APRIL 2024

Submissions report:

Liquidity risk management guide

Summary of themes from submissions made on the draft liquidity risk management guide as part of our consultation

FINANCIAL MARKETS AUTHORITY
TE MANA TĀTAI HOKOHOKO

Contents

Executive summary

Between September and November 2023, the Financial Markets Authority – Te Mana Tātai Hokohoko (**FMA**) consulted on a proposed guide to liquidity risk management (LRM).

The draft guide described how fund managers and their supervisors may design, run and monitor liquidity to help ensure investors are treated equitably and investments can be transferred or cashed out during normal and stressed market conditions.

We thank all 12 submitters for their feedback, which provided helpful observations and insights.

This document summarises the key themes raised in those submissions and our comments about what changes have been made to the guide. It also collates the written submissions. These may withhold some information in accordance with the Official Information Act 1982 and the Privacy Act 2020.

The final version of the guide is now published on our website.

Feedback themes

There were three key feedback themes:

1. Being clear about what are statutory duties, what are FMA expectations, and what (if any) part is 'best practice'
2. Certainty about what the term 'illiquid assets' means
3. Unintended costs and impacts from implementing the draft guide

Expectations, statutory responsibilities, and best practice

Submissions

- Several submitters requested certainty about whether the FMA expected Managers and Supervisors to incorporate all 11 features of the guidance into their liquidity risk management processes and, if so, the legal basis for doing so.
- Some submitters sought word changes to clarify what was mandatory or good practice (e.g. looking at what is a "must" or "should").

Changes to guide

In relation to statutory duties: [1]

- We have clarified that Managers should consider how features in the guide apply to their operations and to each of their funds. This is to ensure Managers have appropriate liquidity risk management-related policies, processes, and tools. Where Managers have not considered the features, we are likely to ask questions of the Supervisor and the Manager. We consider effective LRM is necessary for Managers to demonstrate they are meeting their statutory duties. Those duties are to exercise care, diligence, and skill in performing any duties or exercising any powers, treating scheme participants equitably and acting in the best interests of scheme participants.[2]
- We have made the same clarifications for Supervisors – that a Supervisor exercising care, diligence and skill regularly assesses a Manager's LRM policies, processes and tools, has an active oversight role, and is in a position to identify and make reports under s 203 of the FMC Act.

In terms of our expectations and what (if any) aspects were 'best practice':

- Managers and Supervisors have the best understanding of the asset allocation, markets and risks for the specific funds they offer and oversee. While the guidance draws on international organisations' recommendations for policy makers and scheme managers, we recognise the size, scale, and complexity of domestic funds and markets are very different to most major jurisdictions and funds.

[1] See sections 143(1)(b), 144, and 153(1)(b) of the Financial Markets Conduct Act 2013 (**FMCA).**

- The guide asks for Managers and Supervisors to consider what the essential features of effective liquidity risk management look like in the context of the funds they manage and oversee, and identifies areas we think could improve.
- We have made changes to better illustrate this purpose, including updating the terminology noted above.

Definitions and prescriptiveness

Defining illiquid assets

The revised guidance includes an expectation that the Manager's monitoring framework will have a definition of 'illiquid asset' for the particular fund(s) asset composition. The definition will be used alongside other monitoring measures (such as current time to liquidate) to monitor and manage relative liquidity across the fund.

Submissions

- Many submitters asked the FMA to provide a definition of 'illiquid asset', or offer guidance on calculating the liquidity ratio to assist Managers to prepare their own definitions. Some concerns were noted about Managers adopting overly rigid definitions or about specific markets, and unintended impacts for using standard vendor solutions.
- There were suggestions that FMA should formally adopt the "bucketing" definitions of liquid, illiquid or less liquid (or equivalent) used by the Financial Stability Board (**FSB**) to promote market consistency in New Zealand, so that Managers determine which category or categories apply to their funds, rather than defining the buckets themselves.

Changes to guidance

- We generally agree it would be valuable for New Zealand to have a broadly standard approach to defining illiquidity. We have chosen not to do so in this guidance for two reasons:
  - Guidance is not generally a suitable place for that type of definition.
  - Further consideration is required of how (or whether) New Zealand managed funds would align with the FSB's focus on macro-stability risks given the difference in the size, scale, and complexity compared with global markets.
- We suggest Managers and Supervisors work together with their professional advisers to ensure they adopt definitions that are appropriate for the funds they manage and oversee.

Disclosure and investor communication

Submissions

- Submitters generally sought clarification about the framing of this section, including better aligning terminology with industry use, the role of communications with investors, and expectations for specific liquidity risk management features to be in the Product Disclosure Statement.

Changes to guidance

- We have updated the guide to clarify specifically how Managers can ensure investors are aware of the fund's liquidity risk through effective disclosure, and revised the communications aspect on material changes to focus on matters such as what liquidity management tools (LMTs) the Manager has available.

KiwiSaver and voluntary transfers

Submissions

- Submitters asked the FMA to provide a clearer position on the rules for voluntary transfer of members to another scheme and liquidity risk management.

Changes to guidance

- We have made changes to note that the KiwiSaver Act 2006, s 56(4) permits scheme providers handling a voluntary transfer request from a member to agree a timeframe longer than 10 working days, which may be appropriate for situations such as scheme-specific liquidity events.

Using the guide

There were a range of submissions about the perceived burden of using and applying the proposed guide, which we have considered and endeavoured to address.

Not a 'one-size fits all' guide

Submissions

- Some submitters raised views about the cost and regulatory burden to implement the guide. Submissions noted it is important the guide clearly allows Managers to tailor their approach to their specific fund(s) to help ensure their LRM framework is fit for purpose.

Changes to guidance

- We do not expect the guide to be 'implemented' by Managers – its purpose is to assist Managers and Supervisors to understand how we see LRM in light of their statutory duties, and to consider at their discretion what (if any) changes to their fund LRM practices should be made.
- The essence of the guide is that Managers must use their discretion and judgement in designing, operating and reviewing LRM for the specific fund(s) they manage. We have made several changes to help ensure the guide reflects this intent and is not seen as 'prescribing' matters (such as frequency of stress testing – see below).

Stress testing and specific LMTs

Submissions

- Some submitters expressed views about the proposed guide's comments on the use and frequency of stress testing. Submitters noted that hard testing frequencies were not a necessary or cost-effective tool to manage liquidity risk for a range of funds.

Changes to guidance

- We have removed references to a particular frequency for stress testing, to preserve Managers' discretion to determine what (if any) stress testing is appropriate for a particular fund.

Updating governing documents

Submissions

- Some submitters noted that governing documents may need to be updated to ensure the fund has access to appropriate LMTs, such as the need to suspend redemptions.

Changes to guidance

- We encourage Managers to consider what LMTs they believe are appropriate for the funds they offer, and work with the fund Supervisor to amend governing documents as necessary.

Appendix: Submissions received

- Bloomberg LP
- Boutique Investment Group
- Corporate Trustees Association
- Dentons Kensington Swan
- Financial Services Council
- Fisher Funds Management Limited
- Forsyth Barr Limited
- Milford Funds
- Mosaic Financial Services Infrastructure
- NZX Limited
- Pathfinder Asset Management
- Securities Industry Association

Bloomberg L.P. [redacted] [redacted]

Bloomberg

Submitted by email

Financial Markets Authority
Te Mana Tātai Hokohoko
consultation@fma.govt.nz

Re: Bloomberg feedback to "Proposed liquidity risk management guidance"

22 November 2023

Dear Sir/Madam,

Bloomberg appreciates the opportunity to provide feedback to the Financial Markets Authority ("**FMA**") consultation on "Proposed liquidity risk management guidance" ("**Consultation**").

Bloomberg supports hundreds of asset managers globally to manage and monitor liquidity risk using Bloomberg's Liquidity Assessment solution (LQA). The award-winning solution utilizes Bloomberg's robust financial data sets to provide data-driven quantitative evaluation of market liquidity across multiple asset classes.

LQA facilitates regulatory compliance and enhances risk management and investment processes allowing clients to:

- Estimate liquidation cost and horizon for assets under current market conditions, and stress scenarios;
- Assess daily changes in liquidity based on changing market conditions;
- Compare liquidity analytics across asset classes and global coverage using consistent output; and
- Customize model parameters to create firm-specific views, scenario analysis, and stress tests.

From our ongoing market engagements, we understand that market participants welcome the FMA's leadership in incorporating international regulatory initiatives into the liquidity risk management ("**LRM**") guidance. The guidance well-aligns to emerging best practices and industry trends, while encouraging global regulatory consistency.

We would be happy to elaborate further on any of the points raised in the paper, as well as share our global experience in working together with policymakers and regulators on a data-led approach in addressing liquidity risk management.

Please find below our responses to the Consultation questions.

In the meantime, if there is any way in which I or Bloomberg can be of assistance going forward, please do not hesitate to get in touch.

Your sincerely,

[redacted]

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line.

Date: 22 November 2023 Number of pages: 2

Name of submitter: [redacted]

Company or entity: Bloomberg LP

Organisation type: information and technology

Contact name (if different): [redacted]

Contact email and phone: [redacted]

Question number	
5. Are there any emerging best practices or ongoing trends in the industry that should be considered?	The FMA's proposed guidelines for LRM are well-aligned to emerging best practices and industry trends. We have seen a significant increase in focus on liquidity stress testing driven by the recent events that caused significant market volatility (e.g., COVID-19, the Ukraine War and the SVB/Credit Suisse bank runs), and regulatory guidelines in other regions (e.g., the European Securities and Markets Authority Guidelines on Liquidity Stress Testing in UCITS and AIFs). While a robust stress testing framework does require some initial investment, we have observed that firms have embraced these capabilities as essential for proactively managing liquidity in their products and that firms find it especially useful to satisfy growing demand from their investors for reporting on a funds' resilience to potential market shocks. In addition, we see a growing trend of firms incorporating liquidity analysis throughout their product lifecycle, rather than solely for post-trade reporting. Portfolio managers are increasingly incorporating liquidity metrics into their analysis during the security selection, portfolio construction and re-allocation processes to proactively prevent liquidity threshold breaches. Firms have reduced risks and operational overhead by implementing a consistent liquidity risk framework across their front, middle and back-offices.
7. Do you have any views in particular about:	**a. the approach to defining illiquid assets** We believe that the FMA's Liquidity Risk Management guidance should specify a definition of 'illiquid assets' to reduce operational overhead for scheme ("**MIS**") managers and provide consistency to investors. If each MIS manager is responsible for their own definition of 'illiquid assets', they may not be able to leverage standard vendor solutions as-is and, therefore, they will need to invest time and resources into implementing custom reporting logic for their own custom definitions. Vendor solutions, like Bloomberg LQA, provide ready-to-use classifications aligned to specific regulatory requirements globally (e.g., the U.S. Securities and Exchange Commission's Rule 22e-4, the Alternative Investment Fund Managers Directive and rules introduced by the Hong Kong Securities and Futures Commission and the Japan Financial Services Agency) in addition to detailed liquidity analytics to simplify firms' reporting workflows so they can focus their efforts on risk monitoring and management.

