

Code of Professional Conduct for Financial Advice Services

Submission Template

Submissions close Monday 30 April 2018

Please send submissions to:

code.secretariat@mbie.govt.nz or

Code Working Group
c/o Code Secretariat (Poppy Haynes and Max Lin)
Ministry of Business, Innovation & Employment
PO Box 1473
Wellington 6140
New Zealand

Submissions process

The Code Working Group (CWG) seeks written submissions on the issues raised in this document by **5pm on Monday 30 April 2018**

We welcome submissions on any or all consultation questions. You are welcome to comment only on the issues most relevant to you.

Where possible, please include evidence to support your views, for example references to independent research, facts and figures, or relevant examples.

Please direct any questions that you have in relation to the submissions process to code.secretariat@mbie.govt.nz.

Use of information

The information provided in submissions will be used to inform the CWG's development of the draft Code. We may contact submitters directly if we require clarification of any matters in submissions.

Release of information

The CWG intends to upload PDF copies of submissions received to MBIE's website at www.mbie.govt.nz. The CWG will consider you to have consented to publication of your submission, unless you clearly specify otherwise in your submission.

If your submission contains any information that is confidential or you otherwise wish us not to publish, please:

- indicate this on the front of the submission, with any confidential information clearly marked within the text
- provide a separate version excluding the relevant information for publication on our website.

Submissions remain subject to request under the Official Information Act 1982. Please set out clearly in the cover letter or e-mail accompanying your submission if you have any objection to the release of any information in the submission, and in particular, which parts you consider should be withheld, together with the reasons for withholding the information. The CWG will take such objections into account and will consult with submitters when responding to requests under the Official Information Act 1982.

Private information

The Privacy Act 1993 establishes certain principles with respect to the collection, use and disclosure of information about individuals. Any personal information you supply to the CWG in the course of making a submission will only be used for the purpose of assisting in the development of the draft code. Please clearly indicate in the cover letter or e-mail accompanying your submission if you do not wish your name, or any other personal information, to be included in any summary of submissions that the CWG may publish.

Information about you

Share your details	
i.	<p>Please provide your name and (if relevant) the organisation you represent</p> <p>Melior Law & Regulation</p>
ii.	<p>Please provide your contact details</p> <p>Melior Law & Regulation</p> <p>For the attention of S 9(2)(a), Director</p> <p>S 9(2)(a)</p> <p>S 9(2)(a)</p>
iii.	<p>Please provide any other information about you or your organisation that will help us understand your perspective (e.g. the financial advice situations you have experience with)</p> <p>Melior is a commercial law firm that specialises in financial services regulation.</p>
iv.	<p>Please indicate whether your submission contains any information that is confidential or whether you do not wish your name or any other personal information to be included in a summary of submissions. (See page 2 of this document)</p> <p>No confidential information.</p>

Principles for drafting the Code

Share your views	
A.	<p>What comments do you have regarding the overarching theme of “good advice outcomes” and the underlying principles?</p> <p>We support the overarching theme of “good advice outcomes” and note that the focus on “outcomes” is consistent with international regulatory trends.</p>
B.	<p>Are there any further principles that should be included, or existing principles that should be removed?</p> <p>Principle 2: The Code will be drafted on the assumption that most retail clients have the basic knowledge but not the Financial Advice Provider’s expert understanding.</p> <p>While we support this principle we question whether it goes far enough to produce a client-centric Code. Cognitive psychology and behavioural economics suggest that financial literacy is not the only reason people make poor financial decisions. Focusing on the knowledge of the client may limit the usefulness of the Code. Knowledge is part of the picture, but drivers of behaviour and levels of client engagement are also important.</p>

Ethical behaviour

Act with honesty, fairness and integrity

<i>Share your views</i>	
C.	<p>Do you agree with a requirement to act with honesty, fairness and integrity? If not, please set out your reasoning.</p> <p>Yes.</p>

