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Committee Secretariat
Finance and Expenditure Committee
Parliament Buildings
Wellington

Email: fe@parliament.govt.nz

Dear Committee Members,

ICNZ submission on Financial Markets (Conduct of Institutions) Amendment Bill

Thank you for the opportunity to submit on the *Financial Markets (Conduct of Institutions) Amendment Bill* ('the Bill'), which was introduced to Parliament on 11 December 2019.

ICNZ represents general insurers that insure about 95 percent of the New Zealand general insurance market, including about a trillion dollars' worth of New Zealand property and liabilities. ICNZ members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers liability insurance).

We wish to appear before the Committee to speak to our submission.

Please contact Andrew Saunders (andrew@icnz.org.nz) if you have any questions on our submission or require further information.

This submission is in two parts:

- Overarching comments
- Clause by clause comments on the Bill

Submission

Part 1 - Overarching comments

Conduct legislation is welcomed but needs to be well integrated with related legislation and reforms

ICNZ supports efforts to ensure good conduct in financial services. This is why we introduced the Fair Insurance Code in 2011, which covers all our members' dealing with their customers and sets high standards in excess of statutory minima to govern those dealings. It was recently reviewed and a revised and an updated version came into effect from 1 April 2020.

We support in concept the introduction of conduct legislation for financial services to ensure good conduct and fair treatment of customers is more widely achieved. To ensure that such provisions are to the benefit of consumers, it is however critical that the legislative provisions, and the regulations and other instruments developed under them, are comprehensive, proportionate, and carefully integrated with related regulatory frameworks. If not, there is a risk that extra complexities and costs are introduced that ultimately act against consumers interests rather than in favour of them (for instance if the added compliance burden deterred financial institutions from entering the market or broadening their range of products into consumer products).

The Bill includes some novel concepts, particularly the nature and role of the fair conduct programme (FCP). These concepts have not been the subject of specific consultation as they were rapidly developed after the mid-2019 Options Paper consultation and are outlined only at a high level in the Bill. Consequently, it is not possible to properly understand how this would work in practice nor what the full implications will be, until further regulatory detail is put in place and these novel elements are being implemented by entities. It is likely this will reveal issues with the provisions in the Bill that are not evident at this stage and which may require amendment at that time.

Taking a more careful and slower approach to developing a conduct regime through this Bill and subsequent regulation would have advantages in terms of regulatory coherence and integration. Specifically it would enable the impacts and practical operation of the new financial advice regime to be better understood and the detail of changes for insurance in the review of insurance contract law to be worked through, which importantly include matters related to intermediaries and their interactions with insurers and customers.

We are also mindful that further developing and then implementing the proposals in the Bill would put significant additional pressure on an industry already stretched by years of ongoing regulatory reform and now wider global events. Combined with planned FMA levy increases (and probable further increases to fund FMA's increased jurisdiction under the Bill), affected businesses will be concerned about their ability to resource these new regulatory obligations and costs.

This was an issue already, however, since ICNZ started writing this submission the global context has radically changed due to the spread of COVID-19. For the financial services sector this has meant abrupt changes in financial markets and in working arrangements, and through this period insurers want to focus all their efforts on meeting the needs of their customers and staff. This reduces insurers ability to participate in regulatory processes or to progress regulatory implementations in the short to medium term.

Over the longer term the likely significant impacts on global economic conditions, and all the consequences that flow from this, will mean these reforms land in a very different environment to the one they were designed in. Further developing and implementing the elaborate regime in the Bill in such a climate will impose additional costs on financial services entities and distract them from meeting the needs of their customers and maintaining the resilience of their firms. Rushing it info force could be counterproductive and we support a more measured approach being taken. It is noteworthy that the principle regulators of the financial sector, the Reserve Bank of New Zealand (RBNZ) and the Financial Markets Authority (FMA) have successfully set conduct expectations for the market, through direct communication and in writing, during the crisis without the need for additional legislation.

In the rest of Part 1 of this submission we discuss some high-level issues and propose an alternative approach.

Nature of the regime and the introduction of the fair conduct programme (FCP)

We recognise the deliberate nature of the regime provided by the Bill is to apply it to certain entities (insurers, banks, NBDTs) and then for the scope to be pretty much all the consumer facing services/products <u>they</u> offer, rather than to capture any entity that offers such products services/products. However, if the customers' interest and their fair treatment were to be at the heart of a comprehensive regime, then it ought to include any entity offering such products/service. As this is not the case, then this regulatory design choice inherently creates asymmetries and results in an uneven regulatory playing field in relation to the provision of certain types of products (e.g. vehicle lending products in connection with car insurance or KiwiSaver).

