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Financial Markets Policy
Commerce, Consumers and Communications
Ministry of Business, Innovation and Employment
PO Box 1473
Wellington 6140

CONSULTATION – REGULATIONS TO SUPPORT THE NEW REGIME FOR THE CONDUCT OF FINANCIAL INSTITUTIONS

This submission is made on behalf of AIA New Zealand Limited and its related entities (together "AIA NZ"). It relates to the Ministry of Business, Innovation and Employment's April 2021 discussion document on regulations to support the new regime for the conduct of financial institutions. AIA NZ has provided a separate submission on the discussion document relating to the treatment of intermediaries under the regime.

About AIA NZ

AIA NZ is a member of the AIA Group ("AIA"), which comprises the largest independent publicly listed pan-Asian life insurance group. It has a presence in 18 markets in Asia-Pacific and is listed on the Main Board of The Stock Exchange of Hong Kong. It is a market leader in the Asia-Pacific region (excluding Japan) based on life insurance premiums and holds leading positions across the majority of its markets.

Established in New Zealand in 1981, AIA acquired Sovereign Assurance Company Limited in 2018 which, at the time, was New Zealand's largest life insurer having been in business in New Zealand for over 30 years. Sovereign formally amalgamated under the AIA brand in August 2019, and we have been protecting New Zealanders and helping them to lead Healthier, Longer, Better Lives ever since.

AIA NZ offers a range of life and health insurance products that meet the needs of over 450,000 New Zealanders. AIA NZ is committed to an operating philosophy of *Doing the Right Thing, in the Right Way, with the Right People*. AIA NZ launched the New Zealand Conduct Framework in January 2019 to help ensure the consistent delivery of good customer outcomes across the organisation.

In addition to being a licensed insurer, AIA NZ (through its subsidiary AIA Services New Zealand Limited) is a licensed financial advice provider and provides financial advice services through two authorised bodies: AIA Thrive Limited and AdviceQual Limited. AIA NZ is also a prominent member of the Financial Services Council ('FSC').



Key submission points

AIA NZ continues to broadly support the conduct regime that will be introduced by the Financial Markets (Conduct of Institutions) Amendment Bill ("Bill"). We also largely support the proposals outlined in this discussion document, but have some specific points of feedback on their implementation.

The key points of our submission are:

- We consider a principles-based approach to sales incentives would be preferable to an outright prohibition. A principles-based approach is more likely to achieve balance between the needs of consumers, advisers, FAPs and financial institutions.
- In general, AIA NZ believes the Bill contains sufficient detail and therefore that regulations are largely unnecessary at this time. Time should be given for changes already made by the industry and for the Bill, once in force, to embed before additional regulations are considered. If additional detail is needed, we suggest Financial Markets Authority guidance (issued after consultation) would be a better option. Guidance is generally more agile and can be better tailored to industry-specific issues.

Our full submission is **attached**, and follows the format outlined by MBIE. In addition to our own submission, we contributed to and support the FSC submission on this discussion document.

Confidentiality / release of information

This submission contains some information that is confidential, as identified in our response. We kindly request that if a request under the Official Information Act 1982 for this submission is received, the indicated confidential information is withheld.

We would be pleased to discuss any questions you have on this submission and we would welcome the opportunity to collaborate or consult further with MBIE as it considers the next steps.

Yours sincerely

Nicholas Stanhope
Chief Executive Officer
AIA New Zealand

Regulations to support the new regime for the conduct of financial institutions

Your name and organisation

Name	Privacy of natural persons
Email	
Organisation/Iwi	AIA New Zealand Limited

[Double click on check boxes, then select 'checked' if you wish to select any of the following.]

The Privacy Act 1993 applies to submissions. Please check the box if you do not wish your name or other personal information to be included in any information about submissions that MBIE may publish.

MBIE intends to upload submissions received to MBIE's website at www.mbie.govt.nz. If you do not want your submission to be placed on our website, please check the box and type an explanation below.

Not applicable.

Please check if your submission contains confidential information:

I would like my submission (or identified parts of my submission) to be kept confidential, and **have stated below** my reasons and grounds under the Official Information Act that I believe apply, for consideration by MBIE.

