MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HIKINA WHAKATUTUKI

Regulatory impact statement

Further amendments to the Financial Advisers Act and the Financial Service Providers Act

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Agency disclosure statement

This regulatory impact statement (RIS) has been prepared by the Ministry of Business, Innovation and Employment (MBIE).

The purpose of this RIS is to support a Cabinet paper proposing further amendments to the Financial Advisers Act 2008 (FA Act) and Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act). This builds on previous Government decisions on a new overall framework for the regime made in July 2016. The options analysed in this RIS relate to the:

- compliance and enforcement provisions of the new regime;
- obligations that apply to the provision of financial advice to wholesale clients
- mechanics of the Code and Code Committee;
- regulation of personalised discretionary investment management service; and
- complementary measures for misuse of the Financial Service Providers Register.

The analysis is based largely on:

- Impacts identified in submissions received in response to two consultation documents – a May 2015 Issues Paper and a November 2015 Options Paper.
- Extensive consultation with adviser and consumer representatives, other government agencies (particularly the Financial Markets Authority (FMA)), and members of the public through workshops, focus groups and meetings, held over the past 20 months.
- Desk-based research including academic papers, international trends and experiences.

There are some limitations on the analysis undertaken:

- The analysis is based partly on impacts identified in submissions and meetings. In some instances, stakeholders shared anecdotal evidence but did not include quantitative evidence of the problems identified. They also included qualitative descriptions of the costs and benefits of the options rather than quantitative estimates.
- Some of the options have been consulted on at a relatively high-level to date. This includes the options relating to the compliance and enforcement provisions and the obligations that apply to the provision of financial advice to wholesale clients, analysed in this RIS. The next step in the process is the release of an exposure draft of the legislation. The release of the exposure draft will provide a further opportunity to confirm that the more detailed arrangements outlined in this RIS are fit for purpose.

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List of Acronyms

AFA	Authorised Financial Adviser
DIMS	Discretionary Investment Management Service
FA Act	Financial Advisers Act 2008
FADC	Financial Advisers Disciplinary Committee
FATF	Financial Action Task Force
FDRS	Financial Dispute Resolution Service
FMA	Financial Markets Authority
FMC Act	Financial Markets Conduct Act 2013
FSP	Financial Service Provider
FSP Act	Financial Service Providers (Registration and Dispute Resolution) Act 2008
FSPR	Financial Service Providers Register
MBIE	Ministry of Business, Innovation and Employment
PCO	Parliamentary Counsel Office
QFE	Qualifying Financial Entity
RFA	Registered Financial Adviser

Executive Summary

In July 2016 Cabinet agreed to a comprehensive package of changes to the regulation of financial advice in New Zealand. These changes will contribute towards the confident and informed participation of consumers in financial markets by improving the quality of, and access to, financial advice.

The Ministry of Business, Innovation and Employment (MBIE) has continued to assess certain aspects of the new regime which required further analysis, or have come to our attention since the July Cabinet decisions. This regulatory impact statement (RIS) is divided into five separate sections which analyse and recommend options relating to these discrete aspects of the regime.

Part A recommends that financial advice firms should be subject to the same compliance and enforcement tools that apply to other licensees under the Financial Markets Conduct Act 2013 (FMC Act). Individual financial advisers will be subject to a financial adviser disciplinary process, similar to the process that currently exists in the Financial Advisers Act 2008 (FA Act). This provides significant incentives for compliance and provides for a range of proportionate compliance and enforcement tools.

Part B includes the analysis of options relating to the provision of advice to wholesale clients, and recommends changes to the obligations that apply. These changes are intended to reduce the risk to consumers who may meet the wholesale threshold by virtue of their wealth, ensure that all advice is held to appropriate standards and improve the ability for wholesale clients to understand their status.

Part C recommends changes to the mechanics of the Code of Conduct and Code Committee that will increase certainty for industry participants around the code standards, and increase transparency in the process for developing the standards.

Part D recommends changes to the regulation of personalised discretionary investment management services (DIMS), which will place the same requirements on all DIMS providers. This change will require those currently providing this service under the FA Act to obtain a FMC Act DIMS licence. It is proposed that these providers automatically receive a restricted FMC Act DIMS licence to minimise the impact of transition.

Part E includes the analysis of options intended to reduce the misuse of the Financial Service Providers Register (FSPR) by offshore-controlled firms wishing to appear as though they are regulated in New Zealand.

Introduction

Background: Review progress and Cabinet decisions to date

The Ministry of Business, Innovation and Employment (MBIE) has been reviewing the operation of the Financial Advisers Act 2008 (FA Act) and Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act) over the past 20 months.

In July 2016 Cabinet agreed to a comprehensive package of changes to the regulation of financial advice in New Zealand [CAB-16-MIN-0336]. This package of changes will improve the quality of, and access to, financial advice by:

- creating an even playing field for the provision of advice by requiring all advisers to put the interests of the consumer first and meet competency requirements;
- removing regulatory boundaries to encourage innovation, enable the provision of online 'robo' advice, and ensure consumers can access good advice in response to discrete questions such as 'what KiwiSaver fund is right for me?';
- improving consumer understanding by introducing simple disclosure requirements and meaningful terminology; and
- maintaining the integrity of New Zealand's financial markets by requiring businesses to demonstrate a strong connection to New Zealand in order to be registered on the Financial Service Providers Register (FSPR).

The key structural changes agreed by Cabinet for the new regime are as follows:

- The three current types of advisers - 'authorised financial adviser' (AFA), 'registered financial adviser' (RFA) and 'qualifying financial entity' (QFE) – which each have different standards, will be removed. Rather, anyone providing financial advice will be a 'financial adviser' or an 'agent'.
- All financial advice will be required to be covered by a licence granted by the Financial Markets Authority (FMA) and licensing will occur at the firm level. All financial advisers and agents providing financial advice will need to be engaged by a licensed financial advice firm.
- All financial advice will be subject to the same broad legislative requirements, which are as follows:
  - a conduct obligation to place the interests of the consumer first;
  - an obligation to only provide financial advice where competent to do so;
  - a disclosure obligation to disclose prescribed information; and
  - a client care obligation to ensure that consumers are aware of the limitations of their advice.
- All financial advice will be held to a Code of Conduct, which will contain minimum standards for conduct, competence, client care and continuing professional development. (Currently a Code of Conduct only applies to AFAs.)

Analysis of the above changes can be found in a previous Regulatory Impact Statement (RIS), which is available at www.mbie.govt.nz/faareview.

Particularly in light of the move to firm-level licensing (which is already provided for under Part 6 of the Financial Markets Conduct Act 2013 (FMC Act)), the changes are being achieved by repealing the FA Act and incorporating the regulation of financial advice into the FMC Act. A Bill that gives effect to these changes is currently being drafted.

Purpose and content of this RIS

Taking the overall framework of the regulatory regime as decided by Cabinet as given, MBIE has continued to assess certain aspects of the regime. These are elements which were deferred in July due to the need to undertake further analysis or which have come to our attention since the July decisions. In particular this RIS includes the analysis of options relating to:

- setting enforcement mechanisms that provide sufficient incentives for compliance with obligations, provide compensation to consumers who suffer loss, and are proportionate;
- setting requirements for the provision of advice to wholesale clients that ensures all advice is held to appropriate conduct standards and risks to consumers are minimised, while not imposing undue compliance costs;
- establishing the mechanics for the Code of Conduct and Code Committee with a view to ensuring that the Code Committee has the requisite knowledge, skills, and experience, that the rule-making processes reflect best practice, and that certainty is provided to industry as soon as practicable;
- regulating personalised discretionary investment management services (DIMS) providers as a consequence of incorporating the regulation of financial advice into the FMC Act; and
- introducing complementary measures to address misuse of the FSPR to protect the reputation of New Zealand's FSPR regime.

Objectives

As set out in the previous RIS, the long-term objective of the regulatory regime for financial advice is the more confident and informed participation of consumers in financial markets. To achieve this, the following objectives were adopted for the review of the FA Act and FSP Act:

- consumers can access the advice they need;
- advice makes consumers better off;
- regulation is enabling with no undue compliance costs, complexity, or barriers to innovation; and
- consumers can access redress.

This RIS relates to discrete elements within the overall regulatory framework. Specific objectives, consistent with the four high-level objectives above, have been developed for each discrete element.

Next steps

The next step in the process is the release of an exposure draft of the legislation. This will provide a further opportunity to confirm that the proposals outlined in this RIS are fit for purpose and address any potential issues with legislative drafting.

Alongside the exposure draft, MBIE will also consult on transitional arrangements to enable existing advisers and firms to transition to the new regime. The aim is to bring each element of the new regime into effect as soon as practicable, ensure participants can transition smoothly, minimise unnecessary compliance costs, and minimise disruption to consumers.

Alongside the progress of the legislation in 2017, MBIE will progress work on the detailed matters that will sit in Regulations (rather that in primary legislation). This includes work with industry and consumer groups to develop the content, format and timing of disclosure.

Part A: Compliance and Enforcement

Status quo and problem definition

Current enforcement regime

Compliance and enforcement of financial advice obligations are currently split between the FMC Act and the FA Act.

Financial advisers and financial advice firms are subject to Part 2 of the FMC Act, which contains general 'fair dealing' provisions – such as prohibiting false or misleading representations. Breach of any of these provisions can result in civil pecuniary penalties of up to $1 million in the case of an individual or $5 million in any other case, and compensation.

The FA Act provides a range of offences for breaches of specific provisions. These include offences for providing a service without being permitted, falsely holding out that a person is authorised, and a failure to make required disclosures.

The FA Act also provides a Financial Advisers Disciplinary Committee (FADC) for breaches of the Code of Conduct by AFAs. The FADC can censure, suspend or cancel an AFA's authorisation, require supervision or training and issue AFAs with fines for up to $10,000.

The FA Act provides civil pecuniary penalties and compensation if an adviser, QFE or broker accepts a false certification that a person is a wholesale client.

The FA Act provides some statutory duties that appear to codify common law duties, and do not have criminal or civil liability consequences in the Act. These are requirements to exercise care, diligence and skill, and personalised DIMS duties. However, the FMA can amend, suspend or cancel an AFA's authorisation for breaches of these provisions.

