FINANCIAL SERVICES FEDERATION

5 November 2021

Financial Markets Policy
Building, Resources, and Markets
Ministry of Business, Innovation & Employment

By email to: FMALevyReiew@mbie.govt.nz

Dear Sir/Madam,

Discussion document: 2021 Review of the Financial Markets Authority Funding and Levy

The Financial Services Federation ("FSF") thanks you for the opportunity to submit on the discussion document: 2021 Review of the Financial Markets Authority Funding and Levy.

By way of background, the FSF is the industry body representing the responsible and ethical finance, leasing, and credit-related insurance providers of New Zealand. We have over eighty members and affiliates providing these products to more than 1.7 million New Zealand consumers and businesses. Our affiliate members include internationally recognised legal and consulting partners. A list of our members is attached as Appendix A.

As you will see from Appendix A, the financial institutions to which these three regimes will apply to are predominantly our Non-Bank Deposit Takers (NBDT) members, Credit Union and Building Society members, and our Credit-Related Insurance Provider members. This submission will largely represent the views of these members rather than the remainder of the membership that are Non-Deposit-Taking Lending Institutions (NDLIs) or the Affiliate membership. With that being said, the remainder of the FSF is keenly observing regulation and developments in these three spaces, as they are indicative of what may they may expect with respect to regulation applying to them in the future and also because they would always aim to emulate the responsible behaviour expected by the regulator even if they are not in the scope of the regime.

The FSF will firstly outline more general comments in relation to the discussion document, before proceeding to answer relevant questions as structured in the discussion document.

General comments on the CoFI regime

The FSF remains of the robus belief that there is no need for an entirely new licensing regime for the conduct of financial institutions under the Financial Markets (Conduct of Institutions) Amendment Bill ("CoFI"). The FSF has consistently strongly opposed the

introduction of CoFI, and subsequently, any funding and levies raised in support of its implementation. You will be aware of this stance on the CoFI regime from the FSF's previous submissions on consultation with both the Financial Markets Authority ("FMA") and the Ministry of Business, Innovation and Employment ("MBIE"); a summary of our previously made points are as follows:

The CoFI Bill is unnecessary and will impose further costs on the financial institutions within its scope all of whom already have a requirement to hold several other licences, registrations, or certifications with regulators such as with the Reserve Bank of New Zealand ("RBNZ") and the FMA in order to be able to conduct their business. It seems more logical to the FSF to include the conduct of these institutions within an already existent licensing regime. This would be less onerous and more cost-effective for both regulators and regulated entities.

There is a large number of other legislative reforms or initiatives affecting the financial services sector outside CoFI that have either only recently been implemented or are currently in the process of implementation. This places a tremendous regulatory burden on business and, alongside the navigation through this challenging COVID-19 period, entities are under immense pressure to remain afloat.

These other substantial pieces of legislation include:

- The Financial Services Legislation Amendment Act, which brought into scope all financial advisers rather than distinguishing between authorised and registered advisers, consequently bringing in another licensing regime.
- The suite of changes coming in under the Credit Contracts Legislation Amendment Act 2019 and associated instruments.
- The Reserve Bank Act review.
- The Deposit Takers Act.
- The Insurance Prudential Supervision Act review.
- The RBNZ's Enforcement Principles and Criteria review.
- And many others in the pipeline, all aimed at enhancing consumer protections.

The FSF believes that the process of legislation reviews currently in play should be allowed to be completed before introducing yet another regime. Applying yet another licensing regime to those financial institutions that are already in the scope of these regimes, is in the FSF's view a clear example of regulatory overlap taken to such an extreme as to render it nonsensical.

Previous discussion documents have referenced the FMA and RBNZ's joint review on the conduct and culture of banks and life insurers in New Zealand that were carried out in 2018 and 2019. Whilst these reviews identified some issues with the conduct of banks and life insurers, the proposed conduct regime will apply to all insurers (including small credit-related insurance providers) and to NBDTS where there has been no evidence found of the existence of any conduct-related issues.

On this basis, the FSF submits that there is no proportionality or justness in imposing fees and levies upon such smaller entities, in addition to the costs of the novel CoFI licensing

regime, when considering the negligible consumer risks and harm posed by such credit-related insurers and NBDTs.

FSF members, when compared to larger institutions such as banks, life and fire and general insurers, hold a minuscule portion of the market. Because of the size of FSF members, they are much closer to their customers and are important parts of their local communities with loyal customer bases. FSF members also provide transactional facilities, which larger institutions are removing, aiding with financial inclusion of marginalised and exploitable groups.

As a result of the nature of FSF members and their operations, their ongoing successful assistance to smaller groups and communities across Aotearoa translates into records of equitable and customer focussed behaviours. The lack of evidence disputing this is sufficient evidence that a further conduct licensing regime is unnecessary, and it's associated cost, alongside the proposed levies, is likely to detrimentally affect the operations and sustainability of such entities and consequently affect the financial inclusion of overseen communities across the motu.

The FSF understands that no number of submissions opposing the CoFI regime will slow or halt the regime's implementation completely. However, in light of the comments made above, the FSF urgently request equity, proportionality, and variability be considered amongst the smaller entities within the scope of CoFI, when concluding on this review.

The FSF will now go on to answer the specific questions of the review.

Question 1: Do you have any feedback on the objectives of the review?
The objectives of the review are agreed upon in principle. However, the FSF's disagreement on the need for the introduction of the CoFI regime influences our perception of the objective for FMA's additional funding for this regime, as we think that funding, and any further progress, towards this regime is unnecessary entirely.

In regard to the Climate-Related Disclosure ("CRD") regime, the FSF supports this in principle, particularly as amendments made to the Bill met our requests for variability and proportionality for smaller entities, reducing disproportionate costs on such entities. The regime is a significantly positive step towards further financial and business sustainability, and the objectives associated with this regime are agreed upon.

For Insurance Contract Law ("ICL"), the FSF is hesitant to agree with much of the objectives or proposals associated with ICL due to the lack of clarity or information given on what the regime will actually entail. Further details will need to be released before submitters, and regulators, should be making decisions on funding and levy options regarding this regime. Generally, when removing the particulars, the objectives of the review seems sufficient.

Question 2: Do you have any feedback on the criteria for assessing the funding options?
No feedback for this question.

Question 3: Do you agree with the analysis of the FMA funding options for CoFI? Which option do you consider to be most appropriate and why?
The FSF queries the FMA's capability to adopt a proactive approach so suddenly as a result of increased funding. The FSF is concerned that a reactive approach from the Council of Financial Regulators ("CoFR") has not yet been adequately established. Confidence in the CoFR's ability to adopt a proactive approach so swiftly is not yet concrete, and thus, particularly as the variance between the cost options is so great, the FSF thinks it would be wiser to begin with the lower option to ensure the approach is increased systemically and not set up for failure so suddenly.

The FMA should also consider the extreme labour shortage, prior to allocating funds towards FTEs. The possibility of acquiring high-caliber individuals to fulfill their Option 1 criteria will be met with difficulty.

The FSF respectfully disagrees with the analysis that with Option 2, entities may be left with a higher total cost of compliance, compared to those entities who would have had access to compliance guidance and engagement in Option 1. Engagement is required no matter the amount of funding provided to the regulatory body. And, aligned with our more general comments, the FSF points to the lack of evidence from smaller entities which suggest their conduct is not already compliant with the CoFI regime. The larger institutions, who were found to have these failures, have far larger access to resources which will allow them to be less reliant on communication from the FMA.

The FSF also respectfully disagrees with the analysis that a reactive approach, under Option 2, renders the cost of rectifying inadequate. The FSF queries whether the regimes currently enforced by the FMA are also inadequately rectified. There has already been an increase of $24.805 million to the FMA's baseline funding, and engagement, enforcement, or 'rectification' has not increased proportionality to this increase in funding. For a regime that is so novel and unnecessary, the FSF is concerned that this exorbitant increase in funding is likely to not contribute much good or rectify the gaps which the CoFR has so identified. Reactive engagement with entities must be increased before there can be justification for a proactive approach.

Lastly**,** the FSF is concerned that there is not sufficient clarity surrounding what the CoFI regime will entail, to justify the increase in funding and large increase in FTE in both options. The FSF suggests it would be wiser and more prudent to establish the regime and assess its required resources before allocating labour and funds on guesses and judgements. Basing these costs on possibility rather than fact destroys the predictability and certainty of budgets. As these costs are also not insignificant, they are substantial increases from current levies so consideration should be given to this and more care taken in determining budgets once all facts are known. Smaller entities particularly cannot afford to be allocating money to hypothetical plans.

Question 4: How would CoFI Option 1 impact you/your business compared to CoFI Option 2?
The proposed levy under Option 1 for CoFI will disproportionately affect smaller entities, such as FSF members. This would cause great detriment to their sustainability and

continuation of high-quality customer focussed outcomes. As a result, this disproportionality affecting smaller community-based entities is detrimental to consumers and to financial inclusion.

It would be naïve to suggest that levies imposed on entities would be met by the entities themselves. This is not correct. Consumers will resultantly have to meet higher fees therefore affecting financial inclusion, particularly for those consumers who rely on community-based financial institutions and who are typically less financially literate and more marginalised by larger institutions.

Question 5: If you were to make material changes to the CoFI options, how would you do so and on what basis?

Ideally, the FSF would appreciate no funding of CoFI to be an option, particularly from small entities like the FSF's credit-related insurance providers and NBDTs. However, we are acutely aware that our concerns throughout the CoFI consultation period, have not been listened to as we hoped.

As a result, the FSF requests that entities of the smallest class be exempted from the proposed levies under both CoFI options.

Under proposed Option 1, where setting standards and guidance are highlighted, the FSF thinks it is unnecessary to jump to proactivity prior to the FMA achieving reactivity. The FSF sees no issue with those who already comply with good conduct standards, and their current regimes, to have any difficulty in complying and therefore not requiring the proposed guidance and engagement from the FMA. Reacting to those who already do not comply with their current conduct obligations, is a preferred approach rather than punishing compliant entities with a harsher levy for their present compliance.

The thematic monitoring approach proposal is effective at determining where the gaps are if there are any. However, if thematic monitoring is likely to become a regular occurrence under the funding options, then the FSF suggests that this goes both ways.

FMA's efficiency at enforcement and reaction should be assessed regularly to ensure that their objectives are being fulfilled with respect to these regimes. Previous efficacy reviews should not be sufficient to determine the regulatory body's effectiveness and it would assure smaller entities that those entities who have catalysed regulation in the form of these regimes, are being monitored sufficiently and the burdens imposed on these smaller entities are not in vain. This would also prevent the rush of further unnecessary regulation down the line.

Question 6: Do you have any feedback on the objectives for the implementation of the CoFI regime?

The FSF's overarching dissatisfaction with the CoFI regime informs our view of the objectives, and therefore, we do not see the need for such objectives. The burden of CoFI and its unnecessariness causes the objectives to be rejected.

Question 7: Do you agree that the CoFI licensing window should begin after financial advice provider transitional licensing window has closed?
In light of our arguments stating that the regulatory burden is too onerous for entities, any and all delays to the transitional licensing window will be better received and more equitable. Entities will require more time for compliance than regulatory bodies, as policies and procedures, including technical system changes, and their resource intensity should not be understated.

Question 8: Are there other areas of regulatory reform in the financial services sector, where implementation overlaps with the proposed timeframes above, and that you consider it would be preferable to align CoFI implementation with those timeframes from an efficiency perspective? If so, please provide examples.
No feedback for this question.

Question 9: Do you have any feedback on the proposed 18-month window between applications for a conduct licence opening and all the obligations of the CoFI Bill coming into force (including having a conduct licence)?
Consideration must be taken to the upcoming Deposit Takers Act, due to be implemented in 2023, and ensuring there is no conflict here, as it will then become more difficult and onerous for entities to comply with the Deposit Takers Act alongside the CoFI regime. This compliance heavy toll is again likely to more adversely affect smaller entities.

Question 10: Do you think a phased approach to CoFI licensing would be preferable, compared to a single licensing window for all types of financial institutions? Please provide reasons.
A phased approach could reflect proportionally and the variability between the entities and their resource availability.

Smaller entities are more likely to require further time to comply with such licensing requirements, resources are more intensive, resources cannot often be diverted from customer focusses for compliance, whereas with larger entities compliance teams can take on a project at any moment and this is far more achievable in a smaller timeframe. The FSF suggests that larger institutions and their conduct, which were found to be wanting should be the priority.

Question 11: If a phased approach to CoFI licensing would be preferable, what factors do you think should be considered in determining the order of phasing?
Members of the FSF are considerably more resource-restricted than larger institutions and pose less conduct risk to consumers.

For these reasons, CoFI licensing should not be such a priority for such entities, but rather should focus on the larger institutions with far greater conduct risk (particularly as has been identified in RBNZ and FMA reviews themselves). Larger institutions should then be prioritised accordingly with the regime’s objectives.

Question 12: Do you have any other general comments regarding the implementation timing of the CoFI regime?
With the Deposit Takers Act, and the non-bank deposit takers regulations, coming in in 2023, consideration should be given as to whether the timing of implementation would cause an insupportable regulatory burden on those smaller entities, such as FSF members, and render their participation in such licensing regimes too onerous and unsustainable.

Question 13: Do you agree with the analysis of the FMA funding options for ICL? Which option do you consider to be most appropriate and why?
Due to the lack of an exposure draft of the proposed ICL Bill, and any clarification on the high-level requirements such a bill will impose on insurers, the analysis for the funding options for ICL should not be concluded purely on guesswork. These should be addressed once ICL details are confirmed and provided to the industry for appropriate consultation. The FSF refers to our answer to Question 3, in regard to funding being estimated, as relevant to this question as well. Proposing further requirement of new FTEs, capabilities and resources for the operation of the regime, without any actual legislation to understand what the regime requires, seems illogical and strange.

The novelty of such a regime arrives with associated with costs for compliance. These compliance costs need to be considered. The levies will not be the only costs to be met by the affected entities. For this reason and considering the lack of clarity on the regime itself, it would be best to suggest a final review once the legislation is finalised.

The FSF also presents a more general query as to why this enforcement is being redistributed to the FMA when it is typically the RBNZ that licenses and supervises insurance providers.

Question 14: How would ICL Option 1 impact you/your business compared to ICL Option 2?
As FSF's members who are within the scope of this regime are small entities, they will be disproportionately impacted by Option 1. Option 2 provides for a smaller levy to be imposed, causing less disproportionate consequences.

Question 15: If you were to make material changes to the ICL options, how would you do so and on what basis?
Material changes are not suggested without the details of the ICL regime being released.

Question 16: Do you agree with the analysis of the FMA funding options for CRD? Which option do you consider to be most appropriate and why?
The FSF agrees with the principle of the CRD regime, and the analysis of the need for further skilled staff to implement this is agreed upon, particularly as domestically we are short-staffed for people within this field of knowledge, and generally short on labour. As compliance with reporting requirements will also require external services, the cost of such skills should not be underestimated once the regime nears closer.

The novelty of this regime and the importance of climate sustainability within the financial services sector is important to consider, and the FSF agrees with the analysis.

However, the FSF remains concerned regarding the efficacy the FMA will be able to produce on this topic, particularly as proactive approaches have not been evident to the FSF in other regimes.

Question 17: How would CRD Option 1 impact you/your business compared to CRD Option 2?
As proportionality and variability were provided for, through the consultation process, the FSF is more neutral as to whether Option 1 or Option 2 is implemented. Smaller entities have been excluded from the reporting requirements, and this reflects many of the FSF's requests articulated in submissions.

However, as the assurance requirement remains in the CRD regime, ensuring the costs associated with the implementation and enforcement of this regime are considered will be important in the funding assessment. Compliance with this regime will also require many external services and consultancy, and this should also be considered as in the funding assessment.

Question 18: If you were to make material changes to the CRD options, how would you do so and on what basis?
No material changes suggested.

Question 19: Do you think that the proposed additional FMA funding should be wholly levy recovered or should the Crown contribute towards the increase? Why?
Because of the nature of the FSF's smaller entities, Crown contribution is likely to decrease pressures.

Question 20: Do you think that the Crown should contribute relatively more to any of the regimes that others? If so, please explain why.
No feedback suggested.

Question 21: What is the appropriate Crown/levy split of the FMA's appropriation and why?
No feedback suggested.

Question 22: Do you have any feedback on the objectives underlying the levy model?
The objectives of the levy model are well thought out, however, the FSF has serious concerns regarding whether the objectives will be met.

Insight has shown that the levy, along with the CoFI regime and the potential ICL regime, is likely to unduly burden smaller market participants, as highlighted in our general comments earlier in this submission. This in turn is likely to affect the continued supply of financial products or services. It's naïve to suggest that with continued levies and regulation that smaller entities will remain in their sustainable present positions with the same affordability.

Question 23: Do you agree that larger entities should pay a relatively larger portion of any levy increase? If not, please explain why.
As alluded to in our general comments, larger entities should pay a relatively larger portion of all levy increases.

Our arguments for this are themed throughout our submission but predominately centered around the onerous burden placed upon smaller entities, who have resource constraints, and their ability to continue sustainable operations in such a compliance heavy industry. Evidence has not suggested that these smaller entities are also responsible for the gaps in conduct and non-customer focussed outcomes which the FMA and RBNZ reviews have identified. Therefore, disproportionate impacts on smaller entities should be removed from these proposals.

Question 24: Do you think the proposed levy changes meet the objectives?
Refer to answer in Question 22.

Question 25: Do you have any comments on the proposed new levy classes/tiers? Should further classes be considered?
Smaller entities should not have any levy increase, as the cost of compliance for the new regimes is burdensome enough.

Question 26: Do you have any feedback on the impacts of the proposed changes to the levies presented in Annex 1? How would the proposed changes impact your business? Please provide examples.
Refer to answer to Question 25.

Question 27: Do you think any of the levy classes in Annex 2 should pay an increased levy as a result of these new regimes? If so, why?
No comment.

Please do not hesitate to contact me for any further details.

Yours sincerely,

Diana Yeritsyan
LEGAL AND POLICY MANAGER
FINANCIAL SERVICES FEDERATION

Appendix A

FINANCIAL SERVICES FEDERATION

FSF Membership List as at November 2021

Non-Bank Deposit Takers, Insurance Premium Funders,	Vehicle Lenders	Finance Companies/ Diversified Lenders	Finance Companies/ Diversified Lenders, Leasing Providers	Credit Reporting, Debt Collection Agencies, Insurance Providers	Affiliate Members
XCEDA (B) Finance Direct Limited ➢ Lending Crowd Gold Band Finance ➢ Loan Co Mutual Credit Finance Credit Unions/Building Societies First Credit Union Nelson Building Society Police and Families Credit Union Westforce Credit Union Insurance Premium Funders Elantis Premium Funding NZ Ltd Financial Synergy Limited Hunter Premium Funding IQumulate Premium Funding Rothbury Instalment Services	AA Finance Limited Auto Finance Direct Limited BMW Financial Services ➢ Mini ➢ Alphera Financial Services Community Financial Services European Financial Services Go Car Finance Ltd Honda Financial Services Kubota New Zealand Ltd Mercedes-Benz Financial Motor Trade Finance Nissan Financial Services NZ Ltd ➢ Mitsubishi Motors Financial Services ➢ Skyline Car Finance Onyx Finance Limited Toyota Finance NZ Yamaha Motor Finance	Avanti Finance ➢ Branded Financial Basalt Group Basecorp Finance Ltd Blackbird Finance Caterpillar Financial Services NZ Ltd Centracorp Finance 2000 Finance Now ➢ The Warehouse Financial Services ➢ Southsure Assurance Humm Group Future Finance Geneva Finance Harmoney Instant Finance ➢ Fair City ➢ My Finance John Deere Financial Latitude Financial Lifestyle Loans NZ Ltd Metro Finance NZ Finance Ltd	Pepper NZ Limited Personal Loan Corporation Pioneer Finance Prospa NZ Ltd Smith's City Finance Ltd Speirs Finance Group ➢ Speirs Finance ➢ Speirs Corporate & Leasing ➢ Yoogo Fleet Thorn Group Financial Services Ltd Turners Automotive Group ➢ Autosure ➢ East Coast Credit ➢ Oxford Finance UDC Finance Limited Leasing Providers Custom Fleet Fleet Partners NZ Ltd ORIX New Zealand SG Fleet	Baycorp (NZ) ➢ Credit Corp Centrix Collection House Debtworks (NZ) Limited Equifax (prev Veda) Illion (prev Dun & Bradstreet (NZ) Limited Intercoll Quadrant Group (NZ) Limited Credit-related Insurance Providers Protecta Insurance Provident Insurance Corporation Ltd	Buddle Findlay Chapman Tripp Credisense Ltd Credit Sense Pty ltd Experian EY FinTech NZ Finzsoft Green Mount Advisory Happy Prime Consultancy Limited HPD Software Ltd KPMG LexisNexis PWC Simpson Western Verifier Australia Total 83 members