

Financial Markets Conduct (FNZ Group) Exemption Notice 2021

Pursuant to section 556 of the Financial Markets Conduct Act 2013, the Financial Markets Authority, being satisfied of the matters set out in section 557 of that Act, gives the following notice.

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Notice

1 Title

This notice is the Financial Markets Conduct (FNZ Group) Exemption Notice 2021.

2 Commencement

This notice comes into force on 1 July 2021.

3 Revocation

This notice is revoked on the close of 30 June 2026.

4 Interpretation

(1) In this Notice unless the context otherwise requires—

Act means the Financial Markets Conduct Act 2013

buffer means firm money belonging to an FNZ group member that is deposited into the FNZ client money trust account and retained in that account for the purpose of rectifying or reducing the risk of a shortfall arising in respect of—

(a) scheme property; or

(b) client money

held in the FNZ client money trust account

business day means a day on which banks are open for trading in Auckland and Wellington

client has the meaning set out in clause 2(b) of Schedule 5 of the Act

client money and **client property** have the meanings set out in section 431W(5) of the Act

eligible financial adviser means an individual who:

- (a) is registered under the Financial Service Providers (Registration and Dispute Resolution) Act 2008; and
- (b) is lawfully able to design an investment plan for a retail client in terms of section 431C(1)(c) of the Act and is:
 - (i) engaged to provide regulated financial advice on behalf of a financial advice provider licensed under the Act; or
 - (ii) is a financial advice provider licensed under the Act

financial product transaction means a transaction involving the acquisition or disposal, or the variation of the terms of an acquisition or disposal, of a financial product or other dealing in relation to a financial product

financial product transaction business means the business of facilitating or arranging the settlement of financial product transactions on behalf of, or for the benefit of, scheme participants in a self-select scheme (within the investment options approved by the manager for the self-select scheme) or clients under a client money or property service

firm money means money held by or for a FNZ group member on its own account

FNZ client money trust account means an account that a FNZ group member operates as a custodian and that is required by section 157(1) or 431ZC(1)(b) of the Act

FNZ group member means any of FNZ Limited, and FNZ Custodians Limited

former exemption notice means the Financial Markets Conduct (FNZ Group) Exemption Notice 2018 or the Financial Markets Conduct (FNZ Group) Exemption Notice 2020 as applicable

gap analysis means a document that maps the controls in place for the regulation 229U custodian assurance report, against the controls set out in regulation 88 of the Regulations

good custodial practice means exercising the care, diligence, and skill that a prudent custodian would exercise in the conduct of a custodial business in the same circumstances

qualified auditor has the meaning given to it in section 461E of the Act

regulation 229U custodian assurance report has the meaning set out in (a) of the definition of required assurance reports

Regulations means the Financial Markets Conduct Regulations 2014

registered bank has the same meaning as in section 6 of the Act

relevant date, in relation to a FNZ group member means either of the following:

- (a) the FNZ group member's balance date; or
- (b) an alternative date in each calendar year determined by the FNZ group member and notified to the FMA in writing to be its relevant date for the purposes of this notice (but that first relevant date need not be in a particular calendar year)

relevant period, in relation to a FNZ group member, means a 12-month period ending on the relevant date of that FNZ group member, or if there is a change of the relevant date of that FNZ group member, such that the period ending on that date is longer or shorter than 12 months, that longer or shorter period is a relevant period.

relevant persons has the meaning given to it in clause 87(4) of the Regulations

required assurance reports means:

- (a) an assurance report obtained under regulations 229U and 229V of the Regulations in respect of client money and client property held by a FNZ group member for each relevant period
- (b) a type 2 assurance report that is obtained by a FNZ group member under International Standard on Assurance Engagements (New Zealand) 3402 *Assurance Reports on Controls at a Service Organisation* (ISAE (NZ) 3402), issued in New Zealand with reference to Guidance Statement GS007 *Audit Implications of the Use of Service Organisations for Investment Management Services* (GS007) issued by the Australian Auditing and Assurance Standards Board in respect of client money and client property held by a FNZ group member for each relevant period

self-select scheme means a managed investment scheme under which a scheme participant or his or her eligible financial adviser can select the assets to be acquired and held by the scheme for that scheme participant's benefit.