What has Cabinet decided to date?

In July 2016 Cabinet decided [CAB-16-MIN-0336]:

- Financial advisers will be individually accountable for their financial adviser legislative and regulatory obligations.
- Financial advice firms will be accountable for the financial advice firm's legislative and regulatory obligations, will be accountable for their agents, and are required to put in place processes and provide resources to assist their financial advisers to meet their obligations.
- Financial advice firms will be licensed by the FMA consistent with the licensing regime under Part 6 of the FMC Act.

As discussed in the earlier RIS, these decisions respond to concerns that:

- The current regime does not reflect a firm's ability to influence consumer outcomes. The move to dual accountability aims to ensure that all parties with an ability to control advice quality are accountable.
- In some instances it is the firm's controls and processes that predominantly determine consumer outcomes and compliance with legislative outcomes. The 'agent' model, with firms fully accountable for agents, aims to ensure accountability sits with the party best able to influence consumer outcomes.

As the FMC licensing regime will apply, breaches of various FMC Act licensing obligations may result in civil pecuniary penalties and compensation orders being imposed on financial advice firms and, where applicable, individual financial advisers or agents. These include breaches of the need for a licence, the prohibition on false or misleading statements and omissions in a disclosure document, and requirements to comply with licence conditions. Some of these, such as no holding out, apply to both firms and individuals. Others apply specifically to licensees (who will be firms).

Breach of some of these provisions (such as operating without a licence) can result in civil pecuniary penalties of up to $1 million in the case of an individual or $5 million in any other case. Breaches of other provisions (such as licence conditions) result in civil pecuniary penalties of up to $200,000 for an individual or $600,000 in any other case. A customer who is harmed by a breach of any of these obligations can claim compensation for loss or damage.

Cabinet also agreed to introduce new legislative obligations (advice obligations) that will apply to all financial advice:

- a conduct obligation to place the interests of the consumer first;
- an obligation to only provide financial advice where competent to do so;
- a disclosure obligation to disclose prescribed information;
- a client care obligation to ensure consumers are aware of the limitations of advice; and
- a requirement that all advice is held to a Code of Conduct.

Where licensed financial advice firms breach the advice obligations, the FMA will have a range of standard FMC licensing tools – such as censure, action plans, directions or suspension/cancellation of licence.

What is the remaining policy issue?

Cabinet directed officials to report-back on the compliance and enforcement provisions that sit alongside the new financial advice regime. As described above, some aspects of compliance and enforcement fall out of Cabinet's previous decisions. However, other issues require further Cabinet decisions.

Key remaining issues are:

- the liability consequences for breaches of the new advice obligations; and
- which parties these liability consequences sit with.

As the financial advice regime is likely to be incorporated into the FMC Act, there is an opportunity to utilise and align with the existing FMC Act obligations.

There is also an opportunity to address specific issues with the current FA Act compliance and enforcement regime. In particular, one issue that has been raised is that currently if an FMA investigation finds than an AFA has breached the Code, it *must* refer the complaint to the FADC. We have been informed by the FMA that this is unnecessary and costly where the breach is minor and technical – such as a minor error in a record keeping – and is inconsistent with the FMA's prosecutorial discretion in other legislation that it enforces. By requiring FMA to refer complaints to the FADC it may also impede the ability of FMA to settle claims against AFAs.

Objectives

The primary objective of the regulatory regime for financial advice is to promote the confident and informed participation of consumers in financial markets. Consistent with this, the objectives of the financial advice compliance and enforcement regime are to:

- Provide sufficient incentives for financial advice firms and financial advisers to comply with advice obligations, and for corrective actions where there are breaches.
- Provide adequate compensation to clients who suffer loss or damage as a result of breaches of advice obligations.
- Ensure that compliance and liability consequences are proportionate and do not result in over-resourcing of compliance or an overly risk averse approach to advice.
- Ensure that liability sits with appropriate parties (firms or individuals).

There are potential trade-offs between meeting the first and second objectives and meeting the third objective. Stronger enforcement and greater consequences for breaches may encourage over resourcing of compliance and risk aversion. There is no perfect balance of these objectives, and it may be difficult to determine whether an appropriate balance is being struck in advance.

The fourth objective (liability sits with appropriate parties) includes examining:

- Whether liability sits with parties (firms or individuals) who are in the best position to manage liability risks at least cost.
- Whether liability sits with the parties that benefit from the contravening conduct.

The options considered in this RIS are also analysed against whether they result in a positive net assessment of costs, benefits and risks.

Options and impact analysis

Because the remaining policy question relates to the appropriate enforcement approach for new obligations, there is no clear status quo. We have therefore not analysed the status quo as a single option. Rather, we have identified two options which utilise relevant enforcement mechanisms from the current FA Act and FMC Act.

Option 1 – standard FMC Act liability + financial adviser disciplinary process

New obligations of financial advice firms would be subject to civil pecuniary penalties and compensation, similar to FMC obligations on DIMS providers.

Breaches of the new advice obligations by financial advice firms (e.g. placing the interests of the consumer first) would result in civil pecuniary penalties of up to $200,000 for an individual or $600,000 in any other case. Compensation would be available to clients who are harmed by contraventions. This is consistent with breaches of similar obligations in the FMC Act for DIMS providers.

Directors and financial advisers would be liable for civil pecuniary penalties and compensation where they were deliberately involved in a contravention by the financial advice firm. This is a consequence of the FMC Act's general provisions for liability of parties to contraventions (s.533).

Financial advisers would have additional, individual compliance and enforcement processes similar to that under the current FA Act

The FMC Act 'direction order' provisions would apply to individual advisers who breached their obligations.

As per the FA Act provisions for AFAs, the FMA would be able to deregister a financial adviser who contravened their duties and obligations under the Act.

The existing FA Act FADC provisions would be retained, with the following changes:

- As well as breaches of the Code of Conduct, the FADC could deal with breaches of the new advice obligations.
- The FMA would have discretion about whether or not to refer a complaint to the FADC.

It would deal with breaches of obligations by financial advisers only, with a maximum fine of $10,000. As at present, the FADC could not order a financial adviser to pay compensation.

Further consultation regarding compliance and enforcement: MBIE is to undertake additional consultation alongside the exposure draft on options to extend the jurisdiction of the FADC to financial advice firms, as well as advisers.

Benefits

This option provides significant incentives for compliance by financial advice firms, compared to the FA Act regime.

It also provides some incentives for compliance by individual financial advisers, although these are weaker as they are mainly confined to administrative actions taken by the FMA and actions taken through the FADC. Unlike the FA Act regime, advisers would not be criminally liable for misleading and deceptive conduct or disclosure failures, reducing the likelihood of compliance tools resulting in a risk-averse approach to advice.

This option provides compensation to clients, primarily from the assets of financial advice firms.

Costs/risks

As financial advice firms will be liable for the actions of their advisers, they are likely to subject them to stronger oversight, limiting individual adviser freedom. This may result in firms limiting their services to ensure that they can retain control of the advice provided, thereby reducing their exposure.

Small firms may be relatively lightly capitalised, providing limited scope for compensation.

Option 2 – standard FMC Act liability + financial adviser disciplinary process + defence for firms with advisers

This option is the same as Option 1, except firms would not be liable for contravention of the new advice obligations if both of the following hold:

- the financial advice firm shows that a financial adviser was responsible for the breach; and
- the financial advice firm met its duty to support the financial adviser to comply.

Financial advisers would be subject to disciplinary action and personal liability (compensation for loss only).

The effect of this option is that if a firm provides advice through advisers rather than agents, then instead of the firm being subject to pecuniary penalties of up to $600,000, their advisers have personal liability for fines of up to $10,000. Firms could choose to indemnify their advisers against this liability (i.e. agree with the adviser that they will pay any fine or compensation), substantially reducing their liability (compared to employing agents) without adversely affecting the adviser.

Benefits

To the extent that individual advisers are in a better position to manage the risk of contravention than firms, e.g. in the case of complex or bespoke advice, this option ensures accountability rests with the party best able to manage outcomes.

This option may slightly increase the availability of compensation from small, adviser-owned firms (where the adviser's personal assets are available, in addition to their equity in the adviser firm).

Costs/risks

Increased personal liability for advisers, and sole liability of advisers, may result in more risk averse and limited advice. To the extent that clients contract with firms, and firms benefit financially from the advice given by advisers, it creates a mismatch between those who receive benefits and those who are liable for negligent advice.

This option may have different effects in small adviser-owned firms compared to large firms who employ advisers:

- In large firms, it creates incentives to shift liability from the firm to advisers and is likely to reduce the scope for compensation for clients.
- In firms where advisers have a concentrated shareholding, there are some incentives to shift liability to advisers (because of the reduced penalties) but these may be outweighed by the possibility of personal liability for compensation. Depending on whether licensing criteria permits it, firms with a single adviser/shareholder/director may choose to treat their adviser as an agent.

It is increasingly recognised that a firm's culture can significantly influence the conduct of individuals within the firm[1]. This option may fail to hold a firm accountable for its role in contributing, through its culture and approach to conduct, to breaches by an adviser.

[1] For example, as set out in the FMA's draft conduct guide "*In all workplaces, people look to examples set by their colleagues, and especially their leaders, for a sense of whether formal conduct expectations are real, or just rhetoric. They also observe whether there are clear consequences, including for the leadership, if those expectations are not met*". *https://fma.govt.nz/assets/Consultations/160728-A-guide-to-the-FMAs-view-of-conduct.pdf*.

