Reserve Bank
of New Zealand
Te Pūtea Matua

Review of the Insurance (Prudential Supervision) Act 2010

Options Paper 4: Governance, supervisory processes and disclosure

15 November 2022

CONSULTATION
PAPER

General information

Information about the review, including the Terms of Reference, is available on the Reserve Bank website at:

https://www.rbnz.govt.nz/regulation-and-supervision/oversight-of-insurers/how-we-regulate-and-supervise-insurers/our-policy-work-for-insurer-oversight/review-of-insurance-prudential-supervision-act-2010

Submission contact details

The Reserve Bank of New Zealand - Te Pūtea Matua invites submissions on this consultation paper by 5pm on 21 February 2023.

Please note the disclosure on the publication of submissions below.

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Publication of submissions:

All information in submissions will be made public unless you indicate you would like all or part of your submission to remain confidential. Respondents who would like part of their submission to remain confidential should provide both a confidential and public version of their submission. Apart from redactions of the information to be withheld (i.e. blacking out of text) the two versions should be identical. Respondents should ensure that redacted information is not able to be recovered electronically from the document (the redacted version will be published as received).

Respondents who request that all or part of their submission be treated as confidential should provide reasons why this information should be withheld if a request is made for it under the Official Information Act 1982 ('OIA'). These reasons should refer to section 105 of Banking (Prudential Supervision) Act 1989, section 54 of the Non-Bank Deposit Takers Act, section 135 of the Insurance (Prudential) Supervision Act 2010 (as applicable); or the grounds for withholding information under the OIA. If an OIA request for redacted information is made we will make our own assessment of what must be released taking into account the respondent's views.

We plan to publish an anonymised summary of the responses received in respect of this Consultation Paper.

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1 Introduction

1.1 Background

1.1.1 In 2017, we began a review of the Insurance (Prudential Supervision) Act 2010 ('**IPSA**'). The first stage of the review, which comprised identification of issues at a high level and an initial public consultation process, was completed in 2017.[1] The review was suspended in early 2018 to allow resources to be focused on the review of the Reserve Bank Act. We announced the relaunch of the review on 1 October 2020.[2]

1.1.2 We are now in the second phase of the review, which involves releasing a series of options papers that work through different sections of IPSA.

1.1.3 This is the fourth and final options paper in the series. It discusses governance, supervisory processes and data disclosure.

The IPSA review process

1.1.4 In this second phase, we are working through IPSA, producing options papers on a range of issues initially identified in the 2017 issues paper.

1.1.5 These options papers are open and we do not have a fixed policy position prior to the publication of papers. The papers are designed to raise issues, explore ideas and seek input that we will draw on when making decisions.

Table One: Review Timeline

Consultation	Description	Options Paper and indicative date	
Scope of the Act and overseas insurers	Does the legislation apply to the appropriate range of entities? Treatment of branches and overseas insurers	Paper 1 Q4 2020	Completed
Policyholder security	Financial strength disclosures, solvency requirements, statutory funds, termination values and a policyholder guarantee scheme	Paper 2 Q3 2021	
Enforcement and distress management	Penalties for non-compliance, supervisory tools, and reviewing the distress management provisions available to the Reserve Bank	Paper 3 Q1 2022	

[1] The first issues paper, published in 2017, can be found here.
[2] The relaunch paper can be found here.

Governance, supervisory approvals, and disclosure	Responsibilities of directors and key officers, governance and the effectiveness of key control functions. Is the system for approving amalgamations, change of control and transfers appropriate? Discussion of use of legislation, standards, regulations and guidance notes.	Paper 4 Q3 2022	In process
Omnibus consultation	Our overall proposals for amendments to IPSA. Remaining minor issues – e.g. treatment of small insurers.	Q2/3 2023	Forthcoming

1.1.6 We had originally planned for five options papers, followed by a final omnibus paper setting out all our proposed amendments to IPSA. However, we felt there were relatively few 'new' issues remaining to include in a fifth paper. We have included the most significant issues that we had planned for the fifth consultation in this paper. The remaining relatively minor issues (including, amongst other things, treatment of small insurers) will be included in the omnibus consultation.

1.1.7 The omnibus consultation will predominantly contain relatively settled positions for final confirmation before the legislative process begins. However, there are also a few areas where significant optionality will remain (for example, group supervision).

1.1.8 We will publish the omnibus consultation in mid-2023. We will then seek Cabinet decisions and proceed to drafting legislation to implement the review. We do not expect primary legislation to be in place before the end of 2026.

Considerations shaping the options presented

1.1.9 The options for consultation have been developed based on stakeholder feedback from the 2017 issues paper and in light of recent developments in the insurance sector.

1.1.10 The 2017 issues paper attracted 42 submissions from a range of stakeholders including insurers, industry bodies and law firms. A high-level feedback statement providing a summary of responses was published in October 2017.[3] We have built on these responses to identify the most important issues for reform and shape our discussion of possible options.

1.1.11 Additionally, the discussion of options reflects the Reserve Bank's experience of supervision under IPSA and a range of important developments in the regulatory environment.

1.1.12 In 2016, the International Monetary Fund ('**IMF**') undertook a comprehensive review of New Zealand's financial sector as part of its global Financial Sector Assessment Programme ('**FSAP**'). The FSAP review evaluated New Zealand's alignment with the International

[3] The feedback statement review can be found here.

Association of Insurance Supervisor's ('**IAIS**') 'Insurance Core Principles' ('**ICPs**'). The ICPs are an outcomes-based global benchmark for systems of insurance supervision. The IMF identified a number of areas in which New Zealand's observation of the core principles could be improved.[4] The ICPs are a key point of reference in developing options for consultation.

1.1.13 The events leading to the liquidation of CBL Insurance Ltd also provided some valuable supervisory and policy lessons for us. We commissioned a report from John Trowbridge and Mary Scholtens KC on our supervision of CBL, to identify these lessons and we have indicated our commitment to comply with that report's recommendations.[5] There is considerable alignment between the report's recommendations and those in the FSAP review.

1.1.14 In particular, the Trowbridge-Scholtens report recommended:

- clarifying the Reserve Bank's ability to challenge the opinions of the Appointed Actuary and other professionals; and
- strengthening some guidelines that currently do not have the force of law and expanding the Reserve Bank's power to issue new prudential standards.

1.1.15 The Reserve Bank has conducted two important recent reviews relating to the insurance sector, whose findings will feed into the IPSA review. The Reserve Bank and the Financial Markets Authority ('**FMA**') published the findings of our joint review of life insurer conduct and culture in 2019 and we published the findings of our thematic review of the Appointed Actuary regime in 2020. The Culture and Conduct Review noted that some life insurers were complacent in considering conduct risk, showing weak governance and lack of focus on good customer outcomes. The Appointed Actuary review concluded that the Appointed Actuary role remained valuable but also identified some lack of clarity around expectations.

1.1.16 The International Accounting Standards Board ('**IASB**') has released a new international accounting standard for insurance contracts (IFRS 17 *Insurance Contracts*), which will affect some of the definitions used in IPSA.

1.1.17 Finally, where appropriate, we will seek to align IPSA with the other sectoral acts that the Reserve Bank administers.

1.1.18 Following the Treasury's review of the former Reserve Bank of New Zealand Act 1989, our legislation is being restructured. Our institutional structure and governance are now set out in the Reserve Bank of New Zealand Act 2021 ('**RBNZ Act**'). There will be three 'sectoral acts' sitting beneath that institutional framework: IPSA, the Financial Markets Infrastructures Act 2021 ('**FMI Act**') and the Deposit Takers Bill ('**DTB**') (which is intended to replace the current Banking (Prudential Supervision) Act 1989 ('**BPSA**') and the Non-bank Deposit Takers Act 2013 ('**NBDT Act**'). The Deposit Takers Bill is currently before the Finance and Expenditure Committee.

1.1.19 While there are important differences between the sectors we regulate, there are also some core similarities in how financial sector prudential regulation is carried out. We will seek to apply similar rules to each sector unless there are good reasons for different treatment.

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[4] The IMF's recommendations and assessment, published in 2017, can be found here.
[5] The Trowbridge-Scholtens report can be found here.

1.1.20 When we discuss alignment with the planned legislation for deposit takers in this paper, we refer to the version of the DTB as at the date of this paper. As this IPSA review progresses, we will consider in tandem any amendments to the DTB as it proceeds through the legislative process.

1.2 This consultation

Overview: governance, data and a more proactive approach to supervision

1.2.1 The previous consultations in this stage of the IPSA review have explored: the scope of IPSA and how it applies to different kinds of insurance entity, provisions relating to policyholder security (including solvency capital requirements), and tools for enforcement and distress management.

1.2.2 This consultation is particularly concerned with how the legislation facilitates supervisory oversight of insurers. We wish to ensure that IPSA provides a solid underpinning for the more proactive and intensive approach to supervision that we have been developing across all the sectors we regulate. We will look at: rules around governance and risk management, supervisory oversight of significant restructuring transactions, and how we gather and publish data to support supervisory and market discipline.

1.2.3 The Reserve Bank's approach to insurance supervision has gradually evolved over time. Under IPSA, we have two core purposes: to promote the maintenance of a sound and efficient insurance sector, and to promote public confidence in the insurance sector.

1.2.4 Our prudential supervision is underpinned by a 'three pillars' approach: market discipline, self-discipline and regulatory discipline. Calibration of the three pillars is adjusted from time to time to reflect developments in international best practice and changes in domestic circumstances. Over the past decade, we have shifted to placing greater emphasis on regulatory discipline.[6]

- Market discipline reflects the influence that market participants can have on an institution's behaviour and risk profile. The Reserve Bank supports market discipline in the insurance sector, by requiring the disclosure of information which supports the ability of market participants to make informed decisions and exert influence.

  In our second options paper (*Policyholder Security*), we discussed some policyholder-oriented disclosure: ratings and solvency information. In this consultation, we will examine our broader powers to gather information from, and require disclosure by, insurers. In particular, we will ask whether our existing information-gathering and disclosure powers require enhancement, to facilitate us publishing data for the purpose of supporting market discipline.

- Self-discipline concerns insurers' internal risk management and governance systems – ensuring that internal decision-making structures, policies and procedures support the soundness and efficiency of the insurer.

[6] For an overview of the development of the three pillars approach over time, see Chris Hunt 'A short history of prudential regulation and supervision at the Reserve Bank' *Reserve Bank Bulletin* Vol.79 No.14 August 2016. For a recent statement of our current approach, see Christian Hawkesby 'Our transformation as a prudential regulator', speech given to the Financial Services Council, 22 September 2022 (available here)

The Reserve Bank's role is to monitor how self-discipline is operating and verify that appropriate governance and monitoring settings are in place. Over time, our approach has shifted away from relying on director attestations (confirming that appropriate procedures are in place) towards undertaking more supervisory verification that governance, control and risk management functions are well-designed and operating effectively. We describe this as a more intensive and proactive approach to supervision.

- Regulatory discipline involves the setting of rules and requirements. These are IPSA and associated regulations and standards.

1.2.5 A key purpose of this consultation is to understand how IPSA can support a more proactive approach, including by empowering us to set out and (where necessary) enforce clear expectations for governance, controls and risk management. In this consultation, we propose that IPSA should empower a range of additional standards so that we can both clarify our expectations of insurers and create rules with greater enforceability.