It is also important to avoid problematic duplication of regulation where such products are already subject to their own regulatory regimes (e.g. the *Credit Contracts and Consumer Financial Act 2003* (CCCFA) for lending products and FMCA for KiwiSaver). The impact of these duplications is hard to assess given the undeveloped nature of the new regime (e.g. requirements and detail to come through regulations), however, they should be avoided where possible and regimes properly integrated if necessary.

Some of these asymmetries and duplications could be avoided if the scope of the Bill was applied more clearly only to products and services where the financial institution is the entity responsible for the legal obligations under the product or service contract, as opposed to the scope being defined by the somewhat convoluted definitions of "relevant service" and "associated product".

Focusing initially on the 'financial institution', the regime provided in the Bill then imposes the majority of its obligations on the financial institution and its intermediaries through each institutions' FCP, which as noted above is a novel and unique concept. While the overarching elements of a FCP are outlined in section 446M, ultimately there are a lot of questions around what sort of document the FCP is, how it will function, and how it will be overseen, including:

- the FCP is proposed as the financial institution's document but performs an essentially quasi-regulatory role in relation to the entity and its intermediaries - intermediaries can have civil liability (up to \$1m for an individual and \$5m in any other case) for breaching a document (the FCP) that has not been drafted through any legislative process or by a regulator;
- whether FCPs are expected to be homogeneous across entities or highly individualised for each entity, which will amongst other things have an impact on the compliance costs for intermediaries that work with multiple financial institutions (e.g. insurance brokers);
- whether the FCP is a document that is actually used within the company itself (and its intermediaries), or whether it is simply an additional document that represents an agglomeration or summary of other documents and used predominately to satisfy the regulatory obligations;

- the detail of what an FCP would needs to contain will only be determined once regulations are made specifying this, and potentially any further guidance is issued and industry standards developed;
- how the FCP can balance the need to be sufficiently detailed to outline the policies, processes, systems and controls applying across a range of legal regimes, and potentially to a diverse range of products supplied in some cases through many different intermediaries, while at the same time not giving away potentially confidential information;
- where a FCP applies to many products and intermediaries, how only the relevant parts of the FCP will be communicated to intermediaries (to support their compliance with section 446I);
- how the FMA's regulatory role would be exercised in relation to FCPs, for example there is no approval or acceptance power in the Bill in relation to FCPs, although it is necessary to notify 'material changes' to one to the FMA as per 446H(2)(b), and it is unclear whether there will be any interface with the conduct licencing process; and
- ultimately It would be necessary to flesh out the required detail and oversight of FCPs through the development of regulations, potentially guidance and industry standards, the development of its regulatory approach in this area by the FMA, and ultimately through financial institutions developing and implementing their FCPs.

Given all this we have serious concerns with the introduction of the FCP concept and this is discussed further below.

Coverage of intermediaries needs to minimise duplications and asymmetries

The Bill deliberately focusses on financial institutions and imposes obligations on these directly, and through these and their respective FCPs onto intermediaries. There are proposed carve outs in relation to other financial institutions and financial advice providers (sections 446J and 446L) that recognise their own responsibilities and the nature of financial advice. It would be important there is clarity in how the law is applied so that gaps in regulatory coverage do not emerge, for example in regard to:

- the application of 'giving financial advice', is that clear enough to distinguish when a financial advice provider (FAP) should be subject to an FCP or not in relation to section 446M(2)(a)?
- whether the asymmetry that an FAP intermediary has a duty under section 446I to take all steps to comply with a financial institutions' FCP, but the financial institution has no duty or enforcement capability to ensure that they do, be workable?

There are also specific features of the insurance industry that need to be considered in designing and applying this regime. For example, the wording of the definition of intermediary in section 446E potentially goes well beyond the stated policy intention of including entities involved with distribution of products. It could potentially include a much wider range of entities involved with administering contracts and even performing physical services, which we do not consider is appropriate or necessary.

While we are mindful the framework specifically includes for example 'handling a claim under an insurance contract', the way this is worded currently could cover a range of entities that have not at any stage been discussed as being within the purview of the conduct regime. The focus has been largely on the distribution of products and so neither the rationale for this, nor the consequences of this wider coverage to potentially include parties entirely unrelated to sales/distribution have been explored. Careful consideration needs to be given to whether it is appropriate for responsibilities (i.e. beyond sales and distribution) to be extended to those third-party entities undertaking activities in these areas, by deeming them to be intermediaries, and if so how? How this relates to the scope of potential entities classified as intermediaries is discussed in Part 2 of this submission below in relation to section 446E.

