Financial Services Council.
Growing and protecting the wealth of New Zealanders

Financial Services Council
of New Zealand
Level 17, Commercial Bay Tower,
11-19 Customs Street West, Auckland 1010
P: +64 9 802 1532
E: fsc@fsc.org.nz
www.fsc.org.nz

Friday 5 November 2021

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

By email: FMALevyReview@mbie.govt.nz

2021 Review of the Financial Markets Authority Funding and Levy

This submission on the 2021 Review of the Financial Markets Authority (FMA) Funding and Levy, 5 October 2021 (the 2021 Review), is from the Financial Services Council of New Zealand Incorporated (FSC).

As the voice of the sector, the FSC is a non-profit member organisation with a vision to grow the financial confidence and wellbeing of New Zealanders. FSC members commit to delivering strong consumer outcomes from a professional and sustainable financial services sector. Our 98 members manage funds of more than $95bn and pay out claims of $2.8bn per year (life and health insurance). Members include the major insurers in life, health, disability and income insurance, fund managers, KiwiSaver and workplace savings schemes (including restricted schemes), professional service providers, and technology providers to the financial services sector.

Our submission has been developed through consultation with FSC members and represents the views of our members and our industry. We acknowledge the time and input of our members in contributing to this submission.

The FSC's guiding vision is to grow the financial confidence and wellbeing of New Zealanders and we strongly support initiatives that align with our strategic intent and deliver:

- strong and sustainable customer outcomes
- sustainability of the financial services sector
- increasing professionalism and trust of the industry.

As submitted in response to the Review of the FMA Funding and Levy, 28 January 2020 (the 2020 Review), we remain strongly of the view that there needs to be an increase in the proportion of Crown contribution to FMA funding. Also as previously submitted, and in a follow up letter in June 2020, the FSC expressed concern on the timeline for consultation. Once again, the 2021 Review contains substantial detail, with a consultation timeframe that is too short to enable fully informed decisions and feedback from across the industry. This is further exacerbated by the volume of consultations at this time and the difficulties that our industry is facing in light of Covid-19 and the Delta outbreak (COVID).

The timing of the 2021 Review is also not conducive to enabling considered responses when the impacts of the CoFI, ICL and CRD regimes are still unknown. CoFI is yet to pass its second reading, no exposure draft of the ICL Bill has been released and the first consultation on the External Reporting

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Board (XRB) climate standards has only just commenced making it too early to ascertain additional funding requirements that may be required.

The workshops that were held with the FMA and MBIE were considered very helpful and informative, and we would like to express appreciation for the opportunity to attend and engage. We hope that the concerns expressed in those meetings have been noted as due to their timing there is limited time to incorporate new understandings and updated views in this submission.

We welcome continued discussions and engagement.

I can be contacted on Privacy of natural persons or Carissa Perano, Head of Regulatory Affairs, Privacy of natural persons, to discuss any element of our submission.

Yours sincerely

Richard Klipin
Chief Executive Officer
Financial Services Council of New Zealand Incorporated

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of New Zealand
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E: fsc@fsc.org.nz
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Purpose of the review and context

1. Do you have any feedback on the objectives of the review?

We wish to reiterate the points made on the objectives of the 2020 Review in response to this 2021 Review, noting also the significant impact of COVID on the industry since the 2020 Review.

FSC Submission 2020:

The FSC supports increased funding to meet the objectives of the Review. The financial services sector has undergone significant change since the last fees and levies review in 2016. This has in turn required significantly increased resources to respond to regulatory change, the financial advice regime, legislative and policy reform and has been felt across the industry. Those sectors impacted by the culture and conduct reviews have also had to manage and implement change, and the wider industry has been strongly encouraged to do the same. In addition, the financial burden to meet Government and Regulator expectations has been significant. With this growth, the FSC supports more funding however the key funding principles to be fair, equitable, proportionate, appropriate and strategic can only be met if more consideration is given to the appropriation between industry and the Crown.

We strongly support an increase in the proportion of Crown contribution to FMA funding. Without this, we query whether the desired outcomes will eventuate in practice if increases are solely borne by industry. For example, industry stability and consumer trust and confidence may not be achieved if levies and resources to respond to regulatory activity are transferred to consumers. There are also concerns that increased levies may provide the ability for the FMA to expand beyond its remit and risk reduced transparency, particularly given recent history of rapid change, with much more still to come.

2021 Review Objectives:

We consider that the first objective of the review, "review the FMA's additional funding requirements to ensure it can meet its new statutory functions under the CoFI, ICL, and CRD regimes, and can operate as a credible and effective financial markets regulator", should be modified to acknowledge that the impacts of the CoFI, ICL and CRD regimes are still unknown. CoFI is yet to pass its second reading, no exposure draft of the ICL Bill has been released (and the FMA's statutory functions are therefore unknown to the sector) and the first consultation on XRB climate standards has only just commenced, so we submit that it may be too early to ascertain additional funding requirements that may be required. Accordingly, the first objective should be qualified to limit it to reviewing the FMA's additional funding requirements for the implementation of these regimes (or to review the funding required to meet statutory functions to the extent currently possible).

The funding options

2. Do you have any feedback on the criteria for assessing the funding options?

There is a perception that value to the public may only be achieved when the costs are not passed onto customers. It is inevitable that increasing levies on insurers and fund managers without balancing the Crown contribution could see premiums and fees rise for customers.

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Smaller Financial Institutions and entities may be impacted by increased levies to a greater extent, given they are continuing to be hit hard by COVID, as well as wider economic uncertainties. This should be accounted for in some way to avoid the unintended consequence of reducing market participation.

Funding options – Conduct of Financial Institutions

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?

We agree that Option 1 would enable the FMA to take a proactive and collaborative regulatory approach by setting standards and issuing guidance, rather than focussing on enforcement after the fact. However, as highlighted in the 2021 Review, the key risk for achieving either Option (but more so for Option 1) is staff recruitment and retention. As the 2021 Review notes, the FMA has in recent years faced a highly competitive and tight labour market, managing both recruitment and retention pressures. This reflects that the skill sets required by the FMA have been in demand within the financial services industry. Therefore, we submit that it would be incredibly difficult for the FMA to successfully recruit 102 staff members over four years in this area. Seeking to achieve such a level of recruitment could result in recruitment of staff who do not have the requisite experience or expertise which could undermine the FMA achieving its objectives. This impacts the Achievability and Good Public Value criteria in respect of Option 1 (and to a lesser extent, Option 2). We question the feasibility of Option 1 in the proposed timeframe and agree with the FMA's concerns at paragraph 90.

There remains considerable uncertainty on the CoFI regime, particularly in circumstances where the CoFI Bill (as at the date of this submission) has not yet passed its second reading, MBIE have yet to formally respond to industry submissions from May 2021, no exposure draft of the Supplementary Order Paper has been released, the regulations have not yet been drafted, the requirements for the licensing process have not been confirmed and there is a risk that with hindsight these requirements could be seen to have been incorrectly targeted. Therefore, we consider that it is challenging to consider and comment on best options, in terms of regulatory approach and requisite funding and staffing at this time. It is also difficult to ascertain resource requirements for a four year implementation period (resulting in high impact changes) prior to commencement. The uncertainty of this impact suggests a moderate approach in year one may be prudent.

We note that Option 1 is said to equip the FMA with a full range of regulatory responses, including enforcement and litigation, to deter misconduct. However, under the proposed licensing window, the obligations of the CoFI Bill will not come into force until December 2024, meaning no enforcement would be possible until early 2025. It is not clear whether the proposed levies have been calculated on this basis, or whether additional enforcement funding has been included for each year from 2022. To address this, we set out proposed changes below in response to Question 5.

The parameters of the CoFI regime should be known before any funding requirements are set. CoFI applies to banks and insurers who have all been through the culture and conduct reviews and for whom the Financial Services Legislation Amendment Act 2019 (FSLAA) is likely to apply (along with other aspects of the Financial Markets Conduct Act 2013, which also focuses on conduct). Given the work that has been done by the industry since October 2019 and the voluntary engagement industry

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is already having with the FMA, we do not believe the problems they are attempting to remedy justify the proposed increased costs at this stage.

The CoFI regime (and the other significant industry changes) needs the time to embed before increasing costs so substantially and the FMA have often stated that industry should understand their expectations as these have been made clear and widely available for some time. They have also indicated they are already in the process of revising their guide to good conduct which should be issued for consultation in early 2022. This will provide updated guidance on FMA's expectations.

There will be the initial set up and embedding stages for COFI (and ICL and CDR), for example, Identify and Set Standards pillars. As such, we would expect there would be a large amount of work up front and then reducing at which point those staff could move on to other regulatory regimes (this is how we would expect commercial organisations to operate). Similarly, if the FMA is effective then we would expect that work in the Assess and Respond areas would also decrease over time (for example, noting comments in paragraph 93 regarding relatively less resourcing for enforcement in long term).

We note that at paragraph 4 of the 2021 Review where Option 1 is outlined, the term 'deep engagement' is used and 'guidance that sets clear expectations and identification of risks at an earlier stage'. We consider that such a term and a reference to further guidance requires more clarification as to what is intended and to justify the benefits assumed from that level of increase in funding.

4. How would CoFI Option 1 impact you/your business compared to CoFI Option 2?

It is challenging to respond to this question as differences in monitoring activity and licensing are not known at this time. However, some of our members have provided feedback on how Option 1 would impact their businesses compared to Option 2.

Positively, Option 1 would provide greater clarity and certainty to businesses in respect of regulator expectations compared to Option 2 (under which the FMA proposes to undertake a more enforcement led approach, rather than setting standards and engaging with industry to improve practice). If Option 2 was adopted, businesses may instead seek additional guidance, engagement, and support from their FMA Relationship Managers. This relationship may be able to be leveraged to cover some of the processes that are not in scope for Option 2, such as providing specificity in the context of a more generic licensing process and enabling more desk based and entity based monitoring and entity based engagement.

However, Option 1 will impact businesses in other ways, including through increased regulatory engagement, as noted at paragraph 84, in the form of proactive onsite monitoring (particularly large insurer members) and thematic reviews. This would be impactful in terms of generating increased workload and potentially requiring the hiring of additional FTE to support regulatory engagement activities. As discussed at Question 3 above, the recruitment of additional staff may be challenging in the current environment and the industry and the FMA would essentially be competing to recruit the same pool of people to fill positions.

In the present regulatory environment of near continuous high impact change (particularly the frequency and complexity of regulatory reforms in the insurance sector in the next three years) it is

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important that the FMA carefully considers the significant time and resource required to prepare for and respond to monitoring and reviews.

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

Based on our feedback on Question 3 above, we suggest that CoFI initially be funded on a two year basis, which provides sufficient funding for the FMA to develop the licensing process, application questions and guidance, and licensing standard conditions whilst the relevant legislation and regulations are finalised. The FMA will then have a clearer idea of the level of funding required to assess applications through the majority of the licensing window, plus the move into a monitoring and enforcement environment. At the two year point, the FMA and market participants will be in a better position to understand the FMA's funding needs going forward, as the regime is implemented and then embedded. This would enable the FMA to better meet the criteria of Good Public Value and Achievability, while maintain Strategic Alignment.

We encourage consideration of a potential Option 1.5, a halfway point between Options 1 and 2. An Option 1.5 could have a lower proposed number of FTE required to support a more targeted scope of work initially to implement the regime. This would more realistically reflect the FMA's ability to scale its resources, focus that growth on establishing the licensing process, the development of standards and guidance for market participants and consumers, and increased engagement in the lead up to licensing and prior to the commencement of the regime. We consider that an emphasis on establishing a strong regime from the outset, will strengthen compliance across the industry and lead to overall better outcomes for the FMA, market participants and consumers.

We consider that standards setting, and regulatory guidance will be fundamental to the success of the CoFI regime. Under Option 2, if the FMA is unable to provide sufficient support through guidance and regulatory expectations, significant divergence across the industry is possible, particularly for conduct which is very broad and highly subjective.

We reference the FMA's comments about the options for the implementation of the CRD regime at paragraph 177, "given the time frames for implementation and the degree of uncertainty about the regime, it is likely that the FMA would need to review it approach in the medium term. There is a risk that future changes to the FMA's approach would be more difficult under CRD Option 1, in the event the FMA is unable to meet industry expectations in terms of proactive engagement". We consider these same factors are present in the implementation of the CoFI regime, and accordingly the FMA should give due consideration to either a two year approach to funding, or a potential Option 1.5 as a more measured approach given the complexity of the situation.

Implementation – Conduct of Financial Institutions regime

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

We agree with the objectives and would emphasise the importance of Financial Institutions being provided with an appropriate amount of time to prepare for the new regulatory regime, so that public trust and confidence in the industry does not suffer. It would be helpful if the objectives for implementation could include reference to the FMA's intention to provide guidance and support to

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E: fsc@fsc.org.nz
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participants during the transition period. We submit that the second objective, "Minimise, to the extent possible, unnecessary compliance costs and burden associated with preparation and transition to the new regime", should be expanded to specifically refer to this.

Whilst the 2021 Review makes reference to Financial Advice Provider (FAP) licenses, we consider that the desire to avoid potential overlap and duplication should form an additional objective to the implementation of the CoFI regime, namely "avoidance of unnecessary duplication or conflict with other regulatory requirements".

7. Do you agree that the CoFI licensing window should begin after financial advice provider transitional licensing window has closed?

We agree that the CoFI licensing window should begin after the FAP transitional licensing window has closed.

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.

We agree that the proposal to start the CoFI licencing after the FAP transitional licencing window has closed make sense.

In terms of other regulatory developments that should be accounted for, we encourage the FMA to work with the Reserve Bank of New Zealand (RB) to consider whether there is any overlap between CoFI implementation and the current Insurance (Prudential Supervision) Act 2010 (IPSA) Review, given both will likely involve changes to the payment of incentives. Other developments that should be taken into consideration include the expected introduction of the Deposit Takers Bill and a Consumer Data Rights Bill.

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)?

The proposed 18 month window between applications for a conduct licensing opening and all of the obligations of CoFI coming into force will be unachievable, especially as the window for applicants will in practical terms only be just over a year (given the time period that the FMA will then be required to assess conduct licence applications). In addition, in the absence of information on the licensing requirements for the CoFI regime, the timeframe seems challenging for both the FMA and Financial Institutions to meet. Consideration needs to be given to not only the issuance of licences but also preparing for the regime, embedding the requirements and ensuring the licence is maintained. We note that this will come at the same time or in quick succession to other significant regulatory change. IFRS17 and the Final Interim Solvency Standard, CRD, the IPSA Review, Credit Contracts and Consumer Finance Act 2003 (CCCFA) changes, ongoing Culture and Conduct updates and immediately following changes to the financial advice regime pursuant to FSLAA.

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To assist Financial Institutions, we request that the FMA issue the application and application guidance well in advance of the application window opening, work closely with the industry on the regime's implementation and provide guidance where needed to ensure that the industry is clear on what is required. As noted, significant work has been done across the industry to mature Conduct and Culture frameworks, but the FMA has yet to issue detailed guidance on its expectations under CoFI, some of which may require major shifts in business processes and spending.

We note at paragraph 14, the FMA states that the first tranche of funding is not available until July 2022, which leaves just 12 months for the FMA to prepare for the opening of the licensing window in July 2023. The dependency is on the FMA being able to provide the required information and deliver a process for administering the applications, well in advance of the window for license applications opening. If the licensing requirements for CoFI are complex and involved, Financial Institutions will need sufficient notice to prepare licensing applications otherwise this may result in a bottle neck of applications during the tail end of the licensing window. If the licensing requirements for CoFI are more straightforward, for example, exemptions are required for some requirements where there is duplication under FAP licenses, the proposed 18 month timeframe might be more realistic. We also query whether FMA's existing processes for licenses under other regimes, can be leveraged.

Considering the above, we support launching the CoFI regime with a transitional license, and a longer transitional window for the FMA and market participants to gear up to complete the full licensing process. We note that the new conduct licences are effectively coupled to existing prudential registration and licences and the FMA cannot refuse to issue or remove a conduct licence without the RB's approval. A transitional license arrangement would allow for timeframes that assist the FMA to guide Financial Institutions through the licensing approval process and avoid potential administrative issues for the FMA and the RB.

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.

We do not fully agree with a phased approach to CoFI licensing as it is not fair for certain classes of financial institutions to be given a longer period to prepare their license application than others. To reduce the risk of many applications being received towards the end of the licensing window, the FMA should ensure that they are working closely with the industry, providing guidance where required, and ensuring that the application requirements and guidance are provided well in advance. For example, the FSLAA full licencing guide was released four months (which traversed the Christmas period) prior to the licencing window opening which did not provide sufficient preparation time for firms, particularly those with complex applications, to be ready to apply early in the licencing window.

There may be limited circumstances where a phased approach to licensing is appropriate. Provided the FMA has the licensing framework in place, guidance on licensing is published well in advance, and the licensing requirements are very straightforward, namely FAP license holders are deemed to be able to obtain a conduct license, then a phased approach to licensing may be an option.

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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?

We have no further comments on this approach other than noted in response to Question 10.

12. Do you have any other general comments regarding the implementation timing of the CoFI regime?

The proposed timing for the implementation of CoFI is too short. We consider that 24 months would be a more reasonable period between applications for conduct licensing opening and all of the obligations of CoFI coming into force, which will allow sufficient time for the FMA to properly assess conduct licence applications and for Financial Institutions to prepare their businesses for implementation.

Funding options – Insurance Contract Law

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?

We consider that the ICL reforms are not sufficiently developed for appropriate funding analysis to be undertaken at this time, as acknowledged in paragraph 137 of the 2021 Review. We agree that the details of the ICL options should be reviewed once the regime has been finalised. If either option is to be progressed in the meantime, then it would be more appropriate to be option 2 given the uncertainty.

In the interim, we note that compliance with the existing Unfair Contract Terms Guidelines, plus the plain language requirements in the CCCFA and the CCCFA Responsible Lending Code are monitored by the Commerce Commission. We submit that the existing knowledge and expertise within the Commerce Commission should be leveraged for the purposes of the ICL regime. In addition, there is a risk that the insurance industry will be held to a different standard compared to either general businesses or banks (requirements in relation to unfair contract terms or plain English requirements respectively) if the same types of regimes are enforced by a different regulator for insurance companies only, and that the FMA should work closely with the Commerce Commission as a result. The options in the 2021 Review should be revised accordingly which would assist the FMA to meet the criteria of Good Public Value.

14. How would ICL Option 1 impact you/your business compared to ICL Option 2?

As stated under Question 13 above, it is difficult to determine the impact on business while the regime has not been finalised.

15. If you were to make material changes to the ICL options, how would you do so and on what basis?

Please refer to our comments under Question 13 above.

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Funding options – Climate-related Disclosures

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 FSC's members support the FMA being well funded to regulate climate-related activities. This is critical in order for New Zealand to meet its climate goals, especially the ambition of promoting the allocation of private capital to low-emissions investment as discussed in the Government's consultation on "Transitioning to a low-emissions and climate-resilient future."[1] In the context of a world leading and highly technical regime, it is vital for the relevant regulator to take a proactive approach to the regime, including informing the market through guidance on compliance expectations. As the 2021 Review notes, relevant skills are globally scarce and in high demand, and so financial institutions will require strong regulator support.

However, as noted in response to the questions in this submission on CoFI, and Question 13 on ICL, it is too early to know with certainty the final shape CRD will take and therefore challenging to comment on what best the options for the regulatory approach to implementation might look like. Consideration should be given to what the FMA would require to "operate as a credible and effective financial markets regulator" and the legislative intent of the CRD regime. The specific purposes of the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act include the economy wide objectives of ensuring "that the effects of climate change are routinely considered in business," leading "to smarter, more efficient allocation of capital," and smoothing "the transition to a more sustainable, low-emissions economy."

We caution against resourcing limitations that may preclude the FMA from monitoring voluntary CRD disclosures to ensure they do not inadvertently or deliberately distort markets. That is because mandatory CRD has a cascading effect: other businesses may opt to make voluntary CRD disclosures either for competitive purposes or because their stakeholders demand it, not least investor stakeholders who require others' CRD information to aggregate into their own mandatory CRD. We note that climate-related risks are a rapidly growing aspect of boards' routine practice, which will inevitably require the regulator to augment its existing remit with additional climate-related expertise.

Climate standards are future looking and in contrast with existing accounting standards, they depend on forward looking scenarios, which although previously used in part for prudential stress testing purposes, have never been used for reporting or conduct regulation. As the XRB consultation process unfolds, and internationally as the proposed new International Sustainability Standards Board develops sustainability standards on climate, there is likely to be a vast range of issues where a clear answer is unobtainable, and a balanced discretion is essential. This requires a regulator to be fully across the detail and involved in helping coordinate the development of new corporate, market and regulatory norms.

Given the Government's broader climate-related objectives which are underpinned by the need for reliable climate-related disclosure, it is critical that the FMA is well funded by the Crown particularly when CRD delivers value that transcends the financial sector, providing a public good. Therefore, we submit that a substantial proportion of any expanded funding should come from Crown funding. In addition, to maximise efficiency and decrease resulting costs for both regulators and industry, the

[1] https://environment.govt.nz/assets/publications/Emissions-reduction-plan-discussion-document.pdf

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FMA should collaborate closely with the MBIE, the Ministry for the Environment, the XRB and the RB on the development and implementation of this new regime.

17. How would CRD Option 1 impact you/your business compared to CRD Option 2?

As noted in response to Question 16 above, institutions will require strong support in the face of a world leading and highly technical regime. Less guidance on compliance expectations will increase the burdens on institutions in the face of a likely skills shortage.

18. If you were to make material changes to the CRD options, how would you do so and on what basis?

It would be helpful for entities if the FMA could indicate how it intends to work with the XRB in respect of recognising XRB guidance in its regulatory approach, and how it intends to leverage the XRB's guidance in respect of guidance issued by the FMA. Working closely with the XRB to avoid duplication of work would meet the criteria of Good Public Value.

FMA funding recovery options

19. Do you think that the proposed additional FMA funding should be wholly levy recovered or should the Crown contribute towards the increase? Why?

We support Option B. We consider Crown contributions should be more than the proposed 17% and we expect Government contribution better drives oversight of costs and efficiency. Although the FMA's funding has been increased several times in recent years, the percentage of the Crown contribution has decreased from 25% to the current 17% (despite the May 2020 Regulatory Impact Statement recommending the 25% contribution be maintained).

As well as increased levies to fund the new regimes, Financial Institutions will also need to pay licence application fees for conduct licenses and incur other internal costs to meet the increased obligations, including managing both the regulatory change and ongoing regulatory reporting and oversight for the new regimes. Recognition needs to be given to the additional resources, expertise and compliance costs that will be incurred by industry in connection with the CoFI, ICL and CRD.

When levies increase it is inevitable that they will be passed on and borne by consumers, which does not support measures to address the underinsurance concern for New Zealand if consumers are deterred due to increased premiums. Increased fees also risk discouraging investment or savings for retirement. Having a stable financial industry is important to the New Zealand economy, especially in light of COVID and as the 2021 Review notes, well regulated financial markets benefit all of New Zealand by driving down the cost of capital, which benefits the wider economy. A Crown contribution is more reflective of the private and public good aspect of the FMA's operations (meeting the Proportionality criteria).

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20. Do you think that the Crown should contribute relatively more to any of the regimes than others? If so, please explain why.

We consider that the Crown contribution should be increased in respect of all of the FMA's funding, but if there is a particular regime that will receive an additional Crown contribution, we consider that it should be the CRD regime. As noted in response to Question 16, a financial regulator that is under resourced for CRD would be a barrier to New Zealand meeting its climate goals. In addition, given the public impact, Crown funding should be increased to meet these objectives.

As noted in the 2021 Review, this is a new area of developing specialised knowledge and there is an anticipated demand for skilled staff from financial services businesses. Accordingly, it is appropriate that the Crown provides additional support for this regime.

21. What is the appropriate Crown/levy split of the FMA's appropriation and why?

We refer to our response to Question 1 and more specifically consider, at minimum, returning to the former level of 25% Crown and 75% industry levy.

The FMA levy

22. Do you have any feedback on the objectives underlying the levy model?

Please refer to the following Question 23.

23. Do you agree that larger entities should pay a relatively larger portion of any levy increase? If not, please explain why.

We agree that levies should be proportionate based on the size of an entity, as set out in the objectives, although as discussed in our response below to Question 24, this does result in an increased burden on large entities, and this must be appropriately managed. Some of our members have expressed concerns around the proposed weighting of the levy towards larger entities who are often the ones who do not require as much regulator engagement or assistance.

We also note a further distinction that should be taken is between into account is between for profit and not for profit entities.

24. Do you think the proposed levy changes meet the objectives?

We consider that care must be taken to ensure that the proposed levy changes do not discourage entry into and the continuation of foreign investment in the New Zealand financial services market.

Whilst we agree that it is desirable for the FMA to be a credible conduct regulator that is sufficiently resourced, and that well regulated financial markets are vitally important to New Zealand's economy, New Zealand and its financial markets are relatively small in size on a global scale. There is a risk of compliance costs becoming disproportionate to the market size and foreign investors being deterred from entering or overseas parent companies of New Zealand subsidiaries withdrawing from the market as a result, particularly in light of ongoing COVID disruptions and impacts.

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This is particularly the case for large insurers, who we note will bear the brunt of the proposed levy changes as they alone are impacted by all three regimes. For some members, annual levies would more than double by 2024/2025 under Option 1.

25. Do you have any comments on the proposed new levy classes/tiers? Should further classes be considered?

We agree with this proposal and non-retail should be charged differently.

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.

FSC members may provide business impact examples in their individual submissions.

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?

We have no feedback on this question due to the scope of the FSC membership and in fairness to all members.

Other Feedback

Regulatory engagement and industry resources

If increased FMA resource means significantly increased FMA engagement and information requests then this would need to be balanced with FSC members' resources needed to focus on servicing customers particularly given all the other regulatory change the industry is facing over the next few years (including, but not limited to, IFRS 17 and the solvency standards, the IPSA Review, Deposit Takers Act, Credit Contracts Legislation Amendment Act and full FAP licensing) in addition to the three regimes the subject of this 2021 Review.

In addition, availability and affordability of insurance is also an important consideration. The 2021 Review appears to assume that regulated entities will bear the increased levy costs, but they will ultimately be passed on to the customer whether directly or indirectly. Effectively this is a cost on top of existing resources within companies to respond to regulatory requirements. In particular, if additional resources are required internally to manage more frequent and detailed queries from the FMA this has a double impact for customers.

Methods of calculating levies

Whilst we appreciate this is outside the scope of the 2021 Review, we consider it important to note other matters for consideration. Whichever method is adopted it is important that in obtaining the funding that is required for continued growth and support of the sector, considerations of fairness are paramount and a level playing field across the sector regardless of size.

As indicated in discussions with the FMA, we understand that consultation of fundings and levies will not occur again for a longer period than the previous consultation in 2020 (although as noted above, we support further consultation in the near future given the relevant regimes are not yet finalised).

Financial Services Council
of New Zealand
Level 17, Commercial Bay Tower,
11-19 Customs Street West, Auckland 1010
P: +64 9 802 1532
E: fsc@fsc.org.nz
www.fsc.org.nz

Therefore, this consultation period is perhaps an opportunity for MBIE to reconsider how FAPs are levied. At present a FAP is levied per financial adviser, per nominated representative, and for direct advice. Some of our members consider it may be practical to have a single levy scaled on the FAP's revenue, similar to how all other major financial services sectors are levied, such as managers of managed investment schemes on funds under management, and insurers on premium for example.

These members view a scaled levy based on revenue to be fairer. At present it is possible for a digital advice provider to have millions in revenue for thousands of clients, and pay under $2,000, whereas a business with 20 financial advisers would pay over $6,000. Furthermore, a class 3 licence holder has their levy for the FAP and nominated representatives capped at $80,000, while a financial advice firm with 500 advisers would pay over $150,000 (there are three FAPs with over 500 financial advisers). There is an incentive for a large class 3 FAP to engage nominated representatives instead of financial advisers, which seems contrary to the intent of the regime to raise the quality of advice (on the basis that nominated representatives are not required to individually have the knowledge of the level 5 certificate).

Other FSC members have suggested that the current approach of a levy based on the amount of oversight the FMA needs to have over the FAP, which is dependent on the number of advisers and the type of financial advice given, is appropriate. The Class 3 levy needs to be capped because nominated representatives will often be giving limited advice on a narrow range of products with systems and processes to support this. As such, FMA oversight would be less than if the FAP had a large number of financial advisers. These members support a levy which is proportionate to the degree of oversight the FMA expects to undertake.

For an insurer, premium revenue will not necessarily equate to greater FMA resource for oversight of financial advice, for example, if a large amount of the FAPs premium revenue is generated from digital advice the oversight required from FMA would be less than if the same amount of revenue was generated by a large number of individual financial advisers.