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IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

I TE KŌTI MATUA O AOTEAROA
TĀMAKI MAKAURAU ROHE

CIV 2021-404-1222
[2022] NZHC 2444

UNDER	The Financial Markets Conduct Act 2013
BETWEEN	FINANCIAL MARKETS AUTHORITY Plaintiff
AND	AIA NEW ZEALAND LIMITED First Defendant
	AIA INTERNATIONAL LIMITED Second Defendant

Hearing:	3 February 2022
Counsel:	N F Flanagan and C M Fleming for the plaintiff S P Pope and W M Irving for the defendants
Judgment:	23 September 2022

JUDGMENT OF ROBINSON J

This judgment was delivered by me on 23 September 2022 at 4:00pm pursuant to Rule 11.5 of the High Court Rules

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Registrar/Deputy Registrar

Solicitors:	Meredith Connell, Auckland Russell McVeagh, Auckland

Introduction

[1] The Financial Markets Authority (FMA) alleges that the defendants (together, AIA) have breached section 22 of the Financial Markets Conduct Act 2013 (FMCA). On 27 October 2021 FMA filed an Amended Statement of Claim (ASoC) seeking declaratory relief and a pecuniary penalty in respect of three causes of action.

[2] On 28 October 2021 AIA filed a notice admitting all the facts and causes of action alleged. AIA accepts the Court should make the declarations and impose a pecuniary penalty.

[3] The FMA and AIA agree that a penalty of $700,000 is in order. They ask the Court to impose a penalty of that amount. However, the parties also correctly acknowledge that the amount of any penalty is ultimately a matter to be determined by the Court. In assessing the proposed penalty, the Court must be satisfied that it is within an appropriate range taking into account the objectives of the FMCA and the particular circumstances of the case.[1]

[4] For the reasons set out below I am satisfied that the penalty proposed by FMA and AIA is appropriate.

Background

[5] AIA admits the FMA's claim in its entirety. They filed a common bundle of documents but no other evidence. There is no agreed statement of facts, but counsel's submissions also reflect the high level of agreement between the parties. As such, the summary of relevant facts set out below is taken largely from the ASoC and counsel's submissions.[2]

[6] AIA is New Zealand's largest life insurance company and part of one of the largest insurance groups in the world. It enters into contracts of insurance (policies)

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1 *Financial Markets Authority v ANZ Bank New Zealand Limited* [2021] NZHC 399 [*FMA v ANZ*] at [32], citing *Commerce Commission v Air New Zealand Limited* [2013] NZHC 1414, (2013) 13 TCLR 618 at [27]. See also *Commerce Commission v Alstom Holdings SA* [2009] NZCCLR 22 (HC) at [18]; and *Commerce Commission v Kuehne + Nagel International AG* [2014] NZHC 705 at [21].

2 Defined terms used in this judgment are taken from the ASoC.

with individual or corporate customers. Policies can include a number of benefits or types of cover, for example, trauma, total disability, life cover or income protection.

[7] Under each benefit the customer is insured for a particular amount which is the customer's "cover". The customer pays premiums for that cover, usually in monthly instalments. Each benefit is renewed annually on the anniversary of the date on which AIA first issued the customer's policy (the Anniversary Date).

[8] Unless either AIA or the customer cancel the benefit it renews annually until the particular termination date specified in the policy (Termination Date); or on any other termination event such as death.

[9] For some income protection policies the Termination Date was the date the customer reached an upper age limit (that is on their 65th or 70th birthday) (Attainment Date). For some others it was the Anniversary Date immediately after the Attainment Date (that is after the customer's 65th or 70th birthday) (Final Anniversary Date).

[10] After the Termination Date a policy benefit is "mature". That means it no longer confers any rights or benefits on the customer, either for new claims or in respect of ongoing payments for claims AIA accepted before the Termination Date. It also means the customer is no longer obliged to pay premiums.

Annual Review

[11] Before each Anniversary Date AIA recalculates the customer's cover and premium for each benefit. AIA then sends an anniversary letter to the customer setting out the cover and premiums for the next year, together with any amendments to the policy terms (Anniversary Letter). In these Anniversary Letters AIA represents to its customers that for the next year they have the cover and owe the premium in the amounts referred to in the Anniversary Letter; and that these have been calculated in accordance with the terms of the customer's Policy.

Automated Policy Administration

[12] AIA uses a computer-based policy administration system. This stores information about customer policies and undertakes some automated actions in respect of them; for example, calculating premiums and cover, and providing a trigger for Anniversary Letters to be sent to customers.

[13] AIA sent some Anniversary Letters that made false and/or misleading representations in connection with customer policies. AIA sent some of the letters before and some after 1 April 2014 when s 22 of the FMCA came into force. The letters sent after 1 April 2014 contravened s 22.

[14] The parties agree that these contraventions arose inadvertently as a result of process and systems errors. They also agree that only a very small proportion of AIA's customers were affected.

Three Causes of Action

Summary

[15] There are three causes of action. In summary:

(a) **First cause of action – Passback Benefits:** Between 23 January 2013 and 20 February 2015, AIA sent Anniversary Letters advising approximately 2800 customers that certain benefits had been automatically added to their policies (Passback Benefits) when in fact they had not.

(b) **Second Cause of Action – Age Termination:** Since at least 2009 AIA sent Anniversary Letters to some customers making false and/or misleading representations concerning the Termination Date of their income protection benefits. As a result of the representations in some of those letters, certain customers continued paying premiums after their benefits had terminated. Other customers stopped receiving ongoing payments to which they remained entitled. These issues arose because AIA's system did not in all instances distinguish correctly

between policies that terminated on the Attainment Date and those that terminated on the Final Anniversary Date.