1.2.6 Our approach will remain risk-based. Our expectations for good governance should be well aligned with insurers' own commitment to good business practice. For many insurers, then, governance and risk management requirements will largely reflect existing practice and verification will be straightforward. However, where an insurer breaches our regulatory requirements, it is necessary that we are able to use our enforcement tools to intervene.

1.2.7 Overall, the 'three pillars' approach remains in place. This consultation is concerned to ensure that the IPSA regime supports the recalibration of the three pillars and our move towards a more proactive approach to supervision.

Consultation contents

Governance, key officers and control functions

1.2.8 The first part of the consultation explores how IPSA enables the Reserve Bank to regulate and monitor insurers' governance settings.

Key officers: fit and proper and officers' duties

1.2.9 We begin with key officers - that is, directors and 'relevant officers' (chief executives, chief financial officers, and appointed actuaries).[7]

- *Fit and proper*: We propose some expansion to current fit and proper requirements applicable to key officers. We suggest fit and proper requirements should be extended to apply to senior managers. We also propose that insurers be required to seek Reserve Bank approval before key officers are appointed, and to notify us if they become aware of any information that casts doubt on a key officer's fitness and priority.
- *Key officer duties*: We explore the statutory duties that apply to key officers under IPSA. Given the potential impact of insurer distress on the wider economy and society, we ask whether it is appropriate to impose broader statutory duties on directors. One option would be to impose a duty to exercise due diligence to ensure compliance with prudential obligations. Alternatively, we could consider a more extensive executive accountability regime along the lines of those in the UK and Australia.

[7] As defined in section 6 of IPSA.

- *Role of appointed actuary*: We then consider the role of the appointed actuary. A key finding of our appointed actuary thematic review was that expectations of appointed actuaries' duties are not sufficiently defined. We propose that IPSA empower a standard that would set out appointed actuaries' duties more clearly. We suggest that appointed actuaries be subject to a statutory duty of due diligence, similar to what we are proposing for directors. We also ask whether stakeholders consider it helpful to introduce an actuarial advice framework for insurers, similar to the one that exists under the Australian regime.

- *Consideration of policyholder interests*: For both directors and appointed actuaries, we ask whether there should be any explicit requirements upon them to consider policyholder interests.

- *Banning orders:* Under IPSA, the Reserve Bank may apply to the court to ban a person from participation in the insurance industry, on grounds of serious or persistent misconduct by that person.[8] We ask whether if due diligence duties were imposed, serious and persistent failure to comply with those duties should also be grounds for issuing a wider banning order.

- *Role of auditor*: Finally, we propose that auditors should be required to notify the Reserve Bank if they become aware that an insurer is failing to comply with its accounting and financial reporting obligations.

Governance and risk management

1.2.10 In this part of the consultation, we ask whether it would be appropriate for IPSA to empower standards that set out clearer and more enforceable requirements for insurers' governance and risk management. We also propose introducing a capital and risk management process (i.e. an Internal Capital Adequacy Assessment Process or Own Risk and Solvency Assessment).

Supervisory processes

1.2.11 The second part of the consultation looks at supervisory processes and approvals.

- *Consulting with the FMA*: We ask whether IPSA should include a requirement for the Reserve Bank to consult with the FMA when making licensing decisions, given that insurers will be subject to additional licensing by the FMA in relation to conduct, under new legislation.

- *Approvals of restructuring transactions*: We then discuss provisions of IPSA that are designed to ensure supervisory scrutiny of significant restructuring transactions (change of control, change of corporate form, transfers, amalgamations and some statutory fund restructuring).

  We suggest that the current provisions do not always facilitate a process that is proportionate to the risk associated with a particular transaction. In particular, we note that changes in control can have widely varying significance. We propose to reorganise the relevant provisions into a single approvals process for all restructuring transactions

[8] Sections 222 to 228 of IPSA.

(other than restructures of statutory funds). The process would provide the Reserve Bank greater flexibility, so that our assessments may be more effectively risk-based.

- *Consideration of policyholder interests by the Reserve Bank*: We consider how the provisions governing restructuring approvals should work, to ensure proper consideration of policyholder interests (including in the case of statutory funds).
- *Other issues*: Finally, we consider issues around the scope of transactions caught by the approvals process and some procedural and timing considerations.

Data and disclosure

1.2.12 The final part of the consultation considers disclosure requirements.

1.2.13 We ask whether IPSA should empower a 'data and disclosure standard', alongside the existing information-gathering provisions. While current information-gathering powers are adequate, we consider that a standard will better support the publication of comparative data on individual insurers. A standard could be used to facilitate publication of a limited and well-defined subset of insurer data to facilitate market discipline at some point in the future. A standard might also be more administratively convenient for regular data collection.

Consultation scope and interactions with other policy work

1.2.14 Several of the proposals in this consultation concern the empowerment of new standards under IPSA. If these proposals were adopted, the standards would need to be produced once new legislation was in place. Any standards would be developed through a separate policy process, including extensive consultation with stakeholders.

1.2.15 We do discuss the potential scope of standards, and issues that could be addressed by standards. However in general, this consultation is not concerned with the detailed content of any standards. In terms of submissions then, we are primarily interested in whether stakeholders think it would be appropriate to empower new standards under IPSA, and high level comments on scope.

1.2.16 We are currently carrying out a joint thematic review of both deposit takers' and insurers' governance, in conjunction with the FMA.[9] The findings of the review will not be available until mid-2023 However, we do not consider that this will impact the current IPSA consultation process, which has a high-level focus. Many of the thematic review's findings are likely to be at a more detailed level than is relevant to this consultation. The findings will be more useful when we either develop a standard or revise our current guidance and supervisory practices. The thematic review findings will be available before we make any final recommendations to Cabinet on reforms to IPSA and will be taken into account at that stage.

1.2.17 One reason for considering greater use of standards is that they are directly enforceable, unlike guidance. Our third options paper in this series concerned enforcement powers under IPSA. While we have not made final decisions on our proposals for reform to enforcement powers, we note that the DTB proposes civil pecuniary penalties as the main tool for enforcing standards. We are likely to consider following that approach for IPSA.

[9] For more information about the cross-sector review on governance, see here.

1.2.18 The data and disclosure section is concerned with disclosure under IPSA, and does not discuss insurer financial statements (which are regulated under the Financial Markets Conduct Act 2013). Our discussion is also focussed on collection of data. It is possible that we will also consider requiring insurers to disclose other information in the future (e.g. some version of the reporting that is carried out under risk management or risk and capital processes). However, we would decide that in the context of consulting on any new standards, as part of implementing any new legislation.

2 Governance, key officers and control functions

2.1 Overview: governance, risk management and greater use of standards

2.1.1 The International Association of Insurance Supervisors ("IAIS") helpfully describes good governance in terms of promoting 'the development, implementation and effective oversight of policies that clearly define and support the objectives of the insurer' (ICP 7.0.1). This is achieved by (among other things) defining the roles and responsibilities of people accountable for the management and oversight of the insurer.

2.1.2 Good governance primarily benefits insurers since it underpins business resilience and success. Equally, ensuring good governance is primarily the responsibility of the insurer, particularly its board.

2.1.3 Prudential regulators also have an important interest in aspects of good governance because governance plays an essential role in underpinning financial soundness.

2.1.4 Prudential regulation is necessary because insurers are paid in advance for the services they provide and those services are subject to risk and uncertainty. A key role for prudential regulation is to encourage insurers to make appropriate financial provision for risk so that, when claims come to be made, insurers are able to meet their obligations to policyholders.

2.1.5 This goal cannot be achieved where governance is poor. Regulators can set minimum solvency capital requirements for insurers, but those requirements need to be determined relative to the risks insurers are exposed to. Those risks can only be established where insurers have good procedures for assessing and monitoring risk. In any case, capital requirements alone are insufficient to ensure insurers' soundness. Risk needs to be given appropriate consideration when insurers are setting strategic objectives and considering how to implement them. Insurers also need to have appropriate procedures and controls in place to assess and manage risk and a robust risk culture.

2.1.6 Prudential regulators therefore have an interest in ensuring a certain standard of good governance, with particular emphasis on risk management and control functions.

2.1.7 IPSA already reflects this interest. It contains a fit and proper regime to ensure that directors and 'relevant officers'[10] of insurers are suitably qualified and of good character. The appropriateness of an entity's governance arrangements is assessed when the entity applies to be licensed as an insurer, and as part of some of the supervisory approvals discussed in the second part of this consultation. All licensed insurers must have a risk management programme in place and are obliged to comply with that programme. Finally, insurers'

[10] As defined in section 6 of IPSA.

directors are obliged to prepare annual attestations to the effect that the insurer has systems in place for the purpose of complying with prudential regulations, preserving the integrity of financial statements and solvency calculations.

2.1.8 However, IPSA provides limited mechanisms for enabling supervisors to monitor and assess insurers' governance and risk management on an ongoing basis.

2.1.9 An insurer is required to obtain the Reserve Bank's approval before it makes material changes to its risk management programme.[11] The Reserve Bank will also reassess the adequacy of governance arrangements at the point that a person applies for regulatory approval of a change in control or change of corporate form affecting the insurer. The Reserve Bank can also exercise powers where an insurer exhibits serious governance problems to the extent that the insurer is no longer carrying on business in a prudent manner or where the Reserve Bank believes that an insurer's key officers are not 'fit and proper' for their roles.

2.1.10 However, IPSA is generally designed with the idea that the primary means for assurance of ongoing good governance is director attestation. There is relatively limited scope for the Reserve Bank to 'look behind' those attestations to ask how governance is operating on an ongoing basis.

2.1.11 In keeping with that approach, the Reserve Bank's expectations on governance and risk management are set out in relatively brief guidelines, prepared largely for entities seeking an insurance licence. As a result, insurers may feel that there is insufficient clarity about what our expectations are and, therefore, what should inform director attestations. On a day-to-day basis, there is a risk of inconsistency in the degree to which supervisors engage on governance issues, and both supervisors and insurers may lack a well-defined framework through which to do so.

2.1.12 For some time, the Reserve Bank has been developing a more proactive approach to supervision in which we supplement reliance on director attestations with discussions about the processes and evidence that sit behind those attestations. We also note that both the IMF FSAP and the Trowbridge-Scholtens report into the failure of CBL identified a lack of enforceable, ongoing governance and risk management requirements as a significant weakness in New Zealand's insurance regulation.

2.1.13 In this consultation, we propose amending IPSA so that it empowers us to issue a wider range of standards.[12] Producing standards would clarify our expectations of insurers and provide a framework within which supervisory engagement on governance and risk management could take place. The shift from guidance to standards would also make rules more directly enforceable.

2.1.14 We appreciate that there are a variety of ways of carrying out 'good governance' and organisation-wide risk management. We also note the variety within the New Zealand insurance sector, with wide differences in the size and complexity of insurers' operations. Standards would need to be drafted in ways that would allow some flexibility to enable rules that were proportionate, given this diversity.

[11] Section 73 of IPSA.

[12] The Reserve Bank has some existing standard-making powers. We may issue (and have issued) a Fit and Proper Standard under section 36 of IPSA, and a set of Solvency Standards under section 55 of IPSA.

2.1.15 In this consultation we are asking whether IPSA should empower us to produce a wider range of standards, rather than on the content of any standards. The scope and purpose of any standards would be set out in IPSA but the exact content would be worked through as part of the implementation process, once any amended legislation is in place. The drafting and publication of standards would involve further full public consultations.

