

New Zealand Law Society

Submission on Financial Service Providers (Pre-Implementation Adjustments) Bill and amendments proposed in Supplementary Order Paper No 113

1. Introduction

- 1.1 The New Zealand Law Society ('**Law Society**') welcomes the opportunity to present submissions on the above Bill. The Law Society would like to be heard in support of its submissions.

2. Exemption for lawyers

- 2.1 It is submitted that lawyers should be exempted from the operation of the Financial Advisers Act 2008 ('**FAA**').
- 2.2 Lawyers are already fully regulated under the Lawyers and Conveyancers Act 2006 ('**LCA**') and the regulations and rules made under the LCA.
- 2.3 The legal profession has in place numerous public protection safeguards which are by no means fully replicated in any other profession or occupation group. Some of these are set out below.
- The fundamental obligations imposed on all lawyers by s 4 LCA include the following:
 - (a) to be independent in providing services to clients; and
 - (b) to act in accordance with all fiduciary duties and duties of care owed by lawyers to their clients.
 - Rule 3 of the *Lawyers and Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008* ('**RCCC**') states that a lawyer must always act competently. Accordingly, a lawyer who provides financial services must at all times do so competently.
 - The RCCC comprises a detailed set of rules of conduct and client care which are binding on all lawyers. A copy of these rules is **attached**.
 - Lawyers have fiduciary obligations to their clients which exceed the duties of other professional or occupation groups, including financial advisers.
 - As required by the LCA, the Law Society maintains a Lawyers Complaints Service which operates on a user friendly basis. Complaints are considered by Standards Committees comprising lawyers and at least one lay person. Standards Committees are able to impose a wide range of orders, including orders to:
 - (a) reduce or cancel fees;
 - (b) pay compensation;

- (c) rectify at the lawyer's own expense any error or omission;
- (d) pay a fine.

A complainant may apply to the Legal Complaints Review Officer (an independent Government-appointed person) to review a Standards Committee decision.

- The Law Society operates a comprehensive financial assurance scheme. Compliance with trust account rules is monitored and enforced by a team of Law Society inspectors supplemented by a number of chartered accounting firms.
- The Law Society maintains a fidelity fund which reimburses clients in the event of any theft.
- The Law Society has a continuing legal education division which, among other things, conducts travelling seminars. The seminars cover a wide range of topics. Seminars directed to the provision of financial services can readily be included in this programme.

- 2.4 The obligations of financial service providers would do little other than replicate those already applying to lawyers under their regulatory regime.

This is graphically illustrated by the consultation draft *Code of Professional Conduct for Authorised Financial Advisers*. The obligations of lawyers under the LCA and RCCC meet and in most cases exceed those under standards 1 to 18 of the draft *Code*.

Standards 19 to 21 which address qualifications of authorised financial advisers are understandably not currently replicated in the RCCC. However, the Law Society could readily bring down rules harmonising these requirements for lawyers who provide financial services.

- 2.5 It is inappropriate for lawyers to be subject to two separate regulatory regimes. This would confer little or no benefit on anyone, would cause confusion and add to compliance costs which would ultimately be met by the public.

- 2.6 It would also be unreasonable for lawyers to be subject to two separate complaints and discipline regimes under the Financial Advisers Act ('FAA') and the LCA. This would permit individuals to lodge complaints under either or both regimes. Lawyers should not be exposed to this dual process.

- 2.7 Accordingly, the Law Society submits that:

- (a) s 12(d) of the FAA be amended by omitting the words 'if the advice or decision is a necessary incident of legal practice'; and
- (b) s 77C(a) as set out in the Supplementary Order Paper be amended by omitting the words 'if the broking is a necessary incident of legal practice'.

3 Lawyers involved in contributory mortgage lending

- 3.1 If for any reason the full exemption for lawyers which the Law Society is seeking is not granted, then it is submitted that there should be a limited exemption in terms of which lawyers involved in contributory mortgage lending do not perform a financial adviser service or a broking service in respect of those activities.

