

**CODE COMMITTEE'S RESPONSE TO SUBMISSION POINTS RAISED ON THE REVIEW OF THE EXPOSURE DRAFT OF THE
CODE OF PROFESSIONAL CONDUCT FOR AUTHORISED FINANCIAL ADVISERS RELEASED ON 3 OCTOBER 2013**

4 December 2013

The table in this paper summarises the submissions made on the exposure draft of the Code of Professional Conduct for Authorised Financial Advisers (Code) released on 3 October 2013 (the Exposure Draft) and the Code Committee's response to these issues.

In total nine submissions were received on the Exposure Draft in various forms. Comments and feedback on the Exposure Draft were also received by direct email correspondence and discussion with the Code Committee. The Code Committee has considered all such correspondence and submissions and its response to the main issues raised is set out in the following table.

The overarching purpose of the Financial Advisers Act 2008 is to (i) promote the sound and efficient delivery of financial adviser and broking services; and (ii) encourage public confidence in the professionalism and integrity of financial advisers and brokers. The Code Committee has reviewed each Code Standard as expressed in the Exposure Draft against these overarching principles, in light of the feedback received, in finalising the draft of the new Code to be submitted to the Financial Markets Authority for approval.

CODE OF PROFESSIONAL CONDUCT FOR AUTHORISED FINANCIAL ADVISERS

Table summarising issues identified in submissions received in respect of the Exposure Draft released by the Committee on 3 October 2013 and the Committee's responses to those issues.

Issue raised	Response
Background and Introduction	
No issues were raised on the background and introductory sections in the Exposure Draft.	
Ethical Behaviour Standards	
Code Standard 1 – 4	
<p>A drafting point was identified by the Code Committee in reviewing CS 1, in that limiting the stated practical application of the client first principle to CS 1 was no longer appropriate given the emphasis placed on CS 1 always applying. It was also identified that the Code Standard comprises two obligations – client first and acting with integrity – requiring a semantic adjustment.</p>	<p>CS 1 adjusted to refer to 'These obligations' being paramount. Explanatory text clarified to confirm that what is required to place a client's interests first is relevant to the overall Code, not just CS 1.</p>
No other issues were identified for CSs 1 to 4 in the Exposure Draft.	
Code Standard 5 - Proposed new conflicts of interest Code Standard	
<p>Concern was raised with the inclusion of the following provision into CS5:</p> <p><i>Where a conflict of interest is such that an AFA is unable to place the interests of the client first, the AFA must decline to act</i></p>	<p>The Committee's intended focus of this aspect of the explanatory text was on situations where the AFA might be under an obligation to prefer their own interests over those of the client. In view of the concern raised, the obligation in this sentence has been refined. It now</p>

Issue raised	Response
<p>The concern raised was that this could make it impossible for an AFA to act where the supply of a product is restricted, on the basis that not all clients may be able to be offered the product, and the Code Standard could be interpreted as categorising this as a conflict necessitating the AFA declining to act. The absolute and blanket nature of the prohibition on acting was considered to be potentially contrary to client interests, and inconsistent with Code Standard 1.</p>	<p>reads:</p> <p><i>Where a conflict of interest that arises when providing a financial adviser service is such that an AFA is unable to manage the conflict so as to place the interests of the client ahead of the interests of the AFA or a related person, the AFA must decline to act.</i></p> <p>The prohibition on acting is now clearly limited to situations where the AFA has no options available to enable the AFA to place the interests of the client ahead of their own interests or those of a related person. The expectation of the Code Committee is that in many instances, obtaining the fully informed consent of the client to the AFA continuing to act in conflict situations will be sufficient to demonstrate the client's interests are being placed first, provided Code Standard 1 is observed.</p> <p>It follows that where a conflict of interest arises which does not concern the AFA or a related party of the AFA, such as a conflict arising between clients, then the conflict falls outside the final sentence of the explanatory text in Code Standard 5. In such a scenario the conflict must still be <i>effectively managed</i> and Code Standard 1 must be observed.</p>

Concern was raised that withdrawing a service from a client may in some instances result in an outcome that is more adverse to the client than if the AFA were to proceed with the relationship, in circumstances where the AFA may have difficulties placing the interests of the client first.