2.1.16 However, in making the case for new standards, we think it is helpful to give a broad indication of the type of content we would expect to be included to assist readers in assessing whether standards are likely to be useful or necessary.

2.1.17 In the sections of this paper that propose introducing new standards, we are primarily interested in whether or not the Reserve Bank should be empowered to set standards. However, if stakeholders wish to provide some broad comments about the appropriate scope of standards, they are welcome to do so.

2.1.18 As prudential regulator, we are particularly interested in:

- who makes up an insurer's board and what duties they have;
- how the board governs itself;
- how the board exercises oversight, particularly over risk and compliance issues; and
- the procedures that are required to ensure that oversight is effective.

2.1.19 This part of the consultation works through these issues in turn, exploring how IPSA currently regulates each issue and discussing possible changes.

2.2 Fit and proper

2.2.1 IPSA requires insurers to develop, implement, and comply with their own fit and proper policy.[13] In particular, a fit and proper policy must govern the qualifications, requirements and other criteria that a person must satisfy in order to be appointed (and remain) a director or relevant officer.

2.2.2 The Reserve Bank has also issued a Fit and Proper Standard,[14] which sets out the requirements of a fit and proper policy. This consultation is not concerned with the content of the current standard. Instead, the consultation looks at the legislative framework for fit and proper requirements.

2.2.3 Insurers must provide the Reserve Bank with a fit and proper certificate within 20 working days of the appointment of a director or relevant officer.[15] Under the Insurance (Prudential Supervision) Regulations 2010 ('**IPS Regulations**'), licensed insurers are also required to reassess each director or relevant officer against their fit and proper policy at least once every three years.

[13] Sections 34 and 35 of IPSA.
[14] The Fit and Proper Standard can be found here.
[15] Section 37 of IPSA.

2.2.4 The Reserve Bank has powers to remove a director or relevant officer, where it has reasonable grounds to believe that the person is not a fit and proper person to hold their position.[16]

Limitations and possible changes

2.2.5 The main issue with the current arrangements is that they do not sufficiently promote engagement between the Reserve Bank and insurers about the insurer's choice of appropriate key officers. At least formally, IPSA contemplates that the Reserve Bank must either passively accept a notification or take the very significant step of seeking to have a key officer removed.

2.2.6 The IAIS ICPs state that: the *supervisor* should assure itself that relevant officers are properly qualified (ICP5.2 & 5.3), that this should include senior management (ICP5.1), that assurance should be demonstrated on an ongoing basis (IPC5.2) and that regulated entities should be required to report any concerns that come to light (ICP 5.4).

2.2.7 IPSA currently places more emphasis on insurers monitoring their own fit and proper requirements. Under IPSA, the fit and proper regime does not apply to senior management and does not explicitly provide for ongoing monitoring by the Reserve Bank.

2.2.8 We think this is an area where it may make sense to align IPSA with provisions in the DTB, which address these issues.

2.2.9 Under the DTB, rather than a system of *ex-post* notification, deposit takers will be required to seek Reserve Bank approval before appointments are made, and the Reserve Bank will have the power to impose conditions of approval on appointments.

2.2.10 The DTB also contains a provision requiring deposit takers to notify the Reserve Bank if they become aware of information that might reasonably cast doubt on a relevant officer's fit and proper status. The justification is that the deposit taker will have greater opportunity to become aware of any problems than the Reserve Bank. This provision will incentivise ongoing scrutiny within the current 3 year reassessment period.

2.2.11 Finally, the current IPSA fit and proper requirements apply to directors and 'relevant officers'. Relevant officers mean the chief executive officer, the chief financial officer and the appointed actuary. However, in the DTB, requirements for New Zealand-incorporated deposit takers also apply to senior managers that report directly to the chief executive officer.

Q 2.2.1 Should IPSA be amended so that a licensed insurer must obtain the Reserve Bank's approval prior to appointing a director or relevant officer? Would this create any difficulties for insurers?

Q 2.2.2 Should insurers have a duty to inform the Reserve Bank if they become aware of information that might reasonably cast doubt on a director or relevant officer's ongoing fit and proper status?

Q 2.2.3 Are there any reasons for, or against, extending fit and proper requirements to senior managers? Is 'managers that report directly to the chief executive officer' a useful way of

[16] Section 39 of IPSA.

delineating who should be captured as a 'senior manager'?

2.3 Directors' accountability and duties

2.3.1 Once appropriate directors and relevant officers are appointed, it becomes necessary to ensure that they have appropriate accountabilities.

2.3.2 There are already extensive bodies of law which outline directors' accountabilities to the insurer itself. However, the same issues of trust and economic centrality that underpin the need for prudential regulation of insurers may also suggest the need for directors to have some broader accountability.

2.3.3 In this section, we look at existing director duties under the IPSA and discuss whether it might be appropriate to enhance those duties. (We look at the duties of appointed actuaries later in the paper.)

Existing duties and liabilities under IPSA

2.3.4 This section focuses on duties imposed on directors under IPSA. It does not consider any general duties imposed under other legislation or at common law.

2.3.5 If an insurer is convicted of an offence under IPSA, the directors of the insurer are also deemed liable if it can be proven that the relevant act took place with their authority, permission or consent; or that they knew (or could reasonably expected to have known) that the offence was committed and failed to take reasonable steps to prevent it.[17]

2.3.6 Directors of life insurers also have duties in relation to statutory funds held by the life insurer. All life insurers must have at least one statutory fund, which is a way of ring-fencing the assets that underpin the insurer's liabilities to its life policyholders.[18] Directors have a duty to take reasonable care, and use due diligence, to see that the life insurer: (a) complies with IPSA's requirements in relation to statutory funds and (b) gives priority to the interests of the referable life policyholders when investing, administering and managing statutory fund assets.[19]

2.3.7 In certain circumstances where a life insurer has contravened the statutory fund provisions and the contravention has caused loss to a statutory fund, directors may be personally liable to make good any losses caused by the contravention.[20]

Limitations and possible changes

2.3.8 The current regime creates potential director liability for offences under IPSA, but does less to impose ongoing positive duties.

2.3.9 The global financial crisis demonstrated the scope of harm that may result from failures of governance in financial services firms. This harm extends well beyond the impact on shareholders (the traditional focus of directors' duties).

[17] Section 216 of IPSA.
[18] This is unless the insurer has an exemption under the IPS Regulations.
[19] Section 105 of IPSA.
[20] Section 107 of IPSA.

2.3.10 In the wake of the crisis, regulators have shown increasing interest in creating personal liability for misconduct by directors or other senior office holders. The intent is to clarify responsibilities and expectations, sharpen incentives for good practice, and enable *ex-post* sanction for poor conduct.

2.3.11 Some jurisdictions have established extensive executive accountability regimes in banking and insurance (for example the Financial Accountability Regime in Australia, or the UK's senior managers and certification regime). These regimes involve: mapping responsibilities across an organisation and assigning each significant obligation to particular senior office holders; establishing duties of conduct in relation to those activities; and instituting penalties for non-compliance, from impacts on variable remuneration to civil pecuniary penalties imposed by the courts or disqualification.

2.3.12 The DTB, meanwhile, takes a more limited approach. It proposes to create a new duty for directors to exercise due diligence to ensure that the deposit taker complies with its prudential obligations. Due diligence includes taking reasonable steps to ensure that the deposit taker requires employees and agents to follow appropriate procedures, assesses the procedures in place, and promptly remedies any deficits discovered. Where a director breaches the duty, the courts can impose a civil pecuniary penalty of up to $1,000,000.

2.3.13 The extensive approach promotes careful consideration by firms and individuals about the accountabilities throughout an organisation. Under this approach, regulators may also impose broader duties. The UK regime requires senior managers to 'take reasonable steps' to ensure the area of business for which they are responsible is compliant with Prudential Regulation Authority ('PRA') rules and requires disclosure of issues to the PRA. The Australian regime imposes duties of honesty, integrity, care, skill and diligence as well as a duty to work with the Australian Prudential Regulation Authority ('APRA') in an open and constructive manner. Tying compliance with obligations to remuneration creates clear and immediate incentives for relevant officers.

2.3.14 However, the extensive approach is relatively complex and requires significant resourcing. It may also raise questions about the interaction between directors' duties under prudential legislation and other legislation.

2.3.15 The second approach, adopted in the DTB, is more limited. It imposes a duty upon individual directors to work towards compliance with prudential obligations. However, it is less prescriptive about how directors might seek to exercise that duty and requires less reporting to the regulator. Its coverage is also narrower, both in terms of the scope of the duties imposed and the individuals covered (i.e. it does not extend beyond directors to senior managers).

Q 2.3.1 Are current directors' duties under IPSA appropriate? Or is there a case for imposing wider duties, to reflect the potential impact of insurer distress on policyholders and the wider economy?

Q 2.3.2 If there is a case for broader duties, which approach is more appropriate: the narrower approach proposed in the DTA, the extensive approach adopted in the UK/Australia, or some other approach?

Q 2.3.3 Are there any other considerations you would like to draw to our attention when thinking about director's duties?

Policyholder interests

2.3.16 Under IPSA, directors of life insurers have a duty to the policyholders of life policies referable to a statutory fund. A director must take reasonable care, and use diligence, to ensure that the life insurer: (a) complies with the statutory fund provisions and (b) gives priority to the interests of the referable life policyholders, when investing, administering and managing assets of that statutory fund.[21]

2.3.17 The ICPs state that key officers should have duties to the insurer *and* policyholders (ICP7.4). This begs the question of whether policyholder interests are appropriately or sufficiently incorporated in directors' obligations under IPSA, particularly in relation to policies not held in statutory funds (i.e. non-life policies).

2.3.18 The ICPs suggest that key officers should have a general duty to act in the interests of policyholders. However, we are not aware of any jurisdiction where there is an explicit, direct, general duty to policyholders imposed on directors.[22] IAIS guidance on corporate governance tends to suggest that directors' obligations to policyholders are indirect, through their duties to comply with prudential regulation.

2.3.19 The duty proposed in the previous section (i.e. to exercise due diligence to ensure compliance with legislation) would indirectly strengthen directors' duties to policyholders. We note, though, that a duty to comply with legislation is likely to be weaker than a direct duty to policyholders, since prudential regulation generally sets minimum acceptable standards. We invite stakeholders to consider whether an indirect duty is adequate.

2.3.20 The duty imposed on directors of life insurers, under the statutory fund regime in IPSA, provides more explicit requirements. Arguably, this is justified based on the nature of life policies – they require the investment and administration of funds designed to back policyholders' long-term interests, often in circumstances where a store of value has been built up for policyholders that is being administered by the insurer on their behalf. It is also clear that, in event of a conflict between the interests of the relevant policyholders and the interests of shareholders or members of a life insurer, the director's duty is to take reasonable care, and use diligence, to see that the life insurer gives priority to the interests of relevant policyholders *over* the interests of shareholders or members. Generally, it is problematic to impose conflicting duties on directors in respect of the same matter.

2.3.21 We invite readers to consider whether there are any other activities where it would be appropriate to impose a duty on directors to consider policyholder interests in some form. This could range from ensuring that the insurer gives priority to policyholder interests or that the insurer actively considers those interests as part of its decision-making.

