AMP Financial Services

Submission on:
Consultation Paper – New Financial Advice Regime:
The draft Financial Services Legislation Amendment Bill and proposed transitional arrangements

31 March 2017

About AMP Financial Services ("AMP")

AMP comprises all of the AMP Limited New Zealand-based financial services businesses (excluding AMP Capital). AMP Limited is listed on the Australia and New Zealand stock exchanges. AMP has more than 150 Authorised Financial Advisers, the largest assemblage in the New Zealand market, and has a similar number of QFE Advisers. AMP's brands include:

AMP is a leading retirement savings provider and life insurer with more than 700,000 customers. It has around 20% of the contemporary life insurance market, the majority of the conventional life insurance market, approximately 12% market share of KiwiSaver funds, and the largest retirement savings master trust in New Zealand. AMP Services (NZ) Limited is a Qualifying Financial Entity and a Discretionary Investment Management Services licensee, AMP Wealth Management New Zealand Limited is a Managed Investment Scheme licensee, and AMP Life Limited is licensed insurer.

Spicers is a prominent investment planning provider with around $1.3bn in funds under management. Spicers Portfolio Management Limited is a Qualifying Financial Entity.

AdviceFirst is the largest financial advice business of its type in New Zealand, with ten offices nationwide, providing quality financial advice to individuals and businesses on life and health insurance, general insurance, investments, KiwiSaver, and home loans. AdviceFirst is majority-owned by AMP.

The new regime

AMP supports improving New Zealanders' access to high quality financial advice. The changes proposed in the Consultation Paper and consultation draft Bill are a step in the right direction. With the right adjustments and enhancements we believe the framework will be in place to deliver improved financial advice outcomes for consumers. It will be over to financial advice providers and their advisers to deliver, so getting the settings right is crucial.

Change won't be easy. Legislative overhauls in financial services have continually and significantly disrupted the industry in recent years. However, changes are needed because there are deficiencies in the current regime. Without such changes professionalising advice and improving consumer outcomes won't happen.

Delivering a more level playing field, including greater consistency in the requirements for advisers' skills, competence and knowledge, is laudable. We hope such improvements will contribute to addressing the under-insurance and suboptimal retirement savings planning in place for many New Zealanders today. And enabling robo-advice recognises contemporary developments and, critically, modern-day consumer demand.

We expect the main areas of discussion will be around the areas that we have identified. 'Client interests first' in particular we expect will receive a lot of comment. Getting this and other key components right and ensuring adequate clarity will be vital.

High Level Observations and Key Issues

Intent of the new regime: will the proposed changes deliver desired outcomes?

The new regime is intended to address the deficiencies of the current one, being:

- Some types of financial advice are not being provided
- The quality of financial advice may be suboptimal
- There are unbalanced compliance costs, and
- There is unnecessary complexity.

In principle, AMP supports making changes to address these failings. The consultation draft Bill goes a long way to address these. Examples include:

1) the removal of the Category 1 and Category 2 distinction. This has been a source of unnecessary complexity and stymied advice delivery on many low-risk Category 1 products. Removing this distinction is welcomed.
2) the four-tier adviser categorisation within the current FAA (AFAs, "RFAs", and QFE Advisers who may be either Category 1&2 or only Category 2 advisers). Whilst the new regime's proposed financial adviser and financial advice representative will be hotly debated it should reduce confusion for consumers, especially if disclosure is simplified as promised.

   Further opportunity to simplify the proposed regime exists, however. The prime example is not defining sole trader FAPs as financial advisers: this is a gap in our view.

In line with more recent guidance from the FMA some of the areas reformed are delivered in a more principles-based fashion. We believe that there is scope for greater clarity and precision in some of the key concepts introduced in the Bill. In our view, there is a balance required in this regard to ensure market participant efficiency and effectiveness, lest scores of participants expend undue effort interpreting and determining what they believe will be the FMA's stance on the more equivocal concepts. We address two of these under the headings which follow.

Definition and unclear implications of “client interests first”

We are supportive of a “client interests first” principle being central to the regime. That said, we think that the current drafting could result in unintended outcomes. For example, ensuring that an adviser’s advice is not materially influenced may be very hard to prove definitively, given the levels of commission provided by many product manufacturers of life and health insurance products particularly.

To illustrate: replacing an existing contract of life insurance will often result in a new upfront commission (typically ranging from 160% to 240%, depending on the provider) whereas amending an existing policy is invariably less lucrative for an adviser, where the renewal/trail commission is typically in single figures. Consequently a recommendation to replace an existing contract of insurance almost certainly involves material influence. It is arguably an impossibly high bar to demonstrate that that wasn’t the case, particularly in cases where the client benefit is modest and risks from the move are uncertain.

Clarity on “client interests first” we believe is required, including clearer drafting and subsequently specific guidance and examples. Relying on enforcement and/or trial and error learning would create a lot of uncertainly.