(c) **Third Cause of Action – Inflation Adjustments:** Between December 2014 and October 2015 AIA made false and/or misleading representations to some customers that their cover and premiums had been adjusted for inflation in accordance with their policy terms. In some instances AIA miscalculated this inflation adjustment. As a result these customers paid higher premiums than their policy terms required. They also received more cover.

[16] I deal with each cause of action in more detail below.

First Cause of Action – Passback Benefits

[17] A Passback Benefit is a change made to the terms of an existing policy which enhances the customer's cover under it. Between 23 January 2013 and 20 February 2015 AIA sent Anniversary Letters to customers holding trauma policies representing that AIA had automatically added certain Passback Benefits to those policies (Passback Letters). The Passback Benefits related to cover for conditions such as critical cancer, Alzheimer's disease, intensive care treatment and heart valve replacement. AIA represented that the Passback Benefits applied retrospectively to claimable events occurring after either 1 February 2012 or 12 November 2012.

[18] In fact, approximately 2,800 customers whose trauma policies predated 1 January 2003 did not have these Passback Benefits added automatically to their policy. But AIA's systems did not correctly distinguish between pre- and post-2003 trauma policies when preparing and sending the Passback Letters. As a result, 2,800 customers with policies predating 1 January 2003 received Passback Letters saying they had received Passback Benefits which they had not.

[19] At least five of those 2,800 customers made claims for the Passback Benefits described in the Passback Letters. AIA wholly or partially declined on the basis that their policies did not include the Passback Benefits. This was contractually correct but contrary to the representations set out in the Passback Letters.

[20] Four of these five customers received at least one Passback Letter after the FMCA came into force on 1 April 2014. AIA would have paid those four customers a combined total of $125,414.55 in Passback Benefits had those benefits applied. Two of these four Customers received at least one Passback Letter before making a claim for Passback Benefits.

[21] Since discovering this issue AIA has provided those customers the cover to which they would have been entitled if the Passback Benefits had applied. AIA has also compensated those customers for the late payment. Moreover, AIA has extended the Passback Benefits to all customers holding the relevant trauma policies. So AIA has effectively honoured the representations made in the Passback Letters.

[22] However, there is no dispute that by issuing the Passback Letters dated on or after 1 April 2014, AIA made false and/or misleading representations that:

(a) customers were entitled to certain Passback Benefits under the relevant policies, in breach of s 22(d) of the FMCA; and

(b) customers had the right to claim cover in relation to those Passback Benefits, in breach of s 22(h) of the FMCA.

[23] The parties agree that the Court should make declarations accordingly and impose a pecuniary penalty.

Second Cause of Action – Age Termination

[24] The second cause of action relates to correspondence AIA sent to customers whose income protection benefits were due to terminate in the following year, either on the customer's Attainment Date, or on the Final Anniversary Date.

Incorrect Penultimate Anniversary Letters

[25] For some customers, the last Anniversary Letter issued by AIA before the Attainment Date (Penultimate Anniversary Letter) wrongly represented that their policies would continue in force until the Final Anniversary Date. In fact, the terms

of those customers' policies provided that they each terminated on the customer's Attainment Date.

[26] By using these Penultimate Anniversary Letters, AIA wrongly represented to customers that after the Attainment Date and until the Final Anniversary Date: the policy benefits would continue to be in force; the Customer had cover under the policy; and the Customer was required to pay the annual premium stated.

[27] Since 1 April 2014, when the FMCA came into force, AIA issued incorrect and misleading Penultimate Anniversary Letters to at least 137 customers. As a result of the misrepresentation in those letters, those 137 customers paid a total of $184,272 in premiums after their policies had terminated and their cover was no longer in force.[3]

[28] AIA has returned these premiums to customers. AIA's review has also identified that any claims made by these customers during the period between the relevant Attainment Date and the Final Anniversary Date have been met.

[29] There is no dispute that by issuing the Penultimate Anniversary Letters dated on or after 1 April 2014, AIA made false and/or misleading representations:

(a) that Customers had agreed to acquire cover under the relevant policies until the Final Anniversary Dates of those policies, in breach of s 22(c) of the FMCA;

(b) that Customers were entitled to certain benefits under the relevant policies until the Final Anniversary Dates of those policies, in breach of s 22(d) of the FMCA;

(c) as to the price of those Policies, in breach of s 22(f) of the FMCA;

[3] At least 111 incorrect Penultimate Anniversary Letters were issued prior to 1 April 2014 as a result of which customers paid premiums of $121,149 in respect of policies that had terminated.

(d) that Customers had the right to Cover under the relevant Policies until the Final Anniversary Dates of those Policies, in breach of s 22(h) of the FMCA; or

(e) that AIA had the right to charge premiums under the relevant Policies until the Final Anniversary Dates of those Policies in breach of s 22(h) of the FMCA.

[30] The parties agree that the Court should make declarations accordingly and impose a pecuniary penalty.

Cover Cessation Letters

[31] Conversely, between 11 December 2015 and 2 December 2019 AIA sent letters to three customers misrepresenting that their ongoing payments would cease on the Attainment Date (Cover Cessation Letters). In fact, pursuant to the terms of those customers' policies, their benefits remained in force until the Final Anniversary Date. As a result, AIA underpaid these three customers a total of $87,173.02.[4]

[32] AIA has remediated these customers and compensated them for the delayed payment. However, AIA accepts that by issuing the Cover Cessation Letters on or after 1 April 2014, AIA made false and/or misleading representations that Customers no longer had the right to claim or receive ongoing payments under the relevant Policies, in breach of s 22(h) of the FMCA.

