

FINANCIAL MARKETS CONDUCT BILL
SUBMISSION ON EXPOSURE DRAFT
Securities Industry Association

Clause Number	Clause heading	Submission
N/A	N/A	<p>Development of the Act</p> <p>Much of the detail remains to be set out in regulations. This makes it difficult to give definitive feedback on the proposed draft Bill in parts. While we understand Government's wish to proceed to implement change as quickly as possible, we do not believe this should be at the expense of a more fully considered and cohesive securities law regime. Assuming that the Bill is introduced to parliament before the election as the Minister intends, we submit that officials might consider continuing to consult on development of the regulations as the Bill makes its way through the legislative process, as we believe this will help inform submissions on the Bill during the Select Committee process.</p>
Part 1	Preliminary provisions	
Clause 6	Interpretation - Definition of "derivatives issuer"	<p>This definition is broader than the conventional concept of issuer as it includes persons that 'invite applications' for issue or purchase of derivatives. As a result, the exclusion from the disclosure requirements in Part 3 would be unnecessarily narrow and would mean that those who advise on derivatives products (including those persons that act as intermediary or introducer to another person's products) may be required to meet the disclosure requirements of Part 3. The disclosure obligations in Part 3 should not be placed on persons advising on products originated by a third party. This could be achieved by broadening the exclusion for derivatives too so that those acting as intermediary or introducer are caught by this exception. This would mean that such "derivatives issuers" would still be required to be licensed.</p>
Clause 6	Interpretation - Definition of "prescribed intermediary services"	<p>Consistent with the statement above, we would appreciate the ability to be consulted on this definition, once regulations are available that define what services are to be prescribed.</p>
Clauses 8 and 29	Definitions relating to kinds of financial products / Treatment of offers of convertible financial products	<p>The SIA supports the new definition of securities based on economic fundamentals, together with the FMA's ability to deal with new developments going forwards.</p> <p>Clause 8(1), debt security (b)(ii) defines a convertible note as a "debt security." Clause 8(1), derivative (b)(ii) may be interpreted as applying to the option component of a convertible. Clause 29 appears to contemplate clearing this up by specifically noting that an <u>issuer's</u> convertible that converts into that issuer's financial product is to be treated as an offer of the underlying financial product.</p> <p>Another question is how convertible shares (e.g. Convertible Preference Shares or CPS) are to be treated – convertible notes are debt securities but CPS we assume will be equity securities when issued (unless they are redeemable.) We understand cl 29 to mean that an issuer of a convertible note or a CPS would still need to make disclosure regarding the underlying equity in each case as well as disclosure about the convertible structure itself, which we support.</p> <p>This leaves the status of an exchangeable bond or CPS as unclear. (i.e. an offer of a bond or CPS convertible into another issuer's equity.) Clarification of the intended treatment and</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		disclosure in this circumstance, which does not appear to have been contemplated, would be useful.
Part 2	Misleading or deceptive conduct or false or misleading representations	
Clause 16(b)	Misleading or deceptive conduct generally - the supply of a financial service	The Financial Advisers Act 2008 regulates misleading and deceptive conduct by financial advisers. To the extent this relates to financial services provided by financial advisers (sub clause 16(b)), this provision is duplicative. A carve out should be made for conduct already caught by the Financial Advisers Act 2008.
Clause 18	Misleading conduct in relation to financial services	The concept of “quantity of financial services” is ambiguous and should be deleted. Any misleading conduct in this regard would be caught by the terms “nature” and “characteristics”.
Clause 19	False or misleading representations	This provision would make financial advisers liable for false and misleading statements in an offer document (or otherwise made by an issuer) when such statements should be able to be relied upon by a financial adviser. The clause should therefore be limited to knowingly or recklessly making false or misleading representations or a carve out should be added for statements that a person reasonably believed to be true.
