

# Feedback: Proposed standard conditions for financial advice provider full licences and classes of financial adviser service

Please submit this feedback form electronically in both PDF and MS Word formats via email to [consultation@fma.govt.nz](mailto:consultation@fma.govt.nz) with 'Feedback: Proposed standard conditions for financial advice provider full licences and classes of financial adviser service' in the subject line. Thank you. **Submissions close at 5pm on Friday, 7 August 2020.**

Date: 6 August 2020

Number of pages: 9

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Company or entity: Insurance Council of New Zealand (ICNZ)

Organisation type: Industry Association

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Question number	Comment	Recommendation
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*You don't need to quote from the consultation document if you use page numbers.  
You may insert additional lines or pages - please label each additional page with your name & organisation.*

## 4.1 Condition 1 – Record keeping

(a)	While we are generally supportive of the record keeping condition and the associated guidance, there are aspects that, in our view, are unduly duplicative, onerous or need clarifying.  Please see the additional pages for full comments and recommendations.
(b)	While ICNZ is not a financial advice provider business, our members keep different kinds of records including written records (often electronic or digitised) and recordings of telephone conversations with customers etc.  By way of background, ICNZ's members are general insurers that insure about 95 percent of the New Zealand general insurance market, including about a trillion dollars' worth of New Zealand property and liabilities. ICNZ members provide insurance products ranging from those usually purchased by individuals (such as home and contents, travel and motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability, business interruption, professional indemnity, commercial property and directors and officers insurance).
(c)	Provided the concerns raised in the additional pages are addressed, we do not expect that this condition would impose significant additional compliance costs.
(d)	We refer to our response to (a) above.
(e)	We refer to our response to (a) above.
(f)	No comments.

## 4.2 Condition 2 – Internal complaints process

(a)	While we agree with the proposed internal complaints process condition in general terms, there are aspects that, in our view, need clarifying.  Please see the additional pages for full comments and recommendations.
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(b)	All ICNZ members, irrespective of whether they will be licensed financial advice providers under the new regime, are required to have an internal complaints process, amongst other things, by virtue of the application of the Fair Insurance Code. The Code applies to all ICNZ members.
(c)	Provided the concerns raised in the additional pages are addressed, we do not expect that this condition would impose significant additional compliance costs.
(d)	We refer to our response to (a) above.
(e)	No comments.
(f)	No comments.
<i>4.3 Condition 3 – Regulatory returns</i>	
(a)	We are supportive of the regulatory returns condition in principle provided they are proportionate and not unduly onerous or costly. We note that further details about it are to be provided in a Regulatory Return Framework and Methodology document, which we look forward to providing feedback on in due course. There are also several matters that we consider you ought to consider in this regard.  Please see the additional pages for full comments.
(b)	We note that further details are to be provided in a Regulatory Return Framework and Methodology document, which we look forward to providing feedback on in due course. Until that detail is available we cannot comment on compliance cost.
(c)	We refer to our response to (a) above.
(d)	No comments.
(e)	No comments.
<i>4.4 Condition 4 – Outsourcing</i>	
(a)	While we can appreciate the intention of the outsourcing condition, we consider that there is a need for greater clarity in this respect (noting this has the potential to be very broad).  Please see the additional pages for full comments and recommendations.
(b)	No comments.
(c)	We refer to our response to (a) above.
(d)	We refer to our response to (a) above.
(e)	No comments.
(f)	No comments.
<i>4.5 Condition 5 – Professional indemnity insurance</i>	
(a)	We consider that there are a number of issues with the professional indemnity insurance condition that need to be worked through (including the necessity of this requirement for all licensees, the efficacy of professional indemnity insurance to meet claims for compensation from retail clients and the utility of the proposed disclosure in the event professional indemnity insurance is not held).  Please see the additional pages for full comments and recommendations.
(b)	No comments.
(c)	We refer to our response to (a) above.
(d)	We refer to our response to (a) above.