Keep the commitments you make to your client

D.	<p>Should minimum standards for ethical behaviour for the provision of financial advice extend beyond strict legal obligations, to include meeting less formal understandings, impressions or expectations that do not necessarily amount to strictly legal obligations? If no, please give reasoning. If yes, please propose how a standard for such commitments might be framed.</p> <p>While we support the general principal, we are concerned about the liability implications of extending this proposal to less formal understandings, impressions or expectations that do not necessarily amount to strict legal obligations. The liability provisions of the Financial Markets Conduct Act 2013 as amended by the Financial Services Legislation Amendment Bill (FMCA) are significantly harsher than under the Financial Advisers Act 2008.</p> <p>As you are aware, the FMCA will provide that there is a duty to comply with the standards of ethical behaviour, conduct and client care required by the Code. Where there is a contravention of that duty, the court can make compensation orders, other civil liability orders and order pecuniary penalties of up to \$600,000 in the case of an individual or \$200,000 in any other case. In light of the harsher enforcement regime and the broad principles that will make up the Code, we suggest that consideration is given to working with the FMA to provide guidance on enforcement of the Code. Such guidance could ensure that the spirit of the Code is followed – not a cautious legalistic approach.</p> <p>Commercial entities often do settle disputes where a client has relied on a less formal understanding, impression or expectation. However, to introduce requirements about this into the Code would increase liability, uncertainty and so increase the cost of the complying with the FMCA. That cost would be passed on to all customers – not only those who rely on a less formal understanding, impression or expectation. On that basis our view is that this proposal does not meet the purposes of the FMCA and should not be adopted.</p> <p>If it is decided to include suggestions about best practice, it should be made clear that such suggestions are not enforceable. We note that such best practice statements may expand liability when they are before a court considering negligence claims.</p>
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E.	<p>If there was a minimum standard requiring Financial Advice Providers – or Financial Advice Providers in some situations – to have their own code of ethics in addition to the Code, how would you frame the requirement for it to deal with keeping commitments?</p> <p>We acknowledge that this proposal seeks to engage each Financial Advice Provider in an understanding of what good conduct looks like for their organisation.</p> <p>To impose this as an enforceable requirement would impose great cost across the market. The benefit of that cost would be limited if each Financial Advice Provider produces a written document and did not engage in an attempt to understand its own culture. On that basis we recommend that this is an example of best practice, not a requirement of the Code.</p>
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Manage and fully disclose conflicts of interest

F.	<p>Should the Code include a minimum standard on conflicts of interest in addition to the legislation?</p> <p>This may be appropriate where conflicts of interest are particularly acute, for example, where commission is paid, where advice recommends a replacement product or where advice is provided for a very limited range of products. We support the Code including minimum standards for such circumstances if those standards provided a safe harbour enabling the market to operate efficiently and give good advice outcomes.</p> <p>Because “sales” are effectively unregulated and “advice” is becoming heavily regulated we remain concerned that:</p> <ul style="list-style-type: none"> - There is opportunity for regulatory arbitrage. - Regulation imposes additional costs on responsible market participants who comply with the financial advice regime in order to sell a product. - Customers do not understand the value of financial advice, because they are told they are receiving “financial advice” when a recommendation relates to the sale of a very limited range of products.
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Do no harm to the client or the profession

G.	<p>Do you agree that a person who gives financial advice must not do anything or make an omission that would or would be likely to bring the financial advice profession into disrepute? If not, please set out your reasoning.</p> <p>We question whether it is appropriate to include “harm to the profession” in a Code that is a “service” code. Would it be more appropriate for such a requirement to be imposed by professional organisations rather than by this Code?</p>
H.	<p>Is an additional minimum standard on doing no harm to the client necessary? If so, what standard do you propose?</p> <p>While we support this high level statement in principle, we are concerned as to how it will be enforced. Please see our response to question D for more details.</p>