Part 3 and schedules 1 and 2	Disclosure offers of financial products	
Clauses 39 - 43	Content and presentation of product disclosure statements	As indicated at the commencement of this submission, it is difficult to have firm views on content without the draft regulations. We would welcome greater clarity and opportunity to submit on the regulations and content for PDS. For example, in the absence of draft regulations, it is not clear from clauses 39 – 43 whether it is intended to restrict the PDS to material / prescribed information and have the register with additional material information, and how much flexibility is intended with respect to marketing information.
Clause 40	Meaning of material information in this Part	In our view, neither definition is necessarily optimal. Definitions such as A are potentially flawed when considering variable priced Equity Capital Market (ECM) offers. That is, the definition tries to remove “price” from the equation because, it is argued, there is no price for an Initial Public Offer (IPO). It therefore replaces it with demand – but in an open priced offering, it may be relevant to know whether the information affects demand at a given price point, not just demand per se. For example, if there was a piece of negative information which, if it had been disclosed, would have a material negative impact on an IPO, an institution might bid for a million shares @ 1.20 (top of a price range) whereas if it had known the information, it would have bid for a million @ 1.00. The volume demand is not impacted – but we would say such a piece of information is material. Option B probably puts the bar a bit higher, resulting in less information being disclosed, and assuming a degree of sophistication of investors which may help minimise unnecessary disclosure. On balance, we consider that Option B ties better to clause 33

Securities Industry Association

Clause Number	Clause heading	Submission
		(Purpose of PDS), as both refer to deciding whether to acquire (rather than materiality on a level of demand, which is potentially more subjective.)
Clause 42	PDS must be worded and presented in clear, concise and effective manner	This threshold mirrors the Australian Corporations Act requirement which has been the subject of much discussion and criticism as to its ambiguity and lack of clarity. In response to this, in April 2011 ASIC issued a consultation paper on what is (or is not) “clear concise and effective” in terms of prospectus disclosure (Consultation Paper 155). ASIC is due to issue a Regulatory Guide in response to that consultation in December 2011. We expect considerable guidance prior to this becoming regulated – considerable cost and effort goes into the preparation of a PDS and as evidenced in Australia “clear, concise and effective” is a matter of opinion and not adequate guidance for the market.
Clause 55	Consents needed for lodgement	Is clause 55(1)(b) a reference to persons providing consent in clause 41? In the apparent absence of a definition for “prescribed persons,” it is not obvious exactly who prescribed persons are, accepting that this may be defined in regulations.
Clause 69	Prohibition of offers in course of unsolicited meetings or communications in certain circumstances	<p>The restriction on offers proposed in this clause is unnecessarily restrictive.</p> <p>For example, under clause 69(c), it is proposed that the client must have transacted in the previous 12 months. If such a restriction is retained, it should be sufficient that the person is a client and there should be no requirement for a transaction to have been completed within a defined period. How would an adviser deal with a new client that has not, as yet, transacted? Would the adviser need to get the client to buy 1 share to meet the threshold? If so, what is the transacting requirement aimed to address? We also comment that, in the absence of a definition of “transaction” as relevant to this clause, it may be impractical to determine whether a transaction has occurred.</p> <p>Are we correct to interpret that any communication with a client is solicited as that client has engaged the adviser to provide such advice and section 69 would not apply to such offers? If not, how will the draft Bill apply to situations where a person becomes a client specifically to receive such offers, resulting in section 69 precluding the very purpose behind becoming a client?</p> <p>The use of the language “or because of” is very broad and could be interpreted to prohibit any marketing of new clients. Potential clients, whose first contact with an adviser was unsolicited, would never be able to be offered a financial product as any such offer to a client was ultimately because of (or resulted from) the person becoming a client after the unsolicited contact. Please consider tightening this language so the true intent only is encompassed.</p> <p>The clause would potentially be more effective if it regulated the unsolicited offer, rather than purporting to regulate an unsolicited ‘meeting’ or ‘communication.’ Conceivably the offeror could circumvent the restriction by arranging a meeting or communication at a time that was mutually agreed by the offeree.</p> <p>Further to the comments above, the carve out at section 69(3)(b) for communications by persons regulated by the Financial Advisers Act 2008 is welcomed. We submit that this carve out should include meetings – it currently only includes</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>telephone or electronic communications.</p> <p>However, we see no rationale for limiting this to ‘quoted’ securities. Additionally, in the case of personalised advice, where an adviser has taken into account the circumstances of the client in making a recommendation or expressing an opinion, what is the need for the restriction in clause 69 to apply at all? We submit that there should be no restriction where the adviser is acting in accordance with the provisions of the Financial Advisers Act and/or the Code of Practice applicable to Authorised Financial Advisers.</p>
Section 71-79	Advertising	<p>The omission of the director’s certificate for issuing advertisements under the Securities Act 1978 has the effect of further restricting pre-prospectus advertising, however, we understand the intent under these legislative proposals is to lessen the restrictions under the existing regime.</p>
Schedule 1, Part 1, Clause 7	Disclosure exclusions for offers of financial products for issue or sale / Offers of financial products through DIMS licensee	<p>We read the draft Bill to mean that the intent is to allow the DIMS provider to be able to invest on the client’s behalf as a wholesale investor (Schedule 1, clause 7) in securities exempt from the disclosure requirement, which we support.</p> <p>On this basis, we would like to see the mandate for the provision of such DIMS requiring an explicit acknowledgment that the investment universe extends to products that are exempt from the disclosure requirement, where a DIMS provider intends to utilise such products in delivering the DIMS service.</p>
Schedule 1, Part 2, clause 28	Sale where financial products issued with a view to original subscriber dealing with products	<p>We note the changes proposed have gone some way to address the issues experienced by the market in NZ with the existing section 6 of the Securities Act, as previously set out by the SIA. However, the effect of the deeming provision in clause 28(3) as to what will constitute the “view” of the issuer will perpetuate the current issue, i.e. an acquirer being required to provide representations and warranties to an issuer that either (i) they will not offer the securities for sale for a 12 month period or (ii) they are not acquiring the securities with a view to on-selling them to retail clients.</p> <p>In 2009, the Australian market experienced this exact issue with the ultimate outcome being that parties were unwilling to participate in institutional placements given the risks associated with the restrictions on the on-sale of those securities. Issuers were unwilling to proceed without the requisite representations and warranties from investors and underwriters and investors and underwriters would not invest on those restricted terms. As currently drafted the Bill will perpetuate this same stalemate in New Zealand. As part of the ASIC Guidance for such relief (Regulatory Guidance 173), ASIC identified the following situations where the anti-avoidance intentions of such a provision were not workable and that without relief the on-sale provisions present practical difficulties:</p> <ul style="list-style-type: none"> (a) in certain circumstances, ordinary placements of equities or other financial products might be unduly impeded; and (b) retail clients who are issued financial products without disclosure under a specific exemption from the disclosure provisions (e.g. for dividend reinvestment plans or as consideration for a takeover offer) might not be able to on-sell those products within 12 months of

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>their issue.</p> <p>In Australia, an issuer will issue a cleansing statement prior to quotation of the placement securities. The cleansing statement has the effect of removing the relevance of the original subscriber's intention from any analysis of the purpose* to which the securities were originally issued. The only relevant intention is then that of the issuer, and provided the issuer was not selling the securities for the purpose of on-sale (for which appropriate representations can be made e.g. through a market announcement made by the issuer) and other conditions of the relevant relief are met, the securities will be freely tradeable. This is important as the issuer (and investors and underwriters) can then manage the risk by documenting the issuer's intent.</p> <p>We believe the Australian precedent for this issue (which is we understand the international standard in the predominance of mature markets) should be adopted in New Zealand.</p> <p><i>*We also note the difference between "purpose" in the Australian law and "view" in the NZ law. We advocate for the Australian threshold of purpose. Given the broadening of what the issuer's view might be and the broad definition of an original subscriber "dealing with the products". Issuer's want liquidity in their securities and so it is hard to see how the issuer's view in allotting the securities, at least in part, was not with a view to those securities being traded. The threshold of purpose is, we believe narrower, and more focused on the anti-avoidance risk that this provision is aimed to guard against.</i></p>
