

Version
as at 18 November 2021



Financial Markets Conduct (Property Schemes—Custody of Assets) Exemption Notice 2016

(LI 2016/266)

Financial Markets Conduct (Property Schemes—Custody of Assets) Exemption Notice 2016: revoked, on the close of 17 November 2021, by clause 3.

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

Contents

		Page
1	Title	2
2	Commencement	2
3	Revocation	2
4	Interpretation	2
	<i>Exemptions from independent custody requirements for real property assets</i>	
5	Application of exemptions from independent custody requirements	3
6	Exemptions from independent custody requirements	3
7	Conditions of exemptions in clause 6	3
	<i>Exemption from daily cash reconciliation requirement</i>	
8	Exemption from daily cash reconciliation requirement	5
9	Condition of exemption in clause 8	5
	<i>Exemption from annual assurance engagement requirement</i>	
10	Application of exemption from annual assurance engagement requirement	5
11	Exemption from annual assurance engagement requirement	6

Note

The Parliamentary Counsel Office has made editorial and format changes to this version using the powers under subpart 2 of Part 3 of the Legislation Act 2019.

Note 4 at the end of this version provides a list of the amendments included in it.

This notice is administered by the Financial Markets Authority.

12	Conditions of exemption in clause 11	6
13	Time frame extended because of outbreak of COVID-19	6

Notice

1 Title

This notice is the Financial Markets Conduct (Property Schemes—Custody of Assets) Exemption Notice 2016.

2 Commencement

This notice comes into force on 18 November 2016.

3 Revocation

This notice is revoked on the close of 17 November 2021.

4 Interpretation

(1) In this notice, unless the context otherwise requires,—

Act means the Financial Markets Conduct Act 2013

closed, in relation to a property scheme, means that the scheme does not offer or issue further managed investment products in the scheme

effective date has the same meaning as in clause 16(1) of Schedule 4 of the Act

existing property scheme means a property scheme that is treated as being a registered scheme on and after the effective date under clause 22 of Schedule 4 of the Act

property scheme means a managed investment scheme to which both of the following apply:

- (a) the principal investment policy and objectives of the scheme are to invest, in the ordinary course of business, in residential or commercial real property with the intention of earning a return on the investment through leasing the real property or through the future resale of that real property, or both; and
- (b) the scheme is not a managed fund

Regulations means the Financial Markets Conduct Regulations 2014

relevant date, in relation to a custodian, has the same meaning as in regulation 87(4) of the Regulations

relevant period, in relation to a custodian, has the same meaning as in regulation 88(4) of the Regulations.

- (2) Any term or expression that is defined in the Act or the Regulations and used, but not defined, in this notice has the same meaning as in the Act or the Regulations.

Exemptions from independent custody requirements for real property assets

5 Application of exemptions from independent custody requirements

The exemptions in clause 6 apply to a manager and a supervisor of a property scheme that meets both of the following requirements:

- (a) the scheme is an existing property scheme that is closed; and
- (b) the manager is not exempt in respect of the scheme from the requirement to have a licensed supervisor under an exemption granted under Part 9 of the Act.

6 Exemptions from independent custody requirements

- (1) Every manager of a property scheme to which the exemptions in this clause apply is exempted from section 127(1)(f) of the Act to the extent that it requires the scheme's real property to be held by the supervisor or another person who meets the external custodianship requirements in section 156 of the Act (to the extent that the property is not held directly by scheme participants).
- (2) Every manager of a property scheme to which the exemptions in this clause apply is exempted from section 133(a) of the Act to the extent that it relates to the requirement referred to in subclause (1).
- (3) Every supervisor of a property scheme to which the exemptions in this clause apply is exempted from section 156(1) of the Act to the extent that that section requires the supervisor to hold the scheme's real property or, if authorised by the governing document, contract the holding of that scheme property to another person who meets the external custodianship requirements in that section (to the extent that the property is not held directly by scheme participants).

