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# Fair conduct programme insights report

**Insights from the FMA's review of fair conduct programmes received from financial institutions ahead of the commencement of the CoFI regime**

FMA
FINANCIAL MARKETS AUTHORITY
TE MANA TĀTAI HOKOHOKO

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# Foreword

The Financial Markets Authority – Te Mana Tātai Hokohoko (FMA) was established with the overarching statutory objective of promoting fair, efficient, and transparent financial markets. The **Financial Markets (Conduct of Institutions) Amendment Act 2022 (CoFI)** expands the **FMA's mandate** as a conduct regulator and strengthens consumer protection by requiring financial institutions to prioritise the fair treatment of consumers.

CoFI requires financial institutions to be licensed by the FMA, and to establish, implement, maintain and comply with an effective **fair conduct programme** (FCP). An FCP means policies, processes, systems and controls that are designed to ensure the financial institution's compliance with the **fair conduct principle**, which is that financial institutions must treat consumers fairly**.**

While some financial institutions hold other market service licences issued by the FMA and therefore have experience engaging with the FMA, we acknowledge this will be new to others. We are committed to open, collaborative relationships to support fair consumer treatment. Over the past two years we have supported financial institutions in obtaining their licences and preparing for the new regime. We have published guidance[1], met with financial institutions individually, and engaged with the wider sector in-person and through online webinars and roundtables.

Financial institutions are a diverse population with different business structures, consumers, products and services. CoFI is designed as a principles-based regime, which gives financial institutions the flexibility to design an FCP that fits their business model. For this report, we have reviewed FCPs from a range of entities that vary in size, product offering and consumer profile. We believe that all financial institutions can learn from these insights. Our aim by sharing insights early in the regime is to assist financial institutions to continuously improve their FCPs and their approach to fair consumer treatment.

Encouragingly, we saw that many financial institutions have taken a comprehensive approach to the development of their FCPs, ensuring they align with their business nature, size, complexity and risk profile. Some have gone beyond the minimum requirements to build comprehensive, consumer-focused practices. This report spotlights some of these examples of good practice, as well as evolving areas of risk we think all financial institutions should consider as the financial services landscape evolves.

In these first years of the regime, we will continue to take an educative and collaborative regulatory approach, supporting financial institutions as they refine and strengthen their approach to fair consumer treatment. We also intend to undertake a more in-depth review of FCPs and share findings supported by evidence of how the programmes have functioned in action. We encourage financial institutions to build on the good work they have been doing, think beyond simply meeting the minimum requirements, and foster a culture that actively identifies, monitors and manages current and evolving risks associated with fair conduct.

**Michael Hewes**
**FMA Director, Deposit Taking, Insurance and Advice**

[1] Financial institution licence guide; FCP information sheet; Fair conduct programmes – information for smaller firms; CoFI intermediated distribution guidance

# Executive summary

In the lead-up to the CoFI regime, numerous banks, non-bank deposit takers and insurance companies shared a copy of their fair conduct programme (FCP) with us. These provided insights into how different financial institutions approached designing an FCP and applied the fair conduct principle within the context of their business.

This report provides key findings and observations from our engagement with financial institutions and reviews of the FCPs we received, with a focus on highlighting areas of good practice. We have not reviewed the policies, processes, systems and controls in detail or measured the FCPs' effectiveness.

The insights are based on reviews of 38 FCPs from financial institutions of varying size and complexity, including nine banks, four non-bank deposit takers, six life insurers and 19 non-life insurers. This sample reflects the makeup of the financial institution sector overall.

The examples included are not exhaustive and are not intended to impose any additional obligations or requirements above what is set out in the legislation and regulations.

FCPs are living documents that should evolve to remain effective as consumers, business models and key risks change. Our observations regarding FCPs present an opportunity for financial institutions to consider how relevant and comprehensive their FCPs are, and how improvements can be made over time.

## Key insights

Overall, it is encouraging to see the strong commitment financial institutions have to fair conduct, with many developing robust governance structures, comprehensive frameworks of policies, processes, systems and controls (PPSCs), and proportionate approaches that reflect the specific aspects of their business.

