

READY
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PRACTICAL KNOWLEDGE FOR THE NEW REGIME

Webinar 3- Workbook 3



Client understanding the nature
and scope of advice.

Disclaimer

The information provided in today's webinar is for general information only and is not legal advice.

Please refer to the regulations and seek legal advice in relation to how the regulations apply to you and your Financial Advice Provider.

The source of the information referred to in this webinar:

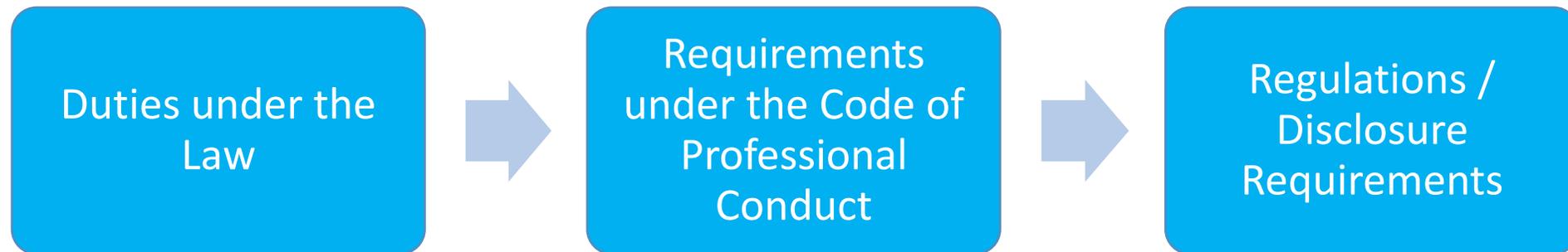
- Financial Markets Conduct (Regulated Financial Advice Disclosure) Amendment Regulations 2020.
- The Financial Service Legislation Amendment Act (FSLAA) has significantly revised the current Financial Markets Conduct Act (FMC Act).
- The Code of Professional Conduct for Financial Advice Services.
- New disclosure requirements – members guide Financial Advice New Zealand.

Agenda

- Duties under the legislation
- Applicable code standards
- Regulations
- An applied example
- Actions: policies, procedures and controls
- Questions – Katrina will manage through Q&A chat function.



3 Levels of obligations



Level 1 – 8 new Duties under the law

The Financial Service Legislation Amendment Act (FSLAA) has significantly revised the current Financial Markets Conduct Act (FMC Act).

The duties of persons who give regulated financial advice, as per new subpart 5a, are in summary:

- 431I Duty to meet standards of competence, knowledge, and skill
- **431J Duty to ensure client understands nature and scope of advice**
- 431K Duty to give priority to client's interests
- **431L** Duty to exercise care, diligence, and skill
- **431M** Duty to comply with code of conduct
- **431N** Duty relating to offer that contravenes Act or regulations
- **431O** Duty to make prescribed information available
- **431P** False or misleading statements and omissions



431J – Duty to ensure clients understands nature and scope of advice

“A person must not give regulated financial advice to a retail client unless the person has taken reasonable steps to ensure that the client understands the nature and scope of the advice being given, including any limitations on the nature and scope of the advice.”

What does nature and scope of advice mean?

The nature and scope of advice can mean different things for different clients.

For clients it is broader than just the written advice – it takes into account a range of factors about the advice environment, the client and the advice.

This includes the following factors:

- The type of advice
- What mediums and how the advice is delivered
- The client's personal circumstances
- The client's likely ability to understand financial matters
- The client's access to support in the advice process (e.g. a family member, spouse)
- When and how the client can ask questions about the advice and scope of service



Practical tips for the new regulations.

- It is not enough to simply agree on the nature and scope of advice then demonstrate you have agreed by getting the client to sign-off on it for example. More work is required!
- The use of the current terms such as 'full, limited and class advice' will need to be removed.
- This does not mean you have to specifically exclude everything you don't advise on – but you need to explain any limitations or exclusions within the range of advice you provide.
- The limitations you place on your advice must be clearly explained and documented in the nature and scope of advice. e.g. I am only accredited 3 main bank lenders and not with ABC bank which limits the range of providers and products I can recommend to you.
- Or I cannot advise you on Personal Risk Insurance as this is not my area of expertise, but I can refer you to a specialist in this area to assist you with your insurance needs.