(e)	No comments.
(f)	No comments.
<i>4.6 Condition 6 – Business continuity and technology systems</i>	
(a)	<p>While we can see merit in the business continuity and technology systems condition and the associated guidance, we consider that these matters should be separated into two separate conditions. There are also areas, in our view, that should be clarified and expanded upon in this respect.</p> <p>Please see the additional pages for full comments and recommendations.</p>
(b)	Both ICNZ and its members have documented business continuity plans.
(c)	No comments.
(d)	We refer to our response to (a) above.
(e)	We refer to our response to (a) above.
(f)	No comments.
(g)	No comments.
<i>4.7 Condition 7 – Ongoing capability</i>	
(a)	<p>While we are generally supportive of the ongoing capability condition, it is considered that allowance should be made for our members who are already subject to robust fit and proper persons requirements as licensed insurers under the Insurance (Prudential Supervision) Act 2010 to avoid unnecessary regulatory burden.</p> <p>Please see the additional pages for full comments and recommendations.</p>
(b)	We refer to our response to (a) above.
(c)	We refer to our response to (a) above.
(d)	No comments.
(e)	No comments.
<i>4.8 Condition 8 – Notification of material changes</i>	
(a)	<p>We consider that the notification of material changes condition and associated explanatory note should be amended to provide more clarity.</p> <p>Please see the additional pages for full comments and recommendations.</p>
(b)	We refer to our response to (a) above.
(c)	We refer to our response to (a) above.
(d)	No comment.
(e)	No comments.
(f)	No comments.
<i>4.9 Financial advice provider full license classes</i>	
(a)	While the proposed three-classes for financial advice service are generally welcomed, we consider that it would be helpful to highlight in the finalised guidance that the level of inquiry of an applicant/licensee within a class may be different. We also consider that 'A', 'B', 'C' classes should be relabelled.

	Please see the additional pages for full comments and recommendations.
(b)	No comments.
(c)	No comments.
<p><b>Feedback summary.</b></p> <p>While overall ICNZ and its members are supportive of the three classes, standard conditions and guidance proposed in principle, as outlined in the additional pages, there are a number of areas (i.e., in respect conditions 1, 2, 4, 6 and 8 ) where we consider refinements should be made and/or clarification provided. There are also some areas where the proposed conditions and guidelines in their current form create an unnecessary regulatory burden and ought to be amended in our view (i.e., conditions 1 and 7). The most significant area of concern from our perspective is condition 5 (professional indemnity insurance), which we consider should either be removed or reframed. We also consider that the three classes should be relabelled to avoid any negative connotations attached to the 'B' and 'C' labels and we would appreciate it if it could be confirmed in guidance that, in making inquiries of applicants/licensees, regard be had to the scope and degree of complexity of the financial advice services provided.</p> <p>Please also see our further comments in additional pages ('Other comments' heading) and let us know if you would like to discuss any of our feedback and recommendations in more detail.</p>	
<p><b>Please note:</b> Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.</p>	
<p><b>Thank you for your feedback – we appreciate your time and input.</b></p>	

ICNZ FEEDBACK (NICK WHALLEY): PROPOSED STANDARD CONDITIONS FOR FINANCIAL ADVICE PROVIDER FULL LICENSES AND CLASSES OF FINANCIAL ADVICE SERVICE

*Condition 1 – Record keeping*

While we are supportive of the record keeping condition generally, the requirement to produce a summary of non-english records in English on an on-going basis is unduly onerous in our view and disproportionate to the intended usage (i.e., being available for inspection/review should you request it). We consider a preferable approach would be for summaries of non-english records to be produced only when you request them. We also consider that the reference in (b) of the condition to “*may be in any language provided you keep an accurate summary of the record in English...*” could be interpreted as requiring summaries of records that are already in English to be produced.

Additionally, while the reference in the explanatory note to records being provided within 10 working days of being requested is workable in most cases, there are circumstances when this will not be the case. For example, when the compilation of a large number of call recordings or electronic notes is required. It is considered that providing flexibility here would still be consistent with the references in the condition to creating records in a 'timely manner' and making records available for inspection at 'all reasonable times'.

