

Departmental Disclosure Statement

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| Financial Markets (Conduct of Institutions) Amendment Bill |
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The departmental disclosure statement for a government Bill seeks to bring together in one place a range of information to support and enhance the Parliamentary and public scrutiny of that Bill.

It identifies:

- the general policy intent of the Bill and other background policy material;
- some of the key quality assurance products and processes used to develop and test the content of the Bill;
- the presence of certain significant powers or features in the Bill that might be of particular Parliamentary or public interest and warrant an explanation.

This disclosure statement was prepared by the Ministry of Business, Innovation and Employment.

The Ministry of Business, Innovation and Employment certifies that, to the best of its knowledge and understanding, the information provided is complete and accurate at the date of finalisation below.

22 November 2019

Contents

| | |
|------------------------------------------------------------|----|
| Contents..... | 2 |
| Part One: General Policy Statement..... | 3 |
| Part Two: Background Material and Policy Information | 5 |
| Part Three: Testing of Legislative Content..... | 7 |
| Part Four: Significant Legislative Features | 10 |

Part One: General Policy Statement

This Bill relates to the conduct of institutions in financial markets.

The purpose of the Bill is to improve the conduct of certain financial institutions in respect of services and products provided to consumers, thereby reducing the risk of harm to those consumers. To achieve this, the Bill makes amendments to the Financial Markets Conduct Act 2013 (the **FMC Act**), amongst other enactments, to ensure that certain financial institutions and their intermediaries comply with a principle of fair conduct and associated duties and regulations.

Introduction of conduct licensing regime for certain financial institutions

The Bill creates a new regulatory regime for the general conduct of financial institutions and their intermediaries. This regime has been designed in response to recent reviews that have identified that certain institutions, particularly banks and life insurers, lack focus on good outcomes for customers and have ineffective systems and controls to identify, manage, and remedy conduct issues.

To address these issues, the Bill—

- requires financial institutions that are in the business of providing relevant services to obtain a licence under Part 6 of the FMC Act. The scope of the regime is intended at this stage to cover registered banks, licensed insurers, and licensed non-bank deposit takers and to apply broadly to all services and associated products provided by those institutions:
- requires financial institutions and intermediaries to comply with a fair conduct principle to treat consumers fairly, including by paying due regard to their interests. That conduct principle sets the framework for the regime and will require institutions and intermediaries to turn their minds to the fair treatment of consumers in a broad range of circumstances, from early design of products and services to post-sale dealings:
- requires financial institutions to establish, implement, and maintain an effective fair conduct programme. That requirement is a way for financial institutions to operationalise the fair conduct principle through policies, processes, systems, and controls throughout every relevant part of their business, from the governance level to day-to-day interactions with consumers, whether those interactions are made directly or indirectly through intermediaries:
- requires financial institutions and intermediaries to comply with the fair conduct programme. This is aimed at ensuring that the chain of distribution of services and products is captured. That requirement is aimed at ensuring that institutions take responsibility from the top down. The requirement does not apply to a financial institution acting as an intermediary of another financial institution, or to an intermediary to the extent that it may be giving regulated financial advice. Those restrictions, however, do not limit a financial institution's obligations to have processes providing for appropriate control of or supervision over their intermediaries, including financial advice providers:
- requires financial institutions to ensure that intermediaries comply with the conduct programme. That obligation is aimed at ensuring that institutions take care that any intermediaries distributing their products or services are doing so responsibly. The obligation, however, does not apply to intermediaries that are financial institutions or financial advice providers:
- requires financial institutions and intermediaries to comply with regulations that regulate incentives. Those regulations will be able to prohibit incentives based on volume or value sales targets:
- provides that financial institutions and intermediaries will be subject to the FMC Act's compliance and enforcement tools such as civil pecuniary penalties for contraventions

of various obligations, and licensed financial institutions will be subject to licensing actions such as censure and the imposition of action plans:

- provides protection to employees and agents of financial institutions and intermediaries who report a contravention of a provision of the FMC Act or of the fair conduct principle to the Financial Markets Authority (the FMA). This will provide support and a clear process for people who may wish to report misconduct issues and help uncover any such issues under the new regime:
- provides for interactions between different regulatory regimes and regulators that arise as a result of the new conduct regime, including multiple pecuniary penalties for the same conduct, proceedings under different enactments, and licensing for conduct and prudential activity.

Transitional arrangements

The Bill allows regulations to be made to apply the licensing requirements to different classes of entities at different times (up to 4 years after the date on which the Bill receives the Royal assent). The Bill also allows licence applications to be made before commencement of the provisions of the Bill and associated regulations, although the FMA may refuse to consider an application if it is made before a specified date, or event or before a specified circumstance arises.

