacted about financial products (thereby making the sales "invited" sales). This could take the form of a broad general consent from customers to being contacted about a range of financial products, or by specifically asking for the customer's consent to being contacted a short time later about particular products that the supplier has identified as being potentially beneficial to the customer.
- 25 A general consent may be a feasible option for certain financial adviser-customer relationships. However, it may be difficult for larger entities that have multiple points of contact with customers to obtain and rely on a general consent that captured all potential instances of cross-selling. A specific consent to receive a separate call or visit may also be confusing and inconvenient for the customer. Further, obtaining either a general or specific consent will involve material compliance costs.
- 26 Compliance costs would therefore not be minimised under the status quo. Where suppliers choose to continue supplying financial products for sales through AFAs or QFE advisers:
- a. suppliers would incur material compliance costs as set out at paragraph 12 above;
 - b. consumers would be detrimentally affected as suppliers would likely pass on increased costs to customers through lower interest rates or higher fees.
- 27 Under the status quo, the UDS provisions may also act as an unnecessary restriction on UDS selling. In order to avoid the costs and difficulties of complying with the UDS requirements under the status quo, suppliers may implement procedures to ensure that financial products are not supplied in UDS circumstances. Implementing such procedures would restrict the manner in which suppliers sell financial products and would be detrimental to consumers as they may not be proactively informed of products that meet their financial needs.

Exempt offers through AFAs and QFE advisers

- 28 Providing an exemption from the UDS provisions for offers through AFAs and QFE advisers means that for transactions subject to the exemption, suppliers would *not* be required to comply with the FTA disclosure requirements or provide consumers with the five working day cancellation right set out in the FTA.
- 29 The purpose of the UDS provisions is to protect against the risks of pressure selling. An exemption means that consumers will not receive disclosure in accordance with those provisions and would not have the right to cancel the purchase within the cooling off period and receive a full refund.

- 30 However, other legislation will continue to protect against the risks of pressure selling:
- a. The FAA provides that a financial adviser, when providing a financial adviser service, must exercise the care, diligence, and skill that a reasonable financial adviser would exercise in the circumstances.
 - b. For AFAs, the Code of Professional Conduct for AFAs provide that an AFA must place the interest of the client first and act with integrity; must not do anything that would be likely to bring the financial advisory industry into dispute; must behave professionally in all dealings with a client, and communicate clearly, concisely and effectively; when providing a personalised service to a retail client, take reasonable steps to ensure that personalised service is suitable for the client.
 - c. For QFE advisers, the standard conditions for QFEs provide that QFEs must ensure that retail clients receive adequate protection; and for personalised services provided by QFE advisers to retail clients in relation to category 1 products, QFEs must maintain procedures to ensure that consumer protection is of a similar standard to that provided by advisers subject to the Code of Professional Conduct for AFAs.
 - d. The FAA and FMC Act also prescribe disclosure requirements.
- 31 In relation to sales through AFAs and QFE advisers:
- a. compliance costs would be reduced as documentation would not need to be changed to take account of the UDS requirements; and
 - b. the practical difficulties with applying the cooling off rights to financial products discussed at paragraphs 10-13 above would be overcome.
- 32 As discussed above, the costs and difficulties of applying the FTA UDS provisions to financial products mean that those provisions may act as a practical impediment on suppliers' ability to sell financial products in UDS situations. An exemption would remove that impediment for sales through AFAs and QFE advisers and means that consumers would continue to receive information from those advisers about products that may potentially be beneficial to them.
- 33 We consider that an exemption from the UDS provisions should be introduced for offers of financial products through AFAs and QFE advisers acting in the ordinary course of business as a financial adviser.

Offers of quoted financial products made through a person permitted to advise on offer

- 34 The FMC Act provides an exemption for offers of financial products quoted on the NZX or another market and the offer is made through a person who is permitted under the FAA to give advice on that offer (or exempted from the FAA).⁵

⁵ Section 34(2)(c) of the FMC Act.

Option	Protects consumers against pressure selling	Minimise compliance costs	Remove unnecessary restrictions on UDS selling
Retain the status quo	Yes	No	No
Exempt offers of quoted financial products <i>(Recommended option)</i>	Yes. Other legislation will continue to protect against the risks of pressure selling, albeit not in the same way.	Yes	Yes

Status quo

- 35 Similar to offers through AFAs and QFE advisers, consumers would be protected against the risks of pressure selling through both the UDS provisions as well as industry-specific regulations in the FAA and FMC Act.
- 36 The problems set out in paragraphs 10-13 would remain in the status quo, so compliance costs would not be minimised and the UDS provisions may act as an unnecessary restriction on pressure selling.