[33] The parties agree that the Court should make declarations accordingly and impose a pecuniary penalty.

Third Cause of Action – Inflation Adjustments

Inflation Adjustments

[34] For some insurance policies customers elect to have their cover adjusted annually for inflation. For customers who make that election, AIA incorporates the

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4 AIA also issued Cover Cessation Letters on 17 January 2014 and 24 January 2014 as a result of which it underpaid benefits of $55,317.89.

Consumer Price Index (CPI) increase into its annual recalculation of the customer's cover (Inflation Adjustment). The amount of a customer's cover is one of the factors in a formula AIA uses to recalculate a Customer's premium annually. So, if the Customer's cover incorporates an Inflation Adjustment, that adjustment will also be reflected in the recalculated premium.

[35] Relevant policy documents set out that if a Customer elects to have an Inflation Adjustment:

(a) the Customer's cover will increase on each Anniversary Date by an amount equal to the CPI increase for the previous year; and

(b) there will be a corresponding increase in the Customer's annual premium.

[36] Anniversary Letters sent to Customers who have elected an Inflation Adjustment advise customers that their cover has been adjusted in line with the CPI increase for that year. Also, that changes to premiums may be due to an Inflation Adjustment. However, AIA does not otherwise inform Customers of the dollar value of the Inflation Adjustment, or the proportion of any premium increase that is attributable to an Inflation Adjustment.

Incorrect Inflation Adjustments

[37] In December 2014 a change made by AIA caused its policy administration system to apply the Inflation Adjustment incorrectly, rather than in accordance with the terms of the customers' policies (CPI Error).

[38] As a result of the CPI error, between December 2014 and October 2015 certain customers received Anniversary Letters which misrepresented that the amount of cover and premium stated in the Anniversary Letters had been calculated in accordance with the customer's policy and thus set by application of the CPI (Incorrect Inflation Adjustment Notifications). Customers who received Incorrect Inflation Adjustment Notifications had no way of knowing that the CPI Error had occurred and

that their cover and premiums had not been calculated in accordance with the terms of their Policy.

[39] AIA became aware of the CPI Error in February 2015 and corrected the cause of the CPI Error in October 2015. However, in March 2018 AIA discovered that some customers impacted by the CPI Error may not have been remediated by the steps AIA took in October 2015. For those customers, the original 2014 error had compounded.

[40] Between March 2018 and March 2020 AIA reviewed in-force policies and lapsed policies to identify Customers who had not been properly remediated in October 2015. By May 2019, AIA had identified that a total of 520 in-force Policies had been impacted by the CPI Error, 357 of which it had remediated in October 2015. AIA later identified that 92 lapsed Policies had also been impacted by the CPI Error.

[41] AIA identified that a total of 239 customers impacted by the CPI Error had not been remediated by the remedies AIA applied in October 2015. For those customers, their cover and premiums had not been returned to the correct level. Between October 2015 and 1 February 2020 these customers received Anniversary Letters recording amounts of cover and premium that were not calculated in accordance with the terms of the customer's policy because of the CPI Error (Subsequent Incorrect Inflation Adjustment Notifications).

[42] These 239 customers were overcharged premiums approximately $21,606 because of the CPI Error (an average of $90.40 per customer).

[43] AIA has refunded these customers the overcharged premium. However, AIA accepts that by issuing the Incorrect Inflation Adjustment Notifications and the Subsequent Inflation Adjustment Notifications, AIA made false and/or misleading representations:

(a) as to price (being the premiums), in breach of s 22(f) of the FMCA; and/or

(b) that AIA was entitled to charge the premiums specified in the Inflation Adjustment Notifications, in breach of s 22(h) of the FMCA.

[44] The parties agree that the Court should make declarations accordingly and impose a pecuniary penalty.

AIA's knowledge of the issues

[45] AIA first identified:

(a) the Passback Letters issues in around May 2019;

(b) the Termination Date issues in around February 2011; and

(c) the Inflation Adjustment issues in around February 2015.

[46] In June 2018, the FMA and the Reserve Bank of New Zealand (RBNZ) commenced a joint review into the conduct and culture of (amongst others) life insurance providers, including AIA (Conduct and Culture Review). During the Conduct and Culture Review, AIA advised the FMA of the Passback Letters issue, the Termination Dates issue and the Inflation Adjustment issue.

[47] Since around April 2019 AIA has actively engaged with the FMA on the issues, including the remediation of affected customers.

[48] On or around 4 August 2020 AIA advised the FMA that it had completed its investigations into and remediations of the Passback Letters issue and the Inflation Adjustment issue. On or around 14 June 2021, AIA advised the FMA that it had completed its investigations into and remediations of the Termination Date issue.

Legal Principles

Court's approach to recommended penalties

[49] In *FMA v ANZ* Muir J noted the significant public interest in bringing about the prompt and efficient resolution of penalty proceedings.[5] Muir J referred to Rodney Hanson J's judgment in *Commerce Commission v Alstom Holdings SA*:[6]

> Finally, in discussing the general approach to fixing penalty, I acknowledge the submission that the task of the Court in cases where penalty has been agreed between the parties is not to embark on its own enquiry of what would be an appropriate figure but to consider whether the proposed penalty is in the proper range – see the judgment of the full Federal Court in *NW Frozen Foods v ACCC*. As noted by the Court in that case and by Williams J in *Commerce Commission v Koppers*, there is a significant public benefit when corporations acknowledge wrongdoing, thereby avoiding time-consuming and costly investigation and litigation. The Court should play its part in promoting such resolutions by accepting a penalty within the proposed range. A defendant should not be deterred from a negotiated resolution by fears that a settlement will be rejected on insubstantial grounds or because the proposed penalty does not precisely coincide with the penalty the Court might have imposed.

