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Kia ora

# INSURANCE COUNCIL OF NEW ZEALAND SUBMISSION ON MBIE'S CAPITAL MARKETS REFORMS PHASE TWO DISCUSSION DOCUMENT

Thank you for the opportunity to provide a submission to the Ministry of Business, Innovation and Employment (**MBIE**) on its Capital Markets Reforms: Phase Two discussion document.

Te Kāhui Inihua o Aotearoa | The Insurance Council of New Zealand (**ICNZ**) represents general insurers. Our members accept the risks of over NZ$2 trillion of New Zealand's assets and liabilities. ICNZ members provide insurance products ranging from those usually purchased by individuals to those purchased by small businesses and larger organisations, including liability insurance such as directors and officers (**D&O**) insurance.

## General Comments

ICNZ welcomes MBIE's focus on ensuring New Zealand's capital markets settings remain fit for purpose, internationally competitive, and proportionate. From an insurance perspective, liability settings are an important part of the broader operating environment for issuers, directors and officers, auditors and other professional advisers. They can affect the availability and cost of insurance, the management of defence costs, and the willingness of suitably qualified people to participate in governance roles.

ICNZ supports regulatory settings that maintain high standards of market conduct and investor protection while ensuring that liability is clear, proportionate and aligned with responsibility and fault. We are also mindful that reduced obligations or selective caps can simply move exposure to a different insured defendant.

We have not commented on all issues raised in the discussion document. ICNZ's comments focus on those areas where our members have relevant experience as providers of liability insurance, including D&O insurance and professional indemnity insurance. We have brought an insurance lens to this consultation and recognise that others will bring different perspectives.

## Consultation Paper Questions

### Issue 1: Product disclosure statements (PDS)

ICNZ's comments on Issue 1 are limited to PDS proportionality, evidence of listing impacts, core information requirements and digital presentation. ICNZ considers that current PDS requirements are generally proportionate but recognises that some simplification may be appropriate where this does not compromise investor understanding. If the full PDS is reduced, ICNZ considers it important to retain sufficient information for both wholesale and retail investors to understand the issuer's financial position and the relative risks of investing. ICNZ also supports the adaptation of PDS requirements to a digital-first format, while noting that Australia, Singapore and Canada may provide useful comparative models for MBIE to consider.

### Issue 2: Civil liabilities for directors and issuers

**2.1 Do you agree with the problem definition around current settings for director liabilities?**

ICNZ agrees with the problem definition outlined in the consultation paper. From an insurance perspective, current director liability settings may affect personal exposure, defence cost risk and D&O insurance costs, and are relevant to whether the current settings remain proportionate.

**2.2 How significant are civil liability settings compared with other factors affecting public market participation, such as market depth, liquidity, access to private capital, listing costs, ongoing compliance costs, and broader economic conditions?**

ICNZ is not in a position to assess the relative significance of civil liability settings compared with all other factors affecting public market participation.

***Questions on liability for continuous disclosure contravention***

**2.3 Which option do you support (A or B) for potential change to liability in relation to continuous disclosure contravention for directors and other persons?**

ICNZ supports Option B(ii). That is, director and other person liability settings for continuous disclosure should be amended by adjusting the statutory defences available to directors and others who may have been involved in an issuer's contravention. Clear and workable statutory defences are important given the wider implications of continuous disclosure claims, including the potential impact on the reputation of the company, the board and individual directors. ICNZ considers directors should have greater recourse to legal defences when faced with litigation.

ICNZ notes that directors already have good access to D&O liability insurance. Whether any changes to the continuous disclosure regime will further improve access to cover remains uncertain. In practice, D&O insurance functions primarily as a defence costs product, providing directors with funding for legal representation and also compensation claims. While some policies may also respond to fines and penalties where legally insurable, cover for such liabilities may be restricted by law or excluded depending on the nature of the underlying conduct.

Any revised defence should be capable of being applied at an early stage of proceedings, rather than operating only after lengthy discovery and trial. A defence that is theoretically available but prohibitively expensive to establish will not materially reduce defence costs, settlement pressure or the burden on directors. The design of the defence should recognise reasonable reliance on appropriately designed disclosure systems, management and professional advice, while retaining accountability where warning signs were ignored or a director acted unreasonably.

### 2.4 Do you have a preference for change not reflected in the options in relation to continuous disclosure contravention for directors and other persons?

ICNZ does not propose an additional option beyond those identified in the consultation paper.

### 2.5 Are there any other issues or impacts the Government should consider in relation to liability for continuous disclosure contraventions for directors and other persons?

