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### **Proposed exemption to facilitate personalised robo-advice – Code Committee Submission**

- 1 This submission is made on behalf of the Code Committee established under the Financial Advisers Act 2008 ('**FAA**') to develop and maintain a code of professional conduct for authorised financial advisers ('**Code**').

#### **Background – the FAA and the Code**

- 2 The statutory framework under the FAA includes a requirement that personalised services in respect of Category 1 Products and Investment Planning Services can only be provided by an Authorised Financial Adviser ('**AFA**'). AFAs are required to comply with the Code, which provides for minimum standards of competence, knowledge, and skills, of ethical behaviour, and of client care. The Code also provides for continuing professional training for AFAs, including specifying requirements that an AFA must meet for the purpose of continuing professional training. The Code is a key mechanism for achieving the overarching purpose of the FAA to 'promote the sound and efficient delivery of financial adviser and broking services, and to encourage public confidence in the professionalism and integrity of financial advisers and brokers'.

#### **Principal submission**

- 3 Given its statutory functions, the Code Committee does not consider it appropriate to express a view as to the merits or otherwise of the Financial Markets Authority ('**FMA**') granting an exemption to permit the provision of personalised robo-advice services as described in its *Consultation Paper: Proposed Exemption to Facilitate Personalised Robo-advice* ('**Consultation Paper**'). Nor do we consider it appropriate for us to express a view as to the FMA's power to grant such an exemption. Rather, the Code Committee's position is that if an exemption is to be granted to facilitate personalised robo-advice then the terms on which any such exemption is granted must be consistent with the terms on which AFAs must operate and the purposes of the FAA consistent with the objectives of the exemption stated at page 13 of the Consultation Paper. This means exemption conditions must ensure that:
  - any personalised service provided through a robo-advice platform is subject to no less a set of minimum standards than would apply to an AFA providing a similar service;
  - permitting robo-advice is consistent with promoting the sound and efficient delivery of financial adviser services; and

- public confidence in the professionalism and integrity of personalised robo-advice services and their providers is encouraged.
- 4 In our view, the above requirements are an absolute minimum. In granting an exemption to facilitate personalised robo-advice, the FMA must be confident that the level of consumer protection involved is no less than that which would be involved had the personalised service been provided by AFA. As a consequence, as level a playing field as is possible is created for the mode of delivery of personalised services. Our primary concern is to ensure that the integrity and effectiveness of the Code is not undermined through the grant of the exemption contemplated in the Consultation Paper.

### **Principles and considerations underpinning an exemption**

- 5 The Code Committee is conscious that a number of overseas jurisdictions have already established regulatory frameworks for the delivery of personalised robo-advice. The Consultation Paper does not provide any evidence that the FMA has taken any learnings from the experiences of those overseas jurisdictions into account in formulating its thinking. Given the likelihood that many of the personalised robo-advice platforms that will be made available to the New Zealand public are likely to comprise New Zealand applications of overseas platforms, we believe it would be helpful for the FMA to document its observations of those overseas experiences. In particular, if the exemption contemplated is to be granted, we believe it would assist public confidence in the outcome if the FMA were to document the consumer protections mechanisms it had considered from overseas jurisdictions, and their perceived effectiveness, and how they translate to the New Zealand regulatory environment.
- 6 The consultation discusses possible limits that might be imposed on the provision of personalised robo-advice if an exemption is to be granted. The limits discussed include limits on the possible scope of any personalised robo-advice service that might be permitted, and financial limits. The Code Committee believes this is an inappropriate approach to take in the granting of any exemption. Either the provision of personalised robo-advice is consistent with the purposes of the FAA and is able to be delivered subject to the same minimum standards as apply under the Code, or it is not. In particular:
- a Limiting the scope of a robo-advice service in the manner proposed at pages 7 and 8 of the Consultation Paper is an approach we have not observed in any overseas jurisdiction that currently provides for the regulation of robo-advice.
  - b The only limits placed on AFAs in providing personalised services are those driven by the AFA's competency and abilities, as provided by the Code. A similar approach should apply to personalised robo-advice.
  - c The proposal that the exemption 'would be limited to personalised robo-advice on products which are easy to exit' is hard to reconcile with a product list that includes KiwiSaver and credit contracts. Even if limits on the possible scope of a robo-advice service were to be imposed, we believe that basing the filter mechanism on such a concept is ill-conceived.
  - d Imposing limits on the scope of permitted robo-advice services is likely to undermine the efficacy of those services. In particular, by limiting the products on which personalised robo-advice services might be provided, it seems unlikely that robo-advice could ever be seen as a suitable option for the provision of investment planning services. Imposing any of the limits discussed would result in consumers accessing a more limited range of

outcomes through robo-advice than would be the access if receiving services from an AFA, which would be a negative regulatory outcome.