[50] In assessing whether a proposed penalty is within the appropriate range, the Court need not accept each step of the methodology proposed. It is the final figure that matters.[7]

The approach to fixing pecuniary penalties under the FMCA

[51] Section 489 of the FMCA provides that the FMA may apply for pecuniary penalty where a person has contravened a civil liability provision such as s 22.[8] Section 489 relevantly provides:

> **489 When Court may make pecuniary penalty orders**
>
> (1) The FMA may apply for a pecuniary order against a person under this Act.

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5 *FMA v ANZ,* above n 1, at [30].

6 *Commerce Commission v Alstom Holdings*, above n 1, at [18] (citations omitted). Rodney Hanson J's comments were endorsed by Allan J in *Commerce Commission v New Zealand Diagnostic Group Ltd* HC Auckland CIV-2008-404-4321, 19 July 2010 at [45]–[46]; and again in *Commerce Commission v Whirlpool SA* HC Auckland CIV-2011-404-6392, 19 December 2011 at [15].

7 *FMA v ANZ*, above n 1, at [32]; and *Commerce Commission v Air New Zealand Ltd* [2013] NZHC 1414, (2013) 13 TCLR 618 at [27].

8 Financial Markets Conduct Act 2013, s 485.

> (2) If the FMA applies for a pecuniary penalty order against a person under this Act, the Court –
>
> (a) Must determine whether the person has contravened, or been involved in a contravention of, a civil liability provision; and
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> (b) Must make a declaration of contravention if it is satisfied that the person has contravened, or been involved in a contravention of, a civil liability provision; and
>
> (c) May order the person to pay to the Crown a pecuniary penalty that the Court considers appropriate if it is satisfied that the person has contravened, or been involved in a contravention of a civil liability provision.

[52] In *FMA v ANZ* Muir J held that the general approach to setting penalties under the FMCA involves a three-stage test:[9]

> (a) first the Court determine the maximum penalty (in accordance with ss 38(2) and 490 of the FMCA);
>
> (b) secondly the Court must set a starting point having regard to the relevant statutory criteria (which are set out at s 492 of the FMCA); and
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> (c) finally, the Court should adjust that starting point by applying an uplift or a discount on the basis of circumstances personal to the individual defendant.

[53] I consider each stage in turn.

Stage 1: The maximum penalty

[54] Section 490(1) of the FMCA provides that the maximum amount of a pecuniary penalty for a contravention of a civil liability provision such as s 22 by a corporate defendant is the greater of:

> (a) the consideration for the transaction that constituted the contravention (if any); and

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9 *FMA v ANZ*, above n 1, at [37]. Muir J noted that this was also the approach taken when setting penalties under the Securities Markets Act 1988 and the principles applied under the Commerce Act 1986.

(b) if it can be readily ascertained, 3 times the amount of the gain made, or the loss avoided, by the person who contravened the civil liability provision; and

(c) $1,000,000 in the case of a contravention, or involvement in a contravention, by an individual or $5,000,000 in any other case.

[55] However, section 506 provides that "no person is liable to more than 1 pecuniary penalty order for the same conduct". So, if several breaches arise from the same conduct, the maximum penalty will be that which applies to a single breach.

[56] The parties agree that s 490(1)(c) applies in this case, so the maximum penalty for a single contravention of s 22 is $5,000,000. However, the parties disagree as to how s 490(1)(c) and s 506 of the FMCA apply together in this case. Mr Flanagan for the FMA submits there were three separate breaches and as such the maximum penalty should be $15,000,000. Counsel submits that although AIA's breaches were all underpinned by a disconnect between the relevant customers' policy terms and AIA's policy administration systems, nevertheless there were three distinct systems failures with distinct causes and effects. He says that although the breaches overlapped in time this was not necessarily because they were related in any way (beyond being the result of AIA's generally inadequate systems and processes).

[57] On the other hand, Ms Pope for AIA relies on *FMA v ANZ* in which the Court found that although there were two breaches of the FMCA the starting point should be realistically assessed against the maximum penalty for a single breach.[10] The Court held (and the parties agreed) that was appropriate because the two contraventions resulted from similar deficiencies in ANZ's processes and systems and occurred over substantially the same period.

[58] On the material before me I agree with Ms Pope that the Court's reasoning in *FMA v ANZ* applies. The parties agree that AIA's contraventions arose out of system issues that led it to send Anniversary Letters containing incorrect information concerning a customer's cover and/or premiums. The timeframes overlapped.

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[10] At [42].

Beyond that, there is insufficient evidence before me to resolve any dispute there may be as to whether or not those contraventions arose out of "the same conduct" for the purposes of s 506.

[59] In reaching this conclusion, I also note the FMA's submission (albeit in relation to setting the starting point) that the appropriate approach is to assess one penalty in totality, comparing AIA's conduct overall with that in *ANZ* overall. I agree. As such, whether the maximum penalty in the present case is $5,000,000 or $15,000,000 will not ultimately be determinative. The Court's assessment of what constitutes "the same conduct" for the purposes of s 506 should be left for a case in which that is a material issue in dispute between the parties and relevant evidence is available to enable the Court to resolve that dispute.

