MyFiduciary
Governance & Investment Support

The New Financial Advice Regulatory Regime and Fi360's Investment Governance Framework

Executive Summary

This paper discusses the new regulatory regime for retail financial advice in New Zealand. It provides information on how Fi360's Investment Governance Framework aligns with the new regulatory requirements.

Under the new regime financial advice is regulated by the Financial Markets Conduct Act 2013 and the amendments introduced by the Financial Services Legislation Amendment Act 2019. The new legislation comes into force on the 29 June 2020.

The new regime simplifies regulation by removing regulatory distinctions. It abolishes differences between types of advisers, 'class' or 'personalised' advice, and the category of financial products. It introduces universal duties, obligations and competency requirements. The new duties are set in the legislation, a new Code of Conduct as well as regulations. All Financial Advice Providers will need to be licensed by the FMA and registered with the Financial Service Providers Register.

The new regulations aim to ensure that consumers have access to quality financial advice. These legislative changes are in the context of increased public scrutiny in the financial advice industry and diminished consumer confidence. In our view, to strengthen the confidence of consumers in the financial industry, there needs to be a shift from the narrow focus of legal compliance. A move to higher fiduciary standards of practices and conduct can ensure better outcomes for all.

Fi360's investment governance framework can help advisers and financial advice providers meet many of the new duties and obligations. It requires following a structured process that is repeatable, defensible and documented. When adopting the Fi360 Practices advisers and clients can be assured that critical components of an investment strategy are properly implemented and followed.

As advisers are subject to financial services legislation as well as general consumer legislation, the Fi360 framework also aligns well with the requirements by other Acts such as the new Trusts Act 2019. For advisers who have clients in trusts arrangements, the new Trusts legislation places a general duty of care on trustees, as well as the duties to act honestly and in good faith and avoid conflicts of interest. The Fi360 Practices also help ensure advisers meet their duties and obligations when acting as a trustees, or when serving trustees.

Background to the Regulatory Changes

In April 2019 a new financial advice regime was introduced to improve the availability and quality of financial advice in New Zealand.[1] The new regime replaces the Financial Advisers Act 2008 (the FA Act) and Financial Service Providers (Registration and Dispute Resolution) Act 2008 (the FSP Act) that have been in force since 2011.

A review of these Acts found that there were several problems with the regulation of financial advice.[2] It found the regulatory regime unnecessarily complicated and that it did not adequately ensure an even level of competency standards and obligations for all advisers.

The FA Act made provision for different types of advisers (AFA, QFE and RFA), different types of advice and products they could provide, and different obligations. This created lots of complexities in the regime and several shortcomings were identified in the review:

- **Lack of clarity for consumers** - the system is difficult for consumers to understand. Consumers are unclear on what services the adviser can provide and what consumer protections apply. In addition, different disclosure requirements make it difficult for consumers to determine whether there is a conflict of interest in the advice or services they receive. The information provided in the disclosure requirements is often lengthy and too complex for clients.

- **Advice gaps** – regulatory boundaries and additional compliance in providing some types of advice has resulted in advice gaps. As an example, not all advisers are able to provide advice on KiwiSaver Providers to clients.

- **Imbalance of conduct and competency requirements** – there are different obligations and competency requirements for the different types of advisers. Consumers are not easily able to distinguish these differences. The competency requirements are not in line with the complexity of the financial products and services being offered to consumers.

The New Financial Advice Regulatory Regime

In the new regime the FA Act 2008 is revoked by the Financial Services Legislation Amendment Act, 2019 (FSLAA). This means the provision of financial advice will be regulated by the FMC Act (Financial Markets Conduct Act 2013) and the amendments introduced by the FSLAA. The new regime comes into effect this year in June.

The new legislation simplifies regulation by introducing universal duties, obligations and competency requirements for all who provide retail financial advice. The FSLAA also introduces a new objective for the regulation of financial advice that is to ensure its availability and quality.[3] There are three main areas of changes introduced by the FSLAA, these are:

[1] It also intends to ensure that there is no misuse of the Financial Service Providers Register (FSP Register).The Review of the legislation found that overseas firms with little or no connection to NZ get on the register and misrepresent themselves as Registered New Zealand Financial Service Providers and imply that they are subject to active regulation in NZ.
[2] The Ministry of Innovation Business and Employment undertook a review of the Act from 2015-2016.
[3] s431B FSLAA

1. **Access to advice:** Improve the access of consumers to all types of advice. The Act makes provisions for 'robo-advice' that will improve the accessibility of advice to consumers.

2. **Standards of conduct and competency:** All advice will be covered by a license. All advisers and firms giving advice must put clients first and comply with the new Code of Conduct.

