

24 November 2020

Summary of key themes:

Consultation on the proposed standard conditions for financial advice provider full licences and classes of financial advice service

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Executive summary

We would like to thank all submitters for their feedback on our [consultation on the proposed standard conditions for financial advice provider full licences and classes of financial advice service](#). We received 49 written submissions from a wide range of stakeholders including financial advisers, industry bodies, banks, insurers, and law firms. We appreciate the points raised and the effort put into each submission.

This document contains a summary of some key themes raised in those submissions. We have included comments in response to some points raised. For a discussion of the costs and benefits associated with each standard condition, including feedback on associated compliance costs, see the [Regulatory Impact Statement: Standard conditions financial advice provider licences](#). We have also published a collation of the written submissions. This may withhold some information in accordance with the Official Information Act 1982 and Privacy Act 1993.

The key themes are split into the following topics:

1. Standard Condition 1 - Record keeping
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 - b. Privacy laws
 - c. Foreign language records
 - d. Small FAP & large outsource provider
 - e. Scope
 - f. Deadline
2. Standard Condition 2 – Internal complaints process
 - a. General
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9. Licence classes
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10. Overarching
 - a. General
 - b. Retail vs wholesale requirements
 - c. Fair conduct

Key themes

Standard Condition 1 - Record keeping

General

Most submitters supported a standard condition requiring FAPs to keep records.

Privacy laws

Some submitters considered that the requirement to allow the FMA to view client records on request would not be consistent with the Privacy Act.

FMA response: As noted in the [Summary of key themes: Submissions on proposed standard conditions for financial advice provider transitional licences](#), we are satisfied the FMA's access to client records under Standard Condition 1 is consistent with the Privacy Act. Providers should ensure they comply with Privacy Act requirements in relation to their financial advice services, and advise clients that they are required by law under the conditions of their licence to make their records available for inspection by the FMA at all reasonable times and that the FMA may access the client's personal information in the course of that inspection.

Foreign language records

A number of submitters did not agree it was reasonable to require FAPs with records in languages other than English to keep an accurate summary of the record in English as well as have to provide a full translation of that record into English when required by the FMA.

FMA response: We acknowledge the extra burden of requiring a summary to be kept in English, and given that the FMA is able to request a full translation of any records in another language (by an approved FMA translator), we have decided to remove the requirement for an English summary to be kept.

Small FAP & large outsource provider:

Some submitters were concerned that a small FAP may not be able to satisfy the requirements of this condition when outsourcing record keeping to a large outsource provider. This is because the FAP may not have the power to negotiate specific terms in the outsourcing agreement in order to ensure the person keeping records on their behalf complies with this condition and that they can retrieve the records if required.

FMA response: We reiterate that the FAP continues to be responsible for meeting the standard conditions. This means that if a FAP engages another person for record keeping, compliance with the standard condition remains the FAP's responsibility. We note that Standard Condition 4 relates to outsourcing.

Scope

Some submitters commented that the breadth of the record keeping requirements was excessive and that they should be restricted to 'material' financial advice only. Other submitters noted that some clients are unidentifiable,

particularly those with brief digital interactions, and questioned whether they would be captured by this standard condition.

FMA response: We note that the FAP is required to keep a record of regulated financial advice given by the FAP (or on the FAP's behalf) and of how the requirements relating to the provision of financial advice and financial advice services have been met. We consider that the current scope of record keeping is appropriate, and will not be restricting it to 'material' financial advice. In regards to unidentifiable clients, FAPs should not provide regulated financial advice to an unidentifiable client.

Deadline

A number of submitters noted that 10 working days may not be sufficient in every situation. One submitter notes the possibility that multiple, or large, client files may be requested and compliance within 10 working days would not be possible.

FMA response: We acknowledge these concerns and have amended the standard condition to require records within 10 working days or as otherwise agreed by us.

Conclusion of a product

One submitter commented that there could be an issue if, for example, a complaint is received about advice given more than 7 years ago, and the relevant financial advice product is still current.

FMA response: We consider it important that records are kept for 7 years after the conclusion of the life of the financial advice product that the financial advice relates to. We have updated this standard condition accordingly.

Standard Condition 2 – Internal complaints process

General

Most submitters supported a standard condition requiring FAPs to have and maintain an internal complaints process.