### The fair conduct principle

We are encouraged to see most FCPs have incorporated the fair conduct principle in a way that reflects the entity's own conduct and culture. They have enhanced their commitment to treating consumers fairly by integrating the fair conduct principle as a key driver of their business.

FCPs provide a window into how financial institutions treat consumers. Many have taken the opportunity to showcase their commitment to treating consumers fairly, providing a clear outline of how they will achieve this.

Financial institutions can continue building on these foundations through regular review. As the regime matures, there is an opportunity for them to further demonstrate how they connect their organisation's purpose to the fair treatment of consumers.

## Making the FCP relevant

In general, financial institutions have tailored their FCP to the nature, size, and complexity of their business. By reflecting these factors in their FCP, they have ensured their approach to fair conduct is both relevant and proportionate.

For those with niche products or consumer groups with specific needs, there is an opportunity to further tailor the FCP to reflect their specific characteristics. By doing so, financial institutions can clearly identify consumer needs and outcomes, and demonstrate how these are considered in the design and delivery of products and services. This is particularly relevant for financial institutions that may have higher exposure to vulnerable consumers.

As financial institutions and the environment they operate in evolve, there will be opportunities to adapt the FCPs to reflect these changes. This ongoing review will help maintain the FCP's effectiveness and relevance, to ensure it continues to support fair treatment of consumers.

## Policies, processes, systems, and controls

Financial institutions have largely demonstrated how their FCPs are supported by well-designed PPSCs. Many institutions have structured their FCP as a framework document, which incorporates relevant supporting documents to enhance clarity and accessibility.

Some financial institutions have used tools (such as glossaries, tables and appendices) to make it easier for stakeholders to navigate and understand the FCP. By streamlining the presentation of PPSCs, they have made it simpler to access relevant information and to make updates when and where required.

As financial institutions continue to refine their FCPs, they can further consider accessibility and ease of navigation within the FCP, to ensure critical information is available and clearly identifiable. This could also deepen transparency and ensure that the fair conduct principle is reinforced in the PPSCs, enhancing effectiveness of the FCP.

## FCP governance and effectiveness

Most financial institutions have integrated the FCP into their governance structures, clearly outlining roles and responsibilities across the board, senior management, committees, assurance functions, and operational staff. These controls will help to ensure that risks to the fair treatment of consumers (conduct risks) are effectively monitored and managed, with clear oversight mechanisms in place.

Financial institutions have also linked their conduct frameworks with broader risk management processes to address any emerging conduct issues in a timely and effective manner. This helps maintain a strong focus on treating consumers fairly and minimises the risks of non-compliance and harm, and that such risks may crystalise.

## Evolving risks and the FCP

Fair treatment of consumers is an ongoing commitment shaped by evolving risks. As financial markets change, financial institutions must continuously assess and adapt their FCPs. A proactive approach to conduct risk management is essential.

Our review considered whether financial institutions incorporated evolving risks into their FCPs, particularly in areas such as innovation and artificial intelligence (AI), technology and cyber risks, financial inclusion, economic pressures, and fraud. While most FCPs were well-structured and tailored to business needs, references to these evolving risks were limited.

To strengthen their conduct frameworks, financial institutions should embed a culture that actively identifies, monitors, and manages evolving risks. This includes considering the broader implications of a rapidly changing financial landscape and associated forecast risks, and ensuring fair treatment remains central to decision-making. By integrating these principles, financial institutions can enhance resilience and deliver fair consumer outcomes consistently.

# Detailed insights

## The fair conduct principle

**What we want to see**: The fair conduct principle is the overarching principle of CoFI that requires financial institutions to treat consumers fairly[2]. CoFI specifies when the fair conduct principle applies[3].

The requirement to establish, implement and maintain an FCP[4] consisting of PPSCs is an opportunity for financial institutions to establish a meaningful framework to support their whole consumer proposition.

### Findings and good practice

The majority of FCPs clearly outline how the financial institution would comply with the fair conduct principle to treat consumers fairly. In many instances, financial institutions have reviewed existing conduct frameworks to incorporate the fair conduct principle into their PPSCs.