The Bill contains a regulation-making power to prohibit or regulate certain activities related to the offering or giving of sales incentives in connection with a relevant service or associated product. These regulations may apply to existing incentive arrangements and those entered into before the commencement of the regulations, but cannot apply to any incentive that is paid, is payable, or to which a person has become entitled before the commencement of the regulations.

Other amendments

The Bill includes other amendments to ensure the licensing regime is implemented effectively across the multiple regulatory systems it affects. Those amendments include—

- an information-sharing power for the Commerce Commission to share with the FMA information it holds in respect of the Credit Contracts and Consumer Finance Act 2003; and
- minor amendments to other enactments.

Commencement

Most of the Bill will come into force on a date or dates specified by 1 or more Orders in Council, but no later than 2 years after the date of Royal assent. The deferred commencement allows regulations to be made to implement the Bill. The Bill's regulation-making powers and a power for the Commerce Commission to share information with the FMA come into force on the day after the Bill receives the Royal assent.

Part Two: Background Material and Policy Information

Published reviews or evaluations

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| 2.1. Are there any publicly available inquiry, review or evaluation reports that have informed, or are relevant to, the policy to be given effect by this Bill? | YES |
| <p>Review of Insurance Contract Law: Issues Paper, Ministry of Business, Innovation and Employment, May 2018: https://www.mbie.govt.nz/dmsdocument/962-issues-paper-review-insurance-contract-law-pdf</p> <p>Conduct of Financial Institutions Review: Options Paper, Ministry of Business, Innovation and Employment, 27 April 2019: https://www.mbie.govt.nz/dmsdocument/5154-conduct-of-financial-institutions-review-options-paper</p> <p>Thematic review of bank conduct and culture, Financial Markets Authority and Reserve Bank of New Zealand, 5 November 2018: https://www.fma.govt.nz/assets/Reports/Bank-Conduct-and-Culture-Review.pdf</p> <p>Thematic review of life insurer conduct and culture, Financial Markets Authority and Reserve Bank of New Zealand, 29 January 2019: https://www.fma.govt.nz/assets/Reports/Life-Insurer-Conduct-and-Culture-2019.pdf</p> | |

Relevant international treaties

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| 2.2. Does this Bill seek to give effect to New Zealand action in relation to an international treaty? | NO |
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Regulatory impact analysis

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| 2.3. Were any regulatory impact statements provided to inform the policy decisions that led to this Bill? | YES |
| <p>Regulatory Impact Statement: Regulatory regime to govern the conduct of financial institutions, Ministry of Business, Innovation and Employment, 13 November 2019: https://www.mbie.govt.nz/assets/regulatory-impact-statement-regulatory-regime-to-govern-the-conduct-of-financial-institutions.pdf</p> | |

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| 2.3.1. If so, did the RIA Team in the Treasury provide an independent opinion on the quality of any of these regulatory impact statements? | NO |
| <p>The Impact Statement did not meet the threshold for Treasury RIA Team assessment and was assessed by the MBIE Regulatory Impact Assessment Review Panel.</p> | |

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| 2.3.2. Are there aspects of the policy to be given effect by this Bill that were not addressed by, or that now vary materially from, the policy options analysed in these regulatory impact statements? | NO |
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Extent of impact analysis available

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| 2.4. Has further impact analysis become available for any aspects of the policy to be given effect by this Bill? | NO |
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| 2.5. For the policy to be given effect by this Bill, is there analysis available on: | |
| (a) the size of the potential costs and benefits? | YES |
| (b) the potential for any group of persons to suffer a substantial unavoidable loss of income or wealth? | YES |
| Analysis of the costs and benefits of the policy to be given effect by this Bill is included in the RIS referenced above in question 2.3. | |

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| 2.6. For the policy to be given effect by this Bill, are the potential costs or benefits likely to be impacted by: | |
| (a) the level of effective compliance or non-compliance with applicable obligations or standards? | YES |
| (b) the nature and level of regulator effort put into encouraging or securing compliance? | YES |
| <p>The Bill introduces a licensing requirement for certain financial institutions (eg banks and insurers) under the Financial Markets Conduct Act 2013 (FMC Act). Once licensed, licensees will be subject to various conduct obligations.</p> <p>In order to achieve the purposes of this new licensing regime, licensees will need to comply with their licence obligations and the regulator (the Financial Markets Authority (FMA)) will need to effectively monitor and enforce licence obligations to ensure compliance. Parts 6 and 8 of the FMC Act, which will apply to licensed financial institutions, sets out a comprehensive licensing framework for ensuring that licensees comply with their licence obligations and provides a range of monitoring and enforcement powers for the FMA.</p> | |

