NOVEMBER 2022

Fair conduct programmes

This information sheet provides information and examples to help entities establish, implement and maintain their fair conduct programmes (FCPs). It will be useful for entities holding or applying for a licence to act as a financial institution under the Financial Markets Conduct Act 2013 (FMC Act), and anyone involved in establishing, implementing and maintaining an FCP.

Overview

Entities licensed to provide the market service of acting as a financial institution are subject to a fair conduct principle that says they must treat consumers fairly. The requirement to treat consumers fairly includes:

- paying due regard to consumers' interests
- acting ethically, transparently, and in good faith
- assisting consumers to make informed decisions
- ensuring the products and services the financial institution provides are likely to meet the requirements and objectives of likely consumers (when viewed as a group)
- not subjecting consumers to unfair pressure or tactics, or undue influence.

Financial institutions are required to establish, implement and maintain an effective FCP designed to ensure their compliance with the fair conduct principle. This information sheet provides information about FCPs, including elements of what we consider to be good practice for establishing, implementing and maintaining an FCP. The examples in this information sheet are suggestions to help financial institutions meet their obligations under the FMC Act. They are not exhaustive, are illustrative in nature, and are not intended to impose any additional obligations or requirements above what is set out in the legislation and regulations.

What is a fair conduct programme?

An FCP means effective policies, processes, systems and controls that are designed to ensure the financial institution's compliance with the fair conduct principle.

The FCP must be in writing. As an FCP consists of policies, processes, systems and controls, it could comprise a number of documents rather than being a single document. We expect financial institutions to be able to identify all of the policies, processes, systems and controls that form their FCP.

Some financial institutions, particularly those with large and/or complex operations, may choose to create an overarching policy or framework document that explains the structure of the FCP and outlines the different policies, processes, systems and controls that comprise the FCP. Other financial institutions may determine that a single document is sufficient to capture their FCP.

Some financial institutions may already have a conduct programme or similar in place, or may form their FCP from a combination of new and existing policies, processes, systems and controls. Where existing programmes, or components of programmes, form part of the FCP, these should be reviewed when the FCP is established, to ensure they will be relevant and effective in supporting the financial institution's compliance with the fair conduct principle.

Minimum requirements for FCPs

The minimum requirements for the content of an FCP are set out in section 446J of the Financial Markets (Conduct of Institutions) Amendment Act 2022 (CoFI Act). These are minimum requirements, and financial institutions may choose to implement additional policies, processes, systems and controls to ensure that consumers are treated fairly.

This information sheet explains some of the minimum requirements, where they relate to establishing, implementing and maintaining the FCP. Information regarding the minimum requirements in the CoFI Act is also provided in the Licence Application Guide.

Establishing an FCP

Setting the context

To be effective, we consider that an FCP needs to be relevant and proportionate to the financial institution's business. This means it should reflect the unique factors that characterise the business.

The CoFI Act requires a financial institution to have regard to the following factors when establishing its FCP:

- the nature, size, and complexity of its business
- the relevant services and associated products it offers
- the methods by which it provides relevant services and associated products to consumers
- the types of consumers it deals with, including consumers in vulnerable circumstances
- the types of intermediaries that are involved in the provision of its relevant services and associated products, including the nature of that involvement and their legal obligations in connection with their involvement (such as obligations related to giving financial advice)
- the types of agents that are engaged to carry out work in relation to its relevant services or associated products, including the nature and extent of that work, and the authority of those agents
- any other factors that may be provided for in regulations (none at present).

We expect financial institutions to be able to demonstrate how they have considered all of these factors, which may be achieved by including commentary about this in their FCPs.

The minimum requirements for FCPs require financial institutions to identify, monitor and manage conduct risks, i.e. risks associated with conduct that fails to comply with the fair conduct principle. Financial institutions should be able to describe those risks, and demonstrate how the policies, processes, systems and controls that form their FCP relate to those risks.

> For example, a financial institution has risk-rated the relevant services and associated products it offers to consumers in terms of the potential risk of harm through unfair treatment. It has used this evaluation to help identify and assess how the characteristics of its business could contribute to the unfair treatment of consumers. Its FCP addresses the identified risks with greater emphasis on the policies, processes, systems and controls that relate to higher-risk services and products, due to the potential harm to consumers.
>
> In another example, a financial institution has identified what it considers to be fair treatment of consumers. It has used this information to identify and document the factors in its business and other circumstances that could lead to consumers being treated unfairly. Its FCP includes details of the policies, processes, systems and controls that are used to monitor and manage those risks.

Identifying the conduct risks that are relevant to the financial institution, and monitoring and managing those risks, means that resources are more likely to be targeted towards the areas of highest risk. Some financial institutions may find it efficient to incorporate the identification, monitoring and management of conduct risks into their existing risk management processes and documentation.

Taking into account the above factors and the specific conduct risks facing the financial institution – rather than a generic set of risks which may not actually be relevant – will help to make the FCP relevant and proportionate.