- e Placing any financial limit on either the value of a product or on the aggregate investments that might be advised on through a robo-advice service, would discourage investment in the system necessary to deliver robo-advice services. Imposing such limits is likely to compromise the ability of a robo-advice service to reliably deliver suitable outcomes on a standalone basis, requiring human advisers (or self-help solutions) to plug the gaps, undermining the objectives of the exemption.
- 7 The Consultation Paper includes as an exemption objective the delivery of personalised robo-advice in a manner consistent with the principles of the Code and other requirements for AFAs. We agree with this objective. Page 13 of the Consultation Paper goes on to express a need to strike an appropriate balance between protecting consumers and 'promoting innovation'. The Committee believes the focus should instead be on promoting innovation that improves consumer access to personalised services, without compromising the level of assurance provided by the Code.

### **Response to specific consultation questions – Conduct and Code Mapping**

- 8 Attached is an appendix setting out the Committee's views as to the applicability of each of the Code Standards to the provision of personalised robo-advice, responding to the equivalent commentary provided by the FMA in the Appendix to the Consultation Paper. This is directed at Question 22 of the Consultation Paper, incorporating some of the themes discussed above.
- 9 Question 23 of the Consultation Paper asks if the exemption conditions should be applied in a manner that is proportionate to the size and scale of the robo-advice service offered. Provided the conditions are expressed on a principled basis, consistent with the Code, the Committee does not see any benefit in incorporating such a prescribed approach in the conditions. Doing so would inevitably constrain the flexibility that would otherwise be available for robo-advice providers to demonstrate that they have placed the interests of the client first and otherwise acted in a manner consistent with the Code, and in turn would constrain the basis on which the FMA might monitor robo-advice services, increasing the risk of a black letter law approach being taken to satisfying exemption conditions.
- 10 Question 24 asks if there are any other limits or conditions we think would be appropriate to put in place. The Committee's view is that imposing an equivalent requirement to the Adviser Business Statement ('ABS') requirement that is imposed on AFAs would be an appropriate approach to take. Not only would this place personalised robo-advice providers on a more equal footing with AFAs, it would provide a useful tool for the FMA to monitor and test the systems that have been put in place, and assist the FMA to hold robo-advice providers accountable for the services they provide.
- 11 Qualifying Financial Entities who move into the personalised robo-advice space will automatically be subject to the requirement to reflect their robo-advice services within their QFE ABS. For the sake of consistency, we do not believe it would be appropriate for the exemption conditions to leave a gap for non-QFE robo-advice providers. Among other things, this would ensure that FMA is able to take a similar approach with such providers as is taken under the QFE regime for vetting, monitoring, and surveillance of qualifying financial entities, with the processes applied there providing a useful benchmark. As a consequence, we disagree with the comment made in the Appendix to the Consultation Paper that the requirement to have and

maintain an ABS is not directly applicable to a robo-advice service. In the Code Committee's view it is absolutely applicable – it just needs to be in a slightly different form.

- 12 Question 25 asks if an information sheet explaining the exemption and providing guidance on how to comply would be helpful. In our view, assuming a relatively principled approach is taken to the formulation of the conditions, the provision of such guidance will be essential, providing transparency as to the FMA's expectations and approach. This will not only promote confident participation by the personalised robo-advice service providers in improving access to personalised financial advice, it should also provide confidence to AFAs and other financial advice sector participants – as well as consumers – as to the robustness of the approach taken.
- 13 As for question 26, the Committee supports the publishing of a list of providers relying on the exemption on the FMA's website. A list of AFAs is maintained on FMA's website. We see no reason why a list of those relying on the exemption should not also be provided, ensuring consistency and transparency.