Schedule 1, Part 5, clause 34	Definitions - Investment activity criteria	<p>The exclusion for investors who have held portfolios of at least \$1million should be expanded to include portfolios within the control of such investors (as control is defined by the draft Bill). Many such wholesale investors will hold their portfolios through nominee companies or custodians.</p> <p>We recommend deleting the term "separate" transactions or that guidance is given on what is intended by this term. While we understand the number of trades may be indicative of sophisticated investors, many sophisticated investors are looking to buy quality investments with a view to holding them long term. Such investors would be excluded from this carve out.</p> <p>We would welcome the opportunity to comment on any frameworks or methodology to be prescribed by the FMA, for example, on how gross income will be determined (under 34(4) and 35(2)). Also, it is not clear how the value of derivative contracts will be included in the calculation of a portfolio and/or a transaction and we look forward to seeing this clarified in the regulations.</p>
Schedule 1, Part 5, clause 35(b)	Definitions - Meaning of large	<p>The wealthy test under the Securities Act 1978 refers to a \$2 million net assets test, taken at any time within 12 months preceding the offer. The proposed net asset test under this clause (35(a)) requires the certification to be taken as at the "last day of each of" the last two preceding financial years. Given that the test is significantly higher than the Securities Act 1978 test (\$10 million rather than \$2 million), it seems unduly restrictive to require the test to be taken as at particular dates within the last 2 financial years. While this seems logical for corporate entities that file financial statements this is less relevant for other "large" persons, such as individuals. We</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		propose that the test is changed to be met once during the last 2 financial years (similar to clause 34(1)(a) of Schedule 1).
Schedule 1, Part 5, clause 39	Definitions - Confirmation of certification	The requirement for an AFA to certify that the person has been sufficiently advised should be expanded to include “or understands the consequences of the certification.” Eligible investors of this nature will not usually require an explanation of the consequences of the certification.
Schedule 1, Part 5, clause 40	Definitions - Safe harbour if certificate is given	<p>The requirement for the investor to state the grounds on which they claim to fall within the particular wholesale test is unnecessary. We assume that the purpose of the clause is for issuers, etc., to be able to rely on a proposition by a person that they are wholesale (by reference to the relevant category of wholesale.) The requirement for the person to state “the grounds on which the person claims that the paragraph applies” suggests that an offeror or other relevant person that is relying on the certificate must do some analysis about whether they agree that the grounds are reasonable. Inevitably this will lead to issuers, etc., requiring lengthy and detailed certificates. This will make the wholesale tests unworkable. It should be sufficient that an offeror or other relevant person may not rely on the certificate if they have reasonable grounds to believe that the certificate is untrue under s41. Alternatively, the Bill or regulation should give guidance on what level of detail is required in the certificate.</p> <p>We would like to be consulted on the content of the safe harbour certificate.</p>
Schedule 1, Part 5, clause 43	Eligible person certificates and safe harbour certificates - Offences relating to certificates	The clause could be interpreted as making a person who is relying on an eligible person or safe harbour certificate liable if the certificate is faulty, even if they have no reasonable grounds to believe the certificate to be untrue. This provision should be limited so that persons who incite, counsel or procure a person to give a certificate are not liable “if they reasonably believe” that the certificate is true in all material particulars.
Part 4 and schedule 3	Governance of financial products	
No submission		
Part 5	Dealing in financial products on markets	
Clause 225	Exception for disclosure in connection with preparing PDS or disclosure document	We would like further clarity (perhaps by way of example) of what this is intended to cover. Refer also the MED request for submissions paragraph 104-105, which refers to “the offeror disclosing inside information to the issuer” – is this supposed to be the other way around?