	In addition, investors will be unable to accurately compare the liquidity profile of funds that use different definitions of 'illiquid assets'. For example, if one MIS manager defines 'illiquid assets' as positions that take longer than 1-week to liquidate and another manager only considers assets that take longer than 1-month to liquidate, an external investor with reports from both managers will not be able to compare the results or may mistakenly assume they are comparable. The lack of a standard definition will also make it easier for an MIS manager to conceal illiquid assets, as seen in a recent case in the United States where the Securities and Exchange Commission fined the manager for intentionally misclassifying an illiquid asset: https://www.sec.gov/news/press-release/2023-90 To provide flexibility to MIS managers, we would recommend that each MIS manager utilizes a standard definition of 'illiquid assets', but defines their own limits for the maximum weight that can be allocated to 'illiquid assets' based on their own risk tolerance and strategy.

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 15 November

Name of submitter: Boutique Investment Group (BIG)

Company or entity: Boutique Investment Group (BIG)

Organisation type: Industry Group (comprising of most non bank fund managers)

Contact name (if different): [redacted]

Contact email and phone: [redacted]

Topic	Response
Overarching thoughts about compliance	The majority of the members of BIG are medium sized businesses with limited compliance resources. Therefore we need to ensure that the resources we do have to spend on compliance are spent in accordance with priority: • Our first priority must be to meet our black letter legal obligations because these are what Parliament has directly instructed us to prioritise and penalties apply if we do not meet these. It is worth noting that at the current moment many of us will be diverting a lot of our resources into preparing for climate change. • Our second priority should be to address the current burning issues in our businesses and products. These will vary from business to business. For example, if a fund manager has found a process vulnerability that is impacting customers, that would rightly be addressed before trying to achieve best practice on some new piece of guidance. For all fund managers, it is important that we are not so overwhelmed by keeping up with the next piece of guidance that we lose capacity to identify and take remedial actions when things go wrong or to take steps in relation to whatever the real issue is within our business, whether it is a legal risk or non legal risk; • Our third priority must be to retain capacity to scan for emergent risks that could be very significant. For example the implications of AI or shifting social expectations. Many of us are struggling to get to this important aspect of compliance due to our current regulatory workload. • Achieving "best practice" or meeting "expectations" that go beyond the law and that do not address the highest risk issues within our businesses, should come after the priorities referred to above. The reality is that most of us will not have capacity to meet a lot of the content of "expectations" based guidance if we are correctly meeting priorities one, two and three. Applying this thinking to the draft liquidity guidance, most of the ideas in the guidance are not things we disagree with per se, but on the other hand having all fund mangers commit to say developing all singing , all dancing, comprehensive frameworks and undertaking significant stress testing would be overkill for many kinds of fund and a misallocation of resource, relative to other things that can go wrong and that are more pressing in the here and now. This is especially the case where we have been subject to ongoing regulatory change with statutory deadlines. Our general approach to this guidance would be that we would like to apply a small number of steps that would take away the bulk of the liquidity risk and only go a lot further if liquidity risk was a particularly prominent feature of an offer.

	The other thing that many of us would seek to do is to incorporate liquidity risk management into our single overarching risk management and CAP frameworks, rather than introducing separate frameworks. As important as liquidity management is, it would not trump cyber risk or valuation risk or key operational processes, for example. Therefore why should it stand apart?
Overarching thoughts about liquidity risk	Liquidity risk is a subset of risk. The general approach to liquidity risk should be the same as every other risk: • Take reasonable steps to form a view as to how significant an issue it is relative to other risks; then • Right size/ mitigate the level of liquidity risk to the level that makes sense for the product; and • Disclose something about the residual risk to customers if; the level of risk remains high relative to other risks, or if there may be a misalignment between the liquidity that a customer would naturally expect for that product, and the actual liquidity of the product. The key points that we are making are that: • That the level of prominence that liquidity risk should receive should be governed by its priority relative to other risks; and • Customer expectation is a key question that should underpin our risk assessment and risk response. For example, if investors go into an illiquid property syndicate, and everyone knows that the investment is illiquid then liquidity is not a problem. However, if investors go into a fund that they reasonably expect to be instantly available on call, but there may be a few days delay before a redemption can be processed, then that is a matter that needs some form of extra disclosure or practical resolution. The one size fits all, extensive body of work envisaged by the guidance involving supervisors checking things all the time is excessive. We believe that liquidity risk management should be incorporated into the generic CAP of a business, rather than being stand alone.
Liquidity Risks and disclosure	As the, FMA will be aware, the PDS for a MIS is intentionally space constrained to 6,000 words or 12 pages. Nearly every MIS manager will be at, or close to the word count. Therefore it is unlikely as to whether anything significant can be added about liquidity without taking something out. It should also be noted that most fund managers will currently not be including much commentary about quite important topics for want of space. For example, there is often little chance to discuss approach to ESG or climate change, or what the philosophy of a fund is, or a detailed biography of the people running a fund. Therefore before we can commit to putting more information in about liquidity, it should shown that its importance displaces that which is already in there and or other topics in the queue. In addition, the PDS has a specific risk section and there are well established principles as to which risks should be disclosed and in what circumstances. These would apply to liquidity risk as a sub set of risk. In essence the position that is well established is that a risk should be disclosed, if it is a very significant feature of the offer or if there is something specific to the particular offer about how the liquidity risk might play out that is unexpected or different from other fund managers. This is a question of fact that will vary from fund manager to fund manager. Further, a lot of the discussion about liquidity may be quite abstract to an investor , for example explaining swing pricing might take up a lot of space to adequately explain to a lay investor, which we do not have. Where there should be disclosure is if there are circumstances in which a customer’s normal expectation about the level of liquidity in a fund is at odds with actual liquidity. Finally, when it comes to additional disclosure during times of volatility, it is worth bearing in mind that the FMA has developed message boards that fund managers should use that are intended to reduce the risks of panic switching,

	we need to be cautious that additional disclosure about liquidity does not cut against those objectives. For example, domestically, equity market liquidity has been 30-40% off historic norms over the past year or so. This has been at a time when most managers are seeing elevated redemptions due to markets and living costs. Yet, unless the FMA have seen something we have not, there has not been even a hint of an issue with meeting funding requirements. This would evidence that we are already fulfilling our fiduciary responsibilities through prudent portfolio management. This also goes to the point in 5.5 about customer communications, if we had universally notified investors that liquidity was low, we suspect this would have generated an unintended liquidity spiral on some funds.
Most valuable thing we can get from FMA guidance and the importance of creating a feedback loop.	The most useful thing that the FMA can do when drafting guidance is to clearly articulate the problem or mischief that it has observed and is seeking to address in a very specific way. This would then enable us to assess whether the problem is relevant to our situation and to how to prioritise it. While this may theoretically reduce the shelf life of guidance, in reality there are not many pieces of guidance that do not become stale or become superseded anyway. Connected to the point above, part of the hesitation on our side is that our funds have managed well during periods of recent volatility, and in very low domestic trading, in terms of being able to remain liquid. In some ways if large fund managers could be accused of anything, it is that they are too risk averse in some cases in terms of willingness to invest in venture capital or small cap stocks. Therefore a statement of problem is particularly important.
1.1	There is a concept of liability projection, which would be appropriate for banking, but is nearly impossible to predict for open ended funds. There are so many variables for why an adviser, or investor group would make an asset allocation change, that it is not something we can predict. We can model past patterns but we doubt the value of that exercise. Certainly, the one size fits all approach is not correct and managers should have scope to determine the most appropriate inputs
The FMA should take into account that the International Organization of Securities Commissions (IOSCO) and the Financial Stability Board (FSB) does not necessarily see the world through the lens of smaller jurisdictions	It is clear that findings by IOSCO have been influential in shaping the FMA's guidance, as they are referenced. However, it should be noted that IOSCO's views are led by jurisdictions that are many times larger and more sophisticated than ours. Therefore their views may not entirely be appropriate for our jurisdiction. For example, the EU is a market of over 440 million people and the US is a market of over 300 million people. The funds on the radar of regulators in those jurisdictions include those operated by the likes of Blackrock and Vanguard, or UCITS funds with many billions of dollars of assets. Consequently, when IOSCO thinks about liquidity risks and funds, and what steps that should be taken, its universe includes funds that would shake the world if there were liquidity issues, funds that actually have the buying power to buy up enough Amazon or Microsoft shares that they have to be careful not to go too far with their buying, and funds that have sufficient scale to absorb almost any regulatory burden thrown at them. An international organisation coming from that starting point may not fully appreciate the practical constraints of medium sized businesses operating in a small market, or the fact that it would be very hard for any New Zealand fund to hold so much of widely traded international stocks for there to be any material probability of liquidity risks arising.
Capability of risk teams	Following on from the point above, it may be international best practice to have for there to be a risk management team with the capability to take full responsibility for stress testing independently from investment teams, and perhaps in banks and internationally owned MIS managers this is possible.

	However, in New Zealand, as well as mid sized MIS Managers being resource constrained in terms of numbers of staff, compliance and risk teams will be comprised of generalists who will likely lack the training and experience to lead stress testing. We believe that as a matter of pragmatism, investment teams will need to take the lead on liquidity risk management, including stress testing. Although having investment teams lead stress testing activities may not be best practice this is compensated for by the fact that our funds will tend to be less complex than overseas equivalence and lack the sheer scale of overseas funds.
Background > Previous developments > bullet 3 ***"public disclosure of liquidity risk be improved"***	Quote from Recommendations for Liquidity Risk Management (IOSCO) Feb 2018 *"IOSCO wishes to remind entities that good communication in liquidity issues with their respective regulators is essential."* Don't agree with the statement within the guidance (left column) as none of the IOSCO recommendations state this. Would like this amended to reflect actual IOSCO intent to communicate with regulators, not the general public, which may be spooked by the message.
Background > Previous developments >para 2 ***"regulators devote closer attention to the liquidity stress testing practices of open-ended collective investment schemes"*** ***Background> Previous developments>para 5*** ***"In July 2023, FSB and IOSCO subsequently consulted on revised guidance, with the goal of significantly strengthening liquidity management by open-ended managers"***	To ensure FMA recommendations are fit-for-purpose, distinction should be made between schemes where funds can withdrawn at any time (open-ended, redeem anytime) and schemes where redemption is restricted e.g. retirement schemes (open-ended, redeem restricted), based on relative liquidity risk. IOSCO and FSB recommendation can/should apply to open-ended, redeem anytime schemes and a risk-based approach regarding recommendations applied to open-ended, redeem restricted schemes. Taking recommendations that are focused on open-ended fund managers (global) and blanket-adopting these to MIS Managers (NZ) is both an over-reach, possibly irrelevant, and creates a cost of compliance burden that does not result in improved liquidity risk management practices for open-ended, redeem restricted MIS Managers.
FMA Our expectations > Key areas for improvement ***"Key improvements we would like to see are:*** • ***Better frameworks, policies and procedures covering LRM.*** • ***More regular stress testing.*** • ***More tailored LMTs made available for use.***	As is detailed (above), these should primarily apply to open-ended, redeem anytime schemes. Some fund managers with a single fund may not require LRM framework standalone from their overall risk management framework. These recommendations should be scaled down for open-ended, redeem restricted schemes which should only need to document these relative to the open-ended portion of their scheme e.g. customers aged > 65 years old, with stress testing covering that portion along with a scheme event that causes customers to transfer out, with LMT's covering those scenarios.
Key features of effective LRM	As is detailed (above) a stipulation should be included noting these key features apply to all open-ended, redeem anytime schemes. Open-ended, redeem restricted schemes should consider each of the features and determine which apply to them.
Feature 5 – Disclosure and communication ***5.1 The MIS Manager will ensure investors are aware of the fund's liquidity risk through effective disclosure, including ongoing disclosure about:*** • ***market movements that are relevant to the fund's holding and liquidity***	Earnings day (material change in asset prices) would meet definition of market movement but seems irrelevant to provide disclosure regarding. What is the expectation regarding ongoing disclosure? e.g.an email to investors following significant market change; if so need to be mindful of any impact message might have re. panic selling.
Feature 5 – Disclosure and communication ***5.5 Communication with investors, the Supervisor and other stakeholders will be more frequent and more detailed in times of fund-specific or market-wide stress.***	Also, IOSCO Recommendation 15 notes *"Where an additional measure is applied (e.g. side pocketing), existing and potential investors must be informed in an appropriate manner, and kept informed over time (e.g. material on the website)".* The implication of increased liquidity risk communication with investors during fund-specific or market-wide stress events may be counter-productive i.e. providing more communication may have the unintended consequence of "fueling the fire" and lead investors to take actions that are not in their best