The amendment to CS5, together with the further amendment to the explanatory text under CS1, balances out this concern. The provision in CS1 requires an assessment to be undertaken as to what is reasonable in the circumstances in order to determine what is required to place the interests of the client first. Obtaining a client's fully informed consent is one option for demonstrating that the client's interests are still being placed first, notwithstanding the conflict.

Issue raised	Response
Client Care Standards	
Code Standard 6 – Clarification of 6 (c)	
<p>A submission was made that the words <i>assessed or reviewed</i> in subparagraph (c) should be replaced with the word “analysed”. ‘Review’ was considered to be insufficiently robust.</p>	<p>Use of the term ‘analysed’ has proven to be problematic, with unintended consequences. The committee remains of the view that the new wording gives more clarity, there being times where technical analysis is not required. The requirement for the AFA to have a reasonable basis for any recommendation made provides guidance as to the extent of the assessment or review required, and ensures the obligation is set at an appropriate level.</p>
Code Standard 7	
<p>A number of submissions considered that the inclusion of the words <i>the basis on which those services are provided</i> into CS7 was unclear, and sought either removal of the words or additional guidance as to what was intended to be covered.</p>	<p>The Committee’s view is that sufficient guidance is provided by the re-worded Code Standard itself. The phrase ‘<i>basis on which those services are provided</i>’ should be interpreted in light of what is required for clients to make an informed decision. By way of example, this would usually include the terms and conditions applying to the service, a description of the systems the AFA has in place to ensure the service is provided appropriately, and identification of the key people involved in formulating any financial advice forming part of the service.</p> <p>The operative provision stating that the CS may be satisfied in whole or in part by complying with the AFA’s disclosure obligations under the Financial Advisers Act 2008 confirms that information required to be disclosed elsewhere need not be replicated.</p>
Code Standard 8 – Suitability of personalised services	
<p>Concerns were identified in respect of the new opt-out relief requirement under subparagraph (b). As initially drafted, this would have required an AFA to write to a client every time a transaction has been completed or advised upon without determining the suitability of the instruction. It was noted that this could be unduly onerous, particularly if multiple</p>	<p>The Committee acknowledges that with multiple instructions within a short timeframe, providing written confirmation in respect of each such transaction could be onerous on the AFA and difficult in practice to achieve. Addressing this issue, the Committee has replaced the words <i>provides written confirmation</i> with <i>expressly confirms</i>, allowing verbal confirmations to</p>

Issue raised	Response
<p>instructions falling within sub-paragraph (b) are received within a short timeframe.</p>	<p>be given at the time the client opts out of a full suitability analysis. The Committee considers this to be a practical approach to addressing the concerns raised, while still maintaining the onus on the AFA to ensure that confirmation is provided to the client. In the context of CS6's requirement to communicate clearly, concisely and effectively with clients, written confirmation, whether by a contract note or other timely written record summarising the transaction, will provide an AFA with best evidence of having discharged the relevant obligations.</p>
<p>A concern was identified with the term <i>transactional advice</i> being included within subparagraph (b) on the basis that the purpose of this provision is to provide the AFA with relief from having to undertake suitability where the AFA has been expressly relieved by the client from these obligations. This means the service may not even involve 'advice', but constitute an execution-only service.</p>	<p>As <i>transactional advice</i> is a defined term, and its only relevance is to assist with describing circumstances where the AFA is relieved from determining suitability of personalised financial advice provided to a client, the Committee considers the term is appropriate within the context of the provision. If the service is genuinely execution-only or non-personalised, CS 8 will not apply in the first place, so the relief mechanism will not come into play.</p>
<p>A comment was made that the transactions the defined term <i>transactional advice</i> applies to may be too broad. It was noted that this concern could be removed by further refinement of the term <i>transactional advice</i>. A further concern raised was that the term did not contemplate multiple transactions.</p>	<p>The Committee has amended the definition of <i>transactional advice</i> in Part 2 of the Definitions Schedule to exclude financial advice regarding a DIMS facility. The restriction of the term to single transactions was deliberate, with the relief mechanism not intended to operate on a blanket basis for multiple transactions. However, it can still be applied to each transaction within a set of multiple transactions.</p>
<p>Code Standard 9 – Clarifying the extent of explanation</p>	
<p>Several submissions identified that it would be helpful if CS9 provided an additional explanation or guidance concerning what is required to comply with the explanation set out at sub-paragraph (b). Particular concerns were expressed regarding the need to outline principal benefits and principal risks in writing, with the term 'outline' suggesting a lot of detail was required.</p>	<p>The Committee has amended sub-paragraph (b) to now refer to <i>a concise description of the principal benefits and principal risks relevant to any financial advice</i>. It considers that this amendment better captures the intent of what is expected under this provision, without being overly prescriptive. The need to be concise clarifies the extent to which benefits and risks need to be described. Whilst the default option remains for explanations to be in writing,</p>

