

FUND MANAGERS FORUM

Emerging Themes from Licensing

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Forum Overview

1. Culture and conduct
2. Licensing process
3. Licensing tips
4. Beyond licensing
5. Public disclosure
6. Consultation papers and others

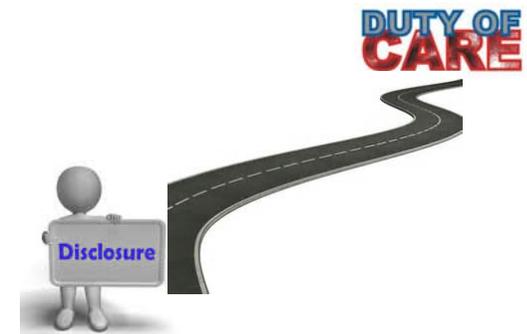


Section 1 – Culture and Conduct

Section 1 – Culture and Conduct

Moving beyond disclosure...

- Traditional approach to securities regulation relied solely on disclosure
- Assumption that if all information is available, investors will be fairly armed and react rationally
- No account taken of natural biases, avoidances, behaviour
- Two main changes under Financial Markets Conduct Act:
 - Nature of disclosure has changed – a useful tool for investors, not a liability cover for firms
 - Good disclosure is still important – but insufficient on its own



Section 1 – Culture and Conduct

... to licencing

Generally focussed on ability to manage conduct risks

- Corporate structure
- Supervision
- Financial management
- Oversight of internal and external stakeholders
- Governance enables knowledgeable decisions
 - Board
 - Senior management

Does structure create a client that puts customer interests at the heart of the business?



Section 2 – Licensing Process

Getting to the end goal

Section 2 – Licensing Process

Time is getting short - Is your plan in place?

Ensure you have a plan

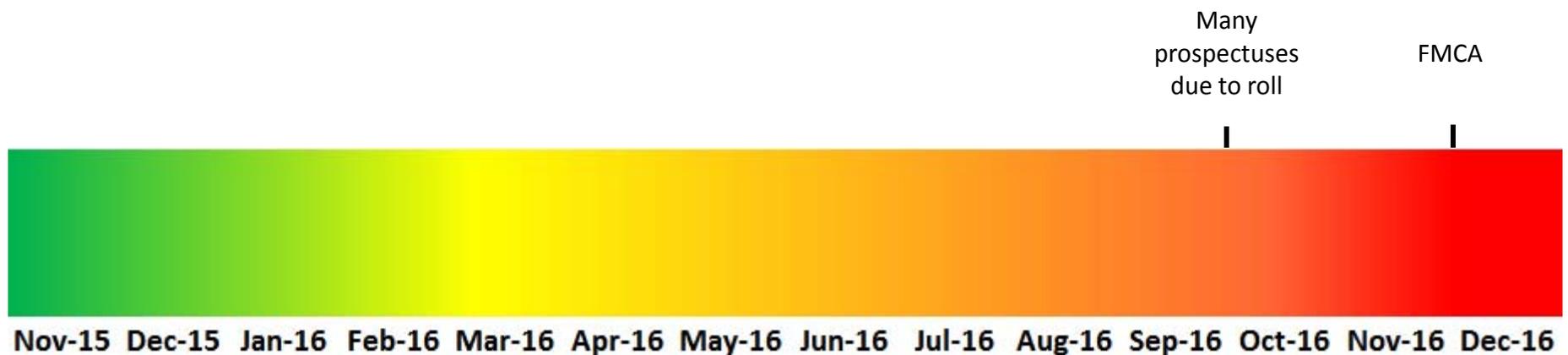
- Timing of application, licence, transition
- Working with your supervisor
- Engaging with the FMA
- Your plan



Section 2 – Licensing Process

Apply in time to meet your requirements

- Engage early with
 - The FMA
 - Supervisors
- Allow enough time between licensing and transition



Section 2 – Licensing Process

Indicative Timeline

Submit Application



Fit & Proper



Assessment



Request Add'l Info



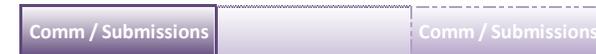
Assess Add'l Info



Peer Review / Decision



Communications / Submissions



Peer Review / Final Decision



Section 2 – Licensing Process

Speeding things up

How to speed up your licensing timeframe...