	interest e.g. advising investors to “hold the course” and not divest turning a market downturn could inadvertently lead them to take that action.
Feature 6 – Monitoring framework ***6.3 Expect MIS managers will define the term “illiquid assets”, having regard to the fund(s) asset composition***	Much of the NZX is traded infrequently; meaning it meets an illiquid asset definition. Different modelling requirement between portfolio invested in NZX vs global equities.
Feature 7 – Liquidity management tools ***7.1 MIS managers will explicitly define the LMT’s they have available for use, assess conditions under which they will be deployed (and withdrawn), and consider how their use ensures equitable treatment of scheme participants***	Note comments above about disclosure for disclosure of tools. We support managers amending governing documents to provide for tools. There are some calls for standardised terms in deeds.
Feature 8 – Stress testing ***8.8 Stress tests will be carried out on normal, and extreme (but plausible) scenarios, and clearly identify sources of relevant risks impacting fund liquidity***	More detail about what “extreme (but plausible) scenarios” covers? Portfolio dependent e.g. heavy investment in global equities less of a concern vs concentrated investment in illiquid assets.
Definitions	*There is discussion of illiquid, versus less liquid, versus liquid assets. If the intent is to create defined lines as to what approach should be taken with different asset mixes then these terms need to be defined. If the intent is less prescriptive then this may not matter so much.*
Role of supervisors	*The FMA should not direct supervisors to undertake streams of work that it would not be prepared to undertake itself if it were an appropriately resourced regulator with a sole mandate.*
Outsource managers	*For international equities, most managers will be reliant on off shore managers.* *In many instances those off shore managers will have the upside of being large well resourced entities that are managing liquidity in accordance with prescriptive requirements of their jurisdiction. However, it is equally true that a large UCITS fund for example would be likely to refuse to provide any kind of bespoke reporting to a New Zealand manager.* *Therefore liquidity management for off shore funds ay really be a matter of upfront due diligence on the manager or regime. This may not be a problem if the assets within the fund are highly liquid.*
Risk, including liquidity risk, is not always a bad thing in products	*Finally, it is worth remembering that the role of the MIS manager is actually to take appropriate risks where there is commensurate possibility of reward, not to eliminate risks.* *The tone and emphasis of liquidity guidance, has the potential to tip choices as to whether a fund manager is willing to branch out into activities like considering funding direct investments, venture capital investments, small cap stocks and impact investments, or whether to play it safe and go more vanilla in the face of heightened regulatory risk. It is therefore important that the regulator is really careful to get the trade off balance right so that the cumulative effect of guidance, or outcomes based regulation (including this guidance) does not promote the culture of an overly risk averse sector to the detriment of consumers and efficient and innovative markets.* *The context of our comment is that there is a clearly observable trend in our market of: consolidation through acquisitions, many of the larger providers are choosing to become more vanilla and passive, and we are suddenly seeing much more entry by the likes of Blackrock and Vanguard. To the extent this is direction of the market is being driven by markets and consumer choice, the outcome is not wrong. However, there is the possibility that the regulator is nudging the market in this direction through rewarding certain styles of investment through creating more “please explain” outcomes if you are choosing to stand apart from the generic. Possibly what we are seeing with the*

	likes of value for money and "outcomes focused regulation" is an increasing incentive to avoid taking risks to avoid a bad outcome, rather than encouragement to take appropriate risks.

Feedback summary – *if you wish to highlight anything in particular*

Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.

Thank you for your feedback – we appreciate your time and input.

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 17 Nov 23	Number of pages:	This page, plus 4 pages attached
Name of submitter:	[redacted]	
Company or entity:	Corporate Trustees Association	
Organisation type:	Industry association	
Contact name (if different):		
Contact email and phone:	[redacted]	

Question number	**Response**
Please see attached	

Feedback summary – *if you wish to highlight anything in particular*

Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.

Thank you for your feedback – we appreciate your time and input.

FMA Consultation: Proposed liquidity risk management guidance

Feedback from the Corporate Trustees Association

1. Do you think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management? If you think it can be clarified or improved, what changes or updates do you suggest we consider? Please give reasons for your view.

The guidance:

- should address how stress testing could be done, which would align with proposed FSB policy recommendation 6, so as to promote NZ market consistency
- should not refer to "scenario testing" which risks conflating the different concept of "scenario analysis" with "stress testing"
- should formally adopt the "bucketing" definitions of liquid, illiquid or less liquid (or equivalent) to promote NZ market consistency. That would then align FMA with the commentary supporting FSB policy recommendation 3 that envisages each jurisdiction determining "an overall approach to defining assets as liquid, illiquid or less liquid (or comparable categories)". Managers should be responsible for determining which category (or hybrid of categories) applies to each of their funds, but not for defining the "buckets" themselves.
- should avoid the passive voice ("will be", eg last sentence of 6.5), and rather use language like: "the manager must/should/may …" so that there is clarity as to who is responsible.

The Scope of the guidance states "While managed funds are the primary focus of this guidance, some aspects may also be relevant for other MIS (such as property syndicates that invest in a single asset class)." It is not clear which aspects are relevant for other MIS. Other MIS schemes such as property syndicates and forestry schemes, tend to have a single asset class (often only one asset), are closed, and have few (if any) redemption rights. It would be helpful if the guidance could annotate the guidance to identify the aspects relevant to other MIS. The annotation could be similar to the XRB's approach in accounting standards whereby requirements specific to other MIS are denoted with an asterisk (*). If there are very few aspects that are applicable CTA suggests that other MIS is removed from the scope.

2. Do you believe there are any features that go too far or are too prescriptive for MIS managers or Supervisors? If so, please explain what should be changed or scaled back, and why.

-

3. Conversely, do you believe there are features that could go further, be more specific, or otherwise be clarified? If so, please explain your suggested changes and the reasons for these.

Stress testing is a broad topic and everyone will look at it differently. The statement in 8.1 (on page 14 of the consultation document) is also very broad. We think there should be greater guidance around this area.

The purpose of the stress test should be clearly articulated so the outcome of the stress test is clear. The key purpose is to determine in what circumstances redemptions would not be able to be paid. What is the outcome that the FMA wants to see? Some Managers may infer that a global equities fund (say) needs to hold a higher level of cash rather than just a well-diversified portfolio of global equity securities. This could dilute returns to investors and may not be in their best interests.

In support of our suggestion that FMA provides more detailed guidance on stress testing, we note that proposed FSB policy recommendation 6 states that: “Authorities should require and/or provide guidance on stress testing at the level of individual open-ended funds to support liquidity risk management to mitigate financial stability risk. The requirements and/or guidance should address the need for stress testing and how it could be done.”

However, the guidance should make it clear that the Manager should adopt a risk-based approach when determining the extent of stress testing. Some funds will have a higher liquidity risk than others, so the approach does not need to be one size fits all.

4. What additional features, if any, do you want to see in this guidance?

The guidance could more directly acknowledge the potential trade-off between liquidity and performance. The fund may be designed to not provide liquidity at all times, which is acceptable provided the risk is fully explained. The Guidance may conclude that this would not be acceptable for KiwiSaver funds due to the consequences set out in paragraph 7b. (That may change if the law is amended to allow a person to be a member of more than one scheme.) If that approach were not the case then Managers may need to hold greater levels of cash, contrary to the interests of investors (as it would likely be at the cost of return).

While we support the proposed Governance and Oversight points within Feature 8 (stress testing), it would assist if the Guidance noted that Stress testing results should be included in the MIS Managers CAP Programme. They should be periodically tested to ensure appropriate stress testing is being undertaken, as required by the Manager’s Liquidity Risk Management Framework.

5. Are there any emerging best practices or ongoing trends in the industry that should be considered?

-

6. Do you expect there will be any material challenges or unnecessary compliance costs to your business as a result of meeting the expectations in the proposed guidance? Please give reasons for your view.

Not a "one size fits all" approach: To impose the same LRM framework on all funds would impose huge compliance costs and be resource intensive for MIS Managers and Supervisors. The guidance should emphasise that the framework will differ depending on the attributes of each fund (such as size, complexity, nature of assets, liquidity).

Fund-of-Fund Managers: The majority of NZ Managers do not manage their international equities or fixed interest exposures in house. Generally these investments are made into offshore underlying managers funds that hold listed securities or high quality credit instruments. These offshore managers' are also generally reputable / large and operate in highly regulated / highly developed jurisdictions.

Any attempt from a NZ MIS Manager to instruct a large overseas manager about liquidity would be relatively challenging. This leaves NZ MIS Manager's, practically, only able to (a) undertake appropriate diligence on portfolios prior to (and during) investing (something which should occur as a matter of course for investment management processes anyway); and (b) to receive liquidity reports that are generally prepared / provided by such underlying managers.

In assessing the liquidity profile of their own funds it therefore needs to be sufficient, from a compliance perspective, for NZ MIS Managers to be able to rely on liquidity profile material provided by underlying managers with respect to the underlying managers fund's investments – without further / deeper assessment being required (unless there is a material basis to doubt the reasonableness of the material received and thereby make further investigation appropriate).

7. Do you have any views in particular about:

a. the approach to defining illiquid assets

As envisaged in the commentary supporting FSB policy recommendation 3, the FMA should provide guidance on the definition of illiquid assets so that investors are not confused when this term is referred to by Managers and to ensure consistency across products. We also note that liquidity reporting is included in the Quarterly Fund Update. To avoid investor confusion those liquidity definitions need to be aligned.

b. the comments on the role of Supervisors

Supervisors take a risk-based approach, tailoring frequency, scope, intensity, etc to the circumstances of particular managers. This is not reflected in the guidance, which at page 6 states that supervisors will "frequently review" a MIS manager's liquidity-related monitoring activities. Perhaps preferable wording would be "regularly review using a risk-based approach, including [the points in the next paragraph in the guidance]".

That expectation could also be noted under Feature 11 – Evaluation and Review.

c. the ability of MIS KiwiSaver Managers to be able to suspend redemptions?

This is likely to be very difficult.

It would mean that members cannot transfer to another scheme. Members may not be aware that the redemptions of a fund have been suspended and are only likely to find out when the impacted scheme receives a transfer request from the scheme being transferred to. Thought will need to be given to including this in the scheme transfer process.

If members are seeking a financial hardship or serious illness withdrawal then it may not be able to be processed.

Where a fund's redemptions have been suspended it is not in the interests of members that the Manager continue to accept monies into the fund. Given that small contributions are being made all the time, the question is how easy it will be for Managers to stop monies going to such funds and what the Manager does with such monies, until the Manager receives an updated instruction from the member. As future preparation, Managers may need to give some thought to updating the offer document for KiwiSaver to advise that where a fund's redemptions are suspended, contributions to such a fund will be included in the Cash Fund or some other fund.

