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**Submission to the Ministry of Economic Development
Financial Markets Conduct Bill Exposure Draft**

Members of the New Zealand Society of Actuaries provide advice to many of New Zealand's stand-alone employer sponsored superannuation schemes. According to information obtained from the Government Actuary's office in February 2011, there were 213 employer sponsored registered superannuation schemes (including the Government Superannuation Fund and alternatives to the GSF). This includes 114 defined benefit schemes and 99 defined contribution schemes. Many of these schemes have been closed to new members as employers move to KiwiSaver as the default workplace savings option for their employees. However, many of these schemes are large and long-standing, and this sector represents a substantial portion of the savings of New Zealanders.

These schemes operate under the legislative framework of the Superannuation Schemes Act 1989, as amended. In the past, it has always been recognized that a stand-alone employer superannuation scheme is different from a financial product offered to the public due to the fact that it is an extension of the employment agreement. This legislation has operated for some time and has proved to be effective in ensuring the prudent management of employer schemes.

We note that many of the defined benefit schemes would be happy to move from being stand-alone schemes to a master trust environment, and therefore subject to the "more standard" new governance provisions. However, the regulator has refused to permit defined benefit master trusts to be established in New Zealand, despite their being common in Australia for many years. This leaves many defined benefit schemes in the difficult position of not being able to take advantage of the benefits and cost savings available to defined contribution schemes, whilst also not being in a financial position to wind up or offer transfers to a master trust. Many do not remain in existence by choice.

We understand that the Financial Markets Conduct Bill is intended to replace the Superannuation Schemes Act as the legislative framework for superannuation schemes. However, we believe that, the Bill as currently drafted does not recognize the practicalities of how employer superannuation schemes operate and we would be keen to spend time assisting officials to clarify the issues and to find workable solutions, where appropriate. Implementing the proposals as drafted will have significant compliance implications for these schemes. This could result in schemes being wound up, to the possible detriment of members and the dissipation of long-term savings.

Given the time constraints for submission, and the length of the draft Bill, we have set down in this submission the more obvious issues we have identified, which in general relate mainly to restricted schemes. There will be more, and we hope to work with you in future to ensure that the new legislation ensures the continued smooth operation of employer superannuation schemes.



The issues that we have identified to date are set out in the following table:

Clause Number	Clause heading	Submission
Part 1	Preliminary provisions	
6	Interpretation	The definition of “restricted scheme” (as applying to a superannuation scheme) is not properly defined, being a circular definition.
6	Interpretation	The definition of “insolvent” in relation to a registered scheme refers to the value of the liabilities of the scheme but what this means is unspecified. For example in a defined benefit scheme, does it mean the actuarial value of future payments or the amount all members are entitled to at the specified date or any entitlement if the scheme is wound up? All options are problematic eg actuarial values can vary depending on the assumptions chosen, a member may not be entitled to any benefit on a particular day (due to the fact withdrawals may be restricted to certain events occurring) and wind up benefits may differ from those the member would be entitled to on an ongoing basis.
Part 4 and schedule 3	Governance of financial products	
111 (2)	Initial and ongoing registration requirements for all managed investment schemes	The draft bill states that the manager of a restricted scheme is the trustee(s) but this conflicts with this clause which says 111 (1) (c) does not apply to a restricted scheme. Clarification of whether any of the supervisor requirements contained in the bill apply to restricted schemes would be helpful.
113 (1)(c)	Additional initial and ongoing registration requirements for superannuation schemes	Membership of a superannuation scheme is not currently restricted to NZ citizens or residents only. Many of the existing schemes are offered by large organisations or employees who wish to provide superannuation benefits to employees in NZ, even though such employees may not stay in NZ permanently. The benefit is necessary to encourage the employee to move to NZ by matching an existing benefit offered overseas. The proposed restriction matches those of KiwiSaver schemes, but superannuation schemes do not have the same crown subsidies as KiwiSaver schemes, so it is difficult to see why the requirement should also apply to superannuation schemes. The effect of the restriction will be that employers will have more difficulty in attracting desirable employees to work in NZ.
113 (1)(b)	Additional initial and ongoing registration requirements for	The current requirement is that a scheme must be established “principally for the purpose of providing retirement benefits”. The proposed change would