We recommend:

- Replacing paragraph (b) of the condition with the following:  
“(b) *may be in any language provided, for any non-english record, you must provide us with either an accurate summary in English, or a full translation by a translator approved by us into English, if we request it;*”.
- Amending the third full paragraph of the explanatory note as follows: “*Your records should be readily available to you, and in any event within 10 working days when requested by us, or such longer timeframe we agree to.*” (amendments underlined).

*Condition 2 – Internal complaints process*

While we agree with the proposed internal complaints process condition in general terms, and note that our members already have similar obligations under the Fair Insurance Code (available [here](#)), [as previously indicated](#), we consider that it is important to clarify that a client service issue raised and resolved during the initial interaction with the client should not be treated as a complaint. Otherwise this will lead to false positives in complaint records and potentially unnecessary record keeping and regulatory burden. In our view such matters are best characterised as a client service issues in respect of which no further action is required.

We are also concerned that the reference in the explanatory note to “[a] *complaint includes a complaint about a failure to provide a service or give advice*” in the condition. This may be interpreted as including a client complaint about a licensee failing to provide certain services or advice which fall outside the scope of its operations, which we understand is not the intention.

We would also appreciate if it could be confirmed how long records of complaints and any actions taken must be held. We assume the intention is for licensees to hold these for 7 years consistent with condition 1 (record keeping).

We recommend that the explanatory note be amended to:

- Include a new sentence at the end of the first paragraph: “*A complaint does not include client service issue raised and resolved during the initial interaction with the client on the matter.*”
- Amend the first sentence of the second paragraph as follows: “*A complaint includes a complaint about a failure to provide a service or give advice, where you have represented that you provide such service or give such advice.*” (amendments underlined).
- Clarify how long records of complaints and actions taken must be kept.

## ICNZ FEEDBACK (NICK WHALLEY): PROPOSED STANDARD CONDITIONS FOR FINANCIAL ADVICE PROVIDER FULL LICENSES AND CLASSES OF FINANCIAL ADVICE SERVICE

### *Condition 3 – Regulatory returns*

We are supportive of this condition in principle, noting that further details about it are to be provided in a Regulatory Return Framework and Methodology document. We look forward to having an opportunity to provide feedback on this document in due course. We encourage drafters to ensure that this document is tailored to the new regulatory framework for financial advice and consider whether there is an intention to make any information provided in regulatory returns publicly available. We also encourage a proportional approach, so the amount of information required and frequency with which it is required reflects the need and perceived risk without being unduly onerous or costly to comply with.

### *Condition 4 – Outsourcing*

While we can appreciate the intention of this condition, we consider that greater clarity needs to be provided about the particular outsource arrangements that fall within its scope, as this condition has the potential to be very broad. In particular, it is unclear what constitutes 'material', and the position regarding systems or processes carried out by a related entity within the same group as a licensee ought to be explained (either within the condition itself, or the explanatory note).

Given these uncertainties, we believe a better way of characterising this condition, would be to refer to outsource arrangements that are essential or fundamental to the provision of financial advice services. This implies a threshold of being necessary for the financial advice provider's operation, which we believe is the intended scope of this condition. We agree with the FMA's final comment but also suggest that this condition not extend to outsource arrangements that simply support the running of a business (such as those supporting back-office or other administrative functions).

We recommend:

- Amending the condition as follows: "*If you outsource a system or process that is ~~material~~ essential to the provision of your financial advice service you must ensure your arrangements enable you to meet your market service licensee obligations.*" (amendments underlined).
- In the explanatory note:
  - Providing further guidance and examples about what specific outsource arrangements would fall within this condition.
  - Clarifying the position and expectation regarding related parties within the same group.

### *Condition 5 – Professional indemnity insurance*

While the initial impression is that this condition looks straightforward, on closer examination it is considered that there are number of issues with it that need to be worked through.

