Regulatory Impact Statement: fit for purpose financial markets conduct regulation

Coversheet

Purpose of Document	
Decision sought:	Reforms to financial services conduct regulation
Advising agencies:	Ministry of Business, Innovation and Employment (MBIE)
Proposing Ministers:	Minister of Commerce and Consumer Affairs
Date finalised:	13/08/2024

Problem Definition

A number of legislative reforms have been made to financial markets conduct regulation over the past decade. While this has improved conduct and outcomes, it has also led to a complex regulatory landscape and some unnecessary compliance costs, including:

- Some requirements introduced by the Financial Markets (Conduct of Financial Institutions) Amendment Act in 2022 (CoFI Act) which is due to come into force in 2025 may be leading to unnecessary compliance costs by: being overly prescriptive, causing unnecessary duplication with other regimes, or limiting flexibility for firms.
- The Minister of Commerce and Consumer Affairs has set an expectation that the Financial Markets Authority (FMA) shift to a single conduct licence. This shift could occur without legislative change to the Financial Markets Conduct Act 2013 (FMC Act), however under current provisions there would be challenges for the FMA in implementing the change operationally (eg to consolidate existing licences held by each firm would likely require each firm's consent).
- In some cases firms are subject to similar or overlapping requirements from both the FMA and Reserve Bank of New Zealand (RBNZ) which could give rise to unnecessary compliance costs.
- The FMA also lacks tools to act proactively in some areas of conduct regulation, such as change in control approval requirements and on-site inspections, which limits its ability to effectively regulate market conduct.

Executive Summary

Context

The Government has committed to reforming financial services regulation, with a view to reducing unnecessary red tape and compliance burden for businesses. As part of this wider reform, the Government is also interested in reviewing whether changes can be made to improve the conduct regulation of financial market participants.

Current state of conduct regulation of financial market participants

New Zealand's financial markets are currently regulated under a 'twin peaks' model, wherein the RBNZ regulates prudential matters, and the FMA regulates conduct matters.

After issues arose in Australia, the FMA and RBNZ released a series of reports in which they reviewed how banks and insurers managed risks relating to conduct. These reviews found there were insufficient controls and processes in place and that more needed to be done to ensure these businesses, and financial institutions generally, were taking steps to consider risks relating to conduct.

The CoFI Act, passed into law in 2022 and due to come fully into force in March 2025, was intended to address this. The CoFI Act introduces a fair conduct principle, which will require financial institutions treat consumers fairly. It also will require financial institutions create and maintain a fair conduct programme, which would set out systems, processes, policies, and controls for how these firms would ensure they complied with the principle.

Summary of problem definition

There are several perceived problems with the current state of financial markets conduct regulation in New Zealand. Some of these are specific to the CoFI Act itself, while others relate to conduct regulation more broadly. These are:

1. The introduction of the CoFI Act has added additional regulatory burden for financial institutions. While most stakeholders agree that the overall intent and framework is sound, some say the requirements are overly prescriptive, duplicative of other regimes, or limit flexibility, all of which can lead to unnecessary compliance costs. Of particular interest to stakeholders are:
    a. the definition of the fair conduct principle, and
    b. the minimum requirements relating to fair conduct programmes.
2. The FMC Act permits a siloed approach to licensing, wherein individual licences are issued for different market services. Some stakeholders have stated that this creates unnecessary duplication and compliance burden.
3. Because the RBNZ and FMA both have roles and responsibilities in relation to the regulation of financial markets, there are points of overlap between them. The FMA does not have the tools to rely on information gathered by the RBNZ even where doing so would be appropriate and reduce duplication, which occasionally creates compliance burden for firms.
4. The FMA lacks proactive tools in respect to some aspects of conduct regulation. This limits its flexibility, forcing it to rely largely on backwards-looking tools, which in turn can create burden for business and affects its ability to effectively regulate market conduct. In particular, the FMA lack:
    a. change in control approval requirements,
    b. on-site inspection powers, and
    c. export report powers.

Summary of options discussed and preferred option

Fair conduct principle

The current definition of fair conduct in the CoFI Act is deliberately open-ended. Some stakeholders have said this open-ended nature may leave firms uncertain about what fair treatment of consumers covers, which could lead to financial institutions being unnecessarily risk averse, reducing the provision of financial products and services that might otherwise be appropriate or desirable.

The discussion document ‘Fit for purpose financial services conduct regulation’ and this Regulatory Impact Statement (RIS) explore two options in relation to this: continuing with the status quo (Option 1) or changing the definition to become exhaustive (Option 2). Through submissions it became clear stakeholders preferred to keep the definition open-

ended. This was supported by our own analysis, which found this to be a more appropriate approach. Keeping the status quo (Option 1) is therefore the preferred option.

Minimum requirements relating to fair conduct programmes

The CoFI Act requires financial institutions to establish, implement and maintain a fair conduct programme. Section 446J sets a non-exhaustive list of minimum requirements that must be met in relation to fair conduct programmes.

Stakeholders say these requirements are overly specific and may not be necessary or appropriate for all fair conduct programmes, which could create unnecessary compliance costs and limit flexibility. This could result in reduced provision of products and services, or additional costs being passed along to consumers.

We proposed several options in relation to the minimum requirements: continuing with the status quo (Option 1), removing some requirements and amending others (Option 2), introducing new requirements relating to fees and complaints (Option 3), and removing all minimum requirements entirely (Option 4).

Stakeholders overwhelmingly supported Option 2 (removing some requirements and amending others) on the basis it would reduce unnecessary compliance burden. Our analysis also supported this as the option most likely to achieve the outcomes we sought. Some submitters, and the Minister of Commerce and Consumer Affairs, also supported including Option 3 (introducing new requirements) in addition to Option 2. Because the two are not mutually exclusive, both amending and removing some minimum requirements (Option 2), as well as introducing new requirements (Option 3), are the preferred options.

Licensing

Under the FMC Act, the FMA may issue different licences for each type of market service, or a single licence covering more than one type of market service. Currently, the FMA chooses to issue different licences for each type of market service, but the Minister of Commerce and Consumer Affairs has set an expectation that a single licence will be issued by the FMA. The FMA has indicated that it intends to proceed with this approach in future.

While a shift to a single licence could occur operationally and without legislative change to the FMC Act, there would be practical challenges with this approach (eg consolidating existing licences held by each firm would likely require each firm's consent). These problems would be solved largely by amendments to the legislation.

We proposed two options in relation to licensing: transition to a single licence without legislative change (Option 1) or amend the FMC Act to require the FMA issue a single licence covering different types of market services (Option 2). Submitters strongly supported Option 2. This was supported by our analysis as the outcome most likely to support the objectives of the review. Amending the FMC Act (Option 2) is therefore the preferred option.

Reliance provision

The FMA and the RBNZ both have regulatory oversight of financial institutions (ie registered banks, licensed insurers, and non-bank deposit takers (NBDT)) and their requirements sometimes overlap. Stakeholders have stated both regulators may request and consider similar information from firms around specific matters (eg business continuity plans) and that the compliance burden could be reduced if regulators coordinate and collaborate more effectively on these matters. Although regulators do coordinate in

informal ways, there is no formal mechanism which would allow one to rely on assessments made by the other.

We proposed two options in relation to reliance between regulators: keeping the status quo (Option 1), and amending the FMC Act to enable the FMA to rely on an assessment by the RBNZ if they so choose (Option 2). All submitters supported Option 2. This option was also supported by our analysis and is our preferred option.

FMA toolkit

The FMA has said it lacks the tools it requires to perform its role as regulator effectively. They wish to see three new tools introduced, which were consulted on as part of the discussion document:

1. Change in control approval requirements

Financial institutions are required to obtain regulatory approval from the RBNZ prior to a change in control, but not from the FMA (although the FMA does have an expectation that licensed firms engage with it in advance of any change in control). This limits the FMA's ability to scrutinise the impacts of a change in ownership of a licensed firm on consumers before it takes place, which is significant since a change in control can affect the treatment of customers and consumer outcomes.

We proposed three options in relation to change in control: continue with the status quo (Option 1), introduce this requirement and apply it to CoFI regulated entities only (Option 2), and introduce this requirement and apply it to all entities licensed under Part 6 of the FMC Act (Option 3).

Stakeholders were split between all three options. Our analysis supports Option 3 as the most likely to meet the objectives of the review. Introducing this requirement and applying it to all entities licensed under Part 6 (Option 3) is therefore the preferred option.

2. On-site inspection powers

A core part of the FMA's role is monitoring compliance with financial markets legislation, but the FMA does not currently have powers to conduct on-site inspections without prior notice except for Anti-Money Laundering and Countering Financing of Terrorism Act 2009 purposes. This does not align with international expectations and good practice and limits the FMA's ability to assess compliance relating to conduct.

We proposed two options in relation to on-site inspections: continuing with the status quo (Option 1) or amending legislation to ensure the FMA has a without-notice inspection power (Option 2).

Stakeholders were split on which option was preferred. Our analysis found Option 2 would be the mostly likely to meet the objectives of the review. Amending legislation to introduce such a power (Option 2) is therefore the preferred option.

3. Introducing expert report powers

While this was consulted on in the discussion document, and officials do see potential merit in this power, the Minister of Commerce and Consumer Affairs decided not to progress this at this time and no further analysis has been conducted at this point.

Limitations and Constraints on Analysis
The scope of the options considered in this document reflects the Minister of Commerce and Consumer Affairs' objectives in relation to financial services reform: to simplify and streamline regulation of financial services, to reduce undue compliance costs for financial markets participants, and to improve outcomes for consumers. The Minister of Commerce and Consumer Affairs met with several industry representatives and stakeholders to discuss their views as part of the development of options for consultation. Officials also consulted with the FMA, RBNZ, the Treasury and the Commerce Commission at this stage. A discussion document was prepared in a short timeframe and consulted on over a period of four weeks. We received 37 submissions from a range of stakeholders including industry organisations, financial markets participants, consumer representatives and law firms. Additional time for consultation could have enabled higher quality responses, but we are satisfied that a wide range of stakeholder views have been heard. Further public input will be possible through the select committee process. In relation to specific proposals covered in the discussion document: • There is limited evidence to support the changes proposed to the Conduct of Financial Institutions (CoFI) regime, as the regime has not yet come into force. However, public consultation on the discussion document means that we have heard from institutions who have started or completed development of their fair conduct programmes under the regime and who now have a good idea of what the practical impacts of the regime are likely to be. • In relation to the proposal for the FMA to issue a single licence covering different market services, the Minister of Commerce and Consumer Affairs expects that a single licence will be issued (which is possible under the existing legislative framework) and the FMA has advised it intends to proceed with this approach. The options considered in this document are therefore limited to whether the legislation should be amended to require the FMA to issue a single licence (ie make this approach mandatory) or whether the FMA should proceed with consolidation under the existing legislative framework. Therefore, it does not consider whether the status quo (under which the FMA issues separate licences for different market services) should be retained. • In relation to the proposal to enable the FMA to rely on work undertaken by the RBNZ, the discussion document invited submissions on amending prudential legislation to introduce an equivalent provision allowing the RBNZ to rely on an assessment by the FMA. While submitters were generally supportive of this option, amending prudential legislation is outside of the scope of this process, so work on this option will be progressed separately. • In relation to the proposals for ensuring the FMA has effective monitoring powers, the options considered in this document are whether to introduce change in control approval requirements and on-site inspection powers. The discussion document also invited submissions on introducing expert report powers. While officials see potential merit in the expert report option, the Minister of Commerce and Consumer Affairs decided not to progress it at this time. • Due to the limited time available for analysis, this Regulatory Impact Statement (RIS) does not address other issues relating to the CoFI Act raised by submitters (for

example the requirement for financial institutions to publish a consumer-facing summary of their fair conduct programmes).

Overall, Ministers can be reasonably confident when using this analysis to inform their decisions but will need to bear in mind the limited nature of the evidence on changes to the CoFI regime.

Responsible Manager(s) (completed by relevant manager)

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Financial Markets

Ministry of Business, Innovation and Employment

13 August 2024

Quality Assurance (completed by QA panel)

Reviewing Agency:	The Ministry of Business, Innovation and Employment's Regulatory Impact Assessment Review Panel
Panel Assessment & Comment:	The Ministry of Business, Innovation and Employment's Regulatory Impact Assessment Review Panel has reviewed the Fit for purpose financial services RIS and consider that it fully meets the quality assurance criteria. The panel was satisfied with the problem definition, options identified, analysis undertaken and the consultation process.

Section 1: Diagnosing the policy problem

1.1 What is the context within which action is proposed?

The Government has committed to reforming financial services regulation

1. During the 2023 General Election the National Party committed to reforming financial services regulation as part of its 100-point plan for rebuilding the economy. The Government has also committed to cut red tape and provide regulatory clarity to make it easier to invest and grow New Zealand's capital markets.
2. The Minister of Commerce and Consumer Affairs followed through on these commitments in 2024 by announcing a package of reforms which would alter the financial services regulatory landscape. The proposals in this paper are part of this package that were consulted on in May/June 2024, including:
   a. reforms to relevant legislation for transferring responsibility of the Credit Contracts and Consumer Finance Act 2003 (the CCCFA) to the Financial Markets Authority (FMA), broader reforms to the CCCFA, and high-cost credit provisions.
   b. how financial dispute resolution schemes could be improved to become more effective and accessible for consumers.
3. The intention of the reforms to conduct regulation, as well as to the financial services landscape more generally, are to simplify and streamline the obligations which are placed on businesses. The reforms to conduct regulation will be achieved through a mixture of changes to the Financial Markets (Conduct of Institutions) Amendment Act 2022 (CoFI Act), changes to other pieces of conduct legislation, and operational changes.