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	superannuation schemes	fundamentally change the purpose of the existing schemes, which does not seem necessary to the stated purpose of bringing the governance of such schemes into line with other financial products. It is more important to ensure the legislation is appropriate for existing schemes than try and also cover future new schemes when the possibility of new schemes being registered in the future is low.
113 (1)(d)	Additional initial and ongoing registration requirements for superannuation schemes	It is questionable as to why there needs to be a requirement for a restriction on redemptions and withdrawals. Trust deeds already set out when benefits can be paid and, as noted above, the likelihood of new schemes being registered is low. Superannuation schemes do not have the crown-funded incentives of KiwiSaver schemes so it is questionable why any more restrictions on withdrawals should be imposed. In fact, adding restrictions would be unfair to members, who have joined the scheme on the basis of the existing rules.
114 (1) (b)	Additional ongoing registration requirements for restricted scheme	The definition should include the following options, which are existing scenarios similar to those listed (i.e. not open to the public): <ul style="list-style-type: none"> - industry-wide schemes offered to their employees by a number of companies who operate within the same industry but whose employees are not necessarily members of the same (or any) profession or body. - schemes with members who are employed by a company that has become a participating company when a division of a company is purchased, but the companies are not associated.
114 (1) (d)	Additional ongoing registration requirements for restricted scheme	Very few schemes have an independent trustee at present, but we not aware of any problems that have arisen because of this. Appointing an independent trustee would be an onerous and expensive exercise, especially for smaller schemes.
121	Changes to governing document	This section permits the governing documents to be amended only if the members pass a special resolution or the FMA believes that there will be no adverse effect on members. <ul style="list-style-type: none"> o we are unsure as to how these resolutions would operate in conjunction with the requirements of the existing scheme documentation, as very few superannuation schemes currently have reference to member resolutions in their trust deeds. Section 139



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		<p>does not appear to give any guidance in this regard. Please also see our other comments later, on special resolutions;</p> <ul style="list-style-type: none"> ○ – almost any amendment to a benefit will have an adverse effect on at least one member of a superannuation scheme, even if it is only in respect of the distribution of assets on wind up of the scheme; current legislation recognises this and permits amendments providing they don't adversely affect members' accrued benefits. We believe this is the correct position. While most members cannot leave the scheme if they don't like a change in the rules, they can cease contributing to it and their accumulated benefits are protected.
122	Power to make FMA and court-approved changes to governing documents	We are pleased to see that the Court can approve an amendment that it believes is in the best interests of defined benefit members; it is not clear why this power is restricted just to defined benefit schemes.
135	Requirement to have supervisor or other independent person as custodian	The requirement to appoint a custodian will mean additional costs for restricted schemes, where investments are currently held in the name of the trustees.
142-145	Management of scheme	Schemes provide one or more investment options for members. The returns to members are generally, but not always, provided from the earnings from specific assets that are earmarked for each investment choice. The trustees may change the asset mix in these choices, for example, to reduce risk. Following such a change, it may be some months before the assets come back within the ranges specified, especially if the rebalancing is being achieved by directing cashflows, rather than buying and selling assets. During this period the trustees would appear to have to notify the FMA and, if they take more than 5 days to notify the FMA of any changes to the SIPO, they have committed a tier1 offence. This seems unnecessarily restrictive, especially if such a situation has been envisaged and the possibility disclosed previously to members.
160	Removal of manager of registered scheme	The ability to remove trustees by special resolution would be contrary to the terms of most trust deeds, where only



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		the sponsoring employer has the right to appoint and remove the trustees. We do not think this ability should be changed.
170 (1) (c)	Cancellation of Registration	This clause would give the members and trustees the power to request registration is cancelled with no input from the employer sponsoring the scheme. Including the proposed clause would take the ability to control the existence of the scheme away from the employer which does not seem reasonable when the superannuation scheme would have been setup by the employer purely for the benefit of the employees.
173, 174 & 178	Duty of investment manager, administration manager, and custodian to report serious problems. What person must do if duty to report serious problem applies Duty of supervisor to report serious financial problems to FMA	It is not uncommon for a defined benefit scheme to be technically insolvent (but see comments above about definition of insolvency), depending on the definition of insolvent and the particular set of assumptions adopted by the actuary. Most schemes aim for a 100% or slightly higher level of funding because any overfunding cannot be reclaimed by the employer without the FMA's consent (a complicated and costly procedure). As investment markets fluctuate, so does the funding level, so it is just as likely that, at any point in time, the funding level would be above 100% as below 100% (i.e. insolvent). The real issue is whether future contributions have been set at a level which is expected to eventually correct the position. Under the current legislation, the actuary's report will recommend appropriate steps which the trustees and employer should take; if these steps are not taken they are reported to members and the FMA in the Annual Report. Under Section 178, the supervisor (see also comments under clause 111 (2) about supervisors above) must report the insolvency situation to the FMA as a serious problem.
Part 9 and schedule 4	Miscellaneous provisions	
585	Reregistration process for existing schemes	We would like to assist in determining this process, with a view to keeping it as simple as possible for both regulators and schemes which must comply with new requirements. Over-complex requirements which increase compliance time and costs are highly likely to result in the windup of employer sponsored schemes and the dissipation of existing accumulated savings.

Janet Hayden
 Convenor, Superannuation and Savings Committee
 6 September 2011