Simplifying the Bill to achieve the policy intent

ICNZ recognises the efforts that have been undertaken to avoid duplications by designing the new conduct regime in and around the soon to be implemented financial advice reforms provided by the *Financial Services Legislation Amendment Act 2019 (*FSLAA), which is a quasi-conduct regime in its own right (limited to where financial advice is provided but utilising a wide definition of this). We are however of the view, and understand many share it, that if it had been known four years ago that a fully-fledged conduct regime was going to be developed for financial services, the financial advice reforms would have been done in a very different way and/or in a different sequence.

There are two fundamental problems resulting from working around the developed but yet to be implemented financial advice regime:

- potential gaps because the financial advice regime applies to FAPs but generally <u>only applies when financial advice is being provided by them</u> – the provision of financial products by FAPs on a non-advice basis is therefore the largest issue/gap created; and
- potential duplications where both the conduct and financial advice regimes apply, particularly if the requirements are different, even if subtly.

To try and address this, MBIE has created a framework that attempts to avoid most of these issues associated with the interface with the financial advice reforms. The problem however is that doing so relies on elaborate and asymmetrical provisions in the Bill, for example what is covered under an FCP in one context is addressed through FMA licence conditions in another, on quickly developed and untested concepts such as the FCP, and the need to develop most of the detail subsequently through regulation. While much detail is to come later (through regulations and licensing conditions etc.), this approach relies on key definitions and concepts in the Bill and locking in such specific, elaborate and asymmetrical provisions carries significant risks.

Fundamentally, we cannot see how all this would ever fit neatly together while also avoiding regulatory arbitrage. We are therefore concerned that locking in such a complex framework in the Bill is likely to create problems down the track when the detail is being worked through in regulations and/or the regime is being implemented. Providing a regime that is integrated and non-distortionary from a sector and financial services entity perspective, while simultaneously providing consistent levels of protection for consumers, is impractical with a patchwork type approach. This is an inherent problem with adding an institution-centred regime over the top of product/service-based regimes (e.g. financial advice and CCCFA). We also wonder how the FMA would be able to clearly and consistently apply oversight across the sector under such a complicated regime. Good legislation and regulation should be simple to understand, easy to apply and carry least costs.

Reflecting on all of this, ICNZ has come of the view that extending the conduct regime so it clearly applies to the provision of relevant services comprehensively and regardless of by what entity (whether financial institution or FAP etc.), while also simplifying it, would better achieve the policy intent and leave room for further development of the regime once the full outcomes and impacts of the financial advice reforms are better understood.

ICNZ believes that such change is in the best interests of consumers of financial services. One of the flaws of previous financial sector regimes has been that complexity and inconsistency has created a barrier to consumers' understanding of the obligations those they are dealing with have towards them. Creating a single regime that applies to all financial service entities and the products and services they provide would go a long way to giving consumers what they need.

The main changes that would be required to the Bill to achieve this alternative approach would be to:

- amend the definition of 'financial institution' to make clear this applies to banks, NBDTs and insurers to the extent they provide relevant services, as well to FAPs to the extent they also provide relevant services – potentially renaming it to recognise it would cover entities of a different character;
- remove the requirement for a FCP and the related provisions and rely on the development of regulations and the licensing process to provide oversight (why prescribe some of the detail around it in primary legislation when high level principles could be combined with licensing (required anyway) as occurs under the financial advice reforms?).

This materially different approach to achieving the same objectives explicitly recognises that it is better to expand the detail of a principles-based and cross cutting regime to address any specific issues that arise over time, rather than have to completely re-engineer a complicated but not fully comprehensive regime to address gaps in coverage or other fundamental design issues.

We are however mindful that in making it comprehensive across the sector, there is a risk of imposing an additional compliance burden on intermediary FAPs under this regime and on top of FSLAA. As such it would be critical the two regimes are integrated and aligned. We note however that this risk arises under both this alternative approach as well as under the approach outlined in the Bill (e.g. because intermediaries would have to apply with multiple FCPs). However, the interests of the consumer need to be put first.

Finally, we note the additional regime proposed in the Bill is being progressed in parallel to the review of insurance contract law. Providing a more comprehensive and principle-based conduct regime as we are proposing is more likely to fit with any changes to insurance contract law, which will inevitably apply across insurance contracts regardless of distribution method. That review also includes the *Insurance Intermediaries Act 1994*, which contains key provisions for the relationship between insurers and insurance intermediaries such as brokers. Taking time to consider the potential changes in both areas is important.

