大成 DENTONS KENSINGTON SWAN

Insights and Commentary from Dentons

The combination of Dentons and Kensington Swan offers our clients access to 10,000+ lawyers in 182 locations and 74 countries around the world.

This document was authored by representatives of Kensington Swan prior to our combination's launch and continues to be offered to provide clients with the information they need to do business in an increasingly complex, interconnected and competitive marketplace.

大成 DENTONS KENSINGTON SWAN

Insights and Commentary from Dentons

The combination of Dentons and Kensington Swan offers our clients access to 10,000+ lawyers in 182 locations and 74 countries around the world.

This document was authored by representatives of Kensington Swan prior to our combination's launch and continues to be offered to provide clients with the information they need to do business in an increasingly complex, interconnected and competitive marketplace.

KensingtonSwan

AKL. 18 Viaduct Harbour Ave
Private Bag 92101
Auckland 1142
New Zealand
DX CP22001
P +64 9 379 4196
F +64 9 309 4276

WLG. 89 The Terrace
PO Box 10246
Wellington 6143
New Zealand
DX SP26517
P +64 4 472 7877
F +64 4 472 2291

8 November 2019

Ministry of Business, Innovation and Employment
Attention: Financial Markets Policy – Building, Resources and Markets

By email: faareview@mbie.govt.nz

Exposure Draft: Financial Markets Conduct (Regulated Financial Advice Disclosure) Amendment Regulations 2019 – Submission of Kensington Swan

This is a submission by Kensington Swan in response to the consultation paper on the draft financial advice disclosure regulations to support the new financial advice regime under the Financial Services Legislation Amendment Act 2019, scheduled to commence on 29 June 2020.

About Kensington Swan

Kensington Swan is one of New Zealand's premier law firms with a legal team comprising over 100 lawyers acting on government, commercial, banking, and financial markets projects from our offices in Wellington and Auckland.

We have extensive experience advising a range of market participants on financial advice issues and market services licensing, including financial product providers, Qualifying Financial Entities, adviser businesses, dealer groups, and associated service providers.

Our submission

Our submission is attached. Overall, we support the objectives of the proposals for the regulation of financial advice outlined at paragraph 14 of the Cabinet Paper submitted by the Office of the Minister of Commerce and Consumer Affairs in February 2019 ('Cabinet Paper'):

- Provide consumers with the key information they need
- Provide consumers with the right information at the right time
- Provide information in a way that is accessible for consumers
- Provide consumers with effective disclosure, regardless of the channel used
- Not impose unnecessary compliance costs on the industry.

However, we are concerned that the detail of the draft regulations produced to achieve those objectives is such that they will not be effective to achieve the above objectives. In particular, they are likely to impose unnecessary compliance costs on the industry and result in complexity for consumers making the disclosure information inaccessible in a number of financial advice scenarios, potentially overwhelming consumers with the extent of the information that must be disclosed to them, leading to a reduction in consumers seeking and being able to obtain financial advice.

There is also likely to be insufficient time available from the time the regulations are finalised to commencement of the regime for market participants to have reasonable opportunity to adjust systems

to accommodate the new requirements, which may impact on the scope of financial advice services providers are able or willing to offer. We believe some form of transitional relief is essential if the policy objectives of the Cabinet Paper and the new regime are to be achieved.

We confirm that this submission does not contain any confidential information that we consider should be withheld.

Further information

We are happy to discuss any aspect of our feedback on the Consultation Paper. Thank you for the opportunity to submit.

Yours faithfully
Kensington Swan

David Ireland
Partner

P: +64 4 498 0840
E: david.ireland@kensingtonswan.com

Alternative contact: **Catriona Grover**
Partner

P: +64 4 498 0816
E: catriona.grover@kensingtonswan.com

Alternative contact: **Nick Beresford**
Associate

P: +64 9 375 1150
E: nick.beresford@kensingtonswan.com

Submission on discussion document: ***Exposure draft: Financial Markets Conduct (Regulated Financial Advice Disclosure) Amendment Regulations 2019***

Your name and organisation

Name	David Ireland and Catriona Grover
Organisation	Kensington Swan

Responses to discussion document questions

1	Will the proposed record-keeping requirement be workable in practice?

We have concerns that the record-keeping requirement will be difficult for some financial advice providers to comply with by the date the Financial Services Legislation Amendment Act ('**FSLAA**') comes into force on 29 June 2020.