Scope

One submitter commented that it did not seem suitable to specifically identify complaints about a failure to provide a service, given there is no obligation on financial service providers to be full service providers. Another said that capturing complaints "relating to your financial service" is too broad and could include complaints regarding circumstances an entity has no control over, such as market fluctuations. Another mentioned that capturing "any action that was taken in relation to that complaint" is too broad and should be narrowed.

FMA response: We have revised the wording in the explanatory note to clarify that the standard condition applies in respect of financial adviser services covered by the FAP licence. We consider that the current scope of the standard condition is appropriate given the broad nature of complaints, and that a record should be kept of every complaint and what action was taken.

No action taken

The standard condition also requires a record in the instance no action is taken in respect of a complaint received, and the reasons for taking no action. One submitter commented that there should never be a case where 'no action' is taken by a FAP when a complaint is received.

FMA response: We acknowledge these concerns and agree that there should never be a situation where nothing is done in response to a complaint made. We expect FAPs to always take a key set of inherent actions (i.e. recording the complaint, investigating and considering the complaint, and responding to the customer) but from there they may choose to take 'no action', by which we mean no formal or remedial action. We note that the reasons for taking this approach must be recorded.

Identifying complaints

One submitter noted they were concerned about advisers accurately identifying complaints, and determining a complaint is resolved when the customer may not agree this is the case.

FMA response: The explanatory note for this standard condition states that a complaint relating to a financial adviser service is "an expression of dissatisfaction made to you or to a person engaged by you, relating to: your financial advice service (including any regulated financial advice given to a retail client by you or on your behalf); or the complaints handling process itself where a response or resolution is explicitly or implicitly expected". This definition is taken from the ISO 10002 definition and should be used by FAPs to identify a complaint. The explanatory note has been updated to clarify that if a complaint cannot be resolved or is in deadlock, the complainant must be informed about taking the matter to the adviser's dispute resolution scheme. This includes when one party does not consider a complaint to be resolved.

Insurance Council of New Zealand Fair Insurance Code

One submitter noted that ICNZ members already have similar requirements around complaints under the Fair Insurance Code.

FMA response: We acknowledge this overlap but note that not every FAP is a member of ICNZ therefore not subject to the ICNZ Fair Insurance Code.

Standard Condition 3 – Regulatory returns

General

Most submitters supported a standard condition requiring FAPs to submit regulatory returns to the FMA.

Regulatory returns consultation

Many submitters commented that they would like to see the regulatory returns consulted on. Some submitted that this should be done as soon as possible to allow for the longest period of adjustment possible.

FMA response: As we have done in the past, we will consult on any proposed regulatory returns for FAPs. We note that regulatory returns will be, in part, based on what we observe during the first year of transitional licensing. Therefore, there will be no regulatory returns required until all FAPs are operating under a full licence (i.e. not until 15 March 2023 at the earliest).

Recommendations

Some submissions made recommendations about when or how the regulatory returns should be collected, or what the regulatory returns should contain.

FMA response: We will take this feedback into account when determining the information required to be provided in a Regulatory Return Framework and Methodology for FAPs. We recognise that many submitters may have feedback they did not submit during this consultation process, and reiterate that we will consult with industry prior to publication of the Regulatory Framework and Methodology that will form part of the standard conditions.

Standard Condition 4 – Outsourcing

General

Most submitters supported a standard condition on outsourcing arrangements.

FMC Act outsourcing condition

Some submitters commented that other market services licences under the Financial Markets Conduct Act 2013 (FMC Act) include an outsourcing condition. It was noted that the outsourcing condition for FAPs appeared to be stricter than those for other FMC licences. Some submitters were concerned that the outsourcing requirements proposed may increase the cost of outsourcing, given the level of oversight required.

FMA response: We acknowledge these comments and agree that, where possible, the standard condition should be aligned with the outsourcing standard condition for other FMC Act market services licences. We have revised the wording of the condition to align it with other market services licence standard conditions.

Small FAP & large outsource provider

Submitters expressed concern that FAPs (particularly smaller FAPs) may not be able to negotiate specific terms with large outsource providers in order to comply with this standard condition as proposed.

