What the FMA/ RBNZ Conduct and Culture Report means for NZ Insurers

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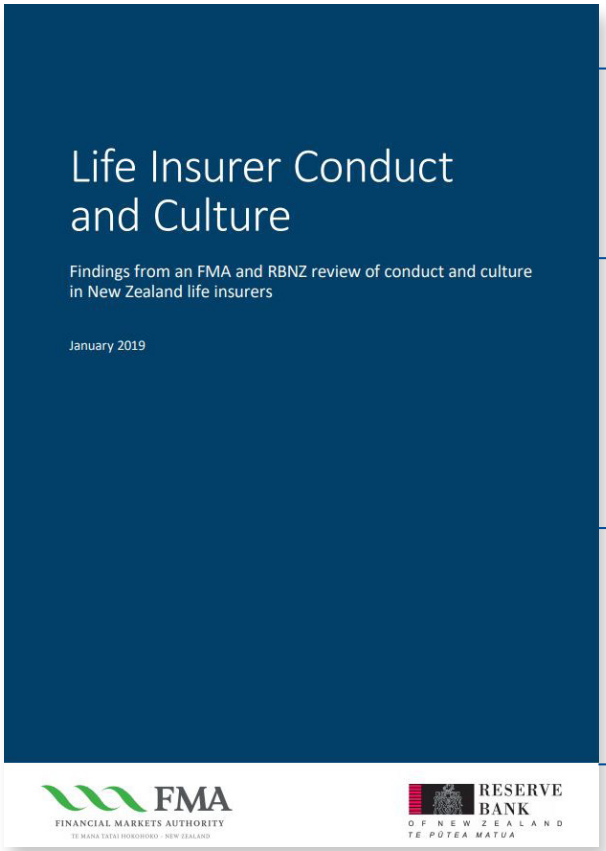
KPMG passionately believe that the flow-on effect from focusing on helping fuel the prosperity of our clients significantly contributes to ensuring that our communities, and ultimately our country and all New Zealanders, will enjoy a more prosperous future.

Report summary key messages



Published on January 29th, the Report is the culmination of the FMA/RBNZ's six month review of whether there are widespread conduct and culture issues present in life insurers in New Zealand, and to understand how life insurers identify and remediate issues.

The Report considers conduct and culture across New Zealand's 16 largest life insurers and sets out 33 'all insurer' recommendations across 6 key areas as well as 56 separate expectations that cover a range of themes, including delivering good customer outcomes, governance, risk management and issue identification/remediation. A full list of these recommendations and expectations is included in the Appendix.

Far from being life insurer-specific, the Report notes that "we expect all insurers to assess their conduct and culture governance frameworks, and consider and act on all relevant recommendations in this report". Furthermore the FMA has made clear that when they launched their conduct guide in 2017 they expected all financial services providers to have compared their conduct to the principles in the FMA conduct guide and taken action where their conduct falls short.

Outside of the ongoing consideration of conduct regulation as part of the MBIE's review of insurance contract law and the consultation on the overall role of the Reserve Bank and how it should be governed, the government has also indicated in response to the report that they intend to fast-track regulatory changes to cover conduct and product marketing across banking, finance and insurance sectors and create a more customer-centric regime. The Commerce Minister is expected to release a consultation paper in May covering:

- Clarity on the duties of both insurers and banks to consider customer interests and improve customer outcomes.
- A response to the issues identified around incentives / commissions.
- The conduct regulatory gap, oversight of intermediaries and regulator resourcing to penalise breaches.

What should your immediate response be?

- Expectations from the FMA and RBNZ are clear - all insurers are expected to develop an action plan by 30th June 2019 to address the findings of the Report together with findings provided separately to each individual life insurer. The specific items to be reported on by the 30th June have been summarised in the Appendix.