- (2) For the purposes of this notice, a practice or an action of a FNZ group member that involves scheme property or client money or client property being held together with firm money is **reasonably necessary** if—
 - (a) the FNZ group member has taken reasonable steps to investigate alternatives that would overcome or reduce the extent to which scheme property or client money or client property is held together with firm money; and
 - (b) the FNZ group member is satisfied on reasonable grounds either that, in the circumstances, there are no alternatives available or that any such alternatives—
 - (i) would pose an undue risk to the prudent and orderly conduct of its financial product transaction business; or
 - (ii) are not able to be accessed or implemented without exposing the FNZ group member or a self-select scheme or its scheme participants or a client under a client money or property service to an unreasonable level of cost or delay or risk; or
 - (iii) would be contrary to the best interests of a self-select scheme or its scheme participants or a client under a client money or property service being able to undertake financial product transactions in a timely and prudent manner
- (3) Any term or expression that is defined in the Act and the Regulations and used, but not defined, in this notice has the same meaning as in the Act and the Regulations.

5 Exemption from obligation to hold scheme property separately

Each FNZ group member is exempt from section 157(2)(a) of the Act in respect of the scheme property of a self-select scheme to the extent that:

- (a) it is reasonably necessary for firm money to be held together with scheme property in the FNZ client money trust account to reduce or rectify the risk of a shortfall arising in the scheme property held for the benefit of a scheme participant in a self-select scheme in that account; or

- (b) firm money is held in that account in order to rectify, or reduce the risk of, a shortfall arising in the client money held for a client under a client money or property service in that account in accordance with section 431ZC(3) and (4) of the Act and regulations 229ZA and 229ZC of the Regulations.

6 Exemption from obligations for handling client money

Each FNZ group member is exempt from section 431ZC(2) and (4) of the Act and regulations 229ZA, 229ZC and Schedule 21C of the Regulations to the extent that firm money is held in the FNZ client money trust account to reduce or rectify the risk of a shortfall arising in the scheme property held for the benefit of a scheme participant in a self-select scheme in that account in reliance on the exemption in clause 5(a).

7 Conditions of exemptions in clause 5

(1) The exemptions in clause 5 are subject to the conditions that:

- (a) firm money must be held together with scheme property only to the extent that is reasonably necessary for the purposes of the FNZ group member conducting its financial product transaction business in a prudent and orderly fashion; and
- (b) the FNZ group member must not place firm money into the FNZ client money trust account for any purpose other than:
 - (i) facilitating or arranging the settlement of 1 or more financial product transactions for a self-select scheme for the benefit of a scheme participant or rectifying or reducing the risk of a shortfall arising in the scheme property of a self-select scheme held for the benefit of a scheme participant in that account; or
 - (ii) facilitating or arranging the settlement of 1 or more financial product transactions for a client under a client money or property service, or rectifying, or reducing the risk of, a shortfall arising in the client money held for a client in that account; and
- (c) the FNZ group member must take reasonable steps to ensure that the amount of firm money in the FNZ client money trust account is no more than the amount that is reasonably necessary to:
 - (i) facilitate or arrange the settlement of 1 or more financial product transactions for a self-select scheme for the benefit of a scheme participant and rectify or cover the risk of a shortfall arising in the scheme property held for the benefit of a scheme participant at any time; and
 - (ii) facilitate or arrange the settlement of 1 or more financial product transactions for a client under a client money or property service and rectify or cover the risk of a shortfall arising in the client money held for their clients at any time; and
- (d) the FNZ group member must take all reasonable steps to ensure that scheme property remains separately identifiable from firm money; and
- (e) the FNZ group member must document, implement, and monitor processes that are consistent with good custodian practice and that are appropriate to manage the risks to any self-select scheme and its scheme participants associated with not separating firm money from scheme property, in reliance on the exemption in clause 5, in the context of the FNZ group member's financial product transaction business.

