

# SELECT COMMITTEE CHANGES TO FINANCIAL ADVISERS (PRE IMPLEMENTATION) BILL

## FINANCIAL PLANNING SERVICE (Internal and external communications)

*Note: assumption made that the proposed changes have been accepted in their current form and will only be released if the changes are confirmed.*

### FAQs

#### What has happened?

Earlier this morning the Commerce Select Committee, who is responsible for the Financial Advisers (Pre Implementation) Bill, has released its report to the House of Parliament. The report recommends significant and wide ranging changes to the Financial Advisers Act and the Financial Service Providers (Registration and Dispute Resolution) Act.

A fundamental change to the industry's understanding of the scope of the regulatory regime and its impact on advisers' obligations has been recommended.

The key issue of whether an adviser, who undertook a comprehensive review of a client's situation, including their financial position, was providing a Financial Planning Service was clarified to a large extent by the Securities Commission earlier this year. The Commission's view was that this did amount to a FPS, and therefore an adviser would need to be Authorised.

However, this has been fundamentally changed by the Select Committee recommendations released this morning.

The definition of Financial Planning Service (FPS) has been revised, with a narrowed scope and a focus on investment activity. The term "financial planning service" is now replaced with "investment planning service."

It is defined as follows:

*A person (A) provides an investment planning service if A designs, or offers to design, a plan for an individual that—*

- (a) is based on, or purports to be based on, an analysis of the individual's current and future overall financial situation (including his or her investment needs) and identification of the individual's investment goals; and*
- (b) includes 1 or more recommendations or opinions on how to realise those goals (or one or more of them).*

The new definition is aimed at capturing the following:

1. the fact that such services should be directed at investment goals;
2. the idea that it should involve a plan (rather than just a simple recommendation or opinion); and
3. the fact that the adviser should consider the overall financial situation (rather than simply some aspects of their finances).

There are also proposed restrictions on who can hold themselves out as financial planners.

### **What does this mean?**

#### Under previous Definition: Financial Planning Service

Advisers who provide advice on Category 2 products only (term insurance, residential mortgages), were required to be Registered (RFA) but not Authorised (AFA) *unless* they provided a FPS. If the adviser provided a FPS, Authorisation was mandatory.

Therefore, providing a FPS had a fundamental impact on an adviser's obligations under the new regime. Given that the previous interpretation of FPS was very broad (see Securities Commission paper <http://www.sec-com.govt.nz/publications/documents/boundary>) and not product specific, this captured a large amount of advisers. This meant that the majority of risk and mortgage advisers would need to be Authorised even if they did not provide advice on category 1 products.

#### New Definition: Investment Planning Service

Because the new definition specifically focuses on investments, advisers whose activities were focused purely on risk or residential mortgages are excluded from this definition. Therefore, risk / mortgage advisers who do not advise on investments (or any other category 1 products) will need to be Registered but not Authorised.

### **Why has this decision been made now? Did Sovereign know about it?**

The changes reflect strong feedback by the financial services industry. A large proportion of the industry felt that the interpretation of FPS was too broad and that it went against the original intent of the legislation and policy work.

The Ministry of Economic Development assessed this feedback and in effect agreed, putting forward the proposed new definition of Investment Planning Services to the Select Committee. The Select Committee accepted the changes and has recommended they be passed them into law.

Sovereign has been involved in every stage of feedback to ensure adviser interests are taken into account. Whilst we were not surprised that there are on-going changes to the regime, the scope of the change and the late stage of its release is of concern and has come as a surprise.

### **Should I be an RFA or an AFA?**

This depends on your business model. You will need to make a reasoned decision based on a thorough review of your business, including the nature of services you want to provide now and in the future.

There are both advantages and disadvantages to being an RFA or AFA. A common misconception is that being an RFA is an easier route for advisers. This is not necessarily the case.

RFAs are subject to the same statutory requirements of *'care, diligence and skill'* and prohibitions on misleading or deceptive conduct as an AFA. They are liable for the advice they provide and will be supervised by the commissioner of financial advisers and the Securities Commission.

Whilst RFAs are not currently subject to the Code of Professional Conduct, Sovereign understands that the Securities Commission's starting point on what defines *'care, diligence and skill'* is full compliance with the Code. RFAs not complying with the Code may need to explain why in the future.