**Spotlight**

**Fair conduct principle linked to purpose and conduct framework**

A small deposit taker explains how its conduct framework embeds the fair conduct principle into key areas, such as product design, distribution and employee support, and demonstrates consideration for the fair conduct principle throughout the product and distribution lifecycle.

The framework is further explained by linking to the financial institution's key consumer outcomes. These are summarised in graphics, making it easy to understand.

Consumer outcomes are supported by specific outcome drivers and enabled by the financial institution's management and governance. This approach clearly ties the fair conduct principle to the deposit taker's own vision, providing a comprehensive overview of how fair consumer outcomes are achieved.

**Recommendations**

The fair conduct principle is at the heart of CoFI. FCPs are a structured representation of how financial institutions provide fair consumer treatment in a consistent manner. Financial institutions should reflect on what the fair conduct principle means within the context of their business, its relevance to their operations, and how it connects to their specific PPSCs.

[2] Financial Markets (Conduct of Institutions) Amendment Act 2022, s446C
[3] Financial Markets (Conduct of Institutions) Amendment Act 2022, s446D
[4] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446G

## Making the FCP relevant

**What we want to see**: FCPs are relevant and proportionate to the financial institution's business. Financial institutions can demonstrate how they have considered the specific factors that characterise their business, including its nature, size and complexity[5], and how these factors influence the PPSCs that are included in their FCP. This will support financial institutions in recognising and addressing the risks that are pertinent to their business, improving the effectiveness of the FCP.

### Findings and good practice

The majority of financial institutions considered the particular aspects of their business when establishing their FCP, for instance explaining their consumer base and the specific details of their services or products.

We also observed financial institutions leveraging their FCP to articulate how their culture and values align with the fair conduct principle, embedding these commitments within their broader approach to conduct and consumer outcomes.

**Spotlight**

**Points of difference explained for niche product offering**

A small insurer that offers insurance through third parties provides a history of its business and operations, an overview of strategic objectives and information about the different types of insurance products it offers. For each product, it explains the objectives and target consumers. The insurer also explains how it monitors its distributors and intermediaries to ensure they treat consumers fairly.

**Recommendations**

Considering nature, size and complexity when developing an FCP allows financial institutions to focus on what is most relevant to them. This might be, for example, the products and services they offer, how these are delivered, the business model, ownership structure, regional considerations, and who their consumers are.

[5] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(2)

## Policies, processes, systems and controls, and the FCP structure

**What we want to see**: Financial institutions choose a structure for their FCP that is relevant and proportionate to their business[6].

FCPs use plain language and are easy to navigate, to ensure they are understood and useable by staff. Supporting documents and additional PPSCs are easily accessible.

Financial institutions identify the specific risks that could impact the fair treatment of consumers. Financial institutions consider these risks when designing their FCP and deciding what PPSCs will be included in it.

### Findings and good practice

The majority of FCPs are structured as a framework consisting of various new and existing supporting documents. These FCPs typically include a description of the purpose of the FCP and how it fits in with the organisation, and refer to supporting documents that contain additional information. Some smaller financial institutions have an 'all-in-one' FCP that captures all PPSCs in a single document.

Most FCPs are clear, written in plain English and laid out in a way that is easy for readers to engage with. The majority are principles-based rather than focusing on 'tick-box' compliance.

We observed instances where PPSCs are recorded in a combination of the FCP itself and separately documented supporting PPSCs. Larger, more complex financial institutions tend to have a large number of PPSCs to manage risk across business units and functions. We saw financial institutions adopt a number of practices to make their FCPs easy to use and navigate, including:

- using a table to record PPSCs and mapping these against the minimum requirements
- creating a PPSC glossary with definitions
- providing hyperlinks to where additional information can be found
- categorising PPSCs into groups to improve accessibility
- using appendices to record additional information such as policy owners and frequency of reviews.

**Spotlight**

**FCP effectively linked to existing conduct policies**

A medium-sized deposit taker integrates its FCP with its policies and principles, many of which intersect with the fair conduct principle. The principles are part of the operating model (i.e. are already embedded in the business), as referenced in the policies, standards and procedures.

