

Submission

to the

Financial Markets Authority

on the

Consultation Paper: Proposal for annual declaration of compliance for Financial Market Conduct Act 2013 licensees

21 December 2015

Submission by the New Zealand Bankers' Association to the Financial Markets Authority on the Consultation Paper: Proposal for annual declaration of compliance for Financial Market Conduct Act 2013 licensees

About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes which contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.
2. The following fifteen registered banks in New Zealand are members of NZBA:
 - ANZ Bank New Zealand Limited
 - ASB Bank Limited
 - Bank of China (NZ) Limited
 - Bank of New Zealand
 - Bank of Tokyo-Mitsubishi, UFJ
 - Citibank, N.A.
 - The Co-operative Bank Limited
 - Heartland Bank Limited
 - The Hongkong and Shanghai Banking Corporation Limited
 - JPMorgan Chase Bank, N.A.
 - Kiwibank Limited
 - Rabobank New Zealand Limited
 - SBS Bank
 - TSB Bank Limited
 - Westpac New Zealand Limited.

Background

3. NZBA is grateful for the opportunity to submit to the Financial Markets Authority (**FMA**) on the Consultation Paper: Proposal for annual declaration of compliance for Financial Market Conduct Act 2013 licensees (**Consultation Paper**) in relation to the Financial Markets Conduct Act 2013 and the Financial Markets Conduct Regulations 2014 (**the FMC Act regime**).
4. The process around the development of the FMC Act regime has been a good example of policy development that has actively involved the industry. NZBA commends the ongoing commitment to meaningful consultation and engagement and appreciates the invitation to participate in this consultation.
5. The following submission provides responses to the questions posed in the Consultation Paper.
6. If you would like to discuss any aspect of the submission further, please contact:

Antony Buick-Constable
Policy Director & Legal Counsel
04 802 3351 / 021 255 4043
antony.buick-constable@nzba.org.nz

Executive summary

7. NZBA and its members do not support the proposed annual declaration of compliance standard condition (**Declaration**), and submit that the compliance burden associated with producing the Declaration is not justified, given that it offers no practical increase in consumer protection, and there are already strong continuous disclosure obligations on participants.
8. If the Declaration is implemented, directors should not personally be required to sign it (because it is ultimately the entity providing the service and any person duly authorised should be able to sign), and it should be accompanied by a materiality threshold.
9. The proposed timeframe for making the Declaration is too short and does not reflect the internal review and approval process that large financial institutions undertake.

Question 1: Do you agree that the requirement to complete an annual declaration of compliance is consistent with the reasons stated above?

10. NZBA and its members do not support the Declaration and do not agree that its production is justified based on the reasons set out in the Consultation Paper.
11. The Declaration is not supported because:
 - a. It unnecessarily duplicates existing obligations, and therefore provides no additional protection to consumers with respect to the services provided by licensees.
 - b. The compliance burden imposed by the Declaration would be out of proportion to any perceived benefit(s).
 - c. The Declaration over-emphasises the provision of the certificate, rather than placing emphasis on the policy requirement of continuous compliance, evidenced by the provisions of the FMC Act.
 - d. The implementation of a Declaration of this nature is a policy decision that should be considered by the government and if appropriate, included in the primary legislation.
12. Material breaches of standard conditions must already be notified to the FMA under section 412 of the FMC Act. Under that section a licensee must:

- a. Have in place effective methods for monitoring compliance with its market services licensee obligations and identifying **material** changes in circumstances; and
 - b. Provide a report to the FMA if it believes it has contravened, may have contravened, or is likely to contravene a market services licensee obligation in a **material** respect.
13. Under section 6 of the FMC Act, a market services licensee obligation includes an obligation imposed by a licence condition. Thus the FMC Act already ensures that the FMA receives accurate information on a regular basis about licensees' compliance with their conditions.
14. Section 412 means that licensees should be focused on continuous monitoring, rather than the provision of an annual confirmation as proposed by the Declaration. As there is already a positive obligation on licensees to continually update the FMA as to the status of their compliance with their licence, the Declaration is unnecessary.
15. Further, entities must have met the FMA's minimum standards to have obtained a market services licence. This includes a requirement "to maintain effective methods for identifying and reporting to the FMA any material change of circumstance or breach of your market services licence obligations". The FMA should therefore have gained assurance through the licensing application process that licensees have effective processes and procedures in place to comply with their continuous monitoring obligations under section 412.
16. The Declaration will also duplicate information that will be required to be reported to the FMA in future as part of the Regulatory Return (see the response to question 5 below).
17. In addition, NZBA and its members believe that the Declaration will achieve the aim of ensuring that 'compliance is on the agenda of licensees' governing bodies each year' only in the narrowest sense. While NZBA and its members sympathise with the FMA's approach of looking for senior sponsorship of compliance and appropriate culture, requiring a Declaration of this sort is unlikely to achieve that aim. Such a Declaration risks putting the emphasis on the process for supporting that Declaration. At a recent seminar discussion with the FMA's CEO, the emphasis seemed more realistically to be on encouraging senior management consideration of risk appetite, and review and challenge of relevant dashboard information. This, along with the FMA's current approach of engagement with senior management through relationship meetings and through monitoring seems more likely to achieve this objective.

Question 2: Who should sign the annual declaration? Should the directors personally be required to sign it or is it more appropriate for it to be executed by management under a standing power of attorney?

18. This question assumes that the Declaration will be introduced, which for the reasons outlined above, we strongly disagree with. Notwithstanding the response to question 1 above, we make the following observations around signing of the Declaration.
19. NZBA and its members submit that if introduced, the Declaration should not be required to be signed personally by directors. Directors' availability to sign documents can be problematic outside regular Board meetings, particularly where the licensee is incorporated overseas.
20. The Declaration should be given by the licensee, so should be capable of being executed in any manner permitted by the licensee's corporate governance structure.
21. The proposed approach also seems at odds with the more flexible approach in licensing materials regarding 'governing bodies' – enabling firms to choose bodies with appropriate levels of seniority and involvement for the size of the firm. This recognises the strategic nature of the Board's role in larger organisations (see also paragraph 17 above). To require director attestation runs counter to the delegation of oversight that the FMA has previously required be implemented through the licensing process.
22. Requiring Board sign off on a Declaration to this effect is not appropriate for large organisations, especially where these entities are already comprehensively regulated by other regimes such as prudential regulation and the QFE regime. If there is a risk of non-compliance which cannot be mitigated through the licensing process for particular licensees, then the FMA has an existing power to take a risk-based approach and impose specific license conditions on those entities that it considers appropriate to require a Declaration of compliance.

Question 3: Do you have any comments on the cost and business impact (including the impact on the governing body) of providing this declaration to the FMA?

23. As the Declaration confirms information that the FMA should have in any event (i.e. any material breaches should have already been reported, for the reasons set out above) the compliance costs involved in producing the Declaration are not justified.
24. Providing a Declaration of the type proposed will require an internal attestation to validate it for the Board. The experience of NZBA members (for example, in relation to Financial Advisers Act 2008 (**FAA**) and Reserve Bank of New Zealand Act 1989 declarations) is that attestation processes can be time-consuming and labour intensive, requiring input from both operational and compliance staff. For example, in a larger organisation it may involve multiple managers within the bank and papers for

several committees, therefore involving a lead time of several months. Time may be absorbed in completion of attestations and management of process, rather than on value-adding with respect to compliance.