3. **Improved consumer understanding:** It simplifies the regime by removing RFA, AFA, QFE and class advice distinctions. It introduces a duty on advisers to ensure consumers are informed and understand the nature and scope of advice. There will be new disclosure requirements to ensure clients can make informed decisions. [4]

The FSLAA defines financial advice as making a recommendation about financial products or designing an investment plan.[5] Recommendations on financial products typically include advice on equities, managed investments, insurance and credit contracts, while investment plan advice involves defining a plan based on the specific client's objectives and financial circumstances. The FSLAA also provides clarification as to what activities do not fall under the scope of regulated financial advice. This includes for example, carrying out an instruction or a general recommendation or opinion.[6]

The new legislation also makes the distinction between 'wholesale' clients and 'retail' clients. This is important as different levels of consumer protection and regulation apply. Wholesale clients are typically, businesses and institutional investors that are relatively large and presumed to be "sophisticated", while retail clients are everyday consumers.[7] The new licensing requirements do not apply for the provision of wholesale advice.

Financial Advice Providers and Licensing

The new legislation will affect all entities and individuals that provide retail financial advice. It removes the RFA, AFA, QFE and class advice distinctions. In the new regime, the person (or entity) who provides financial advice is a **financial advice provider** (FAP). All FAPs need to be licensed by the FMA and registered with the Financial Service Providers Register (FSPR). [8]

Financial advice providers will be able to provide advice via three ways:[9]

1. **Financial advisers:** these are individuals engaged by a FAP to provide financial advice on its behalf. Financial advisers will need to be registered on the FSPR.
2. **Nominated representatives:** these are individuals engaged by a FAP to provide advice on its behalf but have limited discretion and are tightly controlled by the firm.
3. **FAP's own behalf:** Financial advice providers which provide advice on their own account. Firms are also able to provide advise online via an online platform 'robo-advice'.

[4] The FMA says information that must be disclosed will be set in regulations. The new disclosure regulations will be available for consultation at the end of September 2019.
[5] s431C FSLAA
[6] s431C (3) FSLAA
[7] FSLAA Schedule 5, Part 1 defines wholesale client.
[8] Part 6 of the FMC Act
[9] s5 FMC Act

Financial advice providers will vary in size and composition, as these can range from large firms to a single adviser business. The types of FAPs can be:

- Sole adviser businesses or financial advice providers that only give advice on their own account. This can also be through a digital platform or robo-advice.
- Financial advice providers that engage multiple financial advisers but no nominated representatives.
- Financial advice providers that engage one or more nominated representatives (and may also engage financial advisers).

The FSLAA introduces a technology neutral regime as it allows for the provision of robo-advice (in the old regime financial advice could only be provided by a natural person). Entities providing robo-advice will need to have a Financial Service Provider license. This will ensure that the advice is regulated, and clients are afforded the same protections as if the advice had been provided by a natural person. The provision of robo-advice is hoped to improve cost-effectiveness and uptake of advice to consumers, particularly investors with low balances.

Universal Standards of Conduct and Competence

The new regime introduces universal conduct and client care duties. Anyone providing retail financial advice needs to operate under a FAP license, meet client care duties and comply with the Code of Professional Conduct for Financial Advice Services (the Code).[10]

The Code of conduct was approved in May 2019 and comes into force in June 2020. It sets minimum standards of ethical behaviour, conduct and client care, competence and, knowledge and skills. FAPs must ensure that all financial advisers and nominated representatives they engage meet their statutory duties.

The Code takes a principles-based approach, it provides for high-level standards which may vary in implementation depending on the different types of adviser business models. For example, the previous Code had a requirement for record keeping, but in the new code there is a standard to protect client information which has an implied process requirement of record keeping for the FAP.[11]

The Code is divided in two parts, the first sets out the standards for ethical behaviour, conduct and client care. The second part has the standards of competence, knowledge and skills.

FAPs have additional duties when they engage nominated representatives. FAPs are accountable for the advice provided by nominated representatives and must have the necessary processes and controls. [12] In addition, FAPs must ensure that the remuneration model for nominated representatives is not likely to be in breach of the statutory duties, especially the duty to put the client's best interest first.

[10] Part 4, s5 FMC Act. The Minister of Commerce and Consumer Affairs approved the Code of Conduct in May 2019.
[11] Refer to FMA website.
[12] s431P and s431Q FSLAA.

New Disclosure Requirements

Under the new regime there are new information disclosure requirements that apply.[13] These are important as they enable consumers to make informed decisions when choosing where to receive financial advice, and when making financial decisions.

