

Shaping the future of our markets

13 November 2013

Consultation: Licensing MIS managers

Draft minimum standards and licence conditions for managers of non-restricted and registered Managed Investment Schemes (MIS)

The Financial Markets Conduct Act 2013 (the Act) introduces licensing for providers offering certain types of financial services.

In future, you will need a licence if you want to act as a manager of a non-restricted and registered managed investment scheme (MIS) – and will need to meet, and maintain, minimum standards across key areas of your business.

This paper summarises the proposed minimum standards for a MIS licence. There is a separate paper for independent trustees of restricted schemes. We invite you to review our proposal and share your feedback with us. This is our chance to work together to shape the new future for our industry.

Submissions close on 12 December 2013. The form at the back provides more details.

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A. What are MIS?

A Managed Investment Scheme (MIS) pools money from a number of investors, who rely on the investment expertise of a MIS manager. See section 9 of the Act for the definition of MIS.

The definition of MIS is very broad. It includes collective investment schemes, and most schemes involving participatory securities under the Securities Act 1978.

MIS can be structured in different ways and can invest in a wide range of investments. They can be open-ended or closed-ended:

- **Open-ended** schemes are offered continuously – examples include KiwiSaver, superannuation, workplace savings schemes, open-ended unit trusts, and other schemes that invest in relatively liquid assets.

The assets may be held by the MIS on behalf of all its investors, or they may be divided into multiple funds, each held by a different set of investors.

- **Closed-ended** schemes are more equity-like – examples include forestry partnerships and property syndicates which invest in a single asset class.

What's not a MIS?

Discretionary investment management services (DIMS), insurance contracts, and schemes that only involve management of separate and direct interests in underlying property are not considered MIS under the Act.

B. Will you need a licence?

You will need a MIS manager licence if you are the appointed or designated manager of a non-restricted and registered MIS.

Specifically, you will need a MIS manager licence if you intend to:

1. Make a regulated offer of managed investment products to retail investors
2. Register a non-restricted MIS you have been appointed the manager of.

If you currently manage a MIS, there will be a transition period which will allow you to continue operating under the old regime for a certain time. Details will be published on our website about the transition.

C. Minimum standards – five key areas

To become a MIS licence holder your business must meet a range of minimum standards. We propose that providers will need to meet minimum standards in five key areas:

- Fit and proper – ‘fit and proper’ directors, senior managers and other relevant parties
- Capability – the skill and experience of your directors, senior team and staff
- Operational infrastructure – the proper functioning of your MIS business, including your investor services, investment activities and business operations
- Financial resources – financial resources and professional indemnity insurance
- Governance – governance and compliance culture.

You must meet the minimum standards at the time of licensing and on an on-going basis. These proposed standards do not cover all your obligations under the Act or regulations.

D. For your information

Related bodies

You may apply for a licence that covers any related companies who will provide part or all of the licensed service with you. Where we refer to ‘related bodies’ it means any related body corporate we include on your licence under Section 400 of the Act.

If you have related bodies under your licence, they must comply with all licence obligations, and you need to provide oversight to ensure your group as a whole meets the minimum standards. Where you use a related body to provide part of your MIS operations it is usually more appropriate to include them in your licence application than to ‘outsource’ the activity to them.

Systems, processes and procedures

Throughout this paper we talk about the need for systems, processes and procedures, or arrangements. We cannot be more specific because regulations and standards are still being finalised and, importantly, because what will be required will depend to some degree on the nature of your business. We will take the size, complexity and nature of your business into account when we assess your application.

Terms

FMC	Financial Markets Conduct Act 2013 (‘the Act’)
MIS	Non-restricted and registered Managed Investment Scheme
MIP	Managed investment products
SIPO	Statement of investment policy and objectives

Please note

This paper is intended to give you a high level overview of proposed minimum standards and conditions for market service licensees, which will come into effect under the Act, so that you have the chance to comment. Regulations are still being developed and there may be changes. A licence application guide will be published after regulations are finalised.

Fit and proper

Your directors and senior managers must be fit and proper persons to hold their respective positions.