8. Do you have any other feedback or comments on the proposed guidance?

It would be useful if the FMA set out its expectations around when Managers are expected to have fully implemented their LRM process and policy. Prior to this consultation we recall that the Managers had a year after the final guidance to have fully implemented but they should have started preparations in 2022.

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10 November 2023

Submission on Consultation: Proposed liquidity risk management guidance

1 This is a submission by Dentons Kensington Swan on the Financial Markets Authority's ('**FMA**') draft *Consultation: Proposed liquidity risk management guidance* ('**Consultation Paper**') dated September 2023.

About Dentons Kensington Swan

2 Dentons Kensington Swan is one of New Zealand's premier law firms with a legal team comprising over 100 lawyers acting on government, commercial, and financial markets projects from our offices in Wellington and Auckland. We are part of Dentons, the world's largest law firm, with more than 12,000 lawyers in over 200 locations.

3 We have extensive experience advising a range of managers of managed investment schemes and supervisors that will be affected by the proposed guidance set out in the Consultation Paper.

Specific comments

4 We are broadly supportive of the guidance set out in the Consultation Paper in so far as it will assist managers and their supervisors to consider and manage liquidity risks. Providing good quality guidance on liquidity management and making the FMA's expectations clear is always useful, particularly in so far as ideas are refined over time, including off the back of relevant international developments.

5 Managers should rightly address liquidity risks and have in place useful tools to deal with matters if those risks come to fruition. However, the granular requirements of the Consultation Paper go beyond the scope necessary to simply assist and are overly prescriptive.

6 Prudent professional managers already make proper allowances for liquidity matters and should be free to determine the best approach for the various schemes they manage on a scheme by scheme basis. Below we set out some key matters that we believe require further consideration and refinement in order for the guidance to be useful and practicable.

Guidance or law?

7 A flaw of the Consultation Paper is that it seeks to use a guidance framework to create law. There are no express requirements in the Financial Markets Conduct Act 2013 ('**FMC Act**') or Financial Markets Conduct Regulations 2014 ('**FMC Regulations**') regarding liquidity risk management or related tools (although there are disclosure requirements and in particular those regarding the terms of offer for 'other MIS', i.e. those schemes which are less liquid).

8 Further, the FMA has not imposed a standard condition on managed investment scheme manager licences regarding liquidity risk matters, noting that liquidity risk is a scheme specific matter rather than a licensee level one. And, to the best of our knowledge, the FMA has to date not imposed specific conditions on individual managed investment scheme manager licences in regard to liquidity matters for particular schemes.

9 Liquidity risk is raised by the FMA at the licensing phase, whereby potential licensed managers are asked about liquidity risk in respect of various investment strategies and possible illiquidity. Approaches to divestment and the appropriate monitoring and management of liquidity risk are also covered. To this extent the FMA will be aware of specific approaches different managers take to liquidity risk management, noting that must occur at scheme level. If there were concerns at the licensing stage regarding a particular manager's approach then this could have been, or could be, addressed via the imposition of specific conditions of licence.

10 To the extent the FMA wishes to impose 'breachable' obligations on managers (and scheme supervisors) this should be done through the proper channels, being legislative reform or regulatory updates to the FMC Regulations.

11 In our view, more flexible 'best practice' guidance will suffice to ensure managers and supervisors remain cognisant of key elements that they should consider having in place to manage scheme liquidity risk, but with those managers able to adopt measures appropriate to their particular offerings and investment types. This necessitates a reframing of statements in the Consultation Paper from 'ensure', 'will ensure', 'must' and the like, to 'should' and 'should consider' to provide managers scope to apply the guidance in a manner that is appropriate to their particular schemes.

Misuse of best interests concept

12 A key concern, as with previous 'value for money' material published by the FMA, is the awkward reliance on the notion of 'best interests' contained in Part 4 of the FMC Act. There are several instances in the Consultation Paper where the FMA claims that a failure to have a liquidity risk management 'framework' would be a direct breach of section 143 of the FMC Act. We do not support this view.

13 Section 143(1) of the FMC Act provides that:

> A manager of a registered scheme must—
>
> (a) act honestly and in good faith in acting as a manager; and
>
> (b in exercising any powers or performing any duties as a manager,—
>
> (i) act in the best interests of the scheme participants; and
>
> (ii) treat the scheme participants equitably…

14 The duties imposed under section 143(1) are in respect of the manager's role in relation to the particular registered scheme and the powers and duties established primarily by the trust deed for that specific scheme. In this regard the duty is not applicable to the manager at the licensee level but rather on a scheme by scheme basis. That is an important distinction to make.

15 Section 143(1), by broadly reiterating the general law position regarding trust duties, imposes on managers a need to put member interests ahead of their own interests – if there was some conflict as between the manager's own interests, particularly commercial ones, and the interests of members, then the interests of members must prevail. Entrenchment of the duty on managers in the FMC Act also means a manager cannot 'contract out' of those duties, such as by reducing the reach of the duties via the trust deed. Further, the manager must treat members equitably and impartially, particularly where they have similar rights, and fairly where those rights may differ.

16 Failure to have 'effective' liquidity risk management is not a breach of the section 143 duties – it does not equate to a failure to prioritise member interests. In our view, framing liquidity risk management as a 'requirement' of the best interest duty is disingenuous and risks undermining the purpose of that important duty – it is a fundamental fiduciary one and not a granular procedural one.

17 References to liquidly risk management being required by the best interest duty (and the related treating participants equitably duty) should be removed from the Consultation Paper.

Irrelevant regulatory responses

18 It is particularly unhelpful for the guidance paper to set out various regulatory responses the FMA may take when, in many instances, use of such powers cannot be substantiated. As there is no express legal requirement to have, as the FMA frames it, 'effective liquidity risk management', it cannot stand that the FMA would be able to utilise its direction order powers under Part 8 of the FMC Act.

19 Similarly, there is no clear market services licensee obligation regarding liquidity risk management. The best interest duty is a high level principle and is also scheme focused rather than sitting at the licensee level. It is inappropriate to claim that censure is readily available in such circumstances.

20 A similar problem arises when assessing the use of the stop order provisions. The contention that the FMA may issue a stop order in respect of a product disclosure statement ('**PDS**') is unnecessary. A PDS is heavily prescribed in terms of content and constrained by word or page limits. Given such constraints there is limited ability for managers to detail liquidity risk management to any meaningful extent. As mentioned, liquidity is generally covered as a risk of the scheme with the key control of suspending withdrawals ordinarily mentioned. It would be unfair of the FMA to threaten the use of a stop order in circumstances where there is simply no additional available space in a PDS for managers to provide extensive disclosure on liquidity risk management.

Even more disclosure

21 Remaining on the PDS front, the FMA seems to be more frequently suggesting further material be added to these already heavily constrained documents. The integrated financial products review and follow up feedback suggested managers need to include more coverage of ESG matters in their PDS. And now the FMA suggests managers include even more detail, this time regarding various liquidity risk management features and tools. Putting aside, as mentioned, the fact the PDS generally covers off liquidity risks (and, in most cases, suspension powers) there is simply no extra room to include suggested additional material, particularly for schemes and PDS that contain multiple fund

options. And it is not clear exactly where this additional material would best sit within the current prescribed PDS structures for managed funds and other schemes.

22 The suggestion that extensive liquidity risk disclosure be included in the PDS, presumably including relevant market movements, redemption terms and processes, and underlying asset liquidity as mentioned in the Consultation Paper, is not feasible. To the extent that such disclosure is considered 'material' it would be useful for the guidance paper to expressly refer to inclusion in the other material information document as being appropriate, but only if it is actually material, i.e. likely to influence persons who commonly invest in financial products in deciding whether to acquire the financial products on offer.

Illiquid asset definition

23 The FMA suggests that managers define 'illiquid asset' although presumably this will differ on a scheme to scheme basis. Care needs to be taken not to force managers to adopt overly rigid definitions. A definition focused on strict timeframes, for example, could constrain managers from taking appropriate action because the timeframe requirement has been triggered and the particular asset is now viewed as illiquid and must be dealt with via certain avenues under the relevant trust deed.

24 There is likely some benefit in the FMA providing a base definition of 'illiquid asset' that managers can then tailor as need be. Any definition needs to be flexible enough to allow managers to readily act if opportunities arise to deal adequately with the illiquid asset or assets in question. Conversely, any definition should also not restrict managers from acquiring illiquid assets as an investment in such assets may be in the interests of investors on a pure commercial investment basis, i.e. an asset that has the potential to perform well but that is currently undervalued due to the liquidity position.

Risk based review

25 The Consultation Paper requires stress testing to be done 'at least once a year' and suggests that boards and senior management of managers should 'review and approve the entity's LRM framework at least annually'. Again, the final guidance needs to be more flexible and allow for managers to take a risk based approach to stress testing and framework review. Managers must be free to adopt different review practices and timeframes suitable for their various schemes. The imposition of yearly stress testing and liquidity risk management framework reviews add additional time and cost to managers that may be unnecessary in the context of specific schemes.

Suggested approach

26 As suggested, retaining flexibility within the guidance is paramount. Managers and their supervisors must be able to consider and apply the guidance in a manner appropriate to particular schemes. This is the role of a prudent professional manager.

27 If the FMA has specific concerns with a manager's performance then it can engage directly with that manager, in good faith, to resolve the matter without the need to reach for regulatory tools. If the concerns cannot be addressed then perhaps a specific condition would be an appropriate targeted approach, on a scheme by scheme basis, in regard to a particular manager. The imposition of an express specific condition would then allow the FMA to take action, such as requesting an action plan, if satisfactory steps were not taken by that manager to address the FMA's concerns regarding the liquidity risk management framework for a particular scheme or set of schemes.

Conclusion

28 We would welcome the opportunity to discuss any of the points we have raised regarding the Consultation Paper. Thank you for the opportunity to submit.

Yours faithfully

[redacted]

[redacted]

[redacted]

Financial Services Council NZ

Grow the financial confidence and wellbeing of New Zealanders

Friday 17 November 2023

Financial Markets Authority
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Britomart, PO Box 106 672, Auckland 1143

Level 2, 1 Grey Street
PO Box 1179
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By email: consultation@fma.govt.nz

Proposed Liquidity Risk Management Guidance

This submission on the Financial Markets Authority (FMA) consultation on Proposed Liquidity Risk Management Guidance (the Consultation Paper) is from the Financial Services Council of New Zealand Incorporated (FSC).

As the voice of the sector, the FSC is a non-profit member organisation with a vision to grow the financial confidence and wellbeing of New Zealanders. FSC members commit to delivering strong consumer outcomes from a professional and sustainable financial services sector. Our 117 members manage funds of more than $95bn and pay out claims of $2.8bn per year (life and health insurance). Members include the major insurers in life, health, disability and income insurance, fund managers, KiwiSaver, and workplace savings schemes (including restricted schemes), professional service providers, and technology providers to the financial services sector.

Our submission has been developed through consultation with FSC members and represents the views of our members and our industry. We acknowledge the time and input of our members in contributing to this submission. We thank the FMA for the provision of an extension of time to enable this response.

We welcome the opportunity to provide feedback on the proposed liquidity risk management guidance (the Proposed Guidance) for Managed Investment Scheme (MIS) managers and their supervisors for effective liquidity risk management (LRM). We do however query the background and problem or issues the Proposed Guidance is seeking to address. For example, is the rationale to align with international regulators or is there a specific New Zealand problem. If it is the latter, we encourage further engagement to collaboratively address such concerns and to ensure industry consistency as our members appear to have differing views as outlined in this submission. Please note we have removed the questions which our members have no response to at this time.

