

Bank of New Zealand

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

**Code of Professional Conduct for
Financial Advice Services**

30 April 2018

1.0 INTRODUCTION

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

2.0 SUBSTANTIVE BNZ SUBMISSIONS

A. What comments do you have regarding the overarching theme of "good advice outcomes" and the underlying principles?

- 2.1 BNZ supports an approach that is client-centric. However, BNZ submits that the concept of 'good advice outcomes' may cause clients to be confused between the advice they receive, and their investment outcome. The use of the term 'outcomes' suggests that the product(s) or service(s) being advised on must perform well. BNZ therefore suggests that the term 'good advice process' is substituted for 'good advice outcomes'.
- 2.2 In the alternative, should the CWG retain the current wording, BNZ emphasises the need for the Code to stress that 'good advice outcomes' does not mean that the product(s) or service(s) being advised on must perform well. Clients should be aware that 'good advice outcomes' can be achieved, even in the event of a financial loss.
- 2.3 BNZ supports the majority of the drafting principles. However, BNZ suggests that principle 2 is revisited. In some instances, it is not appropriate to assume that retail clients have a 'basic knowledge' of financial matters. Many retail clients may be unaware of basic of financial matters. It is these clients who are most in need of protection under Code of Professional Conduct for Financial Advice Services ('the Code'). As a suggestion, this principle could be amended to recognise the gap between the knowledge of a client and a Financial Advice Provider ('FAP'), and because of this, impose a duty of care on the FAP to ensure that the client is made aware of basic of financial matters.

B. Are there any further principles that should be included, or existing principles that should be removed?

- 2.4 As above, BNZ suggests that principle 2 is revised by the CWG.

C. Do you agree with a requirement to act with honesty, fairness and integrity? If not, please set out your reasoning.

- 2.5 BNZ agrees that this requirement is appropriate to achieve good advice outcomes and supports the use of International Organisation of Securities Commissions ('IOSCO') framework for a code of ethics.
- 2.6 BNZ notes that there is scope to align this requirement with similar regimes. For example, under the Financial Markets Conduct Act ('FMCA'), the manager of a managed investment scheme is under general duties to act 'honestly' and 'in the

best interests’ of the client, and to treat clients ‘equitably’. Under the old Financial Advisers Act, the general requirement for a financial adviser was to act with the ‘care, diligence, and skill that a reasonable financial adviser would exercise’.

- 2.7 BNZ would appreciate clarification from the CWG as to the need for different requirements between these regimes, and conversely, whether there can be some degree of consistency in the tests and duties applied.

D. Should minimum standards for ethical behaviour for the provision of financial advice extend beyond strict legal obligations, to include meeting less formal understandings, impressions or expectations that do not necessarily amount to strictly legal obligations? If no, please give reasoning. If yes, please propose how a standard for such commitments might be framed.

- 2.8 BNZ is of the view that minimum standards for ethical behaviour should reflect legally enforceable obligations. To the extent that ethical standards will apply over and above strict legal obligations, BNZ suggests that appropriate guidance is provided for FAPs.

E. If there was a minimum standard requiring Financial Advice Providers - or Financial Advice Providers in some situations - to have their own code of ethics in addition to the Code, how would you frame the requirement for it to deal with keeping commitments?

- 2.9 If the CWG does implement this requirement, the FAP specific code should be considered with reference to the FMA’s guidance document ‘A guide to the FMA’s view of conduct’¹. This requirement should also be framed with reference other applicable ethical standards, including those already in place through industry bodies.

F. Should the Code include a minimum standard on conflicts management? Should it focus on any particular situations?

- 2.10 BNZ agrees that the Code should include a minimum standard on conflicts of interest. This standard should be reasonably broad (and flexible), and not be worded in such a way to focus on any particular situation, or attempt to deal with only certain types of situations.

- 2.11 Specific guidance would be helpful for FAPs on how advisors should manage circumstances where the best option for the client is also the best financial or non-financial outcome for the provider and/or the advisor.

G. Do you agree that a person who gives financial advice must not do anything or make an omission that would or would be likely to bring the financial advice profession into disrepute? If not, please set out your reasoning.

- 2.12 BNZ agrees that a person who gives financial advice should not do anything to bring the financial advice profession into disrepute. This obligation reflects a common

¹ Financial Markets Authority, ‘A guide to the FMA’s view of conduct’, February 2017.

standard from industry participants and will be present in various industry body codes.