Minimum standards

1. Your directors and senior managers (current or proposed) must be fit and proper persons to hold their position. This requirement broadly covers the tests of:
 - **Good character** covering integrity, probity, trustworthiness, character and reputation (see note 1)
 - **Capability** – competence, skills and experience – the next section on capability provides more details.
2. You must have recruitment and human resources processes to ensure that directors and senior managers undergo a character assessment – and that their competence, skills and experience are assessed before they assume their roles.
3. Your directors and senior managers must not obtain an improper advantage, cause detriment to your clients, or make improper use of their position (see section 145 of the Act).
4. If you have related bodies under your licence, each entity's executive directors and senior managers who are responsible for the licensed service must meet these minimum standards.

Note 1: We will assess **good character** based on various factors including (but not limited to) past non-compliance; convictions or involvement in dishonesty, deceit, theft or fraud; failure to manage business or personal financial affairs; dismissal from a position of trust; and adverse information from other public bodies including other regulators and Inland Revenue.

We must also consider whether your owners or other relevant parties have had any convictions or successful disciplinary actions taken against them. The regulations will provide more details about what we must take into account.

Capability

You need to show you have the right mix of people, with the right skills and experience, in the right roles, to run your MIS business properly and effectively.

Minimum standards

1. Your senior management team (collectively) must have an appropriate breadth and depth of relevant financial industry know-how (relevant to MIS), whether in New Zealand or elsewhere.
2. Roles are documented and include clear responsibility and accountability for:
 - Effective operation of the MIS key activities (see note 1)
 - Strategic development and direction of your business
 - Risk management
 - Financial management
 - Compliance with product-specific laws and regulatory requirements
 - Compliance assurance/internal audit to ensure controls and procedures are effective
 - Investor complaints.
3. Your recruitment and human resources processes ensure that directors and senior management's present and past skills and experience enable them to perform their roles. You will have considered:
 - Present or past roles and length of time in those roles
 - Relevant qualifications (formal qualifications will be particularly relevant when a person is to fill a key financial control role, or a key investment role)
 - Amount of assets under management in current and past roles (if relevant to the specific role they will undertake)
 - If their current role is not relevant – when the last relevant role was held, and for how long.
4. Your business has access to any necessary professional advice (for example legal or tax advice) either through internal appointments or external consultants.

Note 1: For example key activities may include scheme set-up and investment strategy, investment activities, asset valuation and unit pricing, monitoring and reporting, custody, and oversight of outsourced activities.

Part 4. Operational infrastructure

Scheme formation | Advertising & disclosure | Selecting investments | Monitoring performance | Material issues | Asset values | Unit prices | Fund administration | Records Custody | Outsourcing | Resources | Supervision | IT systems | On-going reports & disclosure

A. Scheme formation

The scheme must be properly set up and administered.

Minimum standards

Before you can offer the managed investment products (MIP) in a scheme you must complete certain steps. You need to:

1. Take all necessary steps to register the scheme and maintain the register.
2. Ensure your governing document meets all the requirements of the Act (section 135).
3. Appoint a licensed supervisor, and all other necessary providers.
4. Form an investment strategy – to be included in the scheme’s statement of investment policy and objectives (SIPO).
5. Set a suitable trading frequency – one that is realistic and appropriate for the scheme’s SIPO and which allows redemptions to be processed efficiently.
6. Establish an effective investment governance framework that:
 - Identifies the body (for example an investment committee) responsible for ensuring the SIPO is implemented
 - Sets out your approach to changing the SIPO
 - Ensures the scheme only invests in authorised investments that meet investment policy and objectives.
7. Have adequate resources to implement the investment strategy, including appropriate analyst support.

B. Advertising and disclosure

You give investors the information they need to make informed decisions about investing in your scheme – and your services are not inappropriately marketed.

Minimum standards

1. You must maintain adequate and effective systems to bring investors on board with processes and controls to ensure the requirements of the Act are met, including the
 - Fair Dealing obligations in Part 2 of the Act
 - Disclosure obligations in Part 3 of the Act and the regulations
 - Governance requirements in Part 4 of the Act and the regulations.

You may also have other legal requirements to meet (for example under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009, and the Privacy Act 1993).

2. Staff are aware of their professional obligations and are adequately trained in the systems and processes for bringing investors on board.
3. You promote and maintain an honest and professional culture, which puts the best interests of the investors first.

C. Selecting investments

You exercise a professional standard of skill and care throughout the investment process, including when selecting investments for the initial portfolio and on an on-going basis.