Unclear impact on business models – definitions of “engage” and “authorised body”

The definition of “engage” is critical to the operation of the new regime. The current regime caters for both employees of and nominated representatives of QFEs. *Appointing* a nominated representative requires an affirmative act by the QFE. Conversely, the concept of *engaging* a FA or FAR is nebulous. Consequently, this creates issues for FAPs like AMP. There are some actions (e.g. having a direct contract for services) that clearly qualify as “engaging” an individual as an FA or FAR. Others actions that could amount to “engaging” are not identified. For example, would “nominating” an FA or FAR as QFEs do today still suffice or is more intended to be required? Further, as a result of this lack of clarity, potentially simply having a distribution agreement with an adviser might be considered engagement? (If so, similar problems experienced with ss 5I and 20F of the FAA could be revisited). In summary, AMP considers that a clear and unambiguous definition, and/or guidance, is necessary to remove the uncertainty introduced by the term “engage”.

The concept of an “authorised body” is another definition that that, in our view, is not entirely clear. Its definition is broad (“an entity authorised under section 400 to provide a market service under the licence”). In our view, it is not in anyone’s interest for the regime to be introduced with uncertainty as to the basis of the relationship between FAPs, FAs, FARs and authorised bodies.

It appears that a FAP may have any number of authorised bodies/entities operating under its banner provided its licence conditions can be met. This appears to have some similarities to the existing regime’s QFE “associated entity” construct. This was an underutilised structure in the current regime — only nine QFE entities have associated entities — but the draft Bill is inexplicit in terms of how related an authorised body needs to be to a FAP.

Personalised and class advice removed

Removing the black-and-white distinction between personalised and class advice is consistent with the regularly repeated desire of the FMA for more advice to be given to consumers, for example, in relation to KiwiSaver.

Noting these intentions, we question whether the totally open-ended approach is efficient for the financial services market. Although prescriptive currently, and essentially binary (personalised and class for advice plus execution only for a no advice process), Code Standards 8 and 9 of the current AFA Code (as amended in December 2016) heralded a more fluid approach. This suggests a continuum of advice methods and approaches is necessary. In our view, this will be especially so for FAPs who engage FARs because they will be required to specify the activities and processes followed by their FARs. It might therefore be the case that, to mitigate the limitless optionality the new regime permits, ensuring processes are specified, and licensed accordingly, the industry nevertheless retains some of the certainty advantages of the current regime (essentially three processes: a six step personalised advice process, a class advice process, and a no advice process).

Financial advisers and financial advice representatives

The convergence of “financial advisers” and “financial advice representatives” in terms of meeting standards is welcomed. AMP already expects the same standards of its QFE Advisers as it does of its AFAs and we are supportive of levelling of the playing field on this point across the industry.

We see a significant net benefit if FARs are required to be registered on the FSPR; this is another opportunity to ensure consistency, balance and remove confusion for consumers (i.e. why is person ‘A’ who provides advice on a list but person ‘B’ who provides advice not?).

We also believe that the terminology currently proposed insufficiently distinguishes between FAs and FARs. If the term “financial advice representative” is retained, FARs should be required to present themselves to consumers, including on their consumer-facing business cards, etc., with a set designation: *{Provider} Financial Advice Representative*. It is imperative that that this distinction is clear to consumers. Moreover, in our view, there should be stronger restrictions on how persons who are not of FA or FAR status can hold themselves out in a manner that appears they give financial advice. It must be clear that sales roles that do not provide advice are not capable of being misinterpreted by consumers as being something that they are not. We question whether the holding out provisions in s 431D are sufficient in this respect and we believe this area warrants rigorous enforcement, otherwise sales roles may be misunderstood by consumers as being advisory in nature.

AMP's responses to the specific questions posed

Part 1 of the Bill amends the definitions in the FMC Act

1 If an offer is through a financial advice provider, should it be allowed to be made in the course of, or because of, an unsolicited meeting with a potential client? Why or why not?

Yes, it general it should be allowed, though there should be some restrictions (refer our answer to questions 2and 3).

Subject to our comments in response to questions 2 and 3, any meeting regarding an offer made through a FAP would be with the FAP if they are an individual, a financial adviser (FA) or financial advice representative (FAR). All three will meet the necessary competency requirements and will have a duty to act in the best interests of the customer, so the customer will be significantly protected from being negatively impacted.

Restrictions may potentially prevent consumers getting access to products and advice. Where *advice* is provided carving out FAs and FARs makes sense because they will be subject to conduct requirement. If they are not excluded there's potential to curb or significantly curtail the ability to advise on financial products; even approaching people at a trade fair would be questionable, which is an undesirable outcome when so many consumers need more access to financial advice rather than less.

2 If the exception allowing financial advice providers to use unsolicited meetings to make offers is retained, should there be further restrictions placed upon it? If so, what should they be?

Yes, restrictions should be:

a) that certain activities (prescribed by the FMA) include a 'pause', followed by documented advice. A documented standard for replacement transactions of a kind where poor outcomes have a higher likelihood (e.g. replacement risk insurances where full appreciation of the complexity and risks involved is necessary) should be required. This approach would align with the desire to have necessary information provided to consumers, and at the right time. It would be consistent too with the incumbent Code for AFAs, which expects the type of service to be suitable for the client. A replacement risk transaction completed during an unsolicited meeting using an undocumented advice process has a high risk of a poor consumer outcome
b) a 'free look' or 'cooling off' period to apply to sales resulting from unsolicited meetings, unless product terms already provide for this, and
c) there must be financial advice provided, not information only, so duties in relation to advice apply.