H. Is an additional minimum standard on doing no harm to the client necessary? If so, what standard do you propose?

- 2.13 BNZ submits that an additional minimum standard on ‘doing no harm to the client’ is not necessary. Where the Code requires an adviser ‘not to do anything or make an omission that would or would be likely to bring the financial advice profession into disrepute’, this should be sufficient to cover this scenario.

I. In which situations, if any, should the retention, use or sharing of anonymised bulk customer data be subject to Code standards?

- 2.14 BNZ submits that Code standards on the retention, use or sharing of anonymised bulk customer data are not necessary. As above, if there is a Code requirement ‘not to do anything or make an omission that would or would be likely to bring the financial advice profession into disrepute’, this should be sufficient to cover this scenario. Furthermore, New Zealand’s privacy law regime is responsible for ensuring the protection of data confidentiality.

J. Do you agree that the Code should cover the various aspects of maintaining client confidentiality discussed in this paper [see paragraph 100-102]?

- 2.15 It is not necessary for the Code to address client confidentiality. This falls within the ambit of New Zealand’s privacy law regime.
- 2.16 BNZ notes that dual regimes will create issues from an interpretation and precedence perspective. If there is a need for increased functionality or regulation of existing privacy arrangements, this should be addressed as part of consultation and reform of the relevant legislative regimes, rather than be included in the Code. However, should the CWG look to include confidentiality related obligations within the Code, BNZ suggests that these obligations make reference to existing privacy law.

K. Are there any compliance costs or other aspects of maintaining client confidentiality to consider?

- 2.17 No comment.

L. Do you agree that the Code should require the Financial Advice Provider to document and maintain its “ethical processes”?

- 2.18 BNZ agrees that the Code should include documentation and maintenance obligations in respect of ethical processes.

M. Should the Financial Advice Provider be required to have a publicly available corporate code of ethics? Are there particular situations where a corporate code of ethics should be or should not be required?

- 2.19 BNZ submits that the proposed minimum ethical standards are sufficient, and that an additional corporate code of ethics is not necessary. Consumers may be unwilling to invest the time to digest a publicly available code of ethics, which would result in an unjustified compliance obligation on FAPs.

2.20 Should the CWG retain this requirement, BNZ suggests that the code of ethics be available to regulators if and when requested, or as a condition of a FAP's licence would be more reasonable.

N. Should Financial Advice Providers also be subject to additional standards in respect of leadership and culture? If so, how should these be framed?

2.21 BNZ is of the view that it is not necessary for FAPs to be subject to additional leadership and culture standards.

O. Do you propose other additional standards of ethical behaviour that should apply to Financial Advice Providers?

2.22 No comment.

P. Do you agree that Financial Advice Providers should be required to meet standards relating to ethics training? If not, please state your reasoning.

2.23 BNZ agrees that FAPs should be required to meet ethical training standards.

Q. Should ethics training requirements apply to all officers and employees of a Financial Advice Provider involved in financial advice processes, as appropriate to their role and contribution to the process of financial advice provision? If not, please state your reasoning.

2.24 BNZ agrees that ethics training requirements should apply to relevant FAP officers and employees, on a tailored basis. It is important that these requirements are appropriately tailored, noting that employee involvement in the process of providing financial advice can differ significantly. For example, it may not be necessary for financial advice marketing teams to have extensive ethics training when they will rely on subject matter experts to approve the content of any marketing material, and will not be directly involved in the provision of financial advice.

R. Should there be a requirement for ongoing refresher training on ethics?

2.25 BNZ agrees that ethics training should be periodically refreshed. If there are no substantive changes to the Code during the relevant period, and other annual professional development requirements can include a component of ethics training, BNZ suggests that a standalone ethics refresher is not necessary.

2.26 However, if substantive changes to the Code have occurred in relation to ethical standards, a standalone updated refresher programme would be beneficial. As noted above, the content of the refresher training should be appropriately tailored for the audience concerned.

S. Do you agree that Financial Advice Providers should be required to have in place, and use, a framework for resolving ethical dilemmas that may arise in giving financial advice? If not, please set out your reasoning.

2.27 BNZ agrees that FAPs should be required to establish an 'ethical dilemma' framework.

T. Should there be a requirement for explicit sign-off on the soundness of financial advice provided directly by a Financial Advice Provider?