Assessment of options against criteria and summary of cost/benefits analysis

	Provide sufficient incentives for compliance and for corrective actions where there are breaches	Provide compensation to clients who suffer loss or damage as a result of breaches of statutory duties	Ensure the compliance and liability consequences are proportionate	Whether liability sits with the appropriate parties (firms or individuals)	Net assessment of costs, benefits and risks
Option 1: Standard FMC Act liability with financial adviser disciplinary process	Provides significant incentives for compliance by firms, and some incentives for individual advisers. ✓	Provides compensation to clients. ✓	This option provides for dual accountability with different (proportionate) avenues for firms and advisers. The tools available are flexible (e.g. ranging from censure to more serious penalties). ✓✓	Some accountability on both firms and individual advisers, recognising both can influence consumer outcomes. ✓	Net benefit. Creates incentives to comply and proportionate enforcement tools.
Option 2: Standard FMC Act liability with financial adviser disciplinary process and defence for firms with advisers	Yes but provides limited incentives for compliance by firms relative to option 1. ✓	Provides compensation to clients. ✓	This option provides for dual accountability with different (proportionate) avenues for firms and advisers (though firms liability is limited relative to option 1). The tools available are flexible (e.g. ranging from censure to more serious penalties). ✓	This option does not recognise the role a firm's culture can play in contributing to breaches by its advisers. To the extent that firms benefit financially from the advice given by advisers, it creates a mismatch between those who receive benefits and those who are liable for negligent advice. ×	Net benefit, but less of a benefit than Option 1.

Option 1 (standard FMC liability with the disciplinary process for individual financial advisers) is preferred. This option provides significant incentives for compliance and provides for a range of proportionate compliance and enforcement tools.

Key
✓✓ Meets the objective
✓ Partially meets the objective
× Does not meet the objective
~ No impact on achievement of objective
☐ Shaded row = preferred option

Part B: Obligations when advising wholesale clients

Status quo and problem definition

Who are wholesale clients?

Wholesale clients are generally large and/or sophisticated clients who do not require the same degree of protection as retail clients. The full definition for a wholesale client is set out in section 5C of the FA Act. There are a range of different tests that a client can meet in order to be considered a wholesale client, including:

- a person who is a wholesale investor within the meaning of the FMC Act. This includes:
    - A person who owns a portfolio of specified financial products of a value of at least $1 million (in aggregate).
    - A person with net assets of over $5 million.
    - A person who is an investment business which in turn includes a registered bank, a licensed insurer, or an entity whose principal business consists of investing in financial products.
- any other financial adviser or broker who receives the financial adviser service in the course of business as a financial adviser or broker.
- a person who is in the business of providing any other financial service and receives the financial adviser service or broking service in the course of that business.

A client who does not meet the threshold for a wholesale client but wishes to be treated as a wholesale client can do so through an 'eligible investor' certificate. This means they can certify that they have sufficient knowledge, skills, or experience in financial matters to assess the value and risks of financial products and the merits of the service to be provided, and understands the consequence of the certificate.

A client who does meet the threshold for a wholesale client but wishes to be treated as a retail client can opt out of being a wholesale client by giving the adviser a signed notification to that effect.

Why and how are wholesale clients treated differently?

As a result of the size and/or sophistication of wholesale clients, there are lower regulatory requirements that apply when advising wholesale clients. For example:

- there is a lower entry hurdle for advisers wishing to provide advice to wholesale clients only; and
- some of the regulatory requirements, including disclosure and dispute resolution, do not apply when providing advice to wholesale clients.

The current legislative conduct obligations – to exercise care, diligence, and skill and not engage in misleading or deceptive conduct – apply to all financial advice (including advice to wholesale clients).

The philosophy behind the lower obligations is that wholesale clients – particularly those who are truly sophisticated or institutional clients – are less likely to benefit from the protections (e.g. because information asymmetries are less likely). Moreover, if the obligations were the same as for advice to retail clients, wholesale clients may need to pay more for advice (because the compliance costs would likely be passed through). They would therefore be paying more for protections that are unlikely to benefit them.

What obligations apply when an AFA advises a wholesale client?

The regulatory obligations that apply when advising a wholesale client are slightly different if the adviser is an AFA. In this case some elements of the Code of Conduct apply to advice to wholesale clients (including to put the interests of the client first, act with integrity, manage conflicts of interest, and communicate effectively). The intent of this was to treat AFAs as a profession who are held to professional standards at all times, regardless of the client they are advising.

Some elements of the AFA Code apply only to advice to retail clients (e.g. an AFA must record in writing adequate information about any personalised services provided to a retail client).

What has Cabinet already decided?

In July 2016, Cabinet agreed that the broad approach to regulating wholesale clients should be retained [CAB-16-MIN-0336]. In accordance with Cabinet's decisions, the following would be retained:

- The current definition of wholesale client (with any minor or technical amendments needed to incorporate these provisions into the FMC Act and improve alignment with the FMC Act).
- The current entry hurdle for those who wish to provide advice *to wholesale clients only*. That is, a firm or individual providing advice to wholesale clients only would need to be registered but would not need to be covered by a financial advice licence.
- The current requirement that all advice (including advice to wholesale clients) should continue to be subject to the current conduct obligations of due care, diligence, and skill, and not engaging in misleading or deceptive conduct.

The remaining policy issues are:

- The coverage of a financial advice licence (and associated obligations and enforcement) where a firm has both wholesale and retail clients. That is:
  - Should the licence and associated obligations apply to all of a firm's activities or should they only apply in relation to the firm's retail clients?
- The conduct and disclosure obligations that should apply when advising wholesale clients. That is:
  - Should the new conduct and disclosure obligations (to put the consumer's interests first, to disclose prescribed information, to ensure the consumer is aware of the limitations of the advice) apply when advising wholesale clients?

Problem definition: some consumers may meet the definition of wholesale clients who are not truly sophisticated or institutional clients

While the intent of treating wholesale clients differently is clear, the definition of wholesale clients can never perfectly divide those who this regime seeks to protect versus those who are capable and better-off looking after their own interests.

On the one hand, there may be consumers who do not fall into the definition of a wholesale client but who do not require (or benefit from) the full range of legislative protections. The existing 'eligible investor' process overcomes this concern.

The remaining problem relates to consumers who are captured by the definition of a wholesale client but who are not truly professional or sophisticated clients. For example, a client may meet the threshold due to their wealth but lack a sophisticated understanding of financial products. The ability for clients to 'opt-out' of being treated as a wholesale client aims to overcome this concern.

However, MBIE has heard increasing concerns that:

- often wholesale clients are not aware of their status or the implications of it; and
- the number of consumers – who are not truly sophisticated or institutional clients – being treated as wholesale clients is likely to increase. This results from:
    - More consumers acquiring significant amounts of wealth (e.g. through the sale of their home in an environment of rising house prices).
    - A greater incentive for advisers to treat their clients as wholesale if possible, following the decision to more heavily regulate advice to retail clients. There are reports that this incentive played out in Australia when obligations on retail advice increased.

Objectives

The primary objective of the regulatory regime for financial advice is to promote the confident and informed participation of consumers in financial markets. Consistent with this, we have analysed options for the regulation of advice to wholesale clients against the below design characteristics:

- All advice, including advice to wholesale clients, is held to appropriate conduct standards, which is an important element in promoting confidence in our financial markets.
- The risk of consumers who are not truly sophisticated or institutional clients losing protections is minimised. This includes the sub-objective that consumers who meet the threshold of a wholesale client understand what they are getting and how best to respond.
- Undue compliance costs are minimised, including with regard to the fact that wholesale clients are not the key sector this legislation aims to protect.

The options considered in this RIS are also analysed against whether they result in a positive net assessment of costs, benefits and risks.

Options and impact analysis

Options 1A and 1B are mutually exclusive from each other. Otherwise the options below are not mutually exclusive. Note that because the remaining policy questions relate to the application of new legislative obligations and the move to firm-level licensing for all advice, there is no clear status quo. We have therefore not analysed the status quo as a single option.

The earlier RIS considered requiring consumers to 'opt-in' to being deemed a wholesale client (rather than automatically being treated as a wholesale client if they meet the criteria under the Act). This was not a preferred option on the basis that the compliance costs would be disproportionate. We note that the opt-in proposal is not being reconsidered; instead we are considering whether the below options will provide more proportionate means to address the problem.

Option 1A: Licence (and associated obligations) apply to all of the activities under a 'retail service' which may include advice to wholesale clients

Under this option, a firm's licence (and associated obligations such as FMA monitoring, information returns, and adhering to the Code of Conduct and licence conditions) would apply to all advice that falls within the FMC Act concept of a 'retail service', even if the advice is given to a wholesale client.

The FMC Act concept of a retail service is a service supplied to:

- a retail investor, or
- a class of investors where there is at least one retail investor in that class.

Therefore, under this option:

- A financial advice service provided to at least one retail client would be classed as a retail service and would be covered by the financial advice firm's licence (with associated obligations applying). For example, a bank's wealth-banking division would likely involve advice to at least some retail clients and hence would be a retail service.
- In contrast, a firm could have a purely wholesale advice offering which would not be covered by the licence. For example, a bank's corporate/institutional banking unit will likely only provide services to other businesses.

This means that all advice provided under the retail service – whether to a wholesale or retail client – would form part of the licensing assessment, would be subject to the ongoing monitoring requirements, would be required to comply with the Code of Conduct, and would be subject to the licensing enforcement tools.

This option has parallels to the current approach for AFAs. Currently, the authorisation and monitoring of AFAs relates to the full breadth of an AFA's advice services (i.e. including services to wholesale clients) and an AFA is always subject to the Code of Conduct.

The FMA would have the ability to designate a service as retail, including if it is not clearly demarcated from a firm's retail service and therefore not easily recognisable to consumers that it is a wholesale service.

As per the status quo, the Code of Conduct would be able to set proportionate standards for advice to wholesale clients. For example, the current AFA Code of Conduct applies some standards to all advice (including putting the interests of the client first) whereas others apply only to advice to retail clients (e.g. an AFA must record in writing adequate information about any personalised services provided to a retail client).

Benefits

This option minimises the risk of consumers who are not truly sophisticated or institutional clients losing all protections, since such consumers are more likely to seek advice from a provider that advises (at least some) retail clients. For example, a person who meets the wholesale threshold simply because they have sold their house and is investing in a managed scheme would be unlikely to seek advice from a firm/unit that only provides advice to wholesale clients. Moreover, if a client does use a wholesale advice service, they are more likely to be aware this is the case (since it is a clearly demarcated service).

This option ensures that those providing dedicated wholesale services do not face undue compliance costs (with those costs being passed to the consumer).

This option provides a flexible tool for the FMA to ensure that it is not being gamed.