- Engage with the FMA early if any questions
 - Process: Carolyn.Wrightson@fma.govt.nz
 - Application: FMCApplcations@fma.govt.nz
- Don't delay. Submit your application as soon as possible
- Clear and concise explanation of your business
- Supporting evidence
 - Mandatory documents
 - Key policies



Section 3 – Licensing Tips

Ensuring an efficient licensing experience

Section 3 – Licensing Tips

Reading the MIS Manager Licensing Guide

MIS Manager Licensing Guide

- Key licensing document
- Sets out the questions in the licensing portal
- Assessment is against the minimum standards

We assess against Minimum standards

Questions are reference point for discussion

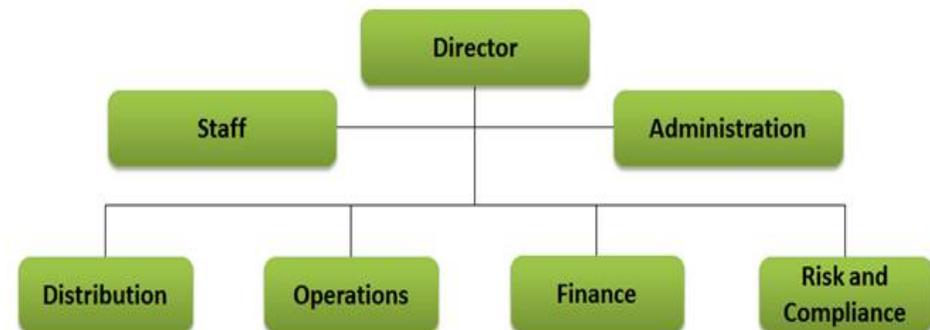
Minimum standards	Information for applicants
<p>A. Selecting investments</p> <p>You must exercise a professional standard of skill and care throughout the investment process.</p> <p>Minimum standards</p> <ol style="list-style-type: none"> 1. You have adequate and effective processes to select and allocate assets/instruments to comply with the investment of investment policy and objectives (including: <ul style="list-style-type: none"> • Your criteria and processes take into account suitability for different types of assets/instruments, and the impact of investment techniques and strategies. • You allocate assets using the limits and parameters set out in your SPO. 2. Key staff involved in investment decisions have sufficient relevant skills, experience and training to ensure you meet the professional standard of care. 3. You stress test your investment strategies as appropriate for the particular investment strategy or scheme assets. <ul style="list-style-type: none"> • You maintain efficient procedures to identify transactions involving a related party benefits and deal with them appropriately. • You maintain efficient procedures to identify conflicts of interest (actual or potential) and deal with them appropriately. 	<p>B. What do we ask?</p> <p>Please explain how you will meet the minimum standards for selecting and allocating scheme investments. How do you fulfil your professional standard of skill and care?</p> <ul style="list-style-type: none"> • Do you stress test your investment strategies? (see comment 2) • Do you have procedures to identify transactions involving related party benefits? • Do the persons involved in investment selection have the skills, experience and training to meet a professional standard of care? <p>C. Our comments</p> <p>10. Selecting and allocating assets</p> <ol style="list-style-type: none"> a. Please explain the methodologies you use to select and allocate assets in the scheme, and how they help you comply with the parameters and/or limits set out in the SPO. Processes for selecting and allocating schemes will vary in complexity depending on the nature of the assets. If the scheme invests in a single asset class, your methodology may be relatively simple. b. If you use an outsource provider, please tell us their name and function's here (later in the outsourcing part of the form) or ask for more details about the arrangement. <p>11. Your investment team</p> <p>10. Your investment decision making team as a whole must have the right mix of skills and there must be appropriate oversight and controls. This skill mix must include input from people with relevant qualifications, such as Chartered Financial Analysts, or equivalent qualifications and/or experience.</p> <p>11. Please describe how you ensure the people involved in the investment decisions collectively have the breadth and depth of knowledge and expertise to make decisions. For example, how do your selection processes and ongoing training ensure your team taken together has the right skill mix and their investment skills and experience remain current?</p> <p>c. When you're placing staff in investment focused roles, we expect you to consider their: <ul style="list-style-type: none"> • Relevant qualifications for the role • Knowledge and/or experience of the types of investments covered in the SPO • Previous past roles involving relevant investment duties, and the time spent in those roles • Amount of time under management in current and past roles • Training received and ongoing training planned. </p>

Comments clarify and provide helpful hints

Section 3 – Licensing Tips

Help us to understand your business

- Key facts – locations, FTE, FUM, funds, schemes, etc.
- Pictures help!
 - Organisation chart
 - Ownership and key stakeholders
 - Related bodies and outsource partners
- Current business model + planned changes
- Conditions or restrictions on license
- Exemptions – engage early!



