

# Proposed guidance on substantial product holder disclosures

## About this consultation paper

We are seeking feedback on our proposed guidance on substantial product holders' disclosure obligations. We specifically want feedback on the section titled *Disclosures by individuals who manage funds* on page 14. This section deals with whether individuals who manage funds in fund management firms should be making substantial product holder (SPH) disclosures about the financial products they manage.

If introduced, this guidance will assist substantial product holders in understanding their obligations and help to promote consistency in disclosures.

Submissions close on Friday 16 June 2017. Please submit your feedback using the form at the end of the paper.

### About this consultation paper:

This consultation is for:

- Fund management firms and their employees
- Anyone who has, or may have, a substantial holding in a listed issuer
- Other interested parties.

It aims to:

Gain feedback on the proposed guidance paper and whether individuals who manage funds should be making SPH disclosures about the financial products they manage.



<a href="#">Proposed guidance on substantial product holder disclosures</a>	<a href="#">1</a>
<hr/>	
<a href="#">Purpose of this consultation paper</a>	<a href="#">3</a>
<hr/>	
Disclosures by individuals who manage funds	3
Effect of this proposed guidance	3
Legislative framework	4
Targeted consultation	4
Our approach	5
<a href="#">Proposed guidance on substantial product holder disclosures (SPH disclosures)</a>	<a href="#">7</a>
<hr/>	
Introduction	7
<a href="#">Background</a>	<a href="#">8</a>
<hr/>	
<a href="#">Compliance with FMC Act and Regulations</a>	<a href="#">9</a>
<hr/>	
Details of relevant transactions in initial disclosures	9
Aggregating on-market trades	9
Describing a ‘relevant interest’	10
Joint disclosures	11
Timeliness	12
<a href="#">Clarification of disclosure requirements</a>	<a href="#">13</a>
<hr/>	
Details of transactions for 1% movements	13
Registered holders	13
Disclosures by individuals who manage funds	14
<a href="#">Glossary of terms</a>	<a href="#">15</a>
<hr/>	
Questions for feedback	16
<a href="#">Feedback form</a>	<a href="#">17</a>
<hr/>	



# Purpose of this consultation paper

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Our proposed draft guidance on SPH disclosures is set out from page 7.

We are seeking feedback on whether this draft guidance requires further clarification. We have included specific questions for you to respond to on page 16. The main issue that we want feedback on is explained in detail below.

## Disclosures by individuals who manage funds

We have noted a difference in approach to the way fund management firms make an SPH disclosure. The section titled *Disclosures by individuals who manage funds* addresses this issue on page 14.

We are aware that one firm identifies both the firm and the individual within the firm who is responsible for managing the listed financial products as an SPH. The majority of firms only identify the firm (not the individual) as the SPH. This causes inconsistency in what is being disclosed to the market.

Our draft guidance provides that, on a natural interpretation of the relevant interest provisions in the FMC Act, individuals who manage funds generally **do** have a relevant interest in the financial products they manage. This is because, even if fund managers have controls or restrictions in place, those individuals will generally have a relevant interest under sections 235(1) (c) and/or (d) if they can still exercise some independent decision-making over those financial products.

## Effect of this proposed guidance

If we introduce this guidance, the effect will be that individuals who manage funds will need to make SPH disclosures when:

- They have the power to acquire, dispose of, or exercise the votes attaching to 5% or more of financial products in a listed issuer which is held in a fund they manage, regardless of whether or not they have a personal holding in the same listed issuer; or
- They have a personal holding in a listed issuer, and the power to acquire, dispose of, or exercise the votes attaching to financial products in the same listed issuer which is held in a fund they manage, and that power to control the firm's holding together with their personal holding reaches the 5% threshold.

A flow-on effect from our proposed interpretation is that other employees within the firm, who do not manage a particular fund, could also have a relevant interest if they, alone or jointly with others, exercise this decision-making power. For example, if investment decisions are ultimately made by an investment committee, each investment committee member may have a relevant interest and will be required to make SPH disclosures.

We understand that there may be less value in the SPH disclosures where the individual does not have their own personal holding in the listed issuer. In cases like this, the value seems to be limited to increased transparency around



who is able to control the relevant interest.