Clauses 262 and 263	Exemption for corporate trustees and nominee companies & Conditions of exemption for corporate trustees and nominee companies	These clauses are materially identical to the equivalent Securities Markets Act sections (sections 31 and 32 of the Securities Markets Act, respectively). We believe this is an opportune time for the legislation to be made consistent with the Australian position as set out in section 609 of the Corporations Act. Specifically, custodians should not have the onus of monitoring and notifying listed issuers and markets with respect to clients’ substantial holdings. In Australia it is widely accepted that a custodian falls within the exceptions in section 609 and therefore does not have a relevant interest. There are

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>no conditions to this exception under the Corporations Act and so the custodian is exempted from any reporting requirements.</p> <p>Requiring the custodian to report is of very limited value, if any. Specifically, the custodian will have limited information about the beneficial holders (for example, if the client is a trust or company). Furthermore, the beneficial holder may hold interests through other means (e.g. other custodians) and so any figures reported by the custodian are unreliable. The monitoring of positions is of significant expense to custodians and, given the limited value of the information reported, the expense is not justified. Both the FMA and a listed issuer have the power to request detail of the beneficial holdings from the custodians. This is considered sufficient investigative powers in Australia. We see no reason for New Zealand to take a different stance from Australia on this matter. Reporting of interests should remain with the persons controlling those interests, not their bare trustees.</p>
Clause 364(1)	Definitions relating to unsolicited offer regulations and related provisions	<p>Working within the Bill's wider framework, and with reference to the notice and pause provisions of the NZX Listing Rules, does this clause adequately provide for an off-market takeover offer for a non-Code entity? (e.g. a listed property trust)</p> <p>We would like the opportunity to submit on the regulations relating to unsolicited offers to purchase.</p> <p>This clause would restrict financial advisers making an offer to purchase on behalf of their clients. We would expect that the legislation (or at least the regulations) would include an exception for financial advisers that are authorised to provide such financial advice. There is a similar exception in Part 1, clause 69 of the Bill (relating to unsolicited offers to sell.)</p>
Part 6	Licensing and other regulation of market services	<p>Overall comment on DIMS:</p> <p>We express support in principle for the regulation of discretionary investment management services (DIMS) on the basis proposed, subject to the following comments.</p>
Clause 408	Disclosure statement	<p>We would like an opportunity to understand and submit on the regulations in regard to the content of the disclosure statement for DIMS providers.</p>
Clause 413	Changes to client agreement	<p>The requirement that each and every change to a client agreement requires the written consent of the retail client party to the agreement is unnecessarily and inappropriately restrictive. For example, it is easy to envisage a circumstance where legislation or regulation (other than this Act) may require or impose a condition requiring a change to a client agreement where it would be inappropriate to require individual retail client written consent. To include such a requirement potentially places the client in a position of power to block a change required by law, placing the licensee in an impossible position. In practice this would result in the services being provided on varying terms and conditions depending on which of the changes any one or more clients have actually agreed to. This would make administering and managing the various contractual agreements excessively difficult. If clients do not like a change to their terms and conditions they can always terminate the relationship.</p> <p>Further, correction of errors or other changes to client agreements that are in favour of the retail client should be able to be effected without requiring written consent from a retail</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>client. We also think that there are a range of other changes, such as the level of fees, that should be able to be amended by notice rather than requiring the written agreement of the client, recognising that the client always has the opportunity to terminate the agreement.</p> <p>This clause should be rewritten to provide for change to client agreements in appropriate circumstances but preferably deleted.</p>