In February 2019 the general disclosure requirements were agreed by Cabinet, while more detailed ones are set in regulations. The new draft regulations were released for consultation in October 2019.[14] Any firm or individual who gives regulated financial advice to retail clients will need to disclose the following information:[15]

- **Licensing:** information about the licence held by the financial advice provider.
- **Duties:** information about certain duties that the person giving advice is subject to.
- **Services:** information about the financial advice service that can be provided, including the financial advice products and product providers that can be advised on, and other limitations on the advice.
- **Fees:** information about the applicable fees and costs relating to the financial advice.
- **Conflicts of interest:** information relating to the commissions, incentives or other conflicts of interest that a client might perceive as having potential to materially influence the financial advice.
- **Complaints handling**: information about the complaints handling and dispute resolution arrangements.
- **Disciplinary history:** information about recent Financial Adviser Disciplinary Committee proceedings, where the disciplinary committee publicly notified the action.
- **Convictions or other proceedings:** information about recent criminal convictions, civil liability findings, or adverse findings from a court or other tribunal, if these would be perceived as relevant to a client's ability to rely on the advice.
- **Bankruptcy proceedings:** in the case of financial advisers, information about recent instances of being adjudicated bankrupt, or admitted to the no asset procedure

Regulation 5 of the draft Regulations introduces a new licence condition on the FAP to keep a record of each disclosure made in accordance with the information disclosure regulations. It will be possible for the information to be disclosed at different stages of the advice process, and when it becomes relevant do so. FAPs will also need to disclose general information on their website (or make it available to clients if there is no website) that includes license information, dispute resolution arrangements, and the scope of the advice they can provide.[16]

[13] s431O FSLAA.
[14] Exposure Draft, Financial Markets Conduct (Regulated Financial Advice Disclosure) Amendment Regulations, October 2019.
[15] MBIE Summary of disclosure requirements in the financial advice regime, March 2019.
[16] The new regulations prescribe information that must be disclosed under s431O, regulation 229A, 229B, 229H and Schedule 21A.

Fi360's Investment Governance Framework and the New Regime

The new regulatory regime is in the context of increased scrutiny of the financial services industry in New Zealand. The public's trust and confidence in the sector have suffered due to several high-profile cases in the media, endemic problems with the remuneration models for advisers and regulation that has not adequately protected consumers' interests.

This paper advocates that to strengthen the confidence of consumers in the financial market industry, there needs to be a shift from the narrow focus of legal compliance. A move to higher fiduciary standards of practices and conduct mean that businesses and consumers can reap greater benefits. This paper explores how Fi360's investment governance framework, and the recently updated Handbook 'Prudent Practices for Investment Advisers', aligns with the duties and obligations of the new regime. The new regime takes a principles-based approach, where regulation is stated in broad principles rather than detailed rules. The benefit of this is that it might encourage the adoption of higher standards of investment governance, as opposed to compliance confined to a set of minimum standards codified in legislation.

Investment governance is a specialised discipline focusing on the legal duties of care and loyalty (fiduciary obligations) owed by investment fiduciaries. Investment fiduciaries are usually people who either give investment advice or oversee the assets of another party and who stand in a special relationship of trust, confidence and legal responsibility. Advisers, as professionals who are responsible for providing investment advice and or managing investment decisions, are typically in a fiduciary role.

Investment governance seeks to define what investment advisers should do and the systems and processes they should have in place to fulfil their fiduciary obligations. It involves working to a defined, objective fiduciary standard, and being able to demonstrate that this is consistently and effectively applied.

Fi360 Pacific provides education and training in investment governance best practices with reference the global fiduciary standard devised by Fi360 (Inc) in the United States and Fi360 Pacific in New Zealand (a sister company to MyFiduciary Limited). The Fi360 Pacific Adviser Handbook has 20 Prudent Practices that form the framework of a disciplined investment process. The Practices are supported by 77 Criteria, that represent the details of the fiduciary standard of excellence (see Appendix 1 for a table of the Practices).

The adoption of good investment governance by firms and advisers helps ensure good decision making, risk management and compliance, as well add value to consumers. Investment Governance can be a driver for excellence, it is guided by the duties of care, loyalty and the commitment of placing the interests of clients first.

This paper looks at how the Fi360 framework aligns with the duties and requirements set out in the new regulatory regime.

Fiduciary Duties of Loyalty and Care

The standards of ethical behaviour, conduct and client care are specified in the FSLAA and the Code. All providers of retail financial advice have a duty to:[17]

- exercise care, diligence, and skill; and
- comply with the Code of Conduct.

The Code sets additional standards of conduct and ethics, these are to treat clients fairly and act with integrity. The Fi360 standard aligns well with these regulatory requirements as it establishes the baseline processes addressing loyalty and care to the client. These fiduciary duties translate into practical and specific requirements. The duty of care requires the adviser to implement investment recommendations and diligently manage assets in the best interest of the client, including prudent selection and monitoring of investments and service providers.

The Fiduciary duties of loyalty and care also help guide advisers in instances when a client agreement, service contract, or the law is silent on a specific obligation. For example, in a situation of a compensation conflict, the duty of loyalty requires the adviser to avoid the conflict or manage it in the best interest of the client. This highlights the benefit of adopting a standard that places more emphasis in the ethics of financial conduct and how it can result in better outcomes for clients.

The fiduciary duty of care is also referred to as the 'prudent person principle', it elevates the obligations of advisers to be the same as to those who are experts in the field. Advisers must understand the obligations that apply to their clients (Practice 1.1). This requires advisers to always serve the client's best interests by staying current with developments in the field, changing economic, market and social conditions, technology, and the body of knowledge in the profession. This is also relevant to Part 2 of the Code that places competence, knowledge and skills standards.