The Bill has widened the scope of the purpose of the Act "so ensuring that there are available to retail clients financial advisers who have the experience, expertise, and integrity to match effectively a person to a financial product that best meets that person's need and risk profile. ...[and]...and ensures that financial advisers are held accountable for the services that they give to retail clients and that there are incentives for financial advisers to manage conflicts of interest appropriately."

Achieving AFA status will entitle you to offer a wider scope of financial adviser services (subject to having appropriate levels of competency, knowledge and skill) and will provide tangible proof on your capability as an adviser. In addition, there are indications that the Securities Commission will market the benefits of being an AFA, as part of their education drive to consumers.

**I have decided to be an RFA, does that mean I do not need to do the Open Polytechnic training?**

The Financial Advisers Act aims to promote good advice and encourage confidence in the professionalism of advisers. A key tool to do this is to establish a competency framework to ensure consumers are confident that the financial adviser they engage is capable of delivering the type of service they provide.

Whilst RFAs are not subject to the Code of Professional Conduct they still must demonstrate care, diligence and skill. A tangible way for RFAs to demonstrate their skill is to complete the Open Polytechnic training (National Certificate in Financial Services, level 5).

This certification will provide you valuable marketing benefits and is also a very effective risk management tool, as it will teach you up to date best practices for carrying on your business which will help ensure you are able to withstand regulatory challenge.

Further, whilst the focus to date has been on AFAs, an educational pathway for RFAs is planned in the future. Whilst no decision has been made on what this will be, potentially the expectations for AFAs will also apply to RFAs.

Another consideration is that the legislation will continue to develop over time. The Government has made it clear that they are laying the foundation for future and that expectations of the industry are likely to increase over time. This is logical in the journey when turning an industry into a profession.

Notwithstanding whether you decide to be an RFA, Sovereign is very proud to have the best training offering in the market. We are of the view that there is no better time to commit to training and development. Doing so demonstrates your commitment to professionalism and will give you a real opportunity to take a position of leadership.

We strongly recommend those who have already started the training continue. It will never be more cost effective or easier to do so.

**What does the term *care, diligence and skill* mean?**

The term is not defined in the FAA and is therefore subject to interpretation from the Commissioner of Financial Advisers and the Securities Commission.

The best indication we have is from the Securities Commission. Their clear steer is that the starting point for demonstrating *care, diligence and skill* will be via comparison to the Code of Professional Conduct.

Therefore, whilst RFAs are not explicitly subject to the Code, in reality they are implicitly subject to its principles.

**If I decide not to continue with the training, will Sovereign still refund the 50% I have paid?**

Sovereign is working through the details of this and will advise our position in due course.

**Has Sovereign made a decision on whether it will be a QFE?**

Given that there remains significant uncertainty, Sovereign is not in a position to announce whether or not it will be a QFE and if so, the details of this. Before doing so, we require absolute clarity and certainty of law.

### Sovereign's approach

Sovereign has previously communicated a desire to set a high bar and take an industry leading position in embracing the principles of the regime. Nothing about today's announcement changes our approach.

We remain committed to leading the way in ensuring professionalism, integrity and public confidence. We are confident that our valued advisers will adopt a similar professional approach.

<b>Decision Tree</b>		<b>Advice</b> "Make or making a recommendation or give or giving an opinion in relation to acquiring or disposing of (including refraining from acquiring or disposing of) a financial product"	<b>Investment Planning Service</b> A designs, or offers to design, a plan for an individual that— (a) is based on, or purports to be based on, an analysis of the individual's current and future overall financial situation (including his or her investment needs) and identification of the individual's investment goals; and (b) includes 1 or more recommendations or opinions on how to realise those goals (or any of them).
<b>Individual</b>	<b>Category 1 products</b>	Authorised Financial Adviser	Authorised Financial Adviser
	<b>Category 2 products</b>	Registered Financial Adviser	NA
<b>Employee / nominated representative of a QFE</b>	<b>Category 1 products (NOT issued/promoted by QFE)</b>	Authorised Financial Adviser	Authorised Financial Adviser
	<b>Category 1 products (Issued/promoted by QFE)</b>	Category 1 adviser (Same requirements as an AFA, but not registered or authorised) <i>* nominated agents may still need to be registered</i>	Authorised Financial Adviser AFA
	<b>Category 2 products</b>	Category 2 adviser (Same requirements as an RFA, but not registered)	NA