

The Financial Advisers Act and Financial Service Providers (Registration and Dispute Resolution) Act

These two Acts introduce regulation of the financial services sector and financial advisers. What follows is only some of the key points from what is complex legislation with much detail yet to be determined and set either as a “code” or in regulations.

The dates for implementation will be set by Order in Council, and various parts will come into force at different times. We anticipate that the main aspects affecting financial advisers will take effect from 2010.

The regulator will be the Securities Commission and a Commissioner for Financial Advisers will be appointed.

Registration of Financial Service Providers

All financial service providers will need to be registered. This will include all financial adviser practices as well as the product providers.

Two tier approach based upon product

Regulation of financial advisers will use a two tier approach largely based upon product.

Category 1	Category 2
Securities (other than a Category 2 security), e.g. PIE, managed fund, equity, bond, debenture, superannuation, KiwiSaver Any estate or interest in land or A futures contract.	Call debt security, Bank term deposit Insurance product, excluding a life insurance policy issued after 31 December 2008 – but this exclusion is only for investment insurance policies. Consumer credit contract, e.g. mortgage, loan, hire purchase

The main basis for regulation is whether someone gives financial advice or makes an investment transaction. In addition, anyone providing a “financial planning service” is required to meet the requirements for a Category 1 product. Obviously, this is to ensure that financial planning without specific product advice is also covered.

The definitions have some interesting effects:

Bank term deposits are Category 2, but a term deposit by the Building Society is Category 1.

The exclusion for a “life insurance policy issued after 31 December 2008” involves complex legal language but seems to mean only insurance policies which are “securities”, i.e. investment insurance products such as whole of life or endowment. This exclusion seems to be targeted at allowing insurance advisers to service old whole of life and endowment policies as Category 2, and for insurance advisers to be Category 2 provided they don’t give advice on or sell any new Category 1 products.

Note: *This change was introduced as the legislation went through its last stages in Parliament so differs from what was stated during the Roadshow.*

Mortgage brokers will be Category 2, provided they don’t also provide advice on Category 1 products such as KiwiSaver. But a mortgage broker could give advice on insurance.

Requirements for Category 1 financial advisers

Financial advisers who provide advice or sell Category 1 products or who provide a financial adviser service need to:

- Be “authorised” by the Securities Commission – which will require them to be of good character

and meet levels of competency, knowledge and skills.

- Be listed on the register of financial advisers.
- Exercise care, diligence and skill.
- Comply with a Code (yet to be developed) which will probably include a code of conduct, practice standards and competency requirements.
- Comply with the terms of authorisation – which will probably mean they may provide advice only for products they are authorised and where they have demonstrated competency.
- Provide clients with a disclosure statement (likely to be similar to what is currently required for investment advisers).

Nobody yet knows what the competency requirements will be for authorised financial advisers. However, IFA members who have CFP/CLU or a Certificate in Financial Services are likely to already meet or exceed what will be required. Those who don't have recent qualifications may have to undertake some form of competency testing or evaluation, but there will not doubt be a transition period for this. So, don't be concerned until this aspect has been clarified.

Requirements for Category 2 financial advisers

Financial advisers who provide advice or sell Category 2 products need not be individually authorised, though they or their firms will need to be registered. They will need to:

Exercise care, diligence and skill.

- Disclose their status as a financial adviser, i.e. whether they are authorised.
- Dispute resolution arrangements
- Business location and contact details

There are no competency requirements specified for Category 2, other than the general requirement for "care, diligence and skill".

Qualifying Financial Entities

There is provision for entities to become Qualifying Financial Entities (QFE). Once approved by the Securities Commission a QFE takes responsibility for its employees and agents who are Category 2 financial advisers. The QFE provides the disclosure statement and is liable for any breaches by their employees or agents.

Employees or agents of a QFE who are Category 1 financial advisers generally need to follow the requirements for other Category 1 advisers. However, employees of a QFE may provide advice on a Category 1 product where the QFE is the issuer.

Note: *This change was introduced as the legislation went through its last stages in Parliament so differs from what was stated during the Roadshows.*

This change means that staff of a bank that becomes a QFE will be able to sell PIEs without needing to be authorised. Similarly, if a Building Society or Finance Company were to become authorised, their staff would be able to sell term deposits or debentures issued by them, without needing to have authorised staff. These staff will not need to meet competency standards unless this was made a condition of approval of the QFE.

Other professionals

There are exemptions for other professionals. Chartered Accountants, Lawyers, registered Tax Agents and Valuers are exempt from the provisions of the Act to the extent that they only give financial advice that is "incidental" to their professional activities. For example, a chartered

accountant giving financial advice that is incidental to tax advice.

Real Estate Agents are covered by their own Act which brings in new regulation of their activities. Anyone else giving advice on real estate investment will need to be an authorised financial adviser.

Code Committee

Under the Act, the Commissioner for Financial Advisers will establish a Code Committee which will be largely made up from industry representatives plus a consumer representative. The committee will elect its own chair and the Commissioner for Financial Advisers will not be a member. The Code Committee's role is to develop a "code of professional conduct for authorised financial advisers". This will include competence, knowledge and skills, ethical behaviour and client care.