We welcome continued discussions and engagement. I can be contacted on [redacted], to discuss any element of our submission.

Yours sincerely

[redacted]

1. Do you think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management? If you think it can be clarified or improved, what changes or updates do you suggest we consider? Please give reasons for your view.

The Proposed Guidance states it is setting out the FMA's expectations for managers to demonstrate that they are meeting their legal obligations. However, we note that the definitive language used may infer that it is more prescription than expectation or guidance.

2. Do you believe there are any features that go too far or are too prescriptive for MIS managers or Supervisors? If so, please explain what should be changed or scaled back, and why.

Feature 2

We consider the expectation that an annual review be conducted of the LRM framework may be too frequent. If there are no new products or significant changes made to existing products or investment strategy, there would not be any significant impact on the framework itself. Therefore, we recommend keeping the requirement for regular review but remove the expectation of such reviews occurring annually. Rather we suggest at the appropriate frequency that suits the size and scale of each individual business.

Feature 5

We consider the level of detail expected to disclose liquidity risks in Product Disclosure Statements (PDS) would be challenging due to the high level of regulatory prescription in a PDS. We suggest that the specific reference to the PDS is removed and replaced with a reference that liquidity risk disclosure is considered material information that should be clearly disclosed to investors in the form that managers consider most appropriate, for example via the PDS, Other Material Information document or on their website.

Feature 7.3

Under the first bullet point of this feature, it is stated that "Tools such as swing pricing and buy/sell spreads should be used …". We consider this definitive language goes against the proposition that the MIS manager uses the most appropriate liquidity management tools for the particular circumstance by being prescriptive in nature. We recommend replacing "should be used" with "may be used" so each manager can select the appropriate action in the specific circumstances.

7. Do you have any views in particular about:
a. the approach to defining illiquid assets
b. the comments on the role of Supervisors
c. the ability of MIS KiwiSaver Managers to be able to suspend redemptions?

Some members consider that industry would benefit from FMA guidance in this area as defining "illiquid assets", for example, would help promote market alignment. Differing definitions may not enable investors to accurately compare the terms and conditions across different issuers. In the absence of such guidance, each provider will be required to formulate its own definition, and this may lead to inconsistent applications. If this inclusion is supported, the definition stated under the Financial Market Conduct Regulations in Regulation 5 could be used, namely, "…reasonably expect to realise the investment, at the market value of the assets, within 10 working days…") as the default, with the ability for industry participants to define their own if there are specific and relevant reasons to do so. If the participant uses a different definition for a set of assets, that definition should be considered material information to be disclosed to investors so they can understand all risks and factors involved in the underlying investment.

Other members would not support FMA guidance that defines “illiquid assets”, taking the view that it is appropriate that different MIS managers define the term in accordance with the nature of the fund, and that a single definition would be overly simplistic.

We support additional guidance from the FMA on the ability of MIS KiwiSaver Managers to suspend redemptions, as it appears that there is divergence in views within the sector, namely the application of, section 56(4) of the KiwiSaver Act. KiwiSaver providers should be able to suspend redemptions if it is in the best interests of members. If the provider has in place a robust LRM framework, then a suspension would be the action of last resort and reflect that the market is unable to be reliably valued.

8. Do you have any other feedback or comments on the proposed guidance?

Some members consider stress testing to be most effective, if the FMA should publish a standard scenario for MIS managers which is potentially reviewed and updated every two years. A standardised scenario may ensures more consistency across the industry and is similar in approach to how international regulators use standard scenarios for financial institutions.

Other members would not support the FMA publishing a standard scenario for use by the sector and consider this may increase systemic risk across the industry. Furthermore, it may be perceived as Managers opting out of broader responsibility for identifying and managing entity specific risk.

There appears to be an overarching expectation that providers could change or introduce new liquidity management tools with ease (and the related disclosures) which we consider is not always the case. Providers are bound by what is allowable under the scheme’s specific Trust Deed and introducing new liquidity management tools is not an easy or straightforward process requiring the approval of the Supervisor, if not the investors in the scheme (depending on materiality of what is being introduced).

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 9 November 2023 Number of pages: 2

Name of submitter: [redacted]

Company or entity: Fisher Funds Management Limited

Organisation type: MIS Manager

Contact name (if different):

Contact email and phone: [redacted]

Question number	Response
1. Do you think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management? If you think it can be clarified or improved, what changes or updates do you suggest we consider? Please give reasons for your view.	Agree
2. Do you believe there are any features that go too far or are too prescriptive for MIS managers or Supervisors? If so, please explain what should be changed or scaled back, and why.	No
3. Conversely, do you believe there are features that could go further, be more specific, or otherwise be clarified? If so, please explain your suggested changes and the reasons for these.	In respect of Feature 7 – Liquidity Management Tools, Fisher Funds agrees with the suggested tools to manage liquidity events when they occur. We believe that inclusion in the guidance of examples or scenarios where the FMA believed certain tools would be used would be helpful. MIS managers could in certain cases be reluctant to implement liquidity management tools due to the potential for reputational damage. Suspension of redemptions can be particularly damaging to a manager's reputation regardless of how unavoidable the suspension was or how well the tool is implemented (notwithstanding an event such as 9/11 where the entire industry was impacted). We believe that by including examples of when the tools should be implemented managers are more likely to implement in a timely and consistent manner. Managers can and will form different views on when tools should be implemented on a case-by-case basis, however having a base to form that view from would be helpful.
4. What additional features, if any, do you want to see in this guidance?	None

5. Are there any emerging best practices or ongoing trends in the industry that should be considered?	No
6. Do you expect there will be any material challenges or unnecessary compliance costs to your business as a result of meeting the expectations in the proposed guidance? Please give reasons for your view.	Fisher Funds undertook significant work post the publication of the recommendations in respect of MIS LRM practices in 2021 to improve our LRM tools and processes. There were significant one-off costs involved in making these improvements e.g. legal in terms of Governing Document and offer document updates, and system development to enable better monitoring and to facilitate the use of the new tools. Less significant, though not immaterial, are the ongoing costs involved in implementing improved reporting and monitoring processes to manage liquidity within the funds. It is noted that the tools and processes implemented at Fisher Funds will be used and/or implemented in the recently acquired Kiwi Wealth business where they are not already present as integration is completed. There will be costs involved in adding some of the LRM tools and processes to the Kiwi Wealth products, however these are not considered to be material.
7. Do you have any views in particular about: a. the approach to defining illiquid assets b. the comments on the role of Supervisors c. the ability of MIS KiwiSaver Managers to be able to suspend redemptions?	The closest that the guidance comes to defining what is a liquid asset is in the reference to the definition of a managed fund in regulation 5. That regulation refers to the fund investing at least 80% of its assets in 1 or more of the following ways: *(A) in debt securities issued by a specified bank or NBDT where the money invested is available for withdrawal immediately on request during the specified bank's or NBDT's normal business hours or at the end of a fixed-term period that does not exceed 3 months:* *(B) in managed investment products that are redeemable on request, or within a period not exceeding 10 working days, on a basis calculated wholly or mainly on the value of the scheme property of the scheme to which those products relate:* *(C) in assets where the manager can reasonably expect to realise the investment, at the market value of the assets, within 10 working days* Fisher Funds believes that a definition of what the FMA considers to be liquid, which would vary by the different types of assets, should be included in the guidance. Definitions would be useful in ensuring that managers create monitoring processes and implement liquidity management tools with a measure of consistency. Managers may have differing views and could use alternative definitions as they consider appropriate, however the guidance could give examples as a starting point. We note that funds must disclose an asset liquidity ratio on the Disclose Register. Definitions of liquid for asset classes in the guidance would also help to ensure a consistent approach could be used to determine those ratios.
8. Do you have any other feedback or comments on the proposed guidance?	See below.

Feedback summary

Fisher Funds is supportive of the proposed guidance. While each manager will take their own approach to manage liquidity risk as appropriate to their business, the issuance of guidance will bring some consistency of approach across the industry. It is to this end that we suggest that the FMA provides a more detailed definition of illiquid assets and provides examples in the guidance of where the regulator would expect the various types of liquidity tools to be used.

Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.

Thank you for your feedback – we appreciate your time and input.

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 10 November 2023 Number of pages: 4

Name of submitter: [redacted]

Company or entity: Forsyth Barr Limited

Organisation type: MIS Manager

Contact name (if different):

Contact email and phone: [redacted]

Question number	Response
1	We support the FMA's description of the proposed guidance as a 'best practice' guide for MIS Managers with respect to the FMA's expectations around liquidity risk management. There are however, a couple of contradictory statements in relation to the guidance that we consider ought to be clarified before the guidance is finalised. For example, in the first paragraph "About this consultation", the FMA notes that "the proposed guidance outlines the essential features for effective liquidity risk management that the… FMA…**expects all managed fund to have**" (emphasis added). Whereas on page 2 (second paragraph) the FMA notes that "The guidance is not intended to prescribe how MIS managers… demonstrate they are meeting their legal obligations for LRM. Rather it sets out the features that we **expect MIS managers to consider** when designing and operating LRM for their MIS" (emphasis added). The identified text raises two issues: 1. The first is a distinction between an expectation to "have" and an expectation to "consider". The former suggests an intention by the FMA that MIS Managers **must** incorporate all 11 features in their LRM processes whereas the latter suggests that those principles ought to be considered by MIS Managers but are not mandatory (which obviously sits better within 'best practice' guidance). We suggest the FMA's expectations in this regard are clarified and, if necessary, the legal basis for imposing the principles as mandatory requirements is explained. *2.* The second is to point out that there is no legal obligation to have and oversee effective liquidity risk management (refer page 2 of the proposed guidance which states that "effective LRM is a legal obligation of MIS managers"). Instead the legal obligation(s) of a MIS manager are those that are expressly imposed on MIS Managers by the Financial Markets Conduct Act 2013 (**FMC Act**) and Financial Markets Conduct Regulations 2014 (**FMC Regulations**). These obligations include the duty to act in the best interests of scheme participants; and to treat those scheme participants equitably (refer s143(b)(i) and (ii) of the FMC Act) as well as the duty to exercise care, diligence and skill when exercising any powers, or performing any duties as MIS Manager (refer s144 of the FMC Act). Of course we appreciate that having an effective LRM process in place helps to