- This includes a detailed gap analysis against relevant insurance and sales advice process issues arising from the Australian Royal Commission (ARC) into Misconduct in the Banking, Superannuation and Financial Services Industry. Up to October 2018, the ARC has held 6 two week Hearings and published a 700+ page Interim Report comprised of a first volume discussing Hearings 1-4 and a second volume discussing case studies from each. The issues specific to insurance are covered under the financial advice section however relevant sales advice process issues will need to be more widely reviewed across the report. The Final Report is expected to be published on February 4th 2019.

- Aligned to this should be the initiation of a project or programme to manage the myriad of different areas arising from the recommendations and expectations. Including the ARC identification work, there are 19 distinct areas that could be used or rolled up into higher level areas to be owned across the business.

What does good look like?

In our conduct work across the Financial Services sector KPMG has developed a series of principles to help guide our clients.

BEYOND LEGAL

Go beyond legal and regulatory minimums.

URGENCY

Act with urgency. This work should be adequately resourced and given high priority.

DEPTH

Deep dive rather than surface review.

EMBEDDED

Drive embedded solutions which are transitioned to BAU.

EVIDENCE

Decisions and change grounded in evidence.

ROOT CAUSE

Don't just fix individual issues, fix root causes.

SET UP FOR THE FUTURE

Initiate long term foundational change rather than short term fixes.

CUSTOMER OUTCOME FOCUS

It's not about satisfaction, it's about outcomes.

CULTURE FOUNDATION

Culture is the foundation of all factors.

PART OF STRATEGY

This is not a programme that sits alongside strategy, it should be embedded in strategy.

BOARD ACCOUNTABILITY

Drive deeper accountabilities particularly at Board level.

SUSTAINABLE PROFIT

Determine new ways to drive sustainable profits.

PROACTIVITY

Be proactive about identifying and remediating rather than reactive.

PROJECT DISCIPLINES

Meet the standard project disciplines around cost, scope and timing, make commitments and be accountable for them.

How KPMG can support you

KPMG have first-hand experience in conduct work and have been supporting clients across the financial services sector on conduct extensively over the last four years. This has included presenting in market, submitting on various regulator consultations and sharing with the market analysis of the issues identified by the Australian Royal Commission. Our projects have included support around conduct risk frameworks and governance, conduct risk assessments, good customer outcomes, remediation support, culture, incentives, quality assurance, conduct investigations, project management, accountability frameworks, subject matter support, Royal Commission analysis, engagements on behalf of the regulators and supporting businesses with their regulatory responses.

During that time we have proactively built up a conduct team with strong reputation in market. It includes global expertise from the UK and Australia, experience in business and at the regulator and experience across a range of sectors in the financial services industry.

Our team are deeply experienced, but also strategic, pragmatic and commercial. We enjoy helping clients understand the challenges, shift perspective and confidently respond to the changing market environment.

KPMG is geared up and ready to support your business around this fundamental change. We understand your needs will change and evolve as the work takes shape and have set out below some of the ways KPMG could support you through this journey as it evolves.

Subject matter expertise

Drawing on your local and global experience, KPMG can leverage the specific technical knowledge of our experts in a number of disciplines across conduct, risk, strategy, transformation, and people and change.

Project support

Providing experience across all stages of project management including scoping, design and delivery, KPMG is well placed to support insurers in the planning and implementation of a programme of work.

Build and change

We bring a flexible workforce to support your resource needs with strong financial services experience and tested methodologies. This enables you to build and change at pace, while keeping your staff focused on servicing your customers and running your business.

Review and validate

An independent view, challenge, verification and sense check on the quality of work undertaken, providing you with strong industry experience, and allowing you to move forward with confidence.

Support and advice

We bring strong advice. Our team have learnt by doing this before, in both the New Zealand international markets.

