



**Ministry of Business,  
Innovation & Employment**

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# **KiwiSaver (Periodic Disclosure) Regulations 2012**

## **Exposure Draft**

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**Request for submissions and guide for submitters**

**Draft October 2012**

**ISBN 978-0-478-38267-9**

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First Published 8 October 2012

Investment Law  
Ministry of Business, Innovation and Employment  
PO Box 1473  
Wellington  
New Zealand  
<http://www.med.govt.nz>

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## Request for submissions

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The Ministry seeks comments on the attached exposure draft of the KiwiSaver (Periodic Disclosure) Regulations 2012. The focus of this consultation is on the technical details of the regulations, rather than policy. Policy issues were consulted on in a discussion document in November 2010. A Cabinet paper containing policy decisions was published in May 2012 and is available at <http://www.med.govt.nz/business/business-law/current-business-law-work/kiwisaver/period-disclosure>.

### When preparing your submission, please:

- **Direct your comments to specific clauses, in clause order.**
- **Use the accompanying template submissions table where practicable.**

This will help your comment to be processed, understood and taken into account.

Please send submissions to:

Email: [investment@med.govt.nz](mailto:investment@med.govt.nz) (preferred)

Post: KiwiSaver Periodic Disclosure Regulations  
Investment Law  
Ministry of Business, Innovation and Employment  
PO Box 1473  
Wellington

Fax: 04 499 1791

The last date for submissions is 5 November 2012.

### ***Publication of submissions, the Official Information Act and the Privacy Act***

The Ministry intends publishing all submissions on its website, other than submissions that may be defamatory. The Ministry will not publish the content of your submission on the Internet if you state that you object to its publication when you provide it.

However, it will remain subject to the Official Information Act 1982 and may, therefore, be released in part or full. The Privacy Act 1993 also applies. When making your submission, please state if you have any objections to the release of any information contained in your submission. If so, please identify which parts of your submission you request to be withheld and the grounds under the Official Information Act for doing so (e.g. that it would be likely to unfairly prejudice the commercial position of the person providing the information).

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## **Part 1: Where are we up to and what are the next steps?**

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### ***Background***

- 1 In April 2010, Cabinet agreed that regulations should be prepared to require all retail KiwiSaver schemes to make periodic reports about fund performance and fees available to investors, the regulator and the public.
- 2 In November 2010 the Ministry of Economic Development (MED, now part of the Ministry of Business, Innovation and Employment) released a discussion document for public consultation.
- 3 The Ministry received 37 submissions (34 of which are available on the MED website). In general, the submitters agreed that there was a need for regulations which require KiwiSaver funds to report consistent and comparable information. However, there were a range of views on the specific requirements, such as what information should be disclosed, how it should be calculated and in what format it should be presented.
- 4 Following feedback on the discussion document, further discussions with stakeholders and consideration of the approaches used in other countries, the Ministry developed a proposal for the content of the reports.
- 5 In March 2012, Cabinet agreed on much of the detail of the reports. Cabinet invited the Minister of Commerce to issue drafting instructions and authorised the Ministry to consult on the draft regulations. The Cabinet paper was publicly released in May 2012. This exposure draft reflects the recommendations in the Cabinet paper.

### ***Next steps***

- 6 Following this round of consultation, the Ministry will consider all submissions and revise the draft regulations before submitting them for approval. We anticipate the following timeline:
  - 5 November 2012 – submissions on the exposure draft close;
  - December 2012 – regulations signed into law;
  - the first quarterly disclosure statement (QDS), relating to the 12-month period ended 30 June 2013, to be due on 12 July 2013; and
  - the first annual disclosure statement (ADS), relating to the 2013-2014 tax year, to be due on 30 June 2014.

## Part 2: Key features of the exposure draft

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- 7 The purpose of these regulations is to require all retail KiwiSaver schemes to publish consistent and comparable information about their funds to enable KiwiSaver members to make better informed decisions. The regulations will require KiwiSaver schemes to report information on returns, fees and costs, assets and portfolio holdings, liquidity and liabilities, and key personnel, along with any conflicts of interest, in a standardised manner for each fund.
- 8 Disclosure of this information is important for a competitive KiwiSaver market. It increases transparency, enabling investors to compare different funds and to make more informed and efficient investment decisions. Ensuring confidence in retail KiwiSaver schemes is important for national savings and economic growth.
- 9 Cabinet's decisions on the March 2012 Cabinet paper were reasonably specific in the items that would be disclosed. The purpose of this document is, therefore, to consult on the detail of the regulations, to ensure that disclosures are workable and comparable.

