

Bank of New Zealand

**Response to the Code Working
Group Consultation Paper:**

The Financial Advice Code

9 November 2018

RELEASED UNDER THE
OFFICIAL INFORMATION ACT

1.0 INTRODUCTION

- 1.1 This submission has been prepared by the Bank of New Zealand ('BNZ') in response to the Consultation Paper, "The Draft Financial Advice Code" ('the Consultation Paper'), released by the Code Working Group ('CWG') in October 2018.
- 1.2 BNZ welcomes this opportunity to provide a response to the Consultation Paper and acknowledges the industry engagement undertaken by CWG on this matter.

2.0 SUBSTANTIVE BNZ SUBMISSIONS

[Standard 1] Treat clients fairly and act in their interests

1. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.1 BNZ agrees with the inclusion of Code Standard 1.
- #### ***2. Please provide any comments on this standard and the proposed commentary.***
- 2.2 BNZ notes that the proposed commentary does not separate 'treating clients fairly' and 'acting in the clients' interests'.
- 2.3 BNZ supports the first aspect of the standard, 'Treating clients fairly', as this would be a straightforward standard and easy for both BNZ staff and clients to

understand. BNZ agrees with the proposed commentary that fairness depends on the particular circumstances.

- 2.4 'Acting in clients' interests' can be interpreted differently in the particular circumstances. An adviser should be able to act in their clients' interests even when they provide advice only on products that their employer produces or manages. BNZ considers that this should be specifically called out in the proposed commentary, on the basis that the standard is not intended to impose an obligation on advisers to be completely independent. The key to managing this is effective disclosure and client understanding, so that clients can make fully informed decisions.
- 2.5 BNZ notes that the proposed commentary is phrased in a way that the examples relate only to what 'treating clients fairly' usually includes. BNZ suggests the commentary should be expanded to examples of what acting in clients' interests usually includes.
- 2.6 BNZ notes that the Ministry of Business, Innovation and Employment (MBIE) had considered using the standard of 'acting in the clients' interest'. Following initial consultation, MBIE had opted to limit the requirement to 'prioritising a client's interest' where there is a conflict of interest. To simplify compliance standards, BNZ submits that this standard should be aligned with section 431J under the Bill.

[Standard 2] Act with integrity

3. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.7 BNZ agrees with the inclusion of Code Standard 2.

4. Please provide any comments on this standard and the proposed commentary.

- 2.8 BNZ considers that while the obligation to behave ethically is implied in Code Standard 2, the proposed commentary should expressly refer to that obligation.
- 2.9 BNZ assumes that the Disclosure Regulations that will accompany the Financial Services Legislative Amendment Bill will supplement this Standard. BNZ assumes that those regulations will include more specific restrictions on how advisers can represent themselves to clients (for example, what nomenclature can be used or not used by advisers). If the Disclosure Regulations do not address this, BNZ requests that this Code Standard provides the appropriate commentary.

[Standard 3] Manage conflicts of interests

5. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.10 BNZ agrees with the inclusion of Code Standard 3.

6. Please provide any comments on this standard and the proposed commentary.

- 2.11 BNZ considers that this proposed Code Standard should be amended to refer to 'material' conflicts of interest. In many cases where an adviser provides advice to a client, there will be some immaterial conflict of interest that arises. BNZ considers that it is not intended that those immaterial conflicts of interest are in breach of this proposed Code Standard. Proposed Code Standard 4 refers to 'material risks', and BNZ's view is that the same approach should be taken in relation to conflicts of interests. The wording in the example to this Code Standard 3 is consistent with this.
- 2.12 BNZ assumes that the Disclosure Regulations will provide additional detail in relation to the management of conflicts of interest (and how to communicate that with clients).

[Standard 4] Take reasonable steps to ensure that the client understands the financial advice

7. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.13 BNZ agrees with the inclusion of Code Standard 4.

8. Please provide any comments on this standard and the proposed commentary.

- 2.14 BNZ notes that the nature and scope of advice agreed between the adviser and client may be shaped in any way the parties agree. There may be material consequences of following the financial advice to the client that sit outside the scope of the advice. The adviser should not be expected to ensure understanding of consequences that sit outside the scope of the advice (for example the consequences of choosing a replacement product if a comparison with the existing product sits outside the scope of the advice).
- 2.15 BNZ notes that record keeping processes can prove that advisers have had the correct conversation but it will be difficult to evidence customer 'understanding'. The principle issue here is what is meant by 'understanding', and how to evidence 'reasonable steps'. BNZ considers that more guidance should be included in the commentary to the Code Standard in this regard.
- 2.16 BNZ notes that the example used in the Code Standard in relation to replacement insurance business could potentially be contradictory. The scope of the advice that Beth provides excludes comparisons between products, but Beth is able to identify that some benefits applicable under the current policy may not be covered under the new policy. This implies that Beth has reviewed the existing policy. Beth would be expected to know if a benefit was present under the new policy.