A number of larger financial service providers (and particularly those that intend to deliver advice through nominated representatives) are currently facing significant logistical challenges in designing and implementing new IT systems for FSLAA by June 2020. Those IT systems need to be sufficiently robust to discharge the new FSLAA conduct duties, and in particular section 431R.

In many cases, the timeframes of these IT projects has been put under further pressure by the delayed the release of this consultation itself, which was originally due in June this year. Given the degree of importance of disclosure requirements in designing and implementing IT systems, we consider it would be unfair to insist on all of the systems required to support the record-keeping requirement being in place by 29 June 2020.

In our view, extending the implementation or enforcement of the record-keeping requirement for, say, 6 months (to 31 December 2020) would be an appropriate way of recognising the impact of the delayed release of this consultation and subsequent finalisation of the regulations. That would allow financial advice providers a more reasonable period of time to integrate disclosure record-keeping functions into their IT and operational systems.

Given the evidentiary and compliance assurance benefits of doing so, we are confident providers will use all reasonable endeavours to maintain adequate records of disclosures made. However, given the limited time available to ensure compliance will occur, it would be unreasonable to treat failure to observe the new regulatory obligation as a breach of the regulations over an initial transition period. This is of particular importance given that any such breach would constitute a reliability event requiring disclosure, at least as that concept is defined in the draft regulations.

An extension of the deadline for this record-keeping requirement would require some consequential technical amendments to the proposed record-keeping standard condition for transitional FAP licences. Those changes would ensure the application of that standard condition is also extended (as it applies to disclosure records).

2	Do you have any comments on the drafting of the Regulations that will require information to be made publicly available?
	We are very supportive of the concept of rendering key information about a financial provider 'publicly available' on a website maintained by the provider. We see this as one of the most beneficial aspects of the innovations proposed for financial advice disclosure. Our primary reservation with the 'publicly available' stage of disclosure as proposed is that not enough use of the publicly available disclosure has been made by way of enabling initial and additional disclosure obligations to be discharged by way of cross-reference to the publicly available information. In our view, this would be the most effective option available to minimise the risk of consumers being overwhelmed by the extent of the information that needs to be conveyed to them, while still ensuring that the information is available. Clause 4(1)(j) of proposed new schedule 21A requires the publicly available information to include descriptions of conflicts of interest. As per the comments we have made in relation to the definition of conflicts of interest in response to question 9 of the consultation, it is critical that this obligation is restricted to conflicts of interest that might 'materially' influence any advice provided by the financial advice provider or its advisers. One technical observation of the list of publicly available information required to be disclosed is the redundancy involved at clause 4(1)(l) by rendering the requirement to provide an overview of the providers internal complaints process subject to the pre-condition 'if' P has an internal complaints process. Given the standard licence condition proposed for financial advice providers, and the essential role that internal complaints processes perform in dispute resolution arrangements, we see it as an essential requirement that every financial advice provider has some form of internal complaints process. As a result clause 4(1)(l) can simply be stated as a requirement to provide an overview of P's internal complaints process.
3	Do you have any comments on the draft Regulations that will require the disclosure of information when the nature and scope of the advice is known?
	In our view, the 'nature and scope' disclosure contained in Regulation 229D is drafted on the assumption that the delivery of regulated financial advice will take place via a structured interaction between an individual client and an individual adviser. That will not always be the case under FSLAA. Given the flexibility in the method of delivering regulated financial advice under FSLAA (and in particular an express statutory permission of entity-level advice) we consider that the existing 'one-size fits all' approach of draft Regulation 229D may be unworkable in some advice interactions. That is particularly so given financial advice under FSLAA does not need to be provided to an identifiable client, or under the terms of a formal engagement, to meet the definition of 'regulated financial advice'. For example, a brokerage firm may publish research on a particular stock that includes a buy or sell recommendation on their website. That research will constitute 'regulated financial advice' as it is an opinion on acquiring or disposing a financial advice product. However, for the purposes of Regulation 229D(1)(a), it is not possible for the brokerage firm to know the nature

and scope of advice that any particular client is seeking (because it has been published to the world at large).

