

# THE FINANCIAL SERVICES SECTOR

THROUGH COVID-19 ALERT LEVEL 3 AND BEYOND

APRIL 2020 – DETAILED REFLECTION AND GUIDANCE

## From COVID-19 Alert Level 3 and beyond – reflecting on the impacts for the financial services sector

As we transition to COVID-19 Alert Level 3, it is timely to reflect on the many rapid changes that the Government and regulators have introduced over a few short weeks to ease the burden of regulatory compliance, and also the FMA's and Reserve Bank's expectations, in turn, that market participants keep their customers' interests front of mind in these extraordinary and challenging times.

Since March, the Financial Markets Authority (*FMA*) has been working closely with the Council of Financial Regulators (which includes Treasury, the Reserve Bank, the Commerce Commission and MBIE), as well as the NZX, supervisors and audit bodies, to ensure a co-ordinated response to the regulatory issues faced by market participants arising from the COVID-19 crisis.

The FMA's announcement, on Friday 24 April, that it intends to use a "no action" approach to address breaches or potential breaches of regulatory obligations arising as a result of COVID-19 is further evidence of the regulators' preparedness to introduce practical regulatory relief for the financial services sector as we move into Alert Level 3.

This Brief Counsel outlines some of the measures taken to date to provide regulatory relief and practical guidance for the financial services sector in response to the disruption caused by COVID-19 – particularly to address

the difficulties posed by remote working arrangements, making collaboration harder and lead times to produce information and reporting longer.

As noted, it's also timely that the FMA and the Reserve Bank have jointly reminded the market (in an article that can be found [here](#) ('Conduct expectations in response to COVID-19') of their ongoing expectations of market participants, noting that they remain vigilant against improper conduct or unfair practices at a time when some may find themselves under financial stress and in need of support. The message remains that customers' interests should continue to be the key focus, and that financial services businesses must act responsibly and with compassion in circumstances where their customers' circumstances may have changed.



## FMA'S "NO-ACTION" APPROACH

On 24 April 2020, in recognition of the significant impact and practical difficulties that COVID-19 is having on many market participants, the FMA announced that where a market participant breaches, or expects to breach, a regulatory obligation as a result of the COVID-19 circumstances and seeks relief from the FMA, the primary approach it intends to take is 'no-action'.

The FMA explained that a 'no action' approach means that the FMA will not take action against a market participant for breach of a statutory or regulatory obligation. Although it is an expression of regulatory intention, a confirmation from the FMA that it will take 'no action' does not necessarily preclude third parties from taking legal action in relation to the same conduct or conduct of that kind.

The FMA also expects market participants to take steps to mitigate any risks resulting from the breach, and that where possible, breaches will be remediated at a later date, so that the requirement to comply is *delayed* rather than removed.

It is also important to note that the 'no-action' approach is not intended to apply to ongoing and open-ended breaches, or where there is significant risk of customer detriment, and exemptions may be required in certain, limited, circumstances.

However the FMA expects to deal with most requests for relief due to COVID-19 with this 'no-action' approach, and market participants are strongly encouraged to promptly report past, imminent or current breaches due to COVID-19. Further details as to how to apply for "no action" relief can be found on FMA's website [here](#).

## FINANCIAL MARKETS CONDUCT (FINANCIAL REPORTING AND OTHER RELIEF – COVID-19) EXEMPTION NOTICE 2020

Regulatory relief for periodic reporting within prescribed time frames was the first law change signalled for the financial services sector to ensure markets would be able to continue to function well and support participants, customers and investors during the COVID-19 lockdown and

beyond. That relief has now been formalised in the [Financial Reporting and Other Relief-COVID-19 Exemption Notice](#), which was granted on 23 April 2020 and takes effect on 29 April 2020.

FMC reporting entities impacted by COVID-19, and with balance dates between 31 December 2019 and 31 July 2020, will have an additional two months over the prescribed statutory timeframes to comply with a range of reporting and information disclosure requirements under the FMCA and related existing exemption notices.

A key exemption gives FMC reporting entities and scheme managers **six months**, as opposed to the standard four months, to produce and file their audited financial statements (and scheme providers will have up to 6 months to produce schemes' annual reports) provided certain conditions are met, including that it believes, on reasonable grounds, that it is not reasonably practicable to comply within the original prescribed time frame because of the outbreak of COVID-19.

In addition, relevant reporting entities who rely on the extension of time for filing audited financial statements, and custodians, will have an additional two months over the prescribed timeframes to comply (as applicable) with the requirements for:

- continuous issuers of debt securities or equity securities to update information about those securities;
- non-unitised restricted schemes which attribute earnings rates to members to make their fund updates available and to provide confirmation information to members;
- scheme managers of closed-ended restricted schemes to hold an annual meeting;
- issuers to have their registers audited;
- scheme custodians to complete their annual custodial assurance engagement; and
- derivatives issuers to complete their assurance engagements.