	demonstrate compliance with those obligations but it's important to point out that having effective LRM is not, in and of itself, a legal obligation.
2	***Nature of Guidance*** As per the above comments, the draft guidance purports to impose obligations, as opposed to merely providing guidance as to the FMA's expectations about how LRM relates to the performance of more general obligations. To the extent the guidance purports to impose obligations, it goes too far. The law has clear mechanisms for imposing obligations, and guidance is not one of those. Using guidance in this manner causes confusion, particularly as regards the enforceability of perceived non-compliance. This adds to uncertainty and costs for MIS managers and Supervisors. ***Ongoing disclosure (Paragraph 5.1)*** It's not clear what "ongoing disclosure" the FMA is referring to in paragraph 5.1 of the proposed guidance. There is already an extensive disclosure regime prescribed by the FMC Act and FMC Regulations. In respect of any ongoing disclosure regarding market movements and the impact on fund liquidity, we expect that this would be based around events rather than periodic timeframes. We also note that this type of disclosure is not a strict statutory obligation, instead it's more about looking at the purposes of the FMC Act and trying to achieve good customer outcomes (e.g. informing investors about what is happening in the market and their investment(s) so that they may make confident and informed decisions). In this regard we note that it is not the role of the MIS Manager to advise investors what to do in times of market stress. Instead, any disclosure would be limited to notifying investors of the use of a liquidity management tool (**LMT**) and what impact, if any, that has on their ability to enter and exit the fund. By limiting disclosure to specific liquidity events, this will give a greater focus for investors at relevant times. Event based disclosure will help ensure that the message is relevant and effective. In contrast, ongoing disclosure may dull the liquidity messages when they matter most. ***Disclosure in the PDS (Paragraph 5.2)*** We support effective disclosure to investors of liquidity risks, LRM processes and LMTs that are (or will be in place) for each fund. However, we believe that the MIS Manager is best placed to determine how and where that disclosure ought to be made to investors. The Product Disclosure Statement (**PDS**) is already subject to strict content and length restrictions and requiring additional disclosures around liquidity risks, LRM processes and LMTs (particularly where those tools are, in the ordinary course of business, unlikely to be implemented otherwise than in extreme circumstances) will add to the length and complexity of that document. Instead we believe that effective disclosure to investors can be achieved by disclosing in the PDS (as is current practice) both the liquidity risks associated with a fund(s) and what LMTs are in place to manage those risks (including high impact tools like suspension). If there is further information that ought to be disclosed to investors (like how those tools operate and the potential impact on investors) then that information can be disclosed in the OMI. We note at page 13 of the proposed guidance that the FMA recognises that the OMI is an appropriate place to disclose information about suspending redemptions – our submission is consistent with this view.
3	See response to question 7 below regarding guidance on the calculation of the liquidity ratio.
4	None

5	We are unsure of the merit of swing pricing. Over the acute COVID impacted period of March / June 2020, we observed in domestic fixed interest markets that both the buy spread and sell spread increased in the over-the-counter market for fixed interest securities. If the intent of a liquidity management tool is that the transacting investor pays the actual transaction cost, then swing pricing may not be fair. For example, unless there are an equal number of buyers and sellers (which is highly improbable) and a mid-market price is used, swing pricing (at a single price for buyers and sellers) is unlikely to produce a fair outcome. Having a different price for buyers and sellers is likely to be fairer. As such a hybrid model may be desirable whereby there is a maximum buy or sell spread but with the actual buy spread or actual sell spread dependent on flows and estimated costs on the day (and, importantly with the buy spread not necessarily being equal to the sell spread on a given day). However, that also needs to be weighed up against the complexities and costs as of having variable spreads.
6	We agree that stress testing is useful and an integral part of risk management. However, the frequency of that testing ought to be a matter of judgement for the MIS Manager. In circumstances where there is regular liquidity monitoring and there hasn't been a change to the investment strategy or profile of a fund, it is hard to see what benefit further and more regular (even annual) stress testing would achieve. This is particularly the case for managed funds that invest mainly (if not solely) in liquid assets (e.g funds that only invest in listed financial products that are redeemable within 10 days). The liquidity profile of these funds will remain the same regardless of the frequency of stress testing imposed. Stress testing imposes a cost to MIS Managers and, in turn, scheme participants and there should be a carefully considered cost/benefit analysis before imposing further and more regular stress tests on MIS Managers. Stress testing is also unlikely to be particularly relevant or meaningful for smaller funds / funds starting out that are investing wholly in liquid assets in deep markets. Ongoing monitoring of liquidity risks and having appropriate liquidity risk management tools are much more important than regular stress testing. Stress testing really just confirms the need for liquidity risk management tools. Ultimately, the key is to be able to manage a liquidity event through putting buy/sell spreads in place or through the suspension of withdrawals.
7	(a) We believe it would be helpful if the FMA were to offer guidance on the calculation of the liquidity ratio (FMC regulation 53 (5)) as this may assist MIS manager's initial thinking when defining illiquid assets. In particular, in what circumstances and to what extent should a large holding in an asset that is liquid in the ordinary course, be considered partially illiquid? Or are the base assumptions in the calculation of the liquidity ratio that the market is operating normally both in terms of the underlying investment and redemptions from the fund? (b) We consider that the proposed guidance overstates the role of the Supervisor and adds costs not anticipated by the legislature, particularly in circumstances where there is not actually a strict legal obligation to have a LRM framework (our comment at 1 that there is no legal obligation on MIS managers to have effective LRM also applies to the FMA's comment that this is a legal obligation on Supervisors). As with other matters, the Supervisor is required to

	supervise the performance by the manager of its functions and issuer obligations. This should just involve seeking regular assurance that the Manager has an effective LRM framework in place, and that it is being appropriately implemented and tested. In the ordinary course the value is in the Supervisor asking the question and having it answered. It should be the exception rather than the norm for a Supervisor to have to do a deep dive into a MIS Managers LRM framework. (c) We agree with the rationale / logic for MIS KiwiSaver Managers to be able to suspend redemptions. We note however, that the ability to suspend withdrawals does not currently sit neatly with the mandatory withdrawal requirements relating to permitted withdrawals and transfers under the KiwiSaver Rules. These are possibly bigger issues for the FMA to work through than liquidity management within the schemes. We would welcome the FMA's view on this as well as the ability for MIS KiwiSaver Managers to introduce side-pockets.
8	On the first page of the draft guidance and in paragraph 2.1, there is reference to adequately or effectively protecting investors. That is too much of a gloss on the purposes of the FMA under the FMA Act, the purposes of the FMC Act, and the overall statutory scheme. In the context of liquidity, it is fair to say that investors should be protected from not being adequately informed and from being treated inequitably or unfairly, but it is wrong to say (or infer) that investors should be protected from liquidity risk (because the law does not require that and it is not actually possible). The key points are that: • MIS managers need to be aware of liquidity risk on an ongoing basis, both in terms of the investments they make and the investors in their funds, • there need to be appropriate LMTs to ensure that there is not a mismatch between the liquidity of the underlying investments and the promises made to investors, and • liquidity risks and LMTs are appropriately disclosed to investors. However, the overall impression created by the guidance is that fund managers must protect investors from liquidity risks. In closing, we also note that IOSCO and FSB reports and recommendations have no standing at law in NZ. As such, to the extent that the FMA considers it desirable to adopt or implement recommendations that are not already expressly provided for in New Zealand law, then without seeking a change in the law or using the formal mechanisms in the FMC Act, the recommendation can and should only be implemented as best practice standards rather than strict legal obligations.
Feedback summary – *if you wish to highlight anything in particular*	
Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.	
Thank you for your feedback – we appreciate your time and input.	

Feedback form
Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 10 November 2023 Number of pages: 5

Name of submitter: [redacted]

Company or entity: Milford Funds Limited

Organisation type: MIS Manager (KiwiSaver and unit trusts)

Contact name (if different):

Contact email and phone: [redacted]

Question number	Response
1 *Do you think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management? If you think it can be clarified or improved, what changes or updates do you suggest we consider? Please give reasons for your view.*	Subject to our comments on specific features of the guidance (as elaborated on below), we consider the FMA's general expectations for liquidity risk management to be sufficiently clear.
2 *Do you believe there are any features that go too far or are too prescriptive for MIS managers or Supervisors? If so, please explain what should be changed or scaled back, and why.*	**Feature 1** We view the last bullet point in paragraph 1.1, which has been defined as a "must", as being too prescriptive. In our view: • it is impractical to produce comprehensive cash flow projections for the funds as there are many variables that do not lend themselves to being predictable/easily modelled. • the MIS manager would be best placed to determine its LRM framework, strategy and supporting processes. We would suggest that the guidance is amended to read: *"Ensure cash flows from assets, liabilities and off-balance-sheet items are ~~comprehensively projected~~* ***considered*** *over an appropriate set of time horizons."* **Feature 2** Paragraph 2.1 We believe that the requirement for an annual review of the LRM framework is too onerous. In the ordinary course of business, there will be minimal value from the associated policy/process review, particularly where regular reporting/monitoring is well established, and all relevant stakeholders are across it. We would suggest a regular review cycle, which is to be determined by the MIS manager as appropriate. Any changes can still be captured in between the relevant timeframe.

	Feature 5 This section proceeds on the basis that it's both desirable and, indeed, realistic to always provide investors with "ongoing disclosure" about liquidity issues especially during times of liquidity stress. The guidance does not appear to recognise that when a manager is dealing with a significant liquidity stress event: • the nature of the event may be such that unfiltered disclosure of the problem to investors may invoke a widespread panic reaction, resulting in a run on the fund. • unchecked disclosure risks damage to the fund becoming a self-fulfilling prophecy. History has shown that in times of acute liquidity stress, the optimum result for investors is often better achieved by the Manager working collaboratively with the Supervisor to manage the situation in a controlled manner so as to achieve the fairest possible outcome for investors as a whole. Disclosure to investors of the existence of an issue and how it will be managed may in certain circumstances be best achieved and appropriate only once a mitigation and ongoing management plan has been put in place by the Manager and Supervisor. We comment further on how we view the role of the Supervisor in this type of scenario in response to question 7 below. <u>Paragraph 5.1</u> What is the FMA's expectation of: • "ongoing disclosure about market movements"? For example, is the fund's daily unit price or monthly fact sheets considered a fulfilment of this requirement? • "ongoing disclosure about the fund's redemption terms and processes, and the liquidity of the underlying assets in the fund"? The wording in the guidance here is confusing. Ongoing disclosure about the funds' redemption terms and processes, is different to ongoing disclosure about the liquidity of the underlying assets in the fund. Unless the intention here is to require Managers to continually update cutoff times, process times, etc. in the middle of a liquidity event? We would only expect communication to investors where there is significant change in the liquidity of the fund that impacts their ability to withdraw their funds. If that is consistent with the FMA's expectation, then we encourage that you make this clear. <u>Paragraph 5.2</u> As you are aware, there are word limits for the product disclosure statement (PDS). We believe that a better place to include information on liquidity risk and liquidity management tools (LMT's) is the Other Material Information document. If you are wanting it in the PDS, it risks diluting the detail. It would also be helpful for the FMA to outline the level of detail expected.

Paragraph 5.4

It is not clear what the intention in relation to communication to investors is. Is this referencing communication at point of sale, ongoing or something else?

We would suggest that the guidance be amended to read:

> *"The MIS manager will proactively engage with investors~~, and not simply leave them to read the detailed terms and conditions~~* ***as appropriate and in a manner determined in conjunction with the Supervisor****."*

From our perspective, the intent is to ensure that clients are aware of adverse events and suitably informed in a measured way.

Paragraph 5.5

We would suggest the guidance be amended to read:

> *"Communication with investors, the Supervisor and other* ***relevant*** *stakeholders will* ***generally*** *be more frequent and more detailed in times of fund-specific or market-wide stress."*

Feature 6

Paragraph 6.2

Is it the FMA's expectation that MIS managers will

- measure and report the price impact of liquidation, or
- is it sufficient to consider it within our liquidity framework?

Milford currently does not explicitly measure and report the price impact of liquidation as our overarching view is:

- there is generally liquidity at a price and as such, we do not believe it is particularly informative compared to other measures of liquidity which we already consider.
- we do not think that there is a strong need to monitor the price impact of liquidation given the use of liquidity management tools such as swing pricing and anti-dilution levy mean that the cost of liquidation will be mitigated by transacting unitholders.
- we will likely need to subscribe to an external vendor service to be able to produce the required reporting for securities other than equities.