**FCP structure is tailored around the fair conduct principle**

While most financial institutions have listed the minimum requirements and explained how the FCP meets these, others have taken a different approach. One large insurer drafted its FCP around its principles

[6] There is no prescribed template that an FCP must follow, but FCPs must be in writing and cover the PPSCs a financial institution has in place to ensure consumers are treated fairly. See Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)

rather than the minimum requirements, tailoring the FCP to its business in a way that is clear and easy to follow. Financial institutions may choose to list the minimum requirements or map the PPSCs to them to demonstrate compliance with the obligations, but this is not mandatory. Other approaches may also be used to meet the requirements.

**Recommendations**

How financial institutions structure their FCP can have a significant impact on how relevant and effective it may be. As there are no prescriptive requirements regarding structure, financial institutions should design their FCP based on what works best for the business. They should consider who their FCP is written for, how easy it is to access relevant information, and whether information is presented in a clear way.

# Products and services

**What we want to see**: Consumers have access to appropriate products and services that meet their needs.

FCPs must include PPSCs that relate to product design, distribution and review, to ensure consumers continue to receive fair treatment and their objectives are being met. Financial institutions must also ensure that if deficiencies are identified, these are remedied within a reasonable timeframe, and that they complete any required enhancements or improvements to products and services.[7]

### Findings and good practice

Most FCPs include a table that captures basic information about the types and characteristics of products offered by the financial institution. To supplement product tables, some financial institutions included additional details about product design, target market determination, product lifecycle and review processes.

The information in FCPs is often presented in summary form with references to a separate policy that contains comprehensive details about the product-related PPSCs used by the organisation.

Some financial institutions have identified consumer objectives, target markets and potential harms associated with their products, and shaped their PPSCs to reflect this. Some FCPs provide a description of the link between product design and fair consumer treatment, while others reference supporting documents for easy access. Clarity is further enhanced where FCPs use plain language to describe products and services.

[7] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)(b)

**Spotlight**

**Focus on products with specific characteristics**

Some financial institutions clearly demonstrated that their FCP has been tailored to their products and services. Two insurers proactively reviewed the products and services they offer and identified that the provision of legacy or closed products has a risk of consumer harm. Having identified the risks associated with these products, these financial institutions were able to describe how they will mitigate the risk and record what additional PPSCs are being used.

**Linking the fair conduct principle with product design principles**

One FCP maps out the fair conduct principle against the financial institution's in-house product design principles. This demonstrates how the FCP has been tailored to the business and provides the reader with a better understanding of the impact product design can have on consumers. The FCP contains a plain-language description of the product design principles and includes a link to a policy that contains additional information. The FCP also touches on the overarching objective of ensuring consumer outcomes are considered at the design phase of the product lifecycle.

**Recommendations**

How products and services are designed and distributed has a significant impact on the ultimate outcomes consumers experience. Financial institutions should consider the impact their products and services will have on consumers and put PPSCs in place to ensure consumers are treated fairly.

Financial institutions should consider how products are designed, marketed, sold and managed throughout the entire product and consumer lifecycle – pre-sale, point of sale and post-sale. This includes assessing how consumer needs may evolve over time, and how technology and innovation could impact both the risks and the opportunities associated with providing products and services at each stage.

## Types of consumers, including those in vulnerable circumstances

**What we want to see**: Consumers, especially those in vulnerable circumstances, are treated fairly by financial institutions.

Financial institutions are required in their FCP to have regard to the types of consumers they deal with, including those in vulnerable circumstances[8]. They should understand the characteristics of consumers, including potential vulnerabilities. The FCP should capture this information, outline how the financial institutions will manage these consumers, and record what PPSCs have been put in place.

[8] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(2)(d)

## Findings and good practice

In general, FCPs included a high-level description of the types of consumers the financial institution deals with, and recorded basic segment details such as the number of consumers, the products held and the value of business. The majority of financial institutions had a specific policy regarding consumers in vulnerable circumstances, and many FCPs included a high-level description of how the financial institution deals with consumers in vulnerable circumstances.