<p>Clauses 422 - 426</p>	<p>Related party transactions & Custodial service performed as part of discretionary investment management service</p>	<p>Amongst other things, Part 6 provides for the FMA to license Discretionary Investment Management Services (DIMS). NZX Market Participant entities that provide DIMS will be required to be licensed, and further in turn it would appear that those NZX advisers that are AFAs may be able to choose whether to obtain a DIMS license or to continue to provide discretionary investment managed services under the FAA.</p> <p>As background, we advise that, typically, client assets managed under a discretionary mandate within an NZX Firm are administered in custody by a nominee company in the same group as the NZX regulated entity. NZX Participant Rule 18.15.1 (b) requires that a separate Nominee Company (as defined in the Rules) be established for the purposes of providing Custody Accounts. NZX Market Participant client agreements contain relevant clauses on the basis upon which the custody service is provided, both reflecting NZX rules and commercial norms for such service. Further, investor property will include cash. Again, the NZX Participant Rules specify how that must be handled and accounted for.</p> <p>Section 426 (2) proposes that the custodian used to hold and safeguard investor property (referred to at (a) as “scheme property” but it won’t in all cases be scheme property in respect of individually managed accounts, therefore use of the term appears to be incorrect, i.e. perhaps it should be “scheme or investor property”) must not be the same person as, or be associated with, the DIMS licensee (unless the license permits otherwise).</p> <p>At first glance, the proposal appears to make sense (i.e. reduce misappropriation risk) but does not appear to give due consideration to the appropriate use of bare nominees as custodian, the practical consequences of having an independent custodian (unless the license otherwise permits) and inefficiency.</p> <p>Further, Section 426 (3) states that the DIMS licensee is jointly and severally liable with any custodian for the holding of investor property in accordance with this subpart. Jointly and severally liable to who? Does the liability extend to any failure on the part of the custodian or indeed any sub-custodian they appoint? If so, there will be far reaching implications in terms of custody agreements, the norms about liability in terms of appointment of sub-custodians, etc. Why would an AFA want to take such liability on?</p> <p>It is our considered view that the proposed use of an independent custodian provides no greater asset protection safeguard to the investor than a properly administered Nominee Company as custodian. The fact that the custodian may be associated with the DIMS licensee and/or AFA should therefore have no bearing.</p> <p>The holding and administration of investor property (cash and</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>securities) is in a fiduciary capacity. In the context of NZX Participant Rules, the main purpose of the Rules is to ensure that through the Client Funds obligations and Nominee Company, the holder accounts for, and safeguards, investor property (client assets) at all times. The Rules dictate a high standard of custodianship and associated record keeping, including reporting to the clients in respect of their property in custody. The financial records in respect of client funds and Nominee Company and the internal controls / safeguards in place are independently audited.</p> <p>We submit that there should be a carve-out from the custodian provisions of NZX Participants as DIMS licensees that administer client property in the form of client funds under the NZX Participant Rules and/or have associated companies that are bare nominees used to safeguard and administer investor property in accordance with the Rules. This is seen as preferable to having to apply for the DIMS license to permit it.</p> <p>Further, we submit that AFAs as employees of NZX Firms would also require a carve out from the custodian provisions, i.e. their employer is a DIMS licensee, the AFA is manager providing a DIMS as an employee representative and manages pursuant to the mandate granted by the client to the AFA's employer (NZX Firm), and the NZX Firm holds / administers client assets pursuant to the NZX Participant Rules.</p> <p>In practice, no NZX Advisor as an AFA will have anything to do with the daily administration and safekeeping of investor property in a Nominee Company. There is legal and functional separation of the custody and manager already.</p> <p>Section 422 (Related party transactions) defines a related party transaction. Section 426 generally prohibits such transactions and Section 424 has certain carve-outs. If NZX Market Participants and associated custodians were permitted under the suggestion above or otherwise by license conditions, then 422 (a) may need to be covered off by an extension of the carve-outs to recognise the fact that it is usual broker practice to collect custody fees out of investor property received by the NZX Firm, i.e. cash on account.</p> <p>Inefficiency is created by the proposal in that NZX Firms and their employees as AFAs are free to provide advisory services and to continue to hold client assets for non-discretionary clients with no apparent impediments. It would make no sense to have two different custodian regimes and create administrative difference.</p> <p>If the proposal stands unchanged, and a license does not permit the holding of client assets by the NZX Firm as the DIMS licensee entity or an associated person, for the record, it will create serious challenges for NZX Firms having to make significant amendments to existing arrangements, including a rewrite of client agreements, getting new ones into place and restructuring client asset administration (including use of sub-custodians) across all NZX Firms. We do not consider the resulting effort that would be required is justified. The proposal fails to recognize the existing regulatory controls to which NZX Firms are subject to under the NZX Participant Rules.</p> <p>For identical reasons, we submit that a similar restriction should not be carried over to any amendments to the Financial Advisers Act 2008 (FAA).</p>