2.28 Explicit sign-off on the soundness of financial advice provided by a FAP is not necessary. BNZ suggests that Quality Assurance should be undertaken in order to ensure that the overarching theme of the Code has been adhered to.

U. Do you agree that Financial Advice Providers should be required to have in place a compliance function aimed at following up on concerns raised by employees and other stakeholders? If not, please set out your reasoning.

2.29 BNZ agrees that FAPs should have a compliance function regarding complaints or concerns raised. This could include details of a FAP's whistleblowing processes.

V. Should this extend further into an internal audit obligation, having in place processes to systematically test for and detect violations of ethical behaviour?

2.30 The Code is arguably an inappropriate mechanism to impose an internal audit obligation in respect of ethical behaviour. However, this requirement could be raised in the licensing application process, as a minimum standard required of licensees, or as a condition of obtaining a licence.

W. Are there any potential compliance costs for small and/or large Financial Advice Providers that need to be considered?

2.31 Large providers with established internal systems for addressing ethical issues are unlikely to face substantial additional compliance costs as a result of the proposed Code requirements.

X. Do you agree that Financial Advice Providers should be required to be able to demonstrate that they meet the standards of ethical behaviour as if the Financial Advice Provider carried out the whole advice process directly itself? If not, please set out your reasoning.

2.32 BNZ is of the view that this requirement extends beyond what should be reasonably expected of a FAP. FAPs provide advice based on the strength of information given to them by, or on behalf of, the relevant client. However, there are instances where third parties may provide input information in the financial advice process. A FAP should be able to rely on the information or services provided by a third party when providing advice, and not be required to demonstrate standards of ethical behaviour as if the FAP had generated or compiled that information or provided that service.

2.33 However, a FAP should be required to take appropriate steps to ensure that any third-party provider that is engaged is professional, reputable and reliable. BNZ is of the view that this requirement falls under the ethical behaviour standard to 'not to do anything or make an omission that would or would be likely to bring the financial advice profession into disrepute'.

Y. What principle or mechanism do you propose the Code could include to reinforce good ethical behaviour on a day-to-day basis?

In order to reinforce good ethical behaviour on a day-to-day basis, the Code could require FAPs to disclose their code of ethics as part of the overall client disclosure requirements.

Z. Are there other delivery methods that should be considered when testing our thinking?

2.34 No comment.

AA. How do the current client care standards work in practice, especially in advice-giving situations not previously covered by the AFA Code? In answering this question, please ignore “scope of advice” (CS-8) and “suitability” (CS-9 and part of CS-10).

2.35 No comment.

BB. Could any aspect of the current client care standards be worded better? (For example, we are aware that the definition of “complaint” could be improved.)

2.36 No comment.

CC. Are there any aspects of the current client care standards that could be expanded or clarified (for example, in light of the published findings of the Disciplinary Committee)?

2.37 No comment.

DD. Are there any potential compliance costs for small and/or large Financial Advice Providers that need to be considered?

2.38 No comment.

EE. Are there any additional matters that should be addressed in the advice-giving standards? Those listed above [see paragraph 130]? Others?

2.39 BNZ emphasises that client care standards should be appropriately flexible to cater for the wide spectrum of potential advice that FAPs can provide. The interests of the client should remain at the forefront of an adviser’s mind – the requirement to provide substantial information as part of the provision of simple product advice may distract an adviser from adhering to the overarching theme of the Code.

FF. Do you think there are any other components that should be included in the design considerations of an advice process?

2.40 BNZ is not aware of any other components that should be included in the design considerations of an advice process.

GG. Should the Code include guidance material to help determine what needs to be considered when designing an advice process?

- 2.41 Non-prescriptive guidance material on the design of an advice process would be welcomed by FAPs. This is particularly necessary to support smaller scale FAPs.

HH. Are there any other important aspects you think should be included in the advice process for all types of financial advice activities under the new regime?