In addition, we note that from a policy perspective it is hard to distinguish the consumer protections required whether the meeting was "unsolicited" by the FAP or whether a consumer approached the FAP for an entirely different purpose and the FAP proposed the sale of its financial product. E.g. you visit your bank branch to make a deposit and are offered an interest in a MIS. In such circumstances consumer protection should be built-in, otherwise consumers could be sold products manufactured or distributed by FAPs with insufficient protection. This is commented on in more detail in the answer to question 3, below.

3 Do you have any other feedback on the drafting of Part 1 of the Bill?

Clause 5(2) of the Bill: Retaining the use of "broker", meaning a money-handler/property-handler, should be re-evaluated. The term "broker" is casually used in the industry. It has been a source of confusion for advisers and others; for example, in registering incorrectly on the FSPR. The use of the terms "insurance broker", "mortgage broker", etc., are common, however, they are rarely 'brokers' in a FMCA s 431Q sense.

Clause 5(2): The definition of "financial advice provider" is "a person that provides a financial advice service". This includes both corporate and natural persons. Sole traders can register as financial advice providers. Consequently that provider would be capable of providing advice without being a financial adviser (s 431C(b)). Consequences of this construct include:

a) A third category of adviser is created: *sole trader FAPs* in addition to FAs, and FARs (plus arguably a fourth category FAPs who provider roboadvice only). This contradicts the aim to simplify the regime.
b) It could result in sole trader FAPs being unable to describe themselves as 'financial advisers', but rather restricted to using the term 'financial advice provider' which may be meaningless to customers.
c) It creates a gap in the disciplinary proceedings provisions. As it is proposed, only FAs are in scope. We discuss this further under question 30.

A solution to this complexity could be to re-define financial adviser by adding to paragraph (b) of that term's definition "(b) does not include a financial advice provider, *except where the financial advice provider is a natural person*".

Clause 5(2): The definition of "financial advice representative" uses the term "is engaged (whether as an employee or otherwise) by a financial advice provider". It is not clear to us (and MBIE has been unable to clarify) whether this concept will extend to individuals who are only indirectly linked to the FAP (e.g. where a contract is with a firm that itself has contracts with advisers). The wording here is inadequate insofar as it leaves the answer to that question equivocal. We believe clearer drafting is needed to:

a) state whether engagement needs to be direct, and/or
b) whether "engaged" encompasses the "nominated representative" construct of s 74 of the FAA.

Clause 5(2): The term 'financial advice representative' may be meaningless to customers. AMP's view is that a prefix indicating the FAP's trading name is necessary. Consumer-facing identification of the FAR should be required to use the prefix and the prescribed term. For example, "AMP Financial Advice Representative" makes it clear to consumers that the adviser provides financial advice but is unmistakably associated with AMP. This would work well in parallel with simplified disclosure in making it obvious to consumers who the representative is working for. There should be stronger restrictions on how persons who are not of FA or FAR status can hold themselves out in a manner that appears they give financial advice. Sales roles, which do not provide advice, should not be capable of being misinterpreted by consumers as being something that they are not. The holding out provisions in s 431D should be reviewed and strengthened in this respect. We also believe this area needs rigorous enforcement. Safeguarding consumers by ensuring that advice is provided only by qualified FAs and FARs is essential. This will also contribute toward professionalising the occupations that deliver high quality financial advice to consumers.

Clause 10 of the Bill: the amendment to s 34(2)(b) uses the term "through a financial advice provider". The intention here is probably to include FAs and FARs as the conduit, however, with FAPs being able to provide roboadvice, conceivably a misinterpretation could be made (reading it as applying only to FAPs and not FAs nor FARs). Clearer drafting on this would help.

Section 34 of FMCA should cover both a "financial product" and a "financial service" and the exceptions in s 34(2) should also apply to the offer of both financial products and financial services. This is necessary to ensure that the sale of financial services through a FAP, such as investment platforms, is not restricted.

Second, the definition of "financial products" in s 34 of the FMCA ought to cover all "financial advice products" (as currently defined in the Bill). This should be hard-coded into FMCA rather than relying on Regulations that will be drafted in accordance with s 18(b) of FMCA. Contracts of insurance, DIMS facilities, and consumer credit contracts all need to be included in the definition of "financial products".

It is also particularly important that "contracts of insurance" captures all types of contracts of insurance as currently defined in the Financial Advisers Act 2008 including:

- an investment-linked contract of insurance
- a life insurance policy (within the meaning of s 2(1) of the Securities Act 1978) issued before 1 January 2009, and
- any other contract of insurance.

It is our view that the current drafting in s 34(2)(b) of FMCA needs to be revisited in light of its policy purpose. The rationale for the exception in s 34(2)(b) appears to be that the consumer protection offered by s 34 isn't required where the offer is through an AFA or QFE adviser because the offer will be accompanied by advice. However, s 34(2)(b) does not contain any requirement for the offer to be accompanied by advice and therefore includes execution only and information only offers within the scope of the exception. As noted above, in our view, amendments should be made to s 34 to address this by providing that the exception applies only where the relevant offer is actually accompanied by financial advice.