APPENDIX:

Summary of recommendations and expectations in the Life Insurer Conduct and Culture Report

Recommendations

Theme	#	Recommendations
Next steps – due by 30 June 2019	**1**	Develop an action plan to address FMA/RBNZ feedback, and report progress to the regulators. Life insurers need to prioritise the development and implementation of these plans.
	2	Explain how they will meet FMA/RBNZ expectations regarding staff incentives and commissions for intermediaries.
	3	**Complete the following exercise and report the results to the regulators:** A detailed gap analysis against the final Australian Royal Commission (ARC) report and all findings relevant to insurance and the sales and advice process for insurance. This analysis should include identification of the risks, issues and implications for the life insurer's business.
	4	**Complete the following exercise and report the results to the regulators:** A systematic review of the insurer's existing life products and policy-holder portfolios in order to proactively identify any conduct and culture risks and issues. This should highlight any issues that require customer remediation and document the root cause of the issues. The review should cover at least the past five years. Where any issues identified pre-date this period, they should be traced back to their origin to determine the full extent of the issue.
General	**5**	All insurers need to make substantial improvements to how they identify, manage, remediate and report on conduct risks and issues, to deliver consistently good customer outcomes. Insurers need to take the FMA/RBNZ recommendations seriously, and proactively work to achieve maturity in this area.
The role of boards	**6**	Boards need to take responsibility for setting the tone from the top, improving the insurer's conduct and culture, and articulating how these are integrated into the business strategy and risk appetite. This includes having a clear plan for change that sets targets, assigns responsibility, includes milestones to ensure accountability, and ensures information flows down to all parts of the organisation. A focus on good customer outcomes should underpin this work.
	7	Boards need to clearly articulate their expectations for how to manage conduct risk within the business, including who is responsible and what reporting is required.
	8	For insurers with foreign ownership, boards need to ensure policies and processes are appropriate for New Zealand staff and customers.
	9	Boards of bank insurers need to ensure they operate independently and with influence within the wider banking group to ensure good governance and conduct risk management within the life insurance arm.
	10	Boards need to have sufficient information to satisfy themselves that issues are being adequately identified, and to challenge and hold senior management to account on conduct and culture matters.
Oversight of intermediaries	**11**	Insurers need greater oversight of how intermediaries are selling and managing their products. While insurers and intermediaries both need to be responsible for ensuring customers experience good outcomes, it is the insurer who is ultimately accountable for this.
	12	Intermediaries need to receive comprehensive training on insurer's conduct expectations, and on all aspects of the insurer's products (including customer suitability) before they can sell them. They should also be subject to ongoing accreditation to ensure knowledge is maintained.
	13	Insurers need a robust and transparent policy and processes for dealing with misconduct by intermediaries.
Product design, training and support	**14**	New products should be designed to provide good customer outcomes.
	15	Target markets and intended outcomes for products need to be clearly identified and articulated.
	16	Products (including policy wording) should be presented clearly, such as through the use of plain English.