Minimum standards

1. You must have adequate and effective processes to select and allocate assets/instruments to comply with the SIPO, including:
 - An investment strategy for each investment option – that includes return and risk objectives, and a benchmark index
 - Supporting your strategy with up-to-date research and analysis of asset classes and benchmarks
 - Selection criteria and processes for direct investments and funds, and for outsourced investment managers
 - Your criteria and processes take liquidity into account – for different types of assets/instruments and the impact of investment techniques and strategies
 - You set trading restrictions, such as authorised investments and price limits
 - Assets are allocated using the limits and parameters set by your investment committee.
2. Staff involved in investment decisions must have sufficient relevant skills, experience and training to meet the ‘professional standard of care’. You will have considered their:
 - Relevant qualifications for the role (see note 1)
 - Knowledge and/or experience of the types of investments covered by the SIPO
 - Present or past roles involving relevant investment duties, and time spent in the roles
 - Amount of assets under management in current and past roles
 - Training received and planned on-going training.
3. You ‘stress test’ your investment strategies. The stress testing scenarios should cover a range of factors that can create extraordinary losses or make the control of risk within the investment strategy difficult.
4. You maintain efficient procedures to identify transactions involving a related party benefit and deal with them appropriately.
5. You maintain efficient procedures to identify conflicts (or potential conflicts) of interest and deal with them appropriately.

Note 1: Your investment decision making team as a whole must have the right mix of skills and oversight controls. The team must have input from people with higher qualifications, such as chartered financial analysts.

D. Investment monitoring

Your systems and processes enable you to measure and monitor investment performance and take appropriate action when necessary.

Minimum standards

1. Your portfolio monitoring systems and processes must enable you to measure and report performance against the objectives, limits and parameters set out in the scheme's SIPO.
2. Corporate actions (such as dividend payments) are identified and dealt with in your investors' best interests.
3. You have adequate and effective policies, procedures and controls to manage the scheme's investments, including:

Restrictions

- On the nature and frequency of switching
- Trades must be allocated to the designated scheme at the time of trading
- Transaction must be at 'arm's length' – with no trades benefiting the manager or investment manager to the investors' disadvantage
- Controls on when employees can trade
- Benchmark limits are monitored independently against the SIPO (for example by a unit not responsible for MIS performance).

Divestment

- Liquidity risk management is correctly implemented, monitored and reviewed.

4. You have adequate and effective systems and procedures to:
 - Identify, and report where necessary, breaches of limits in the SIPO on the nature, type and relative proportions of investments, and any other anomalous performance
 - Escalate, analyse and follow-up any breaches or anomalous performance
 - Identify breach trends and put in place protections to avoid future breaches.

E. Material issues and complaints

You have effective processes and procedures to identify and deal with material issues in your business.

Minimum standards

1. You maintain effective methods for identifying and reporting to FMA any material change of circumstance or breach of your licensee obligations, as defined in the Act (section 410).
2. You monitor complaints to ensure they are dealt with fairly and in the best interests of the investor. You have systems and procedures to identify trends in complaints – and you investigate and address any issues identified.
3. You are a member of a dispute resolution scheme, as required under the Financial Service Providers (Registration and Dispute Resolution) Act 2008.

F. Asset valuation

You ensure scheme assets are accurately valued.

Minimum standards

1. You have documented methodologies to value each type of scheme asset in a way that is appropriate for the asset type and complexity.
2. You apply methodologies consistently across similar assets, and review them periodically.
3. Assets are valued regularly and independently by staff with the right skills, experience and training (see note 1).
4. Conflicts of interest in asset values are addressed – and values authorised before being used to price units.
5. If you use a third party for this function, your due diligence (both initial and periodic) must confirm their processes meet these minimum standards for asset valuation, and their people have the right skills, experience and training to do the valuation.

Note 1: If valuation is done in-house, the function must be carried out independently of the investment management function.

G. Unit pricing

You adhere to pricing methodology – and ensure pricing errors are minimised. If errors are found they are corrected immediately.

