FINANCIAL SERVICES FEDERATION

28 May 2021

Chairperson
Economic Development, Science, and Innovation Committee
New Zealand Parliament
Wellington

Dear Chairperson

The Financial Services Federation (FSF) is grateful to the Select Committee (Committee) for the opportunity to provide feedback with respect to the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill (the Bill).

By way of background, the FSF is the industry body representing responsible non-bank lenders, fleet and asset leasing providers and credit-related insurance providers. We have over 60 members and affiliates providing these products to more than 1.5 million New Zealand consumers and business. Our affiliate members include internationally recognised legal and consulting partners. A list of our members is attached as Appendix A. Data relating to the extent to which FSF members (excluding Affiliate members) contribute to New Zealand consumers, society and business is attached as Appendix B.

The FSF submitted on the 2019 discussion document released by the Ministry of Business Innovation and Employment and the Ministry for the Environment and we are pleased to see many of the concerns the FSF raised then have been addressed in the Bill. However, there are some outstanding concerns which have not been adequately addressed in the current Bill in the FSF's view and therefore FSF respectfully asks that these be considered by the Committee.

Before making these comments, however, the FSF congratulates both the Ministry of Business, Innovation and Employment and the Ministry for the Environment, alongside the Committee and all officials involved for the continued foresight and progression towards appropriately addressing the material risks climate change possesses to our economy and Aotearoa. Having such a greater wealth of information will help ensure better and more sustainable decisions are made in the financial sector, and forward.

Members of the FSF recognise the material risks that climate change poses, and FSF members have demonstrated this stance by their involvement in initiatives aimed at developing a more sustainable and accessible finance sector. This is through FSF member involvement in the 2018 financial inclusion forum and since in the Safer Credit and Financial Inclusion Partnership which includes Government agencies such as MBIE, MSD, Te Puni

Kokiri and others; community agencies such as Good Shepherd, FinCap etc; and industry including FSF members and banks. The SCAFI Partnership has a number of goals to provide a more accessible and inclusive and also sustainable financial services sector in Aotearoa New Zealand.

Despite our overall agreement with the need to progress towards a sustainable financial system and future, the FSF outlines the following significant concerns with the Bill in its current form.

High level analysis

The FSF is in support of more progressive steps towards rectifying and resolving the detriments that will continue to cause havoc from the effects of climate change. However, there are major concerns across all relevant industries regarding the speed with which this Bill and relevant standards are being implemented and regulated.

Lack of warning or engagement
Many, if not most, captured entities have no operations or plans for such a regulatory requirement of disclosure. Consequently, many entities have nothing prepared in response to this regulation and are only now becoming increasingly concerned in regard to the narrow timeframe and rigidity of this proposed regime.

The FSF echo the submissions of many other industry bodies in their encouragement of the Government and the XRB to collaborate further with financial institutions and businesses to create simpler and more time wise requirements, and not the imposition of such a stringent punitive regime with such exceedingly harsh penalties. We do not disagree with the imposition of such a regime – the FSF believes it is a necessity – however we urge for some proportionality and reasonableness to be integrated into the regime.

The critical need for a transition period
Firstly, the standards that are to be issued by the XRB will not be finalised until late next year, with implementation and regulation to then happen early the following year. The requirement for full and comprehensive disclosure so soon after standards are finalised does not give entities sufficient time to respond, let alone build the appropriate systems to collect data required and forecast the relevant information.

It is this narrow timeframe for compliance and implementation that warrants our request for a more graduated approach to be adopted to implementation. It is critical that disclosure gradually accumulates to full and comprehensive disclosure, as opposed to initially being full and comprehensive. The FSF urges that partial disclosure be encouraged and accepted in the initial stages of the implementation of the regime, and entities can gradually accumulate their disclosures to a full and comprehensive standard, as the development of systems respectively evolve to meet the standards imposed.

This request is especially supported by the point that many climate related risks are often identified ex-post as opposed to being forecast.