### **Conclusion**

- 14 Thank you for the opportunity to contribute to the informed development of the conditions that will underpin the exemption, if granted. We would be happy to meet with representatives of the FMA to discuss any of the issues we have raised, and test the eventual conditions that are developed against the Code Standards in due course.

Yours faithfully



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## Appendix A Mapping of exemption conditions to Code Standards

Code Standard	Code Committee's views on incorporating as an exemption condition
<p>1 - An Authorised Financial Adviser must place the interests of the client first, and must act with integrity. These obligations are paramount.</p>	<p>Requiring personalised robo-advice services to place the interests of the client first is essential. We disagree with the FMA's comment that requiring personalised robo-advice to be provided with integrity is not directly applicable. The concept of acting with integrity is at the heart of the Code, and should be incorporated as part of the conditions. In practice, we believe that evidence of complying with such a condition would be evidenced in the negative, with helpful guidance provided in the recent decision of the Financial Advisers Disciplinary Committee decision 2016 FADC 006.</p>
<p>2 - An Authorised Financial Adviser must not do anything or make an omission that would or would be likely to bring the financial advisory industry into disrepute.</p>	<p>We support the FMA's proposal to include this requirement in the exemption conditions. We could not envisage any circumstances in which it would not be appropriate to apply such a condition.</p>
<p>3 - An Authorised Financial Adviser must not state or imply that the Authorised Financial Adviser is independent, or that any financial adviser services provided are independent, if a reasonable person in the position of a client would consider that the Authorised Financial Adviser or the services provided are not independent.</p>	<p>We do not believe that Code Standard 3 is adequately addressed in the proposed disclosure condition. The constraint on AFAs from stating or implying that they are independent or that their financial adviser services are independent, when this is not the case, is absolute. We see no reason to place a lesser standard on providers of personalised robo-advice services.</p>
<p>4 - An Authorised Financial Adviser must not borrow from or lend to a retail client.</p>	<p>We agree that it would not be appropriate to impose this condition on providers of personalised robo-advice services.</p>
<p>5 - An Authorised Financial Adviser must effectively manage any conflicts of interest that may arise when providing a financial adviser service.</p>	<p>We disagree with the comment that the principle is reflected in the proposed disclosure condition. The Code Standard of effective management of conflicts of interest goes beyond merely disclosing conflicts, which is simply the minimum that must be done. We see no reason why a personalised robo-advice service provider should not be required to incorporate mechanisms within their services to manage any conflicts of interest that might arise, and believe they should be placed on an identical footing with AFAs in this regard.</p>

<p>6 - An Authorised Financial Adviser must behave professionally in all dealings with a client, and communicate clearly, concisely and effectively.</p>	<p>While we accept that imposing the high level Code Standard obligation to behave professionally might not seem directly applicable to a robo-advice service, we see no reason why a condition could not be imposed along the lines of requiring a personalised robo-advice service provider to act consistently with the requirements of Code Standard 6. In particular, we believe it would be appropriate to include a condition that requires any recommendation made in relation to financial products to have been assessed or reviewed by the provider to a level that provides a reasonable basis for any such recommendation. The recent 2016 FADC 006 decision provides a good illustration of the application of such a condition in practice.</p>
<p>7 - An Authorised Financial Adviser must ensure each retail client has sufficient information to enable the client to make an informed decision about whether to use the Authorised Financial Adviser's financial adviser services.</p>	<p>We agree that this Code Standard appears to have been adequately picked up in the proposed disclosure condition, and submit that the eventual wording of the condition should mirror Code Standard 7 as far as possible to ensure that consumers are able to base financial product decisions on at least the same quality of information when using a robo-advice service as they would have done had they used the services of an AFA.</p>
<p>8 - When providing a financial adviser service to a retail client, an Authorised Financial Adviser must agree with the client the nature and scope of the service to be provided.</p>	<p>We support the proposed condition for robo-advice service providers requiring to disclose the nature and scope of the robo-advice service provided, including any limitations. Clear disclosure of those limitations will be a key condition to cover off. We agree with the approach taken to not require active confirmation from a client that they agree to receiving advice through the robo-advice service on the basis described. We are comfortable that the mere act of engagement with a robo-advice service can be treated as agreement without requiring anything further.</p>
<p>9 - When providing a personalised service to a retail client an Authorised Financial Adviser must take reasonable steps to ensure that the personalised service is suitable for the client, having regard to the agreed nature and scope of the personalised service provided.</p>	<p>We agree with the proposed conduct condition for robo-advice service providers to take reasonable steps to ensure that the advice given is suitable for the client, having regard to the nature and scope of the robo-advice service provided.</p>
<p>10 - Where an Authorised Financial Adviser provides a personalised service to a retail client</p>	<p>While we agree that the principle underpinning Code Standard 10 is largely addressed through</p>

