

Legal update - Financial Markets Conduct Regulations - Governance

6 November 2014

What's happening?

As mentioned in our previous updates, the 'near final' draft of the Financial Markets Conduct Regulations (Regulations) was released on 26 September 2014 to give market participants an opportunity to prepare for the full implementation of the Financial Markets Conduct Act 2013 (FMCA) on 1 December 2014. The final version of the Regulations was agreed on 3 November 2014 and can be accessed [online](#). The Regulations will cover all aspects of the FMCA and will replace the (more limited) Financial Markets Conduct (Phase 1) Regulations.

This particular update is concerned with the governance obligations under the FMCA. Broadly speaking, the general trend in our financial markets has been to focus more on the responsibilities of managers and trustees in relation to their offerings of financial products, and the FMCA continues this trend.

In a nutshell, what does the FMCA say about governance?

Part 4 of the FMCA provides for the governance of regulated products (which are financial products offered under regulated offers) as follows:

- In relation to regulated offers of debt securities, it sets out the need for a trust deed and a supervisor, as well as other issuer and supervisor obligations
- In relation to regulated offers of managed investment products, it sets out the need for a governing document, a supervisor and for the managed investment scheme offering the managed investment products to be registered (registered scheme), as well as other issuer, supervisor and custodian obligations
- In relation to regulated offers of debt securities and registered schemes, it sets out the duties of persons associated with these offerings to make protected disclosures to the FMA and/or supervisor, as well as powers of intervention to enable supervision by the supervisor or the FMA
- In relation to all regulated products, it provides for ongoing duties of issuers to maintain registers and keep copies of documents.

What do the regulations add?

The Regulations provide more detail on the contents of governing documents, meeting proceedings of product holders/scheme participants and reporting obligations of the issuer, as well as supplementing the provisions that are set out in Part 4 of the FMCA. In addition to the Regulations, the FMA has also published a Guidance Note on Governance (which sets out the FMA's expectations for managers and supervisors in relation to the responsibilities and accountabilities that apply under Part 4 of the FMC) and an Information Sheet on Reporting Duties under Part 4 of the FMCA.

Although the additional content of governing documents, meeting procedures and reporting obligations in the Regulations varies for regulated offers of debt securities and registered schemes, there are certain common elements:

- Meeting procedures are set out in Schedule 11 to the Regulations, except to the extent the governing document provides otherwise (but clauses 2 and 5 of Schedule 11 for debt securities and clauses 2, 3 and 5 of Schedule 11 for regulated schemes cannot be disapplied).
- Governing documents must set out any changes/additions to the meetings procedures in Schedule 11 and frequency and content of reporting by the manager/issuer to the supervisor. (For debt securities, a governing document must also contain financial covenants that the issuer has given in favour of the holders or the supervisor, prohibitions/restrictions on the issuer

entering into transactions with related parties/associated persons, the appointment and removal of the supervisor, and any other matters that materially affect the rights/duties of holders or the powers/rights/duties of the issuer and supervisor.) There are terms that must be implied in the governing documents - for debt securities these terms include clauses 1 to 3 of Schedule 10 to the Regulations (and for a NBDT that is not a building society, credit union or co-operative company clauses 4 and 5 as well), and for registered schemes these terms include clauses 1 to 3 of Schedule 13 (or for a restricted scheme clause 4 only) and the superannuation scheme rules set out in Schedule 12 to the Regulations if the regulated scheme is a superannuation scheme still open to new members.

- Ongoing reporting to the supervisor - for debt securities (where the issuer is a NBDT that is not a building society, credit union or co-operative company) monthly and quarterly reports signed by two directors of the issuer in relation to a range of matters (including management, financial information, compliance with offer documents and governing document, and certain transactions), and for registered schemes quarterly reports from the manager on limit breaks and related party transactions, as well as more immediate reports on limit breaks and pricing errors.

In addition, the Regulations set out:

- The contents of an application to register a managed investment scheme and how to apply
- What records the custodian of a registered scheme must keep in relation to scheme property
- When a register of a regulated product does not need to be kept and when public inspection of that register is not required
- When and how a register of a regulated product needs to be audited
- Reporting obligations and terms implied in the governing documents for a Schedule 3 (of the FMCA) scheme.

What's next?

We recommend that market participants should:

- Reach a view on whether their business will be, or is currently, making a regulated offer of financial products, and therefore will need to comply with the new governance regime
- Once you've mapped out how the governance aspects of the FMCA regime will affect your business, plan the timetable for the transition process - while the transition provisions in the FMCA give businesses up to two years to make the necessary changes, this time will pass quickly
- Keep an eye out for our final update (on the financial product markets aspects of the FMCA regime).

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