Minimum standards

1. Your unit pricing is transparent, applied consistently and reviewed regularly.
2. You have an explicit policy to determine when a pricing error or non-compliance with pricing methodology is a material breach – this includes non-compliance with both the scheme's governing document, or with any FMA notice.
3. There is clear ownership of each input/output to the pricing system.
4. Unit pricing errors (and processes that could lead to errors) are promptly identified and amended.
5. For **KiwiSaver**, the design of the pricing process across legacy, current and proposed schemes does not provide opportunities for arbitrage.
6. All investors (incoming, continuing, outgoing) are treated equitably – purchases and redemptions are done fairly.
7. Data is cross checked for accuracy before it is used.
8. If you use a third party for this function, your due diligence (both initial and periodic) must confirm their processes meet these minimum standards for unit pricing, and their people have the right skills, experience and training to do the pricing.

H. Fund administration

You administer the scheme in a proper and efficient manner.

Minimum standards

1. Your systems, procedures and controls must ensure that all scheme money is properly accounted for at all times.
 2. **Applications, contributions and redemptions** – your systems, procedures and controls ensure:
 - Processing of applications and redemptions is timely – investor’s money is held in trust
 - Money is invested correctly (right price and scheme, recorded against the right investor)
 - Interests in the scheme are issued correctly, as set out in the product disclosure statement (PDS) and governing document.
 3. **Income and distributions** – your systems, procedures and controls ensure:
 - Income is properly calculated, recorded and distributed
 - All sources of income/payments to the scheme are identified and captured
 - Distributions from the scheme are identified according to policy
 - Scheme records accurately reflect corporate actions
 - Income, distributions and re-investments are calculated and processed as set out in the PDS, governing document and investor instructions
 - The scheme’s taxable income is monitored against accounting income to ensure all taxable income is distributed at the end of the financial year
 - Reconciliations with the custodian’s valuations are carried out at appropriate frequencies
 - Discrepancies are dealt with in a timely and efficient manner.
 4. **Fees and expenses** – your systems, procedures and controls ensure:
 - Fees and scheme related expenses are valid, accurate and in keeping with the governing document and information given to investors
 - Fees are charged fairly across all scheme participants.
 5. If you use a third party for this function, your due diligence (both initial and periodic) must confirm their processes meet these minimum standards for fund administration, and their people have the right skills, experience and training to do the administration.
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I. Records

You must maintain adequate records and provide information to FMA in a timely manner.

Minimum standards

1. You must have systems and procedures to maintain proper records (including information about the MIS, the investment decisions made and the reasons for those decisions).
2. You are required to retain these records for at least seven years – and they must be available for immediate inspection by FMA at any time.

J. Custody

Scheme money and property must be held at arm's length.

Minimum standards

1. You ensure scheme property is properly identified, and held separately from your property and the property of any other scheme.
2. You must not hold any scheme property yourself, and any custodian you use must be independent.
3. You regularly reconcile your records of holdings with the custodian's records (see note 1).

Note 1: For registered schemes, the legal requirement is for the supervisor to hold scheme property (unless your governing document authorises someone else who meets external custodianship requirements) [section 156]. The custodian has set obligations, including confirming information about the scheme property they hold to the manager [section 159].

K. Outsourcing (*excluding custody*)

You must ensure all outsourced functions are adequate, effective and comply with your licence obligations.

Minimum standards

1. You must conduct due diligence before outsourcing to ensure the provider is an appropriate entity and capable of effectively performing the outsourced function to an acceptable service level. Your considerations may include:
 - The outsource provider's previous experience
 - Public reports and information about their service
 - Reported complaints about them, and their complaint handling procedures
 - Their operating jurisdiction and any protections/controls imposed in that jurisdiction.
2. You have a proper legal arrangement with the provider, including provisions that enable you to effectively monitor their performance and take appropriate action for non-performance.
3. Records and information the provider holds are available for inspection by FMA at any time.
4. You regularly review the outsource arrangement (at a frequency appropriate to the risk involved) – you must ensure all outsourced functions are carried out as if you were doing them yourself (see section 146(2) of the Act)
5. Your performance monitoring programme includes:
 - Checks that the provider's performance meets required standards
 - Triggers for non-performance
 - A plan for steps you will take in the event of non-performance.
6. **Related bodies** - if you are using a related body to provide part of your MIS functions, these outsourcing minimum standards may not be applicable. However, you must have oversight over the related body to ensure your group as a whole meets the minimum standards.

L. Resources and infrastructure

You must have the necessary technological and human resource capacity to provide the MIS service.

