

6 September 2011

Investment Law Team
Ministry of Economic Development
PO Box 1473
WELLINGTON

WORKPLACE SAVINGS NZ Submission on the Financial Markets Conduct Bill Exposure Draft

We wish to submit the attached in response to the Financial Markets Conduct Bill Exposure Draft (the Exposure Draft).

Workplace Savings NZ is a national, not-for-profit, apolitical membership organisation. Our current membership comprises around 100 major workplace superannuation and KiwiSaver schemes and another 50 organisations and individuals representing the various product and service providers for workplace savings arrangements.

From the perspective of funds under management, the membership of Workplace Savings NZ covers around 90% of retirement savings held through workplace retirement saving arrangements (i.e. Corporate and Master Trust superannuation schemes & KiwiSaver schemes).

Workplace Savings NZ's objective is to be the Voice of Workplace Savings; advancing the sustainable, effective, and efficient delivery of workplace savings outcomes for all involved – including the core workplace superannuation scheme members who remain at the heart of the organisation. We do this through:

- Advocacy – proposing and commenting on legislative and public policy initiatives beneficial to workplace savings and participation in the workplace savings industry, making submissions, engaging with policy-makers and officials and issuing media commentary to advance those causes.
- Education – promoting trustee, employer and member financial and regulatory education through dedicated training programmes, newsletters and special interest seminars.
- Networking – providing trustees, employers and service providers involved in workplace superannuation with a regular forum for sharing ideas and information on industry matters.
- Promotion – publicising the benefits of workplace savings, and helping to improve public confidence and participation in workplace savings.

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I would be pleased to discuss our comments or answer any questions you may have in relation to the submission.

Yours sincerely



Bruce Kerr
Executive Director

Workplace Savings NZ

Submission to the

**Investment Law Team
Ministry of Economic Development**

on the

**Financial Markets Conduct Bill
Exposure Draft**

September 2011

The Workplace Savings NZ Submission

Introduction

1. Workplace Savings NZ welcomes the opportunity to make a submission on the Financial Markets Conduct Bill Exposure Draft.
2. Workplace Savings NZ has restricted its comments to those parts of the Exposure Draft having an impact on Managed Investment Products as offered by our members. We have chosen to not comment on debt securities, equity securities and derivatives.

Submission

Clause Number	Clause heading	Submission
Part 1	Preliminary provisions	
Clause 10	Definition of Issued and Issuer	<ul style="list-style-type: none"> Workplace Savings NZ supports the clarity proposed at clause 10(2)(a) and (c), confirming that an interest in a superannuation scheme or KiwiSaver scheme is only issued when a person first becomes a member of the scheme, and that further contributions by either a member or an employer do not give rise to the issue of a financial product. Whilst this is the way the law has always been interpreted by our members, it is pleasing to see this clarity expressed in the legislation. We would support this position being extended to other managed investment products to which regular contributions are customarily made, such as unit trust investments. For flexibility, provision could be made for extending the 'relief' for further contributions to other prescribed schemes of which a person is already a member. We endorse the submission of the Investment Savings & Insurance Association (ISI) in this regard.
Part 2	Misleading or deceptive conduct or false or misleading representations	
		Workplace Savings NZ does not wish to make submissions on Part 2 of the Exposure Draft
Part 3 and schedules 1 and 2	Disclosure offers of financial products	Workplace Savings NZ makes the following submissions in relation to Part 3, and Schedule 1 & 2, of the Exposure Draft
Clause 40	Meaning of material information in this Part	<ul style="list-style-type: none"> Workplace Savings NZ welcomes the attempt to reduce the uncertainty around the concept of what should be regarded as "material information" in the context of regulated offers. That uncertainty has contributed significantly to the length of disclosure

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		<p>documents and the need for scheme issuers to seek legal and other professional advice, adding to the compliance cost and complexity of scheme disclosure.</p> <ul style="list-style-type: none"> ▪ In the context of a Workplace Superannuation scheme or KiwiSaver scheme, whether or not information is “material” involves considering whether or not the information might reasonably be expected to influence a relevant person in deciding whether or not: <ul style="list-style-type: none"> ○ to join a scheme ○ to withdraw from a scheme, which could be by way of transferring to an alternative scheme or, if eligible to do so, cashing out their savings ○ to continue or commence regular contributions to the scheme ○ to cease contributing or take a contributions holiday ○ to make a lump sum contribution to their existing savings. ▪ Importantly, with the Bill expressly providing for membership of a superannuation scheme or KiwiSaver scheme to constitute a single financial product, materiality cannot just be considered by reference to demand for a scheme or deciding whether to “acquire” a membership of the scheme. A test based on the material effect on demand for a financial product is not directly applicable to the context of a workplace savings scheme and it is unclear how it would apply in an automatic enrolment environment. Of the two options presented, we prefer Option B. ▪ Regardless, many KiwiSaver and Workplace Superannuation members are not people who “commonly invest in financial products”: for many, the only financial product in which they invest will be their KiwiSaver or workplace superannuation scheme. In our context, a test relating to a “prudent but non-expert investor”, is a preferred formula, and it aligns with the clause 42 requirement for a PDS to be worded and presented in clear, concise and effective manner. ▪ Accordingly, our preferred formulation for clause 40(a) would be: <p><i>'A reasonable person would expect would, or would be likely to, influence a prudent but non-expert investor in deciding whether to acquire or make further investments in the financial products on offer'.</i></p> ▪ In addition, relief should be provided where the influence is negligible or not significant to avoid the

