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Financial Markets Policy
Building, Resources and Markets
Ministry of Business, Innovation & Employment
PO Box 1473
Wellington 6140
New Zealand

Conduct of Financial Institutions Options Paper

Thank you for the opportunity to comment on the Conduct of Financial Institutions Options Paper.

This submission is made on behalf of Trade Me. We are New Zealand's largest online auction and classified listing platform. We facilitate millions of transactions each year between our four million members, and employ approximately 600 people (primarily in Wellington, Auckland and Christchurch).

In addition, we operate an insurance comparison service called LifeDirect, where consumers can compare and buy different personal insurance products from New Zealand's leading insurers. We also market general insurance products through Trade Me Insurance, which is underwritten by TOWER New Zealand.

There are a range of issues being considered in the Options Paper. We have focussed on the aspects most relevant to our scope of operations.

Role and benefit of comparison websites

We noted the following paragraphs in the Options Paper on comparison websites:

> *52. Comparison websites exist for some types of financial products e.g. life insurance, credit cards and KiwiSaver. They do not currently exist for general insurance. Discussions with companies providing comparison websites for other parts of the financial sector have suggested that the fact there is a small number of general insurers, each with a significant share of the market, means that if any one general insurer does not wish to participate in a comparison website then the website cannot offer a meaningful comparison and is therefore not viable. General insurers have actively discouraged the development of comparison websites, suggesting that regulation might be required before a general insurance comparison website could be established.*
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> *53. However, while comparison websites can help at the point of purchase, they cannot inform consumers about their ongoing experiences. Product comparison websites which inform consumers prior to purchase cannot effectively alleviate difficulties that exist after the product has been purchased.*

We think that comparison websites like LifeDirect can be powerful consumer enhancing platforms. We provide a meaningful comparison tool for consumers to assess the personal insurance products offered by the insurers featuring on LifeDirect, and believe we could provide similar benefits for consumers if we could feature general insurance products as well.

The benefits of a comparison site extend beyond customers who take out policies. For example, non-customers may use a comparison site to sanity check insurance products offered by other insurers to see if the proposed (initial or renewal) premium aligns with the market. We periodically measure the reasons why customers visit our site, and many of the responses indicate that customers use our platform to inform themselves about their ongoing insurances, and not just to compare and buy a new insurance product.

We think comparison websites could play a bigger role in alleviating difficulties after purchase. For example, we could provide comparison information on consumer experiences with making claims, average claim processing times etc. Similarly, information relating to the proportion of premiums paid out in claims, or the proportion of claims paid out could be relevant metrics for consumers to compare to help them make an informed choice when choosing and purchasing a personal insurance product. This would also be helpful to customers who have a policy and wish to have a useful benchmark to assess that policy against. However, our current scope is limited by the information that is made available to us by insurers. They often use different calculations and measures, making comparison of the information sets more challenging.

The services offered through LifeDirect extend beyond comparison services for customers making their first personal insurance purchase. We have an increasing focus on servicing existing customers, both in terms of encouraging them to review their cover levels to ensure their insurance products are still appropriate for their needs, and helping them make any claims under their existing insurance policies as simply as possible. LifeDirect intends to introduce a customer lifecycle programme in 2020 which will further enhance this service for our customers.

Questions 1-3: Re overarching duties

The Options Paper recommends the following set of overarching duties:

- A duty to consider and prioritise the customer's interest, to the extent reasonably practicable.
- A duty to act with due care, skill and diligence.
- A duty to pay due regard to the information needs of customers and to communicate in a way which is clear and timely.
- A duty to manage conflicts of interest fairly and transparently.
- A duty to ensure complaints handling is fair, timely and transparent.
- A requirement to have the systems and controls in place that support good conduct and address poor conduct.

On our initial reading of the Options Paper, we believe our current operations would comply with each of the proposed duties. Whilst the overarching duties apply primarily to Financial Institutions rather than to intermediaries and distributors, our experience is that often the compliance guidelines prepared by regulators don't consider in any detail innovative or non-conventional business models. In the case of guidance that a regulatory body like the FMA may issue to insurers about these duties, we expect this guidance may lead to some uncertainty for LifeDirect and resolving this uncertainty inevitably gives rise to inefficient business costs and outcomes. Each Financial Institution can have many distributors of their product, and each distributor can distribute products from many Financial Institutions. Given the likelihood of each Financial Institution managing the conduct of its intermediaries and distributors differently, this creates a significant risk of excessive compliance activity and cost to the intermediaries and distributors.

We think it would be useful if any legislative regime or guidance included examples which highlight the actions that must be taken to meet a duty will depend on the extent of a business' functions (i.e. underwriters, advisers and other sales channels might all need to take different actions to satisfy the same underlying duties). For example, we consider that the actions required to meet a duty of care, skill and diligence when operating a comparison website would be different to the actions required to meet a duty of care, skill and diligence in providing and underwriting an insurance product.

In respect of fair and transparent conflicts of interest, we are keen to understand how you envisage this duty being satisfied in practice. As discussed further below, we receive commissions for insurance products purchased through LifeDirect. However, our platform enables our customers to filter insurance products based on the variables they identify as important to them. The commission we receive on an insurance product doesn't influence the insurance product results shown to a potential customer. In respect of transparency, we think it should be adequate to disclose that a commission is received. In practice it would be difficult to disclose the precise commission received for any particular insurance product that is taken out.

Questions 4-5: Re product design

The Options Paper discussed:

- Giving the regulator the power to ban or stop the distribution of specific products.
- A ban on certain products.
- A requirement for manufacturers to identify intended audience for products and a requirement for distributors to have regard to the intended audience when placing the product.

