



# NZX Regulation Case Study

## Adviser Conduct – Participant Rules 5.8.1 and 8.1.1 (7 March 2016 version)

**April 2019**



# Case Study: Participant Rules 5.8.1 and 8.1.1 (7 March 2016 version)

This case study relates to the conduct and ethical standards that apply to the conduct of NZX Advisers under the NZX Participant Rules. Please note that Rule 5.8.1 was removed as part of NZX's Participant Rules review as it was similar to Rule 8.8.1 (which has been retained in the Participant Rules with some changes from the 7 March 2016 version). In the updated Participant Rules, references to NZX Advisor were changed to NZX Adviser.

## Key points

- ▶ An NZX Advisor deliberately falsified a client's signature on a scope of service document (in the context of a compliance process).
- ▶ The NZX Advisor was referred to the NZ Markets Disciplinary Tribunal (the **Tribunal**) by NZX Regulation (**NZXR**) and their designation was revoked.
- ▶ Conduct that reflects on an NZX Advisor's ethical standards and judgement is considered serious. A breach of the rules caused by dishonesty presents a considerable risk to the integrity of the NZX markets and the NZX Advisor designation.
- ▶ Supervision was not an appropriate outcome as a person holding the NZX Advisor designation should not require ongoing supervision. Clients dealing with a Market Participant are entitled to rely on the fact that a person holding the designation has demonstrated fitness and propriety to be individually accredited as an NZX Advisor.

## BACKGROUND

An NZX Advisor was employed by a Market Participant firm and was also an Authorised Financial Adviser (**AFA**) under the Financial Advisers Act 2008 (the **Act**).

The firm conducts regular internal peer reviews of its advisers as part of its compliance programme. One of the adviser's files was selected for a peer review. During that peer review, the firm's Compliance Manager observed that a client's signature was unusually pixelated in a copy of their scope of service document.

The original document subsequently provided by the adviser was different to the one that was originally provided during the peer review.

The adviser ultimately acknowledged falsifying the client's signature to address an administrative oversight, namely the adviser not having had the client sign their scope of service in a timely manner.

NZXR referred the matter to the Tribunal, and sought the revocation of the NZX Advisor's designation under the NZX Participant Rules.

## APPLICATION OF THE RULES

NZXR considered that the adviser failed to comply with the ethical standards and judgement expected of designated NZX Advisors. These standards apply at all times and are essential for the integrity of the NZX markets. Unethical conduct is also an enforcement priority for NZXR. Accordingly, NZXR referred the matter to the Tribunal and sought a revocation of the NZX Advisor's designation under the NZX Participant Rules.

The Tribunal considered the adviser's breach to be very serious, noting it is a fundamental obligation of an NZX Advisor to act with honesty and integrity.

The Tribunal also noted that the adviser had been subject to internal disciplinary action by the firm for other compliance breaches, and had been subject to a prior period of supervision a short time before the falsification.

The Tribunal was concerned that the breach was an escalation in the NZX Advisor's conduct. The breach itself was more serious than the previous concerns about the NZX Advisor's conduct. This was despite the NZX Advisor having completed a nine month period of supervision prior to the breach.

The Tribunal determined that the breach was of a nature which could bring firms and NZX Advisors into disrepute. The deliberate falsification of a client's signature was considered to be conduct that could have a significant reputational impact on firms and other NZX Advisors.

The Tribunal determined that a supervisory order was not sufficient in the relevant circumstances, noting that supervision had previously proved ineffective in ensuring that the adviser complied with the appropriate standards and behaviour expected of an NZX Advisor.

The Tribunal considered that a person holding the NZX Advisor designation should not require ongoing supervision. Clients dealing with a firm are entitled to rely on the fact that a person holding the designation has demonstrated fitness and propriety to be individually accredited as an NZX Advisor.

## OUTCOME

The Tribunal stated that the NZX Advisor designation must be a symbol that investors can have trust and confidence in such advisers to act with honesty and integrity at all times. For the individual to continue to hold an NZX Advisor status would derogate from those high standards of behaviour expected of advisers.