Q 2.3.4 Other than the duty to life policyholders established under the statutory fund regime, are there any other areas under the IPSA regime where directors or insurers should be obliged to consider policyholder interests or give priority to policyholder interests ahead of those of shareholders or members?

[21] Section 105 of IPSA.

[22] The Australian Insurance Act 1973 is an example of an *indirect* requirement. Section 2A(2) of that Act says that the objects of the Act are achieved by 'imposing primary responsibility for protecting the interests of policyholders on the directors and senior management of general insurers;' however the Act doesn't impose an explicit duty upon directors. The Australian life insurance legislation contains very similar duties in respect of statutory funds to those contained in IPSA.

2.4 The appointed actuary

Role and problem definition

2.4.1 The appointed actuary has an important role within the IPSA framework. The primary purpose of the role is to ensure that the board and senior management have access to expert and impartial actuarial advice so that they are in a position to make sound judgements about the risks the business is exposed to. However, the appointed actuary also has a broader role in giving advice on the integrity of the actuarial work carried out by the insurer, which may be relied on by external parties.

2.4.2 IPSA requires licensed insurers to have an appointed actuary,[23] appointed in accordance with the insurer's fit and proper policy.[24]

2.4.3 The appointed actuary's formal roles include:

- reporting on the use of actuarial information in financial statements;
- oversight and involvement in insurers' solvency calculations;
- actuarial advice on certain board decisions (such as making a distribution from a statutory fund or, in some cases, the implications of transfers or mergers); and
- producing a financial condition report which (amongst other things) provides an assessment of the way solvency calculations have been carried out and identifies material risks beyond those addressed by the solvency standard.

2.4.4 The two key words for understanding the appointed actuary's role are 'expert' and 'impartial'. The position is necessary because the valuation of a range of contingent liabilities is an inherently difficult expert task, involving both technical skill and prudent judgement. The appointed actuary's role is partly one of technical quality assurance and partly one of identifying and communicating potential risks to the business.

2.4.5 Being 'impartial' is important because the role should involve alerting the board to risks, even if doing so implies a challenge to current or intended business practices. The appointed actuary also provides assurance to outsiders that the actuarial information in the financial statements is appropriate. The appointed actuary has a limited 'whistle-blowing' duty of sorts: they are required to notify the Reserve Bank if they form the opinion that the insurer is failing to maintain a solvency margin (or is likely to fail to do so at any time within the next 3 years), is in serious financial difficulties, or is (or has been) acting fraudulently or recklessly.[25] While the appointed actuary reports to an insurer's management, a wider range of stakeholders need to be confident that they can rely on the appointed actuary's expertise and integrity.

2.4.6 The Reserve Bank completed a thematic review of the appointed actuary role in 2020. [26] An important finding of the review was that there is insufficient clarity about expectations of the appointed actuary role. That lack of clarity may also have contributed to some uncertainty

[23] Section 76 of IPSA.
[24] Section 34 of IPSA.
[25] Section 78 of IPSA.
[26] The 'Appointed Actuary Thematic' review report can be found here.

amongst insurers about how much resource needed to be devoted to the appointed actuary role, including in the event of a crisis.

2.4.7 The range of audiences for the appointed actuary's work also raises questions about what kinds of formal duties and accountabilities are appropriate. The thematic review found some weaknesses with insurers' and actuaries' awareness of conflicts of interest in the appointed actuary's work and strategies to manage those conflicts.

2.4.8 We suggest that standards could be used to clarify expectations around the appointed actuary's role, competences, and duties. We discuss the possibility of standards also including a broader actuarial advice framework for the insurer.

2.4.9 We then go on to discuss whether appointed actuaries' formal duties and accountabilities are appropriate for their role or whether there is a need to impose some form of additional statutory duty.

Role expectations, resourcing, and an actuarial advice framework

2.4.10 All licensed insurers are required to have an appointed actuary under IPSA. Particular responsibilities of the appointed actuary are set out in the IPS Regulations and relevant solvency standards. However, there is no single, comprehensive statement of the Reserve Bank's wider expectations of the appointed actuary's role and what the corresponding reporting arrangements should be from the appointed actuary to the board.

2.4.11 We propose that standards should:

- clearly set out the Reserve Bank's expectations for the appointed actuary's role;
- set out how the appointed actuary should fit into the insurer's broader governance structure, both in terms of reporting duties and the actuary's right to have access to different parts of the insurer's governance structure;
- require insurers to explicitly consider resourcing needs for the appointed actuary role, including:
    - whether an external appointed actuary has sufficient capacity to undertake the role; and
    - contingency plans, either in the context of crisis management or where an actuary was to unexpectedly resign.

2.4.12 We would need to determine which framework each of these elements best fits into: a new actuarial advice standard, a new governance standard, or the existing Fit and Proper standard. It would be important to ensure that there is consistency and clarity across the standards.

Q2.4.1 Would it be helpful for standards to:

(a) set out clearer expectations for the appointed actuary's role;

(b) set out the appointed actuary's place in the insurer's governance structures; and/or

(c) require insurers to explicitly consider resourcing needs for the appointed actuary role?

2.4.13 The Australian regime requires insurers to maintain an actuarial advice framework approved by the board, which sets out clearly which issues and decisions taken by the insurer require actuarial advice and when that advice should be given by the appointed actuary (with reference to an explicit materiality policy). The framework also sets out who should review those decisions and when actuarial advice should be considered directly by the board. Finally, the framework sets out procedures for identifying and managing conflicts of interest and duty arising in the appointed actuary role.

2.4.14 We think an actuarial advice framework represents good practice and would assist insurers, and particularly their boards, in clarifying the role of actuarial advice in the insurer's governance and risk management. On the other hand, it may increase the compliance burden on insurers. We welcome readers' views as to the value of requiring such a framework under IPSA.

Q 2.4.2 Would it be valuable to require insurers to have an actuarial advice framework in place under IPSA?

Accountabilities and duties

2.4.15 One key aspect of the appointed actuary role is the variety of audiences for the appointed actuary's advice.

2.4.16 The primary purpose of the role is to inform the insurer's board. However, financial condition reports prepared by the appointed actuary may also be designed to provide some assurance to shareholders that the insurer's financial statements are accurate.[27] The Reserve Bank places significant reliance on the appointed actuary as a source of information for supervisory purposes. Additionally, IPSA imposes a limited 'whistle-blowing' obligation on the appointed actuary: they are required to notify the Reserve Bank if they form the opinion that the insurer is failing to maintain a solvency margin (or is likely to fail to do so at any time within the next 3 years), is in serious financial difficulties, or is (or has been) acting fraudulently or recklessly.[28] However, there is no specific offence attached to any failure to do so.

2.4.17 Meanwhile, the appointed actuary works directly for the insurer. They are paid by the insurer and their key duties are defined through their relationship *with the insurer*.

2.4.18 In this section, we ask whether an appointed actuary's incentives, duties and accountabilities are appropriately aligned with their role. We invite readers to consider a range of possible changes to appointed actuaries' duties and accountabilities.

2.4.19 This issue is important because the Reserve Bank places considerable reliance on the appointed actuary's work when exercising its oversight of insurers. The appointed actuary is also expected to challenge the insurer's board and management where necessary, based on objective and impartial professional judgement.

2.4.20 Actuaries have professional obligations imposed by the New Zealand Society of Actuaries' ('**NZSA**') Professional Standards (in particular, to give accurate and objective advice). The NZSA also has its own disciplinary procedures.

[27] Financial condition reports are prepared by the appointed actuary under section 78 of IPSA.
[28] Section 78 of IPSA.

2.4.21 IPSA contains an offence for a person to make any false declaration or representation to the Reserve Bank, for any purpose relating to IPSA.[29] The Reserve Bank has the power to remove an appointed actuary if the Reserve Bank has reasonable grounds to believe they are not 'fit and proper' for their role[30] or if the Reserve Bank believes it is necessary to remove them in a context in which the triggers for issuing directions have been met.[31]

2.4.22 We are interested in whether the existing powers and offences are sufficient both to provide the appointed actuary with appropriate incentives and to deal with situations in which an appointed actuary is not performing their role adequately – particularly in terms of producing impartial objective advice that can be relied on by a variety of stakeholders.

2.4.23 One view is that duties and accountabilities are already correctly aligned.

2.4.24 The Reserve Bank may remove an appointed actuary from their position where we have reasonable grounds to believe that they are not a fit and proper person to hold the position, after having regard to the matters specified in the Fit and Proper Standard.[32] Process requirements and appeal rights apply to any exercise of removal powers.[33]

2.4.25 However, the Fit and Proper standard is quite brief. It is in the nature of 'negative assurance' – it is concerned with ensuring that officers *haven't* committed a crime (for example) but not with their positive skills and abilities. It does not contain great detail about what is expected of a fit and proper appointed actuary. From an enforcement perspective, that may make it difficult to make the case for removing an appointed actuary where there are otherwise good reasons to do so. Meanwhile, it may also make it difficult for an appointed actuary to refer to their statutory obligations as support, if they feel obliged to give advice that is challenging to an insurer's board or management.

2.4.26 Introducing an actuarial advice standard that clearly set out an appointed actuary's duties and referring to it in the Fit and Proper standard could significantly mitigate these difficulties and might be sufficient to provide the appointed actuary with appropriate accountability.

2.4.27 As mentioned, the Reserve Bank may apply for the removal of an appointed actuary. Arguably, this is an insufficient sanction where a failure on the part of the appointed actuary has already produced significant harm to other stakeholders, such as shareholders, investors or policyholders. In particular, the discovery of serious problems with actuarial advice might only come to light after the actuary's role with the insurer has already terminated.

2.4.28 It is possible that an appointed actuary could be subject to civil action based on a breach of their contractual duties. However, we note that the courts have upheld clauses in contracts with external actuaries that significantly limit liability for breaches of duty.

2.4.29 It might, therefore, be appropriate to introduce statutory duties for appointed actuaries that are broadly analogous to those we are proposing for directors. For example, if we introduced civil pecuniary penalties for insurers or their directors in response to a breach of standards, a similar penalty might be imposed on the appointed actuary for breach of their obligations and duties as set out in an actuarial advice standard (except to the extent that

[29] Section 215 of IPSA.
[30] Section 39 of IPSA.
[31] Section 149 of IPSA.
[32] Sections 39 of IPSA.
[33] Sections 42 and 43 of IPSA.

the actuary has behaved with a level of due diligence and competence expected of their profession).

2.4.30 Finally, it is worth considering whether actuaries should have any explicit duties in relation to policyholders. Given the complexity of insurers' financial affairs and policyholders' limited ability to scrutinise internal financial arrangements, the appointed actuary's technical expertise and responsibilities as an impartial voice potentially put them in a unique position to undertake this role.

2.4.31 One proposal is to impose a general duty upon the appointed actuary to consider and report on the interests of policyholders, either as a new provision of IPSA or as part of an actuarial advice standard.

2.4.32 An alternative proposal is to include requirements for the appointed actuary to advise on policyholder interests in particular contexts (e.g. as part of preparing the financial condition report).

Q2.4.3 To what extent do you think that the Reserve Bank's power to remove an appointed actuary based on fit and proper requirements provides adequate incentives and sanctioning power, in light of the role that appointed actuaries play in the regulatory framework?