Section 3 – Licensing Tips

Help us know the people behind your business

Your people

- Name all directors and senior managers
 - CVs and position descriptions
- For small business, name all key people
- Any committees
 - Who sits on these committees, capabilities
- Roles and responsibilities of management team
 - Who performs which function?



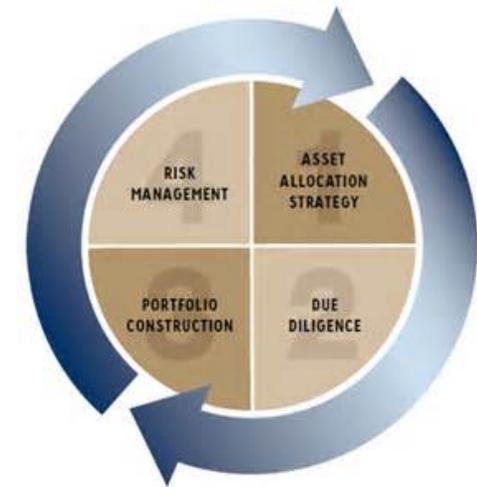
Ref: Minimum standards - Fit and Proper and Capability

Section 3 – Licensing Tips

Tell us how your business is organised and structured

Your operating model

- How your business operates
- Systems, processes, structures
- Policies, procedures and controls
- Provide evidence through key documents
 - Outsourcing, unit pricing, limit breaks, staff trading, related party



- **Ref: Minimum standards** - Operational Infrastructure

Section 3 – Licensing Tips

Tell us what you actually do in practice

How do you prevent misconduct?

- Insider trading
- Market manipulation
- Trade allocation biases
- Provide evidence through key documents
 - Staff trading policy, dealing policy, management of conflict of interests



- **Ref: Minimum standards** - Operational Infrastructure

Section 3 – Licensing Tips

Outsourcing and Custody

Outsourcing

- Can outsource the function but not the obligation
- Arrangements and agreements
- Oversight
- If highly outsourced model, pictures help!

Custody

- Suitable and independent
- Reconciliation



Section 3 – Licensing Tips

Why are you a sound business for investors to invest with

Your finances and financial management

- Demonstrate the strength of your balance sheet
- Cashflows, NTA, auditor, accountant,
- PI insurance –check for exclusions
- Policies, procedures and controls for financial management
- Provide evidence through key documents



- **Ref: Minimum standards** - Financial Resources

Section 3 – Licensing Tips

How you ensure you will meet your obligations as a MIS Manager Licensee

Your governance, culture and compliance arrangements

- **Governance** framework, oversight body
 - Appropriate risk management
- **Culture** – how do you demonstrate?
 - Code of conduct, ethical frameworks
- **Compliance** framework
- Compliance assurance programme
 - Monitoring and testing outsourced service providers
 - Assurance for meeting ongoing obligations



- **Ref: Minimum standards - Governance**

Section 4 – Beyond Licensing

- **First steps**
- **Obligations and duties under the new regime**
- **Ongoing role as manager of registered schemes**
- **Relationship with supervisor**
- **Relationship with the FMA**

Section 4 – Beyond Licensing

First steps

- Licence conditions or prerequisites that impact immediately
- Note section 57 of the Financial Reporting Act 2013
 - Once you are licensed you are an FMC reporting entity and the financial reporting requirements of the FMC Act apply to **all of your schemes**, regardless of whether or not they have transitioned to the FMC Act
- Plan for the transition of your schemes
 - Identify any issues, prepare key documents, and sort out transition timing
 - FMA publications on transition:
 - [Preparing for the FMC Act – Transition for Managed Investment Schemes](#)
 - Transition timelines, timings and road maps (all similar) for: [Unit Trusts](#), [Superannuation](#) and [KiwiSaver](#)
 - [FMA consent to governing document amendments under clause 26, Schedule 4 of the FMC Act](#)
 - [Guidance note on statements of investment policy and objectives \(SIPO\) under the FMC Act](#)
 - Notice of a scheme's effective date can be given to both the Registrar and the FMA at the same time through the Disclose website