Keep your client's data confidential

I.	<p>In which situations, if any, should the retention, use or sharing of anonymised bulk customer data be subject to Code standards?</p> <p>It is appropriate for the Code to include a requirement to “Keep your client’s data confidential” provided it is clear that this requirement goes no further than the requirements of New Zealand privacy legislation, or any applicable overseas legislation, such as the European Union General Data Protection Regulation.</p> <p>We do not consider that the Code should impose standards regarding the retention, use or sharing of anonymised bulk customer data, although there may be circumstances where it is appropriate for the CWG to issue non-binding guidance on best practice.</p>
J.	<p>Do you agree that the Code should cover the various aspects of maintaining client confidentiality discussed in this paper?</p> <p>Please see answer in section I above.</p>
K.	<p>Are there other aspects of maintaining client confidentiality to consider?</p> <p>Please see the answer in section I above.</p>

Ethical processes in Financial Advice Provider entities

L.	<p>Do you agree that the Code should require the Financial Advice Provider to document and maintain its “ethical processes”?</p> <p>Is it appropriate to include process requirements in the Code? We note that the Code is to be drafted with a principles-based approach. We suggest that a requirement that the Financial Advice Provider is able to demonstrate ethical processes would be appropriate.</p> <p>We had anticipated that process requirements (such as documenting or maintaining processes) would form part of the licence requirements managed by the FMA, not part of a principles-based code.</p>
M.	<p>Should the Financial Advice Provider be required to have a publicly available corporate code of ethics? Are there particular situations where a corporate code of ethics should be or should not be required?</p> <p>No. No. We are concerned about the cost and effectiveness of these proposals. Please see our earlier comments in response to question E.</p>

N.	<p>Should Financial Advice Providers also be subject to additional standards in respect of leadership and culture? If so, how should these be framed?</p> <p>What guidance does the CWG anticipate it can articulate in addition to the “Guide to the FMA’s view of conduct”? If there are particular standards of leadership and culture that should apply to Financial Advice Providers, would it be more appropriate to include those standards in the FMA guide? Our view is that it would be better to have consistent guidance.</p> <p>More generally, it may be appropriate for New Zealand to engage in consideration of a senior manager regime, if only to articulate why such a regime is not appropriate in this jurisdiction.</p>
O.	<p>Do you propose other additional standards of ethical behaviour that should apply to Financial Advice Providers?</p> <p>No. Further, we are concerned that there is a potential to expand the scope of the regime by imposing requirements which capture the overall operation of the business. It may be appropriate for New Zealand to more actively supervise the sale of financial products and services, but the Code should be focused on financial advice, not sales or other business processes. Our reasons for this are set out in answer to question F above.</p>

Ethics training

P.	<p>Do you agree that Financial Advice Providers should be required to meet standards relating to ethics training? If not, please state your reasoning.</p> <p>Yes. It would seem appropriate that records be kept of that training as part of the FMA licensing process.</p>
Q.	<p>Should ethics training requirements apply to all officers and employees of a Financial Advice Provider, as appropriate to their role and contribution to the process of financial advice provision? If not, please state your reasoning.</p> <p>Yes, but ethics training in isolation would be of little value. Consideration should be given to including details of the action a staff member should take if he or she is concerned about an ethical issue.</p>
R.	<p>Should there be a requirement for ongoing refresher training on ethics?</p> <p>Yes, this is one way that a Financial Advice Provider could demonstrate an ethical culture. We are concerned that this is too prescriptive for the Code and would more appropriately be dealt with by licensing.</p>

Resolving ethical dilemmas

S.	<p>Do you agree that Financial Advice Providers should be required to have in place, and use, a framework for resolving ethical dilemmas that may arise in giving financial advice? If not, please set out your reasoning.</p> <p>We are concerned about the costs implications of creating such a framework and how useful it would be in practice. Is this an area where the CWG can provide guidance or precedents, particularly for small Financial Advice Providers?</p>
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Compliance functions