The exemption notice provides similar additional time for the completion of custodial assurance engagements prescribed under existing exemptions for Forestry Schemes, Property Schemes and Overseas Custodians.

An entity wishing to rely on any of these exemptions must pay careful attention to the prescribed conditions, which include notifying the FMA of that fact within the original prescribed timeframe for compliance, and in some cases, lodging a copy of that notice with the Registrar of Financial Service Providers, within the required period. If reliance on the exemption would require notice to be given to the FMA on or before 30 April 2020, the notice must instead be given on or before 15 May 2020.

It should also be noted that reliance on this exemption notice for extended time to file audited financial statements will have flow-on effects for some other filing requirements, for example the financial statement and solvency filings of insurers under the Insurance (Prudential Supervision) Act (IPSA).

The Reserve Bank has advised licensed insurers that similar regulatory relief will be available under IPSA. This will be achieved by way of waiver of the Reserve Bank's right to enforce any failure of an insurer to file reports or to make related disclosures, provided the relevant revised deadlines for prudential submissions are met.

## FINANCIAL ADVISERS (CUSTODIAN ASSURANCE ENGAGEMENT RELIEF – COVID-19) EXEMPTION NOTICE 2020

This [new exemption notice](#) provides custodians with a corresponding additional two months to comply with their duty, under the Financial Advisers (Custodians of FMCA Financial Products) Regulations 2014, to obtain a custodian assurance engagement, and provides similar additional time for overseas custodians to obtain their custodian assurance engagement in accordance with the Financial Advisers (Overseas Custodians- Assurance Engagement) Exemption Notice 2018, if the custodian believes, on reasonable grounds, that it is not reasonably practicable for it to comply within the original prescribed time frame because of the outbreak of COVID-19. This exemption notice also amends the *Financial Advisers (Non-NZX Brokers—Client Money) Exemption Notice 2017* to extend by two months the time frame for complying with the

condition that a non-NZX Broker (who is relying on the exemptions in that exemption notice) obtains an auditor's report regarding the non-NZX broker's compliance with the conditions in that exemption notice.

Any custodian or non-NZX Broker wishing to rely on these exemptions must also notify the FMA of that fact within the original prescribed timeframe for compliance, and if reliance on the exemption would require notice to be given to the FMA on or before 30 April 2020, the notice must instead be given on or before 15 May 2020.

## NZX RELIEF FOR LISTED ISSUERS

The NZX has issued similar relief for Listed Issuers. Listed Issuers will still be subject to their continuous disclosure requirements and will need to maintain up to date continuous offer information. Chapman Tripp has published a [brief counsel](#) ('COVID-19 unprecedented relief for NZX listed issuers') covering the periodic reporting changes as they impact on listed issuers, as well as new timing relief for rights issues and share purchase plans.

## REMINDER TO COMPLY WITH INSIDER TRADING RULES

On 22 April 2020, the FMA published a reminder [here](#) for all market participants to comply with the insider trading prohibitions in sections 240 to 243 of the Financial Markets Conduct Act. The FMA stated, although neither the FMA nor the NZX had seen an increase in suspected breaches, that concerns have been raised in offshore markets regarding potential misconduct by information insiders. The FMA noted that all market participants, including listed issuers and their employees, directors, corporate advisers and executing brokers also have a role to play in managing insider information risks.

All NZX listed companies should have policies in place to manage these risks, and should be particularly vigilant at this time. Listed issuers should mitigate inside information misconduct risks by:

- Controlling and limiting access to inside information,
- Retaining detailed records of information insiders, including when they received inside information and for what purpose,

- Providing a reminder to employees regarding inside information conduct prohibitions and any obligations under staff trading policies,
- Requiring employees to proactively notify the company if they disclose or come into possession of inside information (e.g. through inadvertent disclosure),
- Ensuring that the processes governing requests to trade from directors, staff, contractors and associated individuals are adequate and are followed consistently, and
- Ensuring that directors and senior managers promptly file their ongoing disclosures of dealings in relevant interests.

## OATHS AND DECLARATIONS

A significant technical problem caused by the pandemic is the administration of oaths and declarations, including the attestation of affidavits and statutory declarations. The problem arises because the law contemplates that the person giving the oath or declaration is in close physical proximity to the administering person (usually a lawyer).

The challenge with statutory declarations in this environment is particularly acute in the KiwiSaver withdrawals context, as well as for complying superannuation funds, which must obtain statutory declarations whenever members seek withdrawals based on significant financial hardship, emigration or a life-shortening congenital condition (or which include government contributions).