### **Key issues**

#### **Use of international standards**

- 10 The draft regulations contain a mix of international standards that we have selected to suit New Zealand's retail KiwiSaver context. For example, the Global Investment Performance Standards (GIPS) are a set of ethical principles that provide investment firms with guidance on how to calculate and report their investment results to prospective clients, primarily in wholesale managed funds markets. The International Organisation of Securities Commissions (IOSCO) standards provide guidance to regulators on particular issues such as presentation of performance and the calculation of fees and expenses.
- 11 Aspects of these standards are incorporated into the draft regulations. For fees, the regulations have followed the IOSCO standard for calculation of a total expense ratio. For returns, the regulations use time-weighted returns as required by GIPS, and have also followed its treatment of trading expenses in reporting gross and net returns. We do not consider that there are any standards we can adopt in their entirety as each standards system differs in purpose and scope from the draft regulations.
- 12 However, the regulations may be able to integrate additional concepts from international standards. We welcome feedback on areas where this may be the case.
- 13 The Financial Markets Authority (FMA) will also have a role in providing further detail through non-binding guidance, and binding frameworks and methodologies. Some examples may include valuation of assets to ensure comparability and resolving ambiguities in the definitions of asset classes. FMA notices may provide a better way to incorporate the most detailed aspects of international standards into the reporting framework, rather than doing so in regulations.

#### **Data availability issues**

- 14 We understand that providers may face difficulties collecting information in the exact categories and time periods prescribed in the exposure draft.
- 15 Currently, the exposure draft makes allowances for limited or imperfect information in clause 23 in relation to providing the "best estimate" of fees when actual figures for some categories are unavailable (e.g. underlying manager fees). We invite submitters to identify other areas where it may be exceptionally costly or difficult to provide actual figures and therefore a "best estimate" allowance may also be necessary. However, we intend that providers source actual figures where possible.

- 16 In addition, we are considering requiring explanatory footnotes when estimates are used. This would help to inform readers of the robustness of the estimates used.

### **Reporting frequency and timeliness**

- 17 The draft regulations require KiwiSaver schemes to publish five disclosure statements per year for each fund. This comprises:
- one comprehensive disclosure statement, relating to the tax year (known as the annual disclosure statement, or ADS), to be made publicly available within 60 working days after the end of the tax year; and,
  - four briefer disclosure statements, relating to the 12-months preceding the end of each quarter of the tax year (known as the quarterly disclosure statement, or QDS), to be made publicly available within 10 working days after the end of each quarter of the tax year.
- 18 The relatively short deadline for the QDS reflects the appeal of up-to-date information on the performance of members' investments. Because detailed information on fees (particularly fees of underlying funds) can take longer than 10 working days to compile, the fees presented in the QDS repeat the fees information as contained in the latest ADS.
- 19 The 60 working day deadline is therefore set so that the ADS fees information is available for the QDS at the end of the first quarter of the following tax year.

## Part 3: Commentary on specific clauses

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### **Clause 3 – Application**

- 20 The regulations apply for the 2013-2014 and each later tax year. The intention is for:
- the first QDS, relating to the 12-month period ended 30 June 2013, to be due on 12 July 2013; and
  - the first ADS, relating to the 2013-2014 tax year, to be due on 30 June 2014.
- 21 The QDS replicates some information contained in the latest ADS, including much of the information about fees. Because providers will have not yet published an ADS at the time the first QDS is due, providers will need to calculate some information relating to the 2012-2013 tax year for inclusion in the first four QDSs. Clause 46 clarifies this point.