Code of Professional Conduct for Financial Advice Services (The Code)

Part 1 - Ethical behaviour, conduct & client care

Standard 1 – Treat clients fairly *

Standard 2 – Act with integrity

Standard 3 – Give financial advice that is suitable *

Standard 4 – Ensure that the client understands the financial advice

Standard 5 – Protect client information

*also relevant to your Duty 431J



Note: There are a further four standards in the Code that describe the standards of competence, knowledge, and skill.

Code standard 4 - Ensure that the client understands the financial advice

A person who gives financial advice must take reasonable steps to ensure that the client understands the financial advice.

This relates to the financial advice itself.

Understanding the financial advice includes the client having sufficient comprehension of:

- the **content**,
- **risks and consequences** of the financial advice,
- and of the nature of any **ongoing and other services** related to the financial advice,
- to be able to make timely and **informed decisions** about the financial advice.

Code standard 4 - Ensure that the client understands the financial advice

This also takes into account the following:

- Whether the financial advice is based on **valid assumptions** about the client's circumstances.
- Whether **to follow** the financial advice.
- Whether the **fees and costs associated** with following the financial advice, such as those of any financial advice product or platform, **are acceptable, and**
- Whether and when to **seek additional** financial advice.

Other relevant Code standards to Duty 431J

Standard 1 – Treat clients fairly

A person who gives financial advice must always treat clients fairly. What is fair depends on the particular circumstances, including the nature and scope of the financial advice.

Standard 3 – Give financial advice that is suitable

A person who gives financial advice must ensure that the financial advice is suitable for the client, having regard to the nature and scope of the financial advice.

Regulations under the Act - Disclosure

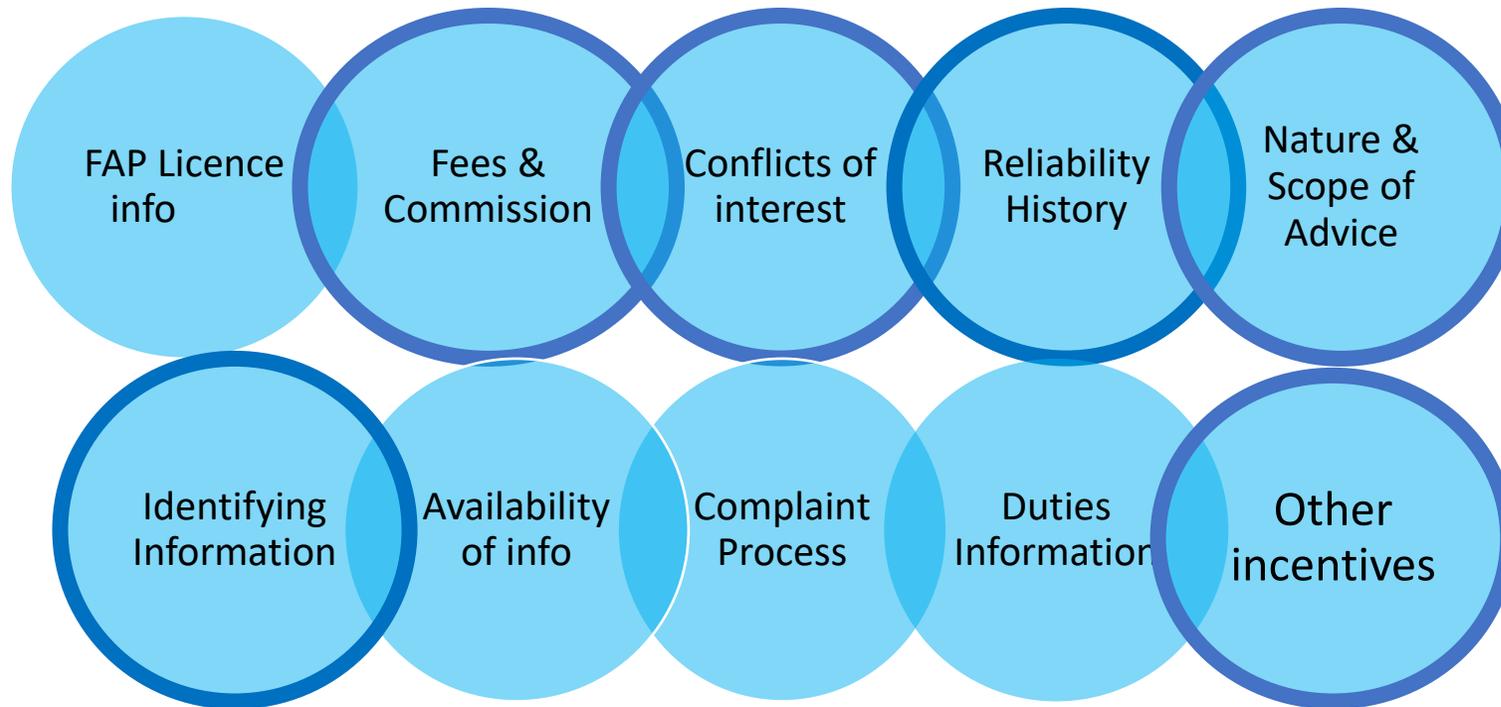
- The Financial Markets Conduct (Regulated Financial Advice Disclosure) Amendment Regulations 2020.
- **The purpose of disclosure is to help consumers make an informed decision on whether to seek, obtain or act on advice from a person or provider.**

