

18 June 2019

Financial Markets Policy
Building, Resources and Markets
Ministry of Business, Innovation and Employment
PO Box 1473
WELLINGTON 6140

Email to: FinancialConduct@mbie.govt.nz

Dear Sir/Madam

Re: Conduct of Financial Institutions Options Paper

I am writing to you regarding the Ministry of Business, Innovation & Employment (MBIE) Options Paper, entitled *Conduct of Financial Institutions* (referred to as 'the Options Paper').

While the Options Paper covers a variety of future possibilities, we wish to concentrate our comments on a few fundamental issues we believe MBIE needs to consider.

Background

Parallel Papers

We note the parallel options paper on insurance contract law is being issued simultaneously with that addressing the conduct of financial institutions. BusinessNZ will not be submitting on the former as it is more industry-specific, compared with the general options applicable to the overall conduct of financial institutions.

General view of the Options Paper

Overall, we believe the Options Paper lacks sufficient evidence to justify regulatory intervention. Our main concern is the disconnect between the conceptual risks identified through both domestic and Australian reviews, and any existing evidence of consumer harm in New Zealand. Any case for policy change requires clear and overwhelming evidence as to the extent of the problem to be rectified. Unfortunately, BusinessNZ does not see an overwhelming need to make changes when the case for intervention appears limited at best.

At the very least, we believe a cost-benefit analysis of all elements in the package is required, making it clear to submitters what the effects of the various options will be.

Initial Preferred Package of Options

Notwithstanding our overarching concerns above, table 1 below outlines our initial thoughts on the range of options presented, should they proceed.

Table 1: Preferred MBIE Options & BusinessNZ Comments

Option	BusinessNZ Support?	Comments
<p>Initial Preferred Package of Options</p> <ol style="list-style-type: none"> 1. A duty to consider and prioritise customer’s interest, to the extent reasonably practicable. 2. A duty to act with due care, skill and diligence. 3. A duty to consider the information needs of customers and communicate in a way which is clear and timely.*Options 3-6 don’t match the wording of the options paper – no biggie? 4. A duty to manage conflicts of interest fairly and transparently. 5. A duty to ensure complaints are handled fairly, timely and transparently. 6. A requirement to have the systems and controls in place that support good conduct and address poor conduct. 	<p>In principle, BusinessNZ generally takes the view that these six proposed duties are appropriate for inclusion in a conduct regime.</p>	<p>While BusinessNZ does not have any strong concerns with the suggested duties and requirements outlined, we believe they must be very carefully thought through in terms of what would be required before legislation is considered.</p> <p>Although we favour a principle-based regime over one that is prescriptive in nature, any set of principles still needs to be supported by certain details, usually provided through codes and guidance material.</p>
<p>Options to Improve Product Design</p> <ol style="list-style-type: none"> 1. Give the regulator the power to ban or stop the distribution of specific products. 2. Ban certain products. 3. Requirement for manufacturers to identify intended audience for products AND a requirement for distributors to have regard to the 	<p>BusinessNZ believes options 1 and 3 could be considered further.</p> <p>Option 2 should not proceed.</p>	<p>While we are not averse to option 1, there would need to be considerable work undertaken to develop this option before the legislative phase begins. In short, the Government would have to engage in a transparent and robust process before any product is banned.</p> <p>BusinessNZ believes that a well-crafted regulatory design around option 1 would make option 2 largely redundant. However, a simple ban of certain products would be a blunt</p>