Section 4 – Beyond Licensing

Obligations and duties under the new regime

- As a manager of a registered scheme you will have a number of duties and obligations under Part 4 of the FMC Act and related regulations
- As a licensed MIS manager you will have obligations under Part 6 of the FMC Act and related regulations, and under the conditions of your licence
- Other parts of the FMC Act also very relevant – fair dealing, initial and ongoing disclosure, secondary market conduct, and financial reporting
- Ensure you have a clear understanding of your duties and obligations
 - Have a compliance calendar
 - Ensure sure you have a clear understanding of:
 - Events that trigger or timing of registration, notification, and reporting obligations
 - Who you need to notify or report to (i.e. the Registrar, your supervisor, or the FMA)



Section 4 – Beyond Licensing

Ongoing role as manager of registered schemes

- Fundamentally, as manager of a registered scheme, your role is to manage the scheme property and investments, and administer the scheme
- The new regulatory overlay under the FMC Act now puts that in the context of:
 - Overarching duties
 - Statutory duty of care
 - Statutory duty to act in the best interests of investors
 - FMC Act compliant trust deed
 - SIPO
- FMA publications:
 - [Information sheet on new governance and accountability framework for MIS managers and their licensed supervisors](#)
 - [Guidance on governance under Part 4 of the FMC Act](#)

Put yourself in
THEIR
shoes



Section 4 – Beyond Licensing

Relationship with supervisor

- Key focus is on overseeing your management of registered schemes
- Work with your supervisor to ensure there are appropriate and effective systems and processes in place
- Reporting and notification obligations to supervisor
- Your relationship with your supervisor is the ‘front line’ compliance supervision relationship relating to your management of registered schemes
- FMA publications
 - [Related-party transactions under the Financial Markets Conduct Act 2013](#)
 - [Reporting SIPO limit breaks](#)



Section 4 – Beyond Licensing

Relationship with the FMA

As market services licensee

- Key focus is on continuing to:
 - Meet eligibility criteria / minimum standards
 - Comply with conditions of licence
- Reporting and notifications direct to the FMA
- Regulatory reporting (forthcoming)

Disclosure

- New/continuous offers (more on this later)
- Fund updates (more on this later)
- Financial reporting
- Fair dealing under Part 2 of the FMC Act
- Secondary market conduct
 - [FMA information sheet - Market misconduct risks: a guide for MIS managers](#)



Questions



Section 5 – Public Disclosure

- PDS
- Disclose Register

Section 5 – Public Disclosure

Drafting a PDS: Example MIS Managed Fund

Describing the investment objectives

- Consider drafting SIPO (Statement of Investment Policy and Objectives) first
 - Involve your supervisor
 - See our guidance on SIPOs (published November 2014) at fma.govt.nz
- Then, summarise investment objectives and investment strategy for the fund to about a paragraph (including a diagram or other description summarising its target investment mix) for the main body of the PDS
- Then, condense to a couple of sentences to describe the fund and its investment objective in the KIS (Key Information Summary)
 - For example: “The Conservative Fund invests mostly in assets with lower risks and returns, with some investment in growth assets that may give higher returns. The fund has a low to medium level of volatility.”



Section 5 – Public Disclosure

Drafting a PDS: Example MIS Managed Fund

Describing the investment objectives

- Be clear, concise and effective in your description
- Avoid industry jargon
- A glossary of key terms can help make the PDS clear
(But, remember there are certain sections of the PDS that are required to contain certain information, so that information must be understandable without referring to the glossary)
- Consider including tables, pictures and info-graphics if they make the PDS clearer and easier to read, but not if it detracts from the information
- Similar tips apply when describing your business in an equity PDS



Section 5 – Public Disclosure

Drafting a PDS: Managed Fund Risk Indicator

- One horizontal bar (from 1 to 7) risk indicator for each:
 - Fund
 - Multi-fund investment option
 - Life cycle stage (or representative stages) within a life cycle investment option
- European CESR Guidelines are useful to help you calculate risk indicator
- Starting point is to calculate volatility over previous 5 year period, but the indicator must reflect the potential future volatility of the fund
- See guidance on risk indicators and descriptions of managed funds on fma.govt.nz, which covers:
 - How to calculate and present the risk indicator;
 - When to update a PDS for a change in the risk category;
 - How to describe your fund's volatility (if you choose to do so); and
 - Tips on avoiding misleading names for your fund.