Some financial institutions further described their consumers, providing information about consumer types, needs, demographics and target market considerations. We saw financial institutions completing assessments of the different customer characteristics, with some describing the link between the fair conduct principle, fair consumer outcomes and the PPSCs designed to manage the risks associated with specific customers characteristics.

We also saw some FCPs referencing guidance about consumers in vulnerable circumstances published by the FMA, the Ministry of Business, Innovation and Employment and the Council of Financial Regulators.

### Spotlight

**Comprehensive assessment of consumer types**

A financial institution went beyond the minimum requirements regarding types of consumers. Its FCP includes comprehensive information about the types of consumers it deals with, broken down by product category, consumer segment, value of business and types of vulnerability, along with an overview of how the financial institution interacts and communicates with its consumers. The FCP also refers to a dedicated consumer resolution team that is responsible for monitoring and reporting on clients experiencing vulnerability circumstances and for facilitating staff training on the subject.

**Approach to consumers in vulnerable circumstances**

One financial institution has comprehensive PPSCs in place to deal with consumers in vulnerable circumstances. It has implemented a consumer vulnerability standard that incorporates a firm-specific definition of vulnerable consumers. Its FCP:

- formally records roles and responsibilities with respect to vulnerable consumers
- describes how vulnerable consumers are identified and what training is provided to employees to recognise key signs of vulnerability
- has a control in place to ensure staff who interact with vulnerable consumers receive appropriate training
- specifies what PPSCs are in place to manage vulnerable consumers.

**Recommendations**

Financial institutions should understand who their consumers are and what objectives they have, and what fair treatment looks like for those consumers. By considering the needs of their consumers, financial institutions are more likely to create an FCP that is effective in ensuring those consumers are treated fairly.

Consumer vulnerability can manifest in many ways and is subject to change over time. Financial institutions could improve their understanding of vulnerability by regularly communicating with their consumers to monitor whether their circumstances have changed and their objectives are being met. Similarly, they could engage with third-party support groups such as mental health charities, debt and budget counsellors, disability support services, victims support groups, and addiction support entities, which could enhance their understanding and assistance of vulnerable consumers.

# Distribution methods and the use of intermediaries

**What we want to see**: Consumers are treated fairly by financial institutions, regardless of the distribution channel they use.

In their FCP, financial institutions are required to have regard to the types of intermediaries that are involved in the provision of their services and products.[9] They are also required to include PPSCs to ensure their distribution methods operate consistently with the fair conduct principle, and to regularly review the distribution methods to confirm that is achieved[10]. To ensure consumers receive products and services that suit their needs, distribution methods need to be fit for purpose.

FCPs document the respective roles and responsibilities of financial institutions and intermediaries, and how these support fair treatment. Financial institutions have adequate oversight of distribution partners, and FCPs include PPSCs to monitor whether distribution methods are operating consistently with the fair conduct principle.

Financial institutions understand the risks associated with different distribution methods, have PPSCs in place to mitigate these risks, and record this information in their FCP.

## Findings and good practice

Almost all FCPs include details about the financial institutions' distribution methods. A majority of the FCPs provide some level of detail around the roles and responsibilities involved in the oversight of distribution methods.

[9] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(2)(e)

[10] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)(b)

Several FCPs describe the controls in place for managing distribution channels, including governance of interagency contracts and review mechanisms. Some financial institutions have completed risk assessments of their distribution channels and have assurance measures in place to ensure fair treatment of consumers. We also saw examples of FCPs evidencing how the financial institution has considered risks related to intermediary remuneration and the use of incentives.

### Spotlight

**Clear process for oversight of intermediaries**

A small insurer outlines its underwriting agency agreements, explaining how these are reviewed, and how it ensures intermediaries receive support to provide products to end consumers. Distributors are monitored through quality assurance, and the results are reported to the board. The insurer also completes a risk assessment of each intermediary to determine the level of assurance activity required.