Costs/risks

This option would increase compliance costs to advisers associated with providing a retail service to wholesale clients (e.g. to comply with the applicable Code of Conduct standards). However, since these advisers will have had to establish processes for compliance with these standards for their retail clients, and because the standards can be set proportionately, these compliance costs are not expected to be significant.

This option could incentivise firms to only deal with wholesale clients so that it is classed as a wholesale service.

Option 1B: Licence (and associated obligations) applies to retail clients only

In contrast to Option 1A, this option would not use the retail service concept in the FMC Act. Instead, a firm's licence (and associated obligations) would only relate to its retail clients. The licensing assessment by the FMA, the ongoing monitoring requirements, the Code of Conduct, and the licensing enforcement tools, would only apply to advice to retail clients.

For example, under this option the licence for a bank's wealth-banking division (which has a mix of wholesale and retail clients) would only cover its advice to retail clients. That is, the granting of the licence, the ongoing monitoring and information returns, and the Code of Conduct, would only relate to the division's advice to its retail clients.

Benefits

This option ensures compliance costs are minimised in relation to wholesale clients (e.g. since the licensing process and Code of Conduct requirements only apply when advising retail clients).

Costs/risks

Under this option, wholesale clients are less likely to be aware of their status and its implications (since the same service may be retail or wholesale depending on who the client is). As a result, this option does not address the risk of removing protections for consumers who are not truly sophisticated or institutional clients.

This option is likely to create confusion and is unlikely to promote confidence in financial markets as the same service is regulated in two different ways.

This option would increase the incentive for advisers to treat their clients as wholesale (i.e. if the client meets the wholesale threshold) even if the adviser knows they are not a truly sophisticated client.

Option 2: Disclosure obligation applies when providing advice to wholesale clients

Under this option, all advice (including advice to wholesale clients) would be subject to the new legislative obligation to disclose prescribed information.

Importantly, the new legislation will take a different approach to setting disclosure obligations. Whereas the FA Act is relatively prescriptive about when and how disclosure must be made, the new legislation will simply require disclosure of prescribed information. The content, format and timing of disclosure will be detailed in Regulations. This means that the requirements for the timing and content of disclosure could differ for advice to wholesale versus retail clients.

Benefits

This option could respond to concerns about some consumers being treated as wholesale clients, when they are not truly professional or sophisticated clients. For example the prescribed disclosure could require advisers to take reasonable steps to ensure the client is aware they are regarded as a wholesale client, the consequences of that status, and that they can opt-out of that status.

This option allows flexibility, recognising that the content, format and timing of disclosure will be set in regulations (and will be subject to detailed regulatory impact analysis at that point) and recognising that it will be able to differ for advice to wholesale versus retail clients.

This option is likely to minimise the confusion that can arise from some advisers having disclosure obligations while others do not. As an example, similar confusion has been highlighted through submissions as a result of the current different disclosure obligations that apply for RFAs versus AFAs.

Costs/risks

This option will impose costs on those providing advice to wholesale clients (i.e. the costs of making the required disclosures). However, the costs will be assessed and subject to regulatory impact analysis at the time the relevant regulations are made.

Option 3: Consumer-first obligation applies when providing advice to wholesale clients

Under this option, all advice (including advice to wholesale clients) would be subject to the new legislative obligation to place the interests of the consumer first.

Benefits

This option would create a level playing field whereby all advice is subject to the same broad conduct standard. This would promote confidence in our financial markets.

This option would improve outcomes for any consumers who meet the definition of wholesale client but who are not truly sophisticated or institutional clients (since the provider must put the consumer's interests first regardless of whether they are a wholesale or retail client).

This option is in line with other professions – e.g. lawyers – whereby all activities are held to strong conduct standards.

This option may decrease the incentive for advisers to treat a consumer as wholesale even if they are not truly sophisticated or institutional clients – i.e. because it would lessen the difference in obligations that apply when giving advice to wholesale versus retail clients.

Costs

This option may impose additional compliance costs on advisers when advising wholesale clients which could be unwarranted in the case of truly sophisticated or institutional clients. These additional costs notwithstanding, those providing advice to wholesale clients would be subject to less oversight and associated compliance costs than those providing advice to retail clients.

Further consultation regarding advice to wholesale clients: MBIE is to undertake additional consultation alongside the exposure draft to better understand the magnitude of the cost associated with the consumer-first obligation applying when advice is being provided to wholesale clients.

Option 4: Obligation to ensure the consumer understands the limitations of advice applies when providing advice to wholesale clients

Under this option, all advice (including advice to wholesale clients) would be subject to the new legislative obligation to ensure that consumers are aware of the limitations of advice. This would include confirming how many types of financial products and providers have been considered and the elements of the consumer's circumstances that have been taken into account.

Benefits

This option may decrease the incentive for advisers to treat a consumer as wholesale even if they are not truly sophisticated or institutional clients – i.e. because it would lessen the difference in obligations that apply when giving advice to wholesale versus retail clients.

This option would improve outcomes for any consumers who meet the definition of wholesale client but who are not truly sophisticated or institutional clients.

Costs

This particular obligation is likely to impose disproportionate costs on advisers when advising wholesale clients (i.e. it requires disclosure specific to each client about the advice and any associated limitations; this level of consumer protection is unlikely to yield net benefits in the context of advice to wholesale clients). This is particularly the case if the other options presented in this section are progressed – i.e. the other options should decrease the risk of the 'wrong' people being treated as wholesale clients.

Assessment of options against criteria and summary of cost/benefits analysis

	Confidence in financial markets promoted through holding all advice to appropriate conduct standards	The risk of consumers who are not truly sophisticated or institutional clients losing protections is minimised	Undue compliance costs are minimised	Net assessment of costs, benefits and risks
Option 1A: Utilise FMC Act concept of a retail service	All advice within a retail service is held to the same licensing obligations and the Code of Conduct. ✓	Minimises the risk of consumers who are not truly sophisticated or institutional clients losing all protections, since: (1) such consumers are more likely to seek advice from a retail advice service and (2) are more likely to be aware when receiving a wholesale service since it is a clearly demarcated service. ✓✓	Ensures that those providing dedicated wholesale services do not face undue compliance costs (with those costs being passed to the consumer). Some increase in compliance costs when advising wholesale clients under a retail service, but these are not expected to be significant. ✓	Net benefit. While this option would impose costs when providing a retail service to wholesale clients, the costs are outweighed by the benefits of minimising the risk to consumers.
Option 1B: Licence (and associated obligations) applies to retail clients only	Having lower obligations for the exact same service (depending on who the client is) is likely to create confusion and unlikely to promote confidence in financial markets. ×	This option does not address risk to consumers who meet the wholesale definition but are not truly sophisticated clients. Wholesale clients are less likely to be aware of their status and its implications (since the same service may be retail or wholesale depending on who the client is). ×	Ensures compliance costs are minimised when advising wholesale clients. ✓	Risk of harm to consumers likely outweighs benefits of lower compliance costs.
Option 2: Disclosure obligation applies when providing advice to wholesale clients	Consistent disclosure likely to minimise confusion and promote confidence in financial markets. ✓	Responds to concerns about consumers being treated as wholesale when they are not truly professional or sophisticated clients. ✓✓	This option will impose costs on those providing advice to wholesale clients (i.e. the costs of making the required disclosures). However, the costs will be assessed and subject to regulatory impact analysis at the time the relevant regulations are made. ~	Net benefit. This option ensures consumers are aware of their status. Any prescribed disclosure will be subject to further regulatory impact analysis at the time regulations are made.

Option 3: Consumer-first obligation applies when providing advice to wholesale clients	This option would create a level playing field whereby all advice is subject to the same broad conduct standard. This would promote confidence in our financial markets. ✓✓	This option would improve outcomes for any consumers who meet the definition of wholesale client but who are not truly sophisticated or institutional clients (since the adviser must put their interests first regardless). ✓✓	This option may impose additional compliance costs when advising wholesale clients which could be unwarranted in the case of truly sophisticated or institutional clients. We will consult further on the magnitude of this cost. ×	This option is expected to result in a net benefit, though we are consulting further on the magnitude of the cost.
Option 4: Obligation to ensure the consumer understands the limitations of advice applies when providing advice to wholesale clients	This option would create a level playing field whereby all advice is subject to the same client care requirement. This would promote confidence in our financial markets. ✓	This option would improve client care for any consumers who meet the definition of wholesale client but who are not truly sophisticated or institutional clients (since the adviser must advise them of limitations regardless). ✓	This particular obligation is likely to impose disproportionate costs when advising wholesale clients (i.e. it requires disclosure specific to each client about the advice and any associated limitations). ×	Net cost. This level of consumer protection – i.e. disclosure specific to each consumer – is unlikely to yield net benefits in the context of advice to wholesale clients (particularly if the options 2 and 3 are adopted).

Our preferred approach is to utilise the FMC Act concept of a retail service. This will mean that there is a clearer dividing line between services that are subject to the licensing process and associated obligations (retail services) and those that are not (wholesale services). This will minimise the risk to consumers who may simply meet the wholesale threshold by virtue of their wealth. In addition, we propose:

- that the disclosure obligation applies to all advice, with the ability for the prescribed disclosure requirements to differ for advice to wholesale clients versus retail clients; and
- that the obligation to put the consumer's interests first apply to all advice.

In combination, the above options will ensure that all advice is held to appropriate conduct standards (including advice to wholesale clients) and will improve the ability for wholesale clients to understand their status and how best to respond.

Key
✓✓ Meets the objective
✓ Partially meets the objective
× Does not meet the objective
~ No impact on achievement of objective
☐ Shaded row = preferred option

Part C: Mechanics of the Code of Conduct and Code Committee

Status quo and problem definition

A Code Committee currently develops and maintains a Code of Professional Conduct for Authorised Financial Advisers…

Under the current financial advisers regime, a subset of advisers (approximately 1,800 AFAs) are required to meet minimum standards of competence, knowledge and skills, ethical behaviour, and client care, as set out in the Code of Professional Conduct for AFAs (the Code). For example, the Code states that "An Authorised Financial Adviser must place the interests of the client first, and must act with integrity" and requires AFAs to attain the relevant National Certificate in Financial Services (Financial Advice).

