

1 May 2018

Adrian Orr
Governor
Reserve Bank of New Zealand

Rob Everett
Chief Executive
Financial Markets Authority

By: email

Dear Adrian and Rob

Re: New Zealand banking industry response to Australian Royal Commission

On behalf of the NZBA Council,¹ thank you for last night's constructive meeting with you both, and the Banking Ombudsman.

Your points on publicly clarifying the differences in banking culture between New Zealand and Australia, and providing evidence of that, were well made and understood.

The banking industry strongly supports regulatory cooperation on this matter, which given the matters emerging in Australia, is entirely warranted. If there are further questions arising from your Council of Financial Regulators meeting tomorrow, you have our commitment that we will respond as a priority.

While we believe there are indicators of strong culture in New Zealand banking, as evidenced through our open and constructive regulatory engagement in relation to BKBM, as well as regulator, industry and government cooperation to develop the customer-focused Financial Services Legislation Amendment legislation, we are not being complacent about Royal Commission matters. We will work openly and constructively with you.

Ultimately decisions about regulatory responses rightfully rest with you and you have our commitment that we will support any response and ensure this is communicated appropriately. The public has a right to expect assurance and we acknowledge the key role we play in delivering that message.

¹ Please note The Hongkong and Shanghai Banking Corporation Limited (Limited) has not taken part in Council discussions on this matter, and is not involved in this workstream.

We set out below a summary of our agreed position on an initial collective industry response and approach. Additionally, each of the four largest banks will separately provide you with information about the work they are undertaking to show what is happening in Australia is not happening here. They have undertaken to provide that information in advance of your meeting with the Council of Financial Regulators. We have included contact details of senior staff leading that work as **Attachment 1** to this letter.

As discussed last night, our member banks also undertake to continue to work closely with you on these issues and engage in free and frank discussions.

Regulatory differences between New Zealand and Australia

NZBA's media statements on the Royal Commission have emphasised that there are cultural differences between the New Zealand and Australian environments. We believe this is largely because we operate within a different regulatory framework which encourages open and constructive dialogue. That helps to ensure any issues are addressed in a timely and proportionate way. We stand by those comments. Some examples of that difference, as we see them, are:

- *Consumer-focused financial regulation:* In the last seven years New Zealand has undertaken a significant overhaul of financial regulation, primarily in response to the global financial crisis and the collapse of finance companies. That has resulted in, among other things, the Financial Advisers Act 2008, the establishment of the FMA under the Financial Markets Authority Act 2011, and the Financial Markets Conduct Act 2013. This legislation has been regularly reviewed (and is currently under review by way of the Financial Services Legislation Amendment Bill) to ensure it remains fit for purpose and focused on the right customer outcomes. We consider the willingness of government and agencies to undertake such an overhaul of relatively recent law is a sign of the cultural willingness here to respond quickly and thoroughly to address any shortcomings. This may in part reflect the relative size of the New Zealand market, but we believe it sets us apart from peer jurisdictions.
- *Superannuation:* The compulsory superannuation scheme in Australia is an extremely large industry managing trillions of dollars, which means almost every Australian needs to access some sort of financial advice, making regulation and enforcement difficult. There are also aspects of the superannuation industry (for example, self-managed super funds or schemes with deferred benefits) that add complexity to both the product and advice required. By contrast New Zealand's KiwiSaver scheme is less complex and much younger than the Australian scheme. It has effectively grown and evolved alongside modernisation of the regulatory system. The FMA has also had a strong and effective focus on KiwiSaver, ensuring the growing financial advice industry is well regulated.
- *Proactive agenda of regulators:* The New Zealand regulatory framework enables regulators to act dynamically and quickly before issues become significant, compared to the slower, less agile pace witnessed in Australia. The FMA's guidance on KiwiSaver practices is a good example of this. We have also seen that foresight and adaptability in RBNZ's use of loan-to-value ratio lending restrictions, which proved effective in managing the escalating housing market and the associated economic risk. There are other instances of proactive reviews we consider well aligned to global best practice. FMA's review into sales incentives in vertically integrated firms is one such example.

- *Independent governance*: New Zealand banks are governed by independent boards that must act in the best interests of the bank (and not, for example, an offshore parent).

For your information, NZBA's full media statement on the regulatory differences between Australia and New Zealand (as provided to Susan Edmunds, Stuff, on 23 April 2018) is included as **Attachment 2**.

Other market differences

We note other important market differences between Australia and New Zealand include:

- New Zealand banks do not own financial planning and mortgage broking businesses to the same extent as in Australia.
- There is no evidence of widespread product packaging in New Zealand.