Q2.4.4 Should the Reserve Bank impose a statutory duty on the appointed actuary to use due diligence to carry out their assigned role, enforceable with a civil pecuniary penalty?

Q2.4.5 Should appointed actuaries have a duty to identify and present the interests of policyholders? If so, should that be a general duty or only one that applies in specific contexts (such as preparing the financial condition report?)

2.5 The auditor

2.5.1 IPSA requires a level of interaction between the appointed actuary and the auditor of an insurer. Under IPSA, the auditor is subject to the same limited 'whistle-blowing' duty as the appointed actuary.[34] We note that there is a specific regulatory regime which applies to auditors of Financial Markets Conduct Act Reporting Entities (which include licensed insurers).[35]

2.5.2 However, the DTB contains an expansion to the 'whistle-blowing' obligations on auditors of licensed deposit takers. It is appropriate to consider whether such expansions should also apply to auditors of licensed insurers. Under the DTB, an auditor of a licensed deposit taker would have a duty to notify the Reserve Bank, if it is their opinion that the deposit taker is failing to comply with its accounting obligations and that disclosing non-compliance would assist the Reserve Bank in carrying out its regulatory functions.

2.5.3 The purpose of expanding notification obligations would be to reduce the information asymmetries between the insurer and the prudential regulator, in circumstances where receiving accurate and timely information is particularly vital.

[34] Section 215 of IPSA.

[35] Auditor Regulation Act 2011.

Q2.5.1 Should IPSA include a provision requiring auditors to notify the Reserve Bank if they become aware that an insurer is failing to comply with its accounting and financial reporting obligations?

2.6 Banning orders

2.6.1 The Reserve Bank has the power to remove a person from their role as director or 'relevant officer' of a licensed insurer, where it has reasonable grounds to believe they are not a fit and proper person.[36]

2.6.2 In particularly serious cases, the Reserve Bank may apply to the court for a banning order, whereby the court may ban a person from involvement across the insurance industry for a period of time, permanently, or until particular conditions have been fulfilled.[37]

2.6.3 Currently, the court may make a banning order where the person:

- has, in connection with an insurance business, engaged in serious wrongdoing and is not a fit and proper person to participate in insurance business; or
- as a director of a licensed insurer, has persistently or seriously failed to comply with IPSA or its regulations; or
- is a director of a licensed insurer that has persistently or seriously failed to comply with requirements under the IPSA or its regulations, and the person has persistently failed to take reasonable steps to prevent or stop that failure; or
- is subject to a similar ban in another jurisdiction.

2.6.4 On the face of it, the introduction of due diligence duties upon directors and appointed actuaries would be captured under the banning order provisions. That is, the duties would comprise a requirement under the IPSA, the persistent or serious breach of which may result in a banning order.

2.6.5 We seek feedback on whether it is appropriate for due diligence duties to be captured as part of the banning order provisions.

Q 2.6.1 Should a serious and persistent breach of statutory due diligence duties (if they were introduced) be grounds on which a court might issue an industry-wide banning order?

2.7 A governance standard? Board composition and operations

2.7.1 An insurer's board is at the core of its corporate governance. The board establishes and provides oversight over compliance and control functions throughout the business. It is therefore vital for good governance that the board itself has an appropriate composition, robust operating procedures, and systems for monitoring its own performance.

2.7.2 The proposals we have discussed so far relate to directors and 'key officers'. In this section, we turn to considerations about whether IPSA does enough to specify board composition and board activities.

[36] Section 39 of IPSA.
[37] Section 222 to 228 of IPSA.

2.7.3 Where monitoring and controls are weak or boards are not providing sufficient oversight and challenge to managers, serious problems may follow. Academic and industry studies of insurer failures frequently find that poor governance and leadership are major contributors to insurer distress.

2.7.4 IPSA provides for regulatory review of an insurer's governance arrangements at the point of licensing. The Reserve Bank has issued a guidance note on corporate governance arrangements, designed particularly to provide guidance for entities seeking an insurance licence.[38] An assessment of governance arrangements is also an important part of the supervisory approvals processes we discuss in part three of this consultation.

2.7.5 However, IPSA does not include specific ongoing requirements in relation to governance. The current guidance note on governance is relatively brief. We believe it may be useful to empower a governance standard to address this:

- A formal governance standard aids transparency – it clearly sets out the Reserve Bank's expectations. It may also promote and enhance consistency of approach across individual supervisors.
- A standard provides a better basis for the Reserve Bank to engage with the board meaningfully and effectively, enabling governance issues to be addressed at an early stage.
- Clear standards can provide a basis for supervisors to inquire as to how corporate governance is working in practice, identify weaknesses and seek to secure improvement.

2.7.6 We believe it is appropriate to address ongoing governance requirements via standard, rather than updating the existing governance guidelines.

- Both the Trowbridge-Scholtens report into the failure of CBL and the IMF's FSAP report (benchmarking New Zealand's regulation against international standards) recommended the introduction of enforceable governance rules into IPSA. Most other jurisdictions set out formal rules for good governance, and extensive governance requirements are included in the IAIS ICPs (in particular, ICP7 & 8).
- Unlike guidelines, standards are also enforceable if necessary. Decisions have yet to be made about the enforcement powers that will be contained in IPSA. However, we would consider enforcing governance standards via enforceable undertakings or through civil pecuniary penalties.
- Standards are a reasonably flexible way of setting rules, but also benefit from greater procedural safeguards than guidelines. They are secondary legislation, so they receive scrutiny and can be disallowed by the House of Representatives.

2.7.7 Appropriate board composition and formal rules do not necessarily guarantee good governance and some organisations may run effectively despite weak formal rule structures. Equally, the exact 'ingredients' of good governance, may vary depending on a business's requirements and culture. It is important that governance is appropriate to the underlying business and that rules do not stifle variation and innovation.

[38] The Governance Guidelines can be found here.

2.7.8 However, although appropriate formal rules do not guarantee performance, they are an important first step, providing a framework that can encourage good governance.

2.7.9 The content of governance standards varies across jurisdictions. At this point, our primary question is whether IPSA should empower a governance standard. The detailed content of a standard would be developed later as part of the implementation process, which would involve a full public consultation. Developing a standard would draw on the current cross-sector governance thematic review being carried out jointly by the FMA and Reserve Bank.

2.7.10 In broad terms, we expect that a governance standard will address the following elements:

- Board composition, including the balance between executive, non-executive and independent directors and their range of skills;
- The board's own governance – division of responsibilities and accountabilities, clarity of delegations, self-assessment of performance; and
- The establishment of particular board responsibilities or committees concerned with risk management, internal audit, compliance and remuneration, including ensuring that those committees have appropriate structures in place to monitor risk management and compliance throughout the organisation.

2.7.11 The drafting in standards can vary from prescriptive rules to broader principles-based and outcomes-focussed requirements. More prescriptive rules provide greater clarity and consistency but less flexibility.

2.7.12 We envisage a governance standard involving a mixture of the two types of rules. For example, there might need to be more prescriptive requirements for the proportion of independent directors on a board, but more principles-based rules on the structures in place to oversee risk management. The key guiding principle would be that the rules would create proportional obligations for all insurers, despite variety in size and business models.

Q 2.7.1 Do you agree that it would be appropriate for IPSA to empower a governance standard?

Q 2.7.2 Can you suggest any principles that should guide the drafting of empowering provisions or the design of governance standards?

2.8 Risk management

2.8.1 As a prudential regulator, we are particularly concerned with the extent to which an insurer's governance secures effective regulatory compliance and risk management.

2.8.2 There are two aspects to effective governance settings: ensuring that the board pays due attention to its oversight of compliance and risk management; and having appropriate procedures in place throughout the organisation to monitor compliance and risk, including procedures to feed information back to the board to enable effective oversight.

2.8.3 The first step is to ensure that compliance and risk management functions are effectively assigned within the board so that committees and/or individuals are given particular responsibility for oversight and for ensuring that the board is appropriately aware of risk and compliance issues. We consider that aspect is best dealt with as part of a corporate governance standard.

2.8.4 Risk officers and committees, though, can only function where appropriate procedures are present throughout the organisation to ensure that policy is implemented and issues are reported to the oversight committee or individual.

From a risk management programme to a risk management standard?

2.8.5 IPSA currently requires insurers to demonstrate that they have a risk management programme at the point of licensing and to comply with that programme.[39] It also requires insurers to obtain the Reserve Bank's approval prior to making any material changes to the risk management programme.

2.8.6 However, the legislation only sets out very general requirements for a risk management programme. The Reserve Bank has issued a guidance note providing more detail of what is expected, but the guidance note is not binding.[40]

2.8.7 Statutory mechanisms for keeping risk management plans up to date are also weak. Insurers are required to demonstrate to the Reserve Bank, at the time of applying for a licence, that they have procedures to ensure that their programme remains current. As mentioned, any subsequent material changes to the programme must be approved by the Reserve Bank. However, the only mechanism available to the Reserve Bank to require insurers to *update* their plans in response to new types of risk or developments in best practice is by adding an additional 'class of risk' by passing regulations. There is also no provision for the Reserve Bank to review or approve incremental (those that fall short of material) changes in risk management programmes over time.

2.8.8 We suggest that it would be preferable to set out risk management requirements in a standard. Risk management requirements and expectations would be clearer to insurers. Standards are relatively easier to update than statute, making it easier to update our requirements to take note of newly emerging risks. A detailed standard would also provide supervisors with greater ability to monitor and assess risk management policies and practice, rather than relying solely on insurers' own obligation to develop and comply with a risk management programme.

2.8.9 A risk management standard might also be used to set out requirements on managing outsourcing risk, managing reinsurance risk or risks emerging from intra-group transactions (as discussed in the previous consultation on *Scope of the Act and Overseas Insurers*).

2.8.10 Again, the content of a risk management standard would need to be determined through further policy work and public consultation. However, following the text of the DTB, we suggest that IPSA should empower a standard for managing an appropriate range of risks, including policies and processes to identify, measure, evaluate, monitor, report on, control, and mitigate those risks.

Risk and solvency capital – an ICAAP or ORSA for insurers?

2.8.11 A good risk identification/management system should also play an important role in the board's consideration of appropriate capital resources for the business. Additionally, there is scope for a risk and solvency capital approach to complement the more graduated approach to assessing solvency capital that we have signalled in previous consultations.

[39] Section 73 of IPSA.
[40] The Risk Management Programme Guidelines can be found here.

2.8.12 It is the insurer's responsibility to ensure it has adequate capital resources. The Reserve Bank has issued solvency standards which stipulate minimum capital requirements, but the insurer's responsibility to hold adequate capital is independent of minimum regulatory requirements. This position is already clear from the requirements that solvency standards place on the appointed actuary to report on any ways in which minimum solvency requirements do not adequately address risks the business is exposed to (as part of the financial condition report). More broadly, the board should establish its own risk appetite, monitor its capital holdings against that risk appetite, and consider the steps it needs to maintain an appropriate capital position.

2.8.13 In many comparable international regimes, there is an explicit requirement for insurers to have a process in place for assessing their capital needs over time, given their risk appetite and the risks they are exposed to. Equivalent requirements apply to the New Zealand banking sector. However, there is currently no such requirement under IPSA.