The Code is set by a Code Committee, whose members are appointed by the FMA on the basis of their knowledge of the financial adviser industry, or, in respect of one member, their knowledge of consumer affairs. The FA Act requires the Code Committee to prepare a draft Code of Conduct for approval by both the FMA and the Minster of Commerce and Consumers Affairs, and to review the content of the code from time to time. In approving the Code the FMA and the Minister must be satisfied that the Code Committee has met its statutory requirements in preparing the draft Code of Conduct.

Through submissions, MBIE received feedback that the Code and the Code Committee process are working well. Submitters highlighted that industry and consumer representation provides appropriate viewpoints and balance in the development of industry standards.

…however, the new financial advice regime significantly expands the scope of who is held to a Code of Conduct

Recent Cabinet decisions will require anyone providing financial advice to be held to a Code of Conduct [CAB-16-MIN-0336]. The new code will be developed by a Code Committee, and will set minimum standards for conduct, competence and client care. The Code Committee will identify sub-specialisations within the industry, and the code will include standards that apply to all providers of advice, and standards that are specific to particular parts of the industry (consistent with the identified sub-specialisations).

In light of the changed scope and coverage of the Code, some functions and proceedings of the Code Committee may no longer be fit for purpose.

The criteria for appointing members of the Code Committee is no longer fit for purpose

As the Code now applies to all providing financial advice, and not just a subset of advisers, it is important that the Code Committee has the expertise necessary to set standards for the whole financial advice industry.

Through consultation, we also heard some concerns that the current Code Committee does not have sufficient consumer representation. This is increasingly important as the new regime places an increased focus on improving consumer outcomes.

The proceedings for the Code Committee and Code of Conduct could be improved

It appears inefficient to have a double approval process for the draft code, particularly where the Minister's approval criteria for the draft Code must already be satisfied in order for the FMA to approve it.

A Code of Conduct is needed for industry certainty, but the Code Committee cannot commence work until the Bill is passed

It is desirable to provide industry with certainty and guidance about what compliance under the new regime will entail as soon as possible. Key feedback from stakeholders following the first set of Government decisions was that many will not know what is needed of them under the new regime until the details are revealed via the Code of Conduct.

As the Code Committee is established through statute, it cannot be appointed until after passage of the Bill. Leaving development of the code until after the Bill is passed would both perpetuate industry uncertainty and delay the benefits of the regime being realised.

Objectives

The primary objective of the regulatory regime for financial advice is to promote the confident and informed participation of consumers in financial markets. Consistent with this, we have analysed the options in this part of the RIS against the following objectives:

- The Code Committee has the knowledge, skills and expertise to draft and maintain a Code of Conduct for all providing financial advice.
- The functions and proceedings of the Code Committee are efficient and reflect occupational regulation best practice for rule-making.
- Provide certainty to industry participants around code standards as soon as possible.

The options considered in this RIS are also analysed against whether they result in a positive net assessment of costs, benefits and risks.

Options and impact analysis

We have identified the following options for meeting those objectives. The status quo is mutually exclusive to all other options, while options 3A and 3B are also mutually exclusive.

Option 1: Status Quo

Under this option the mechanics of the Code of Conduct and Code Committee would remain the same. This would include the membership criteria, and process for the appointment of members to the Code Committee as outlined above, as well as the process regarding the drafting and approval of the Code.

Benefits

Appointment of Code Committee members by the FMA is likely to be more efficient than Ministerial appointment (as outlined in Option 2).

Costs/Risks

Retaining the status quo would result in the initial Code being developed later than in Option 2, and result in a missed opportunity to amend the proceedings to reflect best practice.

The Code Committee may not have the breadth of knowledge, skills and expertise required to draft the new Code, given the significant increase in the activities governed by the new Code.

Option 2: Minister to appoint the Code Committee and approve the draft code

Under this option, the roles and responsibilities currently held by the FMA regarding the Code Committee and Code of Conduct will be held by the Minister of Commerce and Consumer Affairs. This would include appointing and discharging members of the Code Committee (including the chairperson) and approving the draft code. The process for the approval of the draft code would remain similar to that set out in the FA Act, but the Minister would be required to consult with the FMA.

This option would also include the appointment of a Code Working Group by the Minister in early 2017 to develop the Code of Conduct in parallel with the legislative process. This would allow the Minister to approve a draft code soon after the Bill is passed. The membership of the Code Working Group would reflect the required makeup of the Code Committee as outlined in the Bill. The Code Committee would then maintain the Code and recommend changes to the Minister.

Benefits

While Ministerial appointment of Code Committee members is potentially more time consuming than appointment by the FMA, it appears to be in line with common practice in other occupational regulation regimes. There are established protocols for Ministerial appointments, including that appointments are taken through the Cabinet Appointments and Honours Committee (APH), and guidance on addressing conflicts of interests. This creates additional checks and balances on the appointment process.

Ministerial appointment will also mean that the Code Committee is subject to the Official Information Act 1982, increasing the transparency of the Code Committee's proceedings.

This option would increase the efficiency of the approval process for the draft code and remove the duplication in approval criteria, while maintaining the FMA's input. As the regulator, FMA scrutiny of the draft code is important, to ensure the code standards can be implemented and enforced effectively.

Appointing a Code Working Group will allow elements of the new regime, and the associated benefits, to take effect approximately 12 months sooner than under the status quo.

Costs/risks

Shifting appointment to the Minister has implications for the timing and speed of appointment2. If the Terms of Reference for the Code Working Group are set before enactment, there is a risk that the provisions for the content, functions and proceedings of the Code Committee, may be changed during the legislative process. If this happens, further work would be required after the Bill is passed to ensure the legislative requirements have been met. However, this risk is mitigated to some extent

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[2] SSC *Board Appointment and Induction Guidelines* suggest that Ministers need to be engaged at least six months in advance of a member's expiry date, and at least nine months for the appointment of a new chairperson. Ministerial appointment decisions also have to be taken through the APH Committee, followed by Cabinet, which are dependent on sitting dates. State Services Commission. November 2009, updated October 2015. Board Appointment and Induction Guidelines. ***http://www.ssc.govt.nz/sites/all/files/board-appt-guidelines-oct15.pdf***

as the Minister would have the ability to update the Terms of Reference for the Code Working Group.

Option 3A: Broadened appointment criteria and increased consumer representation

This option would broaden the appointment criteria to ensure flexibility, and would increase consumer representation on the Code Committee, as follows:

- two members qualified for appointment based on their knowledge, skills and experience in relation to, consumer affairs or dispute resolution; and
- other members who are qualified for appointment, having regard to the functions of the Code Committee, by virtue of that person's knowledge, skills and experience in financial services, or any other knowledge, skills and experience deemed relevant.

Benefits

This option would provide greater consumer voice in the development of a code that now impacts a larger number of consumers. This may contribute to improving public perception and trust in the financial advice industry[3].

This option would ensure that the Code Committee has a membership with the appropriate mix of skills, perspectives and experiences. Relative to a more rigid approach which lists specific required skills, this option maintains flexibility around the make-up of the Code Committee, and allows it to be adapted based on developments in the financial advice market. For example, depending on the approach taken to setting standards for robo-advice, it may be necessary to have a Code Committee member with experience in algorithms and scenario testing for various robo-advice platforms.

Costs/risks

Having two consumer representatives may come at the opportunity cost of another competency area (as the Code Committee has an upper membership limit). Any risk associated with having a broad membership criteria, which could result in knowledge gaps, is mitigated by the robust appointment process.

Option 3B: Prescribe specific competencies that must be covered by the Code Committee on a collective basis

With this option, legislation would prescribe specific competencies that must be satisfied by Code Committee members. Two members would be qualified for appointment based on their knowledge of, and experience and competency in relation to consumer affairs and dispute resolution, and other members must satisfy, for example, the following competencies:

- knowledge of the financial advice industry;
- general knowledge about how to assess and test competency, or experience in setting competency standards (which may or may not be in relation to financial advice);
- knowledge of financial technology; and
- any other areas as prescribed in regulations.

[3] The Issues Paper consumer questionnaire conducted as part of this review found that 27 per cent of respondents were not confident in the professionalism and integrity of financial advisers, and 30 per cent were only somewhat confident. Fifty percent of respondents said their confidence in the professionalism and integrity of financial advisers has not changed since the FA Act took effect in 2011.

These competencies would be required to be held by the Code Committee on a collective basis, meaning that one member could satisfy one or more of the competencies. Regulations would allow for competencies to be added or subtracted. The two consumer representatives would not be included in the collective approach to ensure a minimum of two distinct consumer representatives.

Benefits

This option provides more guidance for the appointment of Code Committee members, and would ensure that competencies deemed integral are covered. The membership criteria retain a degree of flexibility with the ability to add or subtract competencies through regulations.

Costs/risks

Because of the size of the industry and the broad range of products and services, prescribing a small number of competencies may still be difficult to get right. Prescribing specific competencies is also inflexible, relative to Option 3A.

Again, having two consumer representatives may come at the opportunity cost of another competency area (as the Code Committee has an upper membership limit).

Minor amendments not discussed in this RIS will be made to the proceedings of the Code Committee to ensure consistency with occupational regulation best practice. For example, any draft code produced by the Code Committee would need to be supported by an impact analysis that refers to the purposes of the FMC Act and any additional purposes specific to financial advice. The Code Committee would also be required to publish a summary of submissions received, and a response to these submissions.