We're in favour of future proofing legislation where possible. So, we think it would be preferable to give the regulator the power to ban the distribution of specific products rather than ban particular products in parent legislation.

We are generally supportive of a requirement for manufacturers to identify the intended audience for a product and a requirement for distributors to have regard to the intended audience when placing products. If information on intended audience was readily available in a standard format for all insurance products then it would be useful information for consumers, and it would be a useful input into our comparison services. That said, a consumer's individual situation and individual insurance preferences can vary from the generalised group/class that they are in – such that a consumer that is not part of the intended audience may want to purchase a product that isn't intended for them. We don't think there should be a restriction against this.

LifeDirect can provide further value to customers to help translate policy documentation into simpler, easier to understand language, which is consistent across insurers. In line with option 3, the use of simpler, more consistent language will help improve financial literacy, and allow easier comparison of policies to ensure the consumer is making an informed decision. LifeDirect includes a library of articles which help improve consumers' financial literacy. Our F20 strategy includes incorporating better linkage to these articles to provide more detail to the customer at the relevant point in time. For example, we provide information on the difference between level premiums and rate for age (stepped) premiums.

Questions 6-7: Product distribution

The Options Paper recommended the following measures to apply to all monetary and non-monetary benefits of internal staff and external intermediaries:

- A duty to design remuneration and incentives in a manner that is likely to promote good customer outcomes.
- A ban on target-based remuneration and incentives, including soft commissions (this would apply to both in-house staff and to intermediaries).
- Prohibit all in-house remuneration and incentive structures linked to sales measures.
- Impose parameters around the structure of commissions (i.e. commissions paid to intermediaries).
- A duty on manufacturers to take reasonable steps to ensure the sales of its products are likely to lead to good customer outcomes.

External intermediaries, advisers and comparison services incur costs in providing their services and running their businesses, as well as typically having a driver to return a commercial profit. A variable structure (where payment is made per service, such as a commission arrangement) is a logical remuneration method for a comparison service and other intermediaries and advisers, given the services performed for any given insurer will vary based on what insurance policies are written or what enquiries are made. LifeDirect does not consider there are ethical concerns with a commission model per se. The concern is more that salespeople could be motivated by their personal commissions, rather than consumer outcomes when recommending insurance products.

This ethical concern isn't a problem for LifeDirect. Our business model enables consumers to inform themselves via the provision of information, and the ability to compare and contrast the different policies they might be interested in online. As mentioned above, the commission rates earned vary materially, but do not impact in any way on the order in which a consumer sees the products they wish to compare. The consumer selects the sort order which is most appropriate for them.

Our focus is always on providing as much information as possible so that consumers can make an informed decision about what insurance products might best meet their insurance needs. We do not provide individual advice to any consumer, and as a result there is not the risk that an individual adviser is inappropriately motivated by the sales commission they receive.

Similarly, target-based commissions do not inherently give rise to consumer harm. For example, if LifeDirect achieves more than a certain number of policies in a month, an insurer may incur reduced costs per policy in working with LifeDirect.

LifeDirect is concerned that bans and prohibitions will result in previously rational commercial payment structures that cause no consumer harm becoming illegal. We would prefer a more nuanced and principled approach to commissions. For example, parameters around the use of commissions.

We are more comfortable with the proposal to introduce a duty on manufacturers to take reasonable steps to ensure the sales of its products are likely to lead to good customer outcomes.

Questions 8-10: Insurance claims

Given how our insurance business is structured, LifeDirect's direct involvement in the handling and processing of claims is predominantly administrative.

Question 11: Empower and resource the FMA to monitor and enforce compliance

We agree that the FMA would be the most appropriate regulator, and that consumers are unlikely to individually or collectively take action against a financial or insurance institution so a regulator would be required to enforce conduct obligations.

There would be a cost to us in complying with a new regulatory regime. As we are remunerated by commission, we'd likely expect to negotiate an increase in our commission payments to cover these costs.

We expect insurers would raise premiums to consumers to cover their additional compliance costs. Given the intent for the financial institution to have the responsibility of good customer outcomes when the product is sold through an intermediary, we expect that the Financial Institutions will impose additional compliance and reporting requirements onto the intermediaries. As many intermediaries distribute multiple Financial Institutions products, this could lead to extensive different requirements for the intermediaries, which could become very costly. This could ultimately force many intermediaries out of the industry, thus reducing the options for consumers, reducing financial literacy and increasing the problem of under insurance in New Zealand.

Question 12: Entity licensing

We do not support the proposal to require entities to obtain a 'conduct' licence to operate. We think the costs of such a regime would swamp its benefits. A licensing regime would create an additional barrier to entry and significant compliance costs for new and innovative business models.

We are not aware of historical concerns of non-compliance with regulatory obligations. We expect that insurers will comply with new legislative requirements, without the imposition of a formal licensing regime. If compliance did become a problem following a new regime being introduced, then a licencing regime could be subsequently introduced.

Questions 13-15: Regulatory tools, penalties and executive

Our initial view is that alignment of the penalty regime with the existing penalty regime appears sensible. We do not think the penalties for non-compliance should be higher than the existing FMC Act penalties.

We are concerned about the potential for personal liability of executives, primarily because it could lead to less innovation. For example, a business like LifeDirect offers a unique set of services as compared to a standard broker or adviser. There is effectively a demarcation point where our visibility ends and the insurer's commences. It may be difficult to attract capable senior managers to an innovative new business model that only sees part of the product life cycle if there are significant personal liabilities.

Thanks and further involvement

Thanks for the opportunity to be consulted on the Options Paper. We'd be happy to discuss any aspect of our submission in person with MBIE. We look forward to further opportunities to comment as this policy work progresses.

Sincerely

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