> For example, a financial institution that is large and offers a wide range of relevant services and associated products to different types of consumers through a variety of channels, including intermediaries, may determine that it requires an FCP that is comprised of a number of interlinking policies, processes, systems and controls to address the different conduct risks it faces.
>
> In another example, a financial institution is small and has a simple product suite that it provides directly to consumers. The size and nature of the business may mean that the FCP does not need to be as comprehensive as that of a larger, more complex business. However, the financial institution has identified that a large portion of its consumers are in circumstances that mean they are vulnerable to unfair treatment. As a result, its FCP has a strong focus on how those consumers are identified and supported, which reflects the identified risks.

Roles and responsibilities

The minimum requirements for FCPs require financial institutions to have clearly defined roles, responsibilities and accountability arrangements for identifying, monitoring and managing the risks associated with conduct that fails to comply with the fair conduct principle.

We expect the FCP to include the key roles or types of roles within the financial institution, and provide detail about the responsibilities of each role or type of role in relation to fair conduct. In some financial institutions, particularly small firms, there may not be roles dedicated to fair conduct, but conduct may form part of the responsibilities of one or more roles, which should be documented in the FCP.

Some financial institutions will already have processes and documentation to explain roles and responsibilities across the organisation. Where there are existing processes or frameworks to articulate responsibilities, financial institutions may choose to incorporate conduct responsibilities into these, rather than creating new tools specifically for conduct responsibilities.

> For example, a financial institution already using a 'three lines of defence' model or RASCI (responsible, accountable, supporting, consulted, informed) model may find this will be suitable to articulate roles and responsibilities in relation to fair conduct. In order to meet the minimum requirements for FCPs, that model would become one of the policies, processes, systems and controls that comprise the FCP.

Approval of the FCP

We consider that to be effective, an FCP must have the support of the financial institution's governing body, which would generally be the Board of Directors. We expect the governing body to have oversight and take accountability for the financial institution's compliance with its licence obligations and the CoFI Act requirements.

The governing body should review the FCP to consider its adequacy and effectiveness, and recommend changes where appropriate. We expect that the final approval of the FCP will be provided by the governing body.

Some financial institutions may operate as part of a group of related entities. In this situation, the entities may determine that it is appropriate and efficient to have a single FCP that covers all of the financial institutions within the group. This approach could be taken when a licensee applies to have one or more authorised bodies on its licence, or when each financial institution in a group applies for its own licence.

Where a single FCP is in place to cover two or more financial institutions within a group, we expect the FCP to:

- reflect the unique factors and conduct risks that characterise each of the financial institutions
- be explicitly considered and approved by the governing bodies of each of the financial institutions. We do not consider it appropriate for the governing body of one financial institution to approve the FCP for another financial institution, such as a subsidiary or other related company.

The approval of the FCP by the relevant governing body should be documented in the FCP. Where a single FCP is in place to cover two or more financial institutions within a group, the approval of the FCP by each governing body should be clearly documented.

Outsourcing

Some financial institutions may choose to outsource all or part of the process of establishing, implementing or maintaining the FCP. Outsourcing may be appropriate for businesses that don't have the internal resources for these activities. Regardless of which elements, if any, are outsourced, all financial institutions must recognise that outsourcing does not absolve them of their compliance obligations and responsibilities as a licensed entity. They remain directly subject to, and liable for, compliance with the duties relating to FCPs in the CoFI Act, including the duty to establish, implement and maintain an effective FCP.

Financial institutions must ensure they fully understand any documents, policies, processes, controls and systems produced by external parties, and be able to explain how these are effective in meeting the organisation's obligations. Financial institutions should have personnel who are responsible for implementation and ongoing operation of the FCP, including any components created by external parties, and must be able to explain their meaning and application to the FMA.

Implementing and maintaining an FCP

Communication and training

A key component of implementing an effective FCP is ensuring it is understood by those financial institution employees whose actions and outputs may have an impact on how consumers are treated. We consider that communication and training, where relevant, are essential to effective implementation of the FCP.

The CoFI Act requires an FCP to include initial and regular ongoing training for the financial institution's employees, including training on:

- the relevant services or associated products that are provided to consumers
- the FCP and the processes and procedures that the employee must follow to support the institution's compliance with the fair conduct principle.

Financial institutions will need to determine the frequency, delivery methods and content of initial and regular ongoing training for employees, and ensure this is appropriate for the employees' work in providing the relevant services or associated products to consumers. The training that is provided may need to be tailored for different employees depending on their roles. This means that a single training course or method of delivery may not be suitable or sufficient for all types of employees.

For example, different training may be required for frontline staff who deal directly with consumers, technology staff who develop and maintain the IT systems that are used to provide services and products to consumers, and marketing staff who produce information for consumers, to ensure that their actions and outputs contribute to consumers being treated fairly.

The training should also be relevant and proportionate to the nature and size of the business and the conduct risks that the financial institution faces. Some financial institutions, particularly larger institutions, may choose to implement a more structured training programme and electronic learning methods to provide training to larger numbers of employees. Smaller organisations may find that other methods are more appropriate for their business.

The CoFI Act also requires financial institutions to check that each employee has completed this training, and that they have a reasonable understanding of the matters covered by the training. Training frequency, delivery methods and content should be reviewed over time and updated to reflect insights from assurance activities, any changes to the matters the training is required to cover, changes in the financial institution's business, and new and emerging conduct risks.