Exempt offers of quoted financial products made through a person permitted to advise on offer

- 37 Similar to offers through AFAs and QFE advisers, consumers will still be protected against pressure selling as the person giving advice on the quoted financial would be subject to requirements to exercise care, diligence and skill in the FAA and disclosure obligations in the FAA or be within a limited exemption from the FAA, usually on the grounds that another regime applies. Disclosure obligations under the FMC Act would still apply.
- 38 We therefore consider that an exemption from the UDS provisions should be introduced for offers of quoted financial products made through a person permitted to advise on offer.

Offers of membership in a co-operative

- 39 The FMC Act provides an exemption for financial products of a co-operative where the product is a necessary incident of doing business with the co-operative or the means by which a person can access the benefits of membership of the co-operative.⁶

⁶ Section 34(2)(d) of the FMC Act.

Option	Protects consumers against pressure selling	Minimise compliance costs	Remove unnecessary restrictions on UDS selling
Retain the status quo <i>(Recommended option)</i>	Yes	No	N/A. If offers are made to consumers we do consider that these restrictions are necessary.
Exempt offers of financial products of a co-operative.	No	Yes	N/A. If offers are made to consumers we do consider that these restrictions are necessary.

Status quo

- 40 The FTA UDS provisions apply to agreements for the supply of goods or services to a consumer. We consider it unlikely that such offers associated with co-operative membership would be subject to the UDS provisions as they are unlikely to be the sale of a good or service to a “consumer” as defined under the FTA.
- 41 If there are any such offers to “consumers”, consumers would be protected against the risks of pressure selling by the disclosure and cooling-off requirements in the UDS provisions.
- 42 Such offers were exempt from the FMC Act because the “financial product” (ie, co-operative shares) were the means by which a person joined the co-operative to receive rebates on products or were necessary to do business with the co-operative, rather than being a financial investment in themselves. It was not appropriate for legislation governing financial investments to prohibit unsolicited offers to do business with a co-operative.
- 43 As there are no other specific protections against the risks of pressure selling, it is appropriate that the general law as set out in the UDS provisions applies to the extent that these memberships are sold to consumers. The status quo does not minimise compliance costs because suppliers that undertake UDS transactions of co-operative memberships will need to adapt their processes to comply with the disclosure and cooling off requirements. However, we think that the benefits of protecting consumers outweigh those costs in this case because consumers would otherwise have no specific protection against the risks of pressure selling. If the UDS provisions act as a restriction on selling of co-operative memberships in UDS circumstances, we consider that such a restriction is necessary for consumer protection and should not be removed.

Exempt offers of membership in a co-operative

- 44 To the extent that offers of co-operative memberships are made to “consumers”, those consumers will have no specific legislative protection against the risks of pressure selling if they are exempt from the UDS provisions.
- 45 We therefore consider that an exemption from the UDS provisions should *not* be introduced for circumstances subject to the FMC Act section 34(2)(d) exemption.

Schedule 1 exemptions

Option	Protects consumers against pressure selling	Minimise compliance costs	Remove unnecessary restrictions on UDS selling
Retain the status quo	Yes	No	No
Exempt offers subject to an exemption in Schedule 1 of the FMC Act <i>(Recommended option in specific cases referred to below)</i>	In some cases, the risks of pressure selling are low as the consumer is sophisticated, has a close relationship with the supplier or the products are simple.	Yes	Yes

46 The FMC Act exempts financial product offers that do not require product disclosure under the FMC Act because of various exclusions under Schedule 1.⁷ These “FMC disclosure exemptions” are:

- a. For offers to sophisticated or professional advisers or other persons where, due to their relationship with the issuer, those persons are unlikely to be vulnerable to pressure selling. In many cases, these persons would not be subject to the UDS provisions because they would not be “consumers” under the FTA. Where they are “consumers”, we consider that there should be an exemption from the UDS provisions for persons who come within a FMC disclosure exemption due to the low risks of pressure selling (ie. clauses 3 to 5, 7, 8 and 9 of Schedule 1 of the FMC Act).
- b. For some products where full FMC Act disclosure and other obligations do not apply due to the nature of the product (e.g. due to its simplicity) or the nature of the issuer (e.g. registered banks). The rationale for these exemptions differs, and not all necessarily justify an exemption from disclosure and a cooling off period under the UDS provisions. In principle however, we think that an exemption from the UDS provisions should apply for the following FMC disclosure exclusions:
 - i. Clause 10 of Schedule 1 (dividend reinvestment plans). Dividend reinvestment plans are analogous to “renewal agreements”, which the FTA already exempts from the UDS provisions.
 - ii. Clause 21(a) and (c) of Schedule 1. These are simple “on call” accounts, term deposits, or other standard banking products. These products are simple, low risk, and well understood. Exiting from these products entails little or no cost and there is little risk of pressure selling. The exact scope of these simple products will be reviewed in the review of the FAA 2008 during 2015-2016. We consider that these products should be exempt now from the UDS provisions, but the exact scope of that exemption should be reconsidered in light of that review.

⁷ Section 34(2)(a) of the FMC Act.

Terms and conditions of the exemption

- 47 We consulted with stakeholders on whether terms and conditions should be attached to any exemption. We asked whether a condition should be imposed requiring suppliers to give oral notice to the consumer that the UDS provisions did not apply to the sale being negotiated.
- 48 Following stakeholder feedback, we consider that requiring oral notice that the UDS provisions did not apply would provide little additional benefit and may cause confusion. We consider that working with the Commerce Commission on guidance and fact sheets would help consumer awareness that the UDS provisions did not apply to certain sales of financial products.

Consultation

- 49 We released a targeted consultation document in May 2014. Comments were received from ANZ, ASB, BNZ, Westpac, TSB, HSBC, AMP, Financial Services Federation (FSF), Consumer NZ, Commerce Commission, Financial Services Complaints Limited (FSCL), New Zealand Law Society and Chapman Tripp.
- 50 The banks, AMP, FSF, FSCL, Law Society and Chapman Tripp were all in favour of the proposed exemption or did not see a problem with providing an exemption. Consumer NZ submitted that the UDS provisions were an important protection against the risks of pressure selling and the difficulties associated with applying the UDS provisions to financial products did not provide evidence of a problem. We consider that sufficient protection is available in other legislation to protect against the risks of pressure selling.
- 51 The Commerce Commission commented that the proposed exemption could lead to gaps where some sales of financial products are not subject to protection against pressure selling. The Commission did not identify any specific potential gaps. The Financial Markets Authority were consulted but did not raise any concerns with the proposed exemption.

Conclusions and Recommendations

- 52 We consider that the status quo would impose material compliance costs while conferring little additional protection for consumers.
- 53 We consider that an exemption from the UDS provisions should be provided in some, but not all circumstances subject to the FMC Act exemption as described in the analysis of the scope of the exemption above.

Implementation

- 54 The recommended option can be implemented by making regulations under section 36S of the FTA.
- 55 There is likely to be a very short time frame between the passing of regulations and the time that regulations would come into force on 17 June 2014. The proposed regulations do not in themselves impose any additional compliance requirements on business, so the risks of implementing the regulations are relatively low from a business compliance perspective.

- 56 However, there was some uncertainty for businesses as to whether an exemption would be provided and the scope of the exemption. Therefore, there is a risk that if an exemption is not provided, businesses would need to implement changes within a short timeframe to ensure that any UDS transactions following 17 June 2014 would comply with the UDS requirements.
- 57 We have addressed that risk to the extent possible by updating stakeholders on our progress in developing the regulations so that they were aware of the likelihood of an exemption being provided (while noting that our views were subject to approval by the Minister of Consumer Affairs and Cabinet).
- 58 If regulations are passed, we will work with the Commerce Commission to help make consumers aware that the UDS provisions do not apply to sales of financial products subject to the exemption.

Monitoring, Evaluation and Review

- 59 We intend to monitor and evaluate the results of providing the proposed exemption. We intend to do so by seeking feedback from the Commerce Commission, financial dispute resolutions schemes and Consumer NZ as to whether any issues of pressure selling have arisen in the circumstances subject to the proposed exemption.
- 60 During consultation on the proposed regulations, suppliers have also raised concerns that the proposed exemption should be broader than what the regulation-making power allows. For example, it was argued that the exemption should also include spot foreign exchange products and insurance products. There may be grounds for a broader exemption in some cases. We will consider whether a broader exemption can and should be introduced by primary legislation following implementation of the proposed regulations and seek the feedback referred to above on the impact of the currently proposed exemption as part of that process.