Process for the Bill

The Government has acknowledged this Bill has been developed in haste in the latter part of 2019. MBIE made genuine efforts to engage industry constructively within the constrained timeframe it had, but these engagements were inevitably limited. There was little opportunity to explore new concepts such as the FCP or thoroughly workshop definitions or the coverage of intermediaries.

Given the issues with the Bill itself that we have identified we do not consider the framework should be introduced in its current form. Furthermore, since the Bill was introduced the COVID-19 crisis has changed the context fundamentally. There is absolutely no need to rush this flawed Bill at this time. Regulators are appropriately setting conduct expectations to manage through the current crisis. Time should be taken to get things right by constructing a Bill that puts the consumer at the heart of its design rather than the existing patchwork of legislation, on a 'make-fit' basis.

If ICNZ has raised issues that the Committee, or its advisers, would benefit from discussing further (such as our alternative approach proposed above), or if changes contemplated by the Committee have consequential impacts, ICNZ would welcome the opportunity for further engagement with the Committee or its MBIE advisers on the detail of our submission.

Need for appropriate transitional provisions

The nature of the obligations in the proposed regime, the adjustments they might require, the amount of other regulatory reform planned for coming years and now the significant but uncertain impacts of COVID-19 mean that regardless of what form the Bill is progressed in, appropriate transitional provisions would be critical to avoid unduly disrupting the operation of the sector. These would need to reflect the requirements of this regime (legislation and subsequent regulations) and the content and timing of other reforms (e.g. changes to insurance contract law and licensing of financial advice providers).

The development of regulations under this Bill would need to be given sufficient time and involve significant engagement with the financial services sector and other stakeholders. This would also potentially be happening as part of a period of unprecedented regulatory changes for the financial services sector and its regulators generally, and for insurance in particular due to the parallel review of insurance contract law and planned reviews of solvency standards and the *Insurance Prudential Supervision Act 2010 (IPSA)*.

In particular, should the FCP concept be retained in the Bill it would be necessary to allow time for developing and implementing FCPs as this will not just be a matter of developing them, but also putting in place the internal and external changes required (e.g. changes to intermediaries' distribution contracts (including incentives), training for intermediaries etc.). The time may need to be significant as intermediaries would only know how to comply when FCPs are finalised as their obligations are largely through these rather than from the Bill or subsequent regulations. Strong consideration would also need to be given to how the conduct licencing process would relate to the development of FCPs and to FAP licences, which will be required for relevant entities by early 2023.

There are simply too many uncertainties at this stage to enable an informed position on what the appropriate transitional provisions might be. Accordingly, we support the provisions in clause 2(2) of the Bill that enable commencement dates to be set after its enactment by one or more Orders in Council. We do not support the arbitrary two-year deadline in clause 2(3).

It would be necessary for the Government and its officials to engage closely with the sector in the lead-up to commencement to identify the appropriate sequencing for bringing a new conduct regime into effect. Any timing will need to be based on what can workably and efficiently be put in place by the financial services industry at that time, rather than just choosing the soonest possible date at the point at which the regulations are finished.

Part 2 - Clause by clause comments on the Bill

Clause	ICNZ comments	Recommendation
Clause 2 – Commencement	ICNZ supports the provisions in clause 2(2) of the Bill that enable commencement dates to be set after its enactment by one or more Orders in Council. We do not support the arbitrary requirement that all provisions come into effect within two years of the Bill receiving Royal Assent. Timeframes for regulatory development may leave little time for commencement/transition within a two-year period and lead to sub-optimal decisions on commencement timing in future due solely to a reluctance to amend the legislation. We recommend this arbitrary period is extended to four years or removed to give appropriate flexibility and avoid this risk.	Either: • repeal clause 2(3); or • amend clause 2(3) by replacing 'second anniversary' with 'fourth anniversary'.