First, we query whether it is necessary to require all licensees to have professional indemnity insurance to ensure that retail clients can be compensated. For example, certain large licensees, some of whom may self-insure, are already well placed financially to meet any claims for compensation by clients without recourse to professional indemnity insurance. There may also be relevant regulatory requirements in place in this regard. For example, in addition to satisfying obligations as a licensed financial advice provider (if applicable), ICNZ's members, as licensed insurers under the Insurance (Prudential Supervision) Act 2010 (IPSA) must satisfy comprehensive prudential and solvency requirements. We envisage that the position of our members may contrast with the position of other licensees who may have limited financial resources to meet a substantial claim against them without recourse elsewhere. Additionally, while it may be relatively straightforward for smaller licensees to put in place a conventional professional indemnity insurance policy, the complexities and scale of a larger licensees' operations may make it unnecessarily burdensome to do so.

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Secondly, we have concerns about the efficacy of professional indemnity insurance to meet a claim for compensation even if the ability of it to do so was not in issue. The primary purpose of professional indemnity insurance is to provide protection for those providing professional advice, rather than acting as a surety for compensation to their clients or customers. Additionally, while there are variations in professional indemnity insurance offerings available in the market, we note the following potential limitations in this regard:

- Over recent years there has been a hardening of the market for this line of insurance and there is no guarantee that the appropriate cover would be available and/or at a price point a licensee could afford. This may be a particular challenge for smaller licensees.
- Professional indemnity policies generally exclude liability assumed by agreement unless the insured would otherwise have been liable. In other words, these policies will not respond to a claim the licensee is liable for under contract unless they would have been liable for this anyway (e.g. by virtue of breaching some professional duty in common law).
- Professional indemnity policies generally place limits on the types of activities undertaken and the extent to which cover is extended to agents and past activities, with these matters being subject to policy conditions and underwriting criteria.
- Professional indemnity policies generally require the underwriting insurer of the policy to be involved in the conduct of the dispute. This may be problematic if the client's claim for compensation originated from the licensee's internal and/or external complaints process and they have made concessions without that insurer's involvement.
- Professional Indemnity policies will not respond when the licensee has been dishonest, reckless or malicious.
- Assessing whether indemnity limits in the aggregate or for any one claim are 'adequate and appropriate' may not be straightforward to determine until a loss has occurred.

Also, in respect of that last point, while it makes sense to avoid being unduly prescriptive in our view, it is important to emphasise that satisfying this condition would ultimately involve a judgment call being made by the licensee and their insurer or insurance adviser about what constitutes 'adequate and appropriate' cover, noting that this is inherently uncertain and maybe something scrutinised with the benefit of hindsight after the fact. It is also unclear from the condition and commentary in our view:

- How far the requirement to hold professional indemnity insurance is intended to extend to aspects of the licensee's business beyond the provision of licensed financial advice service directly, noting that some licensees may have a number of business lines unrelated to this.
- When a license will be declined because professional indemnity insurance is not held.

Lastly, in the event that a licensee is required to disclose to its retail clients that it does not have professional indemnity cover as proposed, it is questionable how useful this disclosure would be particularly because, as proposed, no reasons for this are to be provided which would provide relevant context. For example, whether professional indemnity insurance has not been taken because it was not considered necessary or because it was unable to be obtained this would be perceived differently. On this basis:

- The disclosure may result in a client deciding that they should not engage the licensee on the false assumption that it could not meet any claim for compensation against it.
- Conversely, a client may incorrectly assume that, because a licensee holds professional indemnity insurance, it would be able to meet any claim made against which for the reasons outlined above may not be the case.

We recommend either removing this condition or reframing it, adopting a first principles approach that squarely focusses on the problem to be solved and most appropriate solution to address it. Presumably, the focus here would be on licensees with limited financial resources. Again, a targeted and proportional approach is recommended. In so far as any Professional Indemnity insurance requirement is to remain, we recommend that the disclosure requirements be amended to reflect the feedback above and, for consistency with other FMA licenses (such as licenses for [discretionary investment management services \(DIMS\)](#) or [managed investment scheme \(MIS\) manager](#)), this be set out in applicable licensing guides rather than the standard conditions.