Prior to 17 April 2020, (when the *Epidemic Preparedness (Oaths and Declarations Act 1957) Immediate Modification Order 2020* was made under the *Epidemic Preparedness Act 2006* to address the position), the Law Society had recommended an approach to allow remote video conferencing tools such as Skype or Zoom to be used to administer the oath or declaration. Under this approach, the witnessing lawyer would provide a certificate detailing how the oath or declaration was given and ensuring verification of the deponent's identity (where the deponent is not known to the lawyer). The FMA had also issued procedural guidance (which has been updated to reflect the Epidemic Preparedness Order).

Under the Order, oaths, affirmations and declarations can be taken using an audio-visual or audio link instead of in the presence of the person swearing the oath or making the affirmation or declaration. The administrator must be satisfied that the person swearing or making the oath or affirmation signed the document concerned in the course of the audio-visual or audio link. The person signing the document must as soon as practicable then send the signed document (or a photograph or scan of the signed document) to the administrator for the signature of the administrator.

Recognising the particular relevance to KiwiSaver schemes (including restricted schemes) and complying superannuation funds, the FMA has published updated guidance [here](#) ('COVID-19: KiwiSaver significant financial hardship applications') for KiwiSaver members considering making a Significant Financial Hardship Withdrawal application, and the Ministry of Justice has also provided useful supporting procedural guidance [here](#) ('COVID-19: KiwiSaver significant financial hardship applications – alternative steps to verify identity and financial circumstance').

As we move down the Alert Levels, the usual requirements for oaths and declarations to be taken may become less difficult to arrange. However, as isolation measures continue, these modification orders provide useful and pragmatic alternative solutions, particularly in relation to vulnerable individuals, and certainty in relation to legal documents, of considerable importance to the individuals signing them.

## AML/CFT – IDENTITY VERIFICATION

There are also AML challenges relating to face to face identity verification and certification in the current environment. The three AML supervisors have updated their guidance [here](#) for alternative steps to verify identity and financial circumstances during COVID-19 Alert Levels.

These include delaying the verification component for customer due diligence for new business relationships until a further date provided:

- it is essential not to interrupt normal business practice; and

- AML/CFT risks are effectively managed through procedures of transaction limitations and account monitoring or through other appropriate risk management procedures; and
- verification of identity is completed as soon as practicable once the business relationship has been established.

Reporting entities may also offer electronic verification options but must ensure they have exception handling provisions for circumstances where a customer is unable to provide their original identity.

### AML/CFT – BI-ANNUAL AUDIT

The FMA has also acknowledged [here](#) that COVID-19 may impact a reporting entity's ability to have the required bi-annual audit of its risk assessment and AML/CFT programme undertaken within the statutory timeframe. Any reporting entity unable to complete its independent audit on time due to COVID-19 should contact the FMA. The FMA has said that it will consider each reporting entity's circumstances on a case-by-case basis, with a view to granting targeted relief where appropriate.

### FMA LIQUIDITY RISK MANAGEMENT GOOD PRACTICE GUIDE FOR MANAGED INVESTMENT SCHEMES

On 17 April 2020, the FMA published a good practice guide for managed investment schemes (MIS) on liquidity risk management. The guide (which can be found [here](#) ('Liquidity risk management – A good practice guide for Managed Investment Schemes'), sets out the FMA's expectations of licensed MIS Managers in relation to risk management, and in particular managing liquidity risk at times of heightened market uncertainty and volatility. It includes eleven good practice principles in relation to governance, liquidity risk frameworks, monitoring, reporting and disclosure, use of leverage, liquidity management tools, stress testing, data systems and record keeping, contingency plans and assessment by Supervisors.

The guide has been developed to address a July 2018 IOSCO recommendation that regulators devote closer attention to the liquidity stress-testing practices of open-ended collective investment schemes to protect investors, ensure fair and efficient financial markets and reduce systemic risk. This recommendation was intended to address some of the structural vulnerabilities in the asset management sector exposed during and after the GFC. Given the current COVID-19 crisis, the FMA has released the guide earlier than planned.

The purposes of the guide are to:

- remind licensed MIS managers of the FMA's expectations of them in relation to risk management and in particular liquidity risk at times of heightened market uncertainty and global volatility;
- share good liquidity risk management practices that emerged following the GFC that are relevant to the current COVID-19 pandemic crisis; and
- provide context for licensed MIS managers in preparation for the FMA's upcoming survey of MIS liquidity intended to be undertaken later in 2020. The FMA notes that this survey may ask about MIS managers' responses to the COVID-19 pandemic.

The FMA also notes that the information in the guide is also relevant to Supervisors in relation to their frontline regulatory oversight of MIS Managers.