Recommendations

Theme	#	Recommendations
Product design, training and support (continued)	**17**	Products (including definitions of covered or excluded conditions) should be reviewed on a regular basis to ensure they remain relevant and continue to provide the intended cover and are fit for purpose.
	18	Staff should receive ongoing comprehensive training on all aspects of the products they sell and support, including design, suitability, distribution, post-sale advice and claims handling.
	19	Insurers need a communication strategy that sets out how often and in what circumstances customers are contacted.
	20	Insurers should have oversight of all communication about products that takes place through intermediaries.
	21	Insurers need to proactively and regularly encourage customers to consider their needs and whether their current insurance policy is still suitable, particularly where the customer's circumstances might have changed.
Policies and processes	**22**	Risk management policies need to be appropriate and incorporate all material risks in the business, including consideration of conduct risk. Policies should set out roles and responsibilities, outline systems and processes to monitor and control material risks, and be subject to regular review
	23	Insurers must have a relevant code of conduct, and educate staff on what good conduct and culture looks like, focusing on good customer outcomes.
	24	Insurers should foster a 'no-blame, speak-up' environment to encourage staff to disclose conduct issues, and whistleblower processes must be accessible, confidential and independent.
	25	Insurers need to develop clear policies, processes and training for staff for identifying and dealing with vulnerable customers.
	26	Insurers need to prioritise investment in improving internal systems, processes and controls (including reporting mechanisms), in order to effectively monitor and manage conduct risk within the limits articulated in the risk appetite statement set by the board.
	27	Insurers need to have systems to review the advice provided at, and after, the point of sale, and customer outcomes over time.
Identification and remediation of issues	**28**	Insurers need appropriate systems and processes to record and resolve customer complaints and incidents. This includes defining what complaints and incidents are, and training staff on how to deal with these situations.
	29	Insurers need to establish formal remediation frameworks, policies and processes, and dedicate appropriate and sufficient resources to the operation of them. They should emphasise that issue identification and remediation needs to be proactive and undertaken without undue delay.
Incentives	**30**	We expect insurers to remove or substantially revise incentives linked to sales for frontline salespeople and all layers of management within their organisation (no later than the first performance year after 31 December 2019). Where sales incentives are not removed, insurers need to explain how they will strengthen their control systems to adequately mitigate conflicts of interest and risks to customers.
	31	We expect insurers to review their commission structures and volume bonuses for intermediaries – including structures with very high upfront commissions – to ensure they are incentivising intermediaries to deliver good customer outcomes. In our view, high upfront commissions are not acceptable as they drive poor conduct and can result in poor customer outcomes.
	32	We expect insurers to change their qualifying criteria for soft commissions to ensure they mitigate conflicts of interest and incentivise advisers to improve customer outcomes rather than just reward them for the volume or value of products sold.
	33	Authorised Financial Advisers (AFAs) are required to disclose all commissions to customers – we expect insurers to encourage all intermediaries to disclose this information.

Expectations

Theme	#	Expectations
Product suitability	**1**	We expect insurers to carefully evaluate the adequacy of customer input and whether they need to obtain more information from customers directly.
	2	Insurers need to do better to present their products (including policy wording) clearly in plain English. The FMA/RBNZ view is that policy wording should be reviewed on a regular basis, to ensure the policy is understandable and continues to provide cover as promoted. Reviews should include consideration of whether definitions of covered or excluded medical conditions continue to be relevant and align with generally accepted scientific and medical conditions. Insurers should work to improve consistency and clarity around definitions.
	3	Insurers should ensure that customer suitability is considered in product development
	4	Insurers should have systems and controls to monitor and ensure that distribution and performance of products is in line with the product design and customer suitability
	5	Insurers should ensure that customers understand their policy and have processes in place to ensure ongoing suitability
	6	Insurers should train and monitor intermediaries to reduce the risk of unsuitable products being sold to customers.
Legacy or closed products	**7**	The FMA/RBNZ expectation is that legacy customers should not be given less attention than newer customers or treated in a way that risks poorer outcomes for them.
Vulnerable customers	**8**	We expect insurers to identify potentially vulnerable customers, and have policies, processes and training for staff and intermediaries about dealing with vulnerable customers and ensuring they experience good outcomes.
Ongoing customer communication	**9**	Involvement of an intermediary does not discharge an insurer's responsibility for good customer outcomes. Insurers and intermediaries both need to be responsible for ensuring customers experience good outcomes, but it is the insurer who is ultimately accountable for this.
	10	We consider insurers to have a responsibility to satisfy themselves that customers are receiving all relevant information about their policies, including any changes, and are given appropriate opportunity to review their cover or product.
	11	Insurers using intermediaries need to be clear with the intermediary about who will communicate what information to customers.
	12	Insurers also need appropriate checks in place to ensure that communication occurs.
	13	Insurers should think about the best way to encourage customers to consider their ongoing needs, and whether their current insurance policy is still suitable.
Customer-focused culture	**14**	Insurers need to be clear that policy-holders are their customers, and promote a culture that puts customers at the centre of decision-making, product design, sales, advice and claims processes, and all day-to-day activities.
Customer feedback and measuring customer outcomes	**15**	Insurers should also use 'lead' indicators. These can provide insights on potential outcomes and identify emerging trends.
	16	All insurers need to better utilise customer feedback to inform continuous improvement of service, policies and processes.
	17	Feedback from complaints and incidents should be heard and acted upon.
	18	Insurers need to perform root-cause analysis of issues and complaints to mitigate the risk of issues reoccurring.
	19	Insurers also need to continually review products to address issues and improve customer outcomes.