We would like identified parts of this submission to be kept confidential because the identified information is sensitive information about AIA NZ's business, and its disclosure would be likely unreasonably to prejudice our commercial position (section 9(2)(b)(ii) of the Official Information Act 1982).

Requirements for fair conduct programmes

	<p>Do you have any comments on the status quo i.e. no further regulations to support the minimum requirements for fair conduct programmes in the Bill?</p>
1	<p>As a general proposition, and subject to our comments elsewhere in this part of our submission, AIA NZ's view is that regulations are not needed to support the minimum requirements for fair conduct programmes. We agree that changes made by the Finance and Expenditure Committee have added clarity by, in effect, elevating detail that would otherwise have been included in regulations into the Bill itself. For the most part, those changes negate the need for regulations – particularly when, as the discussion document notes, FMA is likely to develop guidance over time as the regime evolves.</p>
2	<p>Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(a)?</p>
	<p>AIA NZ agrees that, at this time, regulations are not needed to support section 446M(1)(a).</p>
	<p>Do you have any comments on the proposals regarding distribution of relevant services and associated products? We are particularly interested in how these proposals may be implemented.</p>
3	<p>AIA NZ considers that the requirements of the Bill, as they relate to the distribution of relevant services and associated products, are sufficiently clear and, as such, further regulations are not needed in this area. Should it become apparent as the regime evolves that financial institutions require further guidance, we suggest that FMA guidance would be a more effective way to outline expectations.</p>
	<p>If regulations are considered necessary, care must be taken to ensure they are reasonable and pragmatic. While it is reasonable for a financial institution to identify target groups of customers when developing products and develop those products based on the groups' likely requirements and objectives there are limitations to how granular such an analysis can be based on the data held by insurers (and other financial institutions) on their customers. In some cases, target customers will be defined broadly on the basis of shared characteristics of the general population rather than at the level of an individual consumer or narrowly defined sets of consumers. Ultimately, however, the suitability of a product for an individual customer will depend on that customer's individual circumstances, which in most cases won't be known by the institution.</p>
4	<p>Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(ac)?</p>
	<p>AIA NZ agrees that, at this time, regulations are not needed to support section 446M(1)(ac).</p>
	<p>Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(bb) to (bd)?</p>
5	<p>AIA NZ agrees that, at this time, regulations are not needed to support sections 446M(1)(bb) to (bd), as they apply to employees or agents.</p>
	<p>Please refer to our submission on the separate discussion document on the treatment of intermediaries for our feedback on proposed amendments to the Bill.</p>

Do you have any comments on the proposal to specify further minimum requirements regarding remediation of issues? Are there any further specific remediation principles that should be specified in regulations?

AIA NZ generally supports the potential additional requirements outlined in paragraph 66 of the discussion document relating to the remediation of issues. Additional detail will help in ensuring a consistent standard of remediation across the wider industry.

However, we have the following comments:

- Requirements (b) and (c) contemplate an institution taking "all reasonable steps". We suggest this should be replaced with "reasonable steps". At law, the requirement to take "all reasonable steps" sets a high bar. While we agree that remediation is hugely important, practical considerations may arise relating to the legacy nature of insurance businesses that impact the ability to remediate issues in a timely and efficient manner – for example, gaps in historical (sometimes decades old) information requiring approximations or reasonable assumptions to be made in identifying impacted customers or calculating remediation amounts. Adopting a threshold of "reasonable steps" would also align with section 446M(1)(ad), which is the existing clause in the Bill addressing remediation.
- Proposed requirement (b) would require the remediation of all affected customers. As the discussion document notes, this is not always possible – for example, where a financial institution does not have current contact details for a customer and cannot locate them after taking reasonable steps. We suggest the requirement should specifically acknowledge that, where a financial institution has not been able to contact a customer having made reasonable efforts to do so, remediation for an affected customer is not required with remediation monies to be subject to the unclaimed monies process.
- A financial materiality threshold should be included, such that remediation for any individual customer is not required where the amount of compensation involved is below a threshold. We would anticipate this threshold being set at a low level. There is precedent for this approach – regulation 99(3) of the Financial Markets Conduct Regulations 2014 allows a manager and supervisor to agree a materiality threshold for compensating consumers for pricing errors in retail managed investment schemes. A materiality threshold would help address the significant cost / benefit considerations in remediation activities and would allow financial institutions to focus remediation resources on activities that would have a bigger impact on customers.
- We consider it important that regulations set a long stop for remediation activities which would help to balance the interests of impacted customers against the interests of all customers who will ultimately be affected by the total cost of remediation activities. For example, we suggest that remediation should only be required for customer detriment over the last 15 years. This aligns with the longstop period for a money claim set out in the Limitation Act 2010.
- Proposed requirement (d) contemplates review and remediation processes being "adequately resourced". While review and remediation activities are inherently time intensive, they are not necessarily constant so financial institutions may scale or allocate remediation resources according to the nature of the issues. This will often involve a reallocation of resource from within the business to ensure that remediation activities are supported with appropriate subject matter experts with relevant institutional knowledge to resolve the issue. In practice, these resources are difficult to source externally so

reasonable prioritisation decisions are required. Regulations should recognise these constraints and allow for reasonable flexibility.

- Proposed requirement (e) contemplates adequate records being kept. Clarity is needed on how long records are to be kept for.
- Proposed requirement (f) contemplates clear, concise, timely and effective communications about the progress and outcome of remediation. Where an issue requiring remediation is discovered by proactive work (rather than as a result of a customer complaint) it is common to communicate with customers only after the issue has been fully investigated and a financial institution is ready to remediate. This provides a better customer experience and allows for the involvement of other stakeholders (e.g. the servicing adviser). We suggest the requirement should provide greater flexibility about communications. One option would be to adopt a more principles-based approach to simply require clear, concise, and effective communications about review and remediation processes as is reasonable given the nature of the incident. This would also have the benefit of aligning with section 446M(1)(bf).

7 Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(be)?

AIA NZ agrees that, at this time, regulations are not needed to support section 446M(1)(be). We agree that incentive structures within financial institutions have already begun to change following joint Financial Markets Authority and Reserve Bank of New Zealand reviews.

Please also see our comments on questions 17 to 31 regarding the regulation of sales incentives.

8 Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(bf)?

AIA NZ agrees that, at this time, regulations are not needed to support section 446M(1)(bf). We agree with the comment in paragraph 77 of the discussion document about the importance of ongoing customer communications and support.

9 Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(d)?

AIA NZ agrees that, at this time, regulations are not needed to support section 446M(1)(d).

10 Do you have any comments on the proposal to specify further minimum requirements regarding consumer complaints handling?

AIA NZ does not have a strong view on this proposal. AIA NZ already has an extensive complaints handling process that will become part of our fair conduct programme, and our expectation is that this is true of all other financial institutions.

If additional requirements are introduced, they should align with the standard condition applying to financial advice providers, as is proposed in the discussion document, and a definition of complaint (also aligning with those standard conditions) should be included.

11 Do you have any comments on the proposals to specify further minimum requirements regarding claims handling and settlement?

AIA NZ supports this proposal and agrees with the list of matters outlined in paragraph 99 of the discussion document.

While we support this proposal, we do not think it will make a significant difference for life insurance consumers. AIA NZ understands how important it is for consumers that claims are handled in a fair, transparent, and prompt way. We invest significant resource in our claims handling functions, and our claims teams are measured on customer experience. We look to support customers by (for example) proactively checking all policies a customer holds to identify the possibility of additional claim payments and we make advance payments when appropriate to assist a customer.

In practice, difficulties at claim time are typically attributable to delays outside the insurer's control – for example, in receiving the information needed to properly consider or pay a claim.

Some claims are, by their nature, complex and take more time to consider – for example, claims involving complex non-disclosure issues or cases where a claim does not meet the policy wording but merits consideration due to individual circumstances. These may also require the opinion of third parties, such as reinsurers. It is important that regulations are sufficiently flexible to provide insurers with the capacity to continue to prudently and fairly assess claims.

