

FINANCIAL MARKETS CONDUCT BILL

SUBMISSION ON EXPOSURE DRAFT

OMFinancial Limited

Clause Number	Clause heading	Submission
Part 1	Preliminary provisions	
Clause 7	Relationship between derivatives and the Gambling Act	The bill needs an enhanced equivalent to section 40 of the Securities Markets Act 1988. We need clarification that NZ gambling laws do not apply to derivatives. We would be happy with the proposed option C.
Clause 8	Definitions relating to kinds of financial products	<p>In the definition of "derivative":</p> <p>(b) (i) futures and forwards should be separated into two categories as a futures contract is usually Exchange traded whilst a forward is always "over the counter" (OTC). Whilst the payoffs are similar the counterparty exposure is vastly different. They should have different disclosure requirements. In our opinion forwards require more disclosure due to the risks, cash flows and because they are not exchange traded.</p> <p>(b) (ii) all options are derivatives – if there is to be exclusion then it should only be options on equity securities, debt securities and managed investment products that are issued by the issuer of the underlying products, or a related party of that issuer. For example, if ABC Limited issues shares to raise capital and also issues associated options for further new shares, then these options may be excluded from the definition of derivative. However options issued by an Exchange on ABC should be regulated as derivatives.</p> <p>Include more under (b) (iv) suggest it should be:</p> <p>(b) (iv) "a contract for difference, <u>margin contract or rolling spot contract</u>; or"</p> <p>If the intention is that deliverable FX transactions (i.e. where the actual currency is delivered) is captured in (d), this should be made clearer (e.g., by specifically referring to FX transactions in (b) of the definition).</p>
Clause 10 (2)(b)	Definitions of issued and issuer	<p>The request for submissions makes it clear that it is the intention of the Bill to capture a broker of exchange traded derivatives. If it was limited to a broker that accepts margins and settles the contract (the option at "72b" of the submission request), it would potentially miss a segment of the futures broking industry, such as Introducing Brokers and "give ups".</p> <p>There are agreements that involve execution only services where the contract is "given up". These "give ups" involve (A) executing the contract order for a client with a clearing participant of an exchange and the resulting contract being "Given Up" to (D) who is the company (usually a Clearing Participant and/or Prime Broker) where the client holds their account. In most cases the client is a bank, but we have had these give up relationships with smaller clients.</p> <p>Some of your definitions would include give ups; some would exclude (A) from being an issuer. So if you intend to capture (A) as an issuer in the give up scenario then the "legal relationship" proposed in "72a" of the submission request is the broadest and therefore would in our view capture give ups.</p>

Clause Number	Clause heading	Submission
Part 3 and schedules 1 and 2	Disclosure offers of financial products	
Clause 28 (1)(a), 29	Treatment of offers of options over financial products [etc.]	<p>OMF totally agrees with Clause 28(1)(a), please do not try to make disclosure requirements for an option the same as for an offer of the underlying financial product.</p> <p>Especially exchange traded equity options, these should not be treated as equity; they are a derivative and should only require disclosure as a derivative. The issuer is an Exchange and the contract can be settled by delivery, offset, and sometimes by cash</p>
Clause 38	Right to withdrawal and have money returned	<p>The "money returned" and "relevant money" terms are a bit vague, for derivatives issuers the liability could be unlimited.</p> <p>Potentially a client could take advantage of the oversight of not being provided with a PDS. They could trade for a period of six months risk free, knowing if they eventually end up losing hundreds of thousands they can use their no PDS "get out of jail free" card. Obviously the issuer must ensure every client gets a PDS, but the potential liability for Derivatives issuers does not appear to currently fit the crime.</p> <p>Suggest this be limited to products that involve subscriptions or exclude derivatives issuers. Derivatives issuers would still be liable for penalties etc for breaching the legislation, but not potentially unlimited liability on out of the money derivative contracts entered into by or on behalf of clients.</p>
	Disclosure to investors	<p>There should be relief from disclosure for derivatives issuers who are participants of the NZX. Particularly in relation to exchange traded derivatives, where the Exchange is the Issuer.</p> <p>Most exchanged traded contracts involve some foreign currency conversion. Most NZX equity participants will also facilitate some form of currency conversions, for example, when dealing in ASX shares or share options for the client. It may be an unintentional consequence that equity participants end up being captured as derivative issuers because they do deliverable foreign exchange.</p> <p>If NZX is happy, then it would seem logical to exempt NZX participants from disclosure on the basis that NZX participation rules are robust enough to ensure NZX participants protect client interests. This is desirable as it would help reduce dual regulation.</p>
Part 6	Licensing and other regulation of market services	
Subpart 7	Holding Funds/Property	<p>OMF supports the creation of new regulations and is very keen to help strengthen this area of law.</p> <p>In particular, we note the existing Futures Industry (Client Funds) Regulations 1990. These are obviously old and self-defeating. We understand that this view is widely shared across the industry, including by the regulators we have discussed them with. We strongly recommend these are repealed and replaced as part of any new regulations.</p>

Clause Number	Clause heading	Submission
Part 9 and schedule 4	Miscellaneous provisions	
Section 557	Other Exemptions	<p>Repealing section 14(1) (n) of the Financial Advisers Act 2008 and its suggested replacement appears to force "Futures Dealers" into becoming AFAs in order to deal with retail clients. Is this the intention?</p> <p>OMF suggests the new wording should include an equivalent exemption to section 14(1)(n) for licensed derivative issuers at least until such a time that there is a relevant financial markets paper that potential AFAs can sit. The current papers are fine for financial planning, but are not relevant to dealing in futures or other derivative instruments.</p>