Expectations

Theme	#	Expectations
Poor-value products	**20**	Enhanced disclosure and training needs to be provided to improve transparency and ensure suitable customer outcomes.
	21	If there is a justification for selling these products [poor-value products], we expect it to be supported by strong systems, processes and controls for ensuring the products are only sold to the target customers, the particular risks, issues and limitations are fully disclosed, and there is evidence the products meet customer expectations.
	22	We expect insurers to be able to justify the rationale for their products in terms of good customer outcomes, and to remove or change products that consistently fail to provide good outcomes or value for customers.
	23	We expect all insurers to identify which products may be poor value for customers and consider the recommendations from this report.
Remuneration and incentives	**24**	As part of their action plans, insurers must explain how they will meet the expectations set out below regarding incentives and commissions.
	25	It is for insurers to determine the most appropriate way to design and control incentive structures to sustain good customer outcomes. Removing any incentives linked to sales measures9 is a significant step towards this goal. However, it may not be sufficient – the pressure that senior managers put on more junior managers and staff to sell can be very powerful, and insurers need to carefully review the structural design of all incentives.
	26	We expect more proactive oversight by boards and senior management in the management of risks associated with incentives.
	27	We expect all life insurers to revise any sales incentive structures for salespeople and through all layers of management. Life insurers need to implement changes to incentive schemes no later than the first performance year beginning after 31 December 2019. Any life insurer that does not, by 30 June 2019, commit to removing incentives linked to sales measures will be required to explain how they will strengthen their controls sufficiently to address the risks of poor conduct that arise with such incentives.
	28	We expect life insurers to manage the risks associated with incentive changes, as changes to incentives may have unintended consequences.
	29	As life insurers develop indicators of good customer outcomes, we expect them to consider incorporating these into staff incentives.
	30	The FMA has previously strongly encouraged all insurers to consider the nature and value of the soft commissions they provide to intermediaries, to ensure that this method of remuneration supports a focus on good customer outcomes. We have yet to see any insurer confirm and announce an intention to change the qualifying criteria for soft commissions so that intermediaries are incentivised to improve customer outcomes rather than merely to sell products. We think this change needs to occur.
	31	We also expect life insurers to review their commission structures for intermediaries, including the very high upfront commissions compared to ongoing or 'trail' commissions.
	32	Insurers need to ensure they are appropriately incentivising the good conduct of intermediaries and the delivery of good customer outcomes.
	33	We would like to see advisers incentivised for providing ongoing service and advice to customers about product suitability and for maintaining good customer outcomes.
	34	AFAs are required to disclose all commissions to customers – we expect insurers to encourage all intermediaries to disclose this information to their customers.
Governance of conduct and culture risk	**35**	For governance to be effective, it must be kept separate from ownership, by having independent directors to provide objectivity and impartiality.
	36	RBNZ would like to see the strength of local boards grow. This can be helped by increasing independence and diversity on local insurance boards.
	37	We expect boards to take ownership of conduct risk, including allocating sufficient resources to the development of effective policies and processes (including, where relevant, that they are tailored to local requirements).
	38	Some boards need to take the fundamental first step of understanding what conduct and culture governance is, and what the risks are for their business.

