NEW ZEALAND BANKERS ASSOCIATION

Submission

to the

Financial Markets Authority

on the

Consultation: Proposed Standard Conditions for Financial Institution Licences

7 September 2022

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About NZBA

1. The New Zealand Bankers' Association (**NZBA**) is the voice of the banking industry. We work with our member banks on non-competitive issues to tell the industry's story and develop and promote policy outcomes that deliver for New Zealanders.

2. The following seventeen 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
   - China Construction Bank
   - Citibank N.A.
   - The Co-operative Bank Limited
   - Heartland Bank Limited
   - The Hongkong and Shanghai Banking Corporation Limited
   - Industrial and Commercial Bank of China (New Zealand) Limited
   - JPMorgan Chase Bank N.A.
   - KB Kookmin Bank Auckland Branch
   - Kiwibank Limited
   - MUFG Bank Ltd
   - Rabobank New Zealand Limited
   - SBS Bank
   - TSB Bank Limited
   - Westpac New Zealand Limited

Introduction

NZBA welcomes the opportunity to provide feedback to the Financial Markets Authority (**FMA**) on the Consultation: Proposed Standard Conditions for Financial Institution Licences (**Consultation Paper**). NZBA commends the work that has gone into developing the Consultation Paper.

Contact details

3. If you would like to discuss any aspect of this submission, please contact:

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Introduction

NZBA appreciates the FMA's engagement on licensing under the Financial Markets (Conduct of Institutions) Amendment Act 2022 (**CoFI**).

We understand the licensing conditions are intended to support the purpose and scope of CoFI and help the FMA effectively monitor the licensed population that is required to comply with the fair conduct provisions of the Financial Markets Conduct Act.

The proposed conditions capture multiple services that are already regulated by existing regimes, and in some cases those existing regimes cover the same matters in the proposed licence conditions. To help avoid an unintended compliance burden on Financial Institutions (**FIs**) that are subject to overlapping prudential requirements, our view is that the language used in the conditions needs to be more specific and targeted so that the intended reach and scope of each condition is sufficiently clear.

We do support the FMA taking a consistent approach with other licences issued by the FMA so that various licensing requirements can be managed efficiently where there is overlap, however this approach needs to be balanced against ensuring that the purpose and scope of each condition within the context of CoFI is clearly articulated.

We set out specific comments on the conditions below. We encourage the FMA to provide further clarity on the requirements as soon as possible, particularly those that will require systems changes for FIs such as the regulatory reporting requirements. We request that any regulatory reporting requirements are subject to a transition period following the commencement of the new conduct regime. We would also be happy to discuss further any changes the FMA is intending to make.

Condition One: Ongoing Requirements

NZBA supports this condition in principle. We agree that this licence should not be a "point in time" licence, but note that it is difficult to make an informed assessment of the impact of this condition until the Financial Institution Licence Application Guide (**Guide**) is available. Accordingly, we strongly encourage the FMA to release this Guide as soon as possible. FIs should have the opportunity to provide feedback on this condition once the extent of the obligations under the Guide is known.

At this stage, and echoing our comments above, our view is that the eligibility criteria for the CoFI license should be consistent with the eligibility criteria across other licensing regimes to avoid additional and duplicative compliance burden. We also point out that entities are subject to "fit and proper" requirements under other regimes administered by the FMA (such as Financial Advice Provider (**FAP**) regime) and the Reserve Bank of New Zealand (**RBNZ**) (see BS10 Review of Suitability of Bank Directors and Senior Managers issued March 2011). We propose that where an entity has met elements of eligibility criteria under other licences, the FMA consider if this information can be utilised under the CoFI licensing process to avoid duplication of efforts for captured entities. There is precedent for this approach under other regimes. For example, registered banks need not obtain fit and proper person certifications for the purposes of the Credit Contracts and Consumer Finance Act 2003 (**CCCFA**).

Condition Two: Notification of Material Changes

In the interests of certainty and future-proofing the licence, the explanatory note should go further to explain and clarify what will constitute a "material change". Additionally, the examples given and the explanatory note creates some ambiguity as to what changes would be considered "material". We would welcome a definition of "a material change to the nature of your financial institution service" and more detailed examples covering a broader range of scenarios.

Condition Three: Regulatory Returns

Further to our comments above, we support this condition on the basis that it is intended to facilitate the FMA obtaining updated information from FIs that the FMA reasonably requires to monitor FIs' ongoing capability to perform the financial institution service in accordance with the applicable eligibility criteria, and in a manner that meets the COFI requirements.

Banks provide (or will shortly be required to provide) a number of comprehensive regulatory returns across different regimes, and to different regulators, for example, under their DIMS, derivatives, MIS and FAP licences, and annual returns under the CCCFA. Banks also provide extensive data and information to the RBNZ. Without understanding the information the FMA expects to receive, we are concerned about the potential duplication of reporting to regulators and the compliance burden this will create. We also note that the FMA has yet to consult on the information that will be required for FAP regulatory returns.