The FSF also believes that more work needs to be done by the scientific community and entities like the Climate Change Commission to inform the vastly complex scenario analysis that needs to be applied to reporting entities to determine their climate-change risks. The requirement to report on climate change issues is a very novel one for the entities who will be required to do so by this regime. They require a scientific basis on which to understand the risks they face and how to manage these. Without this scientific basis such information is even more difficult to report on and this is further reason why the FSF believed it is therefore necessary to give entities a transitional period to respond to the Bill appropriately, as opposed to full initial implementation paired with disproportionate penalties.

Furthermore, in the previous discussion document released in 2019 by MBIE and MoE, some leeway was proposed for some companies that did not feel as though they could meet disclosure fully against the TCFD framework at the time due to insufficiently clear dates. Those entities would be required to include a statement to this effect in their annual report with the proviso that they are expected to report fully in the following year's annual report.

The removal of this leeway in the current Bill is very disappointing to the FSF. Other submissions on the discussion document echoed agreement for such leeway and the FSF queries why it has been removed from the Bill in its current form. A transitional period is undoubtedly possible (as articulated in the 2019 discussion document), and it would be well received, thus, the FSF see no plausible reason as to why it should not be incorporated into the Bill.

Finally, in our argument for a transitional period, the FSF urges the Committee to consider the other extensive reform under way in the financial services sector. The Credit Contracts and Consumer Finance Act, amendment regulations and Code are all required to be complied with by 1 October this year. Compliance with these instruments by 1 October has been putting significant pressure on Non-Bank Lenders and Banks, and the FSF is concerned that serious health and safety issues will arise for employees of these entities being under such pressure to be fully compliant with such a complex piece of legislation within such a tight timeframe.

Certification for Directors and Senior Managers of consumer credit providers as being fit and proper persons is also looming, alongside forecast massive reform to Insurance Contract Law and the Reserve Bank Act reviews. Reform and amendments to comply with these regimes is hugely significant. With the additional narrow timeframe proposed under this Bill, this will put even more pressure on such entities than ever before.

The FSF, alongside all other relevant industry bodies, forecasts significant issues resulting if the Bill and its implementation is rushed through as is currently proposed. We therefore encourage our submissions to be considered seriously as a result of these forecast issues.

Collection of data (in relation to the need for a transitional period)
The collection of data will be a significant issue. Large institutions such as the TCFD and the Climate Change Commission have both proven to find difficulty in collating and presenting data related to the risks and effects of climate change, for the basis of their recommendations.

It is most certain that smaller entities, with resources and capabilities nowhere near as vast, will struggle to harvest and produce relevant data. Their room for error is significantly larger. Bearing in mind the large penalties, and lack of transitional period available to such entities, this is shifting a large and frightening onus on regulated entities to comply. Such a forecast issue provides more rationale for the necessity for a transitional period, so entities are able to build appropriate capabilities to meet the standards required.

Reputational effects
Many entities caught in this regime will be involved with the financing of vehicles. Unfortunately, presently in Aotearoa there is minimal supply of electric vehicles to meet the demand for them. Vehicles which are financed in Aotearoa are therefore predominantly fossil fuelled. The books suggest that less than 1% of vehicle financing is for electric vehicles. It is not plausible for all lending institutions to finance only electric vehicles now as the entire sector would fail.

Disclosure on matters such as this will prove to be reputationally detrimental on those entities which cannot mitigate such effects themselves. Their books finance what is available on the market, and what is currently available is not always climate friendly. The FSF is concerned, in this regard, that rather than promoting awareness and mitigating the risks of climate change, entities will be forced to disclose reputationally damaging information all whilst an opportunity to facilitate any change ceases to exist.

As the Budget 2021 noted, a significant amount of money has been allocated to the facilitation of the uptake of low emission vehicles. With this in mind, the FSF urges officials to look at the supply of electric vehicles first prior to forcefully regulating those entities who have no opportunity to finance electric vehicles. As those who are in the business of financing such products who possess material climate risk, do not proactively have any choice in whether such risk is able to be minimised until further supply and demand issues are resolved.

Legislative analysis

The FSF welcomes section 461P of the Bill, as this ensures that those regulated are those which have more of a capacity to report such disclosures. The notion of “influence” is well regarded within this provision, and the FSF concurs that it is most critical that those with “influence” are those required to provide such disclosures; their facilitation of climate risk awareness is to be more extensive than those smaller to medium entities.