Clause	ICNZ comments	Recommendation
Clause 9 – New subpart 6A of Part 6 inserted		
446B – What is the fair conduct principle	ICNZ supports the framing of the fair conduct principle. We note this is similar to ICNZ's Fair Insurance Code and regimes in other jurisdictions and is consistent with what we submitted on during MBIE's mid-2019 policy consultation.	Note comments.
446C – When the fair conduct principle applies	The way section 446C interrelates with other provisions in the Bill could be made clearer, namely the fact that it is proposed to largely apply through FCPs rather than as a standalone requirement.	Note comments and consider redrafting.
446D – Meaning of financial institution	Please note our overarching comments in Part 1 of this submission, which would have a fundamental impact on elements of the Bill including the approach to 'financial institutions'. The remainder of the comments here respond to the provisions of the Bill as currently drafted. The way 'financial institution' is defined in section 446D could be confusing as to scope. When you work through the other provisions and relevant definitions it is clear, as should be the case, that only financial institutions that are offering products/services to consumers are within the scope of the regime. However, simply reading section 446D suggests it applies to all licensed insurers, which includes reinsurers, captive insurers and insurers that only provide non-consumers products/services. At present, to understand whether section 446D applies it is necessary to read: • the definition of 'financial institution' in section 446D; then • the meaning of 'relevant service' and 'associated product' in section 446F; then • the definition of 'insurer' in section 446S which in turn refers to section 8 of the *Insurance (Prudential Supervision) Act 2010* (IPSA); and finally • the definition of 'consumer insurance contract' (also in section 446S). We suggest redrafting 446D to address the above issue and perhaps the inclusion of a clause like 446C(3) in clause 446D.	Suggest redrafting of section 446D, perhaps the inclusion of a clause like 446C(3).
446E – Meaning of intermediary	Please note our overarching comments in Part 1 of this submission, which would have a fundamental impact on elements of the Bill including the approach to 'intermediaries'. The remainder of the comments here respond to the provisions of the Bill as currently drafted. We support the scope of the regime in the Bill encompassing intermediaries involved in distributing, administering and/or providing advice to consumers on products within the financial services industry (insurers, brokers, banks etc.) and those involved beyond it in distributing products to consumers (e.g. travel agents, car dealers etc.). However, as currently drafted the scope of 'involved' as provided in proposed section 446E(3) goes beyond the scope of the policy in the Cabinet paper, which refers to 'sales made by intermediaries' or 'intermediaries distributing their products', to potentially include other parties	Further consideration be given to the intended purpose of section 446E(3)(b), and whether it can be refined by the use of an alternative term such as 'administrative services'. Amend section 446E(3)(d) by removing 'or performing'.

Clause	ICNZ comments	Recommendation
	involved with the administration of or performance of the contract. While the explanatory note for the Bill uses different language, it also retains an emphasis on people who 'negotiate or otherwise arrange a contract' (i.e. distribution of the product/service). This issue of materially extending the scope of 'intermediary' to includes parties not involved with selling or distributing products manifests in a number of ways in and under section 446E. Overall, we consider that section 446E needs to be reconsidered to ensure that the coverage of other entities is clearly linked to the policy intent as regulatory overreach could create a number of issues. There needs to be a clear policy on whether entities <u>not</u> involved in sales/distribution are intended to be captured as intermediaries (we recommend not). *Section 446E(3)(b)* The wide scoping of section 446(3)(b) and the use of 'other services' potentially captures entities that are <u>not</u> conventionally involved with selling or distributing products (such as lawyers, accountants and valuers) and which would not otherwise be subject to oversight by the FMA. This is beyond the intended scope and would mean for instance that how these entities are paid could possibly be subject to any controls on incentives, which extends those provisions well beyond the stated policy intent. We recommend that further consideration be given to the intended purpose of section 446E(3)(b), and whether it can be refined by the use of an alternative term such as 'administrative services' to make it clear that these are services preparatory to that contract being entered into and not other input/advice to the financial institution that might be considered 'preparatory' but which does not involve any interactions with a customer. In terms of the current drafting, we also note the use of 'other services' in section 446E(3)(b) creates a possible ambiguity as to how the use of 'services' here relates to the defined term 'relevant services' and the extent to which the use of 'other' is intended to extend the scope, or whether the 'other' is simply a reference to the immediately above subclause. This drafting issue would also be addressed by the change we have recommended above. *Section 446E(3)(d)* To align with the scope of the fair conduct principle, the definition of 'intermediary' needs to reflect the involvement of intermediaries at each relevant stage of the product lifecycle (e.g. handling claims). However, as noted above in Part 1 of this submission this aspect has not been explicitly explored in the policy development to this point. At minimum it is necessary to describe and/or differentiate between administering (applying the terms & conditions of a product to a situation to determine if/how the contract responds– i.e. claims handling) and providing a service that facilitates the fulfilment of terms & conditions (i.e. panel beating, building repair work etc.)	