7 Conditions of exemptions in clause 6

The exemptions in clause 6 are subject to the conditions that—

- (a) real property that is not held by the supervisor or another person who meets the external custodianship requirements in section 156 of the Act, or held directly by scheme participants, must be held—
 - (i) by a custodian on trust for the scheme (but that custodian does not need to meet the external custodianship requirements in section 156); or
 - (ii) if the scheme is a limited partnership, by the limited partnership; and

- (b) the real property referred to in paragraph (a) is subject to an encumbrance or a mortgage in favour of the supervisor that is registered against the title to the property and the following requirements are met:
 - (i) the encumbrance or mortgage secures all present and future obligations of the custodian or limited partnership that are owed, under the governing document for the scheme, to the supervisor or the scheme participants; and
 - (ii) the encumbrance or mortgage or the scheme's governing document contains a prohibition on the custodian or limited partnership doing any of the following, except with the prior written consent of the supervisor:
 - (A) leasing all or any part of the real property except in the ordinary course of business of the scheme and in accordance with the scheme's governing document;
 - (B) selling, transferring, or otherwise disposing of the real property or any interest in it;
 - (C) creating, or permitting the continuation of, any mortgage, charge, or other security interest over the real property;
 - (D) creating, or permitting the continuation of, any right or interest in or over the real property, or any right to use any of the real property, except in the ordinary course of business of the scheme and in accordance with the scheme's governing document;
 - (E) agreeing to do any of the things referred to in subparagraphs (A) to (D); and
- (c) the encumbrance or mortgage is otherwise in a form and on terms approved in writing by the supervisor of the scheme; and
- (d) the manager has, before or within 3 months after the effective date, sent scheme participants a written notice—
 - (i) notifying them that the scheme is relying on the exemption in clause 6 from the usual legal requirement that the scheme's real property must be held by the independent licensed supervisor or an independent custodian (to the extent that the property is not held directly by scheme participants); and
 - (ii) giving them a brief explanation of the nature and effect of that exemption and the conditions that apply under this clause.

Exemption from daily cash reconciliation requirement

8 Exemption from daily cash reconciliation requirement

Every custodian of a property scheme, other than a scheme in respect of which the manager is exempt from the requirement to have a licensed supervisor under an exemption granted under Part 9 of the Act, is exempted from regulation 86(3) of the Regulations in respect of that scheme.

9 Condition of exemption in clause 8

- (1) The exemption in clause 8 is subject to the condition that the custodian must reconcile all records of money for the scheme with a frequency that the custodian reasonably determines, in accordance with regulation 86(2) of the Regulations and subclause (2), to be appropriate for the purpose of ensuring that the custodian's records accurately state the scheme's money and all transactions relating to that money.
- (2) For the purposes of determining the appropriate frequency for reconciling records of money for the scheme, the custodian must—
 - (a) consider the frequency, value, and volume of the transactions in respect of the scheme's property; and
 - (b) consider, whenever there is a material change in the frequency, value, or volume of cash transactions, and in any case not less than annually, whether reconciliations are being carried out with appropriate frequency; and
 - (c) consult the manager of the scheme (and the supervisor, if the supervisor is not the custodian); and
 - (d) act to the standard of a prudent and professional custodian.

Exemption from annual assurance engagement requirement

10 Application of exemption from annual assurance engagement requirement

- (1) The exemption in clause 11 applies to a custodian of a property scheme in respect of the most recently completed relevant period if, on the relevant date,—
 - (a) the manager of the scheme is not large; and
 - (b) the manager is not exempt in respect of the scheme from the requirement to have a licensed supervisor under an exemption granted under Part 9 of the Act.
- (2) A manager of a property scheme is **large** for the purposes of subclause (1)(a) if, as at the relevant date, the total gross value of assets under management by the manager in respect of property schemes that are registered schemes is not less than \$200 million (calculated in accordance with generally accepted accounting practice).

11 Exemption from annual assurance engagement requirement

Every custodian of a property scheme to which the exemption in this clause applies is exempted, in respect of that scheme, from regulation 87(1) of the Regulations in respect of the most recently completed relevant period.