**Distribution methods are fit for purpose**

A large bank ensures its distribution channels for products and services are designed for the needs, characteristics and objectives of its consumers. The distribution strategy and distribution channels are considered in the product summaries and in the design phase. When products are reviewed, the bank ensures the distribution channels and distribution strategy remain fit for purpose.

**Consideration of incentives**

A large insurer explains how its remuneration policy sets its approach to assessing and managing third-party distribution risks, including risks relating to remuneration of intermediaries. The FCP outlines that contracts with third-party distributors need to comply with internal policy and the law, and the incentives need to comply with the CoFI Act.

# Training

**What we want to see**: Financial institutions' employees understand the fair conduct principle and what they need to do to treat consumers fairly. Training supports employees in building this understanding and FCPs include PPSCs relating to employee training.[11]

FCPs include training that is relevant and proportionate to the nature and size of the business, and training content is tailored for employees based on their roles.

Financial institutions have controls in place to monitor whether employees have completed and understood this training.

### Findings and good practice

Most financial institutions have existing training policies, which have been updated to include CoFI-specific training. In most cases, FCPs include high-level descriptions of the roles and responsibilities involved in training delivery, note that training will be provided on an initial and ongoing basis, and briefly touch on the

[11] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)(e-g)

consequences of insufficient training. Many financial institutions make use of a training register that records completion rates and the monitoring of employee understanding.

We saw examples where FCPs identify and record training needs for different groups of employees. Some financial institutions provide descriptions of the different training schedules and frequencies, the content of the training, and the assurance practices to monitor delivery, completion and outcomes (often alongside conduct dashboards and key performance indicators).

**Recommendations**

Training programmes need to be relevant, proportionate and tailored to the FI's business. To understand what training might be required, financial institutions may wish to consult the business units that will receive training. Financial institutions also need to consider what controls are required to monitor completion of training, for example a training register.

## Complaints process

**What we want to see**: Consumers and others who wish to make a complaint can do so easily, and the financial institution has processes in place to deal with complaints effectively, fairly and in a timely manner.

The fair conduct principle applies throughout consumers' interactions with financial institutions, including when a financial institution is responding to a complaint.[12]

The FCP includes PPSCs that are aimed at supporting consumers, intermediaries and internal staff to understand how to make a complaint, and to explain how complaints are handled, including the dispute resolution process.

It is also important for financial institutions to learn from complaints. Using analytics to interpret complaint themes and trends, FIs can identify areas of concern, conduct risk and potential compliance breaches, which can be promptly reported and addressed. Complaints can also provide early insights into product suitability and design.

### Findings and good practice

The majority of FCPs reference complaint processes and dispute resolution, outlining how consumers, agents and intermediaries can make a complaint. We have seen examples where FCPs provide detailed descriptions of the process, from submitting a complaint to resolution and root cause analysis. Some entities also explain how complaints from staff and intermediaries are considered and escalated.

[12] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446D (1)(d)

**Spotlight**

**FCP reflects the importance of analysing and learning from complaints**

A small insurer describes how it completes a root cause analysis of complaints, which assists in addressing the complaint and helps identify issues with products, services or communication. The analysis leads to improvements where necessary and contributes to overall risk management.

**Internal and intermediary complaints processes**

Some financial institutions outline processes for staff and third parties to raise concerns and complaints. A small insurer highlights its 'speak up' policy and how employees can safely report conduct that fails to comply with the fair conduct principle. Another insurer, which distributes its products largely through intermediaries, explains its expectations of intermediaries in handling complaints, as well as how complaints regarding intermediaries are managed.

**Recommendations**

Complaints represent an opportunity for financial institutions to get insights into their business and potential areas of conduct risk. Through effective resolution and analysis, financial institutions can reduce risk while improving the consumer experience and business reputation.

Most FCPs outline the complaints process but could provide more information on how financial institutions use complaints data in terms of analysis, reporting and addressing conduct risk.

We also recommend that financial institutions have adequate processes for monitoring complaints from or relating to intermediaries, and for staff to safely report issues or conduct risks – and that these complaints are adequately monitored and acted upon.