It follows that the current exemption that is provided in clause 4 of the Fair Trading (Uninvited Direct Sales – Financial Products) Regulations 2014 will also need to be updated. AMP recommends that this should be updated both in terms of the scope for products and services and our suggested criteria of the offer being accompanied by advice.

Part 2 of the Bill sets out licensing requirements

4 Do you have any feedback on the drafting of Part 2 of the Bill?

Clause 20(2): The new paragraph (d) to s 403(3) enables the FMA to invoke conditions on a FAP by restricting the types of financial advice that may be provided by a FAR. This does not seem to have factored FAPs that have both FAs and FARs. That is, is the intention to only restrict the FARs but not the FAs of a FAP?

Clause 20(2): The new subsection (4) to s 403 appears to provide the FMA with powers that extend beyond the Act in determining certain circumstances where consumers must be treated as retail clients. This power appears to be unnecessary (provided the definitions of retail and wholesale clients are sufficiently prescriptive).

Part 3 of the Bill sets out additional regulation of financial advice

5 Do you agree that the duty to put the client's interest first should apply both in giving the advice and doing anything in relation to the giving of advice?
Yes, in principle, though for this to work in practice it needs to be clear when the duties apply. The current drafting is ambiguous and so unworkable in practice.

Does this make it clear that the duty does not only apply in the moment of giving advice?

It is clear that it applies not only in the moment of giving advice, but, in using the language as drafted, it is unclear how far it extends. This makes it difficult for AMP to support the extension of this duty. Clarification is required.

6 Do you have any comments on the proposed wording of the duty that a provider must not give a representative any kind of inappropriate payment or incentive? What impacts (both positive and negative) could this duty have?

First, s 431O(1)(b) is ambiguous: "*must not give, or offer to give, (whether conditionally or unconditionally) to any of its representative any kind of inappropriate payment or other incentive.*" because "*or other*" is not necessarily connected to "*inappropriate*" and could be read as "or other incentive of any kind". This needs fixing: we suggest "any kind of inappropriate payment or other inappropriate incentive."

Clarity on the specifics of what is "inappropriate" is desirable. For example, would an offshore conference where alcohol is served be inappropriate per se? Although s 431O(2) notes "inappropriate" is where the payment or incentive "is intended to encourage, or likely to have the effect of encouraging, the representative to engage in conduct that contravenes" specified duties, a blacklist of incentive types is desirable to remove uncertainty.

We reiterate our previous submission on the FAA *Options Paper*: AMP supports more transparent and complete disclosure of the remuneration derived from a particular transaction as this would assist in providing transparency to the consumer, enabling more informed inquiry as to how his or her interests are being met. This should include disclosure of all remuneration that is directly or indirectly paid to the adviser as a consequence of that transaction. A value must therefore be attributed to any soft commissions that are payable or any bonus payable based on volumes. In our view if an adviser is unable to quantify the commission earned such a commission should not be paid. To this end disclosure that the adviser might be eligible for an off shore trip would not be sufficient. Additionally it provides a more fact based point of inquiry for FMA to assess whether conflicts have been appropriately managed.

We are also concerned that the same requirement is not proposed for incentives/payments to FAs. Incentives to FAs are as, or more, prone to driving undesirable behaviours. Further, with the desire to have similar standards applying to advice, applying similar standards to incentives seems to have been overlooked. We consider this concern would be largely addressed through the client-first duty, which would prevent FAPs, FAs and FARs participating in remuneration or other incentive arrangements that create a conflict of interest. Any specific residual areas of concern could be addressed through code standards. However, if such a rule is to be retained in primary legislation, we would recommend it should apply consistently to all inappropriate incentives offered by both FAPs and providers of financial advice products to FAPs, FAs and FARs.

7 Do you support extending the client-first duty to providers who do not provide a retail service (i.e. those who only advise wholesale clients)? Why or why not?

We think the question should be considered in reverse – i.e. under what circumstances is it considered diligent and skilful to recommend a wholesale client something that is distinctly not in their interest? Asking the question that way we think makes it desirable that advice that puts the client's interest first should apply by default. However, we recognise that there may be some market participants significantly impacted by this. For such participants whose clients' needs do not necessitate an adviser putting their interests first we believe specific carve-outs should be listed rather than having the currently total exclusion for wholesale clients. We are supportive of opting out for clearly wholesale clients where information and expertise inequality is a non-issue (e.g. advice relating to investments given to fund managers).

We submit that the default position should be for the client-first duty to prevail. The paramount reason is to ensure protection for those consumers who are deemed wholesale (by default under the proposed FMCA Schedule 5, clause 3(1)) not necessarily because of their knowledge/expertise/corporate status but rather by exceeding a bright line (including clause 3(1)(c)(i), which classifies a client with merely $1m in net assets as a wholesale client). There are thousands of consumers who have more than $1m in net assets by virtue solely of the value of their home, for example, who would be deemed wholesale clients and consequently not protected by the regime. Opting out of being wholesale is not the answer: it seems appropriate to ensure that such consumers should be protected by their advisers putting their interests first.