[Standard 5] Give financial advice that is suitable for the client

9. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

2.17 BNZ agrees with the inclusion of Code Standard 5.

10. Please provide any comments on this standard and the proposed commentary.

2.18 BNZ considers that 'suitability' will depend on the nature and scope of the advice, including the limits on the products that the adviser can advise on. The adviser must have robust processes in place to ensure that the adviser is able to understand the client's circumstances, and is then able to recommend a suitable product.

2.19 BNZ considers that the Code Standard should read 'take reasonable steps to give financial advice that is suitable for the client'. This is consistent with the approach taken in Code Standard 4.

2.20 BNZ considers that this Code Standard should clarify that any comparative information that is required to be provided (in the context of a replacement product) be limited to publicly available information. This would prevent a situation where a client may have agreed to certain bespoke terms with their existing provider that are not public knowledge and therefore are not known to the adviser.

2.21 The example given in the proposed commentary refers to the 'implied nature and scope of the advice' being limited to the bank's products only. BNZ considers that in a vertically integrated organisation the adviser can only reasonably be expected to provide advice in relation to products produced or managed by their organisation. BNZ considers that this standard only requires the adviser to provide the client with an explanation of the implications of this. The adviser is not required to advise on other products in the market, and the adviser is not required to scan the market for particular products that may be more suitable for the client. BNZ considers that this obligation could be complied with in the way advisers disclose information about themselves and their business to the client.

[Standard 6] Protect client information

11. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

2.22 BNZ agrees with the inclusion of Code Standard 6.

12. Please provide any comments on this standard and the proposed commentary.

2.23 BNZ considers that if Privacy Act requirements are met regarding 'personal information' as defined in that Act, then the obligation in this Code Standard should also be met. BNZ considers that an undue compliance burden would be placed on advisers if there was a requirement to comply with two separate privacy/confidentiality regimes. This should be expressly stated in the commentary to the Code Standard.

[Standard 7] Resolve complaints

13. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

2.24 BNZ agrees with the inclusion of Code Standard 7.

14. Please provide any comments on this standard and the proposed commentary.

2.25 BNZ considers that the definition of 'complaint' included in this Code Standard is potentially too wide, and could create compliance difficulties. BNZ considers that there should be a materiality threshold applied to the definition. Currently, the Code Standard appears to capture any client dissatisfaction, which would then trigger an adviser to have to undertake a resolution process.

2.26 BNZ notes that the standard is at odds against the current Code of Banking Practice which encourages complaints to be resolved immediately. The requirements for complaints to be dealt with independently may result in poor customer outcomes by extending the time to resolve complaints. BNZ submits that only 'where necessary', complaints should be dealt with independently.

2.27 BNZ assumes that the Disclosure Regulations will adequately cover information about the resolution of client complaints in addition to Code Standard 7.

[Standard 8] Not bring the financial advice industry into disrepute

15. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

2.28 BNZ agrees with the inclusion of Code Standard 8.

16. Please provide any comments on this standard and the proposed commentary.

2.29 BNZ does not have any specific comments on this proposed Code Standard and proposed commentary.

[Standard 9] Have general competence, knowledge, and skill

17. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

2.30 BNZ agrees with the inclusion of Code Standard 9.

18. Please provide any comments on this standard and the proposed commentary.

2.31 BNZ agrees with the requirement for individual financial advisers to have achieved the general qualification outcomes of the New Zealand Certificate in Financial Services (Level 5) or the National Certificate in Financial Services (Financial Services) (Level 5) as a minimum standard of general knowledge, competence, and skill.

- 2.32 BNZ considers that the Code Standard should be clarified as follows:
- a. Confirm whether the bullet-points under the headings 'individuals' and 'entities' are to be read as 'and' or 'or'; and
 - b. The following words should be added under the heading 'Nominated representatives': '... financial advice provider, the nominated representative (with the support of these procedures, systems, and expertise) has the capabilities equivalent to those'.
- 2.33 The reason for this suggested edit in bullet point 2 above is because BNZ is aware of confusion among market participants as to whether a nominated representative must attain a Level 5 Standard. This edit is designed to confirm that it is the overall output of the nominated representative, in conjunction with the financial advice provider's procedures, systems, and expertise, that must attain a Level 5 Standard.
- 2.34 BNZ submits that the way in which a Nominated Representative may demonstrate the standard should be revised. In the current draft, the wording appears to suggest that the burden for complying with standard 9 is directly on the Nominated Represents. BNZ suggests that it should be phrased from the Financial Advice Provider's point of view.
- 2.35 BNZ agrees with the inclusion of the ability for a financial advice provider to deliver advice through its nominated representatives, as this will improve accessibility. BNZ notes that quality control will be important in this regard.
- 2.36 BNZ considers that the flexibility provided for an entity (as a financial advice provider) engaging nominated representatives is appropriate. The proposed Code Standard appropriately provides that entities have procedures, systems, and expertise in place for nominated representatives to complete the learning outcomes specified for their role. This flexibility allows an entity to appropriately differentiate between different roles within the entity.
- 2.37 BNZ notes that flexibility and simplicity when applying Code Standard 9 will be important for nominated representatives who advise on simple products (i.e. deposit accounts). Additional processes and systems that support the nominated representatives should take a 'customer-centric' approach, rather than a 'compliance-centric' approach.