2.8.14 There are different ways of carrying out this process and different overseas jurisdictions do it in slightly different ways. Some jurisdictions require an 'Own Risk and Solvency Assessment' ('**ORSA**') (EU, US, Singapore) while others require an 'Internal Capital Adequacy Assessment Process' ('**ICAAP**') (Australia and the New Zealand banking system). However, most frameworks contain similar broad elements involving insurers:

- carrying out an assessment of their own risk-profile;
- establishing a statement of risk appetite;
- quantifying the amount of capital the insurer needs to hold, given its risk appetite and risk exposure;
- projecting future capital requirements;
- identifying potential sources of capital;
- specifying triggers for management action to maintain or increase capital as capital declines;
- identifying appropriate management action in response to capital weakness; and
- documentation and reporting of these processes.

2.8.15 Further policy work would be needed to work out what exactly would be appropriate in the New Zealand context, bearing in mind the need for proportionality, given the variety in size, form and business of licensed insurers. This policy work might also consider issues such as what role consideration of long-term risks, including climate risk, should play in the risk-capital process. This work would be carried out when we came to implement any standard. It would also be important to consider carefully how the risk management standard, ICAAP or ORSA, financial condition report, and any obligations relating to risk oversight in a governance standard would fit together.

Q 2.8.1 Do you think it is appropriate for IPSA to empower a risk management standard? Are there any high-level issues relating to standard scope or drafting of the empowering provisions that the Reserve Bank should consider?

Q 2.8.2 Do you think it is appropriate for IPSA to empower a standard requiring an ICAAP/ORSA process? Are there any high-level issues relating to standard scope or drafting of the empowering provisions that the Reserve Bank should consider?

3 Supervisory processes

3.1 Licensing

Consultation with the FMA

3.1.1 The Financial Markets (Conduct of Institutions) Amendment Act 2021 (**COFI**) introduces a new conduct licensing regime for insurers. Once the new regime comes into force (expected to be early 2025), insurers will need to operate under a 'financial institution licence' issued under the Financial Markets Conduct Act 2013 (**FMCA**), in addition to pre-existing FMA licensing requirements and to being licensed under IPSA.

3.1.2 It is important that the two regulators ensure that the conduct and prudential licensing regimes work together properly.

3.1.3 Under the new regime, the FMA must not decline an application for a 'financial institution licence' from an existing licensed insurer unless the Reserve Bank has given its consent. We may only withhold our consent if we are satisfied that doing so is necessary in order to maintain a sound and efficient insurance sector.

3.1.4 The FMA is required to consult with us before making licensing decisions under Part 6 of the Financial Markets Conduct Act, including the new COFI conduct licensing regime.[41] We propose that IPSA should be amended so that there is a reciprocal requirement for us to consult with the FMA before issuing or revoking an insurance license.[42] In practice, the RBNZ does consult with the FMA as a joint financial regulator and co-member of the Council of Financial Regulators.[43] However, we consider that providing a specific consultation requirement provides clarity and transparency about the process and co-regulator relationship.

Q 3.1.1 Do you agree that it is appropriate for IPSA to contain a requirement for RBNZ to consult with the FMA, before the RBNZ issues or cancels an insurer licence issued under IPSA?

3.2 Approvals for restructuring

Overview

3.2.1 Restructuring processes are an important part of a functioning insurance market. Allowing the sale and purchase of books of business or of shareholdings is an important way to maintain a free market in capital. It encourages market discipline and allows flexibility in the way that investors and businesses are brought together.

[41] Regulation 190 of the Financial Market Conduct Regulations 2014.

[42] We are also aware of the need to make the two regimes compatible more broadly. So, for example, the COFI legislation includes a provision that the same conduct cannot be subject to penalties under both our legislation and the FMCA. We are also in close communication with the FMA to coordinate supervision activities where appropriate.

[43] Subpart 4 of Part 6 of the RBNZ Act.

3.2.2 Where an insurer is subject to restructuring, it is important that supervisors can ensure that the restructure will not significantly weaken the governance and financial strength of the insurer or weaken policyholder security.

3.2.3 Legislation needs to strike a balance in a way that prevents the proliferation of transactions which reduce the prudential soundness of the sector, while also not unduly impairing the operation of markets for investment capital.

3.2.4 IPSA currently requires certain persons to notify the Reserve Bank in respect of a:

- a change in control of a licensed insurer;[44]
- a change in corporate form of a licensed insurer;[45] and
- a transfer of business or amalgamations between licensed insurers.[46]

3.2.5 In this paper, we describe the above transactions, collectively, as 'restructuring'.

3.2.6 While the provisions in IPSA are broadly appropriate, there are some practical issues with how the regime currently works. Depending on the form of restructure, different notification and approval requirements apply. We consider whether those requirements permit proportionate scrutiny of transactions, given the risks involved in a particular transaction. We consider whether requirements to consider policyholder interests in the restructuring context are appropriately specified. We also review some minor issues around the scope of the provisions and the timeline for approvals. These proposals are relatively independent and stakeholders may see some changes as more appropriate than others.

One test for all restructuring transactions

3.2.7 Currently, under IPSA, different tests and approval processes apply to changes of control or changes in corporate form, and to transfers and amalgamations. We query whether the current settings sufficiently allow the Reserve Bank to look at substance of (and risk presented by) the transaction, over form.

Current arrangements

3.2.8 The 'change of control / change in corporate form' test asks whether, after the relevant transaction takes effect, the Reserve Bank would still be satisfied that the affected insurer meets the licensing requirements set out in section 19 of IPSA.

3.2.9 For transfers and amalgamations, the test is broader. The Reserve Bank may approve the transaction (with or without conditions) or withhold approval. It must have regard to:

- a subset of the matters specified in section 19 of IPSA, which sets out matters relevant to licensing;
- the interests of policyholders of the insurers that are parties to the proposed transaction; and
- any other matter the Reserve Bank considers relevant.

[44] Section 26 of IPSA.
[45] Section 27 of IPSA.
[46] Section 44 of IPSA.

The problem

3.2.10 Our experience with the statutory approval processes is that the differences in impact and risk between types of transaction do not always map well, in practice, to the distinctions between types of transactions contained in statute.

3.2.11 As a result, the approval processes do not always give us enough flexibility to adapt our scrutiny of restructuring proportionally to risk. In our experience, the main issues lie with the assessment of change of control transactions. In some cases, where a change of control is unlikely to have significant practical impact on the operations of an insurer, our obligation to review the insurer's compliance with the full range of licensing requirements can be unduly onerous for insurers. Meanwhile, in some cases, a change of control has a very similar effect to a transfer of business, but the legislation sets out a narrower range of considerations.

3.2.12 The most common example of a change of control with limited impact is a change which affects a (foreign) parent of a (New Zealand-based) licensed insurer. The change of control may occur several steps up the corporate group structure, have little impact on the New Zealand insurer or its policyholders, and already be subject to scrutiny by a high quality overseas regulator. Under these circumstances, we think the compliance costs for insurers are disproportionate to the risk involved and the process is not a good use of our supervisory resources.

3.2.13 In other cases, a change of control may significantly alter the position of policyholders (e.g. where a licensed insurer is purchased by a different corporate group). Policyholders retain the same legal relationship with the insurer, but the insurer may now have different access to parental capital support or be managed in the context of a different business strategy. For example, an insurance company might be bought by a different insurance group which would operate it as a subsidiary. In this case, the effect would be much the same as a transfer of all the underlying business. However, because the transaction has been structured as a change of control, the legislation does not expressly allow the Reserve Bank to have regard to policyholder interests in its decision-making.

3.2.14 We note that insurers should be able to change business strategy, and that this may well occur without a transfer. Nonetheless, there may be value in the Reserve Bank having greater ability to consider policyholder interests in this type of context. (We will discuss what exactly 'consideration of policyholder interests by the Reserve Bank' may mean in the next section).

3.2.15 We are interested in exploring an alternative procedure (which we will refer to as 'the New Process') in which different kinds of 'restructuring' (transfers, amalgamations, changes of control and changes of corporate form) are subject to the same approval process. Insurers would need to obtain the written approval of the Reserve Bank before giving effect to a restructure transaction. The Reserve Bank would then have the right to reject the application from the insurer, approve the application, or approve with conditions.

3.2.16 By way of example only, the provisions underpinning the New Process could state that the Reserve Bank *may have regard* to the following matters (permissible considerations):

- any impact the transaction would be expected to have on the ability of the relevant insurer(s) to continue to meet the licensing requirements set out in section 19 of IPSA;
- any impact on policyholder interests ; and

- any other matters the Reserve Bank considers relevant.

3.2.17 The Reserve Bank would have the express power to commission an actuarial report for all forms of restructuring if we considered that doing so was necessary.

3.2.18 The New Process would provide the Reserve Bank with greater discretion than under current legislation. It would allow the Reserve Bank to determine, with greater flexibility, which factors are relevant to and should be considered as part of the approvals process. That would allow us to approve some low-risk change of control transactions without detailed scrutiny. It would also mean that we could undertake greater scrutiny of transactions that posed a significant risk.

3.2.19 The New Process would also mean that changes of control or in corporate form may not take place without prior Reserve Bank approval. The current legislation leaves room for persons to give effect to a change of control or in corporate form, prior to receiving Reserve Bank approval (accepting the risk of a non-approval).

3.2.20 The New Process would be supplemented by updated guidelines on obtaining supervisory approvals. These guidelines would set out the criteria we would use for determining the degree of scrutiny required for a particular transaction and for making decisions.

3.2.21 It would also be possible to introduce additional constraints.

3.2.22 The New Process would require the Reserve Bank to have regard to certain matters. These mandatory considerations could potentially be supplemented with 'red line' tests – in other words, the Reserve Bank *must not* approve a certain type of transaction where certain circumstances apply (e.g. where the transaction would have a material and unreasonable adverse effect on policyholders). See our further discussion on policyholder interests below.

3.2.23 Another possibility would be to include express constraints on the types of conditions that the Reserve Bank may impose. However, we consider that general administrative law provisions on proportionality and reasonableness should already provide adequate safeguards.

3.2.24 Finally, it would also be possible for the legislative provisions to be drafted more permissively, simply stating that the Reserve Bank may reject, approve or approve with conditions and then leaving details of the application process, decision-making criteria and scope of conditions to be placed in regulations (this is the approach taken in the DTB).

Q3.2.1 Do you agree with the proposal to consolidate the approval process for change of control, change of corporate form, transfers and amalgamations into a single test? Why?

Q3.2.2 Do the proposed permissible considerations cover an appropriate range of considerations or are there other matters the Reserve Bank should be considering?

Q3.2.3 Please identify any issues that you believe should be governed by a 'red line' prohibition – i.e. transactions that the Reserve Bank must not approve.

Q3.2.4 Please identify any constraints that you think should be placed on the Reserve Bank's ability to attach conditions to its approval of a restructuring.

Q3.2.5 What do you consider to be the appropriate mechanism for setting out details of the approval process: primary legislation, secondary legislation (i.e. regulations), guidelines, or other?

Consideration of policyholder interests by the Reserve Bank

3.2.25 This section explores requirements upon the Reserve Bank to consider policyholder interests in a range of supervisory processes, including those discussed in the previous section. We consider the consistency of these tests, how easy it is to apply them, and whether they provide the appropriate level of policyholder security.