When producing this section of the guidance we have considered various matters including:

## Legislative framework

To determine, legally, if a person who manages funds is subject to the SPH regime, they must determine whether they have a ‘relevant interest’ or not in the financial products they manage.

Section 235 of the FMC Act defines when a person has a ‘relevant interest’. In addition to beneficial or registered ownership, sections 235(1) (c) and (d) provide that a person can have a ‘relevant interest’ if they have the *power to exercise, or to control the exercise of, a right to vote attached to the product, or to acquire or dispose of the product*. A person will have a ‘power or control’ regardless of whether or not that power or control is or can be made subject to restraint or restriction<sup>1</sup>. In addition, if two or more persons can jointly exercise that power, each of them is taken to have the power<sup>2</sup>.

## Targeted consultation

In November 2016, we asked for targeted feedback from a number of fund managers on our proposed guidance about this issue. We received five submissions, all of which were largely adverse to the requirement for disclosure from the individuals who manage funds.

Key arguments against our proposed guidance included the following:

- The current market practice is long-standing and aligns with international practice
- If individuals who manage funds have to make SPH disclosures as well as the firms, this leads to confusing disclosures
- The proposed guidance does not lead to establishing regulatory certainty as questions around who possesses power, or what degree of influence or control is required, are difficult to ascertain and likely to be interpreted differently. For example, there was uncertainty around who would have a relevant interest for temporary absences
- The purpose of the regime and scheme of the FMC Act does not support our proposed guidance. It would mean unnecessary compliance costs for fund managers, which do not advance the FMC Act’s purposes
- Individuals’ personal holdings in listed issuers are usually trivial amounts.

We acknowledge that there is some weight to these arguments, but we also acknowledge that other users of SPH notices may have different views. For that reason, we are seeking wider feedback in this consultation paper.

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<sup>1</sup> Section 235(1) (3).

<sup>2</sup> Section 235(1) (4).



## Our approach

A conflict of interest can occur where an individual has a power or control over the firm's holding in a listed issuer, as well as a separate personal holding in the same listed issuer. This might influence decision-making about the fund or the voting rights under the financial products. We understand that some, but not all, fund management firms mitigate this conflict by prohibiting their employees to have a personal holding in the same listed issuers.

There is also an argument that fund managers are better aligned with the interests of investors in the fund if they hold the same investments<sup>3</sup>. Our proposed guidance will provide greater transparency which may help to deter inappropriate conduct.

The SPH regime aims to reduce the risk that the market will not be adequately informed about who controls significant voting rights in a listed issuer. In some cases, it may be that the individual and the firm each have holdings that fall below the 5% threshold but, together, they exceed the 5% threshold. We think the market would want to be informed where that individual is able to control the voting rights attached to both their personal holding and the firm's holding.

### Practicalities

We appreciate there may be practical challenges in applying our proposed guidance. Feedback received during our initial 2016 consultation highlighted the difficulties in determining who has the requisite level of power or control to meet the 'relevant interest' test. In particular, it was highlighted that investment decisions in fund management firms rarely sit with a single individual but instead, are subject to an investment process which means investment decisions are often influenced by a number of people varies from firm to firm. This will, however, vary across firms.

### The position in Australia

We are aware that the current market practice taken by most New Zealand fund management firms is in line with current market practice in Australia. Consequently, our proposed guidance will result in a different approach being taken in the two jurisdictions.

### Alternative interpretations

While our proposed guidance follows the most natural interpretation of the relevant provisions, we acknowledge that there are other interpretations. We are aware that a strict interpretation of the 'relevant interest' provisions may not further the intended purposes of the SPH regime.

We looked at a range of interpretations of these provisions. These interpretations included those received in our 2016 targeted consultation). However, they appear to strain the provision's natural reading. Alternative interpretations may require changes to the current legislation, or mean we have to grant class relief from certain aspects of the current legislation.

We are seeking feedback on whether there are any changes needed to this aspect of the SPH regime. In particular, should a distinction be made between the disclosures required when an individual fund manager has their own personal holding in a listed issuer and the disclosures required when they don't have a personal holding?

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<sup>3</sup> Although alignment could be achieved by a fund manager investing in their own fund rather than directly investing in listed issuers.



We are also seeking feedback from technical experts with a view on the best way to implement any proposed changes, taking into account our range of regulatory powers.