Issue raised	Response
	an appropriate level of relief from providing the written explanation contemplated is available.
Two submitters queried if the Committee had considered merging CS9 into Code Standards 7 and 8 given the combined protections afforded under these Code Standards.	Each of Code Standards 7, 8, and 9 now cover distinct aspects of delivering financial adviser services. The clarity this provides AFAs in terms of identifying the relevant Code Standard to consider in any situation is seen as a useful improvement on the first version of the Code. The Committee feels that the added clarity provided would be compromised if Code Standards were to be merged.
Code Standards 10 – 11	
No issues were raised in respect of CS10 or 11 in the Exposure Draft	
Code Standard 12	
Clarification was sought as to whether it would be acceptable to attach certain information, such as research reports which support a recommendation to a client, to be held in a central data depository rather than having to be physically attached to the client file, albeit the client file would reference the report.	The Committee considers that this would be a practical approach where it is logistically difficult to attach the record or document itself to a client file. No change to Code Standard 12 was considered necessary to provide for this.
Code Standard 13 - 15	
No issues were raised in respect of CSs 13 to 15 in the Exposure Draft.	
Code Standard 16 – Changes to qualifications framework and eligibility sunset	
Concern was raised that sub-paragraph (a) of CS16 allows an adviser to become an AFA without having attained Unit Standard Set C.	Sub-paragraph (a) has not been changed from the first version of the Code. Its practical effect is that prospective AFAs who only operate in the class or wholesale space can satisfy Code competency requirements and become authorised (voluntarily) through only attaining Unit Standards Sets A and B. This is a deliberate exception. Consumer protection consistent with

Issue raised	Response
<p>Concern was raised that the current wording of sub-paragraph (d) does not make it clear that an AFA who has qualified through an alternative pathway, who decides to take a year off from providing advisory services, is able to maintain their authorisation status even if not providing financial adviser services during that period.</p>	<p>the scheme of the Act is already provided by CS14 in respect of class and wholesale services.</p> <p>The Committee considers that it is sufficiently clear that the situation identified in the submission would be accommodated for under CS16 as drafted in the Exposure Draft. The Code does not preclude authorisation being retained through a period of inactivity. However, to be able to continue to rely upon alternative designations, it was considered that maintaining authorisation and fulfilling CPD obligations was essential in order to maintain the integrity of the Code.</p>
<p>In respect of sub-paragraph (c), a submission suggested that the Committee consider lobbying for a legislative change to carve out Kiwisaver withdrawals for the purpose of first home purchase from the scope of personalised financial adviser services requiring AFA involvement.</p>	<p>The Committee’s functions are prescribed under section 82 of the Financial Advisers Act 2008. These functions are specific to the Code and to its review from time to time. It would therefore be outside of the Committee’s functions to lobby for legislative change as suggested. The relief proposed is as far as the Code can go. This suggestion has been referred to MBIE to consider.</p>
<p>During the period from 1 January 2014 until the revised Code comes into effect, applicants for AFA status will be unable to use alternative qualifications and designations expressed in the current version of the Code as being subject to the eligibility sunset, even if those alternatives are now being recognised in the new Code.</p>	<p>The Committee notes that the eligibility sunset in respect of this recognition of alternative qualifications and designations has been in the public domain for some time. It is acknowledged that, for the period that the new revised code is not in effect, the recognition granted under the current version of the Code will not be available. Any applicants for AFA status during this period who would otherwise be able to rely on competence alternatives provided for in the new Code, will therefore have to delay their application for authorisation as an AFA until the new Code comes into effect.</p>
<p>Continuing Professional Training Standards</p>	
<p>Code Standard 17</p>	
<p>A comment was made on the proposed new provision under CS17 sub-paragraph (d) that unless an AFA has actually sat, and therefore experienced, the qualification requirement</p>	<p>The Committee has amended sub-paragraph (d) so that it now states:</p>