Clause	ICNZ comments	Recommendation
	As currently drafted there is some uncertainty as to whether intermediary has an excessively wide scope as 'performing the service or the terms…' in section 446E(3)(d) could be read as covering service providers such as panel beaters, builders, and cleaners that are involved in repairing property as well as others such as goods suppliers and charter airlines (e.g. for travel repatriation), where these are contracted directly by the insurer to perform these sorts of services. If the scope was this wide it would significantly extend the regime for insurers vis-à-vis other parts of the financial services sector (and the current Fair Insurance Code) and would be undesirable and impractical because: • This is beyond the scope of the proposed reforms and not something that has been discussed during the reform process, it appears to be an inadvertent extension that occurred through the drafting process. • The application would be uncertain and could include all sorts of firms, some only infrequently, and some of which may have no standing relationship with the insurer. • This could disadvantage small businesses that are often involved in claims fulfilment – as they would need to increase their own regulatory compliance to give the financial institutions confidence that their obligations are being met. This could also potentially cause a shift to reliance on larger service providers, which would be better positioned for regulatory compliance. • This could impose costs and create unnecessary administration that could impede speedy and efficient claims outcomes for consumers. • The added complexity could incentivise insurers to pay cash settlements rather than to work with the customer to resolve the damage, which may not be the best option for some customers. • It is better for the insurer themselves to be responsible for the settling of the claim than to deem parties that undertake some of that work to be intermediaries and place additional obligations on them. To resolve the above issue associated with 'or performing' it would be necessary to either: (a) amend section 446E(3)(d) by removing 'or performing'; or (b) make regulations (under 446E(4)(b)) to exclude every potentially relevant occupation (e.g. car repairers, builders, cleaners etc.). Of the two options above, we consider (a) to be superior as it would align with the policy intent behind the conduct regime, provide certainty and avoid the need to develop extensive regulations listing numerous occupations, with the risk that this still fails to cover some relevant ones.	

Clause	ICNZ comments	Recommendation
446F – Meaning of relevant service and associated product	As described more fully in relation to section 446S, we note the scope of this definition may be influenced by any review of the *Insurance Prudential Supervision Act* (IPSA) as this will specifically consider the definition of 'contract of insurance' and 'Meaning of carrying on insurance business in New Zealand'. As noted in Part 1 of this submission above, the concept of 'relevant service' and 'any associated product' extends the scope of the Bill to products and services beyond those which the entity that is the financial institution has the legal obligations for under the product or service contract. This causes the following issues: a) Uneven playing field – e.g., loans provided by an insurer (or its subsidiary) in conjunction with insurance may be in scope but loans provided by a credit company are not, KiwiSaver provided by a bank (or its subsidiary) may be in scope but KiwiSaver provided by a fund manager is not. This uneven situation may also deter financial institutions from broadening their range of products, resulting in reduced offerings for customers. b) Duplication of regimes - many of the financial products potentially captured by 'relevant service' and 'associated product' definitions are already subject to their own regulatory regimes and which contain their own conduct obligations, for example the CCCFA. c) There are often multiple entities involved in the product life cycle, for example an insurance product manufactured by an insurer which is sold by a bank. This could result in two financial institutions being subject to the conduct obligations for the same product, noting that the clause 446J carve out only replies in respect of a financial institutions role as an intermediary. Limiting the scope of products and services to those the financial institution has the legal obligations for under the product or service contract would mitigate the issues in this area.	Limit the scope of products and services to those the financial institution has the legal obligations for under the product or service contract.
446G – Duty to establish, implement, and maintain effective fair conduct programme	Note overarching comments on the FCP concept in Part 1 of this submission. The remainder of the comments here respond to the provision if it is to be retained in the Bill. Further to our comments on section 446D, the way this provision and section 446D is drafted makes it appear as if all financial institutions (e.g. all licenced insurers including reinsurers etc.) must 'establish,…… an effective fair conduct programme', when it is only those financial institutions that offer relevant services to customers that must do so. As with section 446D, section 446G would be clearer if it specifically stated that it only applied to those financial institutions that offer relevant services etc. (avoiding potential confusion and the need read through a series of separate provisions and definitions).	Suggest redrafting section 446G to make the scope clearer, perhaps the inclusion of a clause like 446C(3).