12 Conditions of exemption in clause 11

- (1) The exemption in clause 11 is subject to the conditions that, if this subclause applies,—
 - (a) the custodian must, within 4 months after the relevant date, obtain an assurance engagement with a qualified auditor for the most recently completed relevant period (done in accordance with applicable auditing and assurance standards) that—
 - (i) covers custody of scheme property held by that custodian and scheme property held by any sub-custodian appointed by the custodian; and
 - (ii) complies with the requirements of regulation 88 of the Regulations; and
 - (b) the custodian must, within 20 working days after obtaining an assurance report required by paragraph (a), provide a copy of the assurance report to each of the relevant persons as if it were a report required by regulation 87(1) of the Regulations.
- (2) The conditions in subclause (1) apply if, before the relevant date, the supervisor, acting in its capacity as the licensed independent supervisor of the scheme, reasonably determines that it would be desirable to obtain an assurance engagement for the relevant period ending on that relevant date to provide reasonable assurance in respect of the matters provided for in regulation 88 of the Regulations, after the supervisor has had regard to—
 - (a) the nature and value of the scheme property; and
 - (b) whether there are any circumstances that are likely to increase or mitigate risks in relation to custody of the scheme property.
- (3) The conditions in subclause (1) do not apply to a sub-custodian (A) if the custodian that appointed A has complied with the condition in respect of the scheme property held by A.

13 Time frame extended because of outbreak of COVID-19

- (1) This clause applies if a custodian that is exempted under clause 11 believes, on reasonable grounds, that it is not reasonably practicable for it to comply with clause 12(1)(a) within 4 months after the relevant date because of the outbreak of COVID-19.
- (2) The period for compliance in clause 12(1)(a) is extended to 6 months after the relevant date if the custodian gives to the FMA, within 4 months after the relevant date, a written notice that states that the custodian is relying on this clause.

- (3) If subclause (2) would otherwise require the 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.
- (4) This clause applies in relation to relevant periods that end on or after 31 December 2019 but before 1 August 2020.

Clause 13: inserted, on 29 April 2020, by clause 27 of the Financial Markets Conduct (Financial Reporting and Other Relief—COVID-19) Exemption Notice 2020 (LI 2020/71).

Dated at Auckland this 16th day of November 2016.

Nick Kynoch,
General Counsel.

Statement of reasons

Note: the following statement of reasons should be read in conjunction with the statement(s) of reasons appended to:

- **Financial Markets Conduct (Financial Reporting and Other Relief—COVID-19) Exemption Notice 2020**

This notice comes into force on 18 November 2016 and is revoked on the close of 17 November 2021. The notice applies to managed investment schemes that meet the following 2 criteria:

- the principal investment policy and objectives of the scheme are to invest, in the ordinary course of business, in residential or commercial real property with the intention of earning a return on the investment through leasing the real property or through the future resale of that real property, or both; and
- the scheme is not a managed fund.

This notice exempts managers, supervisors, and custodians of these schemes, on conditions, from certain requirements under the Financial Markets Conduct Act 2013 (the **FMC Act**) and the Financial Markets Conduct Regulations 2014 for the scheme's real property to be held by the supervisor or other independent person (to the extent that the property is not held directly by the scheme participants), for an annual audit of custodial processes, procedures, and controls, and for daily reconciliation of scheme cash records. The main effects of the notice are that—

- existing property schemes that are closed to new investment and that transition to the FMC Act will not be required to have real property assets held by the scheme's supervisor, or other independent person, provided that there is an encumbrance or a mortgage registered over that real property in favour of the supervisor:

- custodians of property schemes will not be required to reconcile scheme cash records daily providing that those records are reconciled with a frequency suited to the level of transactions for the scheme:
- custodians of some property schemes will not need to have an annual assurance engagement with a qualified auditor of their processes, procedures, and controls in relation to the scheme property providing that they obtain an assurance engagement when the supervisor determines that this is desirable in the circumstances to provide reasonable assurance in relation to custody of the scheme property. This relief will not apply to schemes managed by a large manager (that is, a manager with more than \$200 million assets under management for registered property schemes).