8 Do you have any other feedback on the drafting in Part 3 of the Bill?

Clause 24 – the new s 431B: Paragraph (b) of subsection (1) introduces "designs an investment plan" into the definition of financial advice. The reason for this is not clear. An investment plan inevitably includes making some form of product recommendation/suggestion so, arguably, including this is redundant. However, if it is added with a clear reason in mind then it would be very useful to know what the driver for this addition is.

Further, in paragraph (b), "investment needs" and "investment goals" are used, yet not defined. These terms are not helpful: a needs analysis, for example, should not only look at *investment* needs, but the client's needs generally. Similarly, considering only *investment* goals (which may be very specific) may be insufficient to ensure that the client's overall financial goals are achieved. To illustrate, a life insurance policy may form part of clients' overall goals to protect their dependants, yet if only *investment* goals are considered when formulating a plan it could ignore this material factor, which could mean a totally different investment plan is required to meet the clients' overall financial goals.

Clause 24 – the new s 431E: the word "financial" is missing from "adviser" and "financial advice" from "representative" in a number of places.

Clause 24 – the new s 431G: the term "reasonable steps" will be crucial now that the clarity of class versus personalised advice has been forgone. Guidance is necessary. Alternatively, an example of reasonable steps should be included (as is provided for some other sections, e.g. s 431L)

Clause 24 – the new s 431H: we question whether the heading should be reworded to reflect managing conflicts, which has been noted as the purpose of this section at the consultation meetings.

However if the policy purpose is broader, having this duty apply only where there "is a conflict between" the client's and any other person's interest is not sufficient. Instances where the other person's interests are advanced to orders of magnitude greater than the client's should also be caught by the subsection (1) requirement. Requiring the *primary motivation* for the advice being the client's interests and not the adviser's is necessary. Subsection (2) seems to do this, but with the current drafting it could be interpreted as only applying if the hurdle in subsection (1) has not been triggered ("This *section* applies if…there is a conflict between…the interests"). It is common for the interests of the parties not to conflict but the motivation for the advice to be overwhelmingly biased towards an adviser's benefit, notwithstanding the client's interests may appear to be marginally benefited.

Finally, guidance on "material influence" will be critical because most life insurance sales in New Zealand are remunerated by commission. That of itself lends itself to influence as different providers pay different rates of commission. There is an inherent conflict in any arrangement whereby the Adviser can get paid more by one provider than another yet the differentials in the products are frequently low.

Clause 24 – the new s 431J: Subsection (2) requires compliance with the Code only to a retail service. This may be problematic for advice that is provided predominantly to wholesale clients but where there are mixed wholesale and retail clients. In such a scenario 'contamination' of retail requirements on wholesale advice would occur. Notwithstanding our recommendation of defaulting treatment of wholesale clients as being eligible for 'client interests first', having the retail service requirement for the Code compliance is unnecessarily wide. A fix for this would be to re-draft s 431J as "A person who gives regulated financial advice to a retail client must comply with the standards of ethical behaviour, conduct, and client care required by the code of conduct."

Clause 24 – the new s 431L: Subsection (1) says "A person who gives regulated financial advice must, at the request of a prescribed person or at the prescribed times or on the occurrence of the prescribed events …." We think "or" in both places should actually be "and" for the requirement to make sense.

Clause 24 – the new s 431N: Requiring FAPs to ensure that all FAs engaged by a FAP comply with ss 431F to 431M needs to be clarified. The FAA ss 5I and 20F caused extensive reworking of contractual arrangements with non-aligned AFAs and RFAs due to the responsibility for advisers' advice that those sections introduced. The definition of "engage" needs clarification – specifically it needs to be stated that "engage" does not include arrangements with a FA that enables that FA to simply *sell* a financial product provider's products. If this is not clarified, conceivably any contractual arrangement in the market enabling an FA to sell a provider's product(s) could require the provider to take responsibility for that FA's advice. This could be clarified by adding a second sentence to s 431N stating that simply enabling a FA to sell a provider's product does not constitute engagement for the purposes of s 431N.

Clause 24 – the new s 431O: As noted above (answer to question 6), we think "inappropriate" needs clarification as it is subjective and will be difficult to apply in practice. Also, the rationale for limiting this section only to FARs is unclear. Section 431N applies to FAs and FARs yet s 431O, which appears under a heading encompassing both FAs and FARs, only applies to FARs.

General: Guidance in relation to "client interests first" is crucial. In Australia, the "client interests first" has been addressed in ASIC guidance: RG 175.371 to RG 175.378. (*http://download.asic.gov.au/media/1240967/rg175-published-3-october-2013.pdf*)

Part 4 of the Bill sets out brokers' disclosure and conduct obligations

9 What would be the implications of removing the 'offering' concept from the definition of a broker?

None are foreseen, provided any advertisement for broking services is required to be in a way that is not misleading, deceptive or confusing.

10 Do you have any other feedback on the drafting of Part 4 of the Bill, for example any suggestions on how the drafting of broker provisions could be simplified or clarified?

We recommend that brokers require a licence rather than simply carrying over the position from the Financial Advisers Act. This would help to resolve the uncertainty as to who is a broker, given the significant numbers of firms that are either incorrectly registered as brokers or have incorrectly failed to register as a broker. This would also enable the FMA to more clearly understand and regulate the broking population. It is an anomaly that this sector of the market remains unlicensed.

