

The Financial Markets Authority speaks!

Conduct and Culture Two – this time its Fire and General

21 September 2021

AT A GLANCE:

- The Financial Markets Authority (FMA) has released its [*Insurance Conduct and Culture: Fire and General Insurers Update*](#).
- This update follows the FMA’s scathing review of life insurers in 2019 – [*Life Insurer Conduct and Culture*](#).
- The report is a key indicator of the regulator’s views of the industry in the context of the suite of regulation that comes into full force in 2023.
- This FMA report should be a wake-up call for the wider insurance industry. While the report has no real bite during the current transitional period, it could flag the FMA’s hit list if insurers don’t address the identified issues before 2023.

After the 2018 Australian Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry highlighted serious shortcomings, the FMA and the Reserve Bank of New Zealand (RBNZ) began their review of the New Zealand industry – starting with life insurers.

In January 2019, the New Zealand report, [*Life Insurer Conduct and Culture*](#), identified several industry failings. In response, the Financial Services Legislation Amendment Act 2019 (FSLAA) and the Financial Markets (Conduct of Institutions) Amendment Bill (**CoFi**) were drafted to address the “extensive weaknesses” identified in the sector.

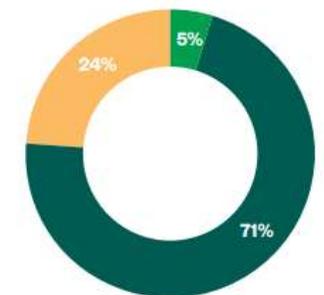
THE REPORT - INSURANCE CONDUCT AND CULTURE: FIRE AND GENERAL INSURERS UPDATE

The FMA’s [*Insurance Conduct and Culture: Fire and General Insurers Update*](#), was based on a review of 42 insurers that operate in New Zealand.

The review investigated six issues:

1. Conduct maturity
2. Product and portfolio reviews
3. Remediation (of identified issued with conduct and product deficiencies)
4. Incentives and commissions
5. Oversight of intermediaries, and
6. Governance and risk management.

Overall, the review was highly critical of insurers, with the FMA stating “[t]he responses were well below our expectations”. Only two of the 42 insurers (5%) were found to be completing all activities to an appropriate standard, even in the areas where the FMA says it provided clear instructions on how to comply.



- Response sufficient
- Response deficient, addressing some but not all of our expectations
- Response inadequate and did not meet our expectations.

KEY ISSUES ADDRESSED IN THE UPDATE

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|--------------------------------------|--|---------------------------------------|---|
| Conduct maturity | <ul style="list-style-type: none"> The FMA considered there to be a poor understanding of, and commitment to, conduct and culture across insurers. It also noted the tone of some responses indicated some insurers did not consider conduct and culture to be relevant to their organisation. Several insurers indicated they were comfortable with their culture, however the FMA was generally critical of a lack of meaningful assessment into culture within organisations. Customer vulnerability was poorly addressed, and the FMA was critical of intermediated insurers who did not consider customer vulnerability to be an issue for them because they did not deal with customers directly. The FMA was critical of the lack of ongoing investment in capabilities to manage conduct risk across all insurers. | Incentives and commissions | <ul style="list-style-type: none"> The FMA praised the 28 insurers that had removed or committed to removing volume-based incentives for internal staff. However, the FMA remained critical of the fact that there was no evidence that incentives and commissions insurers were offering intermediaries were “market rate”. The FMA did not think explanations on how incentives and commissions incentivised “good conduct” were sufficient, or that insurers had shown this ensured fair outcomes for the customer. The FMA was also critical of the lack of clarity around how commissions and incentives were being communicated to the end customer. |
| Product and portfolio reviews | <ul style="list-style-type: none"> Of the 42 insurers reviewed, only 22 completed product and portfolio reviews – of these, all but four insurers identified major issues with the products offered. The main issues identified were weak systems and processes and continued offering of poor value and legacy products, which were unsuitable for the customers they were being sold to. While the FMA was positive about some insurers choosing to withdraw poor value and legacy products from sale, it recommended that all insurers review whether the product remained appropriate to the current and ongoing policy holders of those products. | Oversight of intermediaries | <ul style="list-style-type: none"> The FMA was particularly critical of insurers who did not believe they had a responsibility to customers because they used an intermediary. It stated that insurers needed to be more mindful and ensure their product distribution was in line with the new Code of Professional Conduct. The FMA stated that insurers must ultimately take responsibility for whether customers were experiencing fair outcomes from their products, even where an intermediary has placed that product.¹ |
| Remediation | <ul style="list-style-type: none"> The FMA was most critical of issues identified regarding remediation due to the direct impact these issues had on customers. Across all insurers, it was found that there was evidence that premiums were not accurately calculated, transparent, or administered correctly across several situations. Several personal examples were highlighted. These issues included: <ul style="list-style-type: none"> not applying multi-policy discounts late payment fees being charged for no apparent reason overcharging on agreed premiums customer data being inaccurate no-claims bonuses not being applied, and attempting to provide product benefits that are unlikely to ever be claimed. The FMA identified difficulties for customers in understanding how premiums are calculated, which it flagged as an area requiring improvement. | Governance and risk management | <ul style="list-style-type: none"> The FMA expressed some positivity about senior leadership teams who engaged with the results of reviews and those who engaged external consultants. However, it was critical of insurers that had audit/conduct committees whose recommendations were overlooked by Boards. The FMA commented generally that Boards must set the tone of the conduct conversation and implement policies that develop a culture that balances the interests of shareholders with the interests of customers. |

¹Watch this space, as the CoFi bill has received comment from MBIE about whether it is reasonable to require entities to monitor the strict compliance of their subsidiaries.

WHERE TO FROM HERE FOR NEW ZEALAND'S FIRE AND GENERAL INSURERS?

The FMA's update clearly points to the regulator's expectation for improvement from insurers.

The central theme remains consistent: insurers should identify, manage and mitigate conduct risks in their business, and focus on achieving fair customer outcomes. Insurers shouldn't be waiting for regulations to do this – the message from the FMA is clear: the industry should identify and address risks proactively.

Arguably, many insurers have been focused on the tangible requirements of FSLAA, including making sure advisers have the required certificates and getting a licence. However, these requirements should not be pursued at the expense of the overarching obligation in the CoFi Bill, which is to operate a business that displays "fair conduct" at every level.

The FSLAA remains in its transitional phase until March 2023. The CoFi Bill is at the second reading stage, and is expected to pass in 2021-2022, with some provisions in force from the ascent date.

There's no doubt that insurers, who are already challenged by pandemic pressures, are facing increasing regulatory issues. The FMA has drawn a clear line in the sand, and it is clear it is expecting all insurers to improve before the full suite of regulations come into force in March 2023.

Despite the challenges, the best approach is to address these issues now while the FMA is showing some leniency during the transition period. The latest proceedings brought by the FMA against a major banking institution and a life insurer undoubtedly show a willingness to proactively enforce the regulations, and show what the FMA will expect once the full suite of FSLAA regulations come into force

Insurers should use this opportunity to get all their ducks in a row to ensure they are not caught out by any short comings when the new regime comes into full force.

Need to know more?

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