<p>that is an investment planning service or that relates to a category 1 product, the Authorised Financial Adviser must provide an explanation of the service provided that is sufficient to enable the client to make an informed decision about the financial adviser service.</p>	<p>the proposed disclosure condition for providers to ensure clients are given sufficient information so as to be able to make an informed decision, we believe it would be helpful to expressly require providers to give clients a clear explanation of how the digital tool works.</p>
<p>11 - An Authorised Financial Adviser must ensure there is an appropriate internal process in place for resolving client complaints in relation to the Authorised Financial Adviser's financial adviser services.</p>	<p>We agree with the proposed complaints condition outlined in the consultation paper.</p>
<p>12 - An Authorised Financial Adviser must record in writing adequate information about any personalised services provided to a retail client.</p>	<p>We agree with the proposed record keeping requirement condition outlined in the consultation paper.</p>
<p>13 - An Authorised Financial Adviser must ensure that records of all information and documents required under this Code are kept for a minimum of 7 years.</p>	<p>We agree with the proposed record keeping requirement condition outlined in the consultation paper.</p>
<p>14 - Before providing a financial adviser service, an Authorised Financial Adviser must have the competence, knowledge, and skills to provide that service.</p>	<p>The imposition of a condition to mirror Code Standard 14, tailored to the robo-advice context, is a critical element. The proposed capability condition must ensure that there can be confidence that personalised services provided through a robo-advice platform will be formulated with a level of competence, knowledge, and skills that is no less than would be expected of an AFA.</p>
<p>15 - An Authorised Financial Adviser must have a knowledge of the Act, the Code, and other legal obligations relevant to the operation of the Authorised Financial Adviser's practice as a financial adviser (including relevant consumer protection laws), that is adequate for the proper operation of that practice.</p>	<p>We agree that Code Standard 15 is not directly applicable to a robo-advice service.</p>
<p>16 - To be an Authorised Financial Adviser, a financial adviser must attain the Components of the New Zealand Certificate in Financial Services (Level 5) that are relevant to the financial adviser services provided by the AFA.</p> <p>For the purposes of the Code, an Authorised Financial Adviser is deemed to have attained a particular Component of the New Zealand Certificate in Financial Services (Level 5) where the Authorised Financial Adviser has attained an alternative qualification or designation to that</p>	<p>We agree that Code Standard 16 is not directly applicable to a robo-advice service, although expect the FMA to have regard to this Code Standard in formulating the detail of the proposed capability condition.</p>

<p>Component as specified in the Code's Competence Alternatives Schedule.</p>	
<p>17 - An Authorised Financial Adviser must maintain and keep current a professional development plan for each CPD period.</p>	<p>While we agree that the requirement to maintain and keep current a professional development plan is not directly applicable to a robo-advice service, we would expect robo-advice service providers to maintain a plan to ensure that their service and the systems employed are kept up to date. We believe a condition along these lines should be imposed, to reduce the risk of a 'set and forget' approach being taken.</p>
<p>18 - An Authorised Financial Adviser must undertake sufficient continuing professional training to maintain the Authorised Financial Adviser's competence at a level appropriate for the financial adviser services the Authorised Financial Adviser provides or intends to provide, and keep up to date with developments relevant to the Authorised Financial Adviser's practice.</p>	<p>Again, while we believe that a requirement to undertake continuing professional training is not directly applicable to a robo-advice service, we would like to see a condition imposed that requires robo-advice service providers to demonstrate that their systems have been reviewed to ensure they remain up to date, and have been maintained. Such a condition would link in with our recommended condition that providers be required to keep a maintenance plan, discussed in relation to Code Standard 17.</p>