NEW ZEALAND BANKERS ASSOCIATION

Submission

to the

Financial Markets Authority

on the

Consultation Paper: Exemption to enable personalised digital advice

19 December 2017

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About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes that contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.

2. The following seventeen registered banks in New Zealand are members of NZBA:

- ANZ Bank New Zealand Limited
- ASB Bank Limited
- Bank of China (NZ) Limited
- Bank of New Zealand
- Bank of Tokyo-Mitsubishi, UFJ
- China Construction Bank
- Citibank, N.A.
- The Co-operative Bank Limited
- Heartland Bank Limited
- The Hongkong and Shanghai Banking Corporation Limited
- Industrial and Commercial Bank of China (New Zealand) Limited
- JPMorgan Chase Bank, N.A.
- Kiwibank Limited
- Rabobank New Zealand Limited
- SBS Bank
- TSB Bank Limited
- Westpac New Zealand Limited

Background

3. NZBA welcomes the opportunity to provide feedback to the Financial Markets Authority (**FMA**) on the Consultation Paper: Exemption to enable personalised digital advice (**Consultation Paper**) and commends the work that has gone into developing the Consultation Paper.

4. If you would like to discuss any aspect of the submission further, please contact:

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Comments on the draft exemption notice

Definition of 'digital advice facility'

5. NZBA submits that the definition of 'digital advice facility' (**DAF**) should be amended as follows:

Digital advice facility means a digital facility that provides a personalised service to a client

6. A consequential amendment would also need to be made to cl 6 as follows:

> … in respect of that financial adviser service to the extent that the service is provided through a digital advice facility.

7. NZBA considers that this definition is appropriate because:

(a) Using a definition that directly connects 'digital' with the provision of a personalised service is the simplest way to capture the nature of digital advice not currently permitted under the Financial Advisers Act 2008 (**FAA**).

(b) Using the words 'personalised service' within the definition is not only simple, but it also gives providers certainty that the Exemption will not inadvertently capture existing digital services that providers believe are class services.

(c) Using the words 'digital facility' is broad enough to capture all non-human facilities providing advice, while also being sufficiently certain to operate as a gateway to the Exemption.

(d) The reference to 'a computer program using automated algorithms' is too narrow. It appears targeted towards instances where an end-to-end authorised financial adviser (**AFA**) personalised experience is replaced with a sophisticated computer algorithm. We believe this narrower definition will not enable providers to offer more basic personalised service offerings to their clients. Offering more personalised versions of current digital class services and/or relatively simple digital personalised services (that are not permitted under the current regime) will have the biggest impact by enabling customers access to financial advice through digital channels, thereby assisting them to make informed day-to-day financial decisions.

(e) Additionally, this definition accommodates hybrid business models where there is a collaboration between human and DAF; involvement of any kind by a human should not preclude reliance on the exemption. For example, personalised financial advice generated by a DAF which is transmitted by a human (see s 10(3) of the FAA) should be captured by the exemption (for the avoidance of doubt, the human in this scenario exercises no judgement in respect of the advice provided).

Definition of 'specified product'

8. The definition of 'specified product' should be amended to include:

(a) Units in cash or term PIEs or bank notice products (as defined in the Financial Advisers (Definitions, Voluntary Authorisation, Prescribed Entities, and Exemptions) Regulations 2011). These are all designated as category two products.

(b) Renewals or variations to the terms and conditions of existing specified products, as in s 5 of the FAA.

Clause 7: Provider must notify FMA of material change of circumstances

'Material change of circumstances'

9. Clause 7(3)(a) provides that a 'material change of circumstances' is 'a change that adversely affects the provider's ability to provide the financial adviser service through the digital advice facility in an effective manner'. We read that to mean that all adverse changes, regardless of whether they are *materially* adverse, will need to be reported. NZBA considers that requirement is too broad; there is a risk that any business interruption, however minor (for example the outage of a website), could necessitate a report. Accordingly, NZBA submits that cl 7(3)(a) should be amended so that only materially adverse impacts are required to be reported.

10. Additionally, NZBA seeks clarification of the meaning of "in an effective manner" as that phrase is used in cl 7(3)(a).

11. Finally, we suggest that the circumstances listed in cl 7(3)(b) should be restricted to matters that are linked to cl 7(3)(a) (ie they *materially* adversely affect the provider's ability to provide the DAF in an effective manner). That would align the clause with reg 191 of the Financial Markets Conduct Regulations 2014.

Timeframe for notification

12. Clause 7(1) provides that a provider relying on the exemption must notify FMA within five working days of a material change of circumstances. NZBA considers that a five working day timeframe is too short, relative to the consequences of non-compliance with the clause (that being expiry of the exemption).