New Zealand's regulation of financial markets conduct has evolved over time

4. New Zealand's financial markets regulatory system has undergone an evolution over time in response to the evolving complexity of financial services, societal expectations, and international trends in regulatory practice. Following the Global Financial Crisis and the collapse of finance companies in the mid-2000s, New Zealand's historical product- and disclosure-focused model for securities regulation moved towards a broader focus on conduct in financial markets. This included a focus on outcomes for consumers of financial products and services (rather than just investors), and greater regulatory engagement and supervision (including through the use of licensing).
5. These changes reflected similar shifts internationally and led to the formation of the FMA in 2011 and passage of the Financial Markets Conduct Act 2013 (FMC Act) in 2013. Market conduct requirements have continued to develop since then, including a new financial advice regime and the CoFI Act that sit within the FMC Act framework.

The CoFI Act responds to findings of harm to consumers and fills a regulatory gap…

6. The CoFI Act was developed in response to reviews by the FMA and Reserve Bank of New Zealand (RBNZ) that found that New Zealand banks and insurers did not have robust systems and controls for managing conduct risks, which were affecting outcomes for consumers. They also found that these issues were the result of a regulatory gap that created the risk of ongoing, systemic harm.

7. In particular, the reviews found issues such as poor product design which did not consider the needs of consumers, sales incentives driving sales of unnecessary or inappropriate products, and poor administration or management of products leading to overcharging (eg continuing to charge customers for payment protection insurance after loans had been fully repaid). Financial institutions were asked through these reviews to identify and report on issues requiring remediation. To date, more than $170 million has been paid in remediation to New Zealand consumers (split across many small amounts).

… by introducing conduct regulation of retail banking and insurance services

8. The CoFI (Conduct of Financial Institutions) regime will require financial institutions (ie banks, insurers and non-bank deposit takers (NBDTs)) to comply with conduct obligations for the provision of core retail banking and insurance products and services. Key elements of the regime include:

   a. The introduction of a '**fair conduct principle**' requiring that financial institutions must treat consumers fairly. This effectively means that financial institutions must act responsibly at all times in their design, distribution and ongoing provision of products and services.

   b. A requirement for financial institutions to establish appropriate systems and processes within their businesses (called '**fair conduct programmes**') to ensure they meet the fair conduct principle.

   c. A prohibition on financial institutions and intermediaries from providing sales incentives based on volume or value targets.

   d. A requirement for financial institutions to obtain a conduct licence from the FMA. Licensing enables the FMA to work with financial institutions to ensure they meet the regulatory standards, and to exercise risk-based supervisory tools and enforcement powers.

9. The CoFI regime was designed as principles-based legislation with proportionate and non-prescriptive requirements. The intention was to avoid a rules- or compliance-based regime. The FMA has signalled its intention to take a risk-based approach to licensing and an outcomes-focused approach to ongoing supervision of financial institutions.

10. The CoFI Act is due to come into force on 31 March 2025.

New Zealand's financial markets are regulated under a 'twin peaks' model, with the FMA responsible for conduct regulation

11. New Zealand has a "twin peaks" model of financial markets regulation. The RBNZ is the <u>prudential</u> regulator responsible for the soundness and stability of regulated financial institutions and the broader financial system. The FMA is the <u>conduct</u> regulator responsible for the conduct of market participants.

12. These proposals are about changes to regulation of financial markets <u>conduct</u>. Regulation in this area focuses on behaviours in financial markets. It aims to ensure that consumers are adequately informed and treated fairly, and that regulated entities act with integrity. Conduct regulation promotes confident and informed participation in financial markets by businesses, investors, and consumers.

13. The proposals in this paper will impact a range of financial markets participants:

a. <u>CoFI Act and reliance proposals:</u> The proposals in this paper relating to the CoFI Act (Sections 2A and 2B below) and the FMA's ability to rely on work by the RBNZ (Section 2D below) will impact banks, insurers and NBDTs that provide products and services to consumers (together, **financial institutions**). These entities are subject to licensing and supervision requirements set by both the RBNZ and the FMA. There are approximately 80 financial institutions expected to apply for a licence (around 50 insurers and around 30 banks and NBDTs).

b. <u>Single conduct licence and change in control approval requirements</u>: The proposals in this paper relating to a single conduct licence (Section 2C below) and the introduction of a change in control approval requirement (Section 2E below) will impact all financial service providers who hold a licence from the FMA. Financial service providers are licensed by the FMA to provide certain kinds of market services under Part 6 of the FMC Act. Licensing provides the FMA, as regulator, with a range of tools to enable it to assess, monitor and enforce compliance with obligations, both at the licence application stage and on an ongoing basis. Licences are currently required to be held where the provider is:

   i. acting as a manager of a registered scheme (other than a restricted scheme)

   ii. acting as an independent trustee of a restricted scheme

   iii. acting as a provider of a financial advice service

   iv. acting as a provider of a discretionary investment management service

   v. acting as a derivatives issuer in respect of a regulated offer of derivatives that is made by the derivatives issuer, or

   vi. acting as a financial institution (from 31 March 2025, introduced by the CoFI Act).

c. There are also two opt-in licences for prescribed intermediary services (crowd funding services and peer-to-peer lending services) and financial benchmark administration.

d. Of the approximately 80 financial institutions, approximately 30 are expected to hold more than one conduct licence. Approximately 1,650 financial service providers hold licences only from the FMA; of these firms, fewer than 50 hold two or more licences.

e. <u>On-site inspection power:</u> The proposal relating to an on-site inspection power (Section 2F below) will impact all financial markets participants to an extent (which includes over 14,000 financial service providers), noting that the power is expected to be used in very limited circumstances.

1.2 How is the status quo expected to develop if no action is taken?

14. The Government has committed to reforms now because of concerns that the succession of new rules and requirements over the past decade has become increasingly complex, led to a duplication of the roles of the RBNZ and the FMA, and unnecessary compliance burden for businesses. Without action, the Government considers that regulation will continue to be complex and duplicative, placing a disproportionate compliance cost and burden on businesses.

1.3 What is the policy problem or opportunity?

Financial markets conduct regulation is aimed at improving the conduct of financial markets participants. However, multiple reforms over the past decade has led to an overly complex regulatory landscape and unnecessary compliance costs. Problems within the regime include:

Requirements in the CoFI Act

a. The introduction of the CoFI Act in 2022, due to come into force on 31 March 2025, has added additional regulatory burden for financial institutions by requiring them to develop fair conduct programmes and apply for a separate conduct licence. Most stakeholders agree that the overall intent and framework of the CoFI Act is sound. However, some requirements may be overly prescriptive, cause unnecessary duplication with other regimes, or limit flexibility for firms, leading to unnecessary compliance costs.

Siloed approach to licensing

b. The FMC Act currently permits a siloed approach to licensing that may impose unnecessary costs on some market service providers. The Minister of Commerce and Consumer Affairs has set an expectation that the FMA shift to a single conduct licence. This shift could occur without legislative change to the FMC Act, however under current provisions there would be challenges for the FMA in implementing the change operationally (eg to consolidate existing licences held by each firm would likely require each firm's consent).

Overlap in twin peaks

c. As noted above, the RBNZ and FMA both have roles and responsibilities in relation to regulation in financial markets. For example, RBNZ and FMA may both have interests in the governance activities of firms from independent prudential and conduct perspectives. In some cases firms are subject to similar or overlapping requirements from both regulators which could give rise to unnecessary compliance costs.

FMA lacks certain powers

d. The FMA also lacks tools to act proactively in some areas of conduct regulation, such as change in control approvals and on-site inspections, which limits its ability to effectively regulate market conduct. The FMA's ability to be an effective and proactive conduct regulator is becoming more important, particularly as the FMA takes on new areas of regulation of consumer credit lenders under CCCFA (which is being progressed separately).

1.4 What objectives are sought in relation to the policy problem?

15. The objectives of the Government's reform of the financial services regulatory landscape are to:

    a. simplify and streamline regulation of financial services (including reducing duplication),

    b. remove undue compliance costs for financial markets participants, and

    c. improve outcomes for consumers.

16. These objectives apply to the proposals discussed in this document. Some trade-offs exist between the different objectives. These objectives must be balanced against one another. For example, simplifying regulation could reduce obligations on market participants but make the obligations that remain less clear or certain and therefore increase compliance costs. As another example, increasing complexity might result in more protections for consumers, but result in requirements which are not proportionate to the risks of harm.

1.5 What criteria will be used to compare options to the status quo?

17. To assess all the options in this Regulatory Impact Statement (RIS) against the status quo, we have used three criteria which reflect the policy objectives:

    a. **Promotes the fair treatment of consumers through fair conduct** – whether options promote fair treatment of customers by encouraging fair conduct by financial service providers.

    b. **Minimises the regulatory burden on firms** – whether the options avoid unnecessary compliance costs and regulatory burden being placed on firms, including by:

        i. improving the flexibility of the requirements such that they can be tailored to account for the size and nature of different businesses.

        ii. ensuring that what is required from financial service providers is clear and certain.

    c. **Promotes fair, efficient, and transparent financial markets** – whether the options promote fair (including competitive neutrality), efficient (including avoiding duplication with other regulation) and transparent financial markets.

18. These criteria reflect those used in the discussion document 'Fit for purpose financial services conduct regulation', but with amendments to reflect consultation feedback.

19. We have decided to weight these criteria equally. Criterion **a** reflects the primary purpose of the CoFI Act, while criterion **b** reflects the Government's main motivation for these reforms. Criterion **c** reflects the Government's vision for financial markets generally; this legislation and reform are both aimed at working toward this outcome.

20. As with the objectives, there are trade-offs between the criteria. If regulatory burden on firms is reduced by removing requirements from the legislation, then there may be risks to fair treatment of consumers.

1.6 What scope will options be considered within?

21. The scope of the options considered in this document reflects the Government's objectives in relation to financial services reform: to simplify and streamline regulation of financial services, to reduce undue compliance costs for financial markets participants and to improve outcomes for consumers.

22. The Government's primary objective in relation to the CoFI Act is to simplify and streamline the regime. As a result, this RIS only considers options that align with this objective and does not explore options that would rework or overhaul fundamental features of the CoFI regime. We also note that the regime has not yet come into force and will be subject to a statutory review five years after its commencement, which would provide an opportunity to consider fundamental changes if needed.

23. In relation to the proposal for the FMA to issue a single licence covering different market services, the Minister of Commerce and Consumer Affairs expects that a single licence will be issued (which is possible under the existing legislative framework) and the FMA has advised it intends to proceed with this approach. The options considered in this document are therefore limited to whether the legislation should be amended to require the FMA to issue a single licence (ie make this approach mandatory) or whether the FMA should proceed with consolidation under the existing legislative framework. Therefore, it does not consider whether the status quo (under which the FMA issues separate licences for different market services) should be retained.

24. Time constraints have limited MBIE’s ability to analyse submissions received on the discussion document. This means that this RIS does not address some other issues relating to the CoFI Act raised by submitters (eg the requirement for financial institutions to publish a consumer-facing summary of their fair conduct programmes).

Section 2, Part A: Options analysis – Fair conduct principle in the CoFI Act

2A.1 What is the context?

25. The CoFI Act sets an overarching fair conduct principle (section 446C) that financial institutions must treat consumers fairly.

Current drafting of section 446C ('what is the fair conduct principle')

1) The fair conduct principle is that a financial institution must treat consumers fairly.
2) The requirement to treat consumers fairly includes—
   a) paying due regard to consumers' interests; and
   b) acting ethically, transparently, and in good faith; and
   c) assisting consumers to make informed decisions; and
   d) ensuring that the relevant services and associated products that the financial institution provides are likely to meet the requirements and objectives of likely consumers (when viewed as a group); and
   e) not subjecting consumers to unfair pressure or tactics or undue influence.
3) Subsection (2) does not limit subsection (1).

26. The fair conduct principle was designed to be a broad and relatively high standard of conduct that applies in a wide range of circumstances. It is not intended that legislation endorse a particular concept of fairness, because the concept of what is 'fair' can evolve over time as products and services, industry practices and societal norms change.

2A.2 What is the policy problem or opportunity?

27. A common criticism of principles-based requirements similar to the fair conduct principle (but with liability for failure to meet them) is that it is not sufficiently clear how firms can avoid liability for breaching them.

28. In relation to the fair conduct principle, financial institutions may be uncertain about what fair treatment of consumers covers and whether this could expose them to unexpected liability. For example, some financial institutions perceive there is a risk that when a conduct issue arises, the principle could subsequently be interpreted to include something that is not already on the current list and financial institutions may be held liable to that.

29. This uncertainty could lead to financial institutions being unnecessarily risk averse, and reducing the provision of financial products and services that might otherwise be appropriate or desirable. In addition, some in the industry are concerned that the open-endedness could result in the FMA providing further expectations via guidance, which may be viewed as mandatory. We note however, that most industry feedback received at this stage has been around the minimum requirements for fair conduct programmes set out in section 446J rather than the fair conduct principle.

2A.3 What options are being considered?

Option 1: Status quo (no change to the definition)

30. The fair conduct principle is open-ended and is not an enforceable duty itself but is a guiding principle or policy objective that informs the specific duties imposed by the regime. Financial institutions' fair conduct programmes must be designed to ensure

they comply with the fair conduct principle (section 446G), and financial institutions must then take all reasonable steps to comply with their fair conduct programmes (section 446I).

31. The open-ended approach to the principle is largely in line with other overseas jurisdictions. For example, in Australia, financial providers have a duty to deliver financial advice services “honestly, efficiently and fairly” and this duty is interpreted by the courts.