Assessment of options against criteria and summary of cost/benefits analysis

	The Code Committee has the knowledge, skills and expertise to draft and maintain a Code of Conduct for all providing financial advice	The functions and proceedings of the Code Committee are efficient and reflect occupational regulation best practice for rule-making	Provide certainty to industry participants around code standards as soon as possible	Net assessment of costs, benefits and risks
Option 1: Status Quo	The Code Committee is unlikely to have the breadth of knowledge, skills and expertise necessary given the significantly increased scope of the Code. ×	Missed opportunity to update the process and criteria to reflect best practice. ~	Does not allow Code Standards to be known earlier as per Option 2. ×	Net cost. Retaining the status quo may prevent the Code Committee from having the breadth of knowledge, skills and expertise necessary and will prevent the Code from being developed until after the Bill is passed.
Option 2: Minister to appoint Code Committee and approve the draft code	Legislative criteria and established Ministerial appointment protocols support a robust appointment process for the Code Committee and the Code Working Group. ✓	Common practice for Minister to appoint rule-making authorities and established protocols provide checks and balances on the process. This option increases efficiency in the approval process. ✓✓	This option will provide industry with more certainty about the code requirements sooner. Most elements of the new regime will also be able to take effect sooner. ✓✓	Net benefit. Overall this option is likely to increase efficiency in the approval of the draft Code, provide a more robust appointment process, provide certainty for industry and allow benefits of the new regime to be realised sooner.
Option 3A: Broadened appointment criteria and increased consumer representation	This option provides for a flexible Code Committee membership with a broad range of experiences. It also provides greater consumer representation to reflect the greater number of consumers now impacted by the Code. ✓✓	~	~	Net benefit. Overall this option provides flexible membership criteria covering a range of competencies, as the status quo is no longer fit for purpose.
Option 3B: Prescribe specific competencies that must be covered by the Code Committee on a collective basis	This option ensures certain competencies are included in Code Committee membership and provides greater consumer representation. However, prescribing a small number of competencies for such a diverse industry may be difficult and is inflexible relative to option 3A. ~	~	~	Net benefit relative to the status quo. However, it may be difficult to get the prescribed competencies right in practice.

As a package, our preferred options increase certainty for industry participants around the code standards and increase transparency in the process for developing the standards (by ensuring the proceedings are consistent with occupational regulation best practice). This package also provides for an appropriate balance of flexibility, efficiency and robustness in the processes for appointing the Code Committee, and producing and approving the Code of Conduct.

Key
✓✓ Meets the objective
✓ Partially meets the objective
× Does not meet the objective
~ No impact on achievement of objective
☐ Shaded row = preferred option

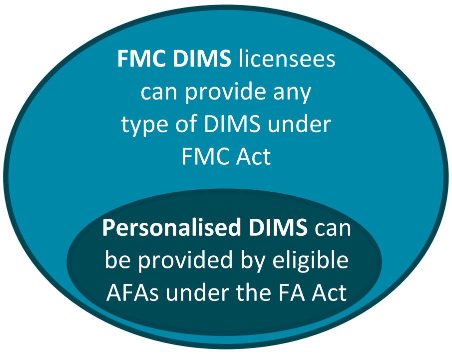
Part D: The regulation of personalised DIMS

Status quo and problem definition

DIMS are currently regulated under two distinct regimes

A discretionary investment management service (DIMS) is defined as any service in which the provider decides which financial products to acquire or dispose of on behalf of and authorised by their client. DIMS are currently regulated under two separate Acts:

- The regulation of most DIMS is provided for under the FMC Act, which introduced a licensing regime for DIMS providers. These providers can offer any sort of DIMS. There are 58 DIMS licensees under the FMC Act.
- AFAs can provide limited personalised DIMS services under the FA Act, if the investment strategy is personalised to the client's circumstances. These advisers are exempt from being licensed under the FMC Act. There are ten AFAs authorised to provide personalised DIMS under the FA Act.



The requirements under both regimes are largely aligned

The requirements applying to FMC Act DIMS providers and FA Act DIMS providers are largely aligned. In particular, when the FMC Act licensing regime for DIMS was introduced in 2014, a series of complementary changes were made to the regulation of personalised DIMS under the FA Act, including as follows:

- An eligibility requirement for AFAs who provide DIMS was introduced, allowing the FMA to assess whether they are capable of effectively performing the service and whether there is any reason to believe that they will not comply with their legal obligations.
- Additional matters were added to the existing disclosure statements of AFAs offering DIMS to align with the disclosure requirements under the FMC Act.
- The requirements for client agreements under the FA Act were aligned with the requirements under the FMC Act.
- A reporting requirement was introduced for AFAs providing DIMS to mirror the FMC Act requirements.

The 2014 Cabinet paper that aligned the requirements noted that ensuring all DIMS providers are subject to similar obligations will have a beneficial impact on consumer confidence, and reduce the risk of regulatory arbitrage and investor confusion.

There are two main differences in the regulation of DIMS between the FA Act and the FMC Act:

- Related party benefits: FMC Act DIMS licensees are prohibited from completing transactions which benefits the licensee, or a related party, at the expense of their client. AFAs are not prohibited from this requirement under the DIMS obligations, but are subject to conduct and client-care obligations in the Code of Conduct for AFAs.
- Reporting on limit breaks: FMC Act DIMS licensees are required to report to the FMA when there are material breaches of the limits set by the client regarding the amount or type of investments made. AFAs do not have this requirement.

The DIMS licensing regime is flexible

The FMC Act DIMS licensing regime was designed to be sufficiently flexible, such that it does not become a barrier to small businesses, recognising the broad range of services that fall under the umbrella definition of DIMS. For example, the systems and controls expected in a single-adviser business will be simpler than those expected in a larger or more complex business. In addition, the FMA produced guidance which outlines how a small business (either a single adviser or small business) providing lower risk DIMS can approach an application for a DIMS licence.

Relevant changes already decided by Cabinet and through the drafting process

The following decisions that have been made to-date are relevant to the analysis of the options relating to DIMS:

- The July 2016 Cabinet decisions include a requirement for all firms providing financial advice to obtain a licence from the FMA.
- The changes are likely to be achieved by repealing the FA Act and incorporating the regulation of financial advice into the FMC Act.

The same service will be regulated in two distinct ways under the same Act

As the regulation of financial advice is to be incorporated into the FMC Act, if DIMS remains a financial advice service it would result in the existence of parallel regulatory regimes operating independently to each other within the FMC Act. This would result in the FMA being required to monitor DIMS providers in two slightly different ways. It could continue to cause confusion to consumers who would receive differing disclosure documents from DIMS licensees subject to different requirements.

Objectives

The primary objective of the regulatory regime for financial advice is to promote the confident and informed participation of consumers in financial markets. In order to achieve this, MBIE has identified the following additional objectives for the regulation of DIMS:

- Regulation is enabling with no undue compliance costs, complexity or barriers to innovation.
    - Suitable transitional arrangements exist for current providers.
- Applies appropriate oversight of financial products and services.

    - The FMA receives sufficient information in order to monitor the populations that it regulates.
- The facilitation of fair and transparent financial markets.
    - Consumers have access to the same information about similar services.
    - Similar activities are regulated in the same way.

The options considered in this RIS are also analysed against whether they result in a positive net assessment of costs, benefits and risks.

Options and impact analysis

We have identified the below mutually exclusive options.

Option 1 – Personalised DIMS treated as a financial advice service (effectively the status quo)

Under this option (which is effectively the status quo, incorporated into the new regime), personalised DIMS would continue to be treated as a financial advice service. A firm's ability to provide personalised DIMS would be considered as part of its FMC Act licence application to provide financial advice. Due to the shift to firm-based licensing (as already agreed by Cabinet), AFAs currently authorised to provide personalised DIMS would be required to obtain a financial advice firm licence in order to continue providing personalised DIMS.

Benefits

This option would not impose additional compliances costs (on AFAs) associated with related party benefits and reporting on limit breaks.

Costs/risks

This option does not address the identified problem. That is, as the regulation of financial advice is to be incorporated into the FMC Act, it would result in the existence of parallel regulatory regimes operating independently to each other within the FMC Act. This would result in the FMA being required to monitor DIMS providers in two slightly different ways. It could continue to cause confusion to consumers who would receive differing disclosure documents from DIMS licensees subject to different requirements.

Option 2A – All DIMS providers subject to the same requirements

Rather than continuing to treat DIMS as a financial advice service, under this option all DIMS providers will be subject to the requirements in the FMC Act and will be required to hold an FMC Act DIMS licence.

Benefits

This option will provide benefits to the FMA due to the fact that all DIMS providers will be regulated in the same way and subject to the same requirements. This may also benefit consumers who will now be able to more easily compare DIMS providers through the same disclosure requirements.

Costs/Risks

AFAs currently providing personalised DIMS may be required to meet some additional reporting requirements regarding limit breaks. However, the requirements for DIMS providers under both regimes are broadly similar and any additional costs are expected to be relatively low.

This option would lead to increased costs for personalised DIMS providers associated with obtaining an FMC Act DIMS licence. These providers' current authorisation is based on their ability to provide personalised DIMS. They may therefore need to implement processes and systems to satisfy the FMA that they can provide other forms of DIMS before being granted a licence.

Option 2B – All DIMS providers subject to the same requirements, with grandfathering for existing personalised DIMS providers

As with Option 2A, under this option all DIMS providers will be subject to the requirements in the FMC Act and will be required to hold an FMC Act DIMS licence. Recognising the broad alignment of the regulation of DIMS under both regimes, AFAs who are authorised to provide personalised DIMS will be granted FMC Act DIMS licences, subject to the condition that the service is limited to that which they can currently provide under the FA Act.

Benefits

This option will provide benefits to the FMA due to the fact that all DIMS providers will be regulated in the same way and subject to the same requirements. This may also benefit consumers who will now be able to more easily compare DIMS providers through the same disclosure requirements.

In addition, this option should ensure AFAs who are currently authorised to provide personalised DIMS will not face compliance costs associated with obtaining an FMC Act DIMS licence (i.e. the cost outlined in Option 2A).

Costs/Risks

AFAs currently providing personalised DIMS may be required to meet some additional reporting requirements regarding limit breaks. However, the requirements for DIMS providers under both regimes are broadly similar and any additional costs are expected to be relatively low.

Any risk associated with grandfathering AFAs authorised to provide personalised DIMS to the new regime is mitigated by imposing a restriction on their FMC Act DIMS licence. This will ensure that they only offer a service that they have already been assessed as competent to provide.