Securities Industry Association

Clause Number	Clause heading	Submission
Part 7	Enforcement and liability	
Clause 431	Meaning of contravene	<p>Extension of liability for defective disclosure.</p> <p>We are pleased to see that the earlier feedback provided by the industry regarding criminal sanctions has been considered and, what we believe, a workable compromise reserving criminal sanction for “knowing” or “reckless” behaviour is reflected in the draft Bill.</p> <p>However, the extension of liability to the following people requires further consideration:</p> <ul style="list-style-type: none"> * any person that "in any way, directly or indirectly, knowingly concerned in, or a party to, the contravention by any other person of the legislation." Without sufficient boundaries, this is simply too broad. We are uncertain as to what activities and which persons the legislation is attempting to target under this provision. As drafted, the printer of a PDS could be liable for a misstatement or omission in a PDS as they indirectly were a party to a contravention of the legislation by the Issuer. This is all the more perplexing given that it is unlikely they could avail themselves of a due diligence defence. * Counselling any other person to contravene - who will be considered counselling - just lawyers or does this extend to other professional services providers * Underwriters (see detail below) * Persons who have consented to provide information and be named in a disclosure. Will this dis-incentivise people consenting to their statements being included and, if so, what will be the consequence for disclosure? <p>Can the scope issue be addressed by expressly including "knowingly" as a threshold for all subsections of section 431?</p> <p>As a specific comment, we note that there should be a demonstrable nexus between the extension of liability to a particular person and the acceptance of that responsibility by that person. We question whether the current drafting incorporates such a precise nexus.</p> <p>We believe these four facets (and potentially others) of the liability regime require more consideration and time to identify the consequences and practical effects of any such policy change and ultimately whether they will drive rather than hinder the objectives of the legislation.</p> <p>Finally, we note the following comment, which we agree with, sourced from Chapman Tripp:</p> <p><i>“There is a real risk that, at least for managed investment products and derivatives, the less onerous (but still appropriate) Australian liability regime and disclosure standards could encourage issuers to prepare disclosure documents under Australian law and offer into New Zealand under the mutual recognition of securities regime - which would undermine the draft Bill objective to develop New Zealand financial markets.”</i></p>
Clause 432	Directors also contravene	<p>Directors would generally rely on experts (lawyers, accountants etc.) to ensure that offers are not illegal or documents prepared are not misleading. The current drafting would require each director to accept liability for each and every offer and exposure to civil remedy provisions, which are also borne by the issuer.</p> <p>Will section 432(1)(a) as drafted mean that a director who votes</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>in favour of a resolution, the implementation of which involves a contravention of the Act (even where the director believed that approving the resolution was in compliance with the Act) is deemed to contravene the Act? Section 432(3) only requires the director to specifically have the state of mind for those offences requiring such a state of mind. As such, a director may find that without any intent or knowledge of a contravention, he/she is found personally liable and guilty of an offence under the Act. From a justice perspective this is alarming as a person may be found guilty of an offence (and liable for financial payments) under the Act without the requirement to establish knowledge or intent.</p> <p>Will the legislative defences in section sections 464 – 466 equally apply? How will this work for the directors of the corporates? Especially directors of corporates that liability is extended to under section 462? How will the legislative defences apply to those directors? It is essential this is made clear as directors need to understand their personal risk in determining whether to accept a directorship.</p>