32. Financial institutions are not directly required to “treat consumers fairly” as specified in the principle. A court could therefore not hold a financial institution liable for not “treating consumers fairly” per se, but instead would consider whether:

    a. the institution has established an “effective” fair conduct programme – s446G(1) – to be considered in light of minimum requirements for fair conduct programmes in s446J, and in light of s446G(3) which requires the programme to be designed to ensure the institution complies with the fair conduct principle, and

    b. the institution has taken “all reasonable steps” to comply with their conduct programme – s446I(1).

33. The fair conduct programme requirements in the CoFI Act will provide financial institutions with a high degree of certainty about what they need to do to comply with the fair conduct principle.

Option 2: Make the fair conduct principle definition exhaustive

34. This option would mean amending the definition of the fair conduct principle to make the current list of matters exhaustive. The current list of matters would become a complete list of what treating consumers fairly means. It would mean that financial institutions only need to consider what is listed under the principle and design their conduct programmes in light of these standards.

Submitter views on Options 1 and 2

35. The majority of submitters (consumer advocacy groups, some financial services providers and the New Zealand Banking Association (NZBA)) supported the status quo to keep the list of matters open because it aligns best with the principles-based approach of CoFI.

36. On the other hand, a number of law firms, industry groups and one bank, supported making the list exhaustive because it provides greater certainty and avoids scope creep. Some were concerned that the open-endedness could mean that, after a conduct issue arises, the fair conduct principle could be interpreted to apply in circumstances the financial institution did not expect.

37. Some submitters suggested, if the list is made exhaustive, that a regulation-making power be added to provide the ability to prescribe further fair treatment considerations, to ensure that the concept of what is fair has some flexibility to respond to a changing environment. Our view is that, given the importance of the fair conduct principle as the overarching principle for the CoFI regime, any additions to the list of matters that the requirement to treat consumers fairly includes should be in primary legislation, rather than in regulations.

2A.4 How do the options compare to the counterfactual?

	Option 1 – *Counterfactual*	**Option 2 – Exhaustive definition**
Promotes the fair treatment of consumers through fair conduct	Allows for a broad interpretation of fair treatment of customers to evolve over time as products and services, industry practices and societal norms change. **0**	An exhaustive list could restrict consideration of other factors that might be relevant to fair treatment over time and may unintentionally exclude circumstances that should be covered. **-**
Minimises the burden on financial institutions	Is flexible to evolve over time as products and services, industry practices and societal norms change. Minor risk of institutions being unnecessarily risk averse and incurring higher compliance costs as a result. **0**	The requirement is not to comply with the fair conduct principle but to comply with an effective fair conduct programme, accordingly this option is not expected to have more than marginal impacts on compliance costs. **0**
Promotes fair, efficient, and transparent financial markets	Promotes fair markets, minimal transparency and efficiency impacts. **0**	Minimal fairness, transparency and efficiency impacts. **0**
Overall assessment	**0**	**-**

2A.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

38. The fair conduct principle is a principles-based concept that is not intended to be bound and limited to a prescribed list of factors. While this could result in less certainty regarding liability, the CoFI Act addresses this concern by structuring the requirements so that the principle is not an enforceable duty in itself. Instead, the statutory duties are to establish, implement and maintain fair conduct programmes (tailored to their businesses, products and customers) and to comply with these. Financial institutions need to consider what fair treatment means for their customers and products, rather than applying standardised rules prescribed in legislation that may not fit well to their customers and products.

39. Our view is that Option 1 (the status quo) strikes an appropriate balance between flexibility and certainty by:

    a. stating exhaustively when the fair conduct principle applies (s446D); and

    b. stating what the minimum requirements of a fair conduct programme are (s446J).

40. Therefore, we recommend maintaining the status quo with an open-ended fair conduct principle as this best meets the objectives. To the extent that there is any uncertainty around what financial institutions need to do to comply with the fair conduct principle, this could be addressed through adjusting the minimum requirements for fair conduct programmes in s 446J.

2A.6 What are the marginal costs and benefits of the option?

41. There are no marginal costs and benefits of this option as we are recommending maintaining the status quo.

Section 2, Part B: Options analysis – Minimum requirements for CoFI Act fair conduct programmes

2B.1 What is the context?

42. The CoFI Act requires financial institutions to establish, implement and maintain a fair conduct programme (section 446G) and comply with it (section 446I). Fair conduct programmes are policies, processes, systems and controls that are designed to ensure the financial institution complies with the fair conduct principle.

43. Section 446J sets a non-exhaustive list of requirements that must be met in relation to fair conduct programmes. These are only minimum requirements, and the overall standard is that a financial institution's fair conduct programme must be designed to ensure the financial institution's compliance with the fair conduct principle. The minimum requirements were based on areas where conduct issues and risks were identified through the FMA and RBNZ conduct and culture reviews, and other evidence of consumer harm.

44. The section has two main parts. Section 446J(1) sets out the minimum areas the programme must cover, while section 446J(2) sets out the factors a financial institution must consider when creating its fair conduct programme, for example, the nature, size and complexity of its business.

45. There are regulation-making powers allowing additional requirements to be prescribed for the purposes of sections 446J(1) and (2). No regulations in relation to fair conduct programmes have been made or are proposed at this stage.

2B.2 What is the policy problem or opportunity?

46. We have heard from stakeholders that some of the minimum requirements in section 446J(1) are too prescriptive. Stakeholders say that these requirements are overly specific and may not be necessary or appropriate for all fair conduct programmes, depending on the nature of the business conducted by the financial institution. They consider some of the requirements may create unnecessary or undesirable overlap with other regulatory regimes.

47. We consider overly prescriptive requirements could create unnecessary compliance costs and limit flexibility in how financial institutions design and maintain fair conduct programmes within their businesses. This could result in reduced provision of products and services, or additional costs being passed along to consumers.

48. We have also heard concerns that section 446J may not directly require financial institutions to include consideration of the transparency of fees and charges, as well as recording and resolving consumer complaints, as part of their fair conduct programmes.

49. Reviewing the minimum requirements is an opportunity to ensure minimum requirements set an appropriate baseline for all fair conduct programmes. The intent is to support programmes being designed to ensure fair treatment of consumers while reducing unnecessary costs for financial institutions and offering them a real scope to tailor their programmes to their businesses.

2B.3 What options are being considered?

Option 1: Status quo (retain existing minimum requirements without change)

Description of Option 1 (status quo)

50. If no changes are made, fair conduct programmes will need to comply with the current list of minimum requirements outlined in section 446J(1) (see context section above). This set of minimum requirements is more extensive and prescriptive than Options 2 (removing/adjusting some minimum requirements) and 4 (removing all minimum requirements) below. This means that, over time, financial institutions might find the current approach creates more compliance burden than those other options.

51. The existing requirements would provide clear guidelines for what must be included in a fair conduct programme, which could create certainty for businesses, and ensure a greater level of consistency across all fair conduct programmes. The level of detail required by the counterfactual compared to options 2 and 4 could also mean fair conduct programmes are more comprehensive and better address fair conduct risks.

52. However, we have heard from stakeholders that the requirements could result in duplication for some financial institutions, and could also leave less leeway for financial institutions to tailor their programme to their business. This might mean some institutions are forced to include information which would otherwise be considered irrelevant.

53. We understand that many financial institutions are already well-progressed in preparing for the introduction of the CoFI regime. This includes developing their fair conduct programmes, and applying for, or preparing to apply for, a CoFI licence, in advance of the regime's commencement date and based on current legislative requirements. Keeping the status quo would mean financial institutions would not have to bear the additional cost and administrative burden of adjusting their fair conduct programmes to meet new or altered requirements at this late stage.

Submitter views on Option 1 (status quo)

54. Most submitters did not favour keeping the status quo, but those who were in favour (5 of 25) expressed their opinions strongly. All consumer and social advocacy groups favoured at least retaining the status quo (with two submitters preferring the status quo be kept as well as proposing the adoption of Option 3, which would add additional requirements).

55. The reasons given for supporting the status quo included that removing or amending minimum requirements would make the requirements weaker and result in worse outcomes for consumers; financial institutions are already making progress toward their fair conduct programmes (and will have established and implemented these by the time any changes come into effect), so changing requirements at this late stage would only increase compliance burden; and the interests of consumers need to be weighted higher against the costs borne by financial institutions when making these decisions.

56. Those who opposed the status quo (because they preferred Option 2 or 4) argued it was unnecessarily prescriptive and that changes to the requirements could be made to reduce compliance costs without negatively impacting on outcomes for consumers.

Option 2: Remove or amend some minimum requirements for fair conduct programmes

Description of Option 2 (remove/amend)

57. One option is to remove or amend certain requirements in section 446J(1). The intent would be to reduce prescription and provide greater flexibility for financial institutions to comply with their obligations, while continuing to provide sufficient certainty and set clear standards of conduct that support fair treatment for consumers. The intent of this option is not to lower the expected standards of financial institutions' conduct but to remove certain elements that may be unnecessary, repetitive or overly prescriptive.

58. We expect this option would reduce prescription, provide for greater flexibility for financial institutions to comply with their obligations and reduce compliance costs (as compared to the status quo). It would do this while continuing to promote fair treatment of consumers by financial institutions.

59. It is important to note there is a risk that simplifying and reducing the specificity of fair conduct programme requirements could make it more difficult for financial institutions to understand what the content of their fair conduct programme should look like (particularly for smaller financial institutions). This means that simplifying the requirements could potentially increase compliance costs rather than reducing them.

60. We have provided more information below about what is proposed as part of Option 2, and consider that the proposals should mitigate these risks. The risk can also be further mitigated by the broad regulation-making power in the CoFI Act which allows further minimum requirements to be specified in regulations if needed. The FMA also has the ability to issue guidance to financial institutions to communicate expectations and highlight best practice, and will be engaging with industry to understand where guidance and support may be desirable.

61. The discussion document gave several examples of changes that could be made based off of previous stakeholder feedback (these are each discussed in further detail below). It also asked submitters to suggest any other changes they thought would improve the regime. The changes given as examples were:

    a. Deleting paragraph (a).

    b. Deleting subparagraphs (i) to (iii) from paragraph (c).

    c. Adjusting or consolidating paragraphs (e) to (h).

    d. Deleting paragraph (k).

Submitter views on Option 2 (remove/amend)

62. This option received the most support from submitters (17 of 25 preferred this approach over the others), with almost all financial institutions and industry groups in favour. Those who expressed support broadly agreed these changes would reduce the compliance burden on financial institutions, improve flexibility, and have little to no effect on outcomes for consumers. Those against this option argued either that these changes would have no meaningful effect on the compliance burden faced by financial institutions, or that it would have a negative effect on consumer outcomes.

What requirements would be removed or amended under Option 2?

63. In the discussion document we listed some examples of changes that could be made to the paragraphs of section 446J(1) under this option, and sought further suggestions and feedback from submitters. We now propose, as part of this option, to make changes to paragraphs (a), (e)-(h) and (k) as set out below.

Current drafting of section 446J(1)(a)

1) The fair conduct programme must be in writing and include effective policies, processes, systems, and controls for—
   a) enabling the financial institution to meet all of its legal obligations to consumers, including under this Act, the Fair Trading Act 1986, the Credit Contracts and Consumer Finance Act 2003, the Consumer Guarantees Act 1993, and the Financial Service Providers (Registration and Dispute Resolution) Act 2008;

64. **We propose to delete paragraph (a).** We understand paragraph (a) has caused some confusion as to its intended scope and effect and has been perceived as introducing unnecessary duplication. Some financial institutions have interpreted it as requiring them to “re-document” processes in other parts of their business (eg their CCCFA processes) into their new fair conduct programme. We proposed this change in the discussion document and its deletion was strongly supported by most submitters who commented on this option for these reasons.

65. We consider removing this paragraph should allow financial institutions to take a more flexible and proportionate approach to areas of their businesses that are subject to requirements under more than one legislative regime.

Current drafting of section 446J(1)(e) to (h)

e) requiring the financial institution's employees and agents to follow the procedures or processes that are necessary or desirable to support the financial institution's compliance with the fair conduct principle; and

f) requiring initial and regular ongoing training for each of those employees on the following matters to the extent that the training is relevant to their work in providing the financial institution's relevant services or associated products to consumers:

   i) the relevant services or associated products in respect of which the employee carries out work; and

   ii) the fair conduct programme and the procedures or processes referred to in paragraph (e) that the employee must follow; and

g) checking that each of those employees has completed that training and has a reasonable understanding of the matters that have been covered by that training; and

h) managing or supervising each of those employees to ensure that they are supporting the financial institution's compliance with the fair conduct principle, and monitoring whether those persons are giving that support, including by—

   i) obtaining reasonable assurance that each employee is competent to carry out the range of work for which they will be, or are, employed (in relation to the financial institution's relevant services or associated products); and

   ii) setting conduct expectations for those persons; and

   iii) establishing robust and transparent procedures or processes for dealing with misconduct by those persons; and

   iv) monitoring whether consumers have been treated by those persons in a manner that is consistent with the fair conduct principle;

66. **We propose to adjust/consolidate paragraphs (e) to (h)*.*** In the discussion document we outlined a few different options for how paragraphs (e) to (h) could be improved, including removing employee requirements but keeping agency requirements, consolidating all the requirements into one broader and higher-level requirements, and simplifying paragraphs (f) to (h). Submitters expressed a range of views, including alternative drafting approaches, but generally agreed that there is scope to adjust these requirements and remove duplication. Options include keeping paragraph (e) but deleting (f) through (h); keeping paragraph (e) only as it relates to agents and amending (f) to (h) to be higher level and less prescriptive; and replacing (f) to (h) with a broader over-arching requirement or some other approach.