We request that any regulatory reporting requirements are subject to a transition period following the commencement of the new conduct regime, similarly to the approach taken to regulatory reporting under the CCCFA. This will allow FIs to implement any required systems changes in an orderly manner.

We encourage the FMA to consider how the existing reporting provided by captured entities can be leveraged where relevant, and how the proposed regulatory returns for both CoFI and FAP regimes can be aligned to avoid unnecessary and duplicative compliance burden for captured entities. We also request that the FMA publish its regulatory return requirements as soon as possible, to allow captured entities sufficient time to understand and prepare for operationalising the requirements.

The explanatory note includes that the regulatory returns are likely to require reporting on numbers and types of breaches. If breach reporting is to be included, there will need to be appropriate materiality thresholds set (we note this position is consistent with the reporting required under the Financial Markets Conduct Act, section 412).

Condition Four: Outsourcing

Some banks are subject to prescriptive and detailed prudential regulation of outsourcing under the RBNZ BS11 Outsourcing Policy. Banks will also likely be required to comply

with standards under the new Deposit Takers Act covering outsourcing, business continuity planning and cyber security risk. Accordingly, we encourage the FMA to consider an exemption for registered banks that are already subject to a significant outsourcing requirement.

If no such exemption is available to registered banks that are already subject to other outsourcing regulatory regimes, it is crucial that the FMA is careful to align any outsourcing requirements to those other regimes, to minimise complexity and compliance burden. We also note that the compliance cost, and impact on commercial outsourcing arrangements could be significant for registered banks that are required to comply with multiple and overlapping regimes. At this stage, we have not seen enough detail on the scope of the condition to comment on the degree of alignment with other regimes. As noted above, the scope of this condition should be specifically linked to conduct requirements rather than being a broader requirement that goes to a FI's operations as a provider of financial services for customers.

We would welcome clarity around whether the "important matters that should be considered when conducting due diligence" are mandatory, or merely suggestions as to what an FI may consider. We would also welcome clarity on whether, and if so, how, such due diligence will be monitored and evidenced.

Further consideration and guidance should be given with respect to some of the complex issues that can arise in relation to the regulation of outsourcing arrangements, for example:

- transitional arrangements (as in some cases, for example, an FI may have entered into a long-term service arrangement, and the terms are not able to be renegotiated until the contract is renewed).
- confidentiality restrictions that prevent access to certain supplier records or information. For example, while service providers usually agree to have BCP obligations, it is not uncommon for the details of their BCP arrangements to be highly confidential and protected.
- record keeping and evidencing expectations of the FMA, particularly given the volume of outsourcing arrangements that this condition may impact.
- the scope of outsourced services and functions that this condition may impact. We understand that substantial effort and resource has been invested in supporting the ongoing management of the RBNZ's BS11 "white list" of services and functions, and we query whether a similar white list may be needed for this condition if the scope of the condition is not further defined.

Condition Five: Business Continuity and Technology Systems

We note the inconsistency between the prescribed time frame of 72 hours for reporting events to the FMA under the proposed standard for business continuity and technology systems, and the 10 working days provided for the equivalent standard under the FAP license. The RBNZ also has different requirements in this area.

Furthermore, as above, CoFI also captures activities related to MIS, Derivatives and DIMS. These activities do not have business continuity and technology systems conditions attached to respective licences, so we note that this proposed condition for the CoFI license may effectively impact and alter existing FMA licences for other regimes.

If the 72 hour window is retained, it would be helpful for the FMA to clarity that this window starts when it has been confirmed that an event has taken place that meets the reporting threshold.

Condition Six: Record Keeping

Further guidance on the scope of this condition is critical. We understand that the intention of the condition is to cover record keeping that directly relates to a FI's fair conduct programme. The drafting of this condition should be sufficiently clear to prevent unintended interpretations (for example the reference to obtaining consumers consent to the FMA viewing records could lead to a position where every single customer interaction is being recorded, which would require significant resource and would be burdensome in terms of compliance costs for businesses without any demonstrable benefit).

We would also welcome clarification on the types of types of records that are expected to be maintained to show how COFI Act requirements are met (as ordinarily FIs would expect to maintain records demonstrating that compliance has been achieved, rather than demonstrating how compliance has been achieved).

It would be helpful if the FMA could provide examples of what specific records they are expecting to be retained and provided.

We have some concerns around the practicalities of implementing "consumer" consent to the FMA viewing or obtaining records in the conduct context because it covers persons to whom a relevant service is offered, even if no service is ultimately provided or associated product acquired. We suggest that the reference to "consumers consent" is replaced with "customers consent" in the explanatory note. If a FI was required to obtain consent from every "consumer" before they had become that FI's customer, significant process changes would be required in order to ensure that consent was obtained.

We also consider that the 10 working day period for providing these records may be difficult, and suggest that a 20 working day period is adopted instead, with FIs being able to apply for an extension of this timeframe if the nature of the request is more complex.