Minimum standards

1. You must have effective processes and procedures to maintain sufficient technological and human resources to deliver your MIS service.
 2. You regularly review resourcing levels and anticipate any increase in demands, so that resource levels remain appropriate for the scale and complexity of your MIS business (reviews should include outsourced functions).
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M. Staffing and supervision

You have adequate and effective arrangements to manage and supervise staff and core processes. Your staff are fit for their roles and act professionally.

Minimum standards

Your arrangements ensure:

1. Staff have the right skills and experience for their roles, and a clear job description that sets out their responsibilities (including authorisation/delegation levels).
2. Roles are designed to support key controls (for example by segregating duties between roles) and enough time is allowed for key processes including compliance activities.
3. Staff are appropriately trained, managed and supervised – you address poor performance and recognise professional conduct.
4. You have appropriate supervisory arrangements, including:
 - Sufficient resources are allocated to supervision
 - Supervisory staff with the right knowledge and experience (including understanding the functions of the roles they supervise)
 - Supervisory staff have the support and authority they need to do the role effectively
 - Any issues identified by supervisory staff are acted on appropriately.

N. IT systems

Your IT systems used to deliver the MIS must be secure and reliable. Your arrangements ensure they perform efficiently and the associated risks are managed.

Minimum standards

1. Your IT systems include all necessary functionality to provide your service, and perform the intended processes effectively.
2. Your IT systems have built in parameters consistent with the governing document or PDS, and pricing IT systems have controls to ensure the integrity of external data feeds, and their accurate use in calculations.
3. You have effective safeguards and controls over the IT systems (and the underlying processes) whether they are built into, or external to, the system.

These include processes:

- To ensure data and system security – and prevent errors or system failure
 - Which take into account risk from human error, technical failure and malicious conduct.
4. You maintain an appropriate (and tested) business continuity plan – including procedures for data back-up and disaster recovery.
 5. You have proper legal arrangements with any third party software providers, including licences for software and contracts for any required maintenance and support.
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O. Reporting and on-going disclosure

You keep your supervisor, investors and public up to date as needed.

Minimum standards

1. You comply with all requests for information from your supervisor or FMA and have identified the:
 - Role of the board in responding to requests from the supervisor, and meeting your reporting obligations under the Act
 - Person who will be responsible for responding to the supervisor.
2. You alert your supervisor and **proactively** tell FMA of any changes to the business that you are required to report (including adverse events), and you have identified the person who will be responsible for the reporting.

Part 5. Financial Resources

Financial resources | Professional indemnity insurance

A. Financial resources

You must, at all times, have adequate financial resources to effectively perform the market service covered by the licence – and to ensure there is sufficient money for the orderly transfer or wind up of the scheme should your business cease.

Minimum standards

1. You must have positive net tangible assets (note 1).
2. You must be able to pay your debts as they become due in the normal course of business (see note 2).
3. At all times, you must maintain an appropriate level of liquid assets for your business – three months of actual or projected outgoings, on a rolling basis, with allowance for contingencies (see note 3).
4. You must have adequate and effective systems, policies, procedures and controls to:
 - Constantly monitor your financial resource levels
 - Consistently calculate an appropriate level of liquid assets to hold for your business
 - Assess the risk of your financial resources not being adequate to continue to provide the service, or a serious financial problem occurring
 - Notify FMA if a material change of circumstance occurs, or is likely to occur, in relation to the licence – as required in section 410 of the Act (see note 4).

Note 1: Your **net tangible asset (NTA)** means your total net assets as they appear in your balance sheet (calculated according to NZ IFRS). Your NTA calculation can't include intangible assets, any client funds you hold, and any related party receivables except those resulting from a transaction done in the ordinary course of business, at arms-length. For the purpose of this calculation we propose to limit related party receivables to no more than 20% of NTA.

Note 2: To satisfy yourself you can continue to meet this standard, we expect you to use a suitable **forecasting** mechanism.

Note 3: For this purpose, **liquid assets** are defined as cash or cash equivalents, trade receivables realisable within the next three months (on a rolling basis), and financial assets that have a ready market and are valued at current market prices. You must not include any client funds you hold, or any investments you have in the portfolios you manage.

Note 4: A **material change** of circumstance includes becoming aware that you will have insufficient liquid assets to meet your liabilities as they fall due.

B. Professional indemnity insurance

You must maintain an adequate minimum level of professional indemnity insurance cover.