[Standard 10] Keep competence, knowledge, and skill up-to-date

19. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.38 BNZ agrees with the inclusion of Code Standard 10.

20. Please provide any comments on this standard and the proposed commentary.

- 2.39 BNZ notes that the proposed Code Standard also does not specify (nor limit) what must be done by an individual or an entity in order to keep competence, knowledge, and skill up-to-date.

- 2.40 Under Standard 19 of the current Authorised Financial Adviser ('AFA') Code of Conduct, AFA's are required to complete no less than 30 hours of structured professional development over the course of two CPD periods. There is no guidance in the proposed Code Standard of what is going to be required in the future. BNZ submits that more guidance is provided in the proposed commentary to this proposed Code Standard of what the minimum requirements on individuals and entities might be, and how this may be achieved through structured and unstructured continuing professional development.
- 2.41 BNZ considers that that proposed commentary to this proposed Code Standard should clarify whether a financial advice provider, nominated representatives, and individuals are required to maintain a professional development plan.

[Standard 11] Have particular competence, knowledge, and skill for designing an investment plan

21. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.42 BNZ agrees with the inclusion of Code Standard 11.

22. Please provide any comments on this standard and the proposed commentary.

- 2.43 BNZ considers that the Code Standard should be clarified as follows:
- Confirm whether the bullet-points under the headings 'individuals' and 'entities' are to be read as 'and' or 'or'; and
 - The following words should be added under the heading 'Nominated representatives': '... financial advice provider, the nominated representative (with the support of these procedures, systems, and expertise) has the capabilities equivalent to those'.
- 2.44 BNZ considers that for most KiwiSaver advice interactions, the investment planning requirements of the Level 5 qualification are likely to be too complex and may hinder the ease with which high quality customer conversations can occur. A distinction between KiwiSaver advice and an investment planning service may be helpful.

[Standard 12] Have particular competence, knowledge, and skill for other types of financial advice

23. Overall, do you agree or disagree with this standard and proposed commentary? (Agree/Neither agree nor disagree/Disagree/Don't know)

- 2.45 BNZ agrees with the inclusion of Code Standard 12.

24. Please provide any comments on this standard and the proposed commentary.

- 2.46 BNZ considers that the Code Standard should be clarified as follows:
- Confirm whether the bullet-points under the headings 'individuals' and 'entities' are to be read as 'and' or 'or'; and

- b. The following words should be added under the heading 'Nominated representatives': '... financial advice provider, the nominated representative (with the support of these procedures, systems, and expertise) has the capabilities equivalent to those'.

General questions

25: Is there anything missing from the code?

- 2.47 Yes.

26. If you answered yes, what is missing?

- 2.48 The current AFA Code of Conduct Standard 3 prevents an AFA from stating or implying that they are 'independent' if a reasonable person would not consider that this is the case. BNZ considers that this restriction should be included in the proposed Code. Nominated representatives may be restricted by the proposed Code in what they are able to be called. BNZ considers that financial advisers (including those employed by a Financial Advice Provider) should be able to use the term 'adviser' to describe themselves. BNZ considers that the alternative is that this issue is dealt with in the Disclosure Regulations.
- 2.49 BNZ supports the technology agnostic approach taken by the CWG. BNZ suggests that further work can be done to make the Code Standards more applicable to both natural people and robo-advice. BNZ notes that Code Standards 1 through 6 begin with the phrase 'a person', a better approach would be to use the phrase 'a person or entity'. In particular, the way those Code Standards are worded does not translate or resonate particularly well when read from a robo-advice or similar context. For example, how does a computer program "take reasonable" steps to ensure a person understands the financial advice?"
- 2.50 The current AFA Code of Conduct Standard 12 requires that AFA's must record in writing adequate information about any personalised services provided to a retail client. An equivalent standard has not been included in the proposed Code. BNZ understands the rationale for this is avoid being too prescriptive as to how records should be kept. However, BNZ considers that there should be some reference to adequate record keeping, even if tied into another Code Standard (possibly Code Standard 4 or Code Standard 5).
- 2.51 The proposed Code does not include an obligation to report Code breaches. BNZ considers that this requirement should be included in the draft Code.

27: Do you have any feedback on the examples, or suggestions on other examples that should be included?

- 2.52 No.

28: Is there anything else you want to say?

- 2.53 No.

CONCLUSION

- 3.1 BNZ appreciates the opportunity to provide this submission and supports the CWG's industry engagement on this matter.
- 3.2 Should the CWG have any questions in relation to this submission, please contact:

Paul Hay
Head of Regulatory Affairs

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