Issue raised	Response
<p>provided for under CS16, then the AFA will not know whether the level of competence, knowledge and skills acquired is of a comparable level to the AFA's.</p>	<p>..., with a view to identifying any gaps in the AFA's competence, knowledge, and skills when compared with that level.</p> <p>Identifying gaps is considered to be a better balanced test for AFAs to consider when devising their professional development plans.</p>
<p>Code Standard 18</p>	
<p>A submission questioned how 30 hours over two years for the structured CDP requirements under this Code Standard had been arrived at by the Committee.</p>	<p>The Committee is comfortable with where it has landed in respect of the quantity of CPD required by AFAs over a rolling two year period. The majority of feedback received on this point has been supportive of the position. Whilst the current minimum is 10 hours per year of structured training, given the more flexible definition a higher minimum threshold was considered appropriate. The minimum commitment of an average of one and a quarter hours per month is seen as the absolute minimum.</p>
<p>A submitter identified a concern that the current CPD requirements impose too much subjective criteria, relying too much on self-responsibility at the exclusion of system moderation. The submission therefore recommended keeping the objective supply side criterion in terms of those who can provide training.</p>	<p>The Committee has retained the proposed wording from the Exposure Draft as it does not want to be overly prescriptive on who may provide training. It considers that the criteria for trainers identified within the definition of <i>structured professional development</i>, provides sufficient rigour.</p>
<p>A query was raised as to whether an 'all purpose' AFA needed to undertake 60 hours of structured CPD, given that a specialist risk adviser would need to do 30, and a specialist investment adviser 30.</p>	<p>30 hours of structured professional development every two years is not a target. It is a minimum requirement, irrespective of the range of financial adviser services required. The greater the range of services, the greater the likelihood that 30 hours will be insufficient for the AFA to continue to satisfy Code Standard 14.</p>
<p>A submission sought clarity on whether online training would fall within the definition of structured professional development.</p>	<p>The Committee considers that the definition of structured professional development is clear. Provided the online training meets the criteria set out in the definition, then it would qualify towards the 30 hours of structured professional development required under CS18.</p>

Issue raised	Response
<p>One submitter commented that he supported the exclusion of training provided for the principal purpose of promoting a financial product from the concept of structured professional development.</p>	<p>The Committee agrees, noting that it is only where the principal purpose criterion is met that the exclusion will apply. Promotional training may be useful to an AFA to help understand the products they are advising on, but should not count as 'structured'.</p>
<p>Several submissions sought clarification over what <i>structured professional development</i> included, and what the verifiable aspect of the definition would entail.</p>	<p>The structured professional development being <i>verifiable</i>, is connected to the AFA's attendance at the training, with participation in the training needing to be verified through documentation. The Committee has clarified this position by inserting the word <i>participation</i> into the definition. All that is envisaged is some form of third party verification of the AFA's attendance.</p>
<p>Definitions Schedule</p>	

Other changes

LIST OF SUBMITTERS

Submissions and feedback on the Exposure Draft were received by the Committee via email correspondence and by way of formal submission from the following entities:

<p>Craigs Investment Partners Limited</p>	<p>Securities Industry Association</p>
<p>Institute of Financial Advisers</p>	<p>SIFA Inc</p>
<p>Katrina Hawker, AFA, Accordia</p>	<p>Simon Hassan, AFA</p>
<p>Kevin Bracken, Manager Southern Region, Finsia</p>	<p>Strategi Institute</p>
<p>Patrick Jackson</p>	<p>Tim Williams, Partner, Chapman Tripp</p>