Minimum standards

1. You must maintain professional indemnity insurance to cover risks related to your market service.
2. Your level of professional indemnity insurance cover should be adequate and appropriate for the nature, scale and complexity of the market service you are licensed for – there is no set minimum cover, it depends on your business.
3. You must have sufficient resources to meet any policy excess.

Part 6. Governance

Governance | Culture | Compliance

A. Governance

You have a high-level body responsible for overseeing compliance with your obligations as a market service licensee, and ensuring appropriate risk management and fair treatment of investors.

Minimum standards

1. You must have a clear reporting and governance framework covering all key aspects of the MIS business (or proposed business) including compliance obligations and key risks of the business.
2. You have an 'oversight body' responsible for overseeing compliance – compliance should not solely be the responsibility of risk, compliance or internal audit functions (see note 1).
3. You have appropriate arrangements to ensure your oversight body and other senior managers and directors get timely, sufficient good-quality governance and management information to allow for proper oversight and decision making.
4. Your oversight body considers the adequacy and robustness of its governance and compliance arrangements at least annually.
5. Your constitution must not have any provision which would allow your directors to act contrary to the MIS manager's best interest, when they are exercising their powers or performing their duties. This also applies to directors of related bodies under your licence. (See Section 396(f) of the Act for more details).
6. **Related bodies** – your oversight body is able to direct and oversee the provision of market services by any related body operating under your licence (see note 2).

Note 1: We expect that the **oversight body** will be the board or a risk committee of the board – or in larger organisations, a committee comprised of senior executives responsible for the MIS services plus representatives from legal, risk and compliance areas.

Note 2: For **related bodies** this is likely to include the ability to approve, or require changes to, key processes and controls, and effective processes to ensure that the oversight body is provided with sufficient good-quality governance and management information.

B. Culture

You have governance and compliance arrangements that promote a culture of compliance with your obligations as a licensee, and ensure appropriate risk management and fair treatment of investors.

Minimum standards

1. You have a good compliance culture, supported by systems, policies, procedures and controls.
2. We expect a good compliance culture to include the following:
 - You clearly communicate your conduct expectations to staff, for example through a code of conduct or code of ethics
 - Management actively supports professionalism in their messages to staff
 - Remuneration, reviews, promotions and other incentives recognise professionalism and compliance, not just the achievement of revenue, cost or profit targets
 - You have processes to identify and manage conflicts between the interests of the licensee (or individual staff) and investors' interests – and you quickly resolve any issues in a way that is fair to investors and reasonable for the licensed business
 - You allocate adequate time and resources for training, supervision and compliance activities
 - Management encourages staff to report breaches or inappropriate behaviour, and deals appropriately with staff who report matters (for example through an independent whistle-blowing policy)
 - Management willingly engages with relevant regulators in an open and honest manner, and are responsive to any regulatory concerns they may raise.
3. **Any related bodies** operating under your licence must also promote a culture of compliance, appropriate risk management and fair treatment of investors.

C. Compliance

You have adequate and effective arrangements for challenging and testing your own compliance, the compliance framework and the outcomes.

Minimum standards

1. Compliance assurance

You must have adequate and effective arrangements to challenge and test the design and operation of processes and controls, and the adequacy of governance and management information (your compliance assurance programme).

Your compliance **assurance programme** goes beyond the day-to-day controls for key processes, by including more in-depth testing of processes and controls including:

- The testing (and the design of the testing) is done independently of those involved in day-to-day processes and oversight – for example testing is done by a separate compliance or internal audit function, or by an external operation
 - You allocate sufficient, appropriate resources to planning and carrying out the programme, and ensure those involved have the skill and experience to carry out the work
 - Your compliance assurance programme is approved by your oversight body
 - Your oversight body is kept updated about progress against the compliance programme – you also report significant findings to them and follow up on remedial action taken.
2. Your compliance monitoring covers both substantive outcomes and procedural correctness.

3. Related bodies

If you have related bodies operating under your licence, they must also have a compliance assurance programme, and your oversight body should:

- Be responsible for, or have significant input into approval of, these programmes (at least to the extent they relate to the licensed service)
- Have adequate information and sufficient authority to monitor progress, consider significant findings, and ensure appropriate remedial action is taken.

Part 7. Licence conditions

A. Standard conditions

If we grant you a MIS manager's licence, it will contain conditions that support your licensee obligations. These are the standard conditions we are proposing to include. The regulations may contain further standard conditions.