Liability settings need to be considered by reference to the total claims environment arising from a single disclosure event. One alleged contravention may generate regulatory investigations, private compensation claims, class actions and contribution proceedings between the issuer, directors and professional advisers. Even where no liability is ultimately established, parallel proceedings have a large impact and can consume substantial defence costs, thereby also reducing the insurance limit available to meet meritorious compensation claims.

To encourage directors to continue to serve on New Zealand boards, and to attract high-quality candidates to become directors, care should be taken to ensure regulatory settings are not prohibitively harsh or punitive. A rounded consideration is therefore required.

### 2.6 Which option do you support (C or D) for potential change to liability in relation to continuous disclosure contravention for issuers? Please indicate a preferred sub-option as well if relevant.

ICNZ supports Option D(iii), amending issuer liability settings for continuous disclosure by moving from strict liability to a fault-based standard.

ICNZ supports this option because it would enable the circumstances of a contravention to be adjudicated on their merits. ICNZ considers this approach would maintain the current high standards of issuer continuous disclosure, while allowing entities and directors to raise defences in line with their degree of knowledge, responsibility and fault.

ICNZ recommends that, consistent with the Australian approach noted in the discussion document, MBIE separately assesses the appropriate threshold for regulator-led enforcement and private compensation proceedings. A regulator may need effective tools to secure timely disclosure and market integrity, while private damages claims can generate substantially greater claims with impacts on aggregate and insurance exposure. Any fault standard should also be defined with sufficient precision to avoid recreating strict liability in practice.

### 2.7 Do you have a preference for change not reflected in the options in relation to continuous disclosure contravention for issuers?

ICNZ does not have a preference for change beyond the options identified in the consultation paper.

### 2.8 Are there any other issues or impacts the Government should consider in relation to liability for continuous disclosure contraventions for issuers?

ICNZ is not aware of any additional issues or impacts beyond those identified in the consultation paper.

*Questions on deemed director liability in relation to disclosure and financial reporting contraventions for issuers*

**2.9 Do you think changes to deemed director liability should be considered in relation to all markets, or for NZX only?**

ICNZ supports changes to deemed director liability at least for NZX-listed issuers and considers that extending changes to deemed director liability to all markets should also be considered. The case for reform may be most apparent for NZX-listed issuers, but similar issues may arise for other firms subject to disclosure and financial reporting obligations.

**2.10 Which option do you support (E, F, or G) for potential change to deemed director liability?**

ICNZ supports Option G(iii) removing deemed director liability and replacing it with fault-based liability for both disclosure contraventions and financial reporting contraventions. ICNZ considers this change should apply to all firms subject to the relevant obligations, or at least to NZX-listed issuers if MBIE prefers a staged or more targeted approach.

ICNZ's reasons are as follows. Deemed director liability is costly in the context of Professional Indemnity and D&O claims. In turn, this may result in higher premiums year-on-year for entities and directors. These costs are likely to be passed on to customers of insured entities or may diminish net profit and shareholder returns.

If an action is taken against several directors on a board, each director may be entitled to defence costs, requiring counsel to be appointed for each director. The interests of individual directors may be contrary to one another, requiring separate representation. This may result in significant legal costs being incurred, potentially over several years while the matter is investigated, charges are laid, and the case progresses through the court process. There may be very little "fault" or "knowledge" on the part of individual directors. This process is wasteful and time-consuming for the parties, including the court, the FMA and insurers who provide indemnity.

When examining the benefit of proceedings against directors for deemed director liability, the question is what public policy outcomes are achieved. It appears unlikely that the number of disclosure or financial reporting contraventions will fall because charges or claims are filed against directors. However, a possible adverse outcome is that experienced directors are deterred from continuing to serve on boards, which would be counterproductive given the scarcity of qualified and experienced directors in New Zealand.

**2.11 Do you have a preference not reflected in the options in relation to deemed director liability?**

ICNZ does not have a preference beyond the options identified in the consultation paper.

**2.12 Do you have other comments on what the Government should consider in relation to deemed director liability?**

ICNZ does not have any further comments on deemed director liability.

**2.13 Are there international models you would like the Government to consider?**

ICNZ recommends that MBIE consider comparable overseas models, including Australia, Singapore, Canada and Ireland, to inform any changes to civil liability settings and ensure New Zealand's framework remains proportionate, effective and internationally aligned.

**2.14 Please share any other comments, evidence or data you have on civil liabilities.**

ICNZ does not have any further comments, evidence or data to provide on civil liabilities.

## Issue 7: Auditor liability

**7.1 Do you agree with the scope of this issue as outlined above (i.e., limiting consideration to FMC audits and civil liability for unintentional wrongdoing)? If not, what else do you think should be considered?**

Yes, ICNZ agrees with the scope outlined for options for change.