Duty to Give Priority to Client's Interests

The duty to give priority to client's interests is underpinned in many of the new obligations and requirements of advisers and FAPs.[18] It is a duty under the FSLAA, the licensing requirements, Standard 2 of the new Code and the new information disclosure requirements.

This aligns well with Fi360's framework as one of its fundamental precepts is to "avoid or manage conflicts of interest in favour of the client". This is supported by Practice 1.4 "the adviser identifies conflicts of interest and addresses conflicts in a manner consistent with the duty of loyalty". Fiduciaries must always act in the best interest of their clients. They must be objective and diligent in the performance of their duties on behalf of the client.

Fi360 has four criteria for dealing with conflicts of interest, these are:

1. To have policies and procedures for overseeing and managing conflicts of interest, including self-dealing and making false or misleading statements (criteria 1.4.1).
2. Conflicts of interests are avoided when possible (criteria 1.4.2).

[17] s4341K and s431L.
[18] s431J FSLAA.

3. Where a conflict does exist, it must be managed in the best interest of the client (criteria 1.4.3).
4. Conflicts of interests that are not avoided must be disclosed to the client and informed client consent must be obtained (criteria 1.4.4).

In the Fi360 standard, it is critical for the adviser to be aware of material conflicts of interest, recognise that the conflicts associated with each client may be unique, and evaluate how each conflict should be handled. The adviser should examine the nature and scope of each conflict, decide if it is a material conflict, and respond accordingly. A conflict is material if awareness of the conflict would reasonably be expected to influence the adviser's decision-making or advice.

Where possible the preferred course of action is to avoid a conflict of interest, in situations where conflicts cannot be avoided disclosure is required. It is important to ensure that in any disclosure the clients are sufficiently informed about the facts of the conflict and understand them.

Conflicts of interests regarding compensation can be complex. It is not merely the receipt of commissions by an adviser that gives rise to a conflict but how the adviser is paid (i.e. non-level compensation) can compound the conflict. For example, if the fiduciary adviser is also able to sell related products or services to the clients in a non-fiduciary capacity. Potential for material conflict will also tend to exist in any FAP that is "vertically integrated" across the investment supply chain, i.e. a business that offers any combination of advice plus brokerage services, funds management or custodial services. The Fi360 standard provides such a FAP with an objective way to show that these conflicts are avoided or well-managed in the interest of the end client.

Ethical Behaviour, Conduct and Client Care Duties in the Code

Part 1 of the Code provides for the ethical behaviour, conduct and client care duties for advisers. There are 5 Standards in Part 1, these are:

1. Treat clients fairly;
2. Act with integrity;
3. Give financial advice that is suitable;
4. Ensure that the client understands the financial advice; and
5. Protect client information.

It is interesting to note that some of these requirements on FAPs and advisers are in line with existing statutory requirements by other Acts such as the new Trusts Act 2019 and general consumer legislation. Part 2, of the FMC Act makes provision for 'fair dealing' in relation to financial products and services. These provisions mirror the provisions of the Fair Trading Act 1986 and expressly prohibit deceptive or misleading conduct. While the new Trusts Act places a general duty of care on trustees, as well as the duties to act honestly and in good faith and avoid conflicts of interest.[19]

Many of the Fi360 Practices that apply to the ethics and conduct of Standard 1 and 2, have already been discussed in this paper under the fiduciary duties of loyalty and care. Additional details on the Fi360 Practices and Criteria that are relevant to Standard 1 and 2 can be found in Appendix 2.

[19] Refer to Fi360 Paper *The New Trusts Act and What Trustees Need to Know* for more information.

Give financial advice that is suitable

In Standard 3, advisers must ensure that the "financial advice is suitable for the client" and "should include having reasonable grounds for the financial advice".[20] Implied in this duty is that all providers of retail financial advice, must exercise the same level of care, diligence and skill of a professional person in the financial advice field. The standard of prudence is the same as what would be considered appropriate of a professional in the investment industry. The commentary on Standard 3, lists some of the matter's advisers should take into consideration when providing advice. These at least include:

- Any Strategy supporting the advice,
- Assumptions underlying the financial advice,
- Any financial advice product covered by the financial advice; and
- The client's circumstances that are relevant to the financial advice, such as client's financial situation, needs, goals and risk tolerance.

Fi360's governance framework requires advisers to define an investment strategy for each client. The appropriate time horizon and risk level must be identified for each investment objective of the client (Practice 2.1). There are several Fi360 Precepts (requirements common to various laws governing fiduciary responsibility) and Practices that are relevant to this Standard. In particular:

- Diversify assets to specific risk/return profile (Precept 2).
- An investment time horizon has been identified for each investment objective of the client (Practice 2.1).
- An appropriate risk level has been identified for the portfolio (Practice 2.2).
- The distribution of projected portfolio returns is evaluated in the context of the client's risk and return objectives (Practice 2.3).
- Selected asset classes are consistent with the portfolio's time horizon and risk and return objectives (Practice 2.4).
- Use "prudent experts" for example, an investment manager, and document due diligence (Precept 4).
- Monitor service providers and prudently manage service provider relationships (Precept 7).