Banking industry actions

In order to maintain public trust and support the industry will take the following actions:

1. Consider how to adopt the findings of the Australian Retail Banking Remuneration Review (Sedgwick Review) where appropriate

The April 2017 Retail Banking Remuneration Review by Stephen Sedgwick AO made a series of recommendations regarding conduct and incentives. While some of the recommendations may not apply in New Zealand, or may be unable to be adopted due to local legislative requirements, the industry is committed to adopting the rest of those recommendations, as appropriate for each bank. In some cases this work has already been completed and the relevant recommendations have already been implemented. The FMA's current work on sales incentives will also inform industry actions in this area.

2. Consider adopting an industry-wide whistleblowers' standard

One of the most effective ways of tackling misconduct is ensuring there are clear processes and safeguards for employees to raise issues safely. NZBA will review standards for whistleblowers and, if appropriate, announce a base industry standard. At least one of our members has also appointed a Customer Advocate to ensure customer-centric behaviour (and acting as an escalation point for elevating concerns).

3. Create a bad conduct register

The industry proposes to work with FMA and MBIE to enable more effective reporting of individual employee conduct that falls below standards expected by our customers and regulators. It is proposed this would apply to bank employees, mortgage brokers, advisers and insurance salespeople. Provision for this register could potentially be included in the Financial Services Legislation Amendment Bill currently going through Parliament, which would ensure that any privacy and natural justice concerns are met. We will explore this option through the consultation process currently underway.

4. Promotion of NZBA's revised Code of Banking Practice

NZBA has recently widely consulted on the revised and updated Code of Banking Practice that has been in force since 1992. In the latest edition we have taken a high-level principles-based approach that's intended to make banks' existing customer commitments more accessible and easy to understand. It will be published on 1 June 2018 and be well-publicised. It can be shared with regulators immediately.

5. Industry funding for regulators

The industry is happy to support regulators by considering how to provide further funding for the FMA and also, if appropriate, for RBNZ to enable it to perform its supervision function effectively.

6. Provide information on IDR to Banking Ombudsman

The industry will provide the Banking Ombudsman with further information on their Internal Dispute Resolution schemes, with a view to ensuring that they are fit for purpose and leading to good customer outcomes. In the meantime we note the reporting on the cases that the Banking Ombudsman has found in favour of the customer (9.5%), which suggests that the industry is likely to be successfully managing customer concerns (see <https://thespinoff.co.nz/business/28-04-2018/banking-inquiry-revelations-are-rocking-australia-what-would-a-nz-inquiry-reveal>).

The culture of trust and openness between regulators and the industry is of utmost importance to the success of the financial sector in New Zealand. NZBA hopes this letter and plan of action meets your expectations. As always, I am happy to discuss this with you as needed.

Yours sincerely

Karen Scott-Howman
Chief Executive

Attachment 1

Senior bank staff contact details

[REDACTED]

Attachment 2

NZBA statement to Susan Edmunds, Stuff, 23 April 2018

"Our banking culture is different from Australia's largely because we operate in a different regulatory environment.

"Our banks are well supervised by the Reserve Bank, the Financial Markets Authority, and the Commerce Commission. The Australian-owned banks are also supervised by the Australian Prudential Regulation Authority.

"The Australian royal commission comes on top of numerous other reviews of the Australian sector. Alongside our regulators, we've been vigilant in responding to the raft of Australian reviews. We'll continue to be so.

"We agree with Reserve Bank Governor Adrian Orr's recent statements highlighting the strong supervisory framework we have under the RBNZ Act.

"We also have a very active conduct regulator in the Financial Markets Authority. The FMA has completed many reviews that have closely examined bank conduct here, and continues to do so. For example, the FMA has signalled it will review bank incentives. As always, we welcome these reviews and will cooperate fully. We are certainly not being complacent in New Zealand.

"One of the things that sets us apart here is our open and transparent relationships with our regulators. That tends to help us proactively address issues before they become serious.

"The attitude of our regulators is supported by strong legislation, which includes powers for regulators to demand information from banks about their practices.

"Our conduct laws also enable the FMA to intervene proportionally where it sees examples of conduct that do not meet required standards. In Australia, the regulatory framework appears to have less flexibility.

"Back in 2008 we also introduced new financial advisers law and regulation. The government is currently reviewing that. Part of that work includes ensuring we put the customer first. We fully support the review and the government's aims.

"Our customers can be assured no systemic issues have been identified to date and can have confidence in the New Zealand banking system overall. We fully support the ongoing efforts of our regulators to examine our conduct and call us to account.

"All of this contributes to a strong banking culture in New Zealand that's different from Australia."