8 Further conditions of exemptions in clause 5

The exemptions in clause 5 are subject to the further conditions that—

- (a) the FNZ group member must maintain at least 1 FNZ client money trust account at a registered bank in each currency in which it accepts scheme property of a self-select scheme; and
- (b) the FNZ group member must provide the manager and supervisor of any self-select scheme with the following information in writing before the FNZ group member holds any scheme property for that self-select scheme:
 - (i) a statement that all scheme property received by the FNZ group member will be held on trust for that self-select scheme for the benefit of a scheme participant and deposited in the FNZ client money trust account; and
 - (ii) a summary of the terms of that trust; and
 - (iii) a statement to the effect that an amount of money held by or for the FNZ group member on its own account may be deposited by the FNZ group member in the FNZ client money trust account to the extent that is reasonably necessary to rectify or reduce the risk of a shortfall arising in the scheme property held for the benefit of a scheme participant or to rectify or reduce the risk of a shortfall arising in the client money held for the benefit of a client under a client money or property service in that account and otherwise on the terms and condition of this notice; and
 - (iv) a description of any risks to scheme participants that the FNZ group member is aware of that exist or are likely to arise as a result of scheme property not being held separate from firm money in reliance on the exemption in clause 5; and
- (c) the FNZ group member must, in relation to each FNZ client money trust account, -
 - (i) have obtained from the bank holding that FNZ client money trust account a written acknowledgement of the trust status of that account; and
 - (ii) ensure that the words "client funds account", "trust account", "client funds a/c", or "trust a/c" appear in the name of that FNZ client money trust account; and
 - (iii) if the name, account number, or status of that FNZ client money trust account changes, obtain from the bank holding that FNZ client money trust account a new written acknowledgement of the trust status of that account as soon as practicable after the date of the change; and
- (d) the FNZ group member must, on each business day, take adequate steps to reconcile the records for each FNZ client money trust account with the records of the bank holding the FNZ client money trust account for the purpose of identifying whether there is any shortfall in the scheme property held for the benefit of a scheme participant in the FNZ client money trust account or any risk that a shortfall may occur; and
- (e) if, on any business day, the FNZ group member identifies that there is a shortfall or a risk that a shortfall may occur, the FNZ group member must take reasonable steps to rectify the shortfall or prevent that shortfall occurring by paying into the account, before the end of that business day, by way of, or on account of, a buffer of an amount affirm money that is not less than the amount of the shortfall or anticipated shortfall; and
- (f) the FNZ group member must retain written records of the operation of each FNZ client money trust account that include the following information, and make those records available to the supervisor as soon as practicable after the supervisor makes any request:

- (i) details of any shortfalls that occurred in the scheme property held for the benefit of a scheme participant of a self-select scheme in the FNZ client money trust account; and
 - (ii) details of any risks that a shortfall might arise in the scheme property held for the benefit of a scheme participant in a self-select scheme in the FNZ client money trust account identified by the FNZ group member; and
 - (iii) details of any payments of firm money into the FNZ client money trust account by way of, or on account of, a buffer; and
- (g) the FNZ group member must obtain, within 4 months after each relevant date, a report from a qualified auditor regarding the FNZ group member's compliance with the conditions in this notice during the relevant period and provide a copy of that report to the supervisor and the manager of the relevant self-select scheme within 20 working days after it has been obtained; and
- (h) the FNZ group member must ensure that the qualified auditor provides to the supervisor of the relevant self-select scheme, any information that the supervisor may request from the qualified auditor regarding the FNZ group member's compliance with the conditions in this notice during the relevant period as soon as practicable after the supervisor makes any request; and
- (i) the FNZ group member must provide the qualified auditor with all necessary access to its systems and records, and otherwise co-operate fully with the qualified auditor, to enable the qualified auditor-
- (i) to assess ongoing compliance by the FNZ group member with the conditions in this notice; and
 - (ii) to provide the reports and other information required by this notice; and
- (j) the FNZ group member must provide the supervisor of the relevant self-select scheme and the qualified auditor with a written consent authorising the qualified auditor to provide the supervisor and the manager of the relevant self-select scheme with the information required by this notice; and
- (k) the report obtained from the qualified auditor under paragraph (g) in respect of the FNZ group member's compliance with the conditions in this notice must be prepared in accordance with the applicable auditing and assurance standards issued by the External Reporting Board under section 12 of the Financial Reporting Act 2013 (for example, the Standard on Assurance Engagements 3100 Compliance Engagements (SAE 3100)).