Assessment of options against criteria (relative to the status quo) and summary of cost/benefits analysis

	Regulation is enabling with no undue compliance costs, complexity or barriers to innovation	Applies appropriate oversight to financial products and services	The facilitation of fair and transparent financial markets	Net assessment of costs, benefits and risks
Option 1: Personalised DIMS treated as a financial advice service (effectively the status quo moved to the new regime)	This option retains the complexity of two slightly different regulatory regimes. ~	~	As per the status quo, the same or similar service is regulated in two different ways. ~	~
Option 2A: All DIMS providers subject to the same requirements	This option removes much of the complexity from the status quo. However, AFAs will face increased compliance costs in order to obtain an FMC Act DIMS licence. ~	Improvement to the status quo by applying the same requirements on all DIMS providers. ✓	Consumers will receive the same information regarding DIMS providers. ✓	Overall this option is an improvement on the status quo for consumers and the FMA. However, AFAs will face increased compliance costs to obtain a FMC Act DIMS licence.
Option 2B: All DIMS providers subject to the same requirements, with grandfathering for existing personalised DIMS providers	This option removes much of the complexity from the status quo, and reduces compliance costs for AFAs who will be granted a FMC Act DIMS licence. ✓✓	Improvement to the status quo by applying the same requirements on all DIMS providers. ✓	Consumers will receive the same information regarding DIMS providers. ✓	Overall this option is an improvement on the status quo for consumers and the FMA, with relatively minimal impact on AFAs authorised to provide personalised DIMS.

We prefer Option 2B which will impose the same requirements on all DIMS providers and avoids the problems associated with having two slightly different regulatory regimes for a similar service. Granting FMC Act licences to existing personalised DIMS providers will enable AFAs currently authorised to provide personalised DIMS to continue offering their service under an FMC Act DIMS licence with minimal disruption.

Key
✓✓ Significant improvement on the status quo
✓ Improvement on the status quo
× Inferior to the status quo
~ No impact relative to the status quo
☐ Shaded row = preferred option

Part E: Misuse of the Financial Service Providers Register

Status quo and problem definition

Some firms have been misusing the FSPR

Anyone who is in the business of providing a financial service is required to be registered on the FSPR. This requirement applies to a range of financial markets participants such as banks, lenders, foreign exchange providers and financial advisers.

The registration system allows for identification of all those in the business of providing financial services in New Zealand and their financial dispute resolution scheme. It also assists with meeting New Zealand's obligations under the Financial Action Task Force (FATF) Recommendations to register or licence all financial institutions.

There is some interrelationship between the FSPR and the decision to licence the provision of all financial advice. The fact that all financial advisers need to be engaged by a licensed firm reduces the likelihood of financial advisers being able to misuse the FSPR. However, licensing of financial advisers alone is not sufficient to meet the FATF Recommendations, which still require a range of other financial institutions be licensed or registered e.g. lenders and money transfer service providers. Therefore, measures to address misuse of the FSPR are still needed.

Some offshore-controlled firms have been registering on the FSPR to take advantage of New Zealand's reputation as a well-regulated jurisdiction. These firms misrepresent to customers that they are licensed or actively regulated in New Zealand. This may enable these firms to enjoy a lesser degree of scrutiny than might otherwise be the case. Some such firms have been connected to fraudulent activities overseas – the FMA receives a large volume of complaints from persons outside New Zealand relating to offshore-controlled firms registered on the FSPR, which have not paid out customer funds when required to.

Firms have been able to misuse the register by:

- registering for particular financial services such as foreign exchange services, which do not require the firm to be licensed in New Zealand (but which do require them to be registered); and
- setting up superficial New Zealand operations in order to fall within the currently wide scope of entities required to register. The requirement to register currently applies to a person who is ordinarily resident in New Zealand or has a place of business in New Zealand, regardless of where they are providing financial services. The entities in question often lease an office and employ a person to provide back-office services in New Zealand. They generally do not make financial services available to New Zealand-based customers, and are therefore unlikely to be subject to oversight by New Zealand regulators; and
- taking advantage of that fact that the public often misinterprets "registered" on the FSPR to mean an entity is actively regulated in New Zealand.

This issue is a risk to New Zealand's reputation as a well-regulated jurisdiction and to the reputation of legitimate FSPs based in New Zealand. Evidence of this problem is outlined in the previous RIS.

Other measures may also be needed to further reduce misuse

In July, Cabinet agreed to address the misuse issue by amending the FSP Act to require that companies registered on the FSPR have a stronger connection to New Zealand. The need to have more substantive operations in New Zealand would significantly reduce the ease and benefit of seeking registration on the FSPR for the purpose of misuse.

Cabinet also directed officials to consider complementary measures which could help address misuse of the FSPR. Even where registration requires a greater connection to New Zealand, there remains a risk that some firms may still find ways to misuse the FSPR. In particular:

- *Applications for registration generally occur before commencing business.* It may be hard to assess at the time of application whether the applicant will have a sufficient connection to New Zealand once they begin operating. An applicant whose business plan shows an intention to provide certain services to New Zealand customers may in fact not do so post-registration.
- *The circumstances of an FSP may change after registration.* The FMA and Registrar of the FSPR are aware of numerous instances of persons offering to buy ownership in existing FSPs, presumably to avoid initial checks as to whether they meet the requirements of the FSP Act.
- *Providers may find new ways of misusing the FSPR or find ways to avoid registration.* Some firms may adjust their operations in order to meet the amended registration requirements, for example, by undertaking token transactions with New Zealand customers. Conversely, some New Zealand-based FSPs that should be registered could adjust their operations in order to avoid registration.

The risks of misuse can never be fully eliminated. However, this RIS assesses options that could be implemented alongside the changes already agreed by Cabinet to assist with reducing the risk of misuse.

Objectives

The primary objective of the regulatory regime for financial advice is to promote the confident and informed participation of consumers in financial markets. We have identified the following objectives which relate to the measures intended to address the misuse of the FSPR:

- Any measures should be effective in helping to reduce misuse of the FSPR regime and therefore upholding the reputation of New Zealand's FSPR regime. Reducing misuse includes:
  - deterring applications from those who intend to misuse the FSPR; and/or
  - allowing regulators to effectively decline applications or deregister FSPs.
- Any measures should facilitate fair, efficient and transparent financial markets. This includes:
  - allowing regulators access to information about FSPs to assist their regulatory functions; and
  - enabling public access to information about FSPs; and

    - meeting New Zealand's obligations under the FATF Recommendations.

- Any measures should not impose unnecessary costs to legitimate businesses.

Options and impact analysis

We have identified options for meeting these objectives in addition to the status quo. These are not mutually exclusive (other than the status quo).

Option 1 – Status Quo

Under this option, the changes previously agreed by Cabinet to require a stronger connection to New Zealand would be implemented to reduce misuse of the FSPR, without any further measures.

Benefits

As set out in the previous RIS, the changes already agreed by Cabinet mean that it would no longer be sufficient for firms to set up superficial back-office operations in New Zealand in order to register on the FSPR. The need to have more substantive operations in New Zealand would significantly reduce the ease and benefits of seeking registration for the purpose of misuse.

Costs

Some risks of misuse may remain as outlined in the problem definition section above.

Option 2 – Limitation on advertising of registered status

Under this option, if an entity is not otherwise licensed in New Zealand, then if it refers to its New Zealand registered status (other than where required by law), it must explain the limitations of being registered, i.e. registration on the FSPR does not indicate the entity is licensed or monitored by a regulatory agency in New Zealand.

Breach of the limitation would be a ground for deregistration.

Benefits

This would prevent businesses that are registered on the FSPR from using that status to imply they are regulated in New Zealand. Therefore, even if a dishonest firm succeeded in passing initial checks to become registered, they would still be prohibited from taking advantage of that registration to mispresent that they are actively regulated in New Zealand.

The prohibition would also lessen the advantages of seeking to register on the FSPR.

There may be jurisdictional issues if New Zealand authorities sought to take enforcement action (other than deregistration) against businesses for breach of the proposed limitation where the relevant conduct occurred overseas. However, this option provides a clear-cut ground for the Registrar to deregister an entity if the proposed limitation is breached.

Costs

Some costs would be imposed on legitimate registered FSPs, who would need to take more care with their advertising to ensure they did not breach the proposed limitation. We have tried to limit those costs by providing that the limitation would not apply to businesses that have been licensed given they would have already been subject to fit and proper checks by the relevant licensing authority. This would be the case for a number of registered FSPs.

We will also test in the exposure draft process whether a transitional period would be required to allow legitimate providers to use existing hardcopy material that was produced before they became aware of the proposed limitation.

Option 3 – Additional registration requirements

Under this option, more stringent registration requirements would apply to certain applicants and registered FSPs. It could require that applicants be licensed or supervised in their home jurisdiction and in any jurisdiction that they are proposing to provide services to. Alternatively, it could require applicants to provide information relating to the regulation which they are subject to overseas, which could be published on the register.

Benefits

This option would provide greater assurances that an entity is reputable, and that there is an offshore regulator who may be able to assist the New Zealand authorities if the entity is allegedly involved in wrongdoing.

Costs

If licensing or some other level of regulation in another jurisdiction is required for registration, this may act as a barrier to entry for some otherwise legitimate entities. For example, they may be based in a country that does not license all financial services (like New Zealand).

There may also be some costs for the applicant and the Registrar and/or FMA to assess the quality of regulation that the applicant is subject to. There are some jurisdictions like Australia or the UK whose financial markets regulation is relatively well-known to the New Zealand authorities. However, in relation to some other jurisdictions, work will be required to establish that the claimed level of regulation is genuine and that it can be relied on as an indication that the applicant is a reputable entity.

Option 4 – Giving the Registrar power to require information from directors

Under this option, the Registrar would be able to require information or confirmation of information from particular directors of a registered FSP or an entity applying for registration. The power would be for the purpose of ascertaining whether an entity is/remains qualified to be registered.

The director would be personally liable for any false or misleading statements given. Failure to comply would, following an appropriate process, also be grounds for deregistration.

Benefits

This option would provide the Registrar with greater tools to detect possible misuse and may deter New Zealand-based directors from aiding misuse. Some New Zealand individuals have contributed to the misuse problem by assisting suspect entities to register on the FSPR.

As noted, the circumstances of an FSP may change after registration and may not reflect the information that was submitted at the point of application.