Do you have any comments on the proposed definition of 'handling and settling a claim under an insurance contract'?

12

AIA NZ agrees that this definition captures the activities involved in handling an insurance claim. However, while we agree with the definition, we do not think it needs to be included. In our opinion, this would add an unnecessary level of detail into what is generally intended to be a principles-based set of regulations.

Please refer to our submission on the separate discussion document on the treatment of intermediaries for our feedback on the concept of "agents".

Do you have any comments on the discussion regarding customer vulnerability?

13

AIA NZ agrees that, at this time, specific regulations addressing customer vulnerability are not needed. We agree that a vulnerability lens will be a necessary part of fair conduct programmes, and is already required by section 446M(1). We also agree that, at this stage, more detailed requirements are better addressed by way of FMA guidance.

Do you have comments regarding the option of including vulnerable consumers in section 446M(1A)?

14

AIA NZ does not think it is necessary to include vulnerable customers in section 446M(1A). While this is a significant and complex issue, in our view it is unlikely to benefit from additional regulation. In our opinion, the treatment of vulnerable customers is better addressed by way of FMA guidance.

Do you think any further factors should be added by regulations to the list under section 446M(1A)?

15

AIA NZ does not think there are any further factors that should be added by regulations to the list under section 446M(1A).

16

Do you think any other regulations that could be made under new section 546(1)(oa) are necessary or desirable? Please provide reasons for your comments.

AIA NZ does not think any other regulations under section 546(1)(oa) are necessary or desirable.

Sales incentives

Do you have any comments on the Status Quo (no regulations)?

AIA NZ acknowledges the likelihood that regulations will be made, given previous Cabinet decisions to do so.

17

However, it is worth noting that other controls on incentives have been introduced following the joint Financial Markets Authority and Reserve Bank of New Zealand reviews. These include the new obligation for those providing financial advice to prioritise clients' interests, and the overarching obligation around the design and management of incentives that will be introduced by the Bill.

While we acknowledge the potential for consumer harm from poorly designed or managed incentives, AIA NZ believes that target or volume-based incentives can have a place within the industry provided that they support good customer outcomes. We do not believe these types of incentives inherently cause poor customer outcomes.

Do you have any comments on the option to prohibit sales incentives based on volume or value targets?

This is not AIA NZ's preferred option. While we acknowledge that a blanket prohibition would provide certainty, there are key disadvantages and unintended consequences with this option when compared to a principles-based approach (which AIA NZ prefers).

In particular:

18

- In some cases, volume-based incentives or value targets can and do support good customer outcomes. For example, AIA NZ and other financial institutions provide monetary payments to larger intermediaries to assist with the costs of compliance and oversight, which are typically higher for larger intermediaries because of the greater support they provide to their financial advisers which in turn supports good customer outcomes. In addition, AIA NZ and other financial institutions will often make additional business support services, professional development and training, and access to software available only to larger intermediaries. These additional benefits support the provision of quality financial advice and removing them to comply with the prohibition would have adverse unintended consequences. A minimum volume or value target is needed for these benefits in order to manage a financial institution's overall cost of providing the additional support.
- AIA NZ considers that it is reasonable for financial institutions to have short term incentives that include a volume-based element within a balanced scorecard, as this aligns with shareholder expectations. It is important to recognise that removing these measures entirely from financial reward is unlikely to change shareholder expectations. Balanced scorecards remain permitted in Australia because the equivalent Australian prohibition does not extend to employees who are not providing advice. We see no reason why balanced scorecards should not also be permitted in New Zealand.

- There is a risk that some financial institutions or intermediaries may restructure incentive arrangements in order to "skirt" the prohibition. This includes adopting less transparent arrangements that are not necessarily captured by financial advice disclosure requirements in the same way as incentives linked to sales. While the Bill's other provisions (particularly section 446M(1)(be)) should help to mitigate this risk, it would be avoided by a principle-based approach.

Please also see our response to question 24, where we suggest exclusions intended to address the first two points should this option be adopted.