# Proposed guidance on substantial product holder disclosures (SPH disclosures)

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## Introduction

Directors, senior managers and people who have a substantial holding<sup>4</sup> in a listed company are required to disclose certain changes to their ownership in a company. These disclosure obligations promote an informed market and deter insider conduct, market manipulation, and secret dealings in potential takeover bids.

We reviewed all SPH<sup>5</sup> notices submitted to the NZX Limited Market Announcement Platform over a three month period<sup>6</sup>.

Our aim was to assess whether the disclosures assisted in the promotion of a fair, efficient and transparent market.

We found:

- A significant number of SPH notices did not comply with the disclosure requirements in the Financial Markets Conduct Act 2013 (FMC Act).
- There was an inconsistency of approach with interpreting certain disclosure requirements.

### Purpose of this guidance note

This guidance note aims to:

- Inform market participants of our review findings and highlight areas of concern.
- Remind substantial product holders (SPH) of their statutory disclosure obligations under the FMC Act and Financial Markets Conduct Regulations 2014 (Regulations),
- Clarify what we expect of market participants for their legal requirements for statutory disclosures.
- Provide guidance in those areas of possible confusion about how the FMC Act and Regulations are applied.

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<sup>4</sup> *Substantial holding* means a relevant interest in 5% or more of quoted voting products in a listed company, as set out in section 274(2) of the FMC Act.

<sup>5</sup> *Substantial product holder* means a person who has a substantial holding in a listed company, as set out in section 274(3) of the FMC Act.

<sup>6</sup> 1 September 2015 – 30 November 2015.



## Background

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In 2013, we reviewed a sample of SPH notices against the requirements in the Securities Markets Act 1988 (SMA). We released our findings in the paper [‘Financial Markets Review of Market Disclosures’](#)<sup>7</sup>.

The disclosure requirements for SPH notices are now contained in Part 5 of the FMC Act and the Regulations, replacing those in the SMA. In 2016 we conducted a further review of SPH notices under the FMC Act.

The obligations under the FMC Act and SMA are broadly similar – a person with a substantial holding in a listed company has statutory disclosure obligations for certain events concerning holding or transacting in the relevant financial product.

SPH notices are provided to:

- Promote an informed market, and
- Deter insider conduct, market manipulation, and secret dealings in potential takeover bids.

This is to ensure participants in financial product markets can access information about the identity and trading activities of anyone who is entitled to control or influence the exercise of significant voting rights in a listed company<sup>8</sup>.

Timely, accurate disclosure is important to promote these purposes.

The Regulations set out the information which must be disclosed to meet these purposes. They include [prescribed forms](#)<sup>9</sup> with general and specific ‘instructions’ on how to correctly disclose the required information.

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<sup>7</sup> <https://fma.govt.nz/assets/Reports/141201-fma-review-of-market-disclosures.pdf>

<sup>8</sup> These purposes are set out in section 276 of the FMC Act.

<sup>9</sup> *Prescribed forms* are the default forms provided under Schedule 14 of the Regulations.



# Compliance with FMC Act and Regulations

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Our review identified a number of SPH notices that did not comply with the disclosure requirements in the FMC Act and Regulations. We follow up on non-compliant disclosures, where appropriate, and we may take further action if we continue to see non-compliance after we release the final version of this guidance.

We saw insufficient or inaccurate disclosures concentrated in the areas outlined below.

## Details of relevant transactions in initial disclosures

The FMC Act requires those with a relevant interest<sup>10</sup> in financial products to disclose on what date their substantial holding began (Initial Disclosure).

The Initial Disclosure must contain details of all transactions<sup>11</sup> or events which led to the acquisition of the substantial holding in the **four months before** its start date (or whichever is the shorter period if the company was listed less than four months ago).

We saw examples of Initial Disclosures that did not provide details of these relevant transactions or events in the four months before the substantial holding commenced. In some cases, the Initial Disclosures only provided information for the individual trade which tipped the SPH holding over the 5% threshold.

**We expect SPHs to ensure that details of all transactions and events in the four months prior to the start date of the substantial holding are included in the Initial Disclosure.**

### Example:

If a person (A) makes on-market acquisitions of financial products in a listed company (B) in the months of March, April and May, and then makes a single, on-market trade in June which results in a substantial holding commencing, the Initial Disclosure must include details of all on-market trades in March, April, May and June not just for the trade in June.