It is not clear to us if the wording of Regulation 229D (and particularly the opening words 'This regulation applies **if**…') are intended to address this concern. However, we recommend that draft Regulation 229D is amended to make clear that the nature and scope disclosure is not required where regulated financial advice is provided to clients in general without reference to a particular client or a particular client's characteristics (i.e. when provided **other than** to an identifiable client).

That exemption from nature and scope disclosure could be subject to a condition that the provider of the financial advice discloses any material conflicts of interest in giving that advice (such as a holding in the financial product that is the subject of the recommendation).

A further option to help address the above concern would be to render the initial information disclosure requirement as applying when ***either*** the general nature and scope of the advice that a client is seeking is known ***or*** the nature and scope of the advice the provider is able to provide is known. That would provide a more effective framework for entity-level financial advice to be provided, as the provider would be able to front-foot the nature and scope of the advice it is proactively delivering.

As far as the specifics of the proposed initial information concerned:

- We see no benefit in providing a statement to the effect that the information that has been provided will help clients understand what type of advice will be provided (clause 5(1)(g) of proposed new Schedule 21A). For initial disclosure to be effective, it is critical that any extraneous information that does not add to the quality of the information provided, is not prescribed. We see clause 4(1)(g) as falling into that category. However, if flexibility was provided to enable initial disclosure content to be addressed by way of cross-referencing to content included in the publicly available information, we would support the requirement of including a statement to the effect that information that will help clients understand the type of advice the provider will provide is publicly available at the provider's website, with a reference to that site.
- Providers should have the option of including reliability history in their publicly available information, with the option of cross-referring to that publicly available information for details of applicable reliability events, as an alternative to needing to outline them in every initial disclosure. As with our previous recommendation, if providers were to take up that option, their cross-referencing to their publicly available information should include reference to the fact that the publicly available information includes details about the provider that will help clients make an informed decision about whether to seek advice from the provider.
- The requirement to provide information about an individual nominated representative providing advice on behalf of a provider is inappropriate in many contexts and not relevant to the provision of the financial advice, given the extent of the controls that need to be imposed on nominated representatives pursuant to the new section 431R to be introduced by FSLAA. That point could be addressed by deleting the current clause 5(2)(c) and amending the opening line to clause 5(3)(b) by adding what was previously in paragraph (c) as a further condition to when the obligation arises – i.e. the need to provide the advisers name and contact details and a statement that they give advice on behalf of the particular provider will only arise if the adviser is a financial adviser, with the obligations including a statement to that effect.

4	Do you have any comments on the draft Regulations that will require the disclosure of information when the financial advice is given?

We recommend that Regulation 229E(5) be amended to change the reference from 12 months to a slightly longer period of, say, 15 months.

For financial advice providers that carry out an annual client review, the longer period would mean that the 'additional information' disclosure is not required to be repeated at every annual review, if that review does not take place in the exact 12-month anniversary following the last review.

We believe this would enable providers to more efficiently manage their additional disclosure obligations, where appropriate, and reduce the risk of inadvertent non-compliance through a failure to observe the strict 12 month timeframe. This may significantly reduce the extent of repeated disclosures, which is otherwise likely to diminish the effectiveness of the disclosure contemplated. As with our comments in relation to initial information to be disclosed, we strongly recommend that flexibility be provided to enable providers to cross-refer to publicly available information, provided that publicly available information is clearly sign posted in the course of discharging the additional disclosure obligation. In our view, this would be a far more effective way of managing the disclosure obligation, minimising the risk that clients will be overwhelmed by the extent of the information needing to be disclosed.

The risk of overwhelming clients was noted as a key concern expressed in the Cabinet Paper. At the very least, an ability to signpost additional information should be made available for one-off limited advice engagements with nominated representatives, such as those that would typically occur with call centre staff and client facing staff at bank branches, where there is a strong risk that clients will simply be deterred from seeking financial advice if they need to sit through anything more than minimalist disclosure.