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		<p>risk of over-disclosure from an abundance of caution.</p>
Clause 43	PDS must comply with prescribed requirements relating to form and presentation	<ul style="list-style-type: none"> ▪ Workplace Savings NZ looks forward to participating in further consultation on the proposed regulations relating to the form and presentation of a PDS. We would hope that the special nature of workplace savings schemes, and in particular defined benefit schemes where disclosure of scheme features does not fit comfortably with a standard template, will be recognised.
Clause 71	Advertising or publicity for regulated offers	<ul style="list-style-type: none"> ▪ Commonly, employers will distribute descriptive information relating to superannuation schemes made available through the workplace. Often, this will be no more than just a comment about the scheme returns, or an anecdote about the scheme membership. ▪ One uncertainty that arises in these circumstances is whether the provision of information of a descriptive nature should be regarded as something that is “reasonably likely to induce persons to apply for the financial products”, and whether the mere fact that a trustee of a superannuation scheme has agreed to an employer’s participation in that scheme, is sufficient to constitute authority for such a statement by or on behalf of the trustee. ▪ Workplace Savings NZ would like to see relief for subsection (1) not applying to prescribed information, where the information that might be prescribed in this context would include descriptive information generated by employer participants in Workplace Savings schemes, similar to the relief that currently applies in relation to the provision of the actual descriptions of KiwiSaver schemes not constituting a financial adviser service, pursuant to Section 206 of the KiwiSaver Act 2006.
Part 4 and schedule 3	Governance of financial products	
Clause 111 (1) (f)	Initial and ongoing registration requirements for all managed investment schemes	<ul style="list-style-type: none"> ▪ Clause 111(2) does not exempt a restricted scheme from the requirement for scheme property to be held by another person who needs external custodianship requirements. ▪ A restricted scheme will not have a supervisor and will therefore be subject to external custodianship requirements. This is not appropriate. In many instances, a restricted scheme will have a special purpose trustee company operating as its trustee, in whose name all scheme investments would currently be held. The benefit of being a restricted scheme is eroded if such schemes are compelled to have external custody in these situations as this will simply add a layer of cost without tangible benefit. ▪ Workplace Savings NZ submits that the requirement for external custodianship should not be imposed on

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		<p>restricted schemes, relying upon the licensing of the restricted scheme’s independent trustee to ensure that custodianship arrangements are appropriate. Alternatively, flexibility could be introduced to only impose that requirement where the FMA is not satisfied that the restricted scheme’s custodianship arrangements are adequate.</p>
<p>Clause 112 and 113 (1) (b)</p>	<p>Additional initial and ongoing registration requirements for KiwiSaver/superannuation schemes</p>	<ul style="list-style-type: none"> ▪ The Superannuation Schemes Act 1989 currently requires registered superannuation schemes to have a ‘principal’ purpose of providing retirement benefits to beneficiaries who are natural persons or paying benefits to persons who are the trustees of a registered superannuation scheme or a KiwiSaver scheme. ▪ Workplace Savings NZ is concerned that the limitation of the initial and ongoing registration requirements for KiwiSaver and superannuation schemes proposed in the Bill is too limited in requiring the purpose of the scheme to be providing retirement benefits directly or indirectly to individuals. Many superannuation schemes, particularly those in the workplace environment, provide for disability benefits, and for benefits on leaving service. Whilst the principal purpose of the scheme remains the provision of the retirement benefits, that is demonstrably not the only purpose. For master superannuation schemes accepting other superannuation schemes as members, it is not a given that the purpose of the scheme is to provide benefits indirectly to individuals: such schemes are often utilised as convenient investment vehicles, with the applicability of the purpose of providing retirement benefits “indirectly to individuals” being debatable. ▪ The concern is even more explicit with KiwiSaver schemes, where a clear purpose is to assist people save for their first home. In our view, no KiwiSaver scheme would satisfy the requirements of clause 112(1)(b) for this reason. ▪ Accordingly, Workplace Savings NZ submits that: <ul style="list-style-type: none"> ○ Clause 112(1)(b) should be deleted. The sole requirement of relevance is captured under the current (d) through restricting redemptions and withdrawals to those permitted under the KiwiSaver scheme rules. ○ Clause 113(1)(b) should be amended so as to reflect the current definition appearing in the Superannuation Schemes Act 1989. Our view is that this definition works appropriately, with sufficient flexibility to enable ancillary benefits to be included without undermining the purpose of a superannuation scheme registration. In particular, we would prefer to see the