- 2.42 BNZ agrees that there are some key aspects that should be included in all advice processes, no matter how simple the advice interaction. As in the current AFA Code of Professional Conduct, the advice process should clearly set out the nature and scope of the service being provided, and the limitations (if any) of that service. It is particularly important for a client to understand the limitations of any financial advice when the adviser is advising on a limited range of investment products.
- 2.43 The timing of the advice should be clearly communicated, such as how long the advice remains ‘live’, and whether it ‘expires’ or under what conditions it may ‘expire’.
- 2.44 Specific consideration should be given to drafting of the Code when requiring information to be ‘explained’ to the client in terms that they understand. This terminology can imply a face to face interaction where client understanding can be assessed. However, when incorporating artificial intelligence (‘AI’) and automated devices, this becomes more difficult. BNZ is of the view that plain English should be sufficient when advice is provided through AI and automated devices.

II. Should any of the key aspects that we have listed above be removed? If so, why?

- 2.45 BNZ has no concerns with the key aspects listed.

JJ. Are there any situations in which an advice process need not be followed?

- 2.46 The requirement to comply with the advice process should not apply when another regime regulates the behaviour e.g. Credit Contracts and Consumer Finance Act 2003 (‘CCCFA’) responsibility principles, and suitability assessment requirements under the FMCA.

KK. What comments do you have about a proposed minimum standard on personalised suitability analysis? What are your views on the example above?

- 2.47 BNZ agrees that there is a need for flexibility in determining an appropriate advice outcome for clients, which may or may not require a personalised suitability analysis. BNZ therefore supports the proposal that the suitability standard will not apply where a FAP demonstrates how a good advice outcome is achieved, without a personalised suitability analysis. This is important to ensure access to advice.
- 2.48 BNZ notes that it may be difficult for FAPs to demonstrate that a personalised suitability analysis is not necessary. This may incentivise FAPs to exclude personalised suitability from the scope of its services. This will exacerbate the problem that the new financial adviser regime is seeking to address, whereby clients will not have access to the quality of advice that they require. BNZ therefore

recommends that the CWG provide guidance on examples of when a personalised suitability analysis may, or may not, be applicable.

LL. What are the practical advantages and disadvantages of including organisational standards as described? What explanatory material or examples could we provide in the Code that might help to make these standards easier to comply with in practice?

2.49 The proposed organisational standards are similar to the proposed ethical standards. BNZ submits that it would be sufficient for the Code to reference either organisational or ethical standards. Imposing both organisational and ethical standards would result in duplicate compliance obligations for FAPs.

MM. Would implementing these organisational conduct and client care standards create a particular compliance burden for your firm? If yes, please explain why.

2.50 No comment.

NN. Do you agree with our interpretation of the meaning of “competence, knowledge, and skill”? If not, why not?

2.51 BNZ agrees that the definitions of competence, knowledge and skill are appropriate.

OO. Are there other factors, which contribute to combined expertise, that we have not listed? We are particularly interested in factors that are relevant to financial advice that is given by a Financial Advice Provider directly, including by digital means.

2.52 BNZ is not aware of any other factors that contribute to combined expertise.

PP. What do you think are the advantages of this approach to general competence, knowledge, and skill?

2.53 The ability to aggregate knowledge, competence and skill will allow a FAP to improve the accessibility of advice to its clients. This approach depends on a FAP’s ability to provide strong systems and processes to support the aggregation of competence knowledge and skill.

QQ. What do you think are the disadvantages of this approach to general competence, knowledge, and skill?

2.54 The proposed approach is likely to require significant changes to organisational structure, roles, and responsibilities to ensure the ongoing compliance. This will include the implementation of additional oversight to provide comfort to FAPs that their aggregation is effective and compliant. This is likely to result in additional compliance costs for FAPs, and may have a disproportionate impact on small scale FAPs.

2.55 Specifically, the proposed second minimum standard of general competence, knowledge, and skill will require a Financial Adviser or Nominated Representative to hold Level 5 Unit Standard equivalent understanding. BNZ acknowledges that this general understanding will be useful in most cases, but notes that the proposed

standard of ‘Level 5 Unit Standard equivalent’ is not necessary for all individuals that provide advice.

- 2.56 BNZ is of the view that FAPs should have flexibility to determine how they will ensure their advisers meet the new competency standards of the Code, as part of evidencing an aggregate level of competence for a level of advice. In this regard, BNZ submits that it is critical that the Code permits financial advice providers to develop and provide in-house training, rather than limit professional training options to external providers only. While financial advice providers may choose to use third party providers (or favour a mix of internal and external trainings), it would materially compromise the cost and efficiency of upskilling an adviser base if advice providers could only do so via an external provider, which may not be as familiar with the particular contexts in which those advisers would be providing advice in the course of their roles.