461R Miscellaneous provisions relating to application
This provision states that if a person ceases to be a climate reporting entity during an accounting period, that person must be treated as continuing to be a climate reporting entity in relation to that period for the purposes of this Act.

The FSF queries the rationale behind this provision. If a person loses assets or the criterion which then makes them of sufficient influence to be defined as “large” and therefore a climate reporting entity, this could be an indication of potential hardship.

The climate related financial disclosures will no doubt require much intense resource to harvest and produce the relevant data. The systems to comply with the legislation will be ongoing and costly. If an entity is currently in a position of hardship, the FSF proposes that a better alternative would be to not require them to continue climate-change financial reporting. If hardship occurs early in the accounting period, the continuation of the reporting requirement may reduce resilience in the entity and catalyse further hardship.

From this rationale, the FSF suggests an amendment to this subsection of the Bill. Instead to read:

> "*461R Miscellaneous provisions relating to application*
> *(1) if a person ceases to be a climate reporting entity during an accounting period, that person**, unless notice is given under (3),** must be treated as continuing to be a climate reporting entity in relation to that accounting period for the purposes of this Act and every other enactment*"

From this amendment, a further subsection, with an exemption could be provided in this section which allows for the opportunity for entities in hardship to no longer be required to produce such reports.

> **"(3) where a person can show that ceasing to be a climate reporting entity has occurred as a result of material hardship, then that person shall only report up to the date that the person ceased being a climate reporting entity".**

The FSF understands an exception as such would be the more just and equitable approach to when a person ceases to be a climate reporting entity. However, if the Committee finds that for whatever reason such an exception may not be beneficial, then the FSF proposes partial exemptions as alternatives to rectifying this issue.

Firstly, the Committee can adopt amendments to the drafting of this section which then would not require those climate reporting entities, who have ceased to be climate reporting entities, to have their climate reports audited in the circumstances of no longer being a climate reporting entity. This aids in the avoidance of the onerous costs coupled with auditing the entities' report.

Otherwise, the FSF also suggests that reducing the level of disclosure in this circumstance of no longer being a climate reporting entity, also removing the onerous costs associated with the auditing requirement. Partial disclosure on high-level aspects would be most appropriate, as an investment into forecasting niche and scientifically based data may be considered redundant information if the entity is no longer in a position of 'influence'.

The FSF urges the Committee to adopt and consider the alternative suggested drafting or partial disclosure requirements in order to address the potential significant issues that may result from entities in hardship having to continue with the resource intensive and onerous costs of continuing to comply with the disclosure standards.

461ZA Exceptions for climate reporting entities not materially affected by climate change
The FSF submits that the exceptions presented in this section are well received and agreed with. However, the FSF requests further clarification on the timeframes that this exception possesses. It is clear that this exception should be relied on for an accounting period. With further reading, it becomes vaguely clear that these exceptions are to be reapplied for every accounting period. However, the FSF recommends that the timeframes for reapplication of the exception should be made more explicitly clear to promote the usability of the Bill.

The most obvious route to resolving this ambiguity would be for an additional subsection to section 461ZB Conditions applying to exceptions. This proposed subsection (d) could read as follows:

> "*461ZB (1) (d) A follows this procedure for each accounting period that it wishes the exemption to apply for*."

461ZC Offence to knowingly fail to comply with climate standards
The penalties outlined in this section appear to be very high. The FSF is uncertain as to whether failure to comply with the standards is proportionate to the high penalties.
As outlined in our prior high-level comments on the Bill, which emphasis the transition into full comprehensive reporting to be difficult and intensive for regulated entities, compliance attempts should not be met with such high penalties.

The penalties outlined echo harsh punitive connotations. For the purposes of this Bill, that being the promotion and facilitation of awareness to climate change and its risks, the FSF suggests a more appropriate approach would be to encourage and educate entities to comply rather than holding over them the threat of punitive penalties. Entities already recognise the material impact climate change has and will have on their business, and it is rare to find an entity which does not recognise this, particularly one that will be defined as a "climate reporting entity".