Clause	ICNZ comments	Recommendation
446H – Duty to make fair conduct programme available	Please note our overarching comments on the FCP in Part 1 of this submission and on the potential removal of the FCP concept. The remainder of the comments here respond to the provision if the FCP concept is to be retained in the Bill. ICNZ does not support (or understand the rationale for) requiring an FCP to be published on an internet site and considers this could have disbenefits. We accordingly recommend that subclause 446H is removed. First, we note the scope and nature of the FCP has yet to be outlined in any detail and this is likely to be something that would emerge in the development of regulatory requirements for it, and as entities and the FMA moved to implementation of the regime. Nonetheless the FCP is likely to be a detailed document and could contain commercially sensitive information. ICNZ's view is that the primary audiences for FCPs would be the financial institution's own staff, the intermediaries subject to it (but perhaps only relevant sections of the FCP) and the regulator (FMA). Fundamentally we do not consider the FCP is logically conceived of as a customer facing document and therefore consider publishing it to be wholly inappropriate. Other reasons for not requiring FCPs to be published online or otherwise include: • A risk that financial institutions may replicate other financial institutions' FCPs, limiting the benefits of it and resulting in little differentiation between them, thereby not achieving MBIE's intention of consumers ascertaining how they will be treated specifically by a particular financial institution (i.e., all FCPs may end up similar). While a level of consistency is desirable (see further comments below), entities copying each other is not what we understand is expected under the regime. • An FCP would likely be a lengthy document for consumers and potentially distract them from reading documents more important to the product/service they are using, such as policy terms of insurance policies and PDSs, which is already an issue. • Consumers would be even more overloaded with non-product specific information and this could add to confusion (and distraction), there are already for example industry codes, financial strength ratings, EDR scheme terms, and then potentially multiple FCPs if comparing providers. • If it is necessary to publish a FCP there would inevitably be a focus on making it look attractive to customers (even though it is likely few would read it) and avoiding giving away anything away to competitors, rather than just focussing on the substance of it and delivering for customers.	If FCPs are retained in the Bill, remove proposed new section 446H and replace it with provisions that recognise the proper role of a FCP and the needs of the FMA in undertaking its regulatory role.
446I – Duty to comply with fair	Note overarching comments on the FCP concept in Part 1 of this submission and on the potential removal of this concept. The	Note ICNZ's comments in regard to the application to intermediaries.

Clause	ICNZ comments	Recommendation
conduct programme	remainder of the comments here respond to the provision if it is to be left in the Bill. For intermediaries that work with many financial institutions (e.g. insurance brokers) they could under this provision be required to take reasonable steps to comply with as many as ten or more FCPs in relation to their engagements with consumers (as well as their own obligations under the FMCA related to financial advice or otherwise, and their own systems and standards). This will inevitably create a level of compliance burden and potential confusion and unworkability if the FCPs' differ in material ways. Avoiding this would in turn require a level of standardisation across the industry based on industry standards or codes and/or regulatory guidance. We note that a separate feature of the current situation that would likely need to change once the provisions in the Bill are in effect is the absence of written distribution agreements between some intermediaries (particularly larger brokers) and insurers. This is a result of those brokers not wanting to enter into such agreements and instead rely simply on statute law. Meeting the 'all reasonable steps' requirement in section 446I would suggest that formal agreements should be entered into and intermediaries would nonetheless be subject to insurers' FCPs. Nonetheless for insurers to be confident of meeting obligations to their intermediated customers (where the intermediary is working for the customer), for example in terms of ensuring information about risk or price changes is communicated to the ultimate customer (by the intermediary or otherwise), it will be necessary for there to be clear agreement on how various obligations from the insurer to the end consumer are met by the intermediary, for instance to ensure information on changes to policy wording or risk is communicated. Drafting comment – the drafting of 446I(2) could be clearer as to which duty is referred to by 'that duty' – suggest including a cross reference to 446I(1).	Reconsider drafting of section 446I(2) to be clearer as to which duty is referred to by 'that duty'.
446M – Minimum requirements for fair conduct programme	We note there may be some uncertainty as to the limits of an FAP's role 'relating to the giving of regulated financial advice', which would in turn make the application of the carve out in section 446M(2)(a) uncertain.	Note comments.
446O – Intermediary must comply with incentives regulations	It is important that controls on incentives apply consistently to financial institutions and intermediaries and so we support this provision (subject to our comments elsewhere on the definition and appropriate scope of 'intermediaries' under the Bill). We have no further comments on this proposed section, noting the substance of these requirements will be applied through regulations.	Note comments.
446P – Meaning of incentive	ICNZ recognises the scope of 'incentive' has deliberately been defined broadly and that how it is ultimately applied will be determined through the development of regulations. Nonetheless, while we have concerns that section 446P is overly	Amend section 446P to ensure that: • the consistency of section 446P(3)(f) with Cabinet policy