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		<p>formula of referring to the provision of benefits to other superannuation schemes included.</p>
Clause 113 (2)	Additional initial and ongoing registration requirements for superannuation schemes	<ul style="list-style-type: none"> ▪ It would be useful to clarify the seeming intention that the New Zealand criteria will only apply at the point when a person joins a scheme. Naturally they are otherwise completely unworkable, including for KiwiSaver, given that current members can retain their membership after moving overseas. ▪ As a minimum, given that a number of superannuation schemes currently registered under the Superannuation Schemes Act 1989 will have a practice of admitting members who do not satisfy the proposed New Zealand criteria, it is important that grandfathering provisions are included so that it is only admissions to membership after the commencement date of the legislation that are affected. Terms of existing memberships should not be affected. ▪ The requirement to limit new membership admissions to New Zealand citizens or those with indefinite entitlement to be in New Zealand may be problematic for those employers who from time to time need to second international labour on local terms and conditions. Workplace Savings NZ submits that specific relief from the citizenship requirement should be included to cater for the position where a person is entitled to join a particular scheme as part of that person's terms of employment. ▪ If the restrictions survive, there should be grandfathering of eligibility for scheme membership that exists in employment contracts entered into prior to the commencement date, as current terms of employment may entitle employees to join the workplace scheme irrespective of where they are resident.
Clause 114 (1)	This is additional ongoing registration requirements for restricted scheme.	<ul style="list-style-type: none"> ▪ The word "industry" should be added into the paragraph after "trade" and before "or occupation" to specifically recognise existing industry superannuation schemes. ▪ For example: the Meat Industry Super Scheme, the Seafarers Super Scheme and the Waterfront Industry Super Fund, are three examples of multi-employer super schemes open to employees from within those particular industries, regardless of their profession, trade or occupation.
Clause 114 (2)	Additional ongoing registration requirements for restricted schemes	<ul style="list-style-type: none"> ▪ Workplace Savings NZ is concerned that the requirement that an independent trustee not be a scheme participant may prevent a former participant from being an independent trustee. We would prefer any doubt to be removed by the insertion of the

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		<p>word "current" in the prohibition on being a scheme participant.</p> <ul style="list-style-type: none"> ▪ At paragraph (e) and (f), it is uncertain as to whether a mere appointee of a union or an employer should be regarded as a 'representative'. In some instances, there will be provision for a party to appoint a trustee, with no constitutional requirement for that person to "represent the interests" of the appointing body. It would be helpful if this point were clarified.
Clause 121	Changes to governing document	<ul style="list-style-type: none"> ▪ Clause 121(3)(a) - the way this clause is drafted amendments to a master trust will require a special resolution of all members of the scheme. This is not appropriate where the amendment only affects employees of a particular participating employer. Accordingly Workplace Savings NZ submits that a special resolution should only be required by those participants that are affected by the proposed amendment. ▪ Governing documents - it is arguable that the definition of governing documents includes not only the trust deed but also an administration agreement and an investment management agreement. These documents "govern the activities of the scheme". Workplace Savings NZ submits that it is not appropriate that these documents are caught within the governing document definition.
Clause 126	Duty of manager and investment manager to comply with relevant professional standard of care	<ul style="list-style-type: none"> ▪ Workplace Savings NZ is supportive of a higher standard of care applying to the licensed independent trustee of a restricted scheme, compared with the obligation placed on a trustee who is not a professional manager. We believe this strikes an appropriate balance in the context of a restricted scheme. ▪ Nevertheless, Workplace Savings NZ does have a concern that the pool of individuals willing to take on trusteeship of a restricted scheme will be detrimentally affected by concerns over the extent of potential liability for those involved. For lay trustees it is particularly important they have comfort that they are able to rely upon professional advice, where it is reasonable for them to rely upon that advice. In our view, this is implicit in the requirement to exercise the care, diligence, and skill that a prudent person of business would exercise in the same circumstances as the lay trustees, but including explicit reference to the ability to rely upon professional advice would provide a desirable additional level of comfort. ▪ Whilst we have focused on the possible concerns of lay trustees in relation to their position under the legislation, the point about being able to rely upon professional advice also applies to professional