These Practices help advisers meet their new obligations and ensure they assess client's circumstances and objectives. Within this framework advisers need to follow a process, as well as define and adopt an investment strategy that meets the client's needs and objectives.

Ensure that the client understands the financial advice

Section 431J of the FMC Act provides that a person must not give financial advice unless the person has taken reasonable steps to ensure that the client understands the nature and scope of the advice. While in Standard 4 of the Code advisers must "ensure that the client understands the financial advice". This is important as financial advice needs to enable consumers to make informed decisions. Clients need to understand risks, costs and returns associated with potential investments.

[20]Code of Professional Conduct, commentary of Standard 3.

This ensures they have confidence as consumers to implement a recommended strategy and buy suitable financial products to meet their objectives.

Under the Fi360 standard, this means preparing an Investment Policy Statement (IPS) for the client (Precept 3). For a client the IPS should reflect their goals, directives, resources, and unique circumstances. The IPS is the essential management tool for directing and communicating the activities of the portfolio. The IPS provides a logical and consistent framework for the adviser to manage the client's investments. It should contain all material facts, assumptions, and objectives. Typically, it contains the factors that may impact the investment, for example:

- Cash flow considerations;
- Current and expected future assets;
- Investment experience and expertise;
- Limits and directives imposed to use or avoid certain types of investments or investment strategies and tactics; and
- Risk tolerance and capacity.

The IPS needs to contain enough detail to define, implement, and monitor the portfolio's investment strategy (Practice 2.6). Advisers also need to define, document, and consistently apply sound due diligence to select or recommend investment strategies, products, platforms, and other service providers. This also includes custodial selection, which is an important fiduciary function.

Protect Client Information

The Code has the standard that "a person who gives financial advice must take reasonable steps to protect client information against loss and unauthorised access, use, modification, or disclosure" (Standard 5). Advisers and FAPs also need to comply with the Privacy Act 1993, however, for the purposes of retail financial advice personal information is defined in broader terms than its definition under the Privacy Act.[21] Client's information should only be used for the purposes of providing financial advice and clients must have confidence that this is the case.

The Fi360 standard requires advisers have procedures in place to ensure all client information is secure (Practice 1.6). This includes having a framework for managing cyber security risks. The Fi360 criteria that support this practice include:

- Appropriate procedures are in place to secure and prudently protect the privacy of client or plan data (Criteria 1.6.2).
- Appropriate procedures are in place to assure that sensitive personal identifying information and assets of clients are prudently protected from physical, operational, virtual, and other material risks associated with business disruptions (Criteria 1.6.3).
- Documents pertaining to the investment management process, including records of decisions made by fiduciaries and clients, are secure and readily and reliably accessible by authorised persons (Criteria 1.2.2).

[21] Refer to commentary of Standard 5.

The Code's Standards of Competence, Knowledge and Skills

Advisers must meet the competence standards and continuing professional requirements as set out in Part 2 of the Code. These are:

1. Have a general competence, knowledge, and skill (Standard 6);
2. Have Particular competence, knowledge, and skill for designing an investment plan (Standard 7)[22];
3. Have particular competence, knowledge, and skill for product advice (Standard 8); and
4. Keep competence, knowledge, and skill up-to-date (Standard 9).

There is a competency exception of 2 years (competency safe harbour). This is a two-year period for existing advisers to meet the Code's competency requirements. The transitional period ends in June 2022.

The Fi360's precepts, practices and criteria serve as a guide to investment governance responsibility and as a standard of competence for advisers and fiduciaries in this field. Fi360's precepts and practices do not replace the specific NZQA requirements in the Code. There is a difference between investment expertise and investment governance expertise.

Fi360's investment governance framework is about having best practices in investment management. It requires following a structured process that is repeatable, defensible and documented. When adopting the Fi360 Practices advisers and clients can be assured that critical components of an investment strategy are properly implemented and followed.

The Fiduciary File and Record Keeping

Record keeping by financial advice providers is a licence condition for transitional licences.[23] Record keeping is a requirement under the current Code of Professional Conduct for Authorised Financial Advisers (the existing code). However, this has not been included as a standard under the new Code. The FMA takes the view that record keeping is a process requirement that should apply to the licensed business. The record keeping standard for transitional FAP license states that:

> *Records will be adequate if they clearly demonstrate (together with your systems, process and controls) how you, and any person engaged by you, and the regulated financial advice given to your retail clients by you or on your behalf, met the requirements relating to financial advice and financial advice services in the Financial Markets Conduct Act 2013, the Financial Markets Conduct Regulations 2014 and the Code of Professional Conduct for Financial Advice Services. Your records should include a record of all regulated financial advice given to retail clients by you or on your behalf. Records may be kept by another person on your behalf providing you ensure that person complies with this condition.*

Relevant to this condition is Fi360 Practice 1.2.2. It requires an adviser to keep a 'fiduciary file' to safe-keep and organise documents pertaining to the client's investment management process in a centralised location.