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

- in general, the exemptions will reduce compliance costs for property schemes by relieving them of certain obligations that are not required, in view of the particular characteristics of these schemes, to ensure that appropriate governance arrangements are in place to allow for effective monitoring and reduce governance risks:
- in relation to the exemptions from independent custody requirements, property schemes generally invest most of their assets into real property assets that are held for a lengthy period and can only be transferred or otherwise dealt with through registration of an instrument under the Land Transfer Act 1952. In view of this, requirements for independent custody of the scheme's real property may not be needed to ensure effective monitoring and reduce governance risks providing the real property is held on trust and there is a registered mortgage or encumbrance over the property in favour of the supervisor to protect scheme participants' interests:
- in relation to the exemption from the daily cash reconciliation requirement, property schemes typically have a low volume and frequency of transactions, and daily reconciliation of records of money for the scheme by the custodian is unlikely to be required to ensure that the records accurately state the scheme's money and all transactions relating to that money, providing those records are reconciled with a frequency suited to the level of transactions for the scheme:
- in relation to the exemption from the annual assurance engagement requirement,—
 - a custodian's processes, procedures and controls are likely to be less complex for property schemes in view of their investments, and risks in relation to custody of the scheme's assets are likely to be reduced. In these circumstances, and where the annual audit of scheme financial statements provides regular independent verification in relation to the scheme property, an annual assurance engagement may not be required

unless the scheme is managed by a large manager (that is, a manager with more than \$200 million assets under management for registered property schemes):

- adequate protection will be provided for scheme participants in relation to custody of the scheme’s assets if an assurance engagement is obtained when the supervisor determines that circumstances have resulted in increased risks for custody of scheme property and therefore the value to investors of an assurance engagement outweighs costs. Supervisors are well placed to decide when an assurance engagement is needed, given their independence, licensed status, and statutory duties to act in the best interests of scheme participants and to carry out their functions and duties to a professional standard of care.

Therefore, the FMA is satisfied that—

- granting the exemptions is necessary or desirable in order to promote the purposes of the FMC Act. Specifically, the exemptions will—
 - promote the confident and informed participation of businesses, investors, and consumers in the financial markets; and
 - avoid unnecessary compliance costs; and
 - promote innovation and flexibility in the financial markets; and
 - ensure that appropriate governance arrangements apply to financial products that allow for effective monitoring and reduce governance risks; and
- the exemptions are not broader than is reasonably necessary to address the matters that gave rise to the exemptions because—
 - the exemptions are restricted to property schemes, which have special characteristics due to the nature of their investments; and
 - the exemptions from independent custody apply only to custody of real property for existing closed property schemes where there is a registered encumbrance or mortgage over that property in favour of the supervisor; and
 - the annual assurance engagement exemption does not apply to schemes that have a large manager (that is, a manager with more than \$200 million total assets under management for registered property schemes); and
 - alternative requirements apply for custodians relying on the exemptions from daily cash reconciliations and annual assurance engagements.

Note: the preceding statement of reasons should be read in conjunction with the statement(s) of reasons appended to:

- **Financial Markets Conduct (Financial Reporting and Other Relief—COVID-19) Exemption Notice 2020**

Issued under the authority of the Legislation Act 2019.
Date of notification in *Gazette*: 17 November 2016.

Notes

1 *General*

This is a consolidation of the Financial Markets Conduct (Property Schemes—Custody of Assets) Exemption Notice 2016 that incorporates the amendments made to the legislation so that it shows the law as at its stated date.

2 *Legal status*

A consolidation is taken to correctly state, as at its stated date, the law enacted or made by the legislation consolidated and by the amendments. This presumption applies unless the contrary is shown.

Section 78 of the Legislation Act 2019 provides that this consolidation, published as an electronic version, is an official version. A printed version of legislation that is produced directly from this official electronic version is also an official version.

3 *Editorial and format changes*

The Parliamentary Counsel Office makes editorial and format changes to consolidations using the powers under subpart 2 of Part 3 of the Legislation Act 2019. See also PCO editorial conventions for consolidations.

4 *Amendments incorporated in this consolidation*

Financial Markets Conduct (Financial Reporting and Other Relief—COVID-19) Exemption Notice 2020 (LI 2020/71): clause 27

Financial Markets Conduct (Property Schemes—Custody of Assets) Exemption Notice 2016 (LI 2016/266): clause 3