NEW ZEALAND
BANKERS ASSOCIATION

Submission

to the

Ministry of Business, Innovation and Employment

on the

Draft Financial Markets Conduct Regulations (second tranche)

14 March 2014

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Submission by the New Zealand Bankers' Association to the Ministry of Business, Innovation and Employment on the Draft Financial Markets Conduct Regulations (second tranche)

About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes which contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.

2. The following fourteen registered banks in New Zealand are members of NZBA:
   - ANZ Bank New Zealand Limited
   - ASB Bank Limited
   - Bank of New Zealand
   - Bank of Tokyo-Mitsubishi, UFJ
   - Citibank, N.A.
   - The Co-operative Bank Limited
   - Heartland Bank Limited
   - The Hongkong and Shanghai Banking Corporation Limited
   - JPMorgan Chase Bank, N.A.
   - Kiwibank Limited
   - Rabobank New Zealand Limited
   - SBS Bank
   - TSB Bank Limited
   - Westpac New Zealand Limited.

Background

3. NZBA is grateful for the opportunity to submit on the second tranche of draft Regulations. The process around the development of the Financial Markets Conduct Act 2013 (the Act) has been a good example of policy development that has actively involved the industry. NZBA commends the on-going commitment to meaningful consultation and engagement.

4. The following submission makes some brief comments on the draft Regulations.

5. If you would like to discuss any aspect of the submission further, please contact:

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Practicalities of implementation and timeframes

6. The key concern for the industry is ensuring that we have timely access to all the material that is required to enable banks to properly implement the new requirements. If we do not receive material early enough, implementation may be delayed. This includes any additional requirements from the FMA. As noted in our meeting on 17 March we would appreciate further information (in areas where this has not yet been done such as governance) around what additional guidance can be expected, and will continue to engage on this with FMA.

7. Furthermore, NZBA wants to emphasise that given the extremely tight timeframes for implementation, it is essential that MBIE and FMA meet all stated timeframes for release of requirements and associated guidance. Any further delays would make implementation within the current timeframes extremely difficult, if not impossible. As such, we believe that it is essential that there is ongoing dialogue with the industry to ensure that any issues can be addressed in a timely fashion. If there are delays, the industry needs to be given more time to ensure they are able to comply in time.

8. Finally, we note that there is still uncertainty around the transitioning of existing customers to the new regime, particularly in regards to DIMS customers. From an implementation point of view the approach taken to transitioning, including whether it is in Regulations or through FMA guidance, has significant practical impact. As such we would appreciate further engagement while the approach is being developed. We appreciate your indication at the meeting that you intend to extend consultation on the need transitional measure for DIMS until after the related FMA information has been released.

Treatment of PIEs

9. Schedule 1 Clause 19 of the Financial Market Conduct (Phase 1) Regulations prescribes PIE call fund units, PIE term fund units and bank notice products that are specified units as category 2 product, allowing them to take advantage of Regulation 12. This means that these existing units will be exempt from the regime, with no related licensing requirements and no requirement for a PDS. The Financial Markets Conduct Act also repeals the Unit Trusts Act in its entirety, including the provisions relating to fund governance. We understand that you are currently looking at governance requirements for PIEs post 1 December (when the requirements in the Unit Trust Act will fall away). We assume that further consultation will take place as this work progresses, and note that we would be eager to be involved further.

10. In addition, we note that the relief for PIE call fund units depends upon the definition in the Financial Advisers (Definitions, Voluntary Authorisation, Prescribed Entities, and Exemptions) Regulations 2011. However, a PIE falls within this definition only if certain rights and requirements are set out in the investment statement. As a result, the proposed relief cannot currently be used. We understand that you are currently working on a change that would broaden the scope of the exemption and support this change.

Limit breaks

11. Regulations 25 and 26 are likely to result in duplication of the provision of information on limit breaks for Managed Investment Schemes (MIS). For any material limit break, information is provided under Regulation 25 if not corrected within 5 days. In addition, Regulation 26 requires additional quarterly reporting on limit breaks. It would be helpful if Regulation 26 were amended to reduce any unnecessary duplication between the two sets of reporting. For example, the requirement could be amended so the quarterly report might include the date, name of Scheme and nature of the limit break (so that there is a complete quarterly list that can be matched to previous submissions), but other information might only be required if not already provided or if updated information is available (e.g. on the steps taken or planned to correct the limit break, or to minimise the risk of recurrence).

12. Similarly, Regulations 112 and 113 are likely to result in identical duplication of the provision of information on DIMS limit breaks. NZBA believes that a similar approach to that suggested for MIS above should also be adopted.

13. NZBA also suggests that in order to ensure the requirements are practical, a provision similar to Regulation 29 (2) (which allows information required on a pricing error to be reported at a later date, if not available at the time the report must be made) should be included for limit break reporting. This is particularly important where a limit break occurs within a few days of the quarter end, where information might need to be included in the quarterly report where no reporting would have been required under Regulation 25 or 112 or the quarter end report effectively sets a shorter timetable.

14. Regarding the quarterly reporting, we note that the Regulations do not specify a timeframe for the report to be provided to the FMA. NZBA notes that any timeframe set should allow time for the information to be gathered or for incomplete information to be provided. As such we suggest that the appropriate period would be ten days which aligns with the reporting timetable at the quarter end.

15. Finally NZBA has some concerns around the requirement in Regulation 114 for limit break reporting for DIMS. The approach taken is identical to that applied to MIS. However, since DIMS service differs from the MIS service NZBA suggests a slightly different approach would be more appropriate. The Regulation should be amended to allow for reporting around limit breaks for DIMS to be aggregated (where appropriate). For example, where a number of clients have the same or similar investment authority, one limit break report could be made with an indication of the number of clients affected (rather than one per client). Similarly where there is one root cause for a number of limit breaks for clients with more tailored DIMS, the regime should allow for one report to be made.

Pricing errors

16. Regulation 30 as currently drafted requires, in the case where pricing errors have occurred, that the manager must agree the minimum compensation level for each fund with the supervisor. The result of this is that it is likely to mean that varying minimum compensation levels may be applied across otherwise comparable funds. A more practicable approach would be for a *de minimis* standard to be prescribed for like-for-like funds. This approach would ensure investors across like-for-like funds are treated equitably in the event of a pricing error or failure to comply with pricing methodologies. It would also reduce the amount of supervisor engagement needed.

17. Regarding the payment of compensation, there is a further concern that it is not clear under the current drafting whether compensation can be paid from sources other than from the Scheme itself. At times it may be appropriate for compensation to be paid from other sources (for example directly by the underlying fund). As such the Regulations should be clarified to ensure that this is possible.

Audit

18. NZBA would also like to make two specific comments relating to audit requirements:

- Regulations 39 and 40 use the terms ‘audit’ and ‘review’, but there is no clear definition of these terms. NZBA suggest that it would be useful to align these terms to XRB guidance relating to levels of assurance engagements.
- Schedule 1(2) refers to the ‘auditor’, although it is not clear if the expectation is that a person needs to be an auditor to perform all of the audit/review assignments contemplated. NZBA would appreciate greater clarity on this point. We note that the industry supports a level playing field for firms and audit or review providers, and would not like to see the supply of such services inadvertently restricted.