3.2 The grounds for this are that:

- (a) Contributory mortgage lending by lawyers is already fully regulated by the Lawyers Nominee Company Rules, which require amongst other things adequate disclosure to prospective investors. This regime dates back to 1975 when the first set of rules came into force. This was some 13 years prior to the advent of the Securities Act (Contributory Mortgage) Regulations 1988.
- (b) The lawyers contributory mortgage regime is fully recognised by the Securities Commission in the exemption which it has granted to lawyers from the Securities Act (Contributory Mortgage) Regulations – see the Securities Act (Contributory Mortgage) Regulations (Solicitors) Exemption Notice 1996.
- (c) Contributory mortgage lending by lawyers is closely monitored by the Law Society’s inspectorate.
- (d) It would be particularly undesirable to have an overlapping regime governing lawyers involved in the narrow area of contributory mortgage lending, when these activities are adequately regulated under the longstanding existing regime.

3.3 Lawyers’ employees involved in contributory mortgage activities under the supervision of lawyers should be similarly exempted from providing a financial adviser service in respect of contributory mortgage lending.

4 Employers having to maintain registration in respect of employees performing a financial adviser service

4.1 Clause 10 of the Bill proposes a new section 18 of the FAA and provides:

Employers or principals of financial advisers must be registered:

- (1) If a person employs an employee or engages an agent (other than as a nominated representative) to perform 1 or more financial adviser services in the course of the person’s business, —
 - (a) the person must maintain registration throughout the time that the employee is so employed or the agent is so engaged; and
 - (b) the employee or the agent must not perform a financial adviser service in the course of the person’s business if the employee or the agent knows or ought to know that the person is not currently registered.

4.2 It is not clear in the case of a law firm partnership or an incorporated law firm who is required to be registered, i.e. a partner or all the partners of the law firm or a director or all the directors of an incorporated law firm. The Law Society submits the requirement should be that one partner or director is registered as a financial adviser.

5 Employees of lawyers may need to register under the Financial Service Providers (Registration and Dispute Resolution) Act 2008

5.1 It is submitted that clause 35 of the Bill requires amendment. Section 7(2)(1) of the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (‘FSPA’) prevents employees of lawyers from being registered as financial advisers. The section states that employees of lawyers are not financial service providers to whom the FSPA applies. Yet

registration as a financial adviser is a requirement under the FAA for the employees of lawyers who are providing a financial adviser service.

5.2 It is suggested that this anomaly be corrected by adding the following provision in clause 35:

35(3) Section 7(2)(l) is amended by adding the following words immediately before the colon:

‘except to the extent that an individual may be required to be registered in order to perform a financial adviser service under the Financial Advisers Act 2008’.

A similar provision was added by amending legislation to the end of section 7(2)(m) of the FSPA.

6 Trustees

6.1 Section 7(2)(k) of the FSPA provides that certain persons are not financial service providers to whom the FSPA applies. Included amongst those persons are:

‘(k) a trustee of a family trust in respect of financial services provided by the trustee to the beneficiaries of that trust.’

The Law Society considers that this should be extended to the executors or trustees of an estate of a deceased person. Accordingly, the Law Society submits that clause 35(1) of the Bill be amended by adding the following paragraph:

‘(ka) an administrator or trustee of an estate in respect of financial services provided by the administrator or the trustee to the beneficiaries of that estate.’

7 Registered Legal Executives

7.1 It is submitted that clause 8 of the Bill should amend section 12 of the FAA to provide that registered legal executives do not perform a financial adviser service in certain circumstances. The reason for the suggested amendment is that the Law Society believes that a registered legal executive giving advice or making an investment management decision in the course of his or her professional practice as a registered legal executive should not be classified as a person performing a financial adviser service, if the advice or investment management decision is a necessary incident of legal practice.

7.2 It is suggested that clause 8 of the Bill be amended by adding the following subclause (6):

(6) Section 12 is amended by inserting the following paragraph after paragraph (ta)

‘a registered legal executive giving advice or making an investment management decision in the course of his or her professional practice as a registered legal executive if the advice or investment management decision is a necessary incident of legal practice; or’.