T.	<p>Should there be a requirement for explicit sign-off on the soundness of financial advice provided directly by a Financial Advice Provider?</p> <p>We consider that further consideration is required of the distinction between financial advice provided by a robo-adviser and financial advice provided through a nominated representative or financial adviser. In most circumstances, civil liability will remain with the Financial Advice Provider. For that reason, we consider that this question should apply to all circumstances where financial advice is provided.</p> <p>Wider consideration is also due because there is no restriction prohibiting financial advisers acting for a number of Financial Advice Providers. Accordingly, to ensure good advice outcomes, there should be a record of which financial advice provider is responsible for the advice.</p> <p>Having widened scope, our view is that in the absence of a senior managers regime, imposing a financial advice provider sign-off process would only impose cost and hinder effective communication of the financial advice to the client.</p>
U.	<p>Do you agree that Financial Advice Providers should be required to have in place a compliance function aimed at following up on concerns raised by employees and other stakeholders? If not, please set out your reasoning.</p> <p>We question whether it could be more appropriate for this to be a market wide function? It can be difficult for an employee to raise concerns internally, see for example https://www.bloomberg.com/news/articles/2018-04-20/barclays-ceo-jes-staley-to-stay-in-job-after-regulatory-probe The existence of outside support, could encourage Financial Advice Providers to develop, resource and publicise an equivalent internal function.</p>
V.	<p>Should this extend further into an internal audit obligation, having in place processes to systematically test for and detect violations of ethical behaviour?</p> <p>Our view is that the role of the CWG is to set the ethical standards and the role of the FMA is to develop licensing requirements for business processes and procedures. Generally, we are concerned about the cost of imposing this requirement on all licence holders, particularly small businesses.</p>

W.	<p>Are there any potential compliance costs for small and/or large Financial Advice Providers that need to be considered?</p> <p>Yes. The costs of imposing these requirements would be significant. In the absence of evidence that such requirements would improve customer advice outcomes, we suggest that this role be carried out by the regulator.</p>
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Responsibility for the whole advice process

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

Y.	<p>What principle or mechanism do you propose the Code could include to reinforce good ethical behaviour on a day-to-day basis?</p> <p>“A principles-based approach does not work with individuals who have no principles.” (Hector Sants, CEO Financial Services Authority, 2009) There will always be rogue individuals who will fail to provide good advice outcomes. Imposing such mechanisms will only be effective in an organisation with an ethical culture.</p> <p>However, we do consider that there could be advantages to requiring the adviser to acknowledge explicitly to the client that the Code applies. Such disclosure could increase customer financial capability as well as reinforcing ethical behaviour within each Financial Advice Provider.</p>
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Conduct and client care

Advice situations

<i>Share your views</i>	
Z.	<p>Are there other delivery methods that should be considered when testing our thinking?</p> <p>The scenarios should include all aspects of communication of advice by an organisation, for example renewal notices, letters and advertisements.</p>

Advice-giving standards

AA.	<p>How do the current client care standards work in practice, especially in advice-giving situations not previously covered by the AFA Code? In answering this question, please ignore “scope of advice” (CS-8) and “suitability” (CS-9 and part of CS-10).</p> <p>We understand that RFAs are not well engaged with the FMCA changes. We recommend that before any new advice process is finalised, it is tested with focus groups of RFAs, particularly those from the general insurance industry.</p>
BB.	<p>Could any aspect of the current client care standards be worded better? (For example, we are aware that the definition of “complaint” could be improved.)</p> <p>No comment.</p>
CC.	<p>Are there any aspects of the current client care standards that could be expanded or clarified (for example, in light of the published findings of the Disciplinary Committee)?</p> <p>Record keeping has been a consistent issue in cases that have appeared before the Disciplinary Committee. It may be more appropriate for detailed record keeping requirements to be dealt with as part of the FMA licensing process.</p>
DD.	<p>Are there any potential compliance costs for small and/or large Financial Advice Providers that need to be considered?</p> <p>No comment.</p>
EE.	<p>Are there any additional matters that should be addressed in the advice-giving standards? Those listed above? Others?</p> <p>No comment.</p>