What would the likely impacts be for financial institutions, intermediaries and/or consumers of prohibiting sales incentives based on volume or value based targets?

The life insurance market is highly competitive and intermediaries depend on commissions and other incentives to fund their business. Commission levels in New Zealand reflect the competitive market environment and what we understand to be a relatively low average premium size compared with other markets. Should the prohibition be introduced as proposed, AIA NZ's expectation is that financial institutions will restructure the way they pay intermediaries by increasing other forms of remuneration to maintain the overall "spend".

In addition, any changes to incentive arrangements have the potential to cause disruption in the industry more generally, which has the risk of leading to bad outcomes for customers. From a market stability perspective, it is important that advisers are appropriately remunerated, and we consider that any restrictions on payments to advisers should be focused on removing conflicts that could lead to poor customer outcomes.

19 Depending on the final scope of the prohibition (and any exclusions from it) there may be unintended consequences for intermediaries. This might include, for example:

- a reduction in access to support for compliance and oversight arrangements, professional development and training. We comment on this point in our response to question 18.
- a reduction in advisers. AIA Australia's experience is that the Australian market has experienced a significant reduction in advisers over the past few years, as an unintended consequence of increased regulation which has increased the cost to serve, at the same time as restrictions on remuneration have made the provision of advice less viable.

AIA NZ does not believe the change will have a significant impact on consumers when compared to other options (including no prohibition and relying on the status quo of new section 446M(1)(be)). While AIA NZ acknowledges the risk of significant harm from poorly designed or managed sales incentive, our view is that other changes proposed by the Bill, in conjunction with new duties under the FSLAA regime, are sufficient to mitigate these risks.

Do you have any feedback on a more principle-based approach to prohibiting some incentives?

20 This is AIA NZ's preferred approach. As noted above, AIA NZ believes that target or volume-based incentives do have a place within the industry provided they support good customer outcomes. A principles-based approach could allow positive incentives to remain while prohibiting the arrangements that have the most potential to cause harm.

We acknowledge that this approach could create uncertainty, when compared to MBIE's preferred option, and result in inconsistent treatment across the industry. However, we think

these risks could be managed. This option would also avoid the key disadvantages of a blanket ban, being the risk of unintended consequences, and the risk of regulatory arbitrage in devising arrangements that skirt the prohibition.

We consider the risk of financial intermediaries and institutions having "wriggle-room" to rationalise incentives is overstated, given the wider conduct requirements that will be introduced by the Bill and the substantial penalties for non-compliance.

How could a more principles-based approach to prohibiting some incentives be made workable?

Confidential information entrusted to the Government

21

If a more principles-based option was chosen, should there be some incentives specifically excluded?

22

AIA NZ suggests the principles-based approach should be limited to sales incentives based on volume or value-based targets only. In other words, incentives should only be prohibited where they are contrary to the principles-based rules and involve volume or value-based targets. This would ensure that volume or value-based incentives that support good customer outcomes (such as adviser group payments supporting FAP oversight and training) are not affected.

23

Do you think there are any other viable options other than what has been put forward by this discussion document? Please explain in detail.

Are there sales incentives based on volume or value targets that should be excluded from the regulations (i.e. allowed to be offered/given)?

AIA NZ believes that sales incentives based on volume or value targets should be permitted in the following instances:

24

- Where the primary purpose of the "incentive" is unrelated to sales promotion. This would include, for example, payments to assist intermediaries with the costs of compliance and oversight, and the provision of professional development and training, software, and business support to intermediaries. In practice, a minimum volume or value target is needed for these types of payments to manage a financial institution's overall cost of providing the incentive.
- Where the volume-based incentives or value target is used in conjunction with non-sales based measures as part of a balanced scorecard in determining remuneration.

Do you think there are any other types of incentives that should be excluded from the regulations? Please provide reasons for your comments.

25

AIA NZ considers that volume-based incentives or value targets used in conjunction with non-sales based measures as part of a balanced scorecard should be excluded from the regulations. In our opinion, these arrangements do not create the same potential for harm as incentives based solely on volume-based incentives or value targets. In addition, we believe that sales incentives based on volume or value targets which are unrelated to sales promotion – for example training, software, and business support – should be excluded.