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[22] This is an interim standard. The Code Committee will consult in the future on the requirement of higher qualifications.
[23] This is a proposed condition from the FMA Consultation paper: Proposed standard conditions for financial advice provider transitional licences.

Documents in the fiduciary file will generally at least include:

- Applicable governing documents and trust deeds;
- Records of decisions made by fiduciaries and clients;
- The investment policy statement (IPS);
- Client engagement agreement;
- Service agreements with custodian, investment managers, consultants, etc;
- Due diligence files;
- Investment performance reports;
- Committee meeting minutes;
- Custodial and brokerage statements;
- Regulatory disclosure requirements; and
- Marketing materials and advertisements (including references or links to the firm's website and commentary in social media).

In this Practice documents must be secured and readily and reliably accessible by authorised persons. Good practice we observed by firms who meet the 'fiduciary file' requirement, which could be followed by a FAP, is the implementation of a robust CRM system that also meets the cyber security and information privacy requirements discussed above.

The adviser must take care to collect, organise, and analyse all documents that are relevant to the management of the portfolio and the advisor's responsibilities. A client engagement agreement between the adviser and an individual investor, sets the parameters for the relationship and how investments are to be managed, while the Investment Policy Statement details the process to be followed for sound portfolio management.

Conclusion

In the new regulatory regime, Fi360's investment governance framework can help advisers and financial advice providers meet many of their new duties and obligations.

The new legislation aims to simplify and improve the regulation of retail financial advice in New Zealand. It is a principles-based regime where regulation is stated in broad principles rather than detailed rules. However, given the scope and complexity of financial advice regulation, the new regime does set out some fixed duties, obligations and conditions. The new Code sets out principles and guidance on conduct, ethics and competence. While other conditions and requirements are set in the licensing and regulations. At the time of writing, not all the rules had been finalised by the FMA, and public consultation is still ongoing.

The introduction of the new regime provides advisers and firms with the opportunity to assess and evaluate their compliance, processes and practices. We advocate for the adoption of higher standards of investment governance, as opposed to stringent compliance.

The Fi360 Practices provide a consistent framework to help advisers achieve compliance and adopt best professional practices. This is both through training and firm-level accreditations on the standard. The latter is awarded by the Centre For Fiduciary Excellence (CEFEX), based in Toronto,

Canada. Good investment governance practices both increase the likelihood of improved investment outcomes and lessen potential reputational and liability risks.

Appendix 1

Fi360's Prudent Practices and Criteria for Investment Advisers

The Fi360 Pacific Adviser Handbook has 20 Prudent Practices that form the framework of a disciplined investment process. The Practices are supported by 77 Criteria, that represent the details of the fiduciary standard. These are organised under the Fi360 4-step process: Organise, Formalise, Implement, and Monitor.

Step 1: Organise	
Practice 1.1	**The adviser demonstrates an awareness of fiduciary duties and responsibilities (twin duties of loyalty and care).**
Criteria	1.1.1 The investment adviser complies with all laws and rules that apply to the services the adviser is providing. 1.1.2 The investment adviser complies with all applicable Practices and Procedures defined in the Prudent Practices handbook. 1.1.3 The investment adviser adheres to all applicable standards of conduct and code(s) of ethics required by law, regulation, employers, and professional organisations.
Practice 1.2	**Investments and investment services provided are consistent with governing documents.**
Criteria	1.2.1 Investments are managed, and investment services are provided in accordance with governing documents, including documents establishing the terms of an account or client engagement and the investment policy statement. 1.2.2 Documents pertaining to the investment management process, including records of decisions made by fiduciaries and clients, are secure and readily and reliably accessible by authorised persons.
Practice 1.3	**The roles and responsibilities of all involved parties whether fiduciaries or non-fiduciaries are defined and documented.**
Criteria	1.3.1 All involved parties have acknowledged their roles and responsibilities and fiduciary or non-fiduciary status in writing. 1.3.2 Each investment committee formed, controlled, or required by the investment adviser has a defined set of by-laws or operating procedures to which the committee adheres.