67. From a policy perspective, we consider that the important thing is that the legislative requirements cover that employees need to receive adequate training, support and supervision to enable them to support the financial institution's compliance with its fair conduct obligations and will seek to adjust these sections accordingly. This view was reflected in the suggestions made by submitters.

Current drafting of section 446J(1)(k)

c) ensuring that there are in place methods for regularly reviewing, and systematically identifying deficiencies in, the effectiveness of the programme;

68. **We propose to delete paragraph (k).** Section 446G(1) already requires that financial institutions "establish, implement <u>and maintain</u> effective fair conduct programmes". While paragraph (k) requires something slightly different (that financial institutions

include policies in their fair conduct programmes setting out how they will maintain them), we consider it may not be strictly necessary to include. This option was included in the discussion document. Most submitters did not express a view on this option, although those who did, generally agreed that it is not strictly necessary.

What requirements do we recommend keeping the same under Option 2?

69. We have considered some other requirements in section 446J(1) and whether these could be removed or amended. However, we have concluded that paragraphs (b), (c) and (j) should remain the same under Option 2.

Current drafting of section 446J(1)(b)

b) designing, and managing the provision of, the financial institution's relevant services and associated products to consumers, including by—
   i) providing for the methods by which the relevant services and associated products are provided to consumers (distribution methods) to operate in a manner that is consistent with the fair conduct principle; and
   ii) regularly reviewing whether the distribution methods are operating in a manner that is consistent with the fair conduct principle; and
   iii) ensuring that any deficiencies identified under subparagraph (ii) are remedied within a reasonable time; and
   iv) regularly reviewing the relevant services or associated products that are provided to consumers on an ongoing basis to determine whether they are likely to continue to meet the requirements and objectives of those consumers (when viewed as a group); and
   v) regularly reviewing whether enhancements or improvements in the financial institution's relevant services or associated products should be made available to those consumers (when viewed as a group); and
   vi) ensuring that any enhancements or improvements identified under subparagraph (v) are made available within a reasonable time

70. One submitter on the discussion document said that the requirements relating to designing, distributing and providing products and services are unduly restrictive and limit the ability of financial institutions to provide these to certain consumers. There was no proposed change to this particular requirement in the discussion document.

71. We do not agree with this view; the requirements in paragraph (b) are high-level. It includes a requirement for fair conduct programmes to include processes for reviewing whether products and services are likely to meet the requirements and objectives of consumers, when viewed as a group, but it is for financial institutions to assess how best to do this based on their own business. There is no requirement for the FMA to be involved in determining which products and services are suitable for different consumers.

Current drafting of section 446J(1)(c)

c) identifying, monitoring, and managing risks associated with conduct that fails to comply with the fair conduct principle, including—
   i) having clearly defined roles, responsibilities, and accountability arrangements in relation to identifying, monitoring, and managing those risks; and
   ii) requiring records to be maintained that are sufficient to allow an assessment to be made of the financial institution's performance in complying with the fair conduct principle; and
   iii) requiring regular and comprehensive reporting about those risks, and about failures to comply with the fair conduct principle, to the board or other governing body of the financial institution

72. As part of the discussion document, we proposed deleting sub-paragraphs (i) to (iii) from paragraph (c) on the basis these subparagraphs may be too prescriptive. We thought removing them could increase financial institutions' flexibility for identifying, monitoring and managing risks, although we still expected that in most circumstances equivalent requirements would be needed in fair conduct programmes.

73. Submitters expressed differing views on this suggestion. Some considered they should be removed as it would allow for more flexibility and align better with the principles-based approach of the regime. Others argued that, since in most circumstances equivalent requirements will still be needed, it would be better to keep the obligations in legislation for the sake of clarity. Some argued the requirements were necessary and should not be removed for that reason. There was no clear consensus of stakeholder opinion on this option.

74. We agreed with submitters who said these issues would most likely need to be considered in all fair conduct programmes regardless of whether this requirement was included or not, and without strong support for removing these sub-paragraphs, we opted to retain them on the basis they should provide certainty and clarity without placing any additional burden on financial institutions.

Current drafting of section 446J(1)(j)

j) communicating with consumers about the financial institution's relevant services or associated products in a timely, clear, concise, and effective manner;

75. A small number of submitters raised that they did not understand how the obligation in section 446J(1)(j) was intended to work in practice and said that this paragraph needed to be removed or amended.

76. In our view, providing further detail in the legislation is unlikely to meet the objectives of this review, as it would likely reduce flexibility for financial institutions; however, the FMA could potentially provide guidance about its expectations (either generally, in particular contexts, or to individual financial institutions on enquiry) if there is any uncertainty.

Option 3: Add new minimum requirements relating to fees and charges and consumer complaints

Description of Option 3 (fees/charges and complaints)

77. This option would involve adding new minimum requirements to section 446J(1) relating to:

    a. applying, disclosing and reviewing fees and charges, and/or

    b. recording and resolving consumer complaints.

78. Both or either of the proposed additions could be implemented together with Option 2 (removing or adjusting some minimum requirements) or Option 1 (the status quo, keeping other minimum requirements the same), but not with Option 4 (removing all minimum requirements).

79. The two potential additions would address areas where conduct risks have been known to arise. In relation to fees and charges, the FMA and RBNZ conduct and culture reviews found instances of fees and charges materially outweighing benefits to customers, incorrect application of fees and charges, and fees and charges being incorrectly disclosed to consumers. In relation to complaints processes, the reviews found instances of poor processes for recording and resolving consumer complaints.

80. The Minister of Commerce and Consumer Affairs has also stated his expectation that fair conduct programmes should address these areas.

81. Section 446J(1) does not currently expressly address these matters, so it may not currently be clear as to how and to what extent financial institutions should address these matters in their fair conduct programmes. However, both matters are arguably already within the broad scope of the fair conduct programme duty (section 446G) and are unlikely not to be addressed in financial institutions' programmes (even without express reference). We note:

    a. In relation to fees, the basis for the relationship between financial institution and customer is the exchange of money for products and services. The fair conduct principle provides that the requirement to treat consumers fairly includes paying due regard to consumers' interests. We expect this would include considering how fees and charges will be correctly applied and disclosed to consumers. In relation to intermediaries, there is also an express requirement in section 446J(1)(i) to address the design and management of incentives.

    b. In relation to complaints processes, paragraphs (c) and (d) of section 446J(1) set requirements around identifying and addressing conduct that may not comply with the fair conduct principle. Complaints are also expressly addressed in section 446D (which gives responding to a complaint as an example of when the fair conduct principle applies) and the duty in section 446H to ensure that information is available to assist consumers to understand how to make complaints.

82. From the date these changes take effect, this option would result in more fair conduct programmes explicitly addressing these matters (as compared to under the status quo). This does not necessarily mean outcomes for consumers will be markedly different though, as it is highly likely these issues would be considered and addressed in conduct programmes under the status quo already. This option may result in higher compliance costs for businesses, as including explicit requirements may reduce flexibility for how these matters can be addressed, but any increase in cost is not likely to be large.

Submitter views on Option 3 (fees/charges and complaints)

83. Some stakeholders (consumer and social advocacy groups) supported including these requirements on the basis that they could improve outcomes for consumers without necessarily negatively impacting on financial institutions. However, adding specific references to these matters could reduce flexibility in how financial institutions can address them, and result in financial institutions needing to review and amend their fair conduct programmes. This may result in an increase in compliance costs, without necessarily advancing the key objectives of the CoFI regime. Industry stakeholders who commented on this option agreed that costs would be increased and disagreed that there would be improved outcomes for consumers.

84. Industry stakeholders also highlighted in their submissions on the discussion document that similar obligations already exist elsewhere. For example, dispute resolution schemes' rules and regulations set requirements for financial institutions' complaints processes, and the Financial Markets Conduct Regulations 2014 (FMC Regulations) set requirements for financial institutions that are financial advice providers to disclose to consumers how to make a complaint, an overview of the complaints process, and an explanation of the external dispute resolution process.

Option 4 – Remove all minimum requirements for fair conduct programmes

Description of Option 4 (remove all requirements)

85. One option to address stakeholder concerns would be to remove all of the minimum requirements in section 446J(1). A financial institution would still be required to have a fair conduct programme including policies, processes, systems and controls designed to ensure the financial institution's compliance with the fair conduct principle, but there would be no minimum requirements set by legislation.

86. This option would maximise flexibility for financial institutions in determining how to establish, implement and maintain effective fair conduct programmes. It would also enable them to make their own decisions about what is necessary to include in the programme to meet the fair conduct principle in a manner that is appropriate for their own business. If any issues arise in the future, further requirements could be introduced through regulations.

87. However, this option would likely decrease clarity and increase uncertainty, which may particularly impact smaller financial institutions. Financial institutions may find it difficult to create their programmes without guidance in the legislation about what it is expected to include. This is why the minimum requirements in section 446J were originally inserted as a result of select committee. This option may therefore increase compliance costs rather than reduce them.

88. This option is also less likely to support the core objective of the CoFI regime to ensure fair treatment of consumers. It could lead to more gaps in fair treatment of consumers as a result of the removal of minimum requirements as interpretations and standards vary between financial institutions and may relax over time.

89. To promote fair outcomes for consumers and the objectives of the CoFI regime, under this option the FMA in practice is likely to continue to expect that fair conduct programmes include certain elements. The FMA may issue guidance to help financial institutions understand expectations. However, from a transparency, certainty and accountability perspective, our view is that it is more appropriate that certainty about regulatory standards be provided through primary or secondary legislation, rather than by the FMA.

Submitter views on Option 4 (remove all requirements)

90. Only one submitter favoured this option. They argued this approach best reflected the principles-based nature of the regime, by allowing financial institutions to truly tailor their fair conduct programme to the nature of their business and consumers. They agreed with those who opposed this option that the FMA would be required to provide guidance under this approach, but argued this more flexible approach was preferred over rigid legislative requirements.

91. All of those opposed to this option (which included all consumer and social advocacy groups and almost all financial institutions and industry groups) considered removing all minimum requirements would likely lead to worse outcomes for consumers. Several financial institutions and industry groups also said that having some requirements helped to provide clarity and that removing all requirements would likely increase compliance burden as financial institutions struggled to understand what was required of them. Several submitters agreed with our concerns about it being more appropriate for certainty about regulatory standards to be provided by legislation rather than by the FMA.

2B.4 How do the options compare to the status quo/counterfactual?

	Option 1 – *Counterfactual*	Option 2 – *Remove/amend some minimum requirements*	Option 3 – *Add new minimum requirements around complaints and/or fees and charges*	Option 4 – *Remove all minimum requirements*
Promotes the fair treatment of consumers	Promotes the fair treatment of consumers by setting minimum requirements which fair conduct programmes must adhere to. **0**	Removing paragraph (a) is unlikely to have a deleterious effect on consumer treatment because the obligations referenced in this paragraph are addressed in other existing legislative regimes. Adjusting/consolidating paragraphs (e) to (h) means the requirements relating to agents and employees will be less specific. However, the general principle underlying all of these specific obligations (that a firm take steps to properly train, supervise and monitor their employees to ensure they support the firm's compliance with the fair conduct principle) will remain. Removing paragraph (k) means there will be no specific requirement that firms have an explicit process for reviewing and renewing their fair conduct programmes. However, we consider the risk introduced by this removal is low because of the obligation elsewhere that firms "maintain" their programme (which would naturally involve periodically reviewing and renewing the programme). **0**	An explicit requirement that fair conduct programmes include these matters would theoretically create slightly stronger protections for consumers. However, any benefits are likely to be small or marginal given that these matters are already likely to be covered in fair conduct programmes. **+**	Removing all minimum requirements does not promote the fair treatment of consumers. Without minimum requirements setting out key areas that must be covered by a fair conduct programme it is likely some firms will fail to consider particular issues. However, there would still be a general requirement to ensure the firm's fair conduct programme supports fair treatment. **-**

	Option 1 – *Counterfactual*	Option 2 – *Remove/amend some minimum requirements*	Option 3 – *Add new minimum requirements around complaints and/or fees and charges*	Option 4 – *Remove all minimum requirements*
Minimising regulatory burden on firms	The current set of requirements is detailed, specific, and provides firms with information about what areas their fair conduct programmes need to address. **0**	This option is expected to provide financial institutions with more flexibility when designing and maintaining their fair conduct programmes. It will also reduce duplication of effort. We expect this will lower the regulatory burden as compared to the status quo. **+**	While these requirements are already likely to be covered in fair conduct programmes, adding explicit requirements to legislation may reduce flexibility in how firms can address these matters in their fair conduct programmes, and therefore increase compliance costs (although the impact is likely to be small). **-**	Removing all minimum requirements will allow for significant flexibility in designing programmes. However, the radically open-ended nature of this approach could create compliance costs – stakeholders have consistently told us that having no guidance at all can often create work in order to understand exactly what is required. **0**
Promoting fair, efficient, and transparent financial markets	The current set of minimum requirements should promote fair, efficient and transparent financial markets. **0**	Removing or amending the minimum requirements as above would likely reduce compliance costs for businesses, whilst still preserving most if not all the benefits of the current approach for consumers. **+**	This requirement would likely have little to no effect on the overall efficiency, fairness and transparency of the market, as any benefits or disadvantages are unlikely to be large enough to be noticed. **0**	Could reduce compliance costs, but the open-ended nature of this approach could also create some compliance burden for financial institutions. Also likely to result in lower transparency and may impact fair treatment of consumers. **-**
Overall assessment	**0**	**++**	**0**	**- -**

2B.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

92. Option 2 (remove some minimum requirements and amend others) is most likely to best address the problem, meet the policy objectives, and deliver the highest net benefits. As discussed above, this option will make obligations more proportionate and promote fair, efficient, and transparent markets without necessarily impacting on the fair treatment of consumers.