## Aggregating on-market trades

SPHs may aggregate on-market trades when they disclose the ‘details of transactions and events’ which led to the relevant event. The Regulations require that an SPH notice for aggregated on-market trade information must contain the following minimum information:

- The date range of the aggregated on-market trades.
- How the relevant interest was acquired, disposed of, or changed in nature.

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<sup>10</sup> The meaning of “*relevant interest*” is set out in sections 235-237 of the FMC Act.

<sup>11</sup> Alternatively, for on-market trades which have been aggregated, include all on-market trades in the aggregated information



- The total consideration paid or received for the on-market aggregated trades.
- The total number of financial products to which the aggregated on-market trades related.

This must be provided separately for on-market acquisitions and on-market disposals.

During our review, we saw examples of SPH notices for aggregated on-market trades that didn't provide all of the information required by the Regulations.

For example, some SPH notices disclosed the total number of financial products acquired, but not the time period of their acquisition, or the total consideration paid or received.

**While SPH notices which contain aggregated on-market trades are not required to detail each and every trade, we expect them to disclose the minimum information required under the Regulations.**

#### Example

Aggregated on-market trades may be disclosed as follows: On-market purchases of 100,000 ordinary shares, for total consideration of \$200,000, made during the period 1 May 2016 – 1 April 2016.

## Describing a 'relevant interest'

The Regulations require each SPH notice to:

- Describe the nature of the relevant interest in the substantial holding.
- Include prescribed information where that relevant interest is qualified or conditional.

During our review, we saw examples of SPH notices where either:

- The nature of the relevant interest was not described well or there was a lack of compliance with the requirements for prescribed information for a relevant agreement<sup>12</sup>. For example, some SPH notices described the nature of their relevant interest simply as “not applicable” or “normal market trading”. This is not enough to tell the market about how the SPH’s relevant interest arises.
- The SPH notices did not provide details of a relevant agreement, and/or
- The person failed to attach the relevant agreement to the SPH notice, and/or
- The person failed to disclose why the relevant agreement document<sup>13</sup> had not been attached, when required<sup>14</sup>.

**We expect to see the description of a relevant interest has sufficient information to enable the market to understand how that interest happened under the requirements of the FMC Act.**

<sup>12</sup> A “relevant agreement” is defined in regulation 139(1) of the Regulations.

<sup>13</sup> A “relevant agreement document” is defined in regulation 139(3) of the Regulations.

<sup>14</sup> Refer to regulations 140-142 which sets out circumstances where relevant agreement documents are not required to be attached to the Notice.

### Example

Person (A) holds 20% or more of the voting shares of a company (B) and B has a substantial holding in a listed company (C).

A could disclose that information as follows: A has the power to exercise the right to vote attached to 20% or more of the voting products of B. So A has a relevant interest in the financial products of C held by B as set out in section 237(b) of the FMC Act.

Where a relevant agreement exists for a relevant interest, we expect the SPH notice to include:

- Details of that agreement.
- Set out the material terms of the relevant agreement (if not in writing), or attach the relevant agreement document (if in writing), to the SPH notice.

## Joint disclosures

In certain cases, it is possible to complete one SPH notice for two or more SPHs under the Regulations. This is permitted as long as prescribed information for each SPH is disclosed.

During our review, we saw examples of SPH notices that were joint disclosures, but did not include this separate SPH information.

**We expect joint disclosure SPH notices to include the prescribed information for each SPH, as required by the prescribed forms.**

**We also expect that the disclosure is not confusing and makes clear which information relates to which person.**

### Example

Corporate (A) and (B) are related bodies each with registered holding in the same class of financial products of a listed company.

A and B make a joint disclosure after on-market acquisitions. This leads to a combined movement of 1% of their holding. In this situation, separate information should generally be provided for A and B under the following headings: 'Summary of substantial holding', 'Details of transactions and events giving rise to relevant event', and 'Details after relevant event'.

The disclosure should clearly state how A and B are connected to each other under 'Additional information'.



## Timeliness

The FMC Act requires SPHs to disclose “as soon as the person knows, or ought reasonably to know” that a relevant event<sup>15</sup> has occurred. This means that the disclosure must be made promptly and without delay.