We do not believe it is appropriate to include any explanation or additional information about a provider's complaints procedures and dispute resolution process at the additional information stage of disclosure. The Cabinet Paper were very clear in pushing out descriptions of complaint processes to be provided at the fourth stage of the decision process, when a complaint is received. There is a high risk that including any detailed information about complaints processes and dispute resolution arrangements at the additional information stage will undermine trust and confidence in financial advice providers, and result in clients receiving information at a time when it is not relevant to them, contrary to one of the key objectives of the new disclosure regime.

Instead, all that should be disclosed in order to provide clients with trust and confidence in this regard is to note that the provider has an internal complaints process and belongs to a dispute resolution scheme, with further details publicly available.

We see no value in including a statement regarding the fact that the person giving financial advice is bound by particular duties, or in including statutory references to those duties. The duties exist and are applicable, whether or not the client is specifically told about them. However, recognising the decisions outlined in the Cabinet Paper that have been made in this regard, we recommend the requirement to disclose information about 'certain duties' be limited

	to an obligation to state that the financial adviser is required to provide advice in accordance with the requirements of the Code of Professional Conduct for Financial Advice, and is required to prioritise the client's interests in the event of a conflict of interest. Such a statement could be accompanied by a reference to publicly available information where a more comprehensive list of those duties is made available, or to an 'official' list of duties maintained by FMA. Given that the duties will be identical across all providers, there seems no value in requiring each provider to come up with a potentially different set of information in this regard. We do not believe it should be a role of financial advice providers to educate consumers in relation to rights and obligations that apply to all instances of regulated financial advice provided to retail clients.
5	Do you have any comments on the draft Regulations that will require the disclosure of a provider's complaints handling and dispute resolution processes when a complaint is received?
	We query the inclusion of the words '…(if P has one);' in Regulation 229F(1)(a). Every person providing regulated financial advice that requires disclosure will be required to (or the FAP they are operating under will be required to) operate an internal complaints handling process. This is because of the proposed standard conditions for transitional licences, which include a condition requiring the FAP to operate an internal complaints handling process. FAPs would also generally be members of an approved dispute resolution scheme. We therefore suggest the words '…(if P has one);' are deleted. This approach is consistent with our recommendation in relation to disclosure of complaints procedures in response to question 3.
6	Do you have any comments on the draft Regulations that set the manner in which information must be disclosed?
	We consider that Regulation 229G should be amended to permit nature and scope disclosure and additional information disclosure to be made by way of a hyperlink in appropriate circumstances. That approach would be particularly suited to 'general' or non-client specific advice (such as the buy/sell recommendation set out at question 3 above). Enabling disclosure to be provided via a hyperlink in these circumstances (rather than in the actual advice itself) would be more manageable then providing long-form disclosure with the financial advice itself.
7	Are there instances in your business when regulation 229D might apply to someone who is not the one to give advice to the client? Please give examples and provide any comments on how the draft Regulations apply in such scenarios.
	We do not have any comments to make in response to this question.