We repeat our suggestion (refer answer to question 3, above) that the use of the word 'broker' should be avoided.

Part 5 of the Bill makes miscellaneous amendments to the FMC Act

11 Should financial advisers have direct civil liability for breaches of their obligations, if the financial advice provider has met its obligations to support its advisers? Why or why not?

Yes, they should, particularly because the FADC has yet to have any deterrent effect and, in our view, its jurisdiction is insufficient to deal with egregious behaviour. Having direct civil liability would add accountability and provide an extra distinction between FAs and FARs, which have converged significantly through the FAAR review process.

12 Should the regime allow financial advice providers to run a defence that they met their obligations to have in place processes, and provide resources to enable their advisers to comply with their duties?

Yes.

13 Is the designation power for what constitutes financial advice appropriate? Are there any additional/different procedural requirements you would suggest for the exercise of this power?

Yes, the power appears appropriate.

14 Do you have any feedback on applying the concept of a 'retail service' to financial advice services? Is it workable in practice?

In practice that is how retail versus wholesale is managed under the securities disclosure regime – i.e. if the security is offered to one retail client, or could be offered to one retail client, providers treat it as retail. However, refer to our previous comments on 'retail service' in the submission to question 8, above, as we believe that there is a preferred solution to ensuring workability.

15 Do you have any other feedback on the drafting of Part 5 of the Bill?

Clause 26 inserting s 432A (replacing s 392): what is the significance of the change from "provides" to "gives" in the definition of discretionary investment management service?

Clause 29(2) inserting s 451(2) is referential and arguably tautologous. The intention is to exclude those who are only financial advice service licensees and not holders of another type of FMC licence. Improved drafting would achieve this and make it clear.

Clause 50: although this makes amendments to Schedule 1, clause 21 of the Act, the heading to clause 21 also needs to be amended to remove reference to “category 2”.

Part 6 of the Bill amends the FSP Act

16 Does the proposed territorial application of the Act set out above help address misuse of the FSPR? Are there any unintended consequences? How soon after the passing of the Bill should the new territorial application take effect?

Improving the integrity and standing of New Zealand financial services providers should be encouraged. Unless there are impracticalities, implementation of territorial provisions should be made as soon as practicable.

We question whether the FSPR is needed in its current form. It arguably confers a standing on those registered that does accord with the regulatory reality. We recommend it is restricted to licensed entities, FAs and FARs. We believe that as New Zealand has moved towards a licensing regime for its financial markets participants the original purpose of the legislation has been superseded.

17 Do you support requiring further information (such as a provider’s AML/CFT supervisor) to be contained on the FSPR to help address misuse?

If the FSPR is retained, except where further information would consume undue resources or costs on FSPs, we support requiring further information to help address misuse of the register. Unless the supervisors are able to audit the entries, however, we question the benefit of providing the details of the AML/CFT supervisor.

We see other improvements to the FSPR as being more worthy. The prime example is extending the register to include FARs. All providers and individuals who provide advice should be registered in a uniquely identifiable and immutable form. The changeover to a new regime provides a unique opportunity to clean the slate and address this gap and the challenges posed by not having QFE Advisers on the register and the register including multiple entries for some individuals due to flawed initial design. The notional extra work involved for providers will be more than offset by the benefits of requiring all those who provide financial advice to be included. FAPs will need to have comprehensive lists of their FARs so as to provide those lists to their DR Scheme. Provided there is an industry standard upload format, a bulk upload-and-replace format and mechanism for FARs could be developed to enable this enhancement

18 Do you consider that other measures are required to promote access to redress against registered providers?

The issue of being unable to pursue complaints through disputes resolution schemes when the provider/adviser is no longer a member of the Scheme requires consideration.

19 Do you have any comments on the proposed categories of financial services? If you’re a financial service provider, is it clear to you which categories you should register in under the proposed list?

Again, it would be advantageous to register FARs as well, so they can be tracked when they move between FAPs (or, potentially belong to more than one FAP, which is permitted).

Use of the word “broking services”. Again, this should be reconsidered because “broker” has been confusing to FSPs – e.g. many AMP nominated representative AFAs included this in error because they provided mortgage broking as a service. Arguably they should have known better, but from a consumer perspective "broker" is not used in the FMC context – it commonly means insurance broker or mortgage broker, and they do not necessarily handle client money or property.

20 Do you support clarifying that schemes must provide information to the FMA if they believe that a provider may be involved in conduct that constitutes breach of relevant financial markets legislation?

A materiality threshold should apply. Schemes should require more than mere suspicion that the FMCA has been breached. Schemes are experts in complaints, not necessarily in the FMCA or licensing, so controls to ensure that there are not unnecessary notifications being made to the FMA should be put in place. Enquiries to the FAP may determine that there's no issue.

21 Do you have any other feedback on the drafting of Part 6 of the Bill?

Schedule 1 of the Bill sets out transitional provisions relating to DIMS and the code of conduct

22 When should an FMC Act DIMS licence granted to AFAs who provide personalised DIMS expire? For example, should it expire on the date on which the AFA's current authorisation to provide DIMS expires?