## Conduct risk

**What we want to see**: Financial institutions identify, monitor and manage conduct risks (i.e. risks associated with conduct that fails to comply with the fair conduct principle), and have clearly defined roles, responsibilities and accountabilities in place for managing those risks.[13]

Financial institutions need to identify the specific conduct risks the business faces, and document in the FCP the PPSCs that are in place to monitor and manage those risks.

For such measures to be effective, financial institutions need to ensure they have considered the types of consumers they deal with, the products and services they offer, and their distribution methods, to ensure conduct risks are identified, monitored and managed. The FCP also needs to include PPSCs relating to regular and comprehensive reporting on conduct risks to the board or other governing body of the financial institution.[14]

[13] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)(c)

[14] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)(c)(iii)

### Findings and good practice

We saw a number of measures used by financial institutions to identify, monitor and manage conduct risk, with respective roles and responsibilities for these documented in the FCP. Many FCPs describe the link between areas of conduct risk and the PPSCs that address them. Dashboards have also been exemplified by some financial institutions as an instrument to support risk identification, monitoring and management. Several firms outline the type of conduct metrics (i.e. lead and lag indicators) they use to detect risks.

**Spotlight**

**Identification of conduct risks**

One small deposit taker includes a conduct risk assessment within its FCP. The assessment covers areas of risk associated with products and services, considering their complexity, distribution methods and potential consumer impact. Based on the risks identified, the financial institution explains the mitigations it has in place for risks assessed as more severe.

**Recommendations**

Financial institutions should consider whether the PPSCs they have in place allow them to identify, effectively mitigate, manage and report conduct risk, and are proportionate to their business. They should consider conduct risks that are specific to their product offering, distribution methods, and consumer types. The PPSCs should be effective and enable the financial institution to respond to risks swiftly and escalate matters effectively where necessary.

## FCP governance and effectiveness

**What we want to see**: Financial institutions have appropriate assurance and governance processes in place to assess the effectiveness of the FCP. FCPs clearly record roles and responsibilities related to assurance processes. Assurance practices include PPSCs to determine whether the FCP is operating in a manner that is consistent with the fair conduct principle.

Financial institutions' assurance programmes and related reporting activities are proportionate to their size and designed to monitor the effectiveness of compliance with the fair conduct principle.

### Findings and good practice

Largely, financial institutions have explained in their FCP how the FCP is governed, showing the link between the board, committees, and assurance functions. The respective roles and responsibilities have generally been explained in a clear and realistic manner, relative to the nature, size and complexity of the business.

We have seen examples, particularly in larger financial institutions, of conduct committees that assess the effectiveness of the FCP. With regards to assurance, we saw some FCPs that describe the interaction between lines of defence, and others that explain the tools and mechanisms that support assurance, such as regulatory registers, risk management frameworks, FCP dashboards and project management frameworks (such as RASCI).

Some FCPs also identify what events would trigger an 'out-of-cycle' review, for example a material conduct issue, or a change to the business, its consumers or the market it operates in.

## Spotlight

### Consider the nature, size and complexity of the business

An insurer explains how it is a smaller subsidiary of a larger multi-national organisation. It reflects on the reporting and oversight lines between parent and subsidiary, and how it ensures the business's New Zealand governance structure has responsibility for governing its FCP. Furthermore, as the insurer's main line of business is commercial consumers, complemented by a smaller retail arm, it considers its simple product offering and tailors the FCP to the nature, size and complexity of the business to ensure its effectiveness.

### Use of conduct dashboards

Embedding the use of data to monitor and identify risks related to consumer outcomes in the FCP can support its effectiveness. Two different large insurers provided example of this. One links an FCP dashboard to its risk management system and provides a detailed view of the PPSCs along with a live and dynamic view of the related risks, controls and issues. The other uses quality assurance and consumer dashboards to track consumer insights. These are presented to the executive committee monthly for discussion and oversight, and are standing agenda items for its board conduct committee. Using up-to-date data to generate insights on consumer outcomes ensures that issues are detected in a timely manner and the FCP remains effective.