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### *Condition 6 – Business continuity and technology systems*

While we can see merit in the requirements set out in this condition, and note that these generally reflect best practice in any event, for clarity we consider that the business continuity and technology systems should be split out into two separate conditions as they relate to different matters and as some of the proposed cyber security requirements go beyond what is typically included in a business continuity plan. Separating these matters out will also reduce the risk that important areas are missed.

We also consider that licensees should be provided with flexibility as to whether the requisite business continuity plan is a separate plan specifically prepared for licensing purposes or an existing plan in place.

We recommend:

- Separating out business continuity and technology systems into two separate conditions.
- Making it clear in the applicable explanatory note that licensees can decide whether they produce a separate business continuity plan for licensing purposes or rely upon an existing plan to meet this requirement.

### *Condition 7 – Ongoing capability*

While we are generally supportive of this condition, it is important to acknowledge that our members, as licensed insurers under the IPSA, are already subject to robust ongoing fit and proper persons requirements under that regulatory regime. In our view, this ought to be reflected in this condition and an adjustment made to avoid unnecessary regulatory duplication.

We recommend amending this condition and explanatory note to either:

- exempt insurers licensed under the IPSA from the fit and proper persons requirement, or
- deem insurers licensed under that regime as compliant with this requirement.

### *Condition 8 – Notification of material changes*

We consider that this condition and explanatory note requires change to make it clearer. In particular:

- The reference to 'commencing to implement' in the condition is unclear as it allows for too many individual interpretations as to its meaning.
- The definition of the 'nature of your financial advice service' in the explanatory note appears to be inconsistent with the narrower characterisation in the comments section.

We recommend:

- Amending the condition as follows: "*You must notify us in writing within 10 working days of commencing to implement any implementing any material change to...*"
- Clarifying the guidance to address inconsistencies regarding the characterisation of the 'nature of your financial advice service'.

### *Proposed new three classes*

While the proposed three-classes for financial advice service are generally welcomed, in our view it is important not to treat all applicants and licensees that fall within a particular class (i.e. class A, class B or class C) the same way. This is because within each license class there will be a range of financial advice providers offering different types of financial advice services with different scopes and varying degrees of complexity. For example, it is possible (and even likely) that a single adviser provider in class A or multi-adviser provider in class B provides advice with a broader scope and more complexity than a provider in class C, whose advice may be limited to their own products. In our view regard should also be had to the scale of the licensee's operations, noting that for small operators for example inquiries and additional requirements have the potential to involve significant resources to comply with which may be unduly disproportionate or onerous.



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Additionally, we understand that license classes are primarily designed to serve an administrative function and the new disclosure regulations do not appear to require these to be referred to. Nonetheless we consider there is a risk of a negative view being formed about licensees with 'B' or 'C' class licenses by current or prospective clients or stakeholders due to the inherent attributes of these 'B' and 'C' labels.

We recommend:

- That in your commentary with the finalised conditions you outline that, in making inquiries and requests of applicants or licensees, consideration will be given to the type and scope of the financial advice services provided, its complexity and the scale of their operations.
- Using numbers rather than letters to label the different classes (i.e., 1 for A, 2, for B, 3 for C). Alternatively, descriptors could be to identify classes i.e., 'single adviser' for A, 'multi-adviser' for B and '' for 'comprehensive' for C.

### *Other comments*

Another matter that should be clarified in our view is the applicability of these standard conditions where the licensee provides regulated financial advice to wholesale clients as well as retail ones. While the intention appears to be for these standards to only apply to financial advice to retail clients based upon the commentary, standard conditions 1, 2 and 4 are framed in such a way as they could be interpreted to apply to both retail and wholesale clients.

We recommend that your guidance be amended to clearly indicate that these general conditions only apply to regulated financial advice to retail clients, noting specifically that conditions 2 and 4 and their guidance may be interpreted as applying more broadly to financial advice to wholesale clients as well.

We also recommend that a document equivalent to the 'Quick guide to licence applications for small businesses providing DIMS' (available [here](#)) be produced for Class A applicants to assist them with their licence application.