<p>intended audience when placing the product.</p>		<p>regulatory tool that would most likely not consider several of the factors outlined in the Options Paper. From our perspective, banning certain products involves zero benefit to customers. Any product should be valued on more than simply the proportion of claims. Many customers of these products derive value from knowing they are covered for certain eventualities - funeral cover, for example - so costs are not passed on to other family members. Also, if a product is banned, would there be an opportunity for adjustments and what would banning a product mean for others similar in nature?</p> <p>Option 3 has two distinct parts. First, despite best intentions, the ability for manufacturers to identify the intended audience for products may not always fit with the product's end users. A product design phase may identify a group or groups of people most likely to purchase the product, but this may be honed down or even changed when in the market. Therefore, we urge caution in placing too much expectation around the identification of an intended audience.</p> <p>Second, we would expect distributors to have regard to the intended audience when placing the product, given that is part and parcel of ensuring a logical fit around the point at which the product is distributed. However, at the same time, distribution obligations should not be so narrow as to substantially limit consumer choice. There will always be customers who do not fit neatly into a certain category, so a wider application of product options should be considered.</p>
<p>Options to Improve Product Distribution</p> <ol style="list-style-type: none"> 1. A duty to design remuneration and incentives in a manner that is likely to promote good customer outcomes. 2. Ban target-based remuneration 	<p>In principle, we are not against options 1 and 5. However, options 2, 3 and 4 may create practical problems.</p>	<p>As with our views on 'Initial Preferred Package of Options' above, we are not against options placing duties on the industry, as long as these are well designed and practical in their nature.</p> <p>From our perspective, options 2, 3 and 4 are all absolute outcomes that represent significant shifts up the</p>

<p>and incentives, including soft commissions (applies to both in-house and to intermediaries).</p> <ol style="list-style-type: none"> 3. Prohibit all in-house remuneration and incentive structures linked to sales measures. 4. Impose parameters around the structure of commissions (i.e. commissions paid to intermediaries). 5. A duty on manufacturers to take reasonable steps to ensure the sales of its products are likely to lead to good customer outcomes. 		<p>regulatory pyramid. If option 1 is implemented successfully, then the need for options 2-4 would largely be redundant.</p>
<p>Options Relating Specifically to Insurance Claims</p> <ol style="list-style-type: none"> 1. Duty to ensure claims handling is fair, timely and transparent. 2. Requirement to settle claims within a set time, with exceptions for certain circumstances. 	<p>BusinessNZ would support a well-constructed legislative duty around option 1.</p> <p>We do not support option 2.</p>	<p>As part of good business practice in such industries, we would expect any claim to be handled in a fair, timely and transparent manner. If this was not the case with certain businesses in that sector, there would be opportunities for others to compete for the business. Therefore, we would again need greater detail about how any legislative duty in this area would lead to better outcomes than currently exist.</p> <p>We do not support option 2 given each claim has its own situations and facts. Simply assigning a timeframe to settle claims could create a worse outcome for a larger proportion of customers. Too short a timeframe would lead to rushed outcomes. Too long a timeframe would essentially make any need for such requirements redundant. In addition, certain claims simply require a longer timeframe to ensure the right outcome is achieved. As with other regulatory interventions, placing an arbitrary restriction across an industry can often result in the solution being worse than the problem.</p>
<p>Options for Tools to Ensure Compliance1. Empower and resource the FMA to monitor and enforce compliance.2. Entity</p>	<p>BusinessNZ has no strong views on these options.</p>	<p>While BusinessNZ has no strong views either way regarding the options for tools to ensure compliance, we would be concerned if any of these approaches led to significant costs for</p>

<p>licensing.</p> <p>3. Broad range of regulatory tools.</p> <p>4. Strong penalties for non-compliance.</p> <p>5. Executive accountability.</p> <p>6. Require whistleblowing procedures to be in place.</p> <p>7. Require regular reporting about the industry.</p> <p>8. Greater role for industry bodies.</p>		<p>providers, without much material benefit to customers.</p> <p>Also, the government needs to have a clear idea about how any of these tools would complement other proposed changes in the sector. We would not support a raft of changes that essentially saw contradictory obligations or outcomes with other legislative requirements.</p>
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Going forward – need for an Exposure Draft Bill

Combined, the potential for unintended consequences with these proposals leads us to strongly recommend an Exposure Draft Bill be part of the consultation process. Unfortunately, BusinessNZ has repeatedly seen poor regulatory processes where there has been an illogical disconnect between the recommendations of the discussion paper and the Bill that follows.

Ultimately, a Bill should not see significant changes if the consultation process behind it has been rigorous and transparent. Given the high propensity for unintended consequences, proposals need to be carefully considered before legislation is passed. An Exposure Draft Bill provides a useful opportunity to address such concerns.

Thank you for the opportunity to comment, and we look forward to further discussions.

Kind regards,



Kirk Hope
Chief Executive
 BusinessNZ