



## FINANCIAL SERVICES FEDERATION

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Dear Richard

### **Issues Paper: Review of the Insurance (Prudential Supervision) Act 2010**

The Financial Services Federation (“FSF”) is grateful for the opportunity to comment on the Issues Paper: Review of the Insurance (Prudential Supervision) Act 2010.

By way of background, the FSF is the industry body representing responsible and ethical finance and leasing providers in New Zealand. The FSF has over fifty members and affiliates providing first-class financing, leasing, and credit-related insurance products and services to over 1 million New Zealand consumers and businesses. The FSF’s affiliate members include internationally recognised legal and consulting partners. A list of the current membership is attached to this submission as Appendix “A”.

The FSF’s credit-related insurance provider members are subject to the Insurance (Prudential Supervision) Act 2010. The questions raised in the Issues Paper are answered as follows from the point of view of credit-related insurance providers.

#### **1. Do you have any comments to make on the discussion in Part 1 of the Issues Paper?**

The FSF fully supports the aim of improving the efficiency of the prudential framework by modifying or removing requirements that are no longer apt, especially where compliance is costly; allowing flexibility in the application of requirements where appropriate; reducing inappropriate barriers to entry and supporting a level playing field (as per para 23 of the Issues Paper).

FSF's credit-related insurance provider members agree that IPSA has resulted in an improvement in the soundness of the insurance sector whilst not overly constraining efficiency (as per para 26 of the Issues Paper).

The FSF suggests however that the general public is largely unaware of how soundly regulated the insurance sector has become and would only become concerned as to the level of regulation in place (or lack thereof) should something go wrong.

**2. Do you consider that the Review should assess the current scope of IPSA in terms of the nature of insurance contracts or entities that are subject to the legislation? Please provide commentary in support of your view.**

Para 45 of the Issues Paper addresses Reserve Bank concerns that there may be a growing non-licensed insurance sector and cites the example of foreign insurance firms that do not require a licence under IPSA and are not required to register as an overseas company under the Companies Act 1993 such as those that provide reinsurance coverage to New Zealand policyholders, directly or indirectly.

The FSF questions whether the Reserve Bank means to consider bringing reinsurers into IPSA's scope. The FSF suggests that it should be remembered that reinsurers fill a vital role in a market as small as that of New Zealand in ensuring that New Zealand policyholders have sufficient cover in the event of a major incident such as the Christchurch earthquakes.

Further, there are obvious difficulties in seeking to regulate offshore entities who do not have a branch in New Zealand. It might instead be worth considering an obligation on New Zealand underwriters to ensure that their reinsurers meet prescribed rating thresholds or similar. That might serve to increase comfort levels in respect of offshore reinsurers without the difficulties that may be involved in extending the scope of the IPSA.

Three further points the FSF would like to make with regard to the scope of IPSA is for the Review to consider the following:

- There are finance companies who sell "Payment Waiver" products where they indemnify the borrower under certain circumstances if they become unable to meet their repayments under the loan etc. These are essentially unregulated insurance policies which the FSF believes should be regulated under IPSA like other insurers;
- Some insurance brokers describe themselves as insurance companies in their names and marketing material. An example of this would be TradeMe Insurance where the sales and distribution channel for the insurance is provided by TradeMe but the insurer is Tower Insurance. Many banks operate similar models which the FSF believes could be misleading for the policyholder.
- There is increasing demand from consumers to access all financial services products via on-line channels and this is certainly also true for insurance products. Any review of current legislation should take this into consideration and ensure that it is sufficiently future-

proofed to allow for changes in the way consumers access products whilst providing them with all necessary protections.

**3. Do you consider that there are entities where the current provisions of the legislation result in inappropriate compliance costs or inappropriate regulatory obligations relative to the risks being addressed by the legislative framework?**

The relevant FSF members are of course sensitive to IPSA compliance costs and the level of their regulatory obligations, but are nevertheless broadly comfortable with the current IPSA regime, and would not describe it as “inappropriate” in such respects.

**4. Are you aware of any currently non-licensed (under IPSA) insurance business activity in New Zealand that you consider should be within the scope of regulation in some form to enhance the effectiveness of the framework?**

The FSF is not aware of any currently non-licensed (under IPSA) insurance business activity in New Zealand that could be considered within the scope of regulation in some form to enhance the effectiveness of the framework.

However the FSF notes with interest that Para 47 of the Issues Paper makes reference to some form of notification or data reporting framework potentially being required if full licensing is disproportionate to the risks presented by the activity and would be interested to know more about what that might entail. At that time the FSF would be in a better position to make more meaningful comment on this issue and relevant FSF members would certainly be interested in doing so.

**5. Do you agree that overseas insurers provide valuable support to the New Zealand insurance market? Please provide commentary in support of your view.**

The FSF refers to the answer provided under question 2 above with respect to the vital role fulfilled by reinsurers in the New Zealand insurance market.

