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# Submission on the Regulations to support the new regime for the conduct of financial institutions

From:

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To:

**Financial Markets Policy**

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Thank you for the opportunity to make a submission on this important issue. Please find CAP's responses to the questions posed in the Discussion Document provided below. If you require any further information or if you have any questions, I welcome your contacting me.

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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.

## Requirements for fair conduct programmes

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?

While CAP is supportive of the intention of the fair conduct principle, CAP believes that the fair conduct principle must be supported by regulations.

CAP assists people daily that are struggling in financial hardship. 3 out of 4 clients owe debt to a financial institution and nearly all clients rely on financial institutions to participate economically in society. The conduct of financial institutions has a very significant influence between clients that repay their debts and move on to a healthier financial future and those that enter insolvency and further hardship.

The reality is that there is a wide variance of conduct of financial institutions that CAP encounters while advocating and negotiating on behalf of clients. Some decisions are positive and helpful, while some are perplexing and frustrating.

CAP argues in favour of regulation for the following reasons:

1. Regulations will provide a framework for fair conduct programmes to specifically include a consideration of vulnerability and hardship, which is not specifically referred to within the minimum requirements of section 446M. The very root of the issue for many CAP clients facing hardship is that current the policies and processes of financial institutions have been built around the needs of “consumers when viewed as a group”. This approach often marginalises and minimises the legitimate needs of those that are not readily identified within a group. Regulations relating to fair conduct programmes would be complementary to changes to regulations relating to credit contracts which focus significantly on improvements for consumer outcomes in relation to hardship.
2. Regulations will provide a framework for consistent structure and consideration of customers in vulnerable circumstances within fair conduct programmes. The status quo expects financial institutions to be able to develop their own effective conduct programme, yet CAP’s experience is that there is a wide variance in outcomes for CAP clients facing vulnerability and hardship among different financial institutions. This can often be associated with the institution’s engagement with the difficult and complex needs of clients facing vulnerability. The FMA Culture and Conduct Review encouraged banks to “accommodate vulnerable customers in a meaningful way”<sup>1</sup> yet there is a long way to go to ensure this is taking place. Regulations will specify with greater clarity the structure and subject matter to ensure all financial institutions are meaningfully incorporating the needs of customers in vulnerable circumstances.

<sup>1</sup> <https://www.fma.govt.nz/assets/Reports/Bank-Conduct-and-Culture-Review.pdf> (page 17)

3. Regulations are necessary to help address the inherent imbalances that exist between large financial institutions and individual customers to “level the playing field” so that good customer outcomes are far more likely. The minimum requirements of s 446M do not appropriately acknowledge this as a factor for consideration yet this “information asymmetry” was referenced in the FMA Bank Conduct and Culture review where “banks typically hold a lot more information about their products, and customers are reliant on the bank providing information so that they understand the products.”<sup>2</sup> For example, there are a wide range of barriers to understanding and engaging with a financial institution through a complaints process. While well-intentioned, some processes for dispute resolution act as barriers that disincentivise participation by would-be complainants. These barriers are disproportionately more pronounced for people in vulnerable circumstances and was referenced in the Australian Royal Commission (ARC): “There will always be a clear need for disadvantaged consumers to be able to access financial and legal assistance in order to be able to deal with disputes with financial services entities with some form of equality of arms.”<sup>3</sup>

This information asymmetry exists not only across disputes resolution, but over product description, advice, communication, etc. Regulation would provide more detailed expectation for financial institutions to acknowledge and address the information asymmetry in fair conduct programmes.

4. Regulations can help establish appropriate expectations of how financial institutions respond to changes in a customer’s use of a relevant services over the lifetime of the customer’s use of a relevant service, particularly as this relates to identification of potential hardship. A lot of energy focuses on initial “point-of-sale” engagement to ensure products and services are appropriate yet, sadly, many of CAP’s clients have experienced a decline into financial hardship and have not received appropriate support to end using services that are no longer appropriate. Good customer outcomes means that products and services are suited to a customer’s needs on an ongoing basis<sup>4</sup> yet current hardship policies and processes of several financial institutions only apply upon the customer telling the financial institution of the circumstances, despite the financial institution holding data that indicates that hardship could very likely be a factor. Regulation will provide clarity to financial institutions about regulators’ expectations of proactive monitoring for cases of hardship.

2

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

CAP has no comments on this question.

3

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.

<sup>2</sup> <https://www.fma.govt.nz/assets/Reports/Bank-Conduct-and-Culture-Review.pdf> (page 33)

<sup>3</sup> <https://financialservices.royalcommission.gov.au/Pages/reports.html#final> (page 491)

<sup>4</sup> <https://www.fma.govt.nz/assets/Reports/Bank-Conduct-and-Culture-Review.pdf> (page 9)

CAP is supportive of the proposals relating to the distribution of relevant services and associated products. Defining this within regulations will ensure that the needs of customers are of primary consideration, which will lead to high-value services and associated products.

4

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

CAP has no comments on this question.

5

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)?

It is of vital importance that intermediaries can be trusted to equally deliver the financial institution's standard of conduct. One of the most glaring examples of poor conduct is in insurances sales that are rolled into vehicle finance credit contracts – often of very limited value and very expensive. There are often intermediaries involved in these transactions and this bill looks to address the current 'gap' of responsibility between financial institution and intermediary. CAP argues that regulations are necessary to support the development of the fair conduct programme, as detailed in the answer to Question 1. If this was the case, then CAP is supportive of MBIE's position that no regulations are needed to support 446M(1)(bb) to (bd).

6

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?

CAP favours converting these specific remediation principles into regulation for two reasons:

1. As found in the FMA’s Conduct and Culture review, there were four banks that had not identified any issues requiring remediation. In the FMA’s view, this “likely reflects weaknesses in the systems and processes for identifying and recording issues, lack of effort in identifying issues, or a lack of understanding about how misconduct may arise.”<sup>5</sup> It can be expected that, over the long-run, there will be a general under-investment and under-emphasis on self-identification for areas of remediation. Regulation will provide the impetus and framework for comprehensive and ongoing remediation reporting.
2. Financial institutions often rely on complaints to identify issues and multiple complaints about a particular issue should trigger more thorough investigations. Root-cause analysis could identify issue to fix but, in practice, financial institutions were not using this information effectively to inform remediation efforts. As the FMA stated, “We expect banks to proactively seek to identify issues in a systematic and methodical way, and prioritise remediation.”<sup>6</sup> Regulation may be necessary to outline the expectations that financial institutions utilise complaints to proactively assess issues for remediation, to outline expectations of timeframes for remediation discovery, etc.

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

- 7 The scope of s 446P seems quite wide, although it would be helpful to have an obligation to ensure that all forms of monetary remuneration are not skewing customer attention away from a fair opportunity for the customer to make an informed choice on all options of products available to them.

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

<sup>5</sup> <https://www.fma.govt.nz/assets/Reports/Bank-Conduct-and-Culture-Review.pdf> (page 27)

<sup>6</sup> <https://www.fma.govt.nz/assets/Reports/Bank-Conduct-and-Culture-Review.pdf> (page 28)

The issue of communication with consumers is a principal area of concern for CAP. The ability for a consumer to understand and appreciate differences between relevant services and the ability for consumers to explain their needs and requirements are fundamental to the relationship between consumer and financial institution.

Misunderstanding/miscommunication is one of the biggest causes of grievance and the concept of communication as a part of good conduct should require regulation to ensure that all factors of vulnerability are considered. CAP agrees with the reasoning provided by the FCA in relation to the specific incorporation of Communication in the “Consumer Duty” currently being developed:

*“Principle 7 already requires a firm to pay due regard to the information needs of clients, and communicate information in a way which is clear, fair and not misleading. However, when this Principle was developed, the assumption to a large extent was that if consumers are provided with information, they will engage with it and act appropriately. We now have a deeper understanding of behavioural economics, and of consumers’ levels of comprehension. As a result, we know that providing information is not enough on its own to ensure that consumers can make informed assessments and decisions. Indeed, an overload of information can sometimes hinder decision-making.”<sup>7</sup>*

CAP favours regulation to bring consistency and clarity in relation to how financial institutions should adapt communication with people in hardship and vulnerability.

9

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

CAP has no comments on this question.

10

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

CAP is supportive of any effort to regulate the process of receiving, reviewing, and responding to complaints. There are many barriers to making a complaint with a financial institution. However, better regulation would not only assist to standardise the process and the expectations of resolution but would importantly bring important protections to people in vulnerable circumstances. This would facilitate appropriate engage in the complaints process.

CAP would support efforts to define the term ‘complaint’ as different financial institutions seem to have varying ‘trigger-phrases’ that need to be communicated for a complaints process to be officially started.

11

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

<sup>7</sup> <https://www.fca.org.uk/publications/consultation-papers/cp21-13-new-consumer-duty#lf-chapter-id-the-four-outcomes>

Making a claim is often associated with a significant event that has taken place and claimants are often in a period of vulnerability or hardship. CAP would support regulations to specify the claims handling and settlement processes and bring consistency to processes and outcomes.

12 Do you have any comments on the proposed definition of 'handling and settling a claim under an insurance contract' means? If so, why?

No comment.

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

13 It is welcoming to hear that there are other significant initiatives in the pipeline from FMA on customer vulnerability. CAP agrees that the sections of 446M mentioned should be considered with a consumer vulnerability lens, however many financial institutions do not have the appropriate skills to self-develop adequate care for consumers experiencing vulnerability. CAP advocates for specific regulation to detail how this is achieved.

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

14 It is important to incorporate a specific reference to people in vulnerable circumstances but would suggest consistency is sought with the work of the Council of Financial Regulators who published their Consumer Vulnerability Framework<sup>8</sup> which rightly points away from defining vulnerable people as 'types' of customers.

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

No comment.

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.

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<sup>8</sup> <https://www.rbnz.govt.nz/-/media/ReserveBank/Files/regulation-and-supervision/banks/relationships/cofr/CoFR-Consumer-Vulnerability-Framework.pdf?revision=f53a37d9-0d75-4fb6-85ed-e2d424bbd1bb&la=en>

CAP advocates for consideration in line with the FCA as they develop their Consumer Duty. One particular area within their framework is in relation to “Price and Value”. This is not specifically mentioned within the Bill but CAP believes that this is worthy to be included in section 546(1)(oa) as a component integral to consumer financial wellbeing.

CAP highlights the following quote from the Consumer Duty summary:

*“When markets function well, with competition working effectively in consumers’ interests, consumers will be able to choose the product or service that represents the best value for them, bearing in mind its quality and other characteristics, as well as its price. Firms will be constrained by the value their competitors offer and will only win business if their product is good value for consumers. However, for a range of reasons, we know that markets do not always function well and that can result in consumers receiving poor value. For example, consumers can find value assessments difficult and firms can sometimes exploit this. We have seen a range of products across financial services markets that have not represented good value, and have had to intervene at different times to address this.*

*Consequently, we want to set out a clear and consistent expectation of how firms should assess whether the price of products and services offers fair value. Firms should be able to demonstrate that the benefits of their products and services are reasonable relative to their price. We want firms to actively put consumers at the heart of their business and assess the price of products and services at the design stage, and through ongoing monitoring.”<sup>9</sup>*

## Sales incentives

Do you have any comments on the status quo (no regulations)?

17 CAP is opposed to the status quo and recommends regulations to mitigate harmful sales incentive practices.

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

18 CAP is supportive of any efforts to remove conflicts of interest. The flexibility provided by the regulations to scoop in other methods of incentivising that could manifest. CAP is also supportive of regulated proactive monitoring by regulating bodies to review new methods of incentivising.

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

19 No comment.

<sup>9</sup> <https://www.fca.org.uk/publications/consultation-papers/cp21-13-new-consumer-duty#lf-chapter-id-the-four-outcomes>



	Do you have any feedback on a more principle-based approach to prohibiting some incentives?
20	CAP is supportive of a principle-based approach as a more general prohibition on any form of remuneration that can cause a conflict of interest. CAP's preference would be for a combination of a ban on value-based targets as well as a principle-based approach.
21	How could a more principles-based approach to prohibiting some incentives be made workable?
	No comment.
22	If a more principles-based option was chosen, should there be some incentives specifically excluded?
	No comment.
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.
	No comment.
24	Are there sales incentives based on volume or value targets that should be excluded from the regulations (i.e. allowed to be offered/given)?
	No comment.
25	Do you think there are any other types of incentives that should be excluded from the regulations? Please provide reasons for your comments.
	No comment.
26	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?
	No comment.
27	Do you agree/disagree that within financial institutions and intermediaries sales incentives regulations should apply to all staff? Why/why not?
	CAP advocates for Option 1, applying to all staff, as this removes conflict of interest from all stages of the supply chain and ensures managers and executives are not subject to sales pressures that could unduly influence staff on the front line.
28	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?

As above in 27.

29 Do you think that external incentives should apply to any incentive paid to an agent, contractor or intermediary? Why/why not?

Yes. All actors in the supply chain should be subject to the same intention to remove conflict of interest between personal gain and the consumer making a fair and transparent choice.

30 Do you agree that both individual and collective incentives should be covered? Why/why not?

Yes. CAP would agree with the statement in the Discussion Document that collective team targets could create a culture of peer pressure and of conflict of interest.

31 Do you have any other comments on the discussion related to incentives?

No comment.

#### Requirement to publish information about fair conduct programmes

32 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?

Yes, more information is required so that financial institutions can meet the requirements and to assist consumers. CAP advocates for the inclusion of a requirement to publish the fair conduct programme in each language that the financial institution advertises its relevant services, consistent with CCCFA changes.

33 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?

CAP advocates for option 2 to specify the standard of publishing the information to provide clarity and consistency to consumers who may use the information to make an informed decision.

34 This discussion document outlines two options regarding the requirement to publish information about the fair conduct programmes. Do you have any other viable options?

No comment.

#### Calling in contracts of insurance as financial products under Part 2

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

CAP supports the declaration of insurance contracts as financial products under Part 2.

Exclusions of certain occupations or activities from the definition of intermediary

36 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)?

No comment.

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

No comment.

Other comments

No comment.