Theme	#	Expectations
Governance of conduct and culture risk continued	**39**	Boards need to be more effective in setting the tone and expectations around conduct and culture, and ensuring that good customer outcomes and good conduct are central to the business strategy.
	40	There is no one-size-fits-all approach, but we expect boards to ensure conduct governance is considered at a board and sub-committee level, and to have effective two-way communication channels and clear expectations for senior management.
Conduct and culture reporting	**41**	We expect boards to determine what information is required from senior management to enable them to effectively oversee conduct and culture risk, require senior management to provide it regularly, and then test and challenge it when necessary.
	42	Some directors noted it was challenging to get information – senior management should be open with the board and give them the information they need.
Sales oversight and controls	**43**	An insurance contract is between the insurer and the customer (policy-holder). Therefore, insurers need to make a real effort to determine whether customers are receiving good outcomes from their products.
	44	Insurers should have adequate mechanisms to monitor the sales and advice processes of intermediaries, to minimise the risks of their products being mis-sold and customers experiencing poor outcomes.
	45	Our strongly held view is that increased regulation of third-party advisers would not discharge insurers' responsibility for customer outcomes. We expect insurers to have an interest in and oversight of intermediaries' conduct when selling their products on their behalf, to ensure good customer outcomes.
	46	Life insurers who are QFEs or an associated entity of a QFE (eight of the insurers we reviewed are QFEs or an associated entity of a QFE) need to do more to meet their obligations.
Conduct and culture risk management	**47**	To achieve good customer outcomes, responsibility for conduct risk management needs to be integrated across all parts of the insurer's business.
Training programmes	**48**	We expect insurers to review their training programmes, to ensure they appropriately support staff and intermediaries in the delivery of good customer outcomes.
Whistleblower policies	**49**	Insurers need to do more to raise awareness and understanding of the types of issues that could be reported through whistleblower mechanisms, which should include concerns about conduct and culture.
Complaint and incident management systems	**50**	Our view is that while the ability to resolve complaints at the frontline is a good thing, this activity still needs to be recorded to contribute to the overall view of conduct issues and customer outcomes.
	51	We expect all insurers to have appropriate systems and processes to record and resolve customer complaints. This includes defining what a complaint is and training staff on how to deal with complaints.
	52	We would like to see the industry, perhaps through the FSC, achieve consistency in this area, raising customer awareness of complaint and dispute resolution processes, and encouraging the use of insights from complaints to improve customer outcomes.
Root cause analysis, systemic assessment and trend analysis	**53**	Insurers need to have systems and processes to proactively identify (from a range of sources) issues that may require remediation.
	54	Insurers need to stop relying solely on lag indicators, and use lead indicators to provide insights and positive assurance about customer outcomes.
	55	It is also imperative that insurers learn from previous instances of poor conduct or misconduct. Boards should seek positive assurances from management about customer outcomes, and not just rely on the absence of reported issues as a measure of effectiveness of the insurer's conduct and culture.
Treatment of issues	**56**	We expect insurers to proactively seek to identify issues in a systematic and methodical way, and prioritise remediation.
Assessment against ARC issues	**57**	We expect all insurers to proactively review the work of regulators and related international examples to help identify potential conduct and culture issues here. This includes examining the key themes and issues arising from the ARC, and determining whether there are similar issues present or possible in New Zealand.

Contact us

Ceri Horwill
Partner, Risk Consulting
Ph: +64 9 367 5348
E: cerihorwill@kpmg.co.nz

Jamie Munro
Partner, Audit
Ph: +64 9 367 5829
E: jamiemunro@kpmg.co.nz

James Brownell
Director, Risk Consulting
Ph: +64 9 364 0956
E: jbrownell@kpmg.co.nz

Adele Wallace
Associate Director, Risk Consulting
Ph: +64 9 367 5941
E: adelewallace1@kpmg.co.nz

Ross Molyneux
Associate Director, Risk Consulting
Ph: +64 9 363 3272
E: rmolyneux@kpmg.co.nz

Kate Stewart
Senior Manager, Risk Consulting
Ph: +64 9 363 3298
E: katestewart@kpmg.co.nz