3.2.26 In addition to the restructuring provisions discussed in the previous section, we also look at approval requirements for the restructuring or termination of statutory funds (sections 109 and 110 of IPSA). Under these sections, the Reserve Bank must not approve an application to restructure or terminate a fund, if it considers that the restructure or termination would result in unfairness to the referable policyholders (viewed as a group). This requirement to consider policyholder interests forms a useful point of comparison for thinking about what arrangements might be appropriate across other supervisory processes. Equally, we think it is desirable either to make the language consistent across these tests or to be clear about the reasons for differences.

3.2.27 Currently, section 44 (which deals with transfers and amalgamations) requires the Reserve Bank to 'have regard to the interests of the policyholders' of the insurers that are parties to the transaction.

Objectives

3.2.28 As explained in the Overview to this section, approval processes need to strike a balance in a way that prevents transactions from reducing the prudential soundness of the sector, while also not unduly impairing the operation of markets for investment capital.

3.2.29 It is clearly important to ensure that, where possible, policyholders are not adversely affected by restructuring. Restructuring should not increase policyholders' risk, for example, through reduced capital backing insurance liabilities, reduced risk diversification, or impaired governance following the restructuring. Restructuring should also avoid improving the position of some policyholders at the expense of others.

3.2.30 However, there also needs to be some flexibility. Arrangements before and after restructuring may not be identical but may nonetheless be broadly equivalent, taken in the round. Equally, in some circumstances, restructuring may be a way of limiting the impact of insurer financial distress. In that case, although the restructuring may involve some apparent detriment to policyholders, it may still be preferable to the *status quo*.

3.2.31 Setting out the details of what should be considered would require some additional policy work and consultation. However, in the interests of having a concrete example to help us think about appropriate scoping, we consider good decision-making might require us to:

- carefully identify all the potential impacts on policyholders, which might include:
    - any impact on the likelihood that claims will be paid, based on a broad risk assessment that goes beyond the solvency standard;
    - any significant impacts on policyholders' rights or likely levels of service;

  - for long-term business, impacts on the reasonable expectations of policyholders;
  - any tax effects;
  - any changes in risk profile;
  - where relevant any impact on rights to participate in profits; and
  - any compensation policyholders are to be provided with to compensate for these risks or additional safeguards to mitigate them.
- compare the effects of the restructuring with the likely consequences of remaining with the *status quo*, particularly where an insurer is in distress and might find itself in further distress in the future; and
- where the insurer is in distress, it might also be necessary to consider whether there are reasonable alternatives to the proposed restructuring that would have better impacts for policyholders.

Options for reform

3.2.32 For the purposes of amending IPSA, we want to consider whether the current approval tests discussed in this section give appropriate weight to the evaluation of the impact of different restructuring processes on policyholder interests, or whether other formulations would be preferable.

3.2.33 There are a range of possibilities with different implications for the relative weight that is put on policyholder interests relative to other factors.

  - At one end of the spectrum, the approvals process could take a permissive approach – e.g. the Reserve Bank *may* have regard to policyholder interests when making an approval decision. That would simply enable us to consider policyholder interests, where we thought it was appropriate to do so.
  - At the other end of the spectrum, the approvals processes could take a mandatory approach – e.g. the Reserve Bank must not approve a transaction where it is likely to result in material detriment to policyholders. In considering such an approach, it would be important to work through any unintended negative impacts on insurer transactions. For example, in situations where a restructuring is taking place because an insurer is in financial distress, it may be in policyholders' interests to compromise (particularly if the alternative was the insurer going into liquidation).

3.2.34 We think that, whatever approach we may settle on (including retaining the status quo), it would also be helpful to update the guidance we provide on approvals processes to provide additional information on how we approach the consideration of policyholder interests. Guidance would provide greater clarity to insurers about what to expect and the information that insurers should provide to the Reserve Bank. It would also assist actuaries who may be required to prepare reports in relation to proposed transactions.

3.2.35 Additionally, we note that the current requirements for the Reserve Bank to consider policyholder interests differ depending on the type of restructuring transaction.

3.2.36 An important question is whether any requirement upon the Reserve Bank to consider policyholder interests should differ depending on the type of insurance business affected.

Arguably, the long-term nature of life insurance policies, and the difficulties of transferring from one provider to another, may mean that policyholder interests should receive greater protection in a statutory fund restructuring or other types of transaction. Alternatively, one might argue that some 'short-term' policies (e.g. health insurance) may also share some of these characteristics (e.g. the difficulty at least some policyholders would face in moving to an alternative provider), or that all types of policyholders should receive equal consideration by the Reserve Bank.

Q 3.2.6 How should the Reserve Bank balance market freedom with policyholder security in assessing restructuring transactions? Do you have any comments on wording that you think would capture this balance appropriately?

Q 3.2.7 Should the requirements for the Reserve Bank to consider policyholder interests be different for statutory funds than for other restructuring transactions for which Reserve Bank approval is required?

Q3.2.8 Would it be helpful for Reserve Bank guidance on approval processes to say more about how we interpret the requirement to consider policyholder interests?

Consulting with the FMA

3.2.37 As noted in section 3.1 above, Insurer conduct will soon be regulated by the FMA (alongside other pre-existing FMA regulation of insurers).

3.2.38 As part of the supervisory approval process, we would be likely to share information with the FMA, particularly as their oversight of insurers increases with the introduction of the COFI licensing regime. The FMA do not have a direct power to scrutinise and approve transactions through a conduct lens. However, licensed firms are required to notify the FMA of transactions. The FMA may consider varying license conditions or other action if a transaction creates a 'material change of circumstances' that affects the licensee's capacity to provide services or means licensing criteria are no longer satisfied. RBNZ and FMA would seek to consider transactions in a coordinated way. We are interested in whether stakeholders think it would improve transparency to include a formal requirement in IPSA for us to consult the FMA as part of any approval process for restructuring transactions.

Q 3.2.9 Should approval processes include a requirement for us to consult with the FMA as part of our approval decision-making?

Scope of 'transfers and amalgamations' provisions

3.2.39 IPSA provides an approval process for transfers and amalgamations.[47] The key provision is section 44. Currently, section 44 does not apply to transfers of insurance business from an overseas unlicensed insurer to a licensed insurer. We believe that section 44 should include these types of transactions.

Q3.2.10 Do you agree that section 44 should be extended to apply to the acquisition of insurance business by a licensed insurer from a non-licensed overseas insurer?

[47] Sections 44 to 53 of IPSA.

Scope of 'change of control' provisions

3.2.40 IPSA provides an approval process for changes of control of an insurer.[48] The scope of transactions covered by this process is narrow relative to international standards for insurance regulation. The threshold for 'control' is specified in section 26(4) of IPSA. Broadly speaking, a person has control of an insurer if they exercise, or control the exercise, of 50% or more of shareholder voting rights in the insurer (whether directly or indirectly, and including where the person acts jointly or in concert with specified persons).

3.2.41 Shareholding and control are of interest to prudential regulators because of shareholders' influence on the governance of the insurer and the personnel and culture of the board (and, in some cases, because of the impact on market entry and competition). Depending on the ownership structure of an entity, it may also be possible for a person to have significant influence over the insurer in situations where they hold less than 50% of the voting rights. In our regulatory experience, there have been transactions where the 50% voting rights threshold was not met, but where we had reason to believe that the change in control had a significant impact on the insurer's governance.

3.2.42 The International Association of Insurance Supervisors' (**IAIS**) Insurance Core Principles discuss change of control in terms that make it clear that 'control' is a matter of degree. For example, ICP6 states that supervisors should be notified when control is obtained or when it is materially increased and notes that control may be direct, indirect, or shared. The IMF FSAP suggested that we consider amending IPSA to refer to a broader conception of 'control'.

3.2.43 One option would be to follow the approach taken for non-bank deposit takers ('**NBDT**') under the NBDT Act (also administered by the Reserve Bank), which sets a threshold for regulatory approval when any person obtains either the ability to appoint 25% or more of the NDBT's governing body or 20% or more of voting rights in the NBDT.[49] This formulation also echoes the Takeovers Code for listed companies, where a 20% shareholding is considered the threshold for requiring a takeover offer. While the Takeovers Code is not directly relevant here (and only applies to large or listed companies), it does suggest that 20% is a significant milestone in terms of altering the structures of control in companies.

3.2.44 We note that the DTB (which will eventually replace the NBDT framework) applies a 50% or more voting rights test for deposit-takers – similar to the current IPSA test. However, we consider that the relationship between policyholders and insurers is different in character to the relationship between banks and depositors in ways that may imply a greater need for caution in the case of insurers. We think this difference underpins the requirements contained in international standards such as the ICPs.

3.2.45 If the Reserve Bank adopts the New Process (i.e. single restructuring test) as suggested in Section 3.2.15 of this paper, giving the Reserve Bank greater discretion to adopt a proportional approach, the proposed lower threshold would trigger notification so the Reserve Bank would be aware of the change. However, the approval requirements for changes of control would be tailored so that they were proportional to the risk involved. In some cases, this would mean that the process might be very straightforward.

[48] Sections 26, 28 and 29 of IPSA.

[49] Section 43 of the Non-bank Deposit Takers Act 2013.

Q3.2.11 What do you think the appropriate threshold should be for a change of control to be notified to the Reserve Bank? Why?

Approval time frame

3.2.46 At present, the Reserve Bank is required to decide whether or not to approve restructuring transactions (under sections 26, 27 and 44 of IPSA respectively) within 20 working days of receiving 'all of the information that is reasonably required'.

3.2.47 In our experience, the expression of this deadline can cause considerable confusion amongst insurers, sometimes raising unrealistic expectations of how quickly the Reserve Bank can process an approval. It appears that some insurers implicitly consider that the Reserve Bank must provide a decision within 20 working days of *receiving an application*. However, it is reasonably common for the Reserve Bank to request more information from the insurer, in order to process an application. We also note that the deadline can be difficult to meet in the more complex cases.

3.2.48 In practice, the amount of time required to approve a transaction is highly variable, depending on: the complexity of the transaction, the degree of risk involved, the quality of information provided by the insurer, and the volume of approvals the Reserve Bank is dealing with at the time. Often, the approval process (from initial application to decision) can be a lengthy process, taking six months or longer for a complex transaction.

3.2.49 One option is to replace the current 20 working day timeframe with a requirement to issue a decision 'within a reasonable time'. This would be supplemented by new or revised guidelines that specify likely time frames for different types of transactions and supervisors would need to communicate actively with applicants about progress. We think that would make it clearer that the process is significant and timeframes may be variable.

3.2.50 Another option is to extend the current 20 working day timeframe. As mentioned, this timeframe commences from the point that the Reserve Bank has received all the information that is reasonably required. In practice, it takes a reasonable length of time to assess an application and determine what (if any) further information is still required. Once the Reserve Bank is in receipt of all information reasonably required, supervisors must analyse what may be complex information, prepare a formal internal report and have the report cleared by senior staff. In complex or ambiguous cases, it may also be necessary to take the decision to internal committees to ensure consistency and fairness of treatment. A legislative time limit should be long enough to accommodate the more difficult cases.

3.2.51 We suggest that 45 working days would be a more appropriate time limit.

Q3.2.12 Please comment on the appropriateness of: (a) replacing the fixed 20 working day timeframe for approvals with a 'within a reasonable time' timeframe, or (b) extending that timeframe to 45 working days. Please provide any other comments or options you consider appropriate.