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		managers (including licensed independent trustees).
Clause 135	Requirement to have supervisor or other independent person as custodian	<ul style="list-style-type: none"> ▪ As noted above, the absolute requirement to contract the holding of the scheme property to another person who meets the custodianship requirements is unduly inflexible in the case of a restricted scheme. ▪ If the relief from external custodianship for restricted schemes requested under clause 111 is not provided, Workplace Savings NZ submits that clause 135(2) and/or 135(4) should be amended to permit the holding of scheme property by the same person as, or a person associated with, the issuer of a restricted scheme, with the consent of the FMA. ▪ If either option for granting relief from external custodianship for restricted schemes is granted, clause 136 and 137 will require consequential amendment so that the obligation for keeping scheme property flows through to situations where the custodian is the same person as the scheme manager (being the trustee, in the case of a restricted scheme).
Clause 153	Additional restrictions on the transactions of restricted scheme	<ul style="list-style-type: none"> ▪ It is possible that some schemes that would otherwise satisfy the requirements for a restricted scheme will currently be in breach of the restrictions on related party transactions, as proposed. For those schemes, it is quite possible that it may not be in the best interests of scheme members for that particular investment to be sold down, due to market conditions or other factors. Accordingly, Workplace Savings NZ submits that, as a minimum, transitional relief should be provided for restricted schemes in relation to investments held as at the commencement date of the new legislation. ▪ Regardless, restricting investments to no more than 5% of scheme property in investments relating to or managed by a scheme participant will present an unreasonable compliance burden on the part of those schemes. Information is not generally held in relation to financial interests of scheme members. The extent of due diligence required of trustees is unreasonable, and there is no lever available to force members to fully disclose related party interests that might be problematic. ▪ Workplace Savings NZ is also concerned that in some situations, investment in a wholesale investment scheme, as commonly occurs, may be prohibited under the proposed restriction. This will be particularly relevant for a restricted scheme provided by a participant in the managed funds industry who would customarily place investments of the restricted scheme in its own wholesale investment scheme, as offered to its other wholesale clients.

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		<ul style="list-style-type: none"> ▪ In order to overcome the above concerns, Workplace Savings NZ would like to see: <ul style="list-style-type: none"> ○ The current maximum of 5% of scheme property invested in related party arrangements being increased to 20%. This would provide a more workable threshold for restricted schemes to work towards, whilst still ensuring that 80% of a scheme's investments are not related. ○ Either removal of the reference to investments related to or managed by a scheme participant, or adjustment of the requirement so that there must be actual knowledge of the trustees before the prohibition applies, so as to avoid the very real risk of inadvertent non-compliance that the trustees are powerless to manage. ○ Relief provided in relation to investment in other managed investment products that are available to third parties. ▪ Clause 153(b) would prohibit the provision of financial assistance to scheme participants. Some schemes will allow members to draw down against the security of their own scheme balances for limited purposes, or otherwise permit limited financial assistance being provided. This is generally seen as a desirable feature of the workplace schemes in question. Workplace Savings NZ would prefer to see more flexibility in the context of the provision of financial assistance to scheme participants, to enable limited provision to be made, with appropriate safeguards. Caps could be placed on the maximum level of financial assistance that could be provided, and relief provided for lending to a member against the security of the members balance in the scheme, up to the level of that balance.
Clause 160	Removal of manager of registered scheme	<ul style="list-style-type: none"> ▪ Workplace Savings NZ submits that sub-clause 160(1)(b) – removal of the manager by a special resolution of the scheme participants – should not apply to restricted schemes and an exclusion from the application of this sub-clause should be introduced for restricted schemes. It is inappropriate for scheme participants to be able to remove the manager (trustee of the workplace savings scheme) in the context of workplace savings schemes which typically have set trustee appointment and removal mechanisms. The employer participants in such schemes will typically have contributed significantly to the scheme yet under proposed clause 160(1)(b) would have no vote/recourse as they are not a scheme participant.
Part 5	Dealing in financial products on markets	
		Workplace Savings NZ does not wish to make submissions

Clause Number	Clause heading	Submission
		on Part 5 of the Exposure Draft
Part 6	Licensing and other regulation of market services	
		Workplace Savings NZ does not wish to make submissions on Part 6 of the Exposure Draft
Part 7	Enforcement and liability	
		Workplace Savings NZ does not wish to make submissions on Part 7 of the Exposure Draft
Part 8	Regulations and exemptions	
		Workplace Savings NZ does not wish to make submissions on Part 8 of the Exposure Draft
Part 9 and schedule 4	Miscellaneous provisions	
		Workplace Savings NZ does not wish to make submissions on Part 9 of the Exposure Draft

Submission Ends