FMA response: We have revised the wording in this standard condition so that a FAP must be satisfied that an outsource provider is capable of performing the service to the standard required to enable the FAP to meet its market service licence obligations, as well as having contractual arrangements in place to enable effective monitoring of performance. We reiterate that a FAP remains responsible for meeting its market service licence obligations when engaging an outsource provider.

Standard Condition 4 (outsourcing) and Standard Condition 5 (business continuity and technology systems) overlap

Some submitters noted that the prevalence of outsourcing technology may lead to an overlap between Standard Condition 4 (outsourcing) and Standard Condition 5 (business continuity and technology plan).

FMA response: We acknowledge this concern and have added to the explanatory note to Standard Condition 4 to recognise that outsource arrangements, and business continuity and technology systems are often interrelated.

RBNZ's outsourcing policy

Some submitters noted that, where possible, this condition should be aligned with banks' existing obligations under the RBNZ's outsourcing policy (BS11).

FMA response: We recognise that RBNZ has a robust outsourcing policy appropriate for its remit. However we also note that our remit covers a different market segment, including individuals and a mix of small to large entities, while the RBNZ's policy is targeted at larger entities. We have therefore decided not to align our outsourcing obligations with those of the RBNZ.

Example

Multiple submitters disagreed that the review of compliance processes by a professional services company should be included as an example of outsourcing.

FMA response: We note that there are situations where this may, and may not, be an example of outsourcing. Review of a FAP's processes, initiated by the FAP, would not be an outsourcing arrangement caught under this standard condition. However, a review by a third party of the work done by an adviser, to ensure the adviser meets their obligations, or done as part of the FAP's compliance assessment processes, would be included as an outsourcing arrangement. We note that this example was included in our comments on the standard condition, and therefore no update to the standard condition is required.

Intragroup arrangements

Some submitters asked whether intragroup arrangements were outsourcing.

FMA response: We do not consider intragroup arrangements outsourcing and therefore they are not captured by this standard condition.

Former Standard Condition 5 – Professional indemnity insurance

General

Many submitters agreed that having professional indemnity insurance (PI cover) is an important part of operating a financial adviser business, and some submitters were supportive of including this requirement as a standard condition.

However, many submitters also commented that compliance costs associated with mandating such cover as a standard condition would be high, and in some cases could create a barrier to entry for new businesses or significant additional compliance costs for current businesses.

Some submitters thought that mandating PI cover would be likely to increase premiums. We subsequently discussed this issue with market participants, many of whom operate in both Australia and New Zealand, and they were of the opinion that mandating PI cover would be likely to result in premium increases. We understand there is a risk that mandating PI cover could lead to increased premiums, and that this may make cover unaffordable for some providers. Further, this may also drive up the cost of financial advice, affecting its availability to consumers.

Many submitters were concerned that mandating professional indemnity insurance would not necessarily achieve the level of customer protection desired, and in some cases provide little protection for customers. They noted that the primary purpose of professional indemnity insurance is to protect those providing professional advice, rather than acting as a surety for compensation to their clients or customers. We found no clear picture of exactly what protection professional indemnity insurance provides customers, due to the broad variance in terms and conditions of coverage. We understand these contracts increasingly include a number of carve-outs for certain breaches and types of liability which mean that compensatory payments for customers are excluded in many cases.

We understand that many product providers already require those holding agency or distribution agreements to have access to PI cover. In some other cases, FAPs may already be well placed financially to meet any claims for compensation by clients without recourse to professional indemnity insurance. We note there is a risk that smaller FAPs may not have the ability to meet large liability claims without professional indemnity insurance, which would leave consumers without recourse.

Given the level of compliance costs associated with this condition, the potential for adverse effects on the availability of financial advice services as a result of mandating cover, and that it may not provide customers with the expected protection, we think removing this proposed standard condition is appropriate at this time. We note that some FAPs will already have professional indemnity insurance or the ability to otherwise appropriately compensate customers when necessary. We continue to recommend that FAPs have professional indemnity insurance as an important part of operating a financial adviser business, and for our own internal purposes we will be asking each FAP in the full licensing application process if they have PI cover.

Standard Condition 5 – Business continuity and technology systems

General

Most submitters supported a standard condition requiring FAPs to maintain a Business Continuity Plan (BCP), including ensuring the information security of critical technology systems is maintained.