Stages of disclosure from 15 March 2021.



When Nature & Scope of Advice is Known

- What information needs to be disclosed.



*Refer to New Disclosure Requirements - Members Guide.

**More Disclosure discussions in webinar 6 – 3rd March 2021.

When Nature & Scope of Advice is Known

- What types of advice will be provided including products providers
- Any limitations or restrictions on advice provided
- Fees or expenses payable by the client, including the amount (if known), how they are calculated and terms of payment.
- Commissions paid by the product providers to the adviser and how they are calculated.
- How any conflicts of interest are managed including any incentives.
- Reliability history
- Financial Advisers identifying information – which FAP are they providing advice on behalf of.

An applied example (Section B of your workbook - page 10)

Aspiring First home owners



- Laura and Izaz are first home buyers in Christchurch.
- They have come to you to get help putting together a mortgage application, as all their friends are getting on the property ladder, and they have decided they want to as well.
- They both have stable jobs, and have saved a deposit of \$130,000, including their two KiwiSaver accounts.
- They think they qualify for a Home Start grant and have included that in their house deposit calculations.

Consider the following 2 scenarios regarding the nature and scope of the advice.

An applied example (Section B of your workbook - page 10)

Aspiring First home owners

Scenario 1

“You have asked me to help you gain approval for a mortgage of up to \$450,000 to buy your first home. You do not want my assistance to determine the appropriate structure for you, as you have decided on a two-year fixed rate, just like your friends have. You have advised your solicitor will help you with your KiwiSaver withdrawals.”

Questions

1. What are the limitations of Scenario 1?
2. What are the risks and consequences of these?

An applied example (Section B of your workbook - page 10)

Aspiring First home owners

Scenario 2

“You have asked me to help you gain approval from a suitable lender, for a mortgage to purchase your first house. You would also like me to assist with how to structure this to suit your needs and objectives. I cannot provide you advice on KiwiSaver, or using KiwiSaver for your first home withdrawal, but can give you information on how to apply for the First Home Withdrawal and the Home Start Grant.”

Questions

1. What are the limitations of Scenario 2?
2. What are the risks and consequences of these?

An applied example (Section B of your workbook - page 10)

Aspiring First home owners - Laura and Izaz - first home buyers in Christchurch.

What are some of the client considerations?

Do they want to get specific advice suitable to their needs and objectives?

Are they happy getting advice from different sources – do they have the financial/literacy or understanding to work through the information provided to them and decide on their actions.

What factors are likely to impact on the nature and scope of your advice?

- The limitations the client puts on you regarding the structure of their loan.
- The limitations you put on your advice around the KiwiSaver advice component.

Consider how you explain the dangers of limiting areas of advice in their circumstances in both scenarios. The outcome could be not ideal when it comes to purchasing their first home if they fail to get the deposit organised correctly and confirmed before signing a contract to buy a home.

Evidence that you have gained the clients understanding and agreement.



PPC – policy procedure control.

Evidence that you have gained the clients understanding and agreement using PPC's.

How you can implement processes and demonstrate how you complete the following good practices?

- Explaining the nature and scope of advice and the types of service you can provide – without going straight to any limitations
- Ensuring the client understands the implications of the limitations, rather than assuming a particular level of financial literacy or understanding of financial services products
- Gaining client understanding, including their feedback, and then proceed to a process of agreement
- Documenting a nature and scope of advice process that does not rely on 'ticking boxes.'