9 Exemption from obligations to obtain assurance engagement

Each FNZ group member is exempted from regulation 87(1) and (2) of the Regulations in relation to a relevant date for the FNZ group member that occurs on or after the commencement date of this notice, and thereafter the relevant period ending on that date.

10 Conditions of exemption in clause 9

- (1) The exemption in clause 9 is subject to the conditions that:
- (a) the FNZ group member obtains the required assurance reports from a qualified auditor; and
 - (b) the FNZ group member provides copies of the required assurance reports to the relevant persons within 20 working days after obtaining the required assurance reports.

- (2) The required assurance reports must include an assessment by the qualified auditor as to whether in the auditor's opinion there is reasonable assurance that the custodian's processes, procedures and controls, in respect of scheme property of any self-select scheme held in the FNZ client money trust account were suitably designed to meet the relevant control objectives; and
- (3) The regulation 229U custodian assurance report provided to the supervisor and manager of the scheme must be accompanied by a gap analysis and where there are any gaps, include a detailed explanation of the gap and any remedial action to be undertaken or why no action is required to be taken.
- (4) Subclauses (1)(a) and (2) must be complied with within 4 months after the end of each relevant date; and
- (5) Subclause (3) must be complied with within 20 working days after obtaining the required assurance reports.

11 Transitional provisions relating to former exemption notice

- (1) If a FNZ group member gave information to the manager and supervisor of a self-select scheme under clause 7(1)(b) of a former exemption notice, the FNZ group member must be treated as having complied with clause 8(b) of this notice in relation to that self-select scheme.
- (2) If a FNZ group member holds a current acknowledgement under clause 7(1)(c) of a former exemption notice in relation to a bank account, the FNZ group member must be treated as having complied with clause 8(c) of this notice in relation to that account (but a new written acknowledgement must be provided under clause 8(c) if there are any subsequent changes as referred to in that clause).
- (3) If a FNZ group member provided a written consent to the supervisor of a self-select scheme and a qualified auditor under clause 7(j) of a former exemption notice the FNZ group member must be treated as having complied with clause 8(j) of this notice in relation to that self-select scheme.
- (4) A FNZ group member's relevant date under clause 4(1) of a former exemption notice must be treated as the FNZ group member's relevant date under clause 4(1) of this notice (until the FNZ group member changes that date).

Dated at Wellington this 28th day of June 2021.



Liam Mason
General Counsel
Financial Markets Authority

Statement of Reasons

This notice comes into force on 1 July 2021 and is revoked on the close of 30 June 2026, exempts FNZ Limited, and FNZ Custodians Limited (each a FNZ group member), on conditions, from the following provisions of the Financial Markets Conduct Act 2013 (the Act) and the Financial Markets Conduct Regulations 2014 (the Regulations):

- section 157(2)(a) and section 431ZC(2) and (4) of the Act; and
- regulations 87(1) and (2), 229ZA, 229ZC and Schedule 21C of the Regulations:

Section 157(2)(a) is the requirement that a custodian for a registered managed investment scheme ensures that scheme property is held separate from property held by the custodian on its own account (the segregation requirement).

Section 431ZC(2) of the Act requires a provider of a client money or property services to keep client money and client property separate from money or property held by the provider on its own account. However, section 431ZC(3) and regulation 229ZA of the Regulations permits co-mingling of client money or property with firm money of a provider in certain circumstances. Section 431ZC(4), regulation 229ZC and Schedule 21C of the Regulations prescribe duties that the provider must meet to be permitted to co-mingle client money or property with firm money.

The main effect of the notice is to allow an FNZ group member to hold firm money with scheme property of a self-select scheme in the FNZ client money trust account to the extent that it is reasonably necessary to rectify or reduce the risk of a shortfall arising in the scheme property held in that account.