Non-technology based planning

Some submitters believed that we did not pay sufficient attention to non-technology related BCP issues in the standard condition. It was also suggested that it would be appropriate to split this condition into two standard conditions, one for business continuity and one for technology systems. Other submitters thought the condition was overly burdensome.

Submitters also noted that the term “cybersecurity” is quite restrictive as it only pertains to data kept in a digital form. They felt it would be better to use the term “information security”, which relates to data kept in any form.

FMA response: It is important that FAPs have suitable arrangements in place to ensure they are able to manage disruptions to their business. As part of their BCP, it is important that businesses have a framework in place to ensure the information security of critical technology systems. Therefore, we do not consider it necessary to split the standard condition into two conditions. Further, we consider that any compliance costs associated with having and maintaining an appropriate BCP will be reasonable and necessary, taking into account the risks associated with not having such provisions in place, for both FAP businesses and their customers.

We have updated the condition to refer to “information security” to ensure more than just cybersecurity is captured. We also note that for FAPs holding a Class 1 licence, the arrangements for locums may form an important part of their BCP.

Breaches

Some submitters were concerned that a 5 working day notification requirement may be too short to fully investigate and identify the cause of a breach. One submitter also asked who would be liable if an outsource provider caused the breach.

FMA response: We have extended the notification requirement to 10 working days. FAPs engaging outsource providers must undertake their own due diligence process; and we reiterate that the FAP is ultimately responsible for the advice provided under its licence.

Ensure at all times

Some submitters thought that ensuring the information security of critical technology systems at all times is a high burden and should be removed.

FMA response: We consider the current requirement is appropriate, especially in light of an increasing number of cyberattacks, and the risk to customers if the integrity and security of critical technology systems is not maintained (e.g. compromised security of the information held about them, or about the financial adviser services received, and vulnerability to cyberattacks).

Multiple BCP documents

Some submitters were concerned that the current wording of the standard condition means that a BCP can only be a single document.

FMA response: We note that a BCP can be made up of multiple documents. We have not amended the standard condition, as the current wording allows for this.

Standard Condition 6 – Ongoing requirements

General

Most submitters supported a standard condition requiring FAPs to continue meeting eligibility and other requirements set out in section 396 of the FMC Act, and if applicable, section 400.

Time to rectify

Some submitters noted that FAPs should be given time to rectify any non-compliance before it is considered a breach. Similarly, one submitter noted that the words “at all times” in the condition and paragraph 2 of the explanatory note should be replaced by “at all reasonable times”, allowing reasonable time to rectify any non-compliance.

FMA response: This standard condition confirms that licensing requirements must continue to be satisfied at all times while a FAP holds a licence, not just at the time the licence is issued. It reiterates the importance of maintaining these standards, including any eligibility criteria prescribed, and remaining capable of effectively performing the market service covered by the licence. This standard condition supplements the ongoing requirements set out in section 396 of the FMC Act, and if applicable, section 400, which continue to apply throughout the life of a licence.

Standard Condition 7 – Notification of material changes

General

Most submitters supported a standard condition requiring FAPs to notify the FMA of material changes to the nature of, or manner in which they provide, their financial advice service.

Commencing to implement

Some submitters commented that “commencing to implement” is confusing or too subjective.

FMA response: We have amended the standard condition to require notification within 10 working days of implementing any material change. An example of a material change would include commencing to (where you did not previously, and are permitted to within your relevant licence class):

- engage any financial advisers to provide regulated financial advice on your behalf
- engage any nominated representatives to provide regulated financial advice on your behalf
- in respect of an individual Class 1 licence holder, engage a locum for a period of 3 continual months or longer, to provide regulated financial advice on your behalf
- provide regulated financial advice directly to your clients, for example through automated digital systems.

Notifications

Some submissions noted that as smaller FAPs grow they are likely to implement a number of material changes, which may result in a significant number of notifications for the FMA. Another submitter questioned why such a strict 10-day deadline is enforced when FAPs are already licensed. One submitter suggested a notification should also be triggered when a FAP stops providing a service.