### KIWISAVER DEFAULT PROVIDER REVIEW

The Minister of Finance and the Minister of Commerce and Consumer Affairs announced in late March 2020 that the process for appointing new KiwiSaver default providers would be delayed due to the exceptional circumstances facing financial services providers as a result of the outbreak of COVID-19. The expiry date for existing appointments has also been extended by five months from 30 June 2021 to 30 November 2021.

The Ministry of Business, Innovation and Employment (*MBIE*) has updated stakeholders to advise that the Government now intends to issue a request for proposals (*RFP*) around September 2020. MBIE has advised, however, that this target timeframe is subject to change.

MBIE has also advised that it may need to engage with KiwiSaver scheme providers before the release of an RFP on more technical details of the review in mid-to-late July, and that the content of any such engagement (and the feedback it receives) will be provided to all stakeholders either via email or on the MBIE KiwiSaver website. MBIE notes that this revised timeframe is subject to change depending on the circumstances at the time. In the meantime, stakeholders are asked to continue to direct any questions they may have regarding the review to this inbox ([defaultkiwisaver@mbie.govt.nz](mailto:defaultkiwisaver@mbie.govt.nz)).

## OTHER FINANCIAL SERVICES LEGISLATION DELAYED

As has been signaled for some time, the **Financial Services Legislation Amendment Act ("FSLAA")** transitional licensing start date has been delayed from the original 29 June 2020 date to early 2021. The exact date the new regime will commence will be communicated in due course (but well in advance), with MBIE confirming that it will be March 2021 at the earliest. The transitional licensing application period will be extended until the same date and the new Code of Professional Conduct for Financial Advice Services will also come into effect on the same date.

Transitional licensing will remain open and those who have already had licences approved or who have already submitted a transitional licensing application will not need to reapply. The existing regime under the Financial Advisers Act 2008 will continue to apply in the meantime.

This is welcome relief for many advisers, particularly since the disclosure regulations had not yet been released, so applying for a transitional licence in the timeframes would have been challenging for some even without the current disruptions. Indications are that the disclosure regulations will be released in the next couple of months.

As a consequence of the deferral of the start of the new financial advice regime, the FMA has released a [consultation document](#) in relation to its proposal to continue the following **Financial Advisers Act exemption Notices** (that are due to expire in November this year) up until the start of the new financial advice regime:

- Financial Advisers (Non-NZX Brokers – Client Money) Exemption Notice 2017
- Financial Advisers (NZX Brokers – Client Money and Client Property) Exemption Notice 2015
- Financial Markets Conduct (Offers of Financial Products Through Authorised Financial Advisers Supplying Personalised DIMS) Exemption Notice 2015

The consultation period for these exemption ends on Friday 22 May 2020.

The **Financial Markets (Conduct of Institutions) Amendment Bill ("COFI Bill")** has also been put on hold. The COFI Bill submission deadline was extended to 30 April 2020 despite the Finance and Expenditure Committee (only days before the announced extension) initially denying a request for an extension.

The commencement of **Part 5A of the Credit Contracts Legislation Amendment Act 2019 ("CCLAA")** (relating to fit and proper person certification) has also been delayed. The commencement date for this part has been delayed from 1 September 2020 to no earlier than 1 March 2021. The commencement of the new regulations and other remaining provisions of the CCLAA will also be delayed from 1 April 2021 to no earlier than 1 October 2021.



The Reserve Bank of New Zealand has also advised that the following regulatory initiatives will be put on hold for “an initial period of six months”:

- Review of the bank liquidity thematic review (and subsequent review of the liquidity policy (BS13));
- Review of the Insurance (Prudential Supervision) Act 2010;
- Standard terms for Residential Mortgage Obligations;
- Cyber resilience guidelines for all regulated entities;
- Revisions to banks’ disclosure of regulatory breaches;
- Review of the stress-testing framework and planned bank stress-tests;
- Revising the process for approving banks’ internal capital adequacy models for credit risk; and,
- Future of cash – standards for banknote-processing machines.

## OTHER DELAYS AND EXTENSIONS

In addition to those referred to above, a number of other legislative and policy reviews have also been delayed. These include the extension of time to make submissions on the Fair Trading Amendment Bill from 27 March 2020 to 26 April 2020, and the extension of time to make submissions on the GST Policy Issues paper from 9 April 2020 to 8 May 2020.

A comprehensive list can be found [here](#) (‘Council of Financial Regulators – Deferral of regulatory initiatives affecting the financial sector’).

The rapid response of the Government and regulators to issues arising due to COVID-19 means that any further changes are unpredictable and may well happen quickly.

## KEY CONTACTS

Please reach out to us if you have any questions in relations to the above. We wish you all the best at this uncertain time.



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