93. We have assessed Option 3 (add new minimum requirements around complaints and/or fees and charges) as having a neutral impact overall. We understand the Minister of Commerce and Consumer Affairs supports this option in addition to Option 2.

2B.6 What are the marginal costs and benefits of the option?

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Financial institutions	Many financial institutions have already begun developing their fair conduct programmes in preparation for licensing. These financial institutions may incur one-off compliance costs from reviewing and, if necessary, adjusting, their fair conduct programmes to respond to the changes to fair conduct programme requirements. Non-monetised impacts are likely to be low. However, it will depend largely on the business itself and how the changes will be implemented.	Low	Low
Intermediaries, agents and affected 3rd parties	There is likely to be no additional cost for these parties. None of the changes we are proposing will directly impact on obligations relating to these parties, as the CoFI Act does not impose any direct requirements on them and the proposed changes do not relate to distribution requirements.	None expected	Medium
Regulators	The FMA will need to reconsider its licensing processes, systems, materials, guidance and approach in light of the changes being made to the requirements, which will incur a cost. The FMA will need to engage with financial institutions to assist them to understand and prepare for the changes to requirements. We have had discussions with the FMA on these points, but the true cost of this change will be difficult to know until implementation has begun.	Low	Medium
Consumers	There is likely to be no cost for consumers. We are confident the changes proposed will not impact the current duties financial institutions have toward their customers, and we know none of the changes we are making will directly impact on consumers either. There may be	None expected	Medium

Affected groups	Comment	Impact	Evidence Certainty
	indirect or unintended costs but it is difficult to gauge them prior to implementation.		
Total monetised costs	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown
Non-monetised costs	We expect there to be some cost incurred as financial institutions may need to adjust fair conduct programmes they have already put in place in preparation for obtaining their licences. The FMA will have to spend time and money updating its licensing processes, systems, materials, guidance and approach and engaging with financial institutions in relation to the changes in obligations. We are aware of the factors which are likely to drive up costs for the parties involved, but the exact costs involved in the change will only be able to be ascertained once implementation has begun.	Low	Medium
Additional benefits of the preferred option compared to taking no action			
Financial institutions	Financial institutions will have more flexibility in maintaining their fair conduct programmes. We know from these stakeholders that they believe more flexibility will decrease their ongoing compliance costs (albeit not significantly given the nature of the changes proposed). Whether or not this happens in practice will depend largely on implementation.	Low	Medium
Intermediaries, agents and affected 3rd parties	We expect this option to have no direct effect on these parties.	None expected	Medium
Regulators	There are unlikely to be any tangible benefits of this option for the FMA.	None expected	Medium
Consumers	We know none of the changes we are making directly impact on consumers. Making the obligations more flexible could theoretically benefit consumers by reducing the costs financial institutions incur (which are often pushed onto consumers), but this relationship is very indirect and difficult to prove. It could also theoretically disadvantage consumers if removing or amending some requirements has a negative impact on fair treatment; although we note the overarching duties remain the same.	Low	Low
Total monetised benefits	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown

Affected groups	Comment	Impact	Evidence Certainty
Non-monetised benefits	We expect the main non-monetised benefit to be reduced compliance burden over the long-term.	Low	Medium

Section 2, Part C: Options analysis – Single conduct licence covering one or more market services

2C.1. What is the context?

94. As noted above at paragraph 13(b), Part 6 of the FMC Act requires providers of certain market services to be licensed by the FMA. This covers a broader population of financial market participants than financial institutions.

95. Under the FMC Act, the FMA may issue different licences for each type of market service, or alternatively may issue a single licence covering more than one type of market service. Currently, the FMA chooses to issue different licences for each type of market service. This means that some licensed firms will hold more than one conduct licence, where they are approved to provide more than one licensed market service.

96. While most firms rarely hold more than one licence, we are aware that some stakeholders have raised concerns about the cost of needing to make multiple licence applications, as well as overlaps and misalignment in requirements under separate licences such as standard conditions and regulatory returns.

97. The Minister of Commerce and Consumer Affairs has set an expectation that a single licence will be issued by the FMA, and the FMA has indicated that it intends to proceed with this approach. This means that the status quo, under which the FMA issues separate licences for different types of market services, is not being considered as an option.

2C.2. What is the policy problem or opportunity?

98. The FMC Act currently permits a siloed approach to licensing that may impose unnecessary costs on some market service providers. A shift to a single licence as per the Minister of Commerce and Consumer Affairs' expectations, could occur without legislative change to the FMC Act, however under current provisions there would be challenges for the FMA in implementing the change operationally (eg to consolidate existing licences held by each firm would likely require each firm's consent).

2C.3. What options are being considered?

Option 1: Operational transition to a single licence (no legislative change)

99. Option 1 means that the current legislative framework for licensing would remain in place, but the FMA would transition operationally towards issuing single licences going forward (as permitted under the existing legislative framework).

100. For example, once FMA is operationally ready to do so, this would mean that going forward:

    a. If the FMA received an application from a new market participant to provide two types of market services, and the FMA approves this, it would issue a single licence covering the two types of market services, rather than issuing two separate licences.

    b. If the FMA received an application from an existing licensee to provide a new market service, and the FMA approves this, it could add this as an additional service to an existing license held by the firm.

101. In terms of implementation timing, we understand it would take the FMA some time to make the necessary operational changes to its licensing systems and materials to

move to a single licence approach, so the operational transition under Option 1 is unlikely to be materially different in terms of timeframes from Option 2 (legislative change).

102. A key issue with an operational transition is that it is not feasible under the existing legislative framework to consolidate the existing separate licences that are already held by a licensed firm into a single conduct licence. The existing provisions of the FMC Act do not provide the ability for FMA to undertake a mandatory consolidation of the licences already held by an existing firm. A non-mandatory consolidation by way of a variation or cancellation and replacement of the existing licences would be complex, is not clearly contemplated by the existing legislative provisions, and would rely on individual firms voluntarily requesting the change. This is not considered to be realistic or feasible in practice.

103. This means that Option 1 would in practice only achieve a single licence approach for new licences that are issued going forward, and would leave existing licensed firms continuing to hold separate licences. This would not address the policy problem of unnecessary compliance costs for those firms. It would also create greater complexity from having firms on two different licensing models, which runs contrary to the objective of simplifying and streamlining the approach to conduct licensing. While these matters fall outside the scope of this law reform process, we understand the FMA would also be considering operational changes to align with the single licence approach. For example, streamlining licence ‘standard’ conditions imposed by the FMA for different market services, and better harmonising annual regulatory returns requirements.

Option 2: Amend the FMC Act to require the FMA to issue a single licence covering different types of market services

104. This option means the FMC Act would be amended to make it mandatory for Part 6 licences issued by the FMA to encompass all market services that a single legal entity is approved to provide. This would remove the current ability that the FMA has under section 399 of the FMC Act to issue separate licences for each type of market service.

105. As under Option 1, this would mean, for example, a firm that applies to provide the services of acting as a manager of a registered scheme and acting as a provider of a financial advice service would, if approved, be issued with a single conduct licence that covers those two market services. If in future the firm applied and was approved to provide an additional market service, this would be added to the same licence. The difference from Option 1 is that this approach would be required by the legislation, rather than the FMA exercising its discretion to take this approach (rather than taking the approach of issuing separate licences). Having the single licence approach be made mandatory in legislation should provide greater clarity and certainty to firms and the FMA regarding the licensing model.

106. The key difference from Option 1 is that Option 2 would also provide for an automatic and mandatory legislative grandfathering process of existing licences into the single licence structure. This would involve:

    a. An amendment to the FMC Act would provide for existing conduct licences held by a licensed firm to be consolidated into a single conduct licence as of a set date (ie so that all existing licensees would move onto the new licensing structure at the same time).

b. The current conditions that apply to each licensed service would continue to apply to each service.

c. Any bodies or entities authorised (under s 400 of the FMC Act) to provide a service under the current licence would continue to be authorised to provide that service under the single licence.

d. FMC Act provisions that enable licences to be varied, suspended or cancelled would continue to apply, with the ability to exercise these in relation to particular market services.

107. As under Option 1 above, while these matters fall outside the scope of this law reform process, we understand the FMA would also be considering operational changes to align with the single licence approach (eg streamlining standard conditions and harmonising regulatory returns). Mandating a single licence approach in legislation should provide a legislative framework that facilitates these changes being made.

Submitter views on Option 1 and 2

108. Submitters strongly supported the FMA being required by legislation to issue a single conduct licence (Option 2). Submitters said that the current model of licensing is an overly onerous process for those who wish to apply and hold more than one market service licence.

109. Some submitters queried how the new approach would apply to corporate groups. We note the intention under Options 1 and 2 is for the single licence to cover the market services that a single legal entity has been approved to provide. There is no proposal to move to a single licence for each corporate group.

110. One stakeholder preferred the status quo and opposed the proposal to move to a single licensing approach. This stakeholder was concerned that a single licence application process may be more complex, be unlikely to give rise to many efficiencies, and may create more problems than it solves. Some of the issues raised by this submitter relate to operational matters (such as streamlining standard conditions) which are outside the scope of this law reform process.

111. Submitters raised some comments on the licensing consolidation process. For example, that this should be an automatic process that does not require firms to apply or incur cost, and that a breach should only effect the relevant market service and not the licence as a whole.

112. A number of submitters also considered that the move to a single licence approach would only be effective in reducing complexity and compliance burden if the FMA also makes operational changes (eg to standard conditions and regulatory returns).

2C.4 How do the options compare to the status quo/counterfactual?

	Option One – *Counterfactual – FMA moves to single conduct licence covering different types of market services operationally*	Option Two – *Amend the FMC Act to require the FMA to issue a single licence covering different types of market services*
Promotes the fair treatment of consumers	We do not expect the move to a single licence to have any direct impacts on fair treatment of consumers. **0**	We do not expect the move to a single licence to have any direct impacts on fair treatment of consumers. **0**
Minimising regulatory burden on firms	Over time compliance costs for firms that apply to provide more than one type of market service are expected to reduce with the switch to a single conduct licence, improving flexibility and proportionality. However, existing firms would continue to hold multiple licences, meaning that complexity arising from holding more than one licence would continue for these firms. **0**	Facilitating the move to a single licence through legislation would improve clarity and certainty for both regulated parties and the FMA regarding the licensing model. The legislative approach would also mean that existing licences held by a firm can be automatically consolidated into a single licence, extending the benefits of the single licence approach to existing firms. **+**
Promoting fair, efficient, and transparent financial markets	The move to a single licence over time should promote more efficient financial markets, although the degree of efficiency gained depends on how the FMA operationally implements this change. This option is expected to maintain current market fairness and transparency. However, because existing firms would continue to hold multiple licences, this option would create more complexity and inefficiencies from having two different licensing models operating at the same time, and would mean the objectives of moving to a single licence approach are not able to be fully realised. **0**	Facilitating the move to a single licence through legislation may marginally improve efficiency, but we think impacts are likely to be low. The ability to undertake the legislative consolidation of existing licences would avoid existing firms remaining on the existing multiple licences model, perpetuating inefficiencies for those firms. **+**
Overall assessment	**0**	**+**

2C.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

113. We recommend Option 2 – that the FMC Act be amended to require the FMA to issue a single licence covering different types of market services.

114. Both options result in a switch to a single licence, however Option 2 better achieves the policy objectives of this reform.

115. The material difference between the two options is that Option 2 would consolidate the existing licences held by a firm through an automatic and mandatory legislative grandfathering process. By contrast, it is not feasible to consolidate licences held by existing firms operationally under Option 1, due to the constraints of the existing legislative provisions. The preferred option means that all firms can move onto the new single licence structure at the same time and on the same terms. This executes a clean transfer to the new licensing approach, avoids the complexity and inefficiencies of existing firms remaining on the current model, and provides certainty and clarity for firms and the FMA.

116. A legislative requirement will also facilitate the FMA making operational changes to standard conditions and regulatory returns.

2C.6 What are the marginal costs and benefits of the option?

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	Firms should see no additional costs imposed outside of what is already required of them to undergo the licensing process.	None expected	Medium
Regulators	Under either Option, the FMA would need to be resourced appropriately in order to facilitate the transition as well as develop guidance for firms in how the application process has changed. No additional marginal costs are expected from Option 2.	None expected	Medium
Consumers	There are no anticipated costs for consumers.	None expected	Medium
Total monetised costs	No additional costs are expected.	None expected	Medium
Non-monetised costs	We do not anticipate the legislative change giving rise to any costs for regulated groups, the FMA or consumers.	None expected	Medium
Additional benefits of the preferred option compared to taking no action			
Regulated groups	We anticipate that firms would benefit from a degree of certainty	Low	Medium

Affected groups	Comment	Impact	Evidence Certainty
	and clarity in legislation about this process. Existing firms would benefit from the ability to consolidate their existing licences into a single licence through an automatic legislative grandfathering process (compared to Option 1 where this would not be possible).		
Regulators	The FMA is expected to benefit from the clarity that a change in primary legislation could provide. Compared to Option 1, the preferred approach avoids the FMA needing to operate two different licensing models.	Low	Medium
Consumers	We do not anticipate consumers will experience any benefits from the transition being made through primary legislation.	None expected	Low
Total monetised benefits	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown
Non-monetised benefits	Both firms and the FMA are expected to experience a greater degree of clarity, certainty and efficiencies from the change being made through primary legislation.	Low	Medium

117. We note that amending the FMC Act to require the FMA to issue a single licence covering different types of market services is expected to decrease compliance costs for firms and therefore increase efficiencies they experience with the system. This expectation depends on how the FMA operationalise any amendments made and whether they identify efficiencies they can make for firms. There is a risk that benefits would not be realised, and an onerous process remains in place. This sits outside the scope of this law reform process, but we do understand that the FMA has begun the process to transition to a single licence structure and this would be a factor for them to consider.