7.3 It is suggested that a definition of ‘registered legal executive’ be added to section 5 of the FAA as follows:

‘registered legal executive’ means an individual who is entitled to use the designation registered legal executive under the rules of the body that immediately before the commencement of section 12 of the Financial Advisers Act 2008 was known as The New Zealand Institute of Legal Executives Incorporated.’

This definition accords with that in the Code Committee's draft Code of Professional Conduct for Authorised Financial Advisers.

- 7.4 As a less preferred alternative to amending section 12 of the FAA, registered legal executives could be declared in regulations not to be giving advice or making an investment management decision in the circumstances described in paragraph 7.1 above. Those persons would then fall under section 12(u) of the FAA (any other person or class of persons specified in the regulations giving advice or making an investment management decision or providing a financial planning service in circumstances specified in the regulations).
- 7.5 The Law Society believes that section 154(4) of the FAA would authorise the Minister to recommend a regulation of this kind because registered legal executives are engaged in an occupation that is subject to other regulation in New Zealand that is equivalent to regulation under the FAA. Members of the New Zealand Institute of Legal Executives Incorporated ('NZILE') are required to abide by NZILE's rules and code of ethics. NZILE has a disciplinary process and the National Council of the NZILE can suspend or terminate the membership of any member who is guilty of conduct unbecoming a member or who wilfully commits a breach of NZILE's rules. In addition, the great majority of registered legal executives are law firm employees and as such are subject to Law Society complaints and disciplinary processes (sections 14 and 132 LCA). Further, their lawyer employers are legally responsible for all actions of legal executives in the course of their employment. Registered legal executives must be employed either:
- (a) by a lawyer; or
 - (b) in the legal department of a non-lawyer entity and under the direct supervision of a lawyer.

8 Law clerks

- 8.1 It is submitted that clause 8 of the Bill should amend section 12 of the FAA to provide that law clerks in the employment of a law firm do not perform a financial adviser service in certain circumstances. Law clerks are individuals who are studying for or who have obtained a law degree but who have not yet become lawyers. The reason for the suggested amendment is that the Law Society believes that a law clerk giving advice or making an investment management decision in the course of his or her employment as a law clerk should not be classified as a person performing a financial adviser service, if the advice or investment management decision is a necessary incident of legal practice.
- 8.2 It is suggested that clause 8 of the Bill be amended by adding the following subclause (7):
- (7) Section 12 is amended by inserting the following paragraph before paragraph (u)
 - 'a law clerk giving advice or making an investment management decision in the course of his or her employment by a lawyer or an incorporated law firm as a law clerk if the advice or investment management decision is a necessary incident of legal practice; or'.

- 8.3 It is suggested that a definition of 'law clerk' be added to section 5 of the FAA along the following lines:

'law clerk' means a person who is studying for or has obtained a law degree but who is not a lawyer'.

- 8.4 As a less preferred alternative to amending section 12 of the FAA, law clerks could be declared by regulation not to be giving advice or making an investment management decision in the circumstances described in paragraph 8.1 above. Those persons would then fall under section 12(u) of the FAA (any other person or class of persons specified in the regulations giving advice or making an investment management decision or providing a financial planning service in circumstances specified in the regulations).
- 8.5 The Law Society believes that section 154(4) of the FAA would authorise the Minister to recommend a regulation of this kind because law clerks are engaged in an occupation that is subject to other regulation in New Zealand that is equivalent to regulation under the FAA. Law clerks are law firm employees and as such are subject to Law Society complaints and disciplinary processes (sections 14 and 132 LCA). Further, their lawyer employers are legally responsible for all actions of law clerks in the course of their employment.

9 Absence of general powers of exemption

- 9.1 The Law Society submits that the absence of general powers of exemption by the Securities Commission is a weakness in the FAA legislation. The exemption powers of the Securities Commission are limited in section 148 of the FAA to granting exemptions from compliance with a disclosure obligation or obligations. It is submitted that the Securities Commission should have wider powers of exemption, including the power to exempt an individual from performing a financial adviser or broking service. This would be consistent with the Securities Commission's functions under the FAA.

John Marshall QC
President

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