Do you think that the scope of who can be covered by the regulations poses a risk of unintentionally capturing other intermediaries that are paid incentives but should not be covered?

26

AIA NZ does not believe the scope of who can be covered by the regulations poses a risk of unintentionally capturing other intermediaries that are paid incentives but should not be covered.

Do you agree/disagree that within financial institutions and intermediaries sales incentives regulations should apply to all staff? Why/why not?

27

AIA NZ believes that sales incentives regulations should apply to all staff. This is a simpler option and, as the discussion document notes, would mitigate the risk of "top down" pressure on sales staff that could undermine the purpose of the Bill.

However, AIA NZ adopts this position on the assumption that either a principles-based prohibition is adopted, or an exclusion is introduced for balanced scorecard arrangements. AIA NZ believes that these remain appropriate and do not create the same potential for harm as incentives based solely on volume-based incentives or value targets.

28	<p>Do you agree/disagree that within financial institutions and intermediaries sales incentives regulations should only apply to frontline staff and their managers? Why/why not?</p>
	<p>AIA NZ believes that sales incentives regulations should apply to all staff. Please see our response to question 27 above for further details.</p>
29	<p>Do you think that external incentives should apply to any incentive paid to an agent, contractor or intermediary? Why/why not?</p>
	<p>AIA NZ believes that sales incentives regulations should apply to any incentive paid to an agent, contractor or intermediary. However, this is subject to our comments in earlier questions about the correct scope of the prohibition itself.</p>
30	<p>Do you agree that both individual and collective incentives should be covered? Why/why not?</p>
	<p>AIA NZ believes that both individual and collective incentives should be covered. However, this is subject to our comments in earlier questions about the correct scope of the prohibition itself.</p>
31	<p>Do you have any other comments on the discussion related to incentives?</p>
	<p>AIA NZ does not have any other comments on the discussion related to incentives.</p>
Requirement to publish information about fair conduct programmes	
32	<p>Is more detail needed to outline what information should be published regarding financial institutions' fair conduct programmes to assist financial institutions to meet this requirement, or to assist consumers in their interactions with financial institutions?</p>
	<p>AIA NZ does not believe more detail is needed. We consider the current wording of the Bill provides sufficient detail to allow financial institutions to meet this requirement, and to assist consumers in their interactions with financial institutions.</p>
33	<p>Do you have any comments on the options outlined above? What do you think the costs and benefits would be to financial institutions and consumers of the two options?</p>
	<p>AIA NZ prefers option 1, being not to prescribe additional detail in regulations.</p>
	<p>We agree with the pros and cons identified in paragraphs 195 and 196 of the discussion document. We prefer option 1 largely because of the greater scope that it would provide for financial institutions to apply the requirements flexibly to their business, and for information to more easily evolve over time. While there is the potential for more uncertainty under this option, we agree that this could be addressed in other ways.</p>
34	<p>This discussion document outlines two options regarding the requirement to publish information about the fair conduct programmes. Do you have any other viable options?</p>

There are no other options AIA NZ wishes to propose.

Calling in contracts of insurance as financial products under Part 2

Do you have any comments on the proposal to declare contracts of insurance as financial products under Part 2?

- 35 AIA NZ agrees with this proposal. Declaring contracts of insurance to be financial products will resolve what has become a technical anomaly and, as the discussion document notes, will provide clarity that FMA is the appropriate regulator for false or misleading conduct in respect of insurance products.

Exclusions of certain occupations or activities from the definition of intermediary

Do you think it would be appropriate to exclude people who are subject to professional regulation from the definition of an intermediary (e.g. lawyers, accountants, engineers)?

- 36 AIA NZ agrees that it would be appropriate to exclude those subject to professional regulation from the definition of an intermediary.

Do you think that any other occupations or activities should be excluded from the new proposed definition of an “intermediary”? If so, why?

- 37 There are no other occupations or activities that AIA NZ considers should be excluded from the new proposed definition of an intermediary.

Other comments

AIA NZ does not have any other comments.