Section 2, Part D: Options analysis – Enabling the FMA to rely on an assessment by the RBNZ where appropriate

2D.1. What is the context?

118. As noted above at paragraph 11 New Zealand has a “twin peaks” model of financial markets regulation.

119. In practice, this means that the FMA and the RBNZ both have regulatory oversight of financial institutions (ie registered banks, licensed insurers, and NBDTs) from their independent prudential and conduct perspectives. At times requirements may overlap. For the twin peaks model to operate as intended, it is important that both regulators have a clear mandate and appropriate powers and that neither is secondary to the other. It is equally important that the regulators coordinate with each other to ensure they work together in a coherent way and do not duplicate requirements for industry.

2D.2. What is the policy problem or opportunity?

120. Stakeholders have raised concerns that the complexity of the current model imposes costs on firms, including potential duplication of requirements. For example, both regulators may request and consider similar information from firms around matters like business continuity plans and cyber-security from their different perspectives. There could be opportunities for the regulators to better coordinate and collaborate to reduce burden on industry.

121. Through discussions with the regulators and submissions on the discussion document we have identified the following specific areas where both regulators have an interest and where industry encounter seemingly overlapping requirements:

   a. ‘fit and proper’ licensing requirements

   b. operational resilience, particularly IT and cyber resilience

   c. business continuity, and

   d. outsourcing.

122. The following table outlines the current regulatory approach by both regulators to these requirements.

	FMA	RBNZ
Fit and proper requirements	The FMA must issue a licence to an applicant if the FMA is satisfied that certain criteria are met including that the applicant’s directors, senior managers and proposed directors and senior managers are fit and proper persons to hold their positions.	In order to issue a licence the RBNZ must be satisfied that certain criteria are met, including: • (in relation to banks and NBDTs) that the applicant’s directors, senior managers and proposed directors and senior managers are suitable persons to hold their positions. • (in relation to insurers) that the applicant has developed a fit and proper policy and provided the RBNZ with fit and proper certificates (see sections 18-19 and 34 of the Insurance (Prudential Supervision) Act 2010 (IPSA)).
Requirements relating to operational resilience,	Market service licences typically held by financial institutions will be subject to	The RBNZ’s current formal requirements relating to operational resilience, business continuity and outsourcing are limited. This reflects a historical

	FMA	RBNZ
business continuity and outsourcing	standard conditions relating to operational resilience (which includes IT and cyber resilience), business continuity and outsourcing.	emphasis on market and self-discipline rather than regulatory discipline. Existing requirements include: • *Statement of Principles: Bank Registration and Supervision (BS1)* which requires banks to satisfy the RBNZ that they have adequate risk management systems and policies. • *Guidance on Cyber Resilience* which applies to all regulated entities. • *Outsourcing policy (BS11)* which applies to the five largest banks in New Zealand. The RBNZ is consulting from August to November 2024 on a proposal for an operational resilience standard for deposit takers as a part of the consultation process to implement the Deposit Takers Act 2023 (DTA). This standard will propose requirements to enable operational resilience, including relating to information and communication technology risk; material service providers (outsourcing); and business continuity planning. The RBNZ anticipates consideration of similar requirements in the future for insurers as a part of changes arising from the IPSA review.

123. Some submitters queried why the FMA is interested in operational resilience, business continuity and outsourcing, while accepting that these requirements are plainly relevant to the RBNZ's prudential concerns around the safety and soundness of financial institutions.

124. The FMA's interest in each of these categories is ensuring that a licensed firm can effectively perform services it is licensed for under the FMC Act and to meet market services licensee obligations. In relation to business continuity, operational resilience and outsourcing, the standard conditions are intended to provide consumers with the security of continuity of services and products they receive from licensed providers and to ensure that consumers are treated fairly during a business disruption. The FMA will ask, in particular:

    a. Are the firm's critical technology systems operationally resilient?

    b. Does the firm have and maintain a business continuity plan that is appropriate for the scale and scope of its service?

    c. Can the firm be satisfied that, where any outsourced provider is used to meet market services obligations, that provider is capable of performing the service to the same standard required to enable the firm to meet its obligations?

125. The difference in remits mean that the FMA and the RBNZ view firms' responsibilities and activities through different lenses. For example, an event may fall within the remit of both regulators, but because of their differing remits, one regulator may take more or less interest in the event depending on whether it relates more to conduct or to prudential risk. It is also possible that both regulators may be equally interested in an event but from different perspectives – for example, the FMA may focus on the impacts of the event on consumer treatment and outcomes, while the RBNZ focuses on the implications of the event for the financial stability of the relevant firm.

126. In terms of supervisory approach, the FMA looks at these questions through the lens of the possible impact on the consumer when there is or could be a critical failure or material disruption to the service. For example, a bank that relies on an external provider to support its website and mobile applications must have appropriate arrangements in place to ensure that the arrangements are operationally resilient and that consumers using the website and mobile applications are treated fairly.

2D.3. What options are being considered?

Option 1: Status quo

127. There are some legislative provisions that require the regulators to consult each other before issuing a licence (eg section 20 of the DTA, regulation 190 of the FMC Regulations) or to have regard to whether an applicant is licensed by the other regulator (eg section 397(1)(b) of the FMC Act). These provisions ensure relevant information held and considerations known by the other regulator are taken into account in licensing decisions.

128. FMA and the RBNZ currently coordinate and collaborate on matters of interest to both regulators, including through sharing information and undertaking joint supervisory and investigatory activity where appropriate and possible to do so. For example, the FMA and the RBNZ have worked together to develop and publish a template that firms regulated by both regulators can use to report cyber incidents, rather than needing to complete different forms for each regulator. Both regulators have statutory functions to co-operate and share information with each other (see section 9 of the Financial Markets Authority Act 2011 (FMA Act) and section 10 of the Reserve Bank of New Zealand Act 2021).

129. We understand the FMA and the RBNZ have begun a process to discuss how to use their existing memorandum of understanding (MOU) to address overlap concerns that have been identified. This work intends to provide greater clarity and certainty on the roles and responsibilities between the two regulators in areas of potential overlap and shared interest.

130. Over time, collaboration and coordination between the regulators is expected to improve. There will likely continue to be areas of actual or perceived overlap and areas where both regulators are making similar assessments and/or requiring similar information from firms, due to their separate mandates.

Option 2: Amend the FMC Act to enable the FMA to rely on an assessment by the RBNZ

131. An option is to amend the FMC Act to explicitly enable the FMA to rely on an assessment by the RBNZ in assessing matters relating to dual-regulated firms, where there may be overlap between both regulators in terms of the assessment.

132. The additional provisions added to the FMC Act would be broad (ie enabling the FMA to rely on or refer to assessments undertaken or work produced by the RBNZ) rather than tailored to particular requirements (eg enabling the FMA to rely on the RBNZ's assessment of whether a firm's directors and senior managers are "fit and proper"). This is because:

    a. A broad approach provides flexibility to capture the nuance of areas of interest. More specific areas generally fit more within the remit of one regulator rather than having overlap (eg capital requirements).

b. A broad approach ensures that the FMA has legislative backing to rely on RBNZ work in any relevant areas. The provisions could give specific examples of where the provision could be applied in order to provide guidance for the FMA and industry about the intended use.

c. A broad approach ensures that any areas of overlapping work that arise in future could be captured. For example, we have consulted on introducing an FMA 'change in control' approval requirement as part of these legislative reforms. The legislative framework should enable the FMA to rely on RBNZ work in relation to a change in control application made under prudential provisions.

133. The provisions would also be permissive (ie the FMA is able to choose to rely on an assessment of the RBNZ) rather than mandatory (ie the FMA *is required to have regard to* the RBNZ's assessment, or the FMA *is required to accept* the RBNZ's assessment and not able to exercise its own discretion). This is because:

a. It is important to maintain the independence of both regulators and to recognise that both regulators have different remits. It will not be appropriate in all instances for the FMA to rely on an assessment undertaken by the RBNZ. For example, both regulators may request similar information from firms but the RBNZ's assessment may only involve considering matters through a prudential lens (eg assessing the soundness and stability of a firm) and the FMA may be required to make an assessment from a conduct perspective (eg assessing the impact on consumers).

b. As outlined above, the FMA and RBNZ requirements (where concerns have been raised) are structured very differently and implemented in different ways (eg operational resilience requirements are set through licensing conditions by the FMA and will be set in future through standards by the RBNZ; fit and proper requirements for insurers are assessed by the FMA during the licensing process but for the RBNZ are dealt with through the insurer developing an appropriate fit and proper policy and providing certificates that requirements are met).

134. Even under Option 2, there will likely continue to be areas of actual or perceived overlap and areas where both regulators are making similar assessments and/or requiring similar information from firms, due to their separate mandates. However, there may be a reduction in regulatory burden compared to the counter factual.

135. We have considered whether a regulation-making power could be of use (enabling specific areas to be designated as areas where the FMA will rely on RBNZ assessments). However, this would not be beneficial for a broad and permissive approach (given that the FMA may choose to rely on any assessments/work done by the RBNZ). If a mandatory approach was being taken, we consider that regulations would not be appropriate in any event because any potential changes that may impact on the FMA's independence should be dealt with in legislation.

Submitter views on Option 1 and 2

136. 17 submissions on the discussion document supported Option 2. No submissions opposed this option.

137. Submitters noted the extensive resources required to respond to similar regulator requests in a different format or scope. Some submitters noted that the RBNZ and the FMA have recently established a common reporting mechanism for cyber-resilience, but that this does not address issues in full. Cyber incident reports still need to be sent

to both regulators and then dual-regulated firms still need to deal with separate correspondence, questions and requests for more information.

138. In comments about the design of the provision, three submitters proposed that the language should be mandatory rather than permissive, requiring the FMA to rely on the RBNZ's assessments in particular areas. For the reasons outlined above, we have not taken this approach.

139. Some submitters suggested that one regulator should be designated as a 'lead' regulator in particular areas. That regulator would be the sole contact for reporting/providing information and responsible for engaging with the other regulator as needed. We agree this is a sensible approach, but consider that it would not be appropriate to specify this in legislation at this time, given that the regulators have different legislative frameworks (functions, powers, and remits) and only the FMA's legislation is within scope of this process. It may also have implications for the independence of the regulators. This approach can be facilitated to an extent already through operational agreement between the regulators (for example through the FMA and RBNZ's MOU).

2D.4 How do the options compare to the status quo/counterfactual?

	Option One – *Counterfactual*	Option Two – *Amend the FMC Act to enable the FMA to rely on RBNZ assessments*
Promotes the fair treatment of consumers	The FMA regulates conduct in financial markets and assesses matters relating to the fair treatment of consumers. **0**	No impact expected of the proposed approach (ie the FMA will continue to be an independent conduct regulator). **0**
Minimising regulatory burden on firms	Currently, regulatory burden and compliance costs may be incurred, where dual-regulated firms are required to be assessed on similar matters by both regulators (dealing with separate correspondence, questions and requests for information). **0**	This option is expected to make it easier for the FMA to rely on existing work already carried out by the RBNZ, and therefore reduce regulatory burden and compliance costs for dual-regulated firms. However, both regulators have separate remits so some overlaps (eg both regulators asking questions) are likely to remain. **+**
Promoting fair, efficient, and transparent financial markets	The regulators already have some existing legislative obligations requiring them to work together and will continue to collaborate and coordinate with each other. **0**	This option is expected to improve collaboration and coordination of the regulators, without impacting on independence or their separate mandates, and therefore should promote fair, efficient and transparent financial markets. **+**
Overall assessment	**0**	**++**

2D.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

140. We recommend Option 2 – that the FMC Act be amended to enable (but not require) the FMA to rely on assessments or work done by the RBNZ where appropriate.

141. This option is expected to better enable the FMA and RBNZ to coordinate and collaborate with each other, without impacting on their independence or separate mandates, and therefore should promote fair, efficient and transparent financial markets.

2D.6 What are the marginal costs and benefits of the option?

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	There are no anticipated additional costs for regulated firms.	None expected	Medium
Regulators	There are no anticipated additional costs for the FMA, given that the FMA already endeavours to collaborate and coordinate with the RBNZ where appropriate.	None expected	Medium
Consumers	There are no anticipated costs for consumers.	None expected	Medium
Total monetised costs	No additional costs are expected.	None expected	Medium
Non-monetised costs	We do not anticipate the legislative changes giving rise to any costs for regulated groups, the FMA or consumers.	None expected	Medium
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Firms may see a reduction in regulatory burden and compliance costs due to better coordination between the FMA and the RBNZ.	Low	Low
Regulators	This option is expected to make it easier for the FMA to rely on existing work carried out by the RBNZ, and may have some efficiency benefits for the FMA.	Low	Low
Consumers	There are no anticipated benefits for consumers.	None expected	Medium
Total monetised benefits	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown
Non-monetised benefits	This option is expected to benefit firms and the FMA.	Low	Medium

Section 2, Part E: Options analysis – Change in control approval requirements

2E.1 What is the context?