Stage 2: The starting point

[60] In *FMA v ANZ* the Court adopted a starting point of $400,000, which was 8 per cent of the $5,000,000 maximum.[11]

[61] In the present case the FMA submits that a starting point of $1,000,000 - $1,200,000 million is appropriate. Counsel for AIA submits that a starting point of $800,000 - $1,200,000 is appropriate, taking into account the $400,000 starting point in *FMA v ANZ*.

[62] For the reasons set out below I find that a starting point of $1,000,000 is appropriate. That is 20% of a maximum penalty of $5,000,000. In my view is an appropriate relativity to the $400,000 starting point adopted in *FMA v ANZ*.[12]

[63] When setting the appropriate starting point the Court must have regard to "all relevant matters", including the statutory criteria set out at s 492 of the FMCA.[13] As well as the statutory criteria, in *FMA v ANZ* the Court also took into account both

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11 *FMA v ANZ*, above n 1, at [85].

12 A $1,000,000 starting point would be 6.67% of a $15,000,000 maximum. That would be too low. Conversely, 20% of a $15,000,000 maximum would give a starting point of $3,000,000. That would be too high.

13 Financial Markets Conduct Act 2013, s 492.

deterrence and ANZ's knowledge of the breaches and the circumstances of its self-report.

Section 492(a): The purposes of the FMCA

[64] Section 492(a) requires the Court to take into account the purposes of the FMCA when determining the appropriate penalty. These are set out in ss 3 and 4 of the FMCA. Counsel submits that the following purposes are particularly relevant:

(a) promoting the confident and informed participation of consumers in financial markets;[14]

(b) promoting and facilitating the development of fair, efficient and transparent financial markets;[15]

(c) providing for accurate and understandable information to be provided to persons to assist them to make decisions about financial products or financial services;[16] and

(d) ensuring that appropriate governance arrangements apply allowing for effective monitoring of financial products and services.[17]

[65] FMA submits that AIA's conduct undermined the first three of these purposes but accepts that this was no more (or less) so than will be the case with most breaches of s 22. It accepts that AIA's size and the nature of its products increase the risk of damage to the reputation of New Zealand's insurance market, and therefore the confident and informed participation of consumers in the market. However, FMA accepts that only seven customers had claims declined as a result of the breaches.

[66] AIA accepts that any contravention of s 22 of the FMCA may undermine confidence in the financial markets. However, AIA submits that the issues arising in

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14 Section 3(a).
15 Section 3(b).
16 Section 4(a).
17 Section 4(b).

this case are not likely to undermine public confidence and the facilitation of fair, efficient and transparent financial markets in any substantial way.

[67] I agree that AIA's conduct has undermined these statutory purposes as any breach of s 22 necessarily will here. AIA told some customers that Passback would be automatically added to their policies, but they were not. AIA changed some customers premiums for policies after they had been terminated. A few customers – seven after 1 April 2014 – were declined cover to which they were entitled.

Section 492(b): Nature and extent of the contravention

[68] AIA's breaches (like *ANZ's)* arose inadvertently and as a result of system and process errors. But FMA submits that ANZ's contravention was more limited. ANZ's breaches resulted from two similar system deficiencies and affected 307 customers who were overcharged (on average) $648.60 each.[18] On the other hand, since 1 April 2014 AIA's breaches affected 383 of AIA's customers who were overcharged premiums or underpaid cover since 1 April 2014. The average financial harm per customer was $1,092.60, but seven of these 383 customers were underpaid cover in amounts between $19,104.36 and $46,044. This would have been significant for those customers and is an aggravating factor. On the other hand, the 239 customers who were overcharged premium as a result of the CPI Error paid additional premiums of $90.40 each as a result but they also received additional cover. That is less significant.

[69] I agree with counsel for AIA it is relevant that only a very small percentage of policy holders have been affected. As Muir J held in *FMA v ANZ* this means that the problem may have been less likely to be identified earlier. Also, for the overwhelming majority of AIA's policy holders the systems proved sufficiently robust.[19]

[70] Counsel for AIA points out that *FMA v ANZ* involved inadvertently selling policies that provided no benefit to customers, either because they were already covered or were ineligible for cover. Conversely, AIA's customers still received some benefit under their policy, albeit that they initially received less than their entitlement

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18 *FMA v ANZ*, above n 1, at [54].
19 At [59].

or paid more for it. Overall, I am not convinced that is a relevant distinction. It may apply to the 239 customers who were overcharged approximately $90.00 each but for CPI adjusted cover. It does not apply to the seven customers who were underpaid between $19,104 and $46,044 in cover.

Section 492(c): Nature and extent of any loss, damage or gains

[71] 383 customers were financially impacted by AIA's contraventions in the period after the FMA came into force on 1 April 2014.

[72] The total financial harm arising from each issue was as follows:

(a) **Passback Letters:** Four customers who received Passback Letters after 1 April 2014 initially had claims declined for Benefits the Passback Letters represented they would receive. The four claims ranged between $26,882.05 and $36,052.68 and were for a total of $125,414.55. Those claims have since been met.

(b) **Termination Date Issues:** Since 1 April 2014:

(i) AIA underpaid three customers a total of around $87,173.02 in income protection payments. The underpayments were for $19,104.36 (disability income protection cover), $22,024.66 (disability income cover), and $46,044 (income protection cover); and

(ii) 137 customers overpaid $184,272 in premiums after their policies had terminated (or $1,345 each on average).

(c) **CPI Error Issues:** AIA overcharged around 239 customers a total of $21,606.33 in premiums ($90.40 each on average) because of the CPI error which first arose in December 2014.