The Tribunal found that the adviser had breached NZX Participant Rules 5.8.1 and 8.1.1 (7 March 2016 version), and accordingly ordered that they be privately reprimanded, have their NZX Advisor designation revoked, and pay the costs and expenses incurred by the Tribunal and NZX in considering the matter.

The Tribunal was also required under Tribunal Rule 9.4.1(h) to take into consideration any other penalty or sanction actually imposed on the adviser by any other body or power in respect of the breach. The Tribunal was advised by the adviser that the Financial Markets Authority (the **FMA**) had also conducted an investigation into the adviser's actions. The FMA had concluded that placing a false signature on the scope of service document was a breach by the adviser of sections 33 and 34 of the Act.

The FMA had also issued a Written Direction pursuant to section 49(3) of the Act, which included supervisory arrangements. Accordingly, the adviser continued to hold their designation as a financial adviser under the Act, subject to compliance with the Written Direction.

The Tribunal noted that the Written Direction did not address the risk to the integrity of the NZX markets arising from breaches of dishonesty and that the supervisory terms were similar to those imposed on a trainee adviser or someone who does not hold the designation of an NZX Advisor. Where a period of supervision had already proved ineffective, the Tribunal did not consider a further period of supervision would be an adequate penalty or protective measure for clients.

## **APPEAL**

The adviser appealed against the Tribunal's determination that the:

- a. adviser had breached Rules 5.8.1(b)(ii) and 8.1.1(b)(ii); and
- b. only appropriate penalty for the breach was to revoke their NZX Advisor designation.

The adviser sought an order from the Appeal Division of the Tribunal that the determination be set aside.

The Appeal Division considered the appeal and affirmed the Tribunal's determination. The Division also ordered the adviser to pay the costs and expenses incurred by the Appeal Division and by NZX in considering the appeal.

The Appeal Division was satisfied that the revocation of the adviser's designation was both proportionate and appropriate in the circumstances of this case, and confirmed that a private censure was appropriate in the circumstances.

The Appeal Division stated that the deliberate falsification of a client's signature on a document in the context of a compliance process and the attempt to hide that falsification by presenting a subsequently signed document as the original document was conduct which undermined the integrity of the market and those operating within it.

# Participant Rules (7 March 2016)

Rule 5.8.1 states:

*"5.8.1 Every Advisor must at all times:*

- a. *Observe proper ethical standards and act with honesty, integrity, fairness, due skill and care, diligence and efficiency and within that person's competence;*
- b. *Refrain from any action, conduct, matter or thing which is, or is reasonably likely to be:*
  - i. *Detrimental to the wellbeing or proper conduct of NZX, any of its markets and/or any Market Participant or Advisor;*
  - ii. *A discredit or bring generally into disrepute NZX, any Market Participants or Advisors; or*
  - iii. *Detrimental to the wellbeing, or contrary to the best interests, of any client, or person who has similar rights to the Securities as that client (e.g. joint account holder);*
- c. *Comply fully with all applicable Rules, any direction given from time to time by NZX, and at all times observe Good Broking Practice; ..."*

Rule 8.1.1 states:

*"8.1.1 Each Market Participant and each Advisor must at all times:*

- a. *observe proper ethical standards and act with honesty, integrity, fairness, due skill and care, diligence and efficiency;*
- b. *refrain from any action, conduct, matter or thing which is, or is reasonably likely to be:*
  - i. *detrimental to the wellbeing or proper conduct of NZX, any of its markets and/or any Market Participant or Advisor;*
  - ii. *a discredit or bring generally into disrepute NZX, any Market Participant and/or any Advisor; or*
  - iii. *detrimental to the wellbeing, or contrary to the best interests of, any client or person who has similar rights to the Securities as that client (e.g. joint account holders);*
- c. *comply fully with all applicable Rules, any directions given from time to time by NZX and at all times observe Good Broking Practice; ..."*





Centre

CABLE STREET



**NZX Limited**

Level 1 / NZX Centre

11 Cable Street

PO Box 2959

WELLINGTON

Tel: +64 4 472 7599

[info@nzx.com](mailto:info@nzx.com)

[www.nzx.com](http://www.nzx.com)