25. Since the most that can be expected as a result of the Declaration is that the FMA receives a series of disclosures about non-material matters (noting that material matters should already have been reported), the view of NZBA and its members is that the costs associated with the Declaration are disproportionate to any perceived benefits.
26. We are not aware that the FMA has made significant use of the equivalent report required under the FAA. Our members have submitted these reports for a number of years with limited feedback received individually or on an industry trend basis. Instead, the FMA could explore other breaches as part of its monitoring visits, if necessary.
27. We are surprised that the FMA wishes to invest more of its own resources in a regulatory approach which is not risk-based and might seem focused on assisting with enforcement action. The FMA is likely to need to consider every report that it receives, regardless of its evaluation of risk. Given the FMA's limited resources, this seems likely to reduce its ability to actively monitor or engage with the industry in more positive ways.
28. Given that the proposal is an addition to existing conditions, we understand that it would be in line with the FMA's policy to consider publishing a Regulatory Impact Statement, providing a view of costs and benefits.

Question 4: Should the scope of the declaration be wider than stated? For example, should it cover **all** of the licensee's obligations under the FMC Act? Or all legislation regulated by the FMA? (Rather than only compliance with licence conditions?)

29. No. The comments made above apply even more cogently to a wider Declaration. The legislation already provides adequate reporting requirements, consequences and remedies for failure to observe the licensee's obligations under the FMC Act. A wider Declaration would merely increase the compliance burden for no additional benefit.
30. In particular, the proposal that the Declaration cover all of the licensee's obligations under all legislation regulated by the FMA seems extreme, and it is unclear what the FMA would be seeking to achieve through such a requirement.

Question 5: Should the declaration be made as part of the Regulatory Returns standard condition in the future or should it remain as a standalone requirement? Is it relevant that the directors sign the declaration but management is likely to sign the Regulatory Return?

31. The Consultation Paper states that the Declaration will ensure that "we [the FMA] receive accurate information on a regular basis to confirm licensees are complying with the FMC Act". This information could be obtained under the existing Regulatory Return standard condition. It is anticipated that when the Regulatory Return is published it will cover information about number and types of breaches and complaints.
32. NZBA and its members submit that the FMA should publish the Regulatory Return first before introducing a new requirement to provide a Declaration. The Regulatory Return and other reporting requirements should provide the FMA with sufficient information to support its monitoring functions. Unless there is some evidence to suggest that licensees are not complying with their regulatory reporting obligations and that this cannot be rectified through appropriate enforcement action, it would be premature to introduce a Declaration at this juncture.
33. If the Declaration is implemented in its current form, it should not be made part of the Regulatory Return.

Question 6: Do you have any comments on the proposed form?

34. See the response to question 2 above regarding who should sign the form.
35. The form does not expressly state that the signatories sign the form on behalf of the licensee. NZBA and its members submit that a possible consequential extension of personal liability to the signatories is contrary to the spirit of the legislation, where personal liability is reserved for culpable acts and we assume this cannot have been intended under the Declaration.

Question 7: How should this form be provided to the FMA? What is your preferred method for submitting the form? (For example: electronic PDF, physical copy or other (please specify)).

36. If implemented, the Declaration should be provided to the FMA by electronic PDF.

Additional comments

37. The proposed standard condition requires that the Declaration to the FMA be provided within 3 months of the licensee's balance date each year. NZBA and its members submit that licensees should have greater flexibility around when they submit the Declaration.

38. Licensees should be able to adopt a date to provide their Declaration by notifying that date to the FMA. This would allow licensees to:
- leverage existing attestation processes for other reporting requirements;
 - time for the provision of the Declaration to minimise disruption to their businesses;
 - integrate the Declaration with more holistic consideration of compliance risk management in the licensed area; and
 - avoid times when governance bodies are often occupied with matters relating to disclosure of results and supporting processes.
39. Maintaining the current timetable is likely to reduce the effectiveness of the requirement as a method of achieving senior management consideration and sponsorship of compliance.
40. Alternatively, to mitigate against the restrictive nature of the proposed 3 month time frame, the Declaration should be required to be provided to the FMA within 5 months of the licensee's balance date each year, which would align with QFE requirements.
41. NZBA and its members also submit that, if it is implemented, the Declaration should be accompanied by a materiality threshold, i.e. require that the licensee declare that it has complied with the conditions of its licence in all material respects.