Next - 4 examples of relevant PPC's.

1. Explain the advice process, products and services you offer.
2. Explain what the 'nature and scope of advice' is and the consequences and risk of limitations.
3. Have documented evidence of the steps taken to ensure client understanding the nature and scope of the advice, along with the risks and consequences of any limitations.
4. Ensure fees and costs associated with following the financial advice, such as any financial advice product or platform are acceptable.

PPC - Example 1

Action 1 – Explain the advice process, products & services you offer.

1. Develop Policy statement - Promise to your clients.

“We will spend time with you to ensure you understand the different types of advice and products we can advise you on.”



Refer to Section C of your workbook. Page 21.

PPC example 1 cont.



2. Develop Processes and Procedures (tasks) how you make this happen.

- Explain on your **website** the different types of advice and products your Financial Advice Provider business (FAP) offers. (publicly available information)
- Explain how you charge for your advice (fees) or if you receive commission from product providers for placing business with them.
- Include any known conflict of interests or incentives.
- Have an easy to understand '**About Us**' document and ensure all the required information under the new disclosure regulations is easy to find, clear and concise.

(This should be available on request and at no cost to the consumer. Have a PDF ready to send)

PPC example 1 cont.

2. Develop Processes and Procedures (tasks) continued.

- Explain to the client in the **first client meeting** the different types of advice offered.
- Explain if there any **fees or costs payable** for your services and how they are determined.
- Disclosure any **commissions payable** for placing business with product providers.
- Allow sufficient time in each client meeting to explain **other service** options.
- Ask for **feedback** to check the clients understanding.
- Identify clients having difficulty and put on your **vulnerable client** register.



PPC example 1 cont.



3. Develop Controls (check it is working)

- Complete a review of your **website, social media and documentation** to meet the new disclosure requirements (prior to 15 March 2021).
- Make sure all relevant information is included in your documents, website and social media.
- Review at least annually and record any issues/updates using version control.
- Check all client files have clear notes of meetings and discussions to evidence clients feedback and understanding of the nature and scope of advice.

PPC Example 2

Action 2- Explain what the ‘nature and scope of advice’ is and the consequences and risk of limitations.

1. Develop Policy statement - Promise to your clients.

“We support our clients by explaining carefully what advice with limitations looks like, and what the risks and consequences of these are. Our clients know what limitations are and why we prefer not to provide this advice.”

PPC Example 2 cont.



2. Develop Processes and Procedures (tasks)

- With client on-boarding , take time to identify, and document, the client's financial literacy.
- Allow sufficient time in each client meeting to explain the nature and scope of advice and the **implication of any limitations requested by the client.**
- Provide a clear **explanation of the nature and scope of advice and what limitations are** and how that affects the nature and scope of advice.
- Provide clear examples of **how limitations can be risky to the client**, especially if the risks and consequences of those limitations are not properly understood.

PPC Example 2 cont.



2. Develop Processes and Procedures (tasks) continued

- Provide clear examples of how **incomplete or incorrect client information** is a limitation with potential serious risks and consequences.
- Ask for **feedback** to check the client's understanding.
- When agreeing the scope and nature of the advice, explain what **options are available** to them.
- **Identify clients** having difficulty and put them on the vulnerable client register and look at support options to assist the client and their understanding.

PPC Example 2 cont.



3. Develop Controls (check it is working)

- Each fact-find should include information on the **client's financial literacy** (including comments on demonstrated financial knowledge)
- Ensure every **identified vulnerable client** is on the register with support and help
- Have a **customer survey** question about the client's understanding of advice given and whether they understand the nature and scope of the advice provided to them
- **Peer review** on random files to check the explanations around the nature and scope of advice to make sure they are easily understandable

PPC Example 3

Action 3 - Have documented evidence of the steps taken to ensure client understanding the nature and scope of the advice, along with the risks and consequences of any limitations.

1. Develop Policy statement - Promise to your clients.

“We will always make sure you understand the nature and limitations of our advice specific to your situation and we won’t rush your decision-making process.”

PPC Example 3 cont.



2. Develop Processes and Procedures (tasks)

Before asking the client to sign the nature and scope of advice document ensure that:

- a) every **client understands** the nature and scope of the advice.
- b) you have **identified the risks of limitations** and communicated these to the client.

All verbal explanations should be followed up with an email to the client and acknowledged by them in a return email, and kept on their client file in your CRM. (Record keeping best practice)

PPC Example 3 cont.



