

The Manager  
Financial Markets Policy  
Building, Resources and Markets  
Ministry of Business, Innovation & Employment  
PO Box 1473  
Wellington 6140

Also by email: [faareview@mbie.govt.nz](mailto:faareview@mbie.govt.nz)

**Submission: Consultation Paper – New Financial Advice Regime: The draft Financial Services Legislation Amendment Bill and proposed transitional arrangements ('Consultation Paper')**

This Submission has been made by Graham Duston in his personal capacity as an Authorised Financial Adviser. Graham Duston is also the Executive Director of Funds Administration New Zealand Limited ('FANZ'). The views expressed in this Submission are the author's own and do not necessarily represent the views of FANZ.

**1. Support for the flexibility offered by the new regime**

The writer supports the flexibility offered by the proposed regime, which will enable providers to pursue a financial adviser-based model, a financial advice representative-based model, or a combination of both, depending on what works best in the context of their business.

As drafted, the financial adviser-based model will enable any licensed financial advice provider (e.g. a SPV financial advice provider entity), to engage financial advisers on a non-exclusive basis. Those financial advisers would 'sit under' the financial advice provider entity and would not need to obtain their own licenses, thereby generating compliance efficiencies by enabling those financial advisers to simply operate under a licensee's umbrella freeing them up to focus on providing the actual financial advice. This would be a great outcome, as an increasing concern of financial advisers is the extent to which the regulatory compliance burden gets in the way of them having capacity to provide the level of service they would like. Being able to align with a number of financial advice licensees would reduce the extent to which financial advisers need their own operations licensed, which is likely to lead to an increase in the availability of financial advice for consumers (subject to removal of the compliance hurdles noted at submission point 2 below).

The financial advice representative model offers a different solution for

providers willing to assume responsibility for their representatives' compliance with the conduct and disclosure rules. In the writer's view, this model will enable consumers to more readily access financial advice.

The final form of the regime should ensure that industry participants have flexibility to utilize both the above models, recognizing that a 'one size fits all' approach to licensing is not appropriate given the diversity of providers operating within the New Zealand financial advice industry.

## **2. Removal of compliance hurdles**

The writer notes that under the current operating regime there are considerable compliance hurdles and "double ups" in the provision of financial advice in New Zealand. Examples include;

- a. Anti Money Laundering (AML) Reporting. Under current legislation an Authorised Financial Adviser (AFA) operating their own practice is an AML Reporting entity. Should they place business with, say, a KiwiSaver provider or third party Discretionary Investment Management Service (DIMS) provider then the AFA would have to report on this client and transaction for AML purposes as well as the third party DIMS provider or KiwiSaver provider. This means that the same client and transaction is being reported on by multiple parties for AML purposes. It also means that the AFA and DIMS provider are both AML reporting entities and both must undergo AML audits etc.
- b. FATCA. The issue noted above in point a. also applies to FATCA reporting for US clients, which will see compliance double ups.
- c. Changes to the Income Tax Act 2007 and the Tax Administration Act 1994 around the Automatic Exchange of Financial Account Information into NZ Domestic Law (AEOI). The AEOI, which is due to commence on 1<sup>st</sup> July 2017, will also see a similar regime in place as noted in point a whereby one client and their transaction may be reported on by multiple entities.

It is the writer's view that the new financial advice regime should allow financial advisers using this designation from a Financial Advice Provider (FAP) licensee to be able to rely on the FAP to undertake the relevant reporting such as AML and FATCA. This would mean that where there are multiple compliance reports being provided on the same clients and transactions the duplication would be removed.

The writer notes that if these practices are not streamlined then FAPs and financial advisers may well focus on providing services to segments of the market that provide sufficient revenue so as to support multiple

compliance reporting and compliance programmes on the same client and transactions. Should this occur then there may be segments of consumers that will be unable to access financial advice due to compliance costs. This would produce a financial advice access issue for some segments of the New Zealand investing public. This would not be a good policy outcome and is contrary to the Bill's stated policy objectives of ensuring consumers can access the financial advice they need and not imposing any undue compliance costs or complexity.

It is important to note that the writer is not advocating that current compliance regimes such as AML and FATCA be dispensed with. Simply put, where there are multiple reports being generated on the same clients and transactions then one entity only should be made responsible for these reports and compliance regime. Under this type of operation a FAP may take responsibility for AML and FATCA reporting on behalf of a financial adviser so long as the financial adviser meets the required standards set down by the FAP. This initiative would be a welcome outcome.

### **3. Support for the proposed transitional arrangements**

The staggered transition period will enable advisers to continue operating as usual during the transitional license period (from February 2019 to February 2021). Those advisers will be permitted to continue providing the same advice services they are currently able to provide under the Financial Advisers Act regime while they work to meet the new Code of Conduct standards (though any new financial advisers who are not AFAs or RFAs at the time the new regime takes effect will need to comply with the new standards). This seems useful, given the extent of the AFA force.