4 Data and disclosure

4.1 Overview: data gathering, publication and disclosure

4.1.1 In this section, we ask whether the Reserve Bank's powers to gather, disclose and publish data and to require insurers to disclose information are sufficient to support our activities going forwards.

4.1.2 This consultation is concerned with the scope of our statutory powers, rather than how we intend to use those powers. In other words, we are not trying to set future data policy for the Reserve Bank and nothing in this section should be taken as a statement about our data policy going forwards. However, some thought about hypothetical future activities is a useful way to test the adequacy of current powers. In particular, we use the idea of what might be required to produce an 'Insurance Dashboard', along the lines of the Reserve Bank's Bank Dashboard,[50] as a way to explore our existing powers and some potential limitations (doing so also creates a link with our earlier discussion, in the *Policyholder Security* consultation, of insurers' market-facing disclosure of financial strength ratings and summary solvency information).

4.1.3 There are three broad reasons for the Reserve Bank to gather data from insurers as part of its prudential activities. Our main priority is to gather data that helps us to assess insurers' compliance with prudential requirements. The production of good data is also an important part of the governance and due diligence that we expect insurers to be undertaking as part of their own business practices. Finally, we have a role in publishing data, statistics and analysis both to promote market discipline and as part of our broader mandate to promote financial stability.

4.1.4 We consider our existing powers to gather information and data are adequate (enabling us to fulfil the first two objectives). However, we explore whether it would be valuable to provide a stronger statutory basis for disclosing information to the public (the third objective). This might be done by allowing the Reserve Bank more freedom to publish a well-defined segment of the information it collects or it might be done by requiring greater disclosure of insurers.

4.1.5 We propose amending IPSA so that it empowers a disclosure standard, which would enable publication of a wider, but well-defined, range of information. Using standards in this way might also simplify some of the administrative procedures around data gathering.

4.2 A data and disclosure standard

Existing information gathering powers

4.2.1 The main legislative tool we use for collecting insurance data is the power to issue notices under section 121 of IPSA. Section 121 gives us a broad power to issue notices requiring 'any information, data, or forecasts about any matters relating to the business, operation, or management of the insurer'. Section 262 of the RBNZ Act also empowers us to issue notices to request information for the purposes of broader financial system oversight.

[50] The Bank Dashboard can be accessed here.

4.2.2 Section 135 of IPSA places important obligations on the Reserve Bank to keep the insurer prudential information confidential. We may need to gather information for prudential purposes that is commercially sensitive or, in some cases, with implications for privacy. It is therefore important that there are restrictions to ensure that we keep data secure. Section 135 says that insurer prudential information may only be published or disclosed under limited grounds, which include:

- where the information is available to the public under any Act (other than the Official Information Act 1982) or is otherwise publicly available;
- where the insurer has given consent to publication;
- where information is in statistical or summary form;
- where publication or disclosure is for the purpose of (or in connection with) the Reserve Bank's statutory functions, powers or duties; or
- where disclosure is to law enforcement or other agencies (as set out in subpart 3 of Part 6 of the RBNZ Act) or to persons with a 'proper interest' in receiving it.

4.2.3 While section 135 provides some limited ability for the Reserve Bank to publish individual insurer data (see the grounds relating to consent and disclosure in connection with the Reserve Bank's functions, powers or duties), we consider that a data and disclosure standard would provide a clearer and more transparent statement of the type of information that the Reserve Bank may wish to publish and the rationale for doing so.

Making additional information publicly available

4.2.4 While we have no specific plans at the moment to do so, we can imagine that publishing some well-defined comparative data could serve a useful purpose in facilitating market discipline.

4.2.5 When we consulted on current insurer disclosure requirements relating to financial strength ratings and solvency as part of our earlier *Policyholder Security* consultation, industry associations and individual insurers suggested that this type of disclosure might be more effective if it took place on a central, Reserve Bank maintained website. A website could be designed to be consumer-friendly with some financial education elements. It would also allow comparison between insurers. It might also be possible to deliver a wider range of data and information than is currently contained in insurer disclosure requirements, perhaps targeted more at an investor or analyst audience.

4.2.6 We believe that a 'disclosure' standard would provide a transparent and potentially stronger basis for this type of publication.

A data and disclosure standard

4.2.7 We propose that IPSA should empower a 'disclosure' standard, alongside the existing information gathering and confidentiality provisions. The standard would set out requirements for the insurer to publish or disclose information to the public, the Reserve Bank or both. It will be important to ensure that the standard does not duplicate any other legislative requirements (e.g. requirements for financial statements under the Financial Markets Conduct Act 2013).

4.2.8 Standards are subject to tighter procedural requirements than section 121 notices. In particular, there would be a legal requirement to consult and to assess the regulatory impact of any material changes to the standard. Using a standard to determine which information could be published by the Reserve Bank would ensure the maintenance of transparency about how data gathered could be used.

4.2.9 We believe that tighter process requirements mean that standards are an appropriate, convenient and transparent way of regulating steady-state information provision and disclosure. However, it would also be important to retain section 121 powers to assist with short-term or idiosyncratic information requirements.

Q4.2.1 Should IPSA empower a data and disclosure standard that could set out disclosure requirements, including data that should be made available to the public?

5 How to make a submission, including summary of questions

5.1 Have your say

5.1.1 We encourage any interested parties to provide comment throughout the review. At this time, we are particularly seeking commentary on the questions in this consultation document summarised below but are also happy to receive any other general comments on the governance, supervisory processes, or data gathering and disclosure provisions in IPSA.

5.1.2 Use this email: ipsareview@rbnz.govt.nz to provide comments and include 'IPSA Review Governance, Supervisory Processes, and Disclosure' in the subject line. Please clearly indicate which question or section your comments relate to.

5.1.3 Comments or submissions should be received by 5pm on 21 February 2023. Submissions received after this date will not be considered.

5.1.4 It is our practice to publish submissions received unless specifically requested not to. We may also publish an anonymised summary of submissions received.

5.2 Summary of questions

2.0 Governance, key officers and control functions

2.2 Fit and proper

Q 2.2.1 Should IPSA be amended so that a licensed insurer must obtain the Reserve Bank's approval prior to appointing a director or relevant officer? Would this create any difficulties for insurers?

Q 2.2.2 Should insurers have a duty to inform the Reserve Bank if they become aware of information that might reasonably cast doubt on a director or relevant officer's ongoing fit and proper status?

Q 2.2.3 Are there any reasons for, or against, extending fit and proper requirements to senior managers? Is 'managers that report directly to the chief executive officer' a useful way of delineating who should be captured as a 'senior manager'?

2.3 Directors' accountabilities and duties

Q 2.3.1 Are current directors duties under IPSA appropriate? Or is there a case for imposing wider duties, to reflect the potential impact of insurer distress on policyholders and the wider economy?

Q 2.3.2 If there is a case for broader duties, which approach is more appropriate: the narrower approach proposed in the DTA, the extensive approach adopted in the UK/Australia, or some other approach?

Q 2.3.3 Are there any other considerations you would like to draw to our attention when thinking about director's duties?

Q 2.3.4 Other than the duty to life policyholders established under the statutory fund regime, are there any other areas under the IPSA regime where directors or insurers should be obliged to consider policyholder interests or give priority to policyholder interests ahead of those of shareholders or members?

2.4 The Appointed Actuary

Q2.4.1 Would it be helpful for standards to:

(a) set out clearer expectations for the appointed actuary's role;

(b) set out the appointed actuary's place in the insurer's governance structures; and/or

(c) require insurers to explicitly consider resourcing needs for the appointed actuary role?

Q 2.4.2 Would it be valuable to require insurers to have an actuarial advice framework in place under IPSA?

Q2.4.3 To what extent do you think that the Reserve Bank's power to remove an appointed actuary based on fit and proper requirements provides adequate incentives and sanctioning power, in light of the role that appointed actuaries play in the regulatory framework?

Q2.4.4 Should the Reserve Bank impose a statutory duty on the appointed actuary to use due diligence to carry out their assigned role, enforceable with a civil pecuniary penalty?

Q2.4.5 Should appointed actuaries have a duty to identify and present the interests of policyholders? If so, should that be a general duty or only one that applies in specific contexts (such as preparing the financial condition report?)

2.5 The Auditor

Q2.5.1 Should IPSA include a provision requiring auditors to notify the Reserve Bank if they become aware that an insurer is failing to comply with its accounting and financial reporting obligations?

2.6 Banning orders

Q 2.6.1 Should a serious and persistent breach of statutory due diligence duties (if they were introduced) be grounds on which a court might issue an industry-wide banning order?

2.7 A governance standard

Q 2.7.1 Do you agree that it would be appropriate for IPSA to empower a governance standard?

Q 2.7.2 Can you suggest any principles that should guide the drafting of empowering provisions or the design of governance standards?

2.8 Risk management

Q 2.8.1 Do you think it is appropriate for IPSA to empower a risk management standard? Are there any high-level issues relating to standard scope or drafting of the empowering provisions that the Reserve Bank should consider?

Q 2.8.2 Do you think it is appropriate for IPSA to empower a standard requiring an ICAAP/ORSA process? Are there any high-level issues relating to standard scope or drafting of the empowering provisions that the Reserve Bank should consider?

3.0 Supervisory processes

3.1 Licensing

Q 3.1.1 Do you agree that it is appropriate for IPSA to contain a requirement for RBNZ to consult with the FMA, before the RBNZ issues or cancels an insurer licence issued under IPSA?

3.2 Approvals for restructuring

Q3.2.1 Do you agree with the proposal to consolidate the approval process for change of control, change of corporate form, transfers and amalgamations into a single test? Why?

Q3.2.2 Do the proposed permissible considerations cover an appropriate range of considerations or are there other matters the Reserve Bank should be considering?

Q3.2.3 Please identify any issues that you believe should be governed by a 'red line' prohibition – i.e. transactions that the Reserve Bank must not approve.

Q3.2.4 Please identify any constraints that you think should be placed on the Reserve Bank's ability to attach conditions to its approval of a restructuring.

Q3.2.5 What do you consider to be the appropriate mechanism for setting out details of the approval process: primary legislation, secondary legislation (i.e. regulations), guidelines, or other?

Q 3.2.6 How should the Reserve Bank balance market freedom with policyholder security in assessing restructuring transactions? Do you have any comments on wording that you think would capture this balance appropriately?

Q 3.2.7 Should the requirements to consider policyholder interests be different for statutory funds than for other restructuring transactions for which Reserve Bank approval is required?

Q3.2.8 Would it be helpful for Reserve Bank guidance on approval processes to say more about how we interpret the requirement to consider policyholder interests?

Q 3.2.9 Should approval processes include a requirement for us to consult with the FMA as part of our approval decision-making?

Q3.2.10 Do you agree that section 44 should be extended to apply to the acquisition of insurance business by a licensed insurer from a non-licensed overseas insurer?

Q3.2.11 What do you think the appropriate threshold should be for a change of control to be notified to the Reserve Bank? Why?

Q3.2.12 Please comment on the appropriateness of: (a) replacing the fixed 20 working day timeframe for approvals with a 'within a reasonable time' timeframe, or (b) extending that timeframe to 45 working days. Please provide any other comments or options you consider appropriate.

4 Data and disclosure

4.2 A data and disclosure standard

Q4.2.1 Should IPSA empower a data and disclosure standard that could set out disclosure requirements, including data that should be made available to the public?