The notice also allows an FNZ group member, where client money and self-select scheme property are held together in the FNZ client money trust account, to keep firm money in that account in respect of the client money as permitted by the client money and property services regime in Subpart 5B of the Act and the Regulations.

A practice or an action will be regarded as reasonably necessary if the FNZ group member:

- has taken reasonable steps to investigate alternatives that would overcome or reduce the extent to which scheme property or client money or client property is held together with firm money; or
- is satisfied on reasonable grounds either that, in the circumstances, there are no alternatives available or that any such alternatives-
 - would pose an undue risk to the prudent and orderly conduct of its financial product transaction; or
 - is not able to be accessed or implemented without exposing the FNZ group member or a self-select scheme or any scheme participant or a client under a client money or property service to an unreasonable level of cost or delay or risk; or
 - would be contrary to the best interests of a self-select scheme or any scheme participant or a client under a client money or property service being able to undertake financial product transactions in a timely and prudent manner.

Regulation 87(1) and (2) is the requirement that a custodian for a managed investment scheme must obtain an assurance engagement that covers the assurance engagement matters specified in regulation 88 of the Regulations.

The exemption relieves the FNZ group member from the requirement to obtain an assurance engagement in relation to custody of scheme property of self-select schemes.

The Financial Markets Authority (the **FMA**), after satisfying itself as to the matters set out in section 557 of the Act, considers it appropriate to grant the exemptions because—

- FNZ group members currently hold self-select scheme property in their client money trust account together with client money under a client money or property service;
- FNZ group members intend to keep a buffer of firm money in their client money trust account from time to time to the extent that it is reasonably necessary to rectify or reduce the risk of a shortfall arising in the scheme property or client money held in that account;
- the Act and Regulations already provide for circumstances in which a provider of a client money or property service is not required to hold client money and property separate from firm money or property and may keep a buffer of firm money in their client money trust account together with client money. Certain duties apply to protect the interests of clients. There is no similar provision for scheme property;
- shortfalls in a custodian's client money trust account may occur for a variety of reasons, including bank reversals, timing issues (eg, for offshore trades), changes in foreign exchange rates, processing errors, tax or fee payment obligations, payments being dishonoured or reversed, failures by clients to lodge funds, and internal errors;
- these shortfalls, unless addressed, may result in insufficient funds being available to settle financial product transactions on behalf of scheme participants in self-select schemes or clients under a client money or property service;
- upgrading or changing existing systems and processes to mitigate the risks of a shortfall arising without use of a buffer is likely to result in significant compliance costs and business disruption for FNZ. The exemptions will reduce compliance costs for a FNZ group member by relieving it of certain obligations while maintaining appropriate protections for scheme participants;
- conditions to the exemptions will only allow the use of buffers where they are reasonably necessary in order to facilitate the settlement of financial product transactions for scheme participants in a self-select scheme or clients under a client money or property service or reduce the risk of a shortfall arising, and a FNZ group member will be required to take all reasonable steps to ensure that scheme property remains separately identifiable and that the amount of firm money held in the FNZ client money trust account is no more than is reasonably necessary to cover the risk of a shortfall arising;
- requirements in relation to the establishment and operation of the FNZ client money trust account and for a declaration of trust, will ensure that a trust is established to protect scheme property held by the FNZ group member in the FNZ client money trust account. Additionally, conditions will also require the FNZ group member to keep records on compliance with the requirements under this notice and make them available on request. Independent verification regarding compliance will be provided through an assurance engagement and reports obtained from a qualified auditor; and
- adequate custodial assurance reporting is provided by the FNZ group member on the FNZ client money trust account under existing custodial assurance reporting obligations, and conditions requiring a gap analysis will ensure there is adequate custodial assurance reporting of self-select scheme property.

Therefore, the FMA is satisfied that –

- granting the exemptions is necessary or desirable in order to promote the purposes of the Act, specifically, the exemptions will avoid unnecessary compliance costs and promote innovation and flexibility in the financial markets; and

- the exemptions are not broader than is reasonably necessary to address the matters that gave rise to the exemptions because the exemptions are restricted to the custodian in respect of the scheme property of self-select schemes.