[73] The average financial harm per customer in this case ($1,092.60) is larger than in *FMA v ANZ* ($648.60). AIA submits that this reflects the nature of its insurance

products; and also, that for seven customers their loss relates not to overcharged premiums but to significant benefit payments to which they were entitled (or, in the case of Passback Benefits, had been told they were entitled).

[74] AIA also acknowledges that Passback Letters were sent to 2,800 customers, not just the four customers that made claims for Passback Benefits. Although those customers did not suffer direct financial harm, AIA responsibly acknowledges that it is appropriate for the Court to have regard to this group of customers in assessing the extent of customer impact.

[75] The FMA submits that for some customers AIA's conduct will likely have caused emotional harm as well as direct financial harm, particularly those few customers who were declined cover or whose cover ceased prematurely. Those customers were declined disability, income replacement and other health-related cover which is only available in inherently stressful circumstances. The wrongful declinature or premature cessation of cover would exacerbate that stress. And those four customers who were denied cover for Passback Benefits they were told they would receive were making decisions in relation to angioplasty.

[76] I agree with the FMA that these are aggravating factors. For these customers, the harm suffered was worse than that suffered by the customers in *FMA v ANZ*, who were charged premiums for Benefits they did not need or to which they were never entitled.

[77] On the other hand, the damage caused by the CPI adjustment issue was less serious than in *ANZ*. 239 customers paid a total of $21,606.33 in extra premiums. This was outside scope of policy, but those customers also received extra cover. Nevertheless, the increased premiums and increased cover were outside the scope of those customers' contractual arrangements with AIA, and to that extent the customers were misled.

[78] In terms of timeframe, I accept AIA's submission that the relevant time periods in this case are significantly shorter than the period that applied in *FMA v ANZ*.

Section 492(d): Compensation

[79] AIA has fully investigated and successfully remediated all of the problems. The FMA acknowledges that AIA should be given substantial credit for its significant investment and comprehensive approach to remediation and investing significant resources into it. In particular, it should be noted that AIA has paid out on the claimed Passback Benefits even though it did not have any contractual obligation to do so.

[80] The FMA nevertheless takes issue with some of the delay in the remediation process. It points out that in *FMA v ANZ,* ANZ had completed its remediation process within two - three years of discovering the relevant issues. In the present case, AIA did not complete remediation for all of the termination date issues until more than ten years after it discovered them, and six years after the commencement of Part 2 of the FMCA. AIA took more than five years to remediate all customers effected by the CPI adjustment error.

[81] FMA says this delay illustrates the extent of AIA's systems failures. AIA disagrees. AIA says its remediation process was more thorough and complex than ANZ's so took more time.

[82] The evidence before me does not permit a meaningful comparison of the relative complexity of ANZ's and AIA's remediation process. In any event, I agree with the parties that AIA is entitled to a substantial credit for its thorough and complete remediation process which included compensating customers for delays in remediation as well as for the original breach.

Section 492(e): Circumstances in which contravention occurred

[83] As noted, the contraventions arose out of process and system deficiencies. AIA responsibly acknowledges that these system failures should not have occurred and should have been remedied more promptly. AIA has now made significant investment to ensure these issues do not reoccur. FMA accept the improvements AIA has made to its systems and culture to ensure future compliance. These improvements can be taken into account in setting the starting point.

Section 492(h): Relationship of the parties to the transaction

[84] FMA submits that the insurer/customer relationship between the parties is an aggravating factor in this case. There is merit in that submission. AIA is a major insurer. Its contraventions went to the essential scope of cover and amount of premiums. These are essential terms in any insurance contract.

[85] AIA responsibly acknowledges that an insurer's customers are entitled to trust that the insurer will: accurately calculate and communicate above cover and premiums; fix any errors promptly; and stop collecting premiums when policies terminate. AIA also accepts that its customers should be able to rely on the robustness of their insurer's systems.

Other relevant considerations

[86] As in *FMA v ANZ* the FMA identifies two other relevant considerations in addition to those identified expressly in s 492. These are deterrence and AIA's knowledge of the breaches and the circumstances of its self-report.

Deterrence

[87] In *FMA v ANZ* Muir J made clear that in the context of pecuniary penalties deterrence will always be a relevant consideration and perhaps "the overriding objective".[20]

[88] FMA refers to the explanatory note to the Financial Markets Conduct Bill 2011 recording that "the level of pecuniary penalties needs to be set at a significantly high level to deter non-compliance, encourage voluntary compliance, and punish non-compliance".[21]

[89] Deterrence can be both specific (in relation to particular defendants) and general (in relation to other market participants). The relevance of each will depend on the facts of each case.

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20 At [45], citing *Department of Internal Affairs v Ping An Finance (Group) New Zealand Co Ltd*, above n 12.

21 Financial Markets Conduct Bill 2011 (342 – 1) (Explanatory note) at 39-40.

[90] There is no particular need for specific deterrence in this case. AIA's breaches were inadvertent, and its remediation process was thorough. Counsel advises there have also been relevant organisational improvements that will help ensure further compliance.

[91] The parties agree that general deterrence is relevant. Counsel for AIA submits that the penalty does not need to be set at a level that deters other market participants from engaging in *intentional* conduct that breaches the FMCA, because AIA's own conduct was *unintentional*. I accept that submission as far as it goes; but I agree with counsel for the FMA that where breaches arise from deficient processes or systems the penalty should deter other market participants from risking similar deficiencies.