Part Three: Testing of Legislative Content

Consistency with New Zealand's international obligations

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| 3.1. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations? |
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| No separate formal steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations as no policy measures in this Bill have been identified, as part of the normal policy process, as raising any questions of consistency with our international obligations. |
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Consistency with the government's Treaty of Waitangi obligations

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| 3.2. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with the principles of the Treaty of Waitangi? |
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| The provisions of the Bill apply generally to the New Zealand public as participants in the New Zealand financial markets and do not impact on the principles of the Treaty of Waitangi. |
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Consistency with the New Zealand Bill of Rights Act 1990

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| 3.3. Has advice been provided to the Attorney-General on whether any provisions of this Bill appear to limit any of the rights and freedoms affirmed in the New Zealand Bill of Rights Act 1990? | YES |
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| Advice provided to the Attorney-General by the Ministry of Justice is generally expected to be available on the Ministry of Justice's website at: |
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| https://www.justice.govt.nz/justice-sector-policy/constitutional-issues-and-human-rights/bill-of-rights-compliance-reports/advice/ . |
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Offences, penalties and court jurisdictions

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| 3.4. Does this Bill create, amend, or remove: | |
| (a) offences or penalties (including infringement offences or penalties and civil pecuniary penalty regimes)? | YES |
| (b) the jurisdiction of a court or tribunal (including rights to judicial review or rights of appeal)? | NO |
| <p>Clause 10 of the Bill amends existing civil liability provisions of the FMC Act so that civil liability, including pecuniary penalties, may arise for a contravention of certain obligations, including:</p> <ul style="list-style-type: none"> - duties to have an effective fair conduct programme, to make that programme available to certain persons, and to comply with the programme (new sections 446G, 446H and 446I) - duties relating to intermediaries (new section 446K) - financial institution's duty to comply with incentives regulations (new section 446N) - intermediary's duty to comply with incentives regulations (new section 446O). <p>The FMA may apply to the court for pecuniary penalty orders in respect of contravention of these civil liability provisions. The maximum amount of pecuniary penalty available for contravention of one of these liability provisions is the greatest of the consideration for the relevant transaction, 3 times the amount of the gain made or the loss avoided, and \$1 million in the case of an individual or \$5 million in any other case.</p> <p>The Bill also extends the primary licensing framework under Part 6 of the FMC Act to persons licensed as financial institutions. This subjects any such person to potential civil liability, including pecuniary penalties, for contravention of relevant obligations set out in section 449 of the Act.</p> | |
| 3.4.1. Was the Ministry of Justice consulted about these provisions? | YES |
| <p>MBIE consulted with the Offences and Penalties team at the Ministry of Justice on the Bill, including the civil liability and pecuniary penalties provisions. The Ministry of Justice did not raise any concerns.</p> | |

Privacy issues

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| 3.5. Does this Bill create, amend or remove any provisions relating to the collection, storage, access to, correction of, use or disclosure of personal information? | NO |
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External consultation

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| 3.6. Has there been any external consultation on the policy to be given effect by this Bill, or on a draft of this Bill? | YES |
| <p>MBIE engaged closely with the FMA, the Reserve Bank of New Zealand (RBNZ), the Treasury and the Commerce Commission in developing the policy proposals.</p> <p>MBIE also conducted a public consultation over a six-week period in April and May 2019 which sought feedback on a broad range of policy options: https://www.mbie.govt.nz/dmsdocument/5154-conduct-of-financial-institutions-review-options-paper. Eighty-five submissions were received. Officials also met with various stakeholders during this consultation process to seek further feedback on the policy proposals.</p> <p>In October 2019, following the announcement of policy decisions, MBIE also consulted with a number of industry associations and key stakeholders during the drafting of the Bill to ensure that the Bill's provisions are workable and complete.</p> | |

Other testing of proposals

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| 3.7. Have the policy details to be given effect by this Bill been otherwise tested or assessed in any way to ensure the Bill's provisions are workable and complete? | YES |
| <p>The policy decisions have been discussed with the Legislation Design and Advisory Committee. The Bill was also discussed with a member of LDAC on an informal basis. Feedback was provided about the design of the regime and structure of the Bill. This feedback has been taken into account in the development of the Bill.</p> | |

Part Four: Significant Legislative Features

Compulsory acquisition of private property

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| 4.1. Does this Bill contain any provisions that could result in the compulsory acquisition of private property? | NO |
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Charges in the nature of a tax