Advice process

FF.	<p>Do you think there are any other components that should be included in the design considerations of an advice process?</p> <p>No comment.</p>
GG.	<p>Should the Code include guidance material to help determine what needs to be considered when designing an advice process?</p> <p>Yes. It is appropriate for the Code to include guidance material, but it must be clear which aspects of the Code are enforceable.</p>
HH.	<p>Are there any other important aspects you think should be included in the advice process for all types of financial advice activities under the new regime?</p> <p>No comment.</p>
II.	<p>Should any of the key aspects that we have listed above be removed? If so, why?</p> <p>No comment.</p>
JJ.	<p>Are there any situations in which an advice process need not be followed?</p>

	No comment.
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Personalised suitability

KK.	<p>What comments do you have about a proposed minimum standard on personalised suitability analysis? What are your views on the example above?</p> <p>In developing this standard there appears to be a focus on the experience of AFAs under the current regime. The FMCA regime will apply to significant numbers of RFAs who have never been required to comply with the AFA Code. We understand that these RFAs are not engaged with this review. As suggested above, it may be necessary to form focus groups to test new requirements on RFAs.</p>
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Organisational standards

LL.	<p>What are the practical advantages and disadvantages of including organisational standards as described? What explanatory material or examples could we provide in the Code that might help to make these standards easier to comply with in practice?</p> <p>We note that what is proposed is could represent a significant imposition of cost for small Financial Advice Providers.</p> <p>We are concerned that there is a potential to expand the scope of the regime by imposing requirements which capture the overall operation of the business. It may be appropriate for New Zealand to more actively supervise the sale of financial products and services, but the Code should be focused on financial advice, not sales or other business processes. Our reasons for this are set out in answer to question F above.</p>
MM.	<p>Would implementing these organisational conduct and client care standards create a particular compliance burden for your firm? If yes, please explain why.</p> <p>No comment.</p>

General competence, knowledge and skills

<i>Share your views</i>	
NN.	Do you agree with our interpretation of the meaning of “competence, knowledge, and skills”? If not, why not? Yes.
OO.	Are there other factors, which contribute to combined expertise , that we have not listed? We are particularly interested in factors that are relevant to financial advice that is given by a Financial Advice Provider directly, including by digital means. No comment.
PP.	What do you think are the advantages of this approach to general competence, knowledge and skills? No comment.
QQ.	What do you think are the disadvantages of this approach to general competence, knowledge and skills? No comment.
RR.	In what ways do you think this proposed standard contributes to, or detracts from, the legislative purposes (for example ensuring the quality and availability of advice, avoiding unnecessary compliance costs, and promoting innovation and flexibility)? No comment.
SS.	What factors should we consider in determining whether to make the proposed unit standard a renewing obligation? No comment.

Particular competence, knowledge and skills

<i>Share your views</i>	
TT.	What are the advantages and disadvantages of our approach of identifying two types of financial advice? What impact would it have on the type of advice you give and on your compliance costs? No comment.

UU.	<p>How should RFA's experience be recognised?</p> <p>Consideration should be given to judging the ability of RFAs through testing individual's performance at a set of standard scenarios before a couple (notional clients, who are regulators or experienced advisers). This could be coupled with mystery shopping by the regulator during the first year post transition and site visits to inspect record keeping and other processes.</p>
VV.	<p>What do you think are the advantages of this approach to particular competence, knowledge, and skill?</p> <p>No comment.</p>
WW.	<p>What do you think are the disadvantages of this approach to particular competence, knowledge, and skill?</p> <p>No comment.</p>
XX.	<p>In what ways do you think this proposed standard contributes to, or detracts from, the legislative purposes (for example ensuring the quality and availability of advice, avoiding unnecessary compliance costs, and promoting innovation and flexibility)?</p> <p>No comment.</p>
YY.	<p>What alterations, if any, would you suggest to the baselines we have nominated: specialist strand for product capability, Level 5 for discipline capability, and relevant degree (or other degree plus Level 6) for planning capability?</p> <p>No comment.</p>

Other comments

<i>Share your views</i>	
ZZ.	<p>Are there any other comments you would like to make to assist us in developing the Code?</p> <p>Thank you for the opportunity to submit. We look forward to engaging further as the Code develops.</p>