3. Develop Controls (check it is working)

- Use a **file checklist** to make sure you have obtained the relevant acknowledgements
- Check for any **noted concerns or questions** raised by the client regarding the scope and nature of advice and limitations.
- Check that **these have been followed up** and addressed also check for omissions and red flags
- Check client files for any **documented client concerns**, feedback and questions on the scope of advice (as evidence of client clarification and understanding).
- If there is no feedback or questions – check if this is a systemic omission and red flag

PPC - Example 4

Action 4 – Explain if there are any fees or costs associated with following the financial advice (product providers or platforms). Include any conflicts, if you receive any incentives, and how they are managed.

1. Develop Policy statement - Promise to my clients.

“We will spend time with you to ensure you understand any costs payable by you for following our advice and that the fees are acceptable to you.”

OR

“We may receive commission from the product providers that we place business with, therefore we do not charge you fees.”

“We disclose any conflicts of interest or incentives to you in our advice process to ensure the way we are remunerated is acceptable to you.”

PPC example 4 cont.



2. Develop Processes and Procedures (tasks)

Before asking the client to sign the nature and scope of advice document ensure that:

- a) Your clients understands if there are any **fees or costs associated** with taking your advice, including the amount (if known) how they are calculated, when they are payable and how they are paid.
- b) Your clients understand that you **may receive commission** from the product provider that you place their mortgage/insurance policy with. The range of this commission paid in percentages (amounts) and
- c) How any **conflicts of interest or incentives are managed** (if there are any).

PPC example 4 cont.

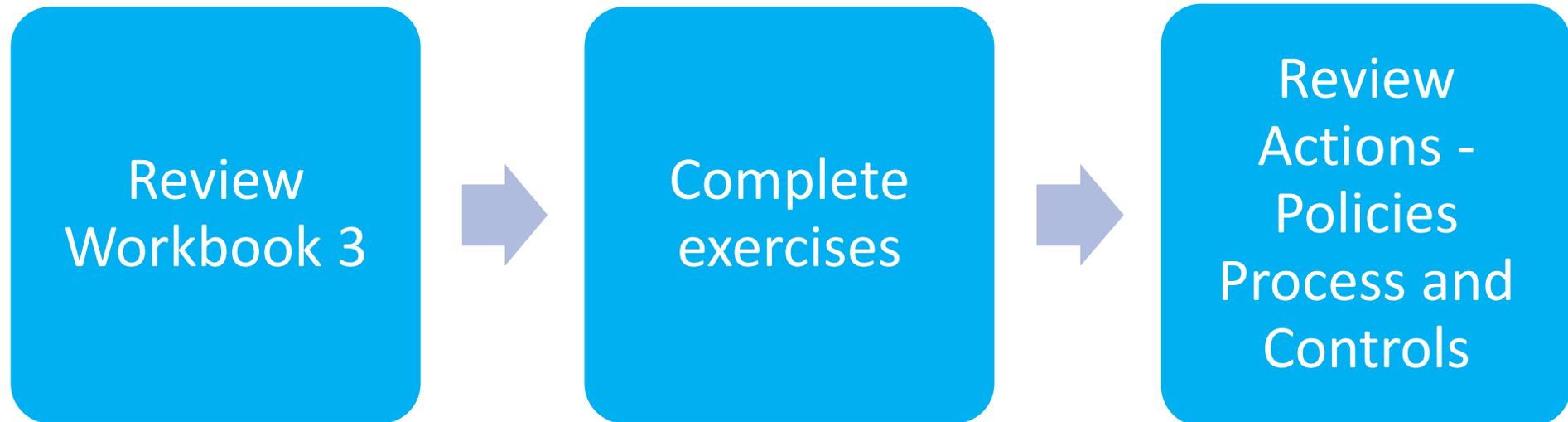


3. Develop Controls (check it is working)

Client file reviews:

- Check all client files have clear notes of meetings and discussions to evidence clients feedback and understanding of the nature and scope of advice, **including fees and commissions payable** or paid to the FAP or Financial Adviser.
- Checks the disclosure for any conflicts or incentives and how they are managed.
- Check all client files to ensure the Nature and Scope of Advice disclosure has been currently provided to the client and evidence in on each client file.

Next steps



Questions?



Webinar 4 – Wednesday 17th February

Workbook 4
Standard of Care Diligence and Skill.