However, we do note that the proposed timing would see FAF licensees having to have their license granted no later than 1<sup>st</sup> February 2021. Given the "great New Zealand shut down" that occurs every year over the Xmas break, the inevitability that a number of FAF's may leave their application "run" late and that a number of organisations may want to change their business model at the start of a new financial year i.e. 1<sup>st</sup> April, then perhaps extending out the implementation date by two months to 31<sup>st</sup> March 2021 would be a more appropriate date to target. The writer notes that many organisations that may wish to change their operating or business model would be likely to support an implementation date which would coincide with the start of a new financial year.

#### **4. Support for the Financial Advice Representative model**

We anticipate that many organisations will be well placed to document the required process to support a license application for a business model reliant on Representatives to deliver advice – without wanting them to be labelled ‘sales people’. Given the extent of the controls that will need to be put in place before a FAP can be licensed, it would be inappropriate for Representatives to be personally accountable for any advice they provide.

The writer expresses strong support for this model as it will enable consumers to more readily access financial advice (especially if some of the compliance “double ups” as mentioned in point 2.a. are reduced or managed).

As noted in submission point 1, it is important that the final form of the regime provides flexibility for industry participants’ different business models, rather than implementing a ‘one size fits all’ approach.

#### **5. How will the ‘client first’ duty operate in practice?**

The draft Bill contains an obligation for a person (‘A’) giving financial advice to take all reasonable steps ‘to ensure that A’s own interests or the interests of any other person do not materially influence the advice’ (see draft section 431H). This obligation applies where there is a conflict of interest between A’s own interests (or the interests of any other person) and the person to whom advice is given. It is unclear to the writer how this obligation can be satisfied in practice.

Where there is a vertically integrated structure (where an organisation both manufactures its own products and has advisers selling those products), it seems unavoidable that the interests of the organisation would be seen to materially influence the advice given. This is because the adviser would only be considering the suitability of the organisation’s products for the client (rather than the suitability of all products available on the market).

The current drafting seems to suggest that, in the example given above, the adviser would need to consider all products available on the market and only recommend one of the relevant organisation’s own products if the adviser comes to the conclusion that it is the most suitable product for the client. The writer submits that this cannot be the intended outcome, because: a) it would place undue restriction on advisers facilitating investments into house products, and b) it does not reflect the reality of how the industry operates.

Guidance is needed as to how this obligation would work in practice as, based on the current drafting, it is unclear what 'reasonable steps' a financial adviser would be expected to take (or could take) to satisfy this obligation where the advice is provided on behalf of a vertically integrated business model. Given this is a key duty of the new regime, it is critical that it is workable in practice, and that advisers have clarity as to what is expected of them in order to discharge the duty.

#### **6. How will the 'nature and scope' requirement work in practice?**

The draft Bill restricts a person from giving regulated financial advice unless the nature and scope of the advice has been agreed with the person to whom the advice is provided (see draft section 431G).

Please advise how this requirement will apply to publications containing class advice (such as an advertisement or investment commentary containing what would be classified as 'class advice' under the current regime). As these types of publications are widely distributed, there is no clear way for the nature and scope of the advice to be agreed with the client, meaning that the requirement will be unworkable in practice.

As noted above in submission point 5, it is critical that all adviser duties are workable in practice, and that advisers have clarity as to what is expected of them.

#### **7. Regulation of advice provided to wholesale clients**

When providing financial advice to wholesale clients, financial advisers should be subject to the fair dealing obligations and the obligation to exercise care, diligence, and skill, as currently contemplated in the draft Bill.

The writer would also be comfortable with the client first duty applying at the wholesale client level, so long as the duty is clear and workable in practice (see submission point 5 above).

The other obligations set out in the Bill, as well as the Code of Conduct, are only appropriate in the retail client context and financial advisers should not have to comply with those when providing a financial advice service to wholesale clients. To require otherwise would run contrary to the very concept of 'wholesale clients' who, by definition, possess special characteristics or meet certain prerequisites which justify them falling outside of the scope of the consumer-focused aspects of the financial advice regime.

## **8. The financial advice exclusions should provide for DIMS advertising**

Clause 6(f)(iii) of Schedule 2 of the draft Bill provides that a person does not give financial advice merely by making available an advertisement referred to in section 89 of the Financial Markets Conduct Act 2013 ('FMC Act'). However, section 89 of the FMC Act only covers advertisements relating to 'financial products'. A DIMS is not a 'financial product', meaning that DIMS advertisements are not covered by this exclusion.

The writer believes that there is no policy basis on which to distinguish between advertisements relating to DIMS and those relating to financial products, and that this exclusion should therefore be extended to cover a DIMS advertisement.

The writer can be contacted as follows;

**Withheld**

Graham Duston