### **Clause 4 – Interpretation**

- 22 **Definition of “fund”:** The exposure draft concept of a fund is intended to divide KiwiSaver schemes into funds – conservative, balanced, growth, etc. – in accordance with common industry practice and the level at which investors might usefully compare performance and fees to make investment decisions. We note that some KiwiSaver schemes allow members to invest in multiple funds. In such cases, the desire was to allow reporting in respect of each fund, and not to adopt a definition that would require disclosure for each individual’s mix of funds. A few schemes also allow members to select individual securities; these are also intended to be excluded from fund-level disclosure.
- 23 Note that this definition differs from the definition of a “separate fund” in section 9A of the Financial Reporting Act 1993, which is where “the liabilities of the issuer or the scheme are limited to [a particular group of assets]”. It appears that for some KiwiSaver schemes, the Financial Reporting Act definition has been interpreted as implying that the scheme’s assets need not be grouped into separate funds.<sup>1</sup>

### **Clause 5 – Compliance with notices issued by the FMA and generally accepted accounting practice**

- 24 Clause 5(b) requires that assets and liabilities be valued in accordance with generally accepted accounting practice. The exposure draft does not provide further requirements for valuation, which can affect reported returns, and (to a lesser extent) figures that are expressed as a proportion of net assets.
- 25 We welcome feedback on whether additional requirements should be specified for the valuation of assets and liabilities. An alternative, more flexible option would be for the FMA to issue binding frameworks and methodologies on this.

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<sup>1</sup> See, for example, ASB KiwiSaver Scheme’s Annual Accounts for the year ended 31 March 2012, page 6: “In accordance with the Trust Deed the liabilities of the issuer, ASB Group Investments Limited, and the Scheme, are not limited to a particular group of assets in an individual fund of the Scheme. The results of the Scheme’s funds have been disclosed in the financial statements to provide more useful and meaningful information to the user of the financial statements of the Scheme”.

### ***Clause 6 – Meaning of publicly available***

- 26 The regulations require providers to submit disclosure statements to the FMA, to publish them on their websites and to provide a hard copy on request.
- 27 The regulations do not require providers to publish the information in an electronic format that allows for automated data extraction. Such a requirement would help reduce the costs for third parties maintaining databases of the information contained in the reports and providing summary and comparative information to the public. We seek comment on the likely additional costs that such a requirement would impose on providers.

### ***Clause 12 – When quarterly disclosure statements are to be completed***

- 28 As discussed in paragraph 20 above, Cabinet has decided to require the publication of QDS within 10 working days after the end of each quarter of the tax year. Given that the QDS for the first quarter of each tax year requires information from the ADS relating to the previous tax year, the 10 working day requirement essentially dictates the 60 working day requirement for the ADS.

### ***Clause 17 – Meaning of return and treatment of trading expenses***

- 29 The regulations adopt the time-weighted method of calculating returns (also used by GIPS). A time-weighted return is suitable for most retail KiwiSaver schemes because fund managers tend to have limited control over contributions and withdrawals of members' funds.
- 30 Trading expenses are not included in fees and costs due to the difficulties involved in calculating them (consistent with GIPS). Trading expenses will still reduce both gross and net returns, therefore fund managers still have an incentive to minimise trading expenses. In place of disclosure of trading expenses, the regulations require providers to disclose the portfolio turnover of the fund, as is required in the United States (see clause 31). This provides some indication of comparative trading expenses between funds and an aspect of the fund's investment strategy over the period.

### ***Clause 18 – Performance and returns example***

- 31 A main component of the disclosure statements is a description of returns and fees in the form of a worked example. In the example, a hypothetical member has \$10,000 invested in the fund at the start of the period, does not make any contributions or withdrawals and does not incur any individual fees. The example focusses on net returns, and shows how gross returns are reduced by fees and tax. This is to enable better comparability between returns and fees in a more understandable format to members.
- 32 The calculation of tax is problematic due to the different prescribed investor rates (PIRs) that can apply to members. We have therefore stipulated that the worked example must use the highest prescribed investor rate for a New Zealand resident individual as at the last day of the period to which the disclosure statement relates.
- 33 We note that in PIEs, taxable returns differ from gross or after-fee returns. Some returns are taxed at the PIR; other returns are not taxable and there is also use of the fair dividend rate (FDR) method of calculating taxable returns under the Foreign Investment Fund (FIF) rules. The calculation of tax is intended to reflect the tax that would have been deducted from the hypothetical member's returns.



### ***Clause 19 – Fund’s returns***

- 34 The regulations require actual fees and costs charged to all members of the fund be calculated as a percentage of the average net asset value, along with the actual tax paid as a percentage of the average net asset value of the fund.
- 35 The formula for calculating the average net asset value has been designed to take account of funds that have not been in existence for the full 12-month period to which the disclosure statement relates.