RR. In what ways do you think this proposed standard contributes to, or detracts from, the legislative purposes (for example ensuring the quality and availability of advice, avoiding unnecessary compliance costs, and promoting innovation and flexibility)?

- 2.57 Allowing a provider to aggregate their capability will improve advice accessibility, and contribute to the legislative purposes of new financial advice regime. However, as set out above, the Level 5 Unit Standard equivalent understanding requirement is likely to impose unnecessary compliance costs for FAPs. BNZ is of the view that good advice outcomes can be achieved without alignment to unit standards.

SS. What factors should we consider in determining whether to make the proposed unit standard a renewing obligation?

- 2.58 A FAP should have an ongoing obligation to demonstrate its ability to meet its competency requirements as part of its licence conditions. In the case of an individual, ongoing competency should be demonstrated by way of personal development plans, and ongoing education and development rather than compliance with a renewing obligation to meet a unit standard requirement.
- 2.59 However, should the CWG implement a renewing unit standard compliance obligation, there are a number of factors that should be considered when developing this obligation, including:

- Compliance cost implications;
- Availability of multiple assessment providers;
- Provision of in-house unit standard equivalent learning programmes (with or without assessment);
- Timing and basis of renewal dates; and
- The review cycle of the unit standard.

TT. What are the advantages and disadvantages of our approach of identifying two types of financial advice? What impact would it have on the type of advice you give and on your compliance costs?

- 2.60 The advantage of identifying two types of advice is that this will enable a client to decide what level of advice they require. However, the main issue with identifying two

types of financial advice is the existence of an overlap between the two. It may not be abundantly clear when product advice transitions into financial planning or vice versa. BNZ therefore submits that clear guidance on the difference between product advice and financial planning is required, particularly in light of the difference in competence, knowledge and skill that is required between the two.

UU. How should RFA's experience be recognised?

- 2.61 In BNZ's view, it is not sufficient for a RFA's period of experience to justify compliance with minimum standards of competence, knowledge and skill. RFA's should have to evidence how they meet the minimum standards under the new regime.
- 2.62 BNZ supports the proposal that AFA's should be recognised as meeting the minimum standards under the Code.

VV. What do you think are the advantages of this approach to particular competence, knowledge, and skill?

- 2.63 This approach enables FAPs to offer different levels of advice to clients, based on their needs.

WW. What do you think are the disadvantages of this approach to particular competence, knowledge, and skill?

- 2.64 As noted above, this approach will require clients to understand the different types of advice they can receive from their provider and is likely to result in increased compliance costs for FAPs.

XX. In what ways do you think this proposed standard contributes to, or detracts from, the legislative purposes (for example ensuring the quality and availability of advice, avoiding unnecessary compliance costs, and promoting innovation and flexibility)?

- 2.65 The product advice option will make it easier for providers to service their clients. The ability for a provider to personalise product advice would improve the quality of that advice.
- 2.66 BNZ reiterates that the Level 5 minimum competency requirement may be a barrier for some providers, and add up front and ongoing compliance costs.

YY. What alterations, if any, would you suggest to the baselines we have nominated: specialist strand for product capability, Level 5 for discipline capability, and relevant degree (or other degree plus Level 6) for planning capability?

- 2.67 BNZ submits that the Level 5 minimum competency requirement is excessive for simple product advice scenarios, for example, the sale of credit cards and banks accounts. As set out in QQ and RR above, BNZ is of the view that good advice process can be achieved without alignment to unit standards. However, should the CWG look to align the unit standards with competency requirements, BNZ submits that Level 4 knowledge should be sufficient for product and discipline capability, and that Level 5 equivalent knowledge is appropriate for planning capability.

ZZ. Are there any other comments you would like to make to assist us in developing the Code?

- 2.68 The Code Committee should ensure that the standards of competency strike a balance between ensuring that “rogue” and negligent conduct is prohibited, but not be so heavy-handed that advisers are too wary of providing meaningful financial advice to their clients.
- 2.69 There is a real risk that over-regulation could result in the same hesitations experienced with the current financial advice regime, where consumers at times lack access to good quality and affordable financial advice due to the high compliance burden for advisers to feel confident that they are in fact legally permitted to provide the requested advice.

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

DDI: **S 9 (2) (a)**
Mobile:
Email: