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Financial Markets Policy
Commerce, Consumers and Communications
Ministry of Business, Innovation & Employment
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Submissions on the Conduct of Financial Institutions (COFI) regime

Our submissions are informed by our role as one of the four approved financial dispute resolution schemes in New Zealand. In terms of 'financial institutions' we have four insurers as FSCL members (AIG, Allianz, Chubb, and QBE), 13 NBDTs (mostly credit unions), and no banks. In terms of intermediaries, we have approximately 4,000 financial adviser members and possibly other financial service providers who may fall under the definition of 'intermediary'.

We are regularly investigating complaints about our insurer, NBDT, and financial adviser members. In the 2019/2020 reporting year we investigated 103 complaints about insurers, 4 complaints about credit unions, and 48 complaints about financial advisers (including risk advisers, financial planners, and insurance and mortgage brokers).

We have provided our submissions on both COFI discussion papers in this letter. Part A focusses on the regulations for the COFI regime, and Part B focusses on the treatment of intermediaries.

PART A – SUBMISSIONS ON REGULATIONS TO SUPPORT THE NEW REGIME FOR THE CONDUCT OF FINANCIAL INSTITUTIONS

Overall, we consider it will be helpful for the industry if some regulations are introduced to support the new COFI regime. We set out below our submissions on specific questions and paragraphs in the discussion paper.

1. Question 2 – Do you have any comments on MBIE's position that no regulations are needed at this time to support section 446M(1)(a)?

1.1. Yes, we support MBIE's position. We consider that the overlap with existing regulatory regimes (for example, under the Credit Contracts and Consumer

Finance Act 2003) can be managed, and in fact, the overlap in the regimes would complement each other.

2. Paragraph 44 – reference to section 446M(1)(ab)

2.1. With reference to the requirement in section 446M(1)(ab) about designing and managing the provision of financial services, we simply comment that we consider this provision will lead to better consumer outcomes. As an example, in 2020 we commenced the investigation of a complaint about a financial adviser where the consumer was advised to change from a trauma policy (with a sum insured of $100,000) to a trauma policy with a sum insured of $100,000 but with a maximum payment of $20,000 for any one trauma claim. Fortunately, this complaint was able to be resolved early, and we did not need to conduct a full investigation.

2.2. However, it was clear from the outset that the new policy did not appear to be fit for purpose for that particular insured. He was aged 65, unlikely to suffer and survive 5 trauma events, and was therefore unable to obtain the benefit he would have received under his old policy. However, in a wider sense, it did not seem to be a policy that would be fit for purpose for most consumers, as it would be unlikely for an insured to suffer and survive 5 trauma events.

2.3. This leads us, however, to ask the question: what next? If the insurer in this case example identified this policy as one that might not be meeting the requirements and objectives of consumers, what would the insurer be expected to do in terms of their next steps? Some guidance may be needed.

2.4. We suggest the development of regulations to provide practical guidance about the steps financial institutions must take when they identify a product or service that does not comply with that financial institution's fair conduct programme.

3. 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.

3.1. We comment that it could be difficult for financial institutions to define the parameters of 'groups of consumers' who may be the intended consumers of a particular product or service. Regulations to guide financial institutions may be useful. We consider the use of examples in the regulations on this issue could be a particularly helpful way to provide this guidance.

4. Question 6 – remediation of issues

4.1. With reference to paragraph 63, our experience mirrors the findings of the FMA-RBNZ's review of banks and life insurers, that financial institutions are more likely to make process and policy changes following lag indicators, rather than what is desired: following both lag indicators and lead indicators. FSCL supports any regulations that encourage financial institutions to be pro-active in monitoring weaknesses in systems and processes.

4.2. We therefore support regulations that reflect the bullet points at paragraph 66. However, we consider it could be helpful to include regulations that help define what 'identifying' means in section 446M(1)(ad). That is, that 'identifying' not only includes when there has been a complaint, but also when a problem has been identified without there having been a complaint, during a regular internal COFI review by a particular financial institution.

4.3. We also note more specifically, with reference to paragraph 66(c), that the paragraph may be better worded as:

> "Once conduct that fails to comply, *or could possibly fail to comply*, with the fair conduct principle has been identified…."

This would encourage pro-active identification of problems. By only including the words 'fails to comply', it implies that there must have been an actual finding of 'failure' (say as the result of an upheld complaint by a dispute resolution scheme (DRS)), before a financial institution must take any remedial action. That would not support the proactive identification of problems.

4.4. In addition, with reference to paragraph 66(f) – this relates to our submission above about the development of some 'what next' regulations. Exactly how would a financial institution communicate with consumers about the progress and outcome of a review and remediation process? And, with reference to paragraphs 74-77, and question 8 – in relation to communicating with consumers – how will financial institutions ensure that communication about remediation actually occurs, when the consumer only deals with their financial adviser? That is, from the consumer's point of view – they may never have direct contact with their financial institution and instead their direct point of contact is their financial adviser.

5. Question 10 – further regulations for complaints handling

5.1. We welcome the development of further regulations for complaints handling. We also comment that although there may be overlap with other regimes (for example, the transitional and full licensing standard condition on complaints handling under FSLAA), if COFI regulations mirror regulations under other regimes, then there will be minimal regulatory duplication (see bullet point 3 of the 'cons' column at paragraph 93).

5.2. At paragraph 90, we suggest a further bullet point stating that: "The complaints process must be clear and accessible". For example, being in an easy to find section of a financial institution's website. We also suggest a further bullet point requiring financial institutions to provide sufficient training for their staff on how to recognise a complaint.

5.3. With reference to bullet point 2 of the cons table at paragraph 93 – we agree that 'timely' is subjective. We suggest there could be some further regulatory guidance provided about what 'timely' means. We point you to the timeliness provisions in the Fair Insurance Code 2020 – which says that if a complaint is not resolved within the insurer's internal complaints process (ICP) within 2 months, the insurer will issue a deadlock letter.

5.4. We find that some financial service providers allow complaints to 'linger' within their ICP which is often to the detriment of the consumer and reduces the chance of a complaint resolving. If the financial service provider cannot resolve the complaint early (within 2 months), then it is probably best for the financial service provider to tell the consumer they have the option to contact the DRS.

5.5. With reference to paragraph 92 – it is correct that the DRSs all have their own (and very similar) requirements on their members in terms of ICPs. However, regulations have more teeth than the DRSs' terms of references.

5.6. With reference to bullet point 3 of the 'cons' table at paragraph 93 – we disagree there would be significant additional costs to 'adjust' complaints processes. All financial institutions should already have mature IT systems in terms of their complaint processes. Any further regulation would only, we suggest, involve 'tweaks' of IT systems, not significant changes.

6. Question 11 – Claims handling and settlement

6.1. We agree that it in supporting good consumer outcomes, regulations that mirror the Fair Insurance Code's requirements on all insurers in terms of claims

handling and settlements, would be desirable. Similar to our comments above, we regularly investigate complaints where the initial claim lingered within the insurer's claims process, for an unreasonable period of time.

6.2. We also wish to highlight for the Ministry's benefit that, with reference to paragraph 96, we are currently entering into an MOU with the EQC in terms of their membership with us generally, and more specifically, in terms of insurers now managing claims handling on behalf of the EQC. It should be noted that in terms of deadlocked complaints where it is an EQC claim (in whole or in part), some complaints will come to the DRS, whereas some will go to the Parliamentary Ombudsman.

6.3. With reference to paragraph 99 – we consider the wording of bullet point 2 could be amended to include reference to communicating with brokers/advisers. Consumers usually communicate with their adviser/broker directly when they have a claim (at least initially), rather than directly with their insurer. The regulations should ensure that brokers/advisers pass on the insurer's updates to the consumer, in a timely manner.

7. Question 12 – definition of 'agents'

7.1. We note our support of specifically identifying as one type of 'agent': 'a loss assessor or loss adjustor acting on behalf of the insurer' (see paragraph 102(b)). It is quite common for consumers to complain about loss adjustors.

7.2. Loss adjustors play a key role in the management and settlement of claims because they provide a significant amount of information (essentially, evidence) relevant to the claim. We have seen cases where loss adjustors issue more than 10 reports. It is also common for the consumer to interact directly with the loss adjustor; opening the door for service complaints to arise.

8. Vulnerable consumers

8.1. We agree, consideration of vulnerable consumers needs to be at the heart of any fair conduct programme. We note here with reference to paragraph 115 that it would be beneficial to specifically mention vulnerable consumers in the list of factors in section 446M(1A), simply from a usability perspective. With the high levels of compliance requirements on financial institutions, it is helpful to have 'reminders' at each stage where consideration may need to be given to vulnerable consumers.

9. Prohibition of sales incentives

9.1. We agree that sales incentives based **solely** on volume or value targets, do not support 'good consumer outcomes'.

9.2. There are other types of sales incentives that can create risky conflicts of interests for advisers and brokers, as noted in the discussion paper from paragraph 163 onwards. However, we agree that a focus on volume or value targets is the best course of action at this stage. We are confident that if other sales incentives result in poor consumer outcomes once the COFI regime is bedded in, this can be addressed in the future.

10. Publishing requirements

10.1. With reference to paragraphs 194(c) and 196 – we consider there should be further prescription. We suggest the Ministry considers requiring financial institutions to publish information about their complaints in a way which mirrors the information financial advisers need to provide about complaints in their disclosure (specifically – publicly available information, and specific complaints disclosure).

10.2. We also support regulations that require disclosure about the expected timelines for complaints (see paragraphs 5.3 and 5.4 above), and the next steps if the complaint is not resolved internally (that is, referral to the DRS).

11. Question 35 – calling in

11.1. We support the calling in of contracts of insurance as financial products under Part 2.

PART B – SUBMISSIONS ON THE TREATMENT OF INTERMEDIARIES UNDER THE NEW REGIME FOR THE CONDUCT OF FINANCIAL INSTITUTIONS

12. Options in relation to definitions

12.1. We support options 1 and 2. In relation to option 1: we agree that the definition of 'intermediary' should comprehensively capture all those involved in the sales and distribution process, including both non-advised sales, and financial advisers/financial advice providers, where that intermediary is not an 'agent' of the financial institution (for example claims fulfilment providers).

12.2. In relation to option 2: we agree that third parties such as lawyers and accountants, who could act as a financial institution's agent in certain circumstances and transactions, should not be covered by COFI.

13. Options in relation to obligations

13.1. We prefer option 5 – financial institutions having different levels of oversight requirements for FSLAA intermediaries compared to the level of oversight requirements on other intermediaries. In particular, we would be concerned if financial institutions needed to 'manage or supervise' FSLAA intermediaries' compliance with the financial institution's fair conduct programme, and consider 'monitoring' to be the better approach. The reason for our view is that a 'managing and supervising' approach would be an overly burdensome compliance requirement for both FSLAA intermediaries and financial institutions, particularly because of the significant overlap with the FSLAA compliance programme, as identified in the discussion paper.

13.2. However, we do not agree with the suggestion in option 5 that all other non-FSLAA intermediaries should only be 'monitored' and not 'managed or supervised' by the financial institution. In essence, we think there needs to be a clearer delineation between who is a non-FSLAA intermediary and who is an 'agent'.

13.3. To unpack this a little further, the discussion paper suggests that a travel agent who sells consumers travel insurance policies would be a non-FSLAA intermediary, but would also be an 'agent' of the insured (because, with reference to paragraph 38, the travel agent assists in the administration of performance of the insurer's service – i.e. they assist in the process of placing the insurance policy).

13.4. But, as the insurer's 'agent', the travel agent should, in our view, be required to follow the financial institution's procedures and processes that are necessary or desirable to support the financial institution's compliance with the fair conduct principle. Travel agents do not have to comply with other regulatory requirements, so there is greater risk that travel agents may not treat customers fairly. This means there should be more oversight by the financial institution on travel agents. We also consider this to be workable in practice, because a travel agent usually only has a few different policy options for consumers, and those are often policies from the same insurer.

13.5. We use the travel agent example because when investigating travel insurance complaints, we have encountered situations where travel agents have placed consumers with travel insurance policies that are unfit for purpose, or where the travel agent has misrepresented the level of cover. In those cases, we have treated the travel agent as the insurer's 'agent', meaning the insurer is

ultimately responsible for any breach of the law on the travel agent's part. We also use the travel agent example to highlight that greater clarity about who is an FSLAA-intermediary, who is a non-FSLAA intermediary, and who is an agent, may be beneficial for the industry.

14. Dealing with misconduct

14.1. Lastly, we note that option 5 would require financial institutions to 'deal with' 'misconduct' by intermediaries, (both FSLAA-intermediaries, and other intermediaries). 'Misconduct' is quite far reaching. It could include findings of misconduct by a DRS about a financial adviser in an upheld complaint. Further, 'deal with' is vague. Does this mean the financial institution needs to be responsible to pay compensation for an upheld complaint against a financial adviser who did not comply with the financial institution's fair conduct principal? Further guidance on what 'dealing with misconduct by intermediaries' means, would be welcomed.

Please contact us if you want to discuss our submissions in more detail.

Yours sincerely

Privacy of natural persons

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