### Trigger events for review of FCP

We saw some good examples of financial institutions considering risk factors that would trigger an out-of-cycle review of the FCP. A medium-sized bank identified the elements it would take into consideration in its regular annual review, along with trigger events that would prompt a review and update of the FCP, such as business changes, audit findings, legislative change, guidance from regulators, conduct failures, and changes to policies, processes, standards and procedures

A smaller deposit taker highlights several factors that would signal that a policy, process or system may not be working as intended or is no longer fit for purpose, such as consumer complaints, feedback from employees, clients or consumers, or economic or market shifts.

**Recommendations**

The assurance and maintenance of FCPs should be proportionate to the nature, size and complexity of the business and include regular reviews, as well as ad hoc reviews in response to trigger events. Financial institutions should ensure assurance activities support the detection of deficiencies in the FCP. Where deficiencies are identified, financial institutions need to update their PPSCs to ensure they remain relevant and effective in enabling fair treatment of consumers.

# Evolving risks and the FCP

Treating consumers fairly is not a set-and-forget activity. It is shaped by both internal and external factors, meaning that the best approach may change over time. As financial services and markets evolve, financial institutions must continually assess the impact that evolving risks have on fair treatment and adapt their FCP accordingly.

To ensure consumers continue receiving fair treatment, financial institutions need to adopt a proactive and forward-looking mindset for conduct risk management. Boards and governing bodies need to play an active role in ensuring this.

Viewing the FCP as a dynamic and iterative programme – rather than a one-time compliance exercise – will help financial institutions to be effective in managing evolving threats and opportunities. This approach is closely aligned with the requirements set out in the legislation, which require financial institutions to actively consider conduct risks[15].

### What we considered

In our review, we were interested in whether financial institutions considered any areas of evolving risk and how this was incorporated within FCPs, specifically in the following areas:

- **Innovation and digitalisation, including the use of AI:** The rapid adoption of AI and digital tools may introduce biases, information asymmetry and 'black box' outputs[16], and potential for reduced transparency where there are inadequate risk management and governance processes in place.
- **Technology and cyber, including technology uplift programmes and the use of legacy systems:** The financial sector may experience tension between outdated legacy software and costly technology uplift programmes. Uneven implementation of technology upgrades has the potential to cause harm and may result in undesirable consumer outcomes, particularly in the event of a data breach or outages.
- **Access to financial services** for underserved consumers: Financial literacy, the design of products and services, algorithmic bias and other barriers to financial inclusion disadvantage vulnerable sectors of society and restrict their access to financial services.

[15] Financial Markets (Conduct of Institutions) Amendment Act 2022 s446J(1)(c)

[16] FMA Occasional Paper Series: Understanding Artificial Intelligence in Financial Services

- **Consideration of economic pressures:** Cost-of-living pressures and financial stress may reduce access, while increasing the need for support for some consumers. A tightening economic environment may also push financial institutions into sales pressure and mis-selling.
- **Scams and frauds[17]:** Increasingly sophisticated scams, combined with digital financial services, raise the risk of consumer losses and harm.

While the majority of FCPs were relevant, proportionate and tailored to the financial institution's business, only a small number referenced the above areas of evolving risk. The FCPs that did include evolving risks took a relatively narrow approach, focusing on innovation and digital distribution. Consideration of other areas of evolving risk was rare. Financial institutions often conduct horizon-scanning analysis (PESTLE or similar), but many have yet to integrate these insights into their FCPs. Embedding this analysis within FCPs would strengthen the ability of financial institutions to anticipate and proactively manage evolving risks.

**Recommendations**

We encourage financial institutions to build on their conduct journey by fostering a culture that proactively identifies, monitors, and manages both current and evolving risks relevant to their business. To achieve this, financial institutions may find it useful to consider:

- the rapidly evolving financial services landscape and the implications for consumer outcomes
- identifying and mitigating not only immediate risks, but also scanning the environment for evolving risks
- the ongoing obligation to treat consumers fairly, which requires firms to continuously adapt and evolve their practices to ensure they remain fit for purpose

By building these principles into their FCPs, financial institutions will be more resilient and better placed to provide fair treatment to consumers in a consistent manner.

[17] Scams | Financial Markets Authority

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