FMA response: We understand there may be multiple notifications at different stages of a FAP’s business growth, but consider it important that we are made aware of any material changes that occur. We think 10 working days is appropriate, especially given the notification requirement only relates to material changes to the nature of, or manner in which a FAP provides, their financial advice service. In the context of implementing a material change, the notification requirement should not be a costly or burdensome exercise. We agree that a FAP ceasing to provide a service is a material change that should be notified to us, and have updated the explanatory note accordingly.

Examples and definitions

Some submitters noted that the examples we provided in the comments section were difficult to understand. One submission suggested that the explanations of “nature of your financial advice” in the explanatory note and comments section are confusing and require clarification.

FMA response: We consider the phrases “nature of your financial advice service” and “manner in which you provide” are clearly defined in the explanatory note and do not require amendment. We have added an additional example in the explanatory note regarding locum arrangements.

Licence classes

General

Most submitters supported the use of licence classes. We do note there was some confusion around the need for classes, and we believe the licensing guide has helped to clarify this.

Class names

Many submitters were unhappy with the naming convention, as it created a sense that A was better than C. However, many of those submitters also noted that they had no issues with the naming if it was not customer-facing. Some submitters suggested Class A should become “single adviser”, Class B should become “multi-adviser”, and Class C should become “comprehensive adviser”.

FMA response: We understand the perceived value in a Class A licence as compared with a Class C licence is derived from conventional grading systems, for example those used in health inspections, where an A grade is the top grade. With this in mind, we have changed the class names from Class A to Class 1, Class B to Class 2, and Class C to Class 3. This naming follows the convention of other licence classes such as vehicle classes in driver licences. We note that although the licence class will be visible on the FSFR, advisers will only be required to tell customers that they have a licence, not which class, unless asked.

Locum

Multiple submitters commented that situations may arise in a single FAP business in which a second adviser would be required to provide cover. This may include situations of extended illness, holidays, winding down of a business, and other situations where the adviser may not be able to service their clients for an extended period of time.

FMA response: We understand that a single adviser business may need to engage a locum in order to provide cover for their business. We have included provision in the Class 1 licence to allow for a locum arrangement. This enables a Class 1 licence holder to appoint a financial adviser as a locum due to a medical or other temporary absence from the business. If a locum arrangement is in place for 3 continuous months or longer, the FMA must be notified (see business continuity requirements in Standard Condition 5 and notification requirements in Standard Condition 7).

Digital advice

Some submitters commented that digital advice did not fit into Class 1 and should be a licence class of its own. Others commented that they were unsure how the FMA's assessment process would work considering a Class 1 FAP not providing digital advice and those providing digital advice are different businesses.

FMA response: We consider the inclusion of digital advice in a Class 1 licence is appropriate, and gives advisers the ability to service a significantly larger number of customers. In terms of licensing, the question set will include specific questions for those wishing to provide digital advice. Furthermore, if a FAP applied for a Class 1 licence without digital advice but later looked to provide digital advice, we would consider this a material change to the nature of its financial advice service and therefore require notification under Standard Condition 7.

Barriers

Some submitters mentioned that the use of licence classes creates a barrier to growth for a business, particularly from a Class 1 licence to a Class 2 licence if adding another adviser.

FMA response: We recognise this possible barrier to growth. However, we consider the differences between a Class 1 and Class 2 licence are significant and therefore warrant a new licence application. We encourage any single advisers that are potentially expanding their business to apply for a Class 2 licence to avoid having to reapply for a licence in the near future.

Overarching themes

General

We note that some submissions apply across many or all of the standard conditions, so we have included this section to summarise these comments.

Retail vs wholesale requirements

Some submitters were concerned that the current wording of the standard conditions indicates that some of them apply to wholesale businesses as well as retail businesses.

FMA response: We reiterate that the standard conditions apply to FAPs providing regulated financial advice to retail clients. In order to clarify this point, we have added a note at the beginning of the standard conditions.

Fair conduct

Some submitters noted that the idea of fair conduct and treating customers fairly should be emphasised more clearly in the standard conditions.

FMA response: We agree that fair conduct is an important principle as it relates back to the FMA's function of creating and maintaining fair, efficient, and transparent markets. As such, we note that anyone giving advice is subject to the [current Code of Professional Conduct](#) and will be subject to the [new Code of Professional Conduct](#) from 15 March 2020. Both Codes contain a standard relating to treating clients fairly.