Section 5 – Public Disclosure

Drafting a PDS: Managed Fund Risk Indicator

Risks

- Not all 'risks' captured in volatility measure
- **General investment risks**
 - Risks that are reflected in the risk indicator
 - Must be 'briefly' described, i.e. a couple of sentences
 - Examples include 'investment return risk, market risk, company risk, credit risk, and currency risk'
- **Other specific risks**
 - Risks that are not already reflected in the risk indicator
 - Must clearly, concisely and effectively describe the risk and context



Section 5 – Public Disclosure

Drafting a PDS: Managed Fund Risk Section

What risks to describe:

- Requirements in equity PDS are similar to requirements for ‘other specific risks’ in managed fund PDS
- Describe **circumstances** that exist or are likely to arise, but only....
 - Where those circumstances significantly increase the risk to the returns for investors [for a managed fund] or to the issuing group’s financial position, financial performance, or stated plans [for equity]
 - Only describe circumstances that relate to the particular fund/ issuer/ security that make the risks of investing different from the risks of investing in other funds/ issuers/ securities
 - Only describe circumstances that a reasonable person would expect to affect an investor’s decision to invest



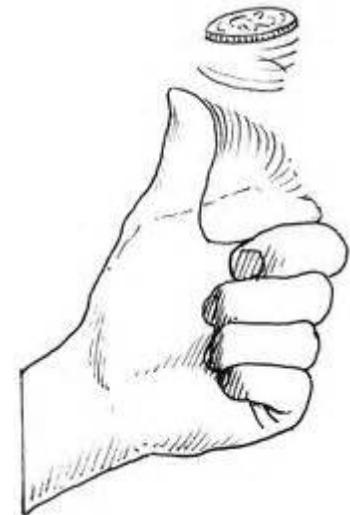
Section 5 – Public Disclosure

Drafting a PDS: Managed Fund Risk Section

How to describe risks:*

Description of each circumstance should say:

- Why the circumstance is of **particular relevance** to this particular scheme / fund/ issuer / issue of securities
- Sufficient information for an investor to assess the **likelihood** of the potential impact happening
- Sufficient information for an investor to assess the **nature** of the potential impact
- Sufficient information for an investor to assess the potential **magnitude** of any potential impact



*Applies to all risks in an Equity PDS, and to 'Other specific risks' in a Managed Fund PDS

Section 5 – Public Disclosure

Drafting a PDS: Describing Managed Fund Fees

Underlying funds' fees

- Ensure that all applicable fees and charges from both **related and non-related underlying funds** have been considered in the fees calculations as appropriate

Fee categories

- Use the defined terms in the regulations to categorise all fees and charges



Section 5 – Public Disclosure

Drafting a PDS: Describing Managed Fund Fees

Hurdle rate of return

- Where a fund's hurdle rate of return is not linked to the performance of an appropriate market index, it should be clearly disclosed in the offer documents

The effect of having no high water mark

- Where no high water mark applies, this should be disclosed

See [draft] guidance on disclosure of certain fees and returns by managed funds on fma.govt.nz.



Section 5 – Public Disclosure

Disclose register information

Three types of information

- Specified information entered into data entry fields
e.g. name of issuer, term of offer etc.
- Other information required by regulations
e.g. constitutional documents
- All other material information not contained in the PDS
e.g. additional information



Section 5 – Public Disclosure

Disclose register information

- Understand what the regulations require. Don't just rely on what is set as mandatory / non-mandatory fields on the disclose register
- The information on the register is dynamic and will require updating
- The register must include a complete list of individual assets of the fund including:
 - The name of the asset,
 - The value of the asset as a percentage of the specified fund's net asset value
 - If applicable, a security identification number, ticker symbol, or exchange code used to identify the asset



Section 6 - Consultation Papers & Others

- **Consultation Papers**
- **Upcoming Exemption Consultation, Guidance Notes and Reports**

Section 6 – Consultation Papers & Others

Current consultation

Consultation paper: disclosure of certain fees and returns by managed funds

Our proposed guidance covers these areas:

- Calculation of returns applying a 0% prescribed investor rate (PIR)
- Classifying underlying fund charges
- Calculation and disclosure of performance-based fees in managed funds.



See guidance on disclosure of certain fees and returns by managed funds on fma.govt.nz.

Section 6 – Consultation Papers & Others

Upcoming

Upcoming Exemption Consultation

- Inactive legacy issues – financial reporting and governance relief
- Independent custody for inactive legacy schemes

Upcoming Guidance Notes

- Updates/changes to the Annual declaration of compliance for FMC Act licensees
- Fund update template and guidance for calculating risk indicators
- Changes to licence standard conditions

Upcoming Reports

- Sales and advice report
- Audit quality review report



Questions