**6. Do you consider that the Review should reassess the application of the legislation to insurers operating as branches? Please provide commentary in support of your view.**

The FSF supports the IPSA in its current form and contends that it has done a lot to protect New Zealand consumers compared to the situation they were in before its enactment.

That said, the FSF accepts that to some degree the system stability issues that have led to the RBNZ’s local incorporation policy in respect of banks may also apply in respect of some foreign-incorporated insurers. While the FSF is not necessarily presently advocating such a policy in connection with IPSA, it can see that the issue may warrant further study.

**7. In the context of overseas insurers, what do you consider are the most significant risks posed to the New Zealand economy or New Zealand policyholders that need to be taken into account?**

This issue overlaps with matters of the kind addressed by Q6 above.

**8. Do you consider that there is opportunity to clarify or enhance the effectiveness of the statutory fund framework? Please provide commentary in support of your view.**

The FSF suggests there is no demonstrated need to enhance the statutory fund framework, and that the RBNZ should leave it as it is.

**9. In the context of overseas insurers, do you consider a statutory fund framework may help protect the interests of New Zealand policyholders? Please provide commentary in support of your view.**

On the basis of the above response to question 7, the FSF would support the idea of some form of “assets in New Zealand test” potentially in conjunction with a statutory fund type of arrangement for overseas insurers.

**10. Do you consider that the expectations placed on the directors, chief executive officer, chief financial officer or appointed actuary of insurers, would benefit from being considered further within the Review? This may include clarifications of current expectations or expansion of responsibilities.**

The FSF’s credit-related insurance provider members report that the current framework works well from their perspective. They report that it has created sound governance through appropriate segregation of duties and a risk management framework review among other things. They also believe that good governance processes and compliance programmes benefit both the business by way of best practice as well as being of benefit to consumers in dealing with well-run companies.

In this regard the FSF would also like to record its members agreement with the statement in para 85 that “the relatively low levels of prescription in the current framework provide a degree of flexibility” which they see as desirable in the interest of both effective regulation and an efficient insurance sector. Further prescription might undesirably limit that flexibility.

**11. Do you consider that the Review should encompass further consideration of an insurer’s key control functions (paragraph 84) to promote effective risk management and consistent application of requirements across the sector?**

The FSF supports the key control functions as they are described in Para 84 and does not see any need to extend requirements beyond those listed in this Para.

It should also be remembered that insurers are also subject to a number of controls from the likes of internal and external auditors and actuaries.

**12. Do you consider that there may be opportunities to enhance the enforcement framework? Please provide comment in support of your view.**

The FSF does not believe that there is any evidence to suggest that there is a need to enhance the range of enforcement sanctions that are available within the current framework.

**13. Do you consider the distress management framework within IPSA could be considered within the Review to enhance the expected effectiveness of the framework, particularly for smaller licensed insurers?**

With regard to the issues referred to in para 101 of the Issues Paper, the FSF agrees that processes to achieve a quick and efficient exit of smaller licensed insurers that are experiencing difficulties are likely to be in the interests of the industry and of policy holders, and therefore may be deserving of further study.

**14. Are there any areas of the framework that may pose particular concerns when considering overseas insurers (branch operations)?**

The areas of concern for New Zealand branch operations of overseas insurers are likely to be the same cross-border issues that exist in many other sectors of the economy, including banking. The FSF notes that such considerations led to the local incorporation policy in respect of banks, and thus sees some overlap between this question and Q6 above.

**15. Do you consider that the current approach to prudential capital requirements by reference to a solvency margin and conditions of licence should be within scope of the Review? Please provide commentary in support of your view.**

As noted in para 107 of the Issues Paper the technical content of the current regime is not within the scope of the review, as the review is concerned with matters that may require legislative change. The FSF is comfortable with the current scope of the review, and its relevant members do not see a present need to address the technical content of the current regime at the level of specific methodologies etc.

**16. Do you consider that consideration should be given to clarifying the Reserve Bank's prudential response to deteriorations in reported solvency levels? Please provide commentary in support of your views.**

In part this depends on the scope of the Review, addressed in Q15 above. Assuming that solvency levels were to be in scope, the FSF sees no need to clarify the RBNZ's prudential response to deteriorations in reported solvency levels. It sees it as being preferable to retain the degree of flexibility that is referred to in para 108 of the Issues Paper.

**17. Do you consider the Review should reassess the current framework for approval of material transactions and policy changes? Please provide commentary in support of your view.**

If as is suggested in the second bullet point in para 124 of the Issues Paper it really is possible to undertake some regulated material transactions in ways that are beyond the current regime, clearly that would be a concern. Otherwise, the FSF sees no need to reassess the current framework for approval of material transactions in any substantive way.