Assurance

Financial institutions are required to maintain an effective FCP. We expect financial institutions to have assurance processes to assess the effectiveness of their FCP.

We do not specify the type of assurance processes that should be implemented; these may comprise internal control or quality testing, measurement against performance indicators, review by an independent party such as an auditor or compliance consultant, or other assurance activities.

Financial institutions will need to determine the appropriate frequency for carrying out these assurance processes. They may find it helpful to assess the effectiveness of their FCP following its establishment and implementation, and following implementation of material changes to the FCP.

Financial institutions are likely to have existing assurance processes to measure the effectiveness of their policies, processes, systems and controls. Some financial institutions may choose to incorporate assurance over their FCP into existing assurance processes, but this is not mandatory.

For example, some financial institutions which are already licensed under the FMC Act – such as financial advice providers and derivatives issuers – are required to have a compliance assurance programme in place. Those financial institutions may choose – but are not required to – use their compliance assurance programme to provide assurance regarding the effectiveness of their FCP.

Assurance is an important part of governance arrangements for a financial institution, but it does not need to be complicated. As with core risk and compliance processes and frameworks, assurance arrangements should be fit for purpose for the entity. Financial institutions should be able to explain their assurance processes and why they consider them appropriate for their business.

Review of the FCP

The CoFI Act requires financial institutions to ensure they have methods for systematically identifying deficiencies in the effectiveness of the FCP and ensuring that any deficiencies are promptly remedied. Assurance processes and reviews of the FCP must be sufficiently detailed to achieve this.

We expect financial institutions to regularly review their FCP to ensure it continues to be relevant and proportionate to their business. Financial institutions should also consider identifying trigger events relevant to their business that will prompt a review of all or parts of their FCP, e.g. during periods of significant change in the business, and following the identification of conduct that fails to comply with the fair conduct principle.

A review should include consideration of the policies, processes, systems and controls that comprise the FCP. Some of these components may be subject to separate regular review, depending on their nature and how critical they are to the business.

We do not intend to specify the frequency for completing regular reviews. It may be influenced by the conduct risks that the financial institution faces, and the reliance placed on the policies, processes, systems and controls to manage those risks.

The review of the FCP should take into account the results of the financial institution's assurance processes, which should provide valuable insights into the effectiveness of the FCP.

Financial institutions should be able to demonstrate when they have undertaken a review of their FCP and the outcomes of the review, including steps taken to remediate any deficiencies. Version control within core documents is one way to demonstrate this. We also expect that the outcome of reviews – including highlighting any material deficiencies – is shared with the financial institution's governing body, and that approval of any material changes is also obtained from the governing body. This is a key component of effective governance over the financial institution's conduct.

Reporting and governance

The governing bodies of financial institutions play a central role in overseeing the establishment, implementation and maintenance of the financial institution's FCP. We expect the governing body to set clear expectations for senior management about the fair treatment of consumers, and take accountability for those expectations being met.

> The minimum requirements for FCPs include regular and comprehensive reporting to the governing body about conduct risks – i.e. risks associated with conduct that does not comply with the fair conduct principle – and about failures to comply with the fair conduct principle.
>
> In practice, this means that the governing body should receive regular reporting about potential conduct risks, as well as actual instances where the financial institution has not complied with the fair conduct principle, including the steps taken to mitigate the effects of the failure. The results of assurance processes will be a key input to the reporting.

Reporting about conduct risks and failures to comply with the fair conduct principle should provide the governing body with appropriate information to exercise their oversight responsibilities. Financial institutions should not rely on a single indicator, such as consumer complaints, to provide assurance about fair conduct. The use of both lead and lag indicators, and data from different sources, should be used to provide the governing body with a comprehensive picture of the financial institution's conduct towards consumers.

Lag indicators measure what has already happened. They confirm past performance or trends that are already in progress. For example, consumer complaints may be used to identify where the financial institution has already treated consumers unfairly.

Lead indicators are forward-looking and can help identify potential risks earlier, to enable a response before the risk materialises. For example, data on how a new financial product is being used by consumers may provide an early indicator of additional actions that should be taken to ensure the product is sold and used as intended.

Governing bodies must be able to satisfy themselves that they are receiving sufficient information from management, and be proactive about requesting what they need. Once boards are receiving the information they require, it can be a key input for strategy setting, and providing direction and guidance for management.

Resourcing

In addition to the requirements detailed above, it is important that financial institutions have adequate resources to support compliance with the fair conduct principle.

We expect that financial institutions will have and maintain sufficient financial and human resources at all levels of the organisation to establish, implement and maintain their FCP.

For example, when a new product is launched for sale to consumers, there should be sufficient investment to ensure that its operation on the financial institution's IT systems is accurate and aligns with how the product is described and marketed to consumers.

Financial institutions also need to ensure their Board of Directors and senior management have sufficient capability to govern conduct and manage conduct respectively. This may require financial institutions to undertake additional training, or strengthen their board and/or senior management team in the area of conduct risk management.