142. The discussion document proposed to introduce change in control approval requirements for FMC Act licensed firms, similar to what applies to prudentially licensed financial institutions. Both the RBNZ and the FMA have a separate and independent interest in a change in control:

    a. from a prudential perspective, a restructure may have an impact on the governance and financial strength of a firm.

    b. from a conduct perspective, a restructure may impact on the interests of consumers and the firm's ability to treat consumers fairly.

143. Financial institutions currently need to obtain regulatory approval from the RBNZ prior to a change in control, but not from the FMA. For firms which hold licences under the FMC Act which are not financial institutions, there is no requirement to obtain regulatory approval from any regulator prior to a change in control.

2E.2. What is the policy problem or opportunity?

144. The current approach limits the FMA's ability to scrutinise the impacts of a change in ownership of a licensed firm on consumers before it takes place. A change in control can affect the treatment of customers and consumer outcomes by fundamentally changing the governance and operation of the licensed firm (eg business model, staffing, outsourcing arrangements). As the FMA only has the ability to scrutinise a change in control after the fact, it may not be able to consider or place conditions on a sale to support the interests of customers.

145. The FMA has advised that there have been instances where conduct issues or concerns regarding consumer treatment have developed as a result of changes made by the new owners after a change in control has taken place, and the FMA's ability to respond reactively has been limited.

2E.3. What options are being considered?

Option 1: Status quo

146. The FMA has an expectation that licensed firms engage with it in advance of any change in control (see the reporting requirements in regulation 191 of the FMC Regulations). However, the FMC Act does not contain similar provisions to those in prudential legislation. This means proposed new controlling owners of licensed firms are not required to obtain a regulatory approval from the FMA ahead of any change in control taking place.

147. Under the existing legislative framework, no requirements attach to the proposed new controlling owner (the purchaser or acquirer). This means the FMA cannot require the new controlling owner to provide it with information about the proposed transaction to assess the impact this may have on the licensed firm's ability to effectively perform its licensed functions. It may have limited visibility or no advance notice of the transaction taking place.

148. This option would mean a current gap in the regulatory settings which may impede FMA's ability to act as an effective and proportionate regulator would continue.

Option 2: Introduce this power and apply to CoFI regulated entities only

149. This option would introduce this power and have it applied to only CoFI licensed entities, ie firms that are regulated by both the FMA and the RBNZ. This would mean that the prospective purchaser or new controlling owner of a bank, insurer or NBDT would be required to seek approval from both the Reserve Bank and FMA in advance of the change in control. To reduce regulatory burden, the thresholds for requiring approval would be aligned to prudential legislation, so that approval of a transaction is required in the same circumstances where a prudential approval is required.

150. Currently, transactions are assessed by the RBNZ in accordance with prudential criteria (eg solvency) which do not have a direct focus on policyholder interests. Under this option, the FMA would also assess the transaction from a conduct perspective, addressing this legislative gap. This could include, for example, an assessment of whether the business and operating models proposed for the licensed institution post-sale would impact on the effectiveness of the licensed institution's conduct programme in ensuring consumers are treated fairly.

151. This option has the advantage that it reduces compliance burden comparatively to Option 3. It also has the advantage that firms who are licensed financial institutions are already subject to a similar power prudentially so they have experience in meeting the requirements should they trigger the provision. But by limiting the scope in who is captured by the requirement, the FMA is limited in addressing conduct issues proactively across all licensed firms, including firms who are otherwise not subject to any regulatory oversight of changes in control.

152. The proposed reliance provision (Section 2D above) could allow the FMA to rely on assessments from the RBNZ. We also expect that the FMA and RBNZ would coordinate to reduce regulatory burden, for example by developing processes so that financial institutions are only required to liaise with a single regulator or submit a single form.

Option 3: Introduce this power and apply it to all entities licensed under Part 6 of the FMC Act

153. This option would introduce this power and have it applied to all firms licensed under Part 6 of the FMC Act. This would operate in the same way that the previous option would, but would expand the firms captured to include those that are not currently subject to any prudential oversight of changes in control. This means there would now be some regulatory oversight of transactions involving these firms.

154. As under Option 2, the requirement to obtain approval would apply to the proposed new controlling owner. A formal requirement to obtain FMA approval, with clarity around the assessment criteria and timeframes, would provide certainty for purchasers, licensed firms, and consumers on the expected role of the conduct regulator and the process that will be followed.

155. This option would increase regulatory and compliance burden, particularly for firms who are not accustomed to meeting this obligation prudentially. There may be direct costs for purchasers associated with applying for consent, in additional to opportunity costs and business costs caused by the uncertainty of waiting for approval.

156. Our regulatory system in general seeks to maintain New Zealand's free and open financial markets, such that control of firms can change, subject to the protection of the interests of consumers and policyholders. The design of this power would seek to strike

an appropriate balance so that there is appropriate scrutiny of changes in control without creating unnecessary compliance costs, burden or delays. This can be achieved through a combination of setting appropriate thresholds for requiring approval, ensuring the assessment criteria for approvals is clearly defined and linked to the original criteria for licensing, and through the FMA taking a risk-based and proportionate approach to approvals that seeks to minimise regulatory burden. For example, this could take into account whether the acquirer is itself an existing FMC Act licensed firm.

Submitter views on options

157. 25 submissions were received on this power. Over half of the submitters (17) came from industry who opposed the introduction of this power, with the remaining submission coming from consumer groups who supported the introduction of this power.

158. Submitters who did not support the introduction of this power were generally of the view:

    a. This power is not relevant to conduct supervision, it is more suited for prudential regulation; and

    b. The introduction of this power would increase duplication between the FMA and RBNZ. This would mean that in the event of a change in control, a financial institution would need to seek dual consents from respective regulators.

159. We are of the view that it is appropriate and desirable for changes in control to be assessed from a conduct perspective, for the reasons set out at in the problem definition at paragraph 144 above. New Zealand's twin peaks model of regulation, places equal importance on prudential and conduct considerations, and we consider that omitting the conduct assessment creates a regulatory gap. For example, a proposed transaction may comfortably satisfy prudential criteria (eg solvency) while still raising serious concerns about the post-sale treatment of consumers. In relation to duplication concerns, we also note the proposed reliance provision as per paragraph 131 above.

160. Submitters who supported the introduction of this power generally agreed that the FMA needed to be equipped with effective supervisory tools to proactively prevent consumers facing harm. Further, some submitters noted the power would allow the FMA to be more proactive rather than acting in retrospect, and that it would improve the operation of the twin peaks model.

161. Submitters who opposed the introduction of the power were evenly split as to whether the power should apply only to financial institutions or to all firms licensed under Part 6, while submitters who supported it agreed that this power should extend to all firms licensed under Part 6.

2E.4 How do the options compare to the status quo?

	Option One – *Status quo*	Option Two – *Introduce change in control approval requirement and apply to CoFI regulated firms only*	Option Three – *Apply change in control approval requirement to all firms licensed under Part 6 of the FMC Act*
Promotes the fair treatment of consumers	Proposed acquirers are not required to obtain the FMA's approval prior to a change in control, limiting the ability of the FMA to scrutinise the impact on consumers and respond proactively to any concerns. The FMA has some limited ability to respond reactively to a change in control due to existing notification requirements. **0**	This option is expected to promote the fair treatment of consumers, by allowing the FMA to engage with the acquiring firm and consider conduct issues before the point of sale. This ensures that the impact of the change in control on consumer treatment and outcomes can be scrutinised in advance and proactive steps taken to address concerns. +	See previous analysis. This option is expected to extend on this, applying conduct oversight to transactions involving firms who are not covered by similar requirements under prudential legislation, so there is now some oversight by a regulator of these transactions (in particular as to any impact on consumers). + +
Minimising regulatory burden on firms	As above, proposed acquirers are not required to obtain prior FMA approval of a proposed transaction, avoiding the time and cost of a regulatory approval process. **0**	This option is expected to somewhat increase regulatory burden, as firms will need to obtain an additional regulatory approval from the FMA in addition to the existing approval required from the RBNZ. -	See previous analysis. The regulatory burden for firms who are not prudentially regulated may be relatively higher as this introduces an approval process where none is presently required. These firms lack experience in change in approval process requirements. - -
Promoting fair, efficient and transparent financial markets	Under the status quo, there is limited assessment of the conduct implications of transactions prior to these taking place, creating a regulatory gap and meaning that concerns need to be addressed reactively after a transaction has taken place. **0**	The introduction of a formal requirement provides certainty and transparency for acquirers, licensed firms, and consumers on the role of the conduct regulator and assessment criteria for transactions. It facilitates engagement between the acquiring firm and the regulator to address any concerns in advance, which avoids undesirable post-transaction licensing consequences for the firm and adverse impacts on consumers. It also creates alignment between the twin peaks. +	See previous analysis. This option ensures change in control approval requirements apply equally across all firms licensed under Part 6 of the FMA Act, rather than applying to a subset of firms. Introducing appropriate regulatory scrutiny at an earlier stage may assist to avoid post-transaction issues and adverse impacts on consumers arising. ++
Overall assessment	**0**	+	+ +

2E.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

162. We recommend Option 3 – Introduce change in control approval requirements and apply it to all entities licensed under Part 6 of the FMC Act.

163. This option ensures there is effective regulatory scrutiny of changes in control from a conduct perspective, by allowing the impacts of transactions on consumers to be proactively considered, providing acquiring firms with transparency regarding the process and the opportunity to establish a dialogue with the FMA and address conduct concerns in advance, and assisting to avoid negative post-transaction impacts on consumers and potential licensing consequences for the licensed firm.

164. Option 3 has relatively higher net benefits compared to Option 2, because this introduces a regulatory approval process for non-financial institutions that are currently not subject to any oversight of this nature by a regulator for a change in control. This is fairer and is expected to deliver a net benefit to consumers impacted by transactions. The design of this power would seek to strike an appropriate balance so that there is appropriate scrutiny of changes in control without creating unnecessary compliance costs, burden or delays.

2E.6 What are the marginal costs and benefits of the option?

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	Increased compliance costs for proposed controlling owners from needing to obtain regulatory approval. Costs increases are expected to be small for transactions involving financial institutions where prudential approval is already required, and somewhat higher for transactions involving non-financial institutions where there is no current approval requirement. This should be moderated through the design of the requirement and FMA taking a risk-based and proportionate approach	Low/Medium	Medium
Regulator	The FMA will need to develop systems, processes and materials to formally consider and approve transactions and engage with firms on the new requirements.	Low/Medium	Medium
Consumers	We anticipate no additional costs for consumers.	None expected	Medium
Total monetised costs	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown

Affected groups	Comment	Impact	Evidence Certainty
Non-monetised costs	We expect acquiring firms and the FMA to incur some costs from introduction of a new formal regulatory approval process for changes in control.	Low/Medium	Medium
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Acquirers will have transparency regarding the process and the opportunity to address conduct concerns in advance, while earlier regulatory scrutiny may avoid post-transaction issues arising for licensed firms.	Low	Medium
Regulator	We expect the FMA to benefit from having more effective monitoring powers in relation to changes in control, assisting to avoid supervisory issues arising post-transaction that would require time and resource	Medium	Medium
Consumers	Consumers should benefit from advance regulatory scrutiny of the impact of transactions on consumer treatment and the ability for proactive steps to be taken to address concerns.	Medium	Medium
Total monetised benefits	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown
Non-monetised benefits	We expect this option to particularly benefit consumers. The FMA will also benefit from more effective monitoring powers and there will be some limited benefits to regulated firms.	Medium	Medium

Section 2, Part F: Options analysis – Empowering the FMA to conduct on-site inspections

2F.1 What is the context?

165. As outlined above, the FMA as the financial markets conduct regulator is responsible for facilitating the development of fair, efficient, and transparent financial markets. A core part of this role is monitoring compliance with financial markets legislation. We also understand that the FMA's current focus is about ensuring the success of a number of significant priorities in financial conduct regulation in New Zealand, including:

    a. implementation of conduct licensing and supervision for banks and NBDTs (ie deposit takers) and insurers through the CoFI regime (discussed above),

    b. addressing the proliferation of harmful investment scams targeting New Zealanders,

    c. deterring misleading conduct in financial services, and

    d. the transfer of credit regulation to the FMA.

166. Effective supervisory tools will allow the FMA to carry out its regulatory role effectively and efficiently, engage proactively with regulated firms and respond proportionately to harm.

2F.2 What is the policy problem or opportunity?

167. On-site inspections can often reveal a markedly different picture of compliance than is evident from written documents, making them a crucial part of a regulator's toolkit.

168. The FMA's predecessor (the Securities Commission) had an on-site inspection power. When the FMA Act was developed it was understood that this power had been translated across into the information gathering powers in section 25 of the FMA Act, but a court decision subsequently clarified that this is not the case.

169. This has meant the FMA does not currently have powers to conduct on-site inspections without prior notice in appropriate circumstances to independently verify compliance with regulatory requirements, other than for Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT Act) purposes. The FMA can otherwise only carry out on-site inspections of regulated firms with consent, require specified information by written notice, or use search powers on the basis of a court ordered warrant for the purpose of seeking evidential material for a suspected contravention. Refusing consent is not grounds to seek a warrant.

170. The RBNZ has recently been granted the power to undertake on-site inspections of deposit takers without prior notice (or consent) under subpart 2 of Part 4 of the DTA following the 2017-2021 Reserve Bank Act review. The power must be exercised at a reasonable time and in a reasonable manner consistent with the purpose of the power. Similar powers in relation to insurers are being considered through the review of IPSA. The lack of alignment with equivalent RBNZ powers may undermine coordinated and efficient supervision and monitoring by the twin peaks regulators (eg joint on-site visits where appropriate).