1. **Skills and expertise**

You, or any related body covered by your licence, must inform us whenever there is a change in the senior management team.

2. **Investing**

You must maintain procedures to monitor any dealings with scheme assets to ensure the limits and asset allocations set out in the SIPO are adhered to at all times.

3. **Outsourcing**

If you outsource a process/system necessary to the effective and proper running of the MIS (or any other licensee obligation) you must have a legally binding agreement with the provider. This must allow both you and FMA access to all the information needed for monitoring.

4. **Regulatory returns**

You must provide us with the information we need to monitor your on-going capability to effectively perform the MIS service in accordance with the applicable eligibility criteria in the Act. This will include updated information on the nature, size and complexity of your MIS business. Information will need to be provided in accordance with any regulatory return framework and methodology we issue under subpart 4 of part 8 of the Act.

5. **Financial resources**

You must continue to satisfy the minimum standards for financial resources, and an external qualified auditor will need to review and confirm your compliance annually.

6. **Governance**

You must have, at all times, adequate and effective systems, policies, processes and controls that are reasonably likely to ensure you will perform the market services you are licensed for in an effective manner.

7. **Compliance**

You must maintain a compliance governance document. This must identify the principal risks and outline the key processes and controls relied on by your oversight body (and board, if different) to ensure you comply with your obligations and adequately manage the risks.

Your compliance governance document will need to:

- Be approved by the oversight body
- Be kept up-to-date, and periodically reviewed by the oversight body
- Reflect your business model and processes, compliance and governance arrangements.

Your governance and compliance arrangements must be substantially the same, or better than, those described in your compliance governance document at the time you applied for your licence (or any later version supplied to us).

8. **Breach of requirements**

You must immediately inform us if you breach any condition of your licence – and you must take immediate steps to rectify the breach.

B. Specific conditions

We may also set extra licence conditions for individual entities on a case by case basis, for example:

1. **Limits**

If you request a limit on your licensed activity, or can only demonstrate the capacity to provide an effective service within certain parameters, we may set limits on your licence.

Part 8. Frameworks and methodologies

The Act allows us to issue ‘frameworks and methodologies’ to set out detailed or technical obligations. Initially, we won’t do this for everything we’re allowed to cover – for some things it may be better to provide non-binding guidance. See subpart 4, part 9 of the Act for more details.

Material limit breaks

We propose to issue a framework and methodology under Section 167 of the Act, which deals with actions required if there is a material limit break under the scheme’s SIPO.

In the box below are the limit breaks we propose you must always treat as material. You may also need to consider other breaches of investment limits as material based on the circumstances – if in doubt a limit break should be considered a material one.

Proposed content of framework and methodology

These are examples of limit breaks that are always material. With any other type of limit break, you need to consider all the surrounding circumstances to decide if it is material – if there is any doubt we suggest you treat it as material.

Limit breaks:

- Any purchase of an investment of a type or nature prohibited under the scheme’s SIPO, must be treated as a material limit break. For example, purchase of Australian shares if Australian equities exposure is not permitted.

Where the scheme’s SIPO involves rebalancing of assets:

- If a **time period** has been clearly set out in the SIPO for rebalancing the proportion of each type of asset that may be invested in, failure to complete the balance within the specified period must be treated as a material limit break.
- If no time period has been set out in the SIPO for rebalancing the proportion of each type of asset that may be invested in, failure to complete the rebalance within five business days must be treated as a material limit break.

Note: If the SIPO specifies a period for rebalancing assets, we expect you to give the investor clear written disclosure of the risks – and the prominence of that disclosure should be proportionate to the risk. For example, the longer the rebalancing period, or the greater the percentage variance allowed, the higher the risk and the more prominent the risk warning must be.

The next step

How do I make a submission?

Please use the form on the next page – this gives the details of what you need to do. Forms must be submitted electronically in both PDF and word formats and emailed to consultation@fma.govt.nz – please put 'Feedback MIS standards and conditions' in the subject line.

Alternatively, you can make an online submission on our engagement site www.talktous.fma.govt.nz. You need to register to be able to use the site.

Submissions close on 12 December 2013.

Where can I get more information?

You'll find more information about the changes on our website www.fma.govt.nz, or at the Ministry of Business Innovation and Employment site www.mbie.govt.nz

If you have questions about the licensing consultation process, please get in touch.

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