Practice 1.4	**The investment adviser identifies material conflicts of interest and avoids or manages conflicts in a manner consistent with the duty of loyalty.**
Criteria	1.4.1 Policies and procedures for overseeing and managing conflicts of interest, including to avoid self-dealing and making false or misleading statements, are defined and followed. 1.4.2 Conflicts of interest are avoided when prohibited by law and/or governing documents. 1.4.3 Conflicts of interest that are not avoided must be managed in the client's best interest. 1.4.4 Conflicts of interest that are not avoided must be disclosed to the client and informed client consent must be obtained.
Practice 1.5	**Agreements under the supervision of the investment adviser are in writing and do not contain provisions that conflict with fiduciary obligations.**
Criteria	1.5.1 The investment adviser fully discloses in writing all compensation arrangements and affiliations associated with the service agreement. 1.5.2 If the investment adviser is responsible for oversight of other service providers, the adviser must evaluate all material compensation, affiliations, and the fiduciary status of each service provider. 1.5.3 Agreements are periodically reviewed to ensure consistency with the needs of the client. 1.5.4 Comparative reviews of service agreements for which the investment adviser is responsible are conducted and documented approximately every three years.
Practice 1.6	**Sensitive personal identifying information and assets of clients are prudently protected from theft, embezzlement, and business disruption risks.**
Criteria	1.6.1 The investment adviser has a reasonable basis to believe assets are within the jurisdiction of a viable judicial system. 1.6.2 Appropriate procedures are in place to secure and prudently protect the privacy of client or plan data. 1.6.3 Appropriate procedures are in place to assure that sensitive personal identifying information and assets of clients are prudently protected from physical, operational, virtual, and other material risks associated with business disruptions. 1.6.4 The investment adviser has a reasonable basis to believe assets are protected by appropriate insurance, bonding, internal controls, and security measures taken by fiduciaries and other service providers, including the investment adviser's own firm. 1.6.5 The investment adviser has procedures in place to manage situations where the adviser reasonably believes that a client's assets are at risk due to suspicious behaviour by service providers, the client, or others with access to or influence over the client's assets. 1.6.6 The investment adviser has documented a succession plan and a business continuity plan that is reviewed and tested periodically.

Step 2: Formalise	
Practice 2.1	**An investment time horizon has been identified for each investment objective of the client.**
Criteria	2.1.1 Sources, timing, distribution, and uses of each client's cash flows are documented. 2.1.2 In the case of an individual investor, an appropriate asset/liability study has been factored into the time horizon. 2.1.3 In the case of a defined benefit retirement plan, an appropriate asset/liability study has been factored into the time horizon. 2.1.4 In the case of a defined contribution retirement plan, the investment options provide for a reasonable range of participant time horizons. 2.1.5 In the case of a foundation or endowment, a schedule of expected receipts and disbursements of gifts and grants has been factored into the time horizon to the extent possible and an estimated equilibrium spending rate has been established.
Practice 2.2	**An appropriate risk level has been identified for the portfolio.**
Criteria	2.2.1 The expected volatility of the portfolio is understood by the investment adviser and communicated to the client, and the quantitative and qualitative factors that were considered are documented. 2.2.2 "Large loss" scenarios have been identified and considered in establishing the portfolio's risk level. 2.2.3 Expected disbursement obligations and contingency plans have been considered when establishing liquidity requirements for the portfolio and assessing the capacity to assume portfolio risk. 2.2.4 In the case of a defined contribution retirement plan, the investment options provide for a reasonable range of participant risk tolerance levels.
Practice 2.3	**The distribution of projected portfolio returns is evaluated in the context of the client's risk and return objectives.**
Criteria	2.3.1 The projected portfolio return is consistent with the client's tolerance and capacity to assume volatility risk and investment goals and objectives. 2.3.2 Projected return assumptions for each asset class are based on reasonable risk-premium assumptions. 2.3.3 For defined benefit plans, the projected return values used for modelling are reasonable and are also used for actuarial calculations 2.3.4 For defined contribution plans, the projected return assumptions for pre-diversified options, such as target date funds or model portfolios, are based on reasonable risk/premium assumptions. 2.3.5 For endowments and foundations, the projected return values used for modelling are reasonable and are consistent with distribution requirements or the projected equilibrium spending rate.

Practice 2.4	**Selected asset classes are consistent with the client's time horizon and risk and return objectives.**
Criteria	2.4.1 Asset classes are appropriately weighted to conform to the portfolio's specified time horizon and risk/return profile. 2.4.2 For participant-directed plans, selected asset classes provide each participant the ability to diversify their portfolio appropriately given their time horizon and risk/return profile. 2.4.3 The methodology and tools used to establish appropriate portfolio diversification are prudent and consistently applied.
Practice 2.5	**Selected asset classes are consistent with implementation and monitoring constraints.**
Criteria	2.5.1 The investment adviser has the time, resources, knowledge and skills to implement and monitor all selected asset classes. 2.5.2 The process and tools used to implement and monitor investments in the selected asset classes are appropriate. 2.5.3 Appropriate investment products are accessible within each selected asset class.
Practice 2.6	**The investment policy statement contains sufficient detail to define, implement, and monitor the portfolio's investment strategy.**
Criteria	2.6.1 The investment policy statement identifies the bodies of law governing the portfolio. 2.6.2 The investment policy statement defines the duties and responsibilities of all parties involved. 2.6.3 The investment policy statement specifies risk, return, and time horizon parameters. 2.6.4 The investment policy statement defines diversification and rebalancing guidelines consistent with risk, return, and time horizon parameters. 2.6.5 The investment policy statement defines the due diligence criteria for selecting investment options. 2.6.6 The investment policy statement defines procedures for controlling and accounting for investment expenses. 2.6.7 The investment policy statement defines monitoring criteria.
Practice 2.7	**Investment due diligence using environmental, social, and governance (ESG) factors conforms to governing documents and the fiduciary obligations of investment decision-makers.**
Criteria	2.7.1 The client's goals, objectives, and investment parameters are evaluated to determine whether ESG investing is necessary and/or desirable. 2.7.2 Provisions regarding ESG investing in governing documents are aligned with fiduciary obligations.