We think that effective monitoring/reporting should be defined by the MIS manager, with oversight by the Supervisor.

If the FMA still requires MIS managers to compute the price impact of liquidation, will it define a materiality threshold or an acceptable range?

Feature 11

As addressed in our feedback on feature 2 above, we do not think that an annual review is practical or useful. We recommend that the guidance be amended to read:

> *"As noted in feature 2, the MIS manager's board and senior management should ensure LRM practices are regularly reviewed~~ (e.g. no less than annually)~~."*

3 *Conversely, do you believe there are features that could go further, be more specific, or otherwise be clarified? If so, please explain your suggested changes and the reasons for these.*	**Feature 5** We think that from a product disclosure perspective, clients may benefit from a comparable/consistent indicator of fund liquidity. This could be in a similar vein to the risk indicator, albeit with a qualitative overlay considering the market/asset class/security type/diversification, etc.
4 *What additional features, if any, do you want to see in this guidance?*	No comment
5 *Are there any emerging best practices or ongoing trends in the industry that should be considered?*	No comment
6 *Do you expect there will be any material challenges or unnecessary compliance costs to your business as a result of meeting the expectations in the proposed guidance? Please give reasons for your view.*	This will be dependent on the FMA's requirement in Feature 6, paragraph 6.2. As addressed in our response to question 2 above, we may need to subscribe to an external vendor service to produce reporting on the price impact of liquidation for securities other than equities, which will incur a cost.
7a *Do you have any views in particular about the approach to defining illiquid assets?*	No
7b *Do you have any views in particular about the comments on the role of Supervisors?*	We consider that Supervisors can come into their own in stressed situations as: • They have only the single vested interest (i.e. the best interests of investors) to weigh-up in these situations. • Their judgement will not be clouded by any considerations of self-interest the MIS manager may be grappling with. • They can bring to bear a range of skills to address the particular liquidity issues that are manifesting, including the ability to introduce independent experts if required. • They can communicate with investors, if necessary, from a position of independence.
7b *Do you have any views in particular about the ability of MIS KiwiSaver Managers to be able to suspend redemptions?*	No
8 *Do you have any other feedback or comments on the proposed guidance?*	We believe that there should be a balance in the focus on: • a qualitative framework that ensures best practice, and • quantitative analytics that provide situational awareness. Clear guidance is welcomed but this needs to be tempered with not being overly prescriptive. There are a myriad of liquidity metrics and stress testing scenarios that can be undertaken by an MIS manager; ensuring managers have a clear and robust framework that encompasses the key elements of good liquidity practice, not just in market stress times but on an ongoing basis, should be the focus.
Feedback summary – *if you wish to highlight anything in particular*	

Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.

Thank you for your feedback – we appreciate your time and input.

Proposed Liquidity Risk Management Guidance – Mosaic

October 2023

Date: 31 October 2023

Number of pages: Four

Name of submitter: [redacted]

Company or entity: Mosaic Financial Services Infrastructure (Mosaic)

Organisation type: Financial Services Consultancy (Funds, Wealth, Banking & Insurance)

Contact email & phone: [redacted]

Mosaic Feedback

Question 1

Do you think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management?

If you think it can be clarified or improved, what changes or updates do you suggest we consider? Please give reasons for your view.

We think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management ("LRM"). In most instances, there is enough flexibility in the guidance for MIS managers to tailor their LRM policies and processes based on the features of their managed investment schemes ("MIS").

Our responses to the questions below outline specific areas for further consideration, clarification and/or improvement.

Question 2

Do you believe there are any features that go too far or are too prescriptive for MIS managers or Supervisors? If so, please explain what should be changed or scaled back, and why.

We consider the reference in section 2.1 (Ongoing Approval & Review) to the Board and Senior Management being... *'satisfied the [LRM] framework meets the objectives of effectively protecting investors, ensuring fair, efficient, and transparent financial markets, and reducing systemic risk'* should be amended to: the Board and Senior Management being... *'satisfied the[LRM] framework meets the objectives of effectively protecting investors in their MIS by ensuring (or promoting) fair, efficient, and transparent treatment of those investors'*.

In our view the focus of a MIS manager Board and Senior Managers should be on ensuring the effectiveness of the LRM for its scheme/funds given MIS manager's legislative duties are primarily to investors in their schemes. Broader financial market fairness, efficiency and transparency objectives, along with a reduction of systemic risk, should be a natural consequence of sound and effective implementation of LRM frameworks across the market at a MIS (and fund) level.

Question 3

Conversely, do you believe there are features that could go further, be more specific, or otherwise be clarified? If so, please explain your suggested changes and the reasons for these.

Underlying asset valuation methodologies and frequency which may be misaligned with a Scheme or fund's application and redemption terms should be given greater emphasis in the guidance note.

The guidance could give greater emphasis to underlying asset valuation methodology and valuation frequency as being an important consideration in designing and implementing an appropriate LRM framework. Alternatively, the FMA could develop and issue separate guidance on the valuation of private market assets, particularly when those private market assets are held by open-ended funds which provide for regular investor transactions.

For MIS that permit investors to enter, exit and transfer between funds and other schemes daily, to ensure investor equity and fairness a MIS manager may be required to suspend applications and redemptions from a fund if there is material valuation uncertainty with respect to a particular asset or asset class regardless of whether there has been a significant increase in redemptions or transfers.

For example, while private assets such as private equity, venture capital, and private debt are typically illiquid, they are also often classified as 'level 3' fair value assets under the NZ IFRS fair value hierarchy as their valuation is typically based on models, unobservable inputs, and subjective assumptions.

Private assets classified as 'level 3' are typically not able to be valued as frequently (or independently) as level 1 and level 2 classified fair value assets, and in times of market volatility and/or significant events impacting level 3 assets, determining a fair value of these assets can become difficult (particularly on a timely basis).

We note that funds within KiwiSaver Schemes will sometimes have an investment allocation to private assets (that are classified as level 3 fair value assets). However, because KiwiSaver Schemes accept application, redemption and transfer requests on a daily or at least weekly basis, KiwiSaver MIS managers (or any manager of a diversified open-ended fund) must consider and be mindful that it may need to suspend a fund(s) in times where the valuation uncertainty with respect to level 3 assets is heightened, and this materially impacts the reliability of the fund's NAV.

We are mindful that during the GFC, some funds were required to suspend redemptions (and applications) due to the inability to appropriately determine the underlying value of some assets (often private market assets) and, therefore, calculate the fund NAV on a timely basis. This was despite there not being any significant increase in redemptions, initially at least and noting the ensuring 'panic' from the fund suspension in these circumstances then led to a significant increase in redemption requests, necessitating a longer suspension period and eventual wind-up of the fund.

We therefore suggest in section 1.1, that 'asset valuation methodology and asset valuation frequency' is included as a consideration and characteristic to be addressed in designing the overarching framework and strategy.

Further, we suggest section 4.2 be amended to:

'During the product design phase, the MIS manager will also explicitly...determine a suitable dealing frequency for units in the fund, based on the transactability, valuation methodology and valuation frequency' of the underlying assets. This should include ensuring that the manager has an appropriate level of confidence that the NAV of the fund can be appropriately calculated, and that redemptions can be met under both 'normal' and 'extreme but plausible' market conditions'.

Question 4

What additional features, if any, do you want to see in this guidance?

There are an increasing number of 'self-select' managed investment schemes (including self-select KiwiSaver schemes) being offered in the New Zealand market. These provide a wide range of investment options comprising both funds and direct securities. While some of the expectations set out in the LRM guidance will be relevant to self-select schemes, they will need to be appropriately tailored.

We suggest that the FMA include specific guidance with respect to LRM expectations of MIS managers that offer self-select schemes. LRM considerations for self-select schemes may need to be considered by the MIS manager at the individual investor/member level with a greater reliance on upfront disclosure to self-select investors of the need to consider underlying liquidity risks when selecting investments, particularly where that member/investor has not received financial advice to support the construction of their portfolio.

The FMA may also want to consider incorporating a more overt expectation that MIS managers have a liquidity crisis management response plan, along the lines perhaps of a BCP, that would bring together all the themes set out in the guidance into a cohesive response framework.

Question 5

Are there any emerging best practices or ongoing trends in the industry that should be considered?

We note that the Australian-based Financial Regulator Assessment Authority review of APRA released in June 2023 noted that there is considerable room for improvement in the Australian superannuation industry regarding unlisted asset valuation, and APRA is expected to undertake further thematic work in the coming months.

The Australian Financial Review, on Jul 17, 2023, noted that "experts have been alarmed by the large investment by super funds in private assets, which have underwritten their strong returns, raising questions about the accuracy of valuations and the management of diversification and liquidity risks".

We suggest that developments in the Australian market in this area are well worth monitoring by the FMA.

Question 6

Do you expect there will be any material challenges or unnecessary compliance costs to your business as a result of meeting the expectations in the proposed guidance? Please give reasons for your view.

Compliance costs

Mosaic is not a MIS manager. However, we don't consider the costs associated with developing and implementing an appropriate LRM framework to be unnecessary (particularly from an investor outcome perspective). We also note that the guidance allows for a "fit for purpose" approach commensurate with the nature of the MIS and its underlying assets.

Anti-Dilution LMTs

While we agree that anti-dilution LMTs should be an important consideration for any MIS LMT framework, they can be complex to implement and administer, particularly where a MIS manager operates a "fund-of-fund" investment management structure (i.e., whereby a range of diversified multi-asset class funds managed by a MIS manager invest into several wholesale single-asset class funds and/or external managers). Fund-of-fund investment management structures are a common feature of the New Zealand market.

No anti-dilution LMT solution can guarantee equal or fair outcomes for every investor all the time. The implementation of anti-dilution LMTs requires judgment, estimation, and the need to balance the interests of fund investors generally (as a collective) against the interests of fund investors individually (or a particular group of investors).

The FMA, Supervisors and MIS managers will need to accept that the implementation of anti-dilution LMTs (e.g., swing pricing, entry and exit pricing or levies) to help ensure that non-transacting/remaining investors are not adversely impacted (directly or indirectly) by transacting investors, will require reasonable judgement and ongoing estimates to be made.

The objective of an anti-dilution LMT is that it should result in more equitable treatment of investors in the MIS than not having one. However, they will typically not remove inequitable treatment entirely, and MIS managers will need to be careful that inequitable treatment does not increase because of implementing anti-dilution LMTs.

We consider that there may be circumstances where the MIS manager determines (so long as its rationale is documented having regard to investor fairness and equity) that it may be appropriate for anti-dilution LMTs (e.g., swing pricing, entry and exit pricing or levies) not to be implemented (i.e., the fund investor benefits are marginal and/or do not outweigh the risks).

Question 7

Do you have any views in particular about:

a. the approach to defining illiquid assets

We support the requirement for MIS managers (with support from Supervisors) to define illiquid assets to enable the monitoring of a fund's liquidity risk and to support decision-making with respect to the management of liquidity risks.

b. the comments on the role of Supervisors

We think that the expectations of Supervisors regarding MIS LRM are appropriate. We agree that Supervisors should develop internal guidelines and prompts with respect to the escalation of particular LRM issues to the FMA (under section 203).