Most of the SPH notices we reviewed had been filed within an appropriate timeframe. However we saw a small number of SPH notices that were not filed within a prompt timeframe.

Sometimes, an SPH knows in advance about relevant events, for example where a purchase or sale agreement is negotiated off-market. There is rarely any justification for a delayed filing of an SPH notice following such events, in particular when any of the parties involved is an existing SPH and should be aware of their obligations. This information may not be delayed in any way or held back.

If an SPH did not expect that they had to complete an SPH notice, we would expect the SPH notice to be filed, usually, within one business day of them becoming aware of the events which triggered the disclosure obligation.

We will continue to monitor the timely completion of SPH notices and we may take appropriate enforcement action where necessary.

### *Disclosure of price sensitive information during market hours*

Sometimes an SPH notice will contain information which could materially affect the price of an issuer’s quoted financial products (for example, transactions by SPHs that relate to takeover offers), if information that relates to the takeover offer is not yet known to the market.

SPH notices do not follow the same application process of administrative trading halts by NZX. This means that when someone releases a SPH notice which contains information relating to takeovers or other price sensitive information, they should, where possible, release this information to NZX outside of market hours.

Further information about NZX’s use of administrative trading halts can be found [on NZX’s website](#).

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<sup>15</sup> *Relevant event* means an event whose results in a person having to make a substantial product holder disclosure under sections 276-279 of the FMC Act, as set out in section 6 of the FMC Act.



# Clarification of disclosure requirements

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Our review revealed a lack of consistency that certain disclosures are being made. This guidance note aims to ensure a more uniform approach to SPH disclosures in future, and this section offers explanations of certain disclosure requirements.

## Details of transactions for 1% movements

The FMC Act requires SPHs to disclose movements of 1% or more in their substantial holding. However, the prescribed form for 1% movements does not set out whether all transactions which led to the 1% movement must be disclosed, or only the final transaction which tipped the substantial holding by 1%.

We expect SPH notices, for 1% movements, to include details of all transactions (including on-market trades which have been aggregated) and events which led to the disclosure of the 1% movement, to comply with the Regulations. This aligns with the requirement for Initial Disclosures to include information for all transactions and events which led to the substantial holding commencing in the previous four months. This is set out in more detail on page 9.

### Example

If a person makes six on-market trades on different days, with the sixth trade resulting in a 1% movement in the substantial holding, the SPH notice must include details of all six trades, not just details about the sixth trade.

## Registered holders

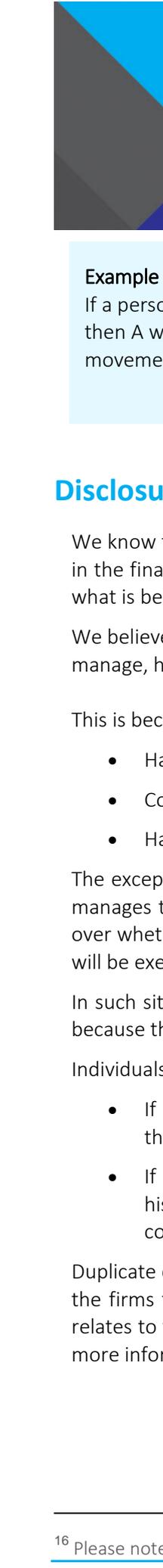
In an SPH notice, it is required that an SPH discloses:

- Who is the current registered holder of the financial products, and
- Who the registered holder of the financial products will be when the transfers are registered.

There appears to be some confusion in the market between the two fields. To clarify, as set out in the instructions to the prescribed forms:

- The “current” registered holder is the person to whom the financial products are registered before the relevant trade, transaction, or event occurs.
- When the transfers are registered, the registered holder becomes the person to whom the financial products are registered after the relevant trade, transaction, or event occurs.

If the registered holder is unknown please state “unknown” in the relevant field. This is commonly the case for on-market trades.



### Example

If a person (A) discloses a 1% decrease in their substantial holding after an on-market disposal of shares, and then A would be the “current” registered holder of the financial products. By contrast, if A disclosed a 1% movement after A acquired shares; A then becomes the “registered holder, after the transfers are registered”.

