

In Confidence

Office of the Minister of Commerce and Consumer Affairs

Chair, Cabinet Economic Development Committee

Regulation of financial advice – code of conduct approval

Proposal

1. This paper informs Cabinet that the Minister of Commerce and Consumer Affairs intends to approve the attached Code of Professional Conduct for Financial Advice Services (the Code), which will apply to those operating in the new financial advice regulatory regime.

Background

2. The Financial Services Legislation Amendment Act 2019 (Amendment Act) introduces a new regulatory regime for financial advice and is intended to improve access to quality financial advice. The new regime will sit in the Financial Markets Conduct Act 2013 and is expected to come into force in mid-2020.
3. A key aspect of the new regulatory regime is the introduction of universal standards of conduct and client care. For example, anyone who gives regulated financial advice to a retail client (i.e. an everyday consumer) is required to give priority to a client's interests and disclose certain information to clients. In addition, they must comply with the Code, and meet standards of competence which are to be set in the Code.
4. The new regulatory regime is important for responding to some of the issues recently identified by the Financial Markets Authority (FMA) and the Reserve Bank of New Zealand in their conduct and culture reviews as they relate to financial advice situations. Further work is also underway to develop legislation containing additional conduct regulation of financial institutions to address other issues that have been identified.

An independent Code Working Group has developed the Code

5. An independent Code Working Group was established in August 2017 by the then Minister of Commerce and Consumer Affairs to develop the Code. The Group comprises nine members with expertise in the financial services industry or experience in consumer matters.
6. Under the current regulatory regime, 'authorised financial advisers' are subject to a Code of Professional Conduct (current Code) which is also prepared by an independent Committee. During a statutory review of the Financial Advisers Act 2008 the Ministry of Business, Innovation and Employment (MBIE) found that this arrangement was one of the successful elements of the current regime. Allowing industry experts to shape some of the detailed requirements of the regime ensured that those requirements worked in practice, and provided greater flexibility.

7. While the current Code was generally viewed positively, it could not simply be updated to fit with the new regime as it only applies to a small subset of financial advisers (predominantly investment advisers). In contrast, the new Code will apply to all financial advice, including advice given by mortgage or insurance brokers, bank staff and advice provided via a digital-advice platform.
8. Following extensive consultation, including two rounds of public submissions, the Code Working Group submitted the attached Code to me on 28 February 2019 for approval.
9. The Amendment Act sets out the process for approval of the Code. In accordance with this process, I have consulted the FMA. I am required to approve or decline the Code by the end of May (within 90 days of receiving the draft).

Content of the Code

10. The Code is required to include minimum standards of professional conduct that must be demonstrated by those who give financial advice. The Code includes nine standards which are generally principles-based in nature. For each standard, the Code provides commentary which is intended to assist compliance with the standards.
11. A number of the standards are similar to those in the current Code, while other standards from the current Code will move into the primary legislation (e.g. the requirement to give priority to a client's interests).

Part 1: ethical behaviour, conduct and client care

12. Part 1 of the Code provides the ethical, conduct and client care standards. These include requirements to treat clients fairly, to act with integrity, to give financial advice that is suitable, to ensure the client understands the financial advice and to protect client information.
13. I understand there was broad public support for the bulk of the standards contained in Part 1 and that the Code Working Group has responded to feedback it received.

Part 2: competence, knowledge and skill

14. Part 2 of the Code provides the standards of competence, knowledge and skill. These standards set the minimum standards of competence that those providing financial advice are required to meet, and includes ways that people may demonstrate that they meet the standard.
15. In essence, the Code requires anyone who gives advice to retail clients to meet a standard of competence that is equivalent to authorised financial advisers in the current regime. One way that a person can demonstrate that they meet this standard is by attaining the New Zealand Certificate in Financial Services (Level 5). Recognising the wide range of advice that may be provided, the new regime provides flexibility to allow people to demonstrate their competence through various means. For example, this may enable someone with a comparable overseas qualification, or a business with an established internal training programme, to demonstrate they meet the competence standards set by the Code.

Availability of KiwiSaver advice

16. The setting of competency standards is one area where there is a tension between the regime's objectives of promoting the availability of financial advice and the quality of that advice. I have heard some concerns that the competence standards could impact on the availability of KiwiSaver advice. The draft code will require anyone who gives financial advice on KiwiSaver to meet the same competency standards as someone who can provide advice on other investment products.
17. My officials sought further information from the Code Working Group regarding the rationale for applying the general investment competency standard to KiwiSaver advice and the impact this could have on the availability of advice.
18. I am advised that, in order to maintain the quality of financial advice, the Code Working Group is of the view that this standard is required in order to ensure that advice is suitable, even when that advice is limited to a client's KiwiSaver.
19. In addition, I have been advised that the new regime contains other measures that promote the availability of advice. For example:
 - 19.1. A person can demonstrate their competence with reference to their provider's procedures, systems and expertise.
 - 19.2. Advice on KiwiSaver can be provided through digital advice platforms.
 - 19.3. The industry has two years from the start of the new regime to work towards the new competence standards (I note that the investment strand can be completed in six months of part time study).
20. Based on the Code Working Group's response and my officials' advice, I am satisfied that the Group has carefully weighed the balance between the availability and quality of financial advice.
21. I have asked my officials to closely monitor the implementation of the new regime. Should they see a reduction in availability of advice, I would expect the Code Working Group to consider whether these standards need to be revised.

Considerations for approval

22. As required by the process set out in the Amendment Act, I am satisfied that:
 - 22.1. the majority of the Code Working Group approved the Code; and
 - 22.2. the Code Working Group complied with its obligations in the Amendment Act, including to prepare a document analysing the impacts of the proposed standards, along with a summary of submissions and brief responses; and
 - 22.3. the Code is consistent with the Financial Markets Conduct Act 2013 (as amended by the Amendment Act).

Consultation

23. In accordance with the process set out in the Amendment Act, I consulted the FMA before deciding whether to approve or decline the Code. The FMA recommended that I approve the Code, and advised that it is “fit for purpose and meets the requisites for approval under the legislation”. The FMA noted that it was concerned about the potential limiting of access to KiwiSaver advice (as outlined in paragraphs 16-21), but noted that the alternative means of demonstrating competence, and the flexibility built into the regime, should help to promote the availability of KiwiSaver advice.
24. The Code Working Group publicly consulted and ran various surveys and workshops in developing the Code. Feedback received throughout this consultation process has been used to develop the Code. Based on the Group’s summary of submissions, I am satisfied that they have responded to the issues raised in submissions.
25. The FMA, the Treasury and the Department of the Prime Minister and Cabinet (Policy Advisory Group) have been consulted on this paper.

Publicity

26. I intend to issue a press release announcing the approval of the Code.
27. The Code Working Group will arrange to have a copy of the Code, its impact analysis document and summary of submissions published.

Proactive Release

28. I intend to release the paper proactively in whole within 30 days. The Ministry of Business, Innovation and Employment will publish a copy of on its website.

Recommendations

The Minister of Commerce and Consumer Affairs recommends that the Committee:

1. **note** that the Financial Services Legislation Amendment Act 2019 will introduce a new regulatory regime for financial advice.
2. **note** that the Financial Services Legislation Amendment Act 2019 requires all those who give advice to retail clients to meet standards of competence and to comply with a code of conduct.
3. **note** that the Minister of Commerce and Consumer Affairs intends to approve the attached code of conduct submitted for his consideration by the Code Working Group on 28 February 2019.

Authorised for lodgement

Hon Kris Faafoi

Minister of Commerce and Consumer Affairs