8	Do you have any further comments on new regulation 229A to 229H of the draft Regulations?
	The proposed framework for the provision of disclosure does not align with a large number of financial advice scenarios where there is a very limited, one-off engagement with an individual providing financial advice on behalf of an organisation, when the transaction in question (such as opening a bank account or taking out a term deposit or insuring a car) is concluded in a matter of minutes, with no ongoing engagement. In those scenarios, the nature and scope of the financial advice that is to be provided is determined at much the same time as the financial advice is given – there is no complexity to the conversation, and all is concluded within a single conversation. To provide greater clarity for financial advice providers as to the flexibility available to them, and ensure efficiency in the discharge of disclosure obligations, it would be helpful if the regulations were to expressly confirm that initial and additional disclosure obligations could be addressed seamlessly in a single stage, without needing to separate out initial from additional information disclosure. Requiring that separation in simple, one-off financial advice engagements is likely to be highly disruptive and potentially confusing for clients, with no corresponding benefit achieved as a consequence.
9	Do you have any further comments on new Schedule 21A in the draft Regulations?
	We are concerned that the definitions of 'conflicts of interest' and 'reliability' in clause 2 of the new Schedule 21A are unduly broad, and may be counterproductive in terms of ensuring that key information is identified by the client. As far as the definition of 'conflict of interest' is concerned, consistent with the Cabinet Paper, it should only be interests that a reasonable client would expect to, or to be likely to, ***'materially'*** influence the advice given that ought to be disclosed. Otherwise, the concept of interests that are likely to merely 'influence' is too broad to be of value. For example, it would be reasonable to expect that every adviser engaged by a provider will want that provider to succeed. Therefore, the advice provided by that adviser is likely to be influenced by that desire, and is something that would need to be disclosed, at least if the definition remains as currently stated. Providing information at that level is of no value to the client, yet would be required, undermining the effectiveness of the disclosures and potentially masking the true conflicts of interest that are more relevant to the provision of advice. The same refinement should be made to the definition of 'commission or other incentive', for similar reasons. 'Reliability events' are very broadly cast at present. The concept of a 'regulatory action' and the range of legislation falling within the definition of 'financial markets legislation', in particular, may result in a reasonably extensive set of disclosures being required for some market participants. This is notwithstanding the fact that the contraventions may have no bearing on the provision or reliability of financial advice, or the regulatory action in question may be technical in nature and ought not reasonably influence a client's assessment as to the reliability of the provider.

A pragmatic way of refining the list of reliability events could be to rephrase the disclosure obligation so as to only capture regulatory actions that a reasonable provider would expect to be likely to materiality influence the decision of a client about whether or not to seek advice from the provider. An alternative would be to only require disclosure of regulatory actions and proceedings that the FMA has required the provider to disclose as a condition of their licence, which would have the benefit of certainty for providers as to what must be disclosed.

In our view, it is not appropriate for the relevant 'person' in respect of whom disclosure of a reliability event is required to extend to nominated representatives. Given the constraints imposed upon such a person by virtue of section 431R to be introduced by FSLAA, the fact that a nominated representative has been discharged from bankruptcy within the past four years ought not to be relevant to the decision-making of the client. Nevertheless, disclosure of that information would materially impact many clients' decision making. It may also result in financial advice providers being reluctant to employ individuals as nominated representatives, if they have been discharged from bankruptcy within the past four years. This seems an undue impediment to discharged bankrupts being able to re-engage in business life, in circumstances where the fact of their past bankruptcy is highly unlikely to be relevant to the advice they provide.

10	What (if any) transitional provisions should be included in the regulations?

As noted earlier in our submission, the extensive delay in finalising the disclosure regulations is likely to prejudice the ability of a number of providers to comply with their new disclosure obligations. The greater the complexity of a provider's business, the greater that challenge will become, especially given the need to ensure that disclosure obligations are discharged on every occasion and full records of every instance of disclosure are maintained.

In order to overcome this practical difficulty, in addition to our earlier recommendations regarding record-keeping relief (see our response to question 1), we recommend that a transition provision be included during which disclosure obligations may be discharged through publicly available information (in similar form to that currently proposed), together with a single, brief up-front disclosure statement to be provided or read out to clients whenever financial advice is provided. This would simply refer them to the provider's publicly available information and contain one or two key pieces of information only from the initial disclosure set.

A number of providers will be able to comply with the disclosure requirements from June 29. As a result, the transitional relief suggested above should be optional, so that providers do not need to develop two separate systems if they do not need the relief. Our suggested form of transitional relief aims at aligning transitional disclosure with what will ultimately be required, but in a more manageable form for a transition period of (say) six months.

Regardless, at the very least providers should be provided with some relief from the need to update and/or replace all existing disclosure information that refers to the Financial Advisers Act regime and concepts. Given the limited time available, it would be unreasonable to expect providers to be in a position to 'flick the switch' on 29 June 2020 to move from a Financial Advisers Act disclosure regime that was in force on 26 June, to a new regime with a different set of terminology and requirements on the 29th.

A further transitional option to consider would be for a ‘no enforcement’ provision to be included, so that providers would have relief from being deemed to be in contravention if they used reasonable endeavours to comply, but were unable to do so. In particular, any breach of disclosure obligations during the transitional period, unless egregious, ought not to be regarded as a ‘reliability event’.