Clause 462	Terms of compensatory orders	<p>Again, we are surprised by the additional amendments being made to the liability regime, not previously identified in prior consultation, affecting underwriting. This is a clear departure from the existing regime where underwriters were not liable for a prospectus as they are potential investors (who currently have protection like other investors by the disclosures made by the issuer.) Not only does the draft Bill propose liability for an underwriter (which is not defined), it does so even where the underwriter does not commit the contravention.</p> <p>We believe that the existing regime, whereby those that sign the prospectus accept responsibility for that document, is entirely appropriate as it is the directors and the management of the issuer who are best-placed to make judgements on the content of the PDS. They are the parties “inside the tent” who will have the necessary background knowledge and understanding of the issuer required to verify and confirm the statements in the PDS.</p> <p>Underwriters are more equivalent to the likes of legal advisors, trustees, accounting advisors, and eventually end investors. These parties are effectively “on the outside looking in” on the issuer, and all have to rely on the board’s and management’s views and opinions on the validity and accuracy of what does and what does not get included in the PDS.</p> <p>Underwriters (along with investors and trustees) will generally conduct their own investigations as to the issuer, but in the end are dependent on the board’s and management’s views as to the position and performance of the issuer.</p> <p>For the reasons above, we are unsure as to the rationale why underwriters should be elevated in the liability regime to the equivalent level of the issuer, as underwriters generally have significantly less insight into the issuer than the issuer itself. Accordingly, we reiterate that we believe strongly that the current regime, whereby those that sign the prospectus accept responsibility for that document, should be maintained and that the potential effect of the proposed regime is completely negative.</p> <p>In addition to the above discussion regarding access to information, there is a natural rationale for issuers to be the responsible party for the PDS, as they are the party who</p>

Securities Industry Association

Clause Number	Clause heading	Submission
		<p>receives the proceeds of the issue. In this respect, underwriters are similar to investors, as they stand to lose a significant amount of value from an unsuccessful issue, through fallout from the potential loss of on-going business from clients who go elsewhere. In this sense, the proposed bill effectively potentially punishes the Underwriters twice for an unsuccessful deal, once for loss of value in an on-going sense, and once for potential compensatory orders, all whilst not having been the beneficiary of the proceeds of the offer in the first place.</p> <p>Under clause 462(5), the Court may make a compensatory order against any party listed in section 462(4) (b) or (c) even if that person did not commit the contravention. Again, from a justice perspective this is alarming as a person may be made to pay compensation without a requirement to show fault. It is unclear whether the Court is able to make a compensatory order against a party where one of the legislative defences is established by that party— e.g. due diligence defence, reasonable reliance or withdrawal of consent at sections 464 - 466)). It is essential this is made clear as directors need to understand their personal risk and organisations need to manage and price the risk.</p> <p>Added to this is the personal liability of the directors of an underwriter and the deeming provisions of section 432. How is a director of an underwriter able to manage that personal risk?</p> <p>We assume that the addition of underwriter's liability, and its form, have been taken from the Australian regime. However, we question whether its application in NZ will meet the objectives of promoting our capital markets, given the additional costs such a regime will bear (given additional due diligence/lawyers, etc) It is our view that the additional costs will be a barrier to capital raising in New Zealand.</p> <p>We note that the Australian market is significantly larger and deeper than New Zealand's, and accordingly such a regime is more workable and would have a lessor effect in that market.</p> <p>As above, we strongly believe that the addition of the underwriter's liability will inhibit the already fragile capital markets in New Zealand, and we are unsure as to the rationale or potential benefits for such an addition (aside from providing investors with another potential target.)</p> <p>It is unclear what policy considerations have led to underwriters but not sub-underwriters being liable. How would an underwriting consortium be affected? What is the definition of "underwriting" (i.e. the types of underwriting that will be caught as liable)?</p>
Clause 465	Due diligence defence	<p>The due diligence defence should apply in respect of any disclosure obligations and/or sanctions for a contravention under the legislation, not simply those imposed under section 462. Why has the due diligence defence been omitted for defective disclosure in advertisements or where a civil remedy is sanctioned under sections 467 and 468? We can see no reason that the application of the defence should be different depending on the type of disclosure or sanction applying. We have not seen, or are not aware of, any policy basis upon which such a distinction is made.</p>

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Clause Number	Clause heading	Submission
Part 8	Regulations and exemptions	
No submission		
Part 9 and schedule 4	Miscellaneous provisions	
No submission		