Merging FMC and FAA DIMS creates challenges. The current FAA DIMs should expire at the point that the FAP provisional license for the FA's FAP starts. There are complications in merging FMCA and FAA DIMS, e.g. where an AFA provides FAA DIMS and simultaneously FMCA DIMS via a FAP's Wrap platform.

23 Do you have any other feedback on the drafting of Schedule 1 of the Bill?

No.

Schedule 2 of the Bill creates a new schedule to the FMC Act with detail about the regulation of financial advice

24 Should the FMC Act definition of 'wholesale' be adopted as the definition of wholesale client for the purposes of financial advice? Why or why not?

Yes, and what is required is a consistent definition and one that does not automatically treat as wholesale "wealthy" clients (merely $1,000,000 in net assets is a very low threshold). Balance is required to ensure protections including "client interest first" are not lost.

25 We understand that some lenders consider that they may be subject to the financial adviser regime because their interactions with customers during execution-only transactions could be seen to include financial advice. Does the proposed clarification in relation to execution-only services help to address this issue?

While we understand that the proposed clarification is intended to address those circumstances where execution only is occurring, there is an equal but opposite concern where execution only is purported to be used as an expedient means of completing a transaction without documented advice following an advice process.

We recommend making further improvements that make it clear that execution only cannot occur at the end of an advice process.

26 Are there any unintended consequences resulting from the minor amendments to the exclusions from regulated financial advice, as detailed above?

We have concerns about the following:

Schedule 5, clause 9(1)(b) – it is not clear why trustee corporations providing estate management should be excluded (where that involves advising clients on financial products).

Schedule 5, clause 10 – it is not clear why non-profit organisations should not be required to meet requirements of regulated financial advice. The consumers provided advice by a non-profit organisation may receive poor financial advice. Just because the organisation does not have profit as a motivator does not automatically mean that the advice they provide will be "good" or necessarily put the "client interests first".
If this exclusion is to be retained, it should not include non-profit organisations who have a material interest in or provide their own financial advice products (or financial advice products of related entities), noting there are licensed providers that are non-profit.

27 Do any of the membership criteria or proceedings for the code committee require further clarification? If so, what?

We question whether the membership expertise is sufficiently prescriptive – only two of the potentially 11 positions are specifically earmarked for consumer or disputes resolution experts. We are supportive of a broad-based membership of the working group/committee to provide a wide perspective and we think it is desirable to specify minimum competency/skills for more than the two currently specified.

A prescribed number of the members of the committee should be required to be representative of the financial advisory industry. This is to ensure representation of financial advisers as well as adding credibility.

The quorum for meetings should align to the actual number of committee members finally determined and also consideration should be given to requiring some of the members to be mandatory (e.g. the ones with key knowledge of the industry).

28 Does the drafting of the impact analysis requirement provide enough direction to the code committee without being overly prescriptive?

29 Does the wording of the required minimum standards of competence knowledge and skill which 'apply in respect of different types of advice, financial advice products or other circumstances' adequately capture the circumstances in which additional and different standards may be required?

This seems to balance precision and flexibility adequately.

30 Should the Financial Advisers Disciplinary Committee consider complaints against financial advice providers as well as complaints against financial advisers? Why or why not?

In all cases where FMA has the option of pursuing FADC action or civil proceedings there needs to be double jeopardy rules to ensure that FMA does not pursue the same conduct in two forums.

An issue is that sole trader FAPs are out of scope of the FADC because they are not FAs. This gap should be plugged – our suggestion is that sole trader FAPs should be automatically deemed financial advisers by including them in the definition of financial adviser. This would simplify the regime and place the same duties on sole trader FAPs, who, in reality are simply financial advisers who do not group together.

A general concern we have with the FADC is unrelated to its jurisdiction. The FADC has been underutilised and unproductive: it has made no decisions for over two years, and only one in 2014. The intention of the FADC was to be a quick and efficient tribunal; its website says it is there:

- to conduct disciplinary proceedings arising out of complaints regarding AFAs referred to it by FMA; and
- to impose a range of penalties ranging from recommending to FMA that it cancel the AFAs authorisation to imposing a fine not exceeding $10,000 as a result of the disciplinary proceedings

It is hard to believe that there has been not even one instance in over two years where an AFA has been assessed by the FMA as inadequately meeting even one Code requirement. The use of fines has been almost totally absent from the current regime; that deterrent aspect/opportunity has been lost. The role, productivity, etc. of the FADC requires review, not just its jurisdiction.

31 If the jurisdiction of the Financial Advisers Disciplinary Committee is extended to cover financial advice providers, what should be the maximum fine it can impose on financial advice providers?

Elsewhere in the FAA it's commonly five times an individual's potential penalty so applying that multiple seems appropriate. The maximum individual fine may be worth reviewing.

32 Do you have any other feedback on the drafting of Schedule 2 of the Bill?

Schedule 5, clause 27 (funding of code committee) specifies the FMA as funding the code committee. This should be funded by MBIE until the new legislation and code drafted for it comes into force. The initial drafting of the code seems to be a policy matter more appropriately funded by MBIE.