Knowledge of the breaches and circumstances of any self-report

[92] AIA first identified:

(a) the Passback Letters issue in around May 2019;

(b) the Termination Date issues in February 2011; and

(c) the CPI Error in February 2015.

[93] In June 2018 the FMA and the Reserve Bank of New Zealand (RBNZ) commenced a joint review into the conduct and culture of life insurance providers, including AIA (Conduct and Culture Review). It was during this Conduct and Culture Review that AIA advised the FMA of the relevant issue giving rise to this proceeding.

[94] The FMA submits that, with the exception of the Passback Letters issue, a lengthy period passed between AIA learning of the relevant breaches and reporting them to FMA. Moreover, FMA submits it is relevant that AIA only reported these issues in response to direct questions from the FMA. So its self-reporting was not entirely voluntary.

[95] AIA disagrees. It says its response to the regulators Conduct and Culture Review in 2018 was thorough and led it to identify that its earlier attempts to remediate the Termination Date issues and the CPI Error issues had not been entirely successful. This is why AIA reported on those issues to the FMA in its response to the Conduct and Culture Review. Moreover, AIA only became aware of the Passback Benefits issue during the course of the Conduct and Culture Review.

[96] Once again, the relatively limited evidence before the Court makes it difficult to fully assess these competing submissions. However, I accept AIA's submission that its reporting is in contrast to *FMA v ANZ* where ANZ was aware of the relevant issues for over a year before reporting them to the FMA; and did not report them during the Conduct and Culture Review despite two requests by the FMA to disclose such issues.[22]

[97] I also tend to agree with counsel for AIA that regulator expectations in relation to self-reporting have developed significantly since 2011 when the Termination Date issues first arose. The Conduct and Culture Review in 2018 arose out of the Australian Royal Commission into Misconduct in the Banking, Superannuation Financial Services Industry. As such it is important to avoid hindsight when considering the timing of self-reporting in the context of assessing pecuniary penalties.

Assessment of starting point

[98] Although *FMA v ANZ* is the only direct comparator, it is a particularly helpful comparator due to its substantial similarities with the present case. In both cases:

(a) The issues arose out of unintentional system and process errors.

(b) Only a very small proportion of customers suffered financial loss.

(c) The breaches were self-reported (noting the differences in [93] above).

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22 *FMA v ANZ*, above n 1, at [66].

(d) ANZ and AIA both completed extensive remediation programmes and systems upgrade to ensure the errors did not reoccur. For its part AIA paid Passback Benefits to customers to whom it was not contractually obliged to pay.

(e) Both defendants are large corporates for whom deterrent penalties are appropriate to ensure proper investment in compliance, but specific deterrence is not a factor.

[99] In terms of an overall comparison with *FMA v ANZ*, FMA submits that a starting point of $1,000,000 - $1,200,000 is appropriate (being 2.5 - 3 x the $400,000 the starting point imposed in *FMA v ANZ*). AIA submits that a starting point of 2-3 x higher than the starting point in *FMA v ANZ* is appropriate ($800,000 - $1,200,000.)

[100] I agree that this is an appropriate range and I set a starting point of $1,000,000. That is 2.5 x the starting point imposed in *FMA v ANZ*. In doing so I take into account the following points by way of comparison with *FMA v ANZ*:

(a) The breaches in both proceedings were inadvertent and arose as a result of systems and process deficiencies that appear to have been difficult to detect.

(b) As stated above,[23] as the facts were presented in this case, I agree with the parties it is appropriate to assess one penalty in totality comparing AIA's conduct overall with that of *ANZ* overall. However, as AIA acknowledges, the three issues in this case have less in common than the two issues in *FMA v ANZ*.

(c) The extent of the loss or damage to customers in this case was greater than in *FMA v ANZ*. Seven customers in particular were underpaid between (approximately) $19,000 and $46,000.

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[23] At [59].

(d) AIA and ANZ both fully remediated their customers, but it took AIA longer to do so. AIA says that is because its remediation process was more complex. That may be so. This may also reflect the nature of AIA's process and systems deficiencies. In any event, customers were generally out-of-pocket for longer.

(e) Total losses to consumers in this case are a little over double those in ANZ. ANZ overcharged effected customers a total of $199,120.76 as result of its error.[24] AIA's customers were overcharged $413,465.57.

(f) More AIA customers were directly affected: 383 compared to 307 in *ANZ*. 2800 misleading Passback Letters were sent between 23 January 2013 and 20 February 2015, although only five customers made claims that were wholly or partially declined on the basis that their policies did not include the Passback Benefits.[25]

(g) In the present case some customers were denied cover that was due to them, particularly in relation to Termination Date issues.

(h) I accept the FMA's submission that customers who were declined cover to which they were entitled (in the case of the Termination Date issues) or to which they had been told they were entitled (in the case of the Passback Letters) would have suffered this harm at an inherently difficult time in their lives; that is, when they were making claims under trauma, disability or income replacement policy, or receiving ongoing payments in respect of income replacement policies.

Pecuniary penalties under other regimes

[101] The FMA suggest that in assessing the reasonableness of a proposed starting point the Court may be assisted by the starting points adopted in cases involving similar conduct in breach of the Fair Trading Act 1986 (FTA); and breaches of New

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24 *FMA v ANZ*, above n 1, at [54].

25 It is unclear how many of those letters were sent after part 2 of the FMCA came into force on 1 April 2014.

Zealand's anti-money laundering regime established under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML-CFT Act).