13. We consider that the requirement should be revised so that it is consistent with the notification requirement for market services licensees under s 412 of the Financial Markets Conduct Act 2013 (**FMCA**). That section provides that a report must be made to FMA 'as soon as practicable' after the licensee has formed the belief that a material change of circumstance has occurred. NZBA submits that this requirement is more appropriate, as five working days may be too short to properly evaluate whether an issue constitutes a material change of circumstances.

14. Finally, NZBA considers that care must be taken to ensure that, where possible, requirements under the exemption align with and do not duplicate procedures and controls under existing licence regimes. For example, the requirement to notify FMA if a senior manager is subject to disciplinary procedures (or any other matter set out at cl 7(3)(b)) is unnecessary if a provider is already subject to another licensing regime administered by the FMA and will create an additional and superfluous administrative burden.

Consequences of a failure to notify

15. NZBA considers that cl 7 is inconsistent with other similar legislative requirements in that breach automatically triggers the loss of the benefit of the exemption.

16. Our understanding is that cl 7 is intended to facilitate supervision, rather than being related to the nature of the personalised advice service. Accordingly, NZBA considers that cl 7 should be amended so that breach will not cause the loss of the benefit of the exemption. Instead, FMA could take action by suspending or cancelling the exemption as a whole or for a particular DAF. This would be more consistent with the FMA's general enforcement approach.

Clause 8: Conditions of exemptions

17. The Consultation Paper proposes that personalised digital advice given in respect of category two products will be subject to the same standards as personalised digital advice given in respect of category one products. We appreciate this reflects the impending removal of the distinction between category one and category two products in the new FAA regime. However, we believe that pre-empting this change is likely to result in providers not providing financial advice through a DAF on category two products until the new regime comes into force. This would be unfortunate, as personalised digital advice for category two products appears to be a key area where customers might benefit from the additional assistance that personalised digital advice offers.

18. With respect to the record keeping requirements, NZBA seeks clarification of the following matters:

    (a) Is there an obligation to maintain a record of the matters set out at cl 8(a) and (b)?

    (b) The exemption does not provide a timeframe for record retention. NZBA considers that any timeframe should be consistent with the requirement contained in the Code of Conduct standards (**Code Standards**) (that being 7 years).

19. With respect to the application of the Conduct Standards, these standards currently apply to human-to-human interactions and it is hard to see how they will apply to the provision of personalised digital advice. We appreciate the thinking FMA have already given to this topic in light of the proposed exemptions. Nevertheless, NZBA recommends that, after the exemption is finalised, FMA issues guidance as to how a digital advice facility might meet those code standards. For example:

    (a) Code Standard 8, which requires customer agreement to the scope of services, will not apply. This is helpful. However, Code Standard 9 requires that the adviser '…must take reasonable steps to ensure the personalised service is suitable for the client, having regard to the agreed nature and scope of the personalised service provided'. NZBA seeks clarification as to whether FMA expects the provider and the customer to 'agree' a scope of services, notwithstanding the omission of Code Standard 8. If so, what might agreement look like in a digital context?

    (b) Some personalised digital advice activities might involve one-way interactions (as compared to AFA interactions with clients that are two-way). To satisfy Code Standard 6, the AFA must take reasonable steps to ensure that the client understands the communication. It will be helpful to discuss with FMA what constitutes 'reasonable steps' in the context of a one-way personalised digital advice interaction.

Schedule 1: Providers

20. NZBA queries whether it is necessary to list the names of approved providers of DAF at Schedule 1. This is likely to require frequent updates as more providers are granted exemptions, and therefore create an administrative burden. From a practical perspective, it makes more sense for this list to be published on the FMA website.

Schedule 2: Information to be disclosed

21. NZBA seeks clarity as to the meaning of the phrase “that a reasonable retail client would find to be reasonably likely to materially influence the provider in providing the service”.

22. NZBA also welcomes guidance on how the disclosure conditions can be satisfied in a way that has regard to the nature of the DAF, and what makes practical sense for the provider and the customer.

Other comments

23. NZBA submits that the exemption should also provide that there has not been a breach of the exemption where a failure to meet a condition is minor or technical only. This will avoid potential criminal liability arising from a breach of the underlying provision in the FAA due to a minor or technical failing on the part of the provider.

24. We consider that such a clause is appropriate from a general policy perspective, as well as from the perspective of encouraging providers to use the exemption.