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| 4.2. Does this Bill create or amend a power to impose a fee, levy or charge in the nature of a tax? | NO |
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Retrospective effect

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| 4.3. Does this Bill affect rights, freedoms, or impose obligations, retrospectively? | NO |
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Strict liability or reversal of the usual burden of proof for offences

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| 4.4. Does this Bill: | |
| (a) create or amend a strict or absolute liability offence? | NO |
| (b) reverse or modify the usual burden of proof for an offence or a civil pecuniary penalty proceeding? | NO |

Civil or criminal immunity

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| 4.5. Does this Bill create or amend a civil or criminal immunity for any person? | NO |
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Significant decision-making powers

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| 4.6. Does this Bill create or amend a decision-making power to make a determination about a person's rights, obligations, or interests protected or recognised by law, and that could have a significant impact on those rights, obligations, or interests? | YES |
| The Bill amends section 388 of the FMC Act to require any person acting as a financial institution (as defined in the Bill) to be licenced under Part 6 of the Act. This requirement gives the FMA the power to issue licences to any such person (see section 394), which it must do if it is satisfied that the grounds in section 396 are made out. | |

Powers to make delegated legislation

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| <p>4.7. Does this Bill create or amend a power to make delegated legislation that could amend an Act, define the meaning of a term in an Act, or grant an exemption from an Act or delegated legislation?</p> | <p>YES</p> |
| <p>Clause 16(2), section 546 amended, allows regulations to be made to prescribe:</p> <ul style="list-style-type: none"> - classes of contracts for the purposes the definition of “consumer credit contract” in new section 44S of the Bill - classes of service for the purposes of the definition of “relevant service” in new section 446F of the Bill, effectively excluding services from being relevant services under that section - requirements which fair conduct programmes must not or are not required to impose, in respect of intermediaries (new section 446M(2)(b)-(c)) - occupations and activities for when a person is <u>not</u> involved in the provision of a relevant service or associated product, effectively carving them out from the definition of “intermediary” in new section 446E. <p>These regulation-making powers allow the regime to be refined in the context of changing technology, circumstances, and market practice: such changes often being unforeseeable.</p> <p>Before regulations:</p> <ul style="list-style-type: none"> - excluding services from being relevant services under new section 446F, or - prescribing occupations and activities for when a person is <u>not</u> involved in the provision of a relevant service or associated product <p>can be made, the Minister must be satisfied that the extent of the exemption or exclusion is not broader than is reasonably necessary to address the matters that gave rise to the regulations (section 550(1)(c)).</p> <p>Before regulations prescribing matters to which fair conduct programmes cannot (or are not required to) relate can be made, the Minister must be satisfied that the extent to which requirements are disapplied is not broader than is reasonably necessary to address the matters that gave rise to the regulations (section 550(1)(b)).</p> | |

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| 4.8. Does this Bill create or amend any other powers to make delegated legislation? | YES |
| <p>Clause 16(2), section 546 amended, allows various regulations to be made, including to:</p> <ul style="list-style-type: none"> - prescribe various requirements for fair conduct programmes, including: <ul style="list-style-type: none"> o governance and management of conduct and risks associated with that conduct (including imposing duties on employees, intermediaries, and other agents) o monitoring outcomes for consumers, including whether consumers' interests are being had regard to o how services or products are designed o dealing with consumer complaints o dealing with insurance claims o communicating with consumers, including particular disclosure requirements and requirements for warnings o appropriate control or supervision over the involvement of intermediaries in the provision of the services and products o the design and management of incentives and other remuneration (for example, managing the risk of poor consumer outcomes associated with incentives) - prohibit or regulate practices, activities or other conduct related to the offering or giving of incentives. <p>These regulation-making powers are included to allow matters provided in the Bill to be implemented effectively, such as the format and content of required documents/systems/procedures, the manner in which duties must be carried out, and subject matter that requires flexibility or updating in light of developments over time.</p> <p>Clause 18 and Schedule 1 allow regulations to provide that the new licensing requirement does not apply until a particular date for a particular class of persons.</p> <p>This regulation-making power is included to enable a phased approach to bringing in the new requirements, in order to manage workloads for the regulator and the industry.</p> <p>Before any regulations can be made, the Minister must consult the FMA (section 549) and, as per standard policy practice, affected stakeholders will be consulted.</p> | |

Any other unusual provisions or features

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| 4.9. Does this Bill contain any provisions (other than those noted above) that are unusual or call for special comment? | NO |
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