[102] In *FMA v ANZ* Muir J referred to three District Court sentencing decisions involving breaches of the FTA by telecommunications companies.[26] Each of these cases dealt with system generated communications misrepresenting to customers who had terminated their accounts part way through the month that they were obliged to make a full monthly payment. In fact, adjustments were necessary to ensure customers only paid until the date of termination.

[103] Although Muir J agreed with the FMA that these cases could be usefully considered, he promptly distinguished them. In those cases the problems were substantially more widespread (between 5,951 and 72,163 customers were affected). As such the opportunities for the defendants immediately to identify the problem were significantly greater than in ANZ's case where so few of its relevant customers had been affected.[27]

[104] There are other important differences. The breaches of the FMCA generally give rise to civil liability while a breach of the FTA is a criminal offence. Moreover, the maximum pecuniary penalty for a corporate defendant in breach of the FMCA ($5,000,000) is considerably higher than the maximum penalty for breach of the FTA ($600,000). Parliament increased the maximum penalty for breaching the FTA from $200,000 to $600,000 in June 2014, shortly after the commencement of the FMCA. I accept the FMA's submission this tends to suggest that Parliament intended for penalties under the FMCA to be higher than fines available under the FTA.

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26 *FMA v ANZ*, above n 1, at [77], citing *Commerce Commission v Spark New Zealand Trading Ltd* [2019] NZDC 7801; *Commerce Commission v Vodafone New Zealand Ltd* [2019] NZDC 15705; and *Commerce Commission v CallPlus Services Ltd* [2020] NZDC 2655.

27 At [78].

[105] FMA also refer me to pecuniary penalties imposed in recent cases involving breaches of the AML – CFT Act.[28] Muir J considered those cases in *FMA v ANZ*.[29] Unsurprisingly, these cases demonstrate that the quantum of a pecuniary penalty as a proportion of the statutory maximum will reflect the seriousness of the breach and the extent to which it is deliberate or inadvertent. Beyond that, I do not consider these cases are particularly helpful. The AML – CFT Act establishes a different regime that is directed at different misconduct. The categorisation of that misconduct into different bands of culpability for the purposes of assessing the starting point with reference to the maximum penalty may assist in other AML – CFT Act cases, but not here.

Stage 3: Adjustments to the starting point

[106] Having identified an appropriate starting point of $1,000,000 I must adjust that having regard to factors specific to AIA.

Aggravating factors

[107] FMA acknowledges there are no aggravating factors specific to AIA. I agree. In particular I note that AIA has not previously been found to have acted in breach of the FMCA.

Mitigating factors

[108] FMA accepts that AIA's admissions were made at the first opportunity and that AIA has cooperated fully throughout the FMA's investigation. FMA also accepts that AIA has made substantial changes to prevent similar breaches recurring. And AIA has fully remediated all affected customers and compensated them for delays.

[109] FMA submits that discrete discounts should be applied for each stage of AIA's cooperation, that is: self-reporting; cooperation during the investigations; and

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[28] See *Department of Internal Affairs v Ping An Finance (Group) New Zealand Co Ltd*, above n 12. See also *Department of Internal Affairs v Jin Yuan Finance Ltd* [2019] NZHC 2510; *Department of Internal Affairs v OTT Trading Group Ltd* [2020] NZHC 1663; *Department of Internal Affairs v Qian Duoduo Ltd* [2018] NZHC 1887; and *Reserve Bank of New Zealand v TSB Bank Ltd* [2021] NZHC 2241.

[29] *FMA v ANZ*, above n 1, at [80]. *FMA v ANZ* predated *Reserve Bank of New Zealand v TSB Bank Ltd*.

admissions. FMA says this is consistent with the purpose of the FMCA to "ensure that 'appropriate governance arrangements apply', 'that allow for effective monitoring' " and reduce governance risk.[30]

[110] Counsel for AIA submits that the pecuniary penalty should recognise the benefit of avoiding the costs and risks of a full hearing. I agree.

[111] AIA and FMA agree that the total discount should be 30% comprising:

(a) 5% for self-reporting;

(b) 5% for cooperation (during the investigation); and

(c) 20% for early admission.

[112] I am prepared to proceed on that basis. In doing so, I note that in *Reserve Bank of New Zealand v TSB Bank Ltd* Mallon J considered that the appropriate discount for the defendant's cooperation was not less than 25%, and higher than the 20% discount to which the parties had agreed.[31]

[113] As noted at the outset, both parties recommend a final penalty of $700,000. For all the reasons set out above I accept that as being within the proper range.

[114] I also note AIA's consent to the various declarations FMA seeks.

Result

[115] I make declarations that AIA:

(a) contravened s 22(d) and/or (h) of the FMCA by issuing the Passback Letters dated on or after 1 April 2014;

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30 *FMA v ANZ*, above n 1, at [69]. There Muir J emphasised this purpose in finding that ANZ's delay in self-reporting was an aggravating feature of its breaches, notwithstanding its subsequent co-operation.

31 *Reserve Bank of New Zealand v TSB Bank Ltd*, above n 30, at [45]-[56], [78], [96] and [104].

(b) contravened s 22(c), (d), (f), and/or (h) of the FMCA by issuing the Penultimate Anniversary Letters;

(c) contravened s 22(h) of the FMCA by issuing the Cover Cessation Letters; and

(d) contravened s 22(f) and/or (h) of the FMCA by issuing the Incorrect Inflation Adjustment Notification.

[116] I impose a penalty of $700,000 on AIA for its contraventions of s 22 of the FMCA as identified.

[117] I make an order under s 493 of the Act that the penalty be applied first to the FMA's costs in bringing this proceeding.

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Robinson J