171. The status quo does not align with international expectations and good practice, which risks reputational harm to New Zealand's financial markets. International standards for

securities regulation are set by the International Organization of Securities Commissions (IOSCO). IOSCO's Principle 10 requires that conduct regulators have the power to carry out inspections of regulated entities on their premises without prior notice (or consent) when appropriate to verify compliance with regulatory requirements. Other international conduct regulators have such powers (eg in Australia, the United Kingdom, Canada, the United States of America and Singapore).

172. As an example of the kind of scenario where issues arise:

    a. The FMA may have concerns about the financial health of a firm that has raised money from New Zealanders for investment purposes. The FMA's concerns may be based on investor complaints and media reports, and the FMA may not have evidence of any specific offence or contravention sufficient to seek a search warrant.

    b. Understanding the financial state of the company is essential to enable the FMA to determine whether it should intervene to support a managed resolution for the company.

    c. If the firm is not cooperative with arranging a visit, then without an on-site inspection power the FMA would need to make broad written notices requiring information. The FMA may need to cross-check this information with records obtained from the firm's bank. The firm may delay responding to the FMA's requests for information and may incur significant expenses responding to the FMA's requests. Given the potentially precarious state of the company, this process could take too long and the firm could collapse.

    d. An inspection power would allow the FMA in these circumstances to inspect the firm's own accounting system, quickly providing it with the information required to understand the state of the firm's health, the risks to investors, and the need for any intervention. This option would have been available to, and was used by, the Securities Commission for this kind of purpose.

2F.3 What options are being considered?

Option 1: Status quo

173. Currently, the FMA has no formal power to undertake a monitoring or supervisory visit if a firm declines to participate (except for AML/CFT Act purposes).

174. The FMA advises that its work has been impeded by the lack of an on-site inspection power. Firms have delayed or refused monitoring visits over months, creating ongoing risks for customers and investors, inefficiencies and expenses both for the firm and FMA. Costs incurred by the FMA are ultimately borne by the Crown and all FMA levy-payers, which is arguably unfair to those levy-payers who do cooperate with the FMA.

175. Under this option there are delays in the FMA being able to understand issues and work with firms on addressing them, which in turn creates risks for consumers and investors (as outlined above at paragraph 172).

Option 2: Amend FMA Act to ensure FMA has effective monitoring powers to conduct on-site inspections

176. This option would give the FMA the power to conduct on-site inspections without prior notice (or consent) for the purpose of carrying out market conduct supervision of firms. It would enable the FMA to:

a. obtain independent verification that firms have adequate policies and procedures, and are complying with regulatory requirements (including providing reliable information), and

b. obtain any additional information and request copies of documents as appropriate, including a proper understanding of the operations of the firms, and the firms' risks and how they are managed

c. monitor how firms are addressing any risks and instances of non-compliance.

177. Under this option, the vast majority of on-site inspections would be carried out with prior notice and the firm's consent (eg through arranging an appointment with the firm's staff). However, where a firm refuses to provide consent following reasonable endeavours, this option would enable the FMA to proceed with conducting an on-site inspection without consent, subject to the safeguards below, and typically still with notice provided to firms. This option will enable the FMA to act in a more efficient and cost-effective way instead of getting entangled in lengthy delays with firms.

178. Additionally, the ability to conduct an on-site inspection without prior notice is essential to ensure that the FMA has sufficient flexibility to turn up at a business at a reasonable time in rare but appropriate cases, for example where there is reason to suspect that giving prior notice will result in a markedly different picture of compliance. These situations are expected to arise infrequently.

179. Under this option the following safeguards would apply to ensure New Zealand is brought into line with international standards for conduct regulators, support the Government's intention to reinforce the 'twin peaks' model of financial regulation (by aligning with existing powers of RBNZ), ensure consistency with the AML/CFT Act power, and support the FMA to deter harmful unregulated activities in New Zealand's financial markets:

a. only being able to exercise the power at a reasonable time and in a reasonable manner consistent with the purpose of the power

b. exclusions for inspections of private dwellings and marae

c. the authorisation or approval of persons carrying out inspections (and these persons being well-trained and having requisite expertise), and

d. appropriate confidentiality protections for information gained from inspection.

180. We expect that in practice this power would not be frequently used by the FMA. For example, FMA has only used the AML/CFT Act inspection power without notice once, when there was a significant lack of trust in a firm and a refusal to allow the FMA to inspect the firm's records. The FMA is also required to exercise its powers in a responsible and proportionate way.

181. In practice, the majority of firms (whether they are licensed or not) are already subject to a broad on-site inspection power available to the FMA, Department of Internal Affairs (DIA) and RBNZ under the AML/CFT Act, and/or consent to FMA monitoring visits. It is therefore unlikely, in practice, that most firms will experience any additional compliance costs.

Submitter views on Option 1 and 2

182. The 29 submitters were relatively evenly split between supporting and opposing the on-site inspection power. Those that opposed questioned the need as the FMA already has the power to inspect with consent, or seek a warrant, and suggested that introducing a further power would harm FMA's relationships with firms and create further burden and inefficiencies, particularly for smaller firms.

183. Those that supported, including NZBA, considered it would give the FMA the ability to act quickly when needed. It would equalise the FMA and RBNZ twin peaks model and be in line with overseas regulators. Submitters noted that it has always been intended for the FMA to have this power, and the gap is due to imprecise wording. Submitters agreed that the 'without notice' aspect of the power should only be used as a last resort and have appropriate safeguards.

184. Submitters agreed that if the power were to apply, it should apply to all firms regulated by the FMA (ie financial markets participants), not just licensed firms.

185. In relation to concerns around regulatory burden and inefficiencies, we note the above safeguards at paragraph 179 and the need for the FMA to act as a reasonable and proportionate regulator.

2F.4 How do the options compare to the status quo/counterfactual?

	Option One – *Status quo*	Option Two – *Amend the FMA Act to ensure the FMA has powers to conduct on-site inspections*
Promotes the fair treatment of consumers	Under the status quo the FMA does not have the power to inspect firms without consent or notice. There can be delays in the FMA being able to understand issues and work with firms on addressing them, which in turn creates risks for consumers and does not promote fair treatment. **0**	This option would better ensure the FMA can act quickly to identify unfair treatment of consumers and prevent harm from taking place. **++**
Minimising regulatory burden on firms	Currently, regulatory burden and compliance costs may be incurred, by firms when FMA conducts on-site inspections with consent or is required to issue multiple written notices requiring information. **0**	Some firms may consider they need new processes and training in place to respond to the potential for an on-site inspection. The majority of regulated entities are currently subject to an AML/CFT Act on-site inspection power (exercisable by FMA, RBNZ or DIA depending on who is the supervisor), and/or consent to FMA monitoring visits. It is therefore unlikely in practice that most firms will experience any additional compliance costs. **-**
Promoting fair, efficient, and transparent financial markets	The current approach can lead to inefficiencies, delays and increased costs for the regulator and firms if firms refuse or stall following a request for a monitoring visit, creating risks to investors and consumers. **0**	This option would improve fairness, efficiency, and transparency by ensuring the FMA has a standard supervisory power for conduct regulators that provides a deterrent for misconduct and helps ensure ongoing and consistent compliance by encouraging firms to maintain acceptable standards, which would in turn help maintain public confidence in the regulated sector and the regulator. **++**
Overall assessment	**0**	**+**

2F.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

186. We recommend Option 2 – the FMA Act be amended to ensure FMA has effective monitoring powers to conduct on-site inspections.

187. This option is expected to better support FMA's current role as the financial markets conduct regulator as well as its increased mandate under the transfer of credit and responsibility for the conduct of insurers and deposit takers. It should enable the FMA to deliver cost-effective and proportionate regulation that allows FMA to identify and respond to the most serious risks without subjecting firms or the wider sector to unnecessary regulatory cost.

2F.6 What are the marginal costs and benefits of the option?

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	There are minimal anticipated additional costs for regulated firms in relation to an on-site inspection power, given that the majority of regulated entities are currently subject to an AML/CFT Act on-site inspection power, and/or consent to FMA monitoring visits already. Some firms may consider they need new processes and training in place to respond to the potential for an on-site inspection.	Low	Medium
Regulators	There are minimal additional costs for the FMA, given that the FMA has an on-site inspection power for AML/CFT Act purposes and already conducts monitoring visits with consent.	Low	Medium
Consumers	There are no anticipated costs for consumers.	None expected	Medium
Total monetised costs	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown
Non-monetised costs	We do not anticipate the legislative changes giving rise to any costs for the FMA or consumers. There may be minimal additional costs for regulated firms.	Low	Medium
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Firms may see a reduction in regulatory burden and compliance costs due to FMA being able to act more effectively, efficiently, and proportionally.	Low	Low
Regulators	This option is expected to enable FMA to act more effectively, efficiently, and proportionally.	Medium	Medium
Consumers	Anticipated benefits for consumers from the FMA being able to act more quickly to prevent harm.	Medium	Medium

Affected groups	Comment	Impact	Evidence Certainty
Total monetised benefits	Without accurate quantifiable evidence, it is difficult to provide an estimate.	Unknown	Unknown
Non-monetised benefits	This option is expected to benefit confidence in financial markets and the FMA.	Medium	Medium

Section 3: Delivering options

How will the new arrangements be implemented?

188. The FMA will be responsible for the ongoing operation and enforcement of the changes to the CoFI Act, as well as implementing the licence consolidation, reliance provisions and on-site inspection power.

189. The CoFI Act will come into force on 31 March 2025. This means financial institutions will be required to comply with the obligations of the CoFI Act from this date, and to apply for and receive a separate financial institution licence under the CoFI Act by this date. Any new obligations as a result of these proposals would likely commence in 2026 at the earliest.

190. Many financial institutions are already well-progressed in preparing for the introduction of the CoFI regime. This includes developing their fair conduct programmes, and applying for, or preparing to apply for, a CoFI licence, in advance of the regime's commencement date and based on current legislative requirements. The Government has encouraged financial institutions to continue to prepare for the introduction of the regime, notwithstanding this review.

191. This timetable means financial institutions will need to comply with the current legislation (without amendments) until the amendment bill is passed and the obligations under it commence in around 2026. This may result in additional costs for financial institutions to review, and if necessary, adjust, their fair conduct programmes later to respond to any changes made through the amendment bill.

192. This risk can be mitigated with clear and proactive communication. The discussion document highlighted to stakeholders:

    a. the importance of continuing with implementation work and licence applications in preparation for the regime commencing on 31 March 2025, and

    b. the proposed timeline for the amendment bill.

193. Officials and the FMA will continue working with stakeholders to ensure that they are aware of the above.

194. This risk is also mitigated by the fact that the objective of the review is to ensure the requirements of the CoFI regime are streamlined and made more flexible. The intention is to allow financial institutions to have more freedom to tailor their fair conduct programmes in a manner that suits their own business on an ongoing basis. Therefore, although there may be some one-off costs involved relating to the need to review and adjust programmes in response to changes, these changes may reduce compliance burden and costs on an ongoing basis.

195. The reliance provisions and changes to FMA monitoring powers are intended to come into effect as soon as practicable. The FMA is already considering the operational changes needed to implement these legislative changes.

196. The FMA will engage and share information as appropriate with other agencies and stakeholders with an interest in the licence consolidation, reliance provisions and changes to FMA monitoring powers. The FMA regularly engages with the RBNZ and has an MOU in place (which may need updating in relation to the reliance provisions). Engagement will also take place through the Council of Financial Regulators. The FMA

will work with the RBNZ on coordinating and streamlining change in control approval processes in relation to transactions involving financial institutions.

197. The timing of obligations commencing in around 2026 will provide lead time to communicate and engage with firms to ensure they are prepared for the new approval process that will apply to changes in control, and so they are aware of the FMA's proposed on-site inspection powers and the reliance provisions. No specific support for regulated firms is anticipated to be necessary for implementing the reliance provision and the on-site inspection powers.

198. Officials and the FMA will also work with stakeholders to ensure that stakeholders are aware of the timing of licence consolidation. As outlined above, the grandfathering of existing licences into the new single licence structure is proposed to be implemented automatically through legislation and so is expected to itself have limited impacts on firms. However, the FMA will communicate with firms in advance of this occurring to ensure they have a good understanding of the process and what this means for them.

199. Additionally, separate to this process, the FMA is considering operational changes to align with the single licence approach to remove unnecessary compliance costs and streamline financial markets regulation. For example, streamlining licence 'standard' conditions imposed by the FMA for different market services, and better harmonising annual regulatory returns requirements.

How will the new arrangements be monitored, evaluated, and reviewed?

200. The system-level impacts of the proposals will be monitored primarily by the FMA as part of its role in monitoring and responding to market conduct issues and in enforcing the new conduct obligations.

201. The CoFI Act is subject to a statutory review five years after its commencement, which provides an opportunity to review the operation of the regime, as amended by the proposals in this document. The FMA will continue monitoring the extent to which entities are complying with obligations and whether any issues are arising through its general monitoring and oversight of firms once the regime comes into effect.

202. MBIE will provide support to the FMA as appropriate and necessary and monitor the regulatory settings as part of its wider regulatory stewardship obligations. No new, specific data collection activity is proposed at this stage but will be considered if enforcement or compliance issues arise.

203. The interaction with stakeholders, including the RBNZ, following implementation of the amendments, as well as the FMA's ongoing monitoring and enforcement of the conduct obligations, should assist to uncover whether there are any issues. MBIE regularly evaluates and reviews amendments to the law it administers even when not subject to statutory reviews.

204. The FMA has a statutory function to keep under review the law and practices relating to financial markets and financial markets participants. The FMA conducts regular market surveys and thematic reviews on various issues as and when it considers relevant. These mechanisms may be used in respect of the new conduct obligations and powers if appropriate.