Comments on the draft information sheet

25. The information sheet includes an example of a KiwiSaver open access tool.

26. First, this case study raises the question of whether the provider is providing personalised advice to “a readily identifiable client” (i.e. satisfying s 15(a) of the FAA), or advice on a class basis. Many open access tools (including those which provide advice in respect of KiwiSaver fund choice) are currently provided on a class advice basis. As currently worded, the case study could be read as implying that a tool of this sort necessarily involves providing personalised advice, and therefore that providers must rely on the exemption to continue offering similar tools. Accordingly, NZBA considers that the case study should use a scenario that is clearly a personalised advice scenario.

27. Secondly, the example assumes that Aaron is automatically identifiable as the same person if he uses the same open access more than once. Online identification is far more complicated than the example suggests.

28. Aaron is a readily identifiable client if Aaron is logged into a provider’s system in a manner that enables the provider to identify that it is Aaron. If Aaron does not log in, Aaron will be identified as a user, assuming the tool was configured to track and remember unique, anonymous visitors. If Aaron uses the same device but a different browser the user tag will be different. Even if Aaron uses the same device and same browser, unless he is authenticated, we could not be certain that it is Aaron, as it might be a different user using the same device.

29. If Aaron uses a system such as a customer app that does not tag users, or the tracking is cookie based and Aaron has turned off his cookies, Aaron would not be tagged (identifiable as a user) at all.

30. Tracking users (who do not authenticate themselves) and recording their usage (meta data) is becoming increasingly problematic from a local and international privacy law perspective because it is now far easier to reverse engineer what is initially intended to be anonymised data. Additionally, providers are coming under increased legislative pressure regarding how they collect, hold and use personal

information. Therefore, FMA should consider whether the customer benefit derived from the proposed reporting requirements is appropriately balanced against customers' preferences for less individualistic and intrusive tracking, and does not impose an additional unintended privacy law compliance burden.

31. We suggest that any required reporting be made in relation to identifiable individuals, as opposed to usage of a DAF (where we may not know who our user is). We also hope that the FMA's interpretation of what constitutes digital class advice will follow that taken in FMA's recent KiwiSaver Sales and Distribution Guidance.

Comments on the draft application form

32. Questions 3-8 of the application form require the provision of an FSP number and other identification documentation.

33. NZBA seeks clarification of how those questions should be completed for a provider that has a number of different entities forming a group. In particular, whether separate entities within a group are required to submit separate applications. That is because there may be instances where the applying entity is responsible for the provision of the personalised digital advice, but a customer of another entity within the group relies on the advice.

34. It is also unclear how the application process will sit alongside QFE obligations. It would appear that if an entity in a QFE Group applies for the exemption, the QFE is automatically responsible for the personalised digital advice given by that entity (see ss 76 and 77 of the FAA). However, the application form does not acknowledge this accountability. While Schedule 1 may require a list of entities that will provide a DAF, NZBA considers that the process should also take account of the QFE relationship in light of the FAA's requirements.

35. The application form also requires providers to list information about the type of products that it will provide advice on through their digital advice service. NZBA seeks to clarify how this will operate when a provider has not yet confirmed the range of products it will provide advice on. Additionally, to the extent that a provider contemplates the provision of advice on an additional product, will an additional exemption application be required?

36. Finally, the 'capability' section (page 18-19 of the Consultation Paper) appears to replicate information provided under the 'good character', 'risk management' and 'IT systems' sections on the application form. Accordingly, NZBA considers that section of the application form is surplus to requirements.

Comments on the draft application guide

37. The 'good character' section of the application guide indicates that existing licence providers do not need to provide forms for directors and senior managers where an entity has 'previously provided … good character declarations'. NZBA supports this approach, but notes that such declarations were only provided at licensing. Directors and senior managers appointed and notified to the FMA after a licence is obtained are not required to complete declaration forms. However, it would seem disproportionate to require additional information given they already hold positions in licensed entities.

38. NZBA also considers that flexibility in both minimum standards and risk management may cause confusion for providers that are required to obtain approval. NZBA considers that the minimum standards should apply to all providers equally as the same level of risk applies in each instance. However, we acknowledge (and agree) that risk management should be commensurate with the size and complexity of the provider.

39. Finally, the 'ongoing obligations' require that minimum standards are maintained, however, it is not clear how those minimum standards interact with cl 8 'conditions of exemptions'.

Other comments

40. NZBA notes that there is no time-frame for the processing of exemption applications by FMA; a timeframe is necessary to give applicants an opportunity to effectively plan go-to-market strategies.

41. Additionally, the guidance does not provide for a formal appeals process for exemption applications that are rejected or withdrawn.