**18. Do you consider that approval by the Reserve Bank is more or less effective than alternative mechanisms e.g. court based systems?**

Yes, RBNZ approval is likely to be more effective than alternatives such as a court based system. Specialised prudential supervision is in the FSF's view preferable to a non-specialised judicial system. That is not to say that recourse to the courts by means of an appeals process at some stage or by judicial review should be excluded, and the Act presently makes adequate provision for that.

**19. Are there any aspects of the current disclosure requirements that you consider do not provide useful information or are unduly onerous or costly to prepare? Please provide commentary in support of your view.**

The FSF suggests the consumers do not find financial ratings to be helpful – in fact the experience with finance company ratings during the Global Financial Crisis proves that they can in fact be misleading to the public because of a lack of understanding of what they mean. Ratings are also only provided once per annum and are therefore a snapshot in time whereas solvency reporting requires ongoing monitoring and is therefore far more relevant to the public when assessing the stability of an insurance provider.

**20. Do you consider that there is information that is not currently required to be disclosed that would be beneficial to market participants? Please provide commentary in support of your view.**

The FSF is not aware of any such information that is not currently required to be disclosed.

**21. Do you consider that the Reserve Bank (or other authority) has a role in providing appropriate industry data to the market? Please provide commentary in support of your view.**

In principle, yes the RBNZ may have such a role. The existence of a prudential system is itself to some extent already a recognition that Government has a public responsibility in respect of the health of the sector, and if communicating appropriate industry data to the market further helped to promote public confidence in the industry, that would be a good thing.

The FSF suggests however that care would need to be taken not duplicate existing individual reporting so that any such industry data enhances rather than duplicates information already available. Any such data should also be provided on an aggregated basis rather than identifying individual insurers.

**22. Do you consider that the Review should reassess the manner in which requirements are currently specified and the mix between requirements set out in legislation, standards or guidance? Please provide commentary in support of your view.**

The relevant FSF members have no strong view on whether requirements are specified in legislation, standards or guidance – either way they must comply with them however the more places in which insurers are required to look to provide information as to their obligations, the more complex it becomes for them to keep up with all information channels.

**23. Are there any aspects of the current requirements that you consider would be better specified using different regulatory tools?**

There are no such matters.

**24. Are there any further issues you would like to raise that you consider should be within scope of the Review? Please provide commentary in support of your view.**

There are no further issues the FSF wishes to raise regarding the scope of the Review.

**25. Are there any areas of the legislation that you consider are now redundant or you feel could have clearer drafting or require technical corrections?**

There are also no further issues the FSF wishes to raise about this question.

**26. Are there any areas of the legislation that you consider, having regard to the purposes of the legislation, unduly restrict competition or innovation within the New Zealand insurance market? Please provide commentary in support of your view.**

The FSF's final point on the IPSA Review is that the current regulation does not restrict competition or innovation which is as it should be as these are areas that should not be controlled by regulation in any event.

The FSF would be happy to further discuss these or any other points with regard to this Review if that would be helpful.

Yours sincerely

A handwritten signature in blue ink, appearing to read "Lyn McMorran".

Lyn McMorran  
EXECUTIVE DIRECTOR



Membership List as at 7<sup>th</sup> June 2017

**Appendix A**

Debenture Issuers - (NBDT) Non-Bank Deposit Takers	Vehicle Lenders	Finance Company Diversified Lenders	Credit Reporting Other	Insurance	Affiliate Members
<u>Rated</u> Asset Finance (B) Flexi Cards (BB+)	BMW Financial Services Branded Financial Services Community Financial Services Go Cars Finance Ltd European Financial Services Honda Financial Services Ltd Mercedes-Benz Financial Services Motor Trade Finance Nissan Financial Services NZ Ltd Onyx Finance Limited Toyota Finance NZ Yamaha Motor Finance <u>Leasing Providers</u> Custom Fleet Fleet Partners NZ Ltd ORIX NZ SG Fleet Lease Plan	L & F Holdings (Trading as Advaro Limited) Avanti Finance Caterpillar Financial Services NZ Ltd Centracorp Finance 2000 Finance Now Future Finance Geneva Finance Home Direct Instant Finance John Deere Financial Latitude Financial Personal Finance Ltd South Pacific Loans The Warehouse Financial Services Group Thorn Group Financial Services Ltd Turners Finance Limited	VEDA Advantage <u>Debt Collection Agencies</u> Baycorp (NZ) Consumer Credit Management Limited Dun & Bradstreet (NZ) Limited Centrix	Autosure Pioneer Finance Protecta Insurance Provident Insurance Corporation Ltd Southsure Assurance	American Express International (NZ) Ltd AML Solutions Buddle Findlay Chapman Tripp EY Finzsoft KPMG PWC SimpsonWestern  (Total : 56 members )