It is with these comments in mind that the FSF requests the Committee to put forward recommendations and amendments to this section in reflection of a more proportionate approach to penalties.

The FSF suggests the approach of a "transitional period", in which minimal or nil penalties are imposed on those entities which have attempted to comply with the disclosure requirements, in recognition of the narrow timeframe and resource intensive processes that will be required for compliance. Without any amendment to the penalties section of the Bill, the FSF has grave concerns regarding entities, which may not have the capabilities that larger entities have, and their vulnerability for penalties and consequent hardship.

Concluding remarks

Thank you again for the opportunity to provide the FSF's view on the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill. We look forward to seeing the Committee's response to ours, and other industry bodies', submissions.

Please do not hesitate to contact me if you wish to discuss the submission any further.

Yours sincerely,

Diana Yeritsyan
Legal and Policy Manager

Appendix A – FSF Membership List February 2021

Non-Bank Deposit Takers Leasing Providers	Vehicle Lenders	Finance Company Diversified Lenders	Finance Company Diversified Lenders	Credit-related Insurance Providers	Affiliate Members
<u>Rated</u> Asset Finance (B) <u>Non-Rated</u> Mutual Credit Finance Gold Band Finance ➢ Loan Co <u>Leasing Providers</u> Custom Fleet Fleet Partners NZ Ltd Lease Plan ORIX NZ SG Fleet	AA Finance Limited Auto Finance Direct Limited BMW Financial Services ➢ Mini ➢ Alphera Financial Services Community Financial Services European Financial Services Go Car Finance Ltd Honda Financial Services Mercedes-Benz Financial Motor Trade Finance Nissan Financial Services NZ Ltd ➢ Mitsubishi Motors Financial Services ➢ Skyline Car Finance Onyx Finance Limited Toyota Finance NZ Yamaha Motor Finance	Avanti Finance ➢ Branded Financial Caterpillar Financial Services NZ Ltd CentraCorp Finance 2000 Finance Now ➢ The Warehouse Financial Services ➢ Southsure Assurance Future Finance Geneva Finance Home Direct Humm Group Instant Finance ➢ Fair City ➢ My Finance John Deere Financial Latitude Financial Metro Finance Pepper NZ Limited Personal Loan Corporation Pioneer Finance Prospa NZ Ltd South Pacific Loans	Speirs Finance Group ➢ Speirs Finance ➢ Speirs Corporate & Leasing ➢ Yogo Fleet Thorn Group Financial Services Ltd Turners Automotive Group ➢ Autosure UDC Finance Limited <u>Credit Reporting & Debt Collection Agencies</u> Baycorp (NZ) ➢ Credit Corp Centrix Collection House Equifax (prev Veda) Illion (prev Dun & Bradstreet (NZ) Limited Intercoll Quadrant Group (NZ) Limited	Protecta Insurance Provident Insurance Corporation Ltd	255 Finance Limited Buddle Findlay Chapman Tripp Experian EY FinTech NZ Finzsoft GreenMount Advisory Happy Prime Consultancy Limited HPD Software Ltd KPMG LexisNexis PWC Simpson Western Total: 65 members

Appendix B

FINANCIAL SERVICES FEDERATION

The Financial Services Federation (FSF) is the association for responsible finance and leasing companies operating in New Zealand. This infographic is a snapshot of our 40 lending members, the membership list can be found at our website www.fsf.org.nz.

Consumer Lending	Business Lending
1.6 million # Consumer Loans	**172,4000** # Businesses Loans
$7.5 billion Total Assets	**$7.6 billion** Total Assets

Consumer Lending		Business Lending	
$355,039,962 Secured	$2,996,322,244 Unsecured	$609,678,636 Secured	$79,625,359 Unsecured
$2,484,376,195 Motor Vehicle	$654,604,625 Mortgage	$4,134,085,468 Motor Vehicle	$133,896,221 Mortgage
		$186,477,244 Operating Lease	

FSF lending members data survey period as at 29 February 2020 . Data collected and aggregated by KPMG. Values in NZ$.