Step 3: Implement	
Practice 3.1	**A prudent due diligence process is followed to select each service provider.**
Criteria	3.1.1 Prudent criteria are identified for each due diligence process used to select service providers. 3.1.2 The due diligence process used to select each service provider is documented. 3.1.3 Each due diligence process used to select service providers is consistently applied.
Practice 3.2	**Decisions regarding investment strategies and types of investments are made in accordance with fiduciary obligations and are documented.**
Criteria	3.2.1 A prudent due diligence process is used to select investment strategies, investment managers, and investments. 3.2.2 Decisions regarding the selection of investments consider both qualitative and quantitative criteria. 3.2.3 The due diligence process used to select investment strategies, investment managers, and investments is documented and consistently applied. 3.2.4 Regulated investments are preferred over unregulated investments when all other characteristics are comparable. 3.2.5 Investments that are covered by readily available data sources are preferred over similar investments for which limited coverage is available when all other characteristics are comparable. 3.2.6 A prudent due diligence process is used to make decisions regarding the use of proprietary versus non-proprietary products, and separately managed versus commingled accounts. 3.2.7 Decisions regarding rollover advice are made in accordance with fiduciary duties of loyalty and care.
Step 4: Monitor	
Practice 4.1	**Periodic reviews compare investment performance against appropriate market and peer group benchmarks and overall portfolio objectives.**
Criteria	4.1.1 Investment performance of the overall portfolio is compared against an appropriate benchmark and evaluated in the context of portfolio objectives. 4.1.2 The performance of each investment option is periodically compared against an appropriate market and peer group benchmark and any other performance-related due diligence criteria defined in the investment policy statement. 4.1.3 Underperforming investments are monitored and decisions to retain or replace investments are documented. 4.1.4 Rebalancing procedures are reasonable, documented, and consistently applied. 4.1.5 Investment performance is periodically reported to the client.

Practice 4.2	**Periodic reviews are made of qualitative and/or organisational changes of investment managers and other service providers.**
Criteria	4.2.1 Periodic evaluations of the qualitative factors that may impact the results or reliability of investment managers are performed. 4.2.2 Negative news and other material information regarding an investment manager or other service provider are considered and acted on in a timely manner. 4.2.3 Deliberations and decisions regarding the retention or dismissal of investment managers and other service providers are documented. 4.2.4 Qualitative factors that may impact service providers are considered in the contract review process.
Practice 4.3	**Procedures are in place to periodically review policies for trading practices and proxy voting.**
Criteria	4.3.1 Procedures are in place to periodically review each investment manager's policies for best execution. 4.3.2 Procedures are in place to periodically review each investment manager's policies for special trading practices such as "soft dollars", directed brokerage, and commission recapture. 4.3.3 Procedures are in place to periodically review each investment manager's policies for proxy voting.
Practice 4.4	**Periodic reviews are conducted to ensure that investment-related fees, compensation and expenses are fair and reasonable for the services provided.**
Criteria	4.4.1 Procedures are in place to periodically review each investment manager's policies for best execution. 4.4.2 Procedures are in place to periodically review each investment manager's policies for special trading practices such as "soft dollars", directed brokerage, and commission recapture. 4.4.3 Procedures are in place to periodically review each investment manager's policies for proxy voting.
Practice 4.5	**There is a process to periodically review the organisation's effectiveness in meeting its fiduciary responsibilities.**
Criteria	4.5.1 Fiduciary assessments are conducted at planned intervals to determine whether appropriate policies and procedures are in place to address all fiduciary obligations and that such policies and procedures are effectively implemented and maintained. 4.5.2 The investment policy statement is reviewed at least annually to ensure it is aligned with current facts and circumstances.

Fi360's Global Fiduciary Precepts

These are based on the common requirements of the laws that define fiduciary obligations
1. Know standards, laws, and trust provisions. 2. Diversify assets to specific risk/return profile of client. 3. Prepare investment policy statement. 4. Prudently select fiduciary and non-fiduciary service providers and document due diligence. 5. Control and account for investment expenses and other costs. 6. Avoid or manage conflicts of interest in favour of the client. 7. Monitor service providers and prudently manage service provider relationships. 8. Monitor and ensure conformity to fiduciary obligations owed to clients and beneficiaries