The FSP Act already provides some tools for the Registrar to ascertain whether an FSP remains qualified to be registered, including a power to require information from the FSP and offences for failure by an FSP to comply with such request or the supply of false or misleading information.

However, the above may not be a strong enough deterrent against misuse in cases involving offshore-controlled limited liability companies with few assets that are set-up primarily for fraudulent purposes.

Under this option, the Registrar could use the proposed powers to request information from (in particular) New Zealand-resident directors of entities identified as being potentially high-risk e.g. if there are doubts about the information provided by the company.

Personal liability for the director would incentivise them to ensure that they are not being false or misleading. Where this power is used, the Registrar would likely have greater assurances about the information provided to help the Registrar consider whether an entity is/remains qualified to be registered. This power would also likely deter some New Zealand individuals from helping to facilitate misuse by agreeing to act as nominee directors of entities applying to be registered FSPs.

Costs

Greater potentially liability for directors may disincentive some individuals from agreeing to become directors of legitimate FSPs. However, the Registrar would be unlikely to use such powers against entities it had no concerns about e.g. licensed entities that had already been subject to fit and proper checks by the relevant licensing authority. Directors would also only be required to provide information within their possession or control.

Related to option 4, the Options Paper also consulted on the option of requiring trust and company service providers (TCSPs) to register on the FSPR. TCSP services include assisting firms to register on the FSPR, and acting as nominee directors and registered offices for their clients. TCSP services can be used to provide anonymity for clients. TCSPs have in some cases contributed to the misuse problem by assisting suspect entities to register as a New Zealand company and/or on the FSPR.

In light of the other measures that are being recommended (particularly the proposed powers for the Registrar to request information from directors), we consider that requiring TCSPs to register on the FSPR would not be materially helpful in addressing misuse. While there was some support in submissions on the Options Paper for greater accountabilities for TCSPs generally, we consider that it is not within the scope of this FA Act/FSP Act review to address more general issues with TCSPs by requiring them to register on the FSPR.

Option 5 – provide ability to designate groups as requiring registration

Under this option a power would be included in the FSP Act allowing groups of person to be designated as requiring registration under the FSP Act (where those persons would not otherwise have been required to register).

To the extent necessary, the exemption power in the FSP Act would be clarified to ensure that certain groups of persons can be designated as *not* requiring registration.

The power(s) would be subject to certain criteria – including that it that it must be exercised consistent with the purposes of the FSP Act and be necessary to protect the integrity and reputation of New Zealand's financial markets.

Benefits

This option provides a more timely means of addressing any potential issue with entities that deliberately structure their operations to:

- *avoid the registration requirements* – some entities that should be registered could seek to avoid the compliance costs involved by setting up their operations in such a way as to avoid the need to register. (However, this is not expected to occur widely given that the costs of trying to avoid registration would likely outweigh the costs of registration itself); or

- *fall within the registration requirements in order to carry out misuse* – the misuse problem has arisen because firms have attempted to structure operations to narrowly fall within the current scope of the entities that are required to register on the FSPR. It is possible (though likely difficult) that firms could adjust their operations to fall within the amended requirements.

To reduce these risks, the proposed powers enable groups of persons to be brought into the FSP Act registration regime, while the exemption power (clarified as necessary) enables other groups of persons to be excluded from the registration regime.

Costs

Some costs will be imposed on the Government to monitor and respond where a designation is required.

There will also be costs for firms that are brought under the regime that would not otherwise have been required to register. However, an analysis would be undertaken at the time of any proposal to widen the regime to ensure that any costs imposed are not disproportionate compared to the benefits.

Assessment of options against criteria (relative to the status quo) and summary of cost/benefits analysis

	Reduce misuse of the FSPR and uphold the reputation of New Zealand's FSPR regime	Facilitate fair, efficient and transparent financial markets	Not impose unnecessary costs to legitimate businesses
Option 1: Status quo	While measures already agreed by Cabinet are likely to significantly reduce misuse, there remains a risk that some firms may still find ways to misuse the FSPR. ~	~	~
Option 2: Limitations on advertising of registered status	Registered firms prohibited from taking advantage of registration to misrepresent that they are actively regulated in New Zealand. The prohibition would also lessen the advantages of seeking to register. ✓✓	~	A small amount of costs may be imposed on legitimate registered FSPs who would need to take more care with advertising. ×
Option 3: Additional registration requirements	Provides greater assurance that an entity is likely to be reputable and that there is an overseas regulator who New Zealand authorities could contact to help obtain redress if something goes wrong. ✓	Provides greater assurance that an entity is likely to be reputable and there are avenues for redress, but requires judgement as to quality of regulation. ~	May prevent some otherwise legitimate businesses from registering. Also costs for both the business and the Registrar and/or FMA to establish the quality of the particular level of regulation an entity is subject to. ×
Option 4: Giving the Registrar the power to require information from directors	Registrar likely to have greater assurances about the information provided to help assess whether an entity is/remains qualified to be registered. Also likely to deter some New Zealand individuals from helping to facilitate misuse by agreeing to act as nominee directors of suspect entities. ✓	~	Legitimate New Zealand businesses unlikely to be subject to such a request. ~
Option 5: Provide ability to designate groups as requiring registration	Provides a more timely manner of addressing any potential issues of firms seeking to deliberately structure their operations to fall outside or within the registration requirements. ✓	Provides a more timely manner of addressing any potential issues of firms seeking to deliberately structure their operations to fall outside or within the registration requirements. ✓	~

Options 2, 4 and 5 are preferred to work alongside changes to the scope of entities required to register in order to help address misuse.
Option 3 is not preferred. However, we will explore whether further information could be provided on the register that may help the public to make decisions about whether they wish to engage with a particular provider. This may include information about the extent to which the provider is regulated offshore.

Key
✓✓ Significant improvement on the status quo
✓ Improvement on the status quo
× Inferior to the status quo
~ No impact relative to the status quo
☐ Shaded row = preferred option

Consultation, Implementation and Monitoring

Consultation

Formal consultation on the FA Act and FSP Act has been ongoing since May 2015. This has included:

- An Issues Paper published in May 2015 that sought public feedback on key issues with the regime and opportunities for change. Alongside the Issues Paper, a simplified consumer brochure was released, with a link to an anonymous, online questionnaire. A total of 166 submissions were received on the Issues Paper. 248 respondents completed the questionnaire attached to the consumer brochure.
- An Options Paper published in November 2015 that sought feedback on potential options for changes to the regulatory regime. A consumer brochure with an online questionnaire was released alongside the Options Paper. A total of 149 submissions were received on the Options Paper. 545 respondents completed the questionnaire attached to the consumer brochure.
- Three consumer focus groups and six public forums to seek public views on what is and is not working well with the current regime and where improvements could be made.
- Ongoing, targeted consultation with industry associations, regulators, other Government agencies, consumer representatives, advisers, QFEs, compliance advisers and academics.

Submissions received on both the Issues and Options Papers represented the views of a wide range of stakeholders, including firms, consumer representatives, dispute resolutions schemes, individual advisers, industry associations and general members of the public. MBIE has published the submissions received on both papers and summaries of the responses to the consumer questionnaire here: ***www.mbie.govt.nz/faareview***. MBIE officials analysed these submissions and the potential options for change to develop their policy recommendations.

Some of the options in this RIS have been formally consulted on at a relatively high-level to date. The next step in the process is the release of an exposure draft of the legislation. This will provide a further opportunity to confirm that the more detailed arrangements outlined in this RIS are fit for purpose. MBIE will also be seeking feedback on a proposal for transitional arrangements that will be released alongside the exposure draft.

Further feedback will also be sought regarding the extension of the FADC's jurisdiction to include financial advice firms as well as financial advisers, and the extent of compliance costs associated with applying the consumer-first obligation to those providing advice to wholesale clients.

Implementation plan

The options analysed in this RIS are part of the wider suite of changes to the regulation of financial advice. The Bill is expected to be passed in late 2017. MBIE is consulting further on the transitional arrangements for bringing the new regime into force.

Successful implementation of the options in this RIS will be dependent on the continued active participation and resource from a number of key parties, namely:

- Consumers and consumer groups - testing and refining disclosure statements, including how best to present conflicted remuneration.
- The FMA – assisting licensees through the transitional period, development and implementation of operational policies, market guidance and enforcement tools.
- The Code Committee and Code Working Group - developing and testing an expanded Code of Conduct, minimum standards for robo-advice, stepped pathway requirements, grandfathering provisions, and competency standards.
- Adviser associations and advisers – assisting members through the transitional period, supporting development of ethical and competency requirements, disclosure documents and possible further tools for consumers to find quality financial advice.
- Commission for Financial Capability - development of possible further tools for consumers to find quality financial advice, and leading the Government's strategy to improve financial capability.

Monitoring, evaluation and review

The impact of the proposals in this RIS, along with those contained in the earlier RIS, will be monitored by MBIE, in close cooperation with the FMA, on an ongoing basis as part of MBIE's ongoing regulatory stewardship obligations. Moreover, MBIE's role as a member of the New Zealand Council of Financial Regulators (COFR) means impacts of the proposed changes will be monitored to ensure the changes made are resulting in a well-functioning financial markets regime.

COFR has produced a Financial Markets Regulatory Charter which aims to promote active management of the financial markets regulatory system, including by reinforcing shared ownership for the system among those with policy and regulatory functions and recording an understanding about respective roles and functions and how the system is intended to perform. Other members of COFR (the FMA, the Reserve Bank of New Zealand and the Treasury) will continue to provide ongoing support to MBIE in monitoring of the impact of the proposals in this RIS.

Specific monitoring resources and activities that will be utilised in monitoring the effectiveness of this regime include:

- FMA and CFFC surveys into public confidence of financial advice.
- FMA information gathering and surveillance activities (as per FMA's current powers), for example, through setting continuous and periodic reporting requirements for advisers. In accordance with the Regulatory Charter, the FMA would feed their intelligence back to MBIE as relevant to MBIE's regulatory stewardship obligations.
- Information on complaints received about financial advice, including those received by the FMA and by the dispute resolution schemes.
- Ongoing engagement with key stakeholders including advisers, professional associations, dispute resolution schemes, consumer representatives, the Code Committee, and academics.