**7.2 Do you agree with how the problem definition is summarised above? Please provide additional information and detail if you think this needs to be refined.**

Yes, ICNZ agrees with the problem definition.

**7.3 The problem definition discussion above lists a number of issues that it is contended are faced by the audit market in New Zealand. Do you agree with these? Are there other issues we should consider? To what extent are these issues caused by the liability exposure of auditors? Are there other factors that are causing these? Please provide concrete evidence and data to support your response where possible.**

Yes, ICNZ agrees with the issues identified in the discussion document. ICNZ also considers that the Government should consider the broader commercial context in which FMC audit-related civil liability claims arise. In practice, these claims may involve reliance not only on audit reports, but also on advice or work undertaken by other professional advisers, including accountants, solicitors, valuers, actuaries and bankers.

**7.4 Do you agree with how the options are summarised above? Are there other options we haven't considered? Please provide additional information and detail if you think these need to be refined.**

Yes, ICNZ agrees with the options considered.

**7.5 Do you have a preferred option? If so, please give your reasons for preferring it (with reference, if possible, to how it would assist addressing the issues with the audit market in New Zealand) and provide as much information as you can in support of your preference, along with any other matters we would need to take into account when designing the detail of that option.**

Of the options set out in the discussion document, ICNZ's preferred option is Option A: status quo – auditors are subject to joint and several liability with no limitation of that liability. We consider that Option B: capped liability and Option C: contractual limitation of liability may create uneven treatment among professions involved in the same loss.

Although it was not an option raised in the discussion document, ICNZ suggests that MBIE should use this review as an opportunity to explore the merits of a proportionate liability regime for auditors and other professional advisers to NZX entities. Such a review could examine the potential benefits and risks of a proportionate liability model, including whether it would provide a more balanced allocation of liability reflecting each party's relative responsibility.

In contrast, the joint and several liability model can, in some circumstances, produce outcomes that do not align with relative fault. This may arise where recovery is influenced by the availability and limits of professional indemnity insurance held by particular parties, whether insurance responds to the claim, or whether policy limits have been exhausted. In multi-defendant litigation, the practical allocation of claims and settlements may be influenced by the solvency of defendants, the existence and limits of available insurance, exclusions, erosion of limits by defence costs, and the ability to enforce contribution claims. These factors can create incentives to pursue an insured or financially viable defendant for a share of loss that exceeds that defendant's relative responsibility.

**7.6 What are the risks associated with limiting liability for auditors in any of the ways indicated in Options B and C? For example, what would the impact on plaintiffs be? And where else might plaintiffs look to recover losses? Would audit quality suffer?**

The key risk is that plaintiffs, including class action plaintiffs, may be unable to recover the full amount of their losses. Options B and C may shift unrecovered losses to plaintiffs, particularly where other potential defendants are unavailable, uninsured, underinsured, or unable to meet the claim. We acknowledge that this would also be a risk if a proportionate liability regime were introduced.

**7.7 Do you see any issues with introducing a capping scheme just for auditors where other professions – e.g. lawyers and accountants – would still be jointly and severally liable for a loss where more than one party has a role?**

Yes. ICNZ sees issues with introducing a capping scheme for auditors alone while other professional advisers remain subject to joint and several liability. Such an approach would address only one part of a broader liability framework and may create uneven treatment between professions involved in the same loss.

An auditor-only cap may produce liability displacement rather than an overall reduction in claims. Plaintiffs and co-defendants may redirect claims towards directors, officers and other professional advisers whose liability remains uncapped. This could increase defence costs, contribution disputes and pressure on D&O and professional indemnity capacity in those sectors. MBIE should therefore model not only the reduction in auditor exposure, but also the likely destination of unrecovered losses and claims.

**7.8 Are there any other issues relating to auditor regulation and the state of the audit market in New Zealand that you would like to bring to our attention?**

Yes. ICNZ understands that there are concerns about the availability of auditors qualified to undertake FMC audits. ICNZ supports initiatives that increase the number of suitably qualified and licensed FMC auditors but considers that any changes to regulatory settings should maintain appropriate standards of capability, experience and quality assurance. Any expansion of the market to additional firms should not come at the expense of audit quality, given the complexity of FMC audits and the reliance that wholesale and retail investors place on audit reports when making investment decisions.

**7.9 Please share any other comments, evidence or data you have on auditor liabilities or related topics.**

ICNZ's experience is that claims involving auditors can be complex, lengthy and costly to resolve, including because of the legal and expert input often required. This reinforces the importance of liability settings that are clear, proportionate and workable in practice.

## Conclusion

Thank you again for the opportunity to submit on this matter. ICNZ would welcome the opportunity to engage further with MBIE as policy work progresses.

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

Ngā mihi,

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