Supervisors should develop internal guidelines as to when they would expect MIS managers to invoke reactive LMTs (such as fund suspension) and communicate this to MIS managers so that they can be considered as part of the MIS manager's LRM framework. We note there will generally be a significant commercial impact on the MIS manager's business if a reactive LMT (such as fund suspension) is implemented for an extended period, so it will be important that the Supervisor can provide necessary guidance and set appropriate expectations to ensure the MIS manager is making decisions in the best interest of investors in the MIS.

c. the ability of MIS KiwiSaver Managers to be able to suspend redemptions?

We note the reference in section 7.3 that the MIS Manager (including KiwiSaver) must have the ability to suspend redemptions, and it may be acceptable to suspend redemptions from a KiwiSaver Scheme. We agree with this comment, noting the expectation that such suspension tools would be used sparingly.

However, has the FMA (perhaps as part of its own contingency planning) considered how a suspension of a fund within a KiwiSaver Scheme would or could operate within the legislative requirement to process a member's KiwiSaver transfer request within 10 business days under section 56(4) of the KiwiSaver Act 2006, also noting member contributions will continue to be received?

Is the FMA of the view that a scheme and/or fund suspension, if necessary to protect the interests of members of that KiwiSaver Scheme (fund), could extend beyond 10 business days? The guidance could expand on this point.

We are aware that subsection 56(4) allows for a longer period than 10 days by arrangement between providers, however this may be practically difficult to implement in a crisis situation.

Because the draft guidance specifically mentions that it may be appropriate for KiwiSaver managers to suspend redemptions (even if sparingly), we consider there should also be specific mention in other sections in relation to how the mandatory 'legislative design' of KiwiSaver should be a particularly important consideration in MIS Manager's 'product design' (and its supporting LRM) for its KiwiSaver Scheme(s) and the funds within it.

Given that KiwiSaver is and will continue to make up a significant share of New Zealand's MIS market by FUM and percentage of the population, we think there may be benefit in the LRM guidance being more explicit in respect of considerations and expectations for MIS managers in respect of KiwiSaver Schemes. We are particularly mindful that a suspension (albeit short) of a KiwiSaver Scheme (or a fund within it) could create a 'run' of redemption requests, further exacerbating the issue which could become systemic from a market perspective.

Question 8

Do you have any other feedback or comments on the proposed guidance?

Not at this time.

For more information, contact:

[redacted] or [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

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Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 10 November 2023 Number of pages: 1

Name of submitter:	[redacted]
Company or entity:	NZX Limited
Organisation type:	Licensed Market Operator
Contact name (if different):	
Contact email and phone:	[redacted] [redacted]

NZX is New Zealand's Exchange operating New Zealand's equity, debt, funds and derivatives markets is and a licensed market operator. The market capitalization of the 207 unique issuers listed on NZX's markets is approximately $214 billion.

Question number	**Response**
7(a): Do you have any views in particular about the approach to defining illiquid assets.	NZX notes that the FMA is proposing that fund managers may define the term 'illiquid asset' for themselves to enhance the oversight of asset liquidity. We wish to emphasize that we consider that all financial products quoted on NZX's markets will be liquid, and that illiquid assets will primarily fall within private or unlisted equity or other unlisted vehicle asset classes. We would be concerned if the intention was that quoted financial products were intended to be included within the definition of an illiquid asset, and that consequentially fund managers were incentivised to invest in international markets rather than supporting participation in New Zealand's capital markets. It will also be appropriate for fund managers to consider a number of factors beyond index inclusion and on-screen trading activity over a particular period when determining the extent of an asset's liquidity. Additional relevant considerations may include: over-the-counter institutional trading, and latent liquidity that may only manifest in certain market conditions (for example: at certain prices). We note that the introduction to the proposed guidance acknowledges the FSB's recommendation that funds that invest in a significant portion (30% or more) of illiquid assets would be best structured as close-ended funds, although this does not appear to be directly reflected in the Guidance. We consider that liquidity management tools may be sufficient to manage liquidity risks in these types of portfolios, absent a close-ended fund structure, and would be concerned about the negative effects on investment in less liquid assets if an expectation set that these types of portfolios were only suitable for close-ended funds (which do not offer a right of redemption).

Feedback summary

Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.

Thank you for your feedback – we appreciate your time and input.

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 10/11/2023 Number of pages: 1

Name of submitter: [redacted]

Company or entity: Pathfinder

Organisation type: MIS Manager

Contact name (if different):

Contact email and phone: [redacted]

Question number	Response
***4.** What additional features, if any, do you want to see in this guidance?*	*We would like to see an additional category to the suggested IOSCO options. Funds that have a 90% or higher liquidity ratio should be treated differently to funds with 50-90%, to align with the level of liquidity risk involved.* *For these types of funds liquidity risk is able to be managed, for example, through internal monitoring processes without the need for external LMTs.*

Feedback summary – *if you wish to highlight anything in particular*

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Thank you for your feedback – we appreciate your time and input.

10 November 2023

Financial Markets Authority,
Level 2 Grey Street,
Wellington 6140
By email: consultation@fma.govt.nz

Tēnā koe FMA,

Securities Industry Association submission: Proposed liquidity risk management guidance (September 2023)

The Securities Industry Association (**SIA**) appreciates the opportunity to submit on the FMA's "Proposed liquidity risk management guidance" consultation.

Please find our submission attached to reflect points held by the wider industry. No part of this submission is required to be kept confidential. We advise that some member firms may make submissions that reflect views relating specifically to their firm's business.

About Securities Industry Association (SIA)
SIA represents the shared interests of sharebroking, wealth management and investment banking firms that are accredited NZX Market Participants. Our members employ more than 500 accredited NZX Advisers, NZDX Advisers and NZX Derivatives Advisers, and more than 500 Financial Advisers nationwide. Our members work with over 300,000 New Zealand retail investors with total investment assets exceeding $80 billion, including more than $40 billion held in custodial accounts. Members also work with local and global institutions that invest in New Zealand.

Thank you for the opportunity to present our comments on this proposal. Please get in touch should you have any questions about this submission or require further information.

Nāku noa, nā

[redacted]

[redacted]

[redacted]

Feedback form

Consultation: Proposed liquidity risk management guidance

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Proposed liquidity risk management guidance: [your organisation's name]' in the subject line. Thank you. **Submissions close on Friday 10 November.**

Date: 10 November 2023 Number of pages: 3

Name of submitter: [redacted]

Company or entity: Securities Industry Association (SIA)

Organisation type: Industry association

Contact name (if different): As above

Contact email and phone: [redacted]

Question number	Response
1. Do you think the proposed guidance is sufficiently clear on the FMA's general expectations for liquidity risk management? If you think it can be clarified or improved, what changes or updates do you suggest we consider? Please give reasons for your view.	The Securities Industry Association (**SIA**) view is the Financial Markets Authority (**FMA**) proposed guidance sets fairly clear expectations for Managed Investment Schemes (**MIS**) managers of products where the fund manager selects the funds' investments. We recognise liquidity risk management is most relevant to managers of these traditional unit trusts, in acknowledging differences across some managed investment products, however, additional information could be provided to address how all businesses should work with the best intentions towards achieving the overarching goal of the framework.
2. Do you believe there are any features that go too far or are too prescriptive for MIS managers or Supervisors? If so, please explain what should be changed or scaled back, and why.	While we regard stress testing as a critical part of product design and risk management alongside liquidity management tools (**LMTs**), we do not believe that any amount of increased frequency of stress testing other than what would be considered reasonable would necessarily provide any further risk information even for a product with a liquidity issue. Furthermore, it is unclear what the benefits would be of regular stress testing for smaller funds that invest exclusively in listed securities or liquid debt securities. Any issues in that regard are more market-specific than fund-specific, therefore the question should be more about having appropriate liquidity management tools to manage any market liquidity event. Stress testing is a cost to businesses and consumers, but whether there are additional benefits should be assessed before considering upweighting testing requirements. What is vital is to ensure that stress testing methods are of a high standard and conducted regularly alongside market monitoring and that risk appetite and assumptions are articulated clearly and reviewed appropriately. However, it is also important to ensure other LMTs are in place to reduce the risk of a liquidity crisis causing a contagion effect to reduce investor harm. We support proactive communications to investors, including liquidity risk disclosures outside of terms and conditions, which is essential to transparency and investor education. However, we believe that requiring additional detail of stress testing in a Public Disclosure Statement (**PDS**) goes beyond what should be required. Consumers are already burdened with a significant amount of

	detail, and we suggest that a statement advising that stress testing is undertaken to the standard required and further information can be provided on request or that a website page with more detail would be sufficient for consumers.
3. Conversely, do you believe there are features that could go further, be more specific, or otherwise be clarified? If so, please explain your suggested changes and the reasons for these.	
4. What additional features, if any, do you want to see in this guidance?	While we understand that the FMA's approach is for the guidance not to be too prescriptive, we believe there is scope for more examples. We suggest that the guidance includes detailed scenarios demonstrating good liquidity risk management, including assumptions. The FMA could expand on what a scheme with too many illiquid securities would look like and the ramifications for that, for example, how different changes in the market could impact more widely. This could also help businesses when designing stress tests. Furthermore, additional detailed case studies on poor liquidity risk management (perhaps from the Global Financial Crisis), what the impact was and how the risk could have been more effectively managed would be helpful.
5. Are there any emerging best practices or ongoing trends in the industry that should be considered?	
6. Do you expect there will be any material challenges or unnecessary compliance costs to your business as a result of meeting the expectations in the proposed guidance? Please give reasons for your view.	In line with our response to Question 1, room for the liquidity risk management practices deployed to be fit for the MIS product would be welcomed to avoid the need to put in place unnecessary protocols. *Please see our response to Question 2 above.*
7. Do you have any views in particular about: a. the approach to defining illiquid assets b. the comments on the role of Supervisors c. the ability of MIS KiwiSaver Managers to be able to suspend redemptions?	
8. Do you have any other feedback or comments on the proposed guidance?	

Feedback summary – *if you wish to highlight anything in particular*

The Securities Industry Association (**SIA**) thanks the Financial Markets Authority (**FMA**) for the opportunity to respond to this consultation. This submission reflects views held by the wider industry. Some member firms may also make a submission that reflects comments and views relating specifically to their firm's business.

SIA understands that the guidance seeks to reflect international best practices and raise the standard and effectiveness of supervision and liquidity risk management (**LRM**) practices, particularly considering the economic environment in the context of the GFC and COVID, international policy recommendation by the International Organisation of Securities Commissions and the Financial Stability Board, and the findings of the FMA's LRM survey.

We support robust and workable regulations and fair requirements of businesses to meet their regulatory responsibilities. SIA recognises and supports the importance of managers of investment schemes to exercise care, diligence, and skill to develop, implement and review policies, processes and tools to ensure that the liquidity of such schemes is effectively managed as a matter of best practice and for consumer confidence.

As noted in our response to Question 4, we think the guidance could include examples of best practices that demonstrate good liquidity risk management, including assumptions that have been made.

Additionally, it would be helpful to have examples of what too many illiquid securities would look like and how various market scenarios could impact more widely. Furthermore, additional detailed case studies of poor liquidity risk management, the impact, and commentary on how the risk could have been more effectively managed would be helpful.

SIA appreciates the opportunity to provide feedback on the proposed liquidity risk management guidance for Managed Investment Schemes. We welcome further engagement should the FMA have questions or require further information on this submission.

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Thank you for your feedback – we appreciate your time and input.

AUCKLAND – Level 5, Ernst & Young Building | 2 Takutai Square, Britomart | PO Box 106 672 | Auckland 1143
WELLINGTON – Level 2 | 1 Grey Street | PO Box 1179 | Wellington 6140