About transitional arrangements

33 Are there any other objectives we should be seeking to achieve in the design of transitional arrangements?

Ensuring consumers are fully informed of transitional aspects where they may experience a lesser service from one FA/FAR versus another due only to the fact that one has transitioned yet another has not. Absolute clarity to the consumer on who is liable for the advice during the transitional period is required.

Proposed transitional arrangements

34 Do you support the idea of a staged transition? Why or why not?

Yes we support a staged transition because there is a lot of change and the current QFEs, AFAs, and especially RFAs will have a lot to take in and adjust to, including uncertainty created by the new Code being unavailable until August 2018.

35 Is six months from the approval of the Code of Conduct sufficient time to enable existing industry participants to shift to a transitional licence?

It is impossible to answer this question confidently since it depends on the content and scope of the code. We expect for many participants it will be sufficient provided the requirements are akin to simple registration rather than meeting 90% of the requirements of a full licence.

36 Do you perceive any issues or risks with the safe harbour proposal?

We consider 2021 for the expiration of the safe harbour is appropriate and gives those in the industry who may choose to exit plenty of time to manage that exit. This is particularly relevant given the average age of advisers. However, the obvious risk of this is that it postpones the requirement for RFAs through to 2021, which delays the realisation of the intended outcomes of the legislation.

37 Do you think there are any elements of the new regime that should or shouldn't take effect with transitional licences? What are these and why?

We support the proposals in the Consultation Paper. We believe the core legislative obligations and duties should apply so that the benefits of the regime are realised at the earliest opportunity whilst recognising that other obligations will require individuals time to upskill/train.

38 Is two and a half years from approval of the Code of Conduct sufficient time to enable industry participants to become fully licensed and to meet any new competency standards?

Yes, this should be adequate. Though it could be shorter, we acknowledge the capacity to licence the numbers of participants involved will be constrained for the FMA.

Possible complementary options

39 Do you support the option of AFAs being exempt from complying with the competence, knowledge and skill standards for a limited period of time? Why or why not?

No, there does not appear to be good justification for AFAs to be allowed until 2026. They should be able to upskill where required within the general two and a half years (or earlier) transitional timeframe. It is RFAs who face a greater upskilling requirement.

40 Would it be appropriate for the exemption to expire after five years? If not, what timeframe do you suggest and why?

Refer above.

41 Is there a risk that this exemption could create confusion amongst industry and for consumers about what standards of competence, knowledge and skill are required

Yes, it defeats the goal of having everyone subject to the same requirements by delaying the implementation by a further 5 years. For that reason the exemption should not be provided. It would create a two-tier hierarchy: "real" qualified advisers and "ad eundum" advisers and an unlevel playing field.

42 If you support this option do you think it should be set in legislation or something for the Code Working Group to consider as an option as it prepares the Code of Conduct?

N/A.

43 Do you support the option of a competency assessment process for existing AFAs and RFAs? Why or why not?

In principle we believe competency assessment is appropriate in some circumstances to demonstrate that aspects of the required standards have been met. In other aspects we believe that demonstrating competency via the same mechanism required of new entrants is appropriate. By way of example, if demonstrating competency in giving advice, a competency assessment would be appropriate. If however, it involves additional knowledge about the regime requiring AFAs to complete those new/enhanced requirements is reasonable provided there is sufficient time (and February 2021 seems reasonable). Similarly, RFAs should be able demonstrate competence in the same way as AFAs.

One of the criticisms at the introduction of the regime last time was the lack of recognition of experience in the field.

If the final decision is to allow this exception, we believe that it needs to be delivered by a competent body with oversight to ensure consistent standards. It should not be delegated to FAPs.

44 Is it appropriate for the competency assessment process to be limited to existing AFAs and RFAs with 10 or more years' experience? If not, what do you suggest?

Competency is not necessarily linked solely to time in the industry. There are some competent advisers who have been operating for only a few years yet others who have been around for decades who are not. If an alternative assessment process is allowed it should impose some 'years of experience' requirement to prevent someone who had just started out before the new regime from taking a shortcut. Ten years may be too much. Additional criteria should also be added though – e.g. a sufficient portfolio of verifiable documented advice provided prior to assessment.

45 If you support this option do you think it should be set in legislation or something for the Code Working Group to consider as an option as it prepares the Code of Conduct?

Purely for timing and consistency purposes it may be more appropriate for the Code Working Group.

Phased approach to licensing

46 What would be the costs and benefits of a phased approach to licensing?

The main benefit is it would allow the FMA and participants to migrate at a considered pace.

A drawback is potentially FAPs that are not QFEs today may be unable to engage FARs until they get a licence, so if they are in the latter groups they may be impacted.

47 Do you have any suggestions for alternative options to incentivise market participants to get their full licences early in the transitional period?

Without financial or other incentives to go early it is unlikely that participant behaviour will change and there will be bottlenecks that impact the FMA and participants.

48 Do you have any other comments or suggestions regarding the proposed transitional arrangements?

Clarify that existing FAs and FARs who switch employers will be able to continue operating under the transitional licence of the FAP without having to upskill at the point in time they switch FAPs.

Demographics

49 Name

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50 Contact Details

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51 Are you providing this submission

☐As an individual
☒On behalf of an organisation

Refer cover page for details