Clause	ICNZ comments	Recommendation
	broad, it also misses one specific type of commission that should be captured within its scope. The broad definition leaves uncertainty for financial institutions as to quite how broad the regulatory prohibitions may be under this provision as they could go significantly further than the stated focus of the Government on target-based incentives. For example, the inclusion of section 446P(3)(f) and the example below it ('A is paid a 5% commission for each life policy that A arranged') are a surprise given comments by the Minister, MBIE and the FMA that there would not be a blanket ban on commissions and given disclosure regulations are being introduced as measure for disclosing commission rates. We recommend this is revisited to ensure it is consistent with policy decisions and is necessary to be included in the Bill. Otherwise it represents regulatory overreach and will create uncertainty regarding incentives that have been stated as being outside the scope of potential regulation. The one type of commission that does not appear to be covered, and should be if general commissions (i.e. no target based component) remain within the scope, is where a product is priced 'net' – that is the insurer sets their price for the product and intermediary chooses what mark-up to add on to it. Omitting this from the definition of 'incentive' could open a significant opportunity for regulatory arbitrage.	decisions is confirmed; and • <u>if</u> general commissions remain included, situations where an intermediary adds a commission to a product that has been priced net are included within the scope of 'incentive'.
446S – Other definitions used in subpart	*Definition of 'consumer insurance contract'* The definition of 'consumer insurance contract' currently utilises the concept of 'New Zealand policyholder' from the *Insurance Prudential Supervision Act* (IPSA). While there is logic for this and aligning with IPSA, it in turn makes the approach to insurance contracts out of step with the treatment of other financial institutions under the Bill that are limited to natural persons rather than potentially including entities (i.e. corporate persons) purchasing policies that are 'wholly or predominately for personal, domestic, or household purposes'. Specifically we note the *Credit Contracts and Consumer Financial Act 2003* (CCCFA) applies to 'natural persons' and given the focus of the Bill, and that the definition is of 'consumers', it is equally logical to apply a consistent approach to consumer insurance contracts and apply these to 'natural persons' and not include potential corporate persons. Further to this, relevant contracts should be limited to insurance contracts that are subject to the laws of New Zealand. This is largely unnecessary at present due to the definition of 'New Zealand policyholder' in the Bill but would be if that was replaced with 'natural person' as there would not be a specific New Zealand element. Making clear that the provisions in this Bill would apply only to insurance contracts subject to the laws of New Zealand would increase certainty and would be consistent with the approach in the CCCFA (refer section 137 of that Act) and throughout the FMCA to limit the application of the FMCA to New Zealand financial markets and products.	In the definition of 'consumer insurance contract' replace 'contract of insurance entered into by a New Zealand policy holder wholly….' with the following: 'contract of insurance subject to the laws of New Zealand entered into by a natural person wholly…'.

Clause	ICNZ comments	Recommendation
	Definition of 'insurer' We note the definition of 'insurer' refers to section 8 of the *Insurance Prudential Supervision Act* (IPSA) and that a review of that Act is planned to recommence later in 2020 and is likely to include review of the concept of 'carries on insurance business in New Zealand'. We also note the 2017 IPSA Issues Paper released by RBNZ identified that 'The criteria related to "carrying on insurance business in New Zealand" or in the definition of an insurance contract are not necessarily clear cut.'[1]	
Clause 18 – New Part inserted to Schedule 4	Support new clauses 92 and 93 of Schedule 4. We note that the proposed new clause 94 of Schedule 4 of the FMCA is explicitly retrospective in the sense that regulations made under it can override existing agreements, although we recognise clause 94(3) provides that it does not apply to incentives already paid and clause 94(4) provides a kind of defence to actions taken by entities in response to such regulations. If this retrospective approach is adopted in regulations made under the Bill, the transition period before commencement of such regulations would need to be sufficient to allow all financial institutions to review their existing agreements against the specific requirements and then renegotiate and implement new agreements where necessary. This could be a significant period, particularly as the entire industry would be doing this at the same time.	Note comments.

Conclusion

Thank you again for the opportunity to submit on the Bill. If you have any questions, please contact our Regulatory Affairs Manager by emailing andrew@icnz.org.nz.

Yours sincerely,

Tim Grafton
Chief Executive

Andrew Saunders
Regulatory Affairs Manager

[1] Paragraph 43 of 'Issues Paper: Review of the Insurance (Prudential Supervision) Act 2010', Reserve Bank of New Zealand, March 2017.