## Disclosures by individuals who manage funds<sup>16</sup>

We know there is currently a difference in opinion on whether individuals managing funds have a relevant interest in the financial products their fund management firms (or employers) hold. This has resulted in inconsistencies in what is being disclosed to the market.

We believe that individual fund managers do, generally, have a relevant interest in the financial products they manage, held by the firms they work for.

This is because, generally, they either:

- Have the power to acquire or dispose of the product, or
- Control the acquisition or disposal of the product, or
- Have the power to exercise, or to control the exercise of, a right to vote attached to the product.

The exception to this is where the fund has frameworks or mandates that place controls on how the person who manages the fund must operate, and these rules or controls stop them from independently exercising discretion over whether the financial products should be acquired or disposed of, or how the voting rights for those products will be exercised.

In such situations, consideration should be given to whether other internal persons may have a relevant interest because they, either alone or jointly with another person or persons, hold the ultimate decision-making power.

Individuals with a relevant interest in the funds they manage should make a SPH disclosure when:

- If they do not have a personal holding in the listed company, when the fund they manage meets the 5% threshold, or
- If they have a personal holding in the same listed company, when that personal holding together with his/her relevant interest in the firm’s holding leads to a combined holding of 5% or more in the listed company.

Duplicate disclosures may confuse the market. Therefore, we recommend that individuals who manage funds, and the firms they work for, consider disclosing their relevant interests on a single SPH notice where the disclosure relates to the same relevant interest and type of event disclosure. See the instructions in the prescribed forms for more information on the requirements for joint disclosures.

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<sup>16</sup> Please note this section may change as the FMA is currently consulting on this section of our draft guidance paper.



## Glossary of terms

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Term	Definition
FMC Act	Financial Markets Conduct Act 2013
Relevant interest	Has the meaning set out in section 235 of the FMC Act
Relevant agreement	Has the meaning set out in regulation 139(1) of the Regulations
Relevant agreement document	Has the meaning set out in regulation 139(3) of the Regulations
Substantial holding	Has the meaning set out in section 274(2) of the FMC Act
Substantial product holder or SPH	Has the meaning set out in section 274(1) of the FMC Act

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## Questions for feedback

1. Do you think any content in our draft guidance is unclear or requires further clarification? Do you think we should include any further guidance relating to substantial product holders' disclosure obligations, which is not currently included?
2. Do you agree that the interpretation of the law set out in the final section of the guidance titled *Disclosures by individuals who manage funds* (the "interpretation") is the most natural interpretation of the law? If not, what is the most natural interpretation?
3. Do you think the effect of the Interpretation is useful to help prevent the 'mischief' outlined on page 5 above, and to help promote fair, efficient and transparent markets?
4. If you don't think the guidance is helpful to promote fair, efficient and transparent markets, please describe what disclosure rules you think should apply to individuals who manage funds? In particular:
  - a. Should individual fund managers be required to disclose a personal holding in a listed issuer if their personal holding plus the holding of the fund they manage exceeds 5%? Why?
  - b. Should fund management firms be required to disclose the names of the individuals that control their investments in listed issuers (when the fund's investment exceeds 5%) even if the individual(s) do not have their own personal holdings in those listed issuers? Why?
5. If you are a technical expert and think that different disclosure rules should apply, we would like your feedback on how best such different rules could be put in place, given the scope of the existing legislation and our regulatory powers.



# Feedback form

## Feedback: Guidance on substantial product holder disclosures

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at [consultation@fma.govt.nz](mailto:consultation@fma.govt.nz) with 'Feedback: Substantial product holder disclosures' and your entity name in the subject line. Thank you. **Submissions close on Friday, 16 June 2017.**

Date: \_\_\_\_\_ Number of pages: \_\_\_\_\_

Name of submitter: \_\_\_\_\_

Company or entity: \_\_\_\_\_

Organisation type: \_\_\_\_\_

Contact name (if different): \_\_\_\_\_ Contact email and Phone: \_\_\_\_\_

Paragraph or Question Number:	Comment	Recommendation
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*You don't need to quote from the consultation document if you use question numbers. You may attach extra pages – please label each page with your name and organisation. You don't need to give an answer to every question if you don't want to.*

Q1		
Q2		
Q3		
Q4		
Q5		

**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.**