### ***Clause 20 – Graphs showing historical annual information***

- 36 The disclosure statements must include a bar graph showing the returns, net of fees and costs, and gross of tax, for each complete tax year that the fund has existed, up to 10 complete tax years. It also requires a bar that shows the annual compound return since the start of the fund. Due to changes in tax rates over time, the return is presented gross of tax.
- 37 The disclosure statements must also include a bar graph showing fees and costs charged to all members as a percentage of the average net asset value, for each complete tax year that the fund has existed, up to 10 complete tax years. A bar that shows the average annual fees and costs as a percentage of the average net asset value is also required. This is intended to be a simple average of the figure for each year.

### ***Clause 22 – Categories of fees and costs***

- 38 For the purposes of these regulations, fees and costs fall into the following four categories:
- **Fund fees and costs** (defined in clause 23);
  - **Membership fees** (defined in clause 24);
  - **Individual fees** (defined in clause 25); and
  - **Trading expenses** (defined in clause 4).
- 39 However, as noted in clause 17, trading expenses are not included in fees and costs as disclosed or used in these regulations due to the difficulty in accurately measuring or estimating them.

### ***Clause 23 – Information about fund fees and costs***

- 40 The regulations define fund fees and costs as those that affect all members in proportion to their interest in the fund. These represent both fees that are charged on the basis of net asset value (e.g. management fees), but also costs that are deducted from the fund’s assets as a whole. These fees are required to be divided into the specific sub-category that applies.
- 41 Acknowledging that in some cases it may be unacceptably costly to compile fees information into the categories prescribed in the draft regulations, and that there may be delays in collecting fees information (e.g. from underlying funds), the regulations allow the use of the best estimate of fees when actual figures are not available.
- 42 The regulations also require underlying manager fees to be disclosed. This is important for enabling a full comparison of fees between funds. Disclosure of underlying manager fees will provide better information for members’ decisions.

43 In addition, the definition of underlying manager fee in clause 4 requires these fees to be disclosed in any other category or sub-category in regulation 23(2) where possible. This may create differences in the way funds report this information and make it difficult to compare. For example, some funds may collect a full breakdown of underlying manager fees while others may not. To make the regulations clearer and to ensure consistent treatment of underlying manager fees, we are considering three options:

- Retaining the current drafting. That is, requiring fees of underlying fund managers to be allocated to any other appropriate category in 23(2) when possible, and aggregated into category 23(2)(b) when not (for example, when fees charged by the underlying fund manager are provided only in aggregate or do not easily fit into the fee categories in the exposure draft).
- Requiring all underlying manager fees to be allocated to any other appropriate fee category in 23(2) when possible, but disclosed separately from the fees of the top level fund, for example in another column in the fees table (Schedule 1, Table 3); or
- Requiring all underlying manager fees to be combined into category 23(2)(b) and not distributed across any other fee category.

#### ***Clause 24 – Information about membership fees***

44 This clause requires information about fees charged in respect of a person's membership in the scheme. It requires both the average membership fee charged to an individual member and the total membership fees charged to all members as a percentage of the average net asset value of the fund.

#### ***Clause 25 – Information about individual fees***

45 The individual fees category is intended to capture other fees and costs charged to members on an individual basis, generally for member-specific decisions. The ADS requires the total of individual fees charged to members as a percentage of the average net asset value of the fund. In the ADS and the QDS, the rate at which these fees are charged is required to be disclosed.

#### ***Clause 27 – Total expense ratio***

46 The regulations require the calculation of a total expense ratio based on IOSCO standards.

#### ***Clause 28 – Information about fees and costs that must be included in quarterly disclosure statements***

47 In the case of the QDS, the information on fund fees and costs, membership fees, and fees and costs charged to all members of the fund is taken from the last ADS. These include figures for fund fees and costs and membership fees in the hypothetical member example (Schedule 1, Table 1) and total fees and costs charged to all members of the fund (Schedule 1, Table 2).

48 The regulations do not require providers to recalculate these figures for each 12-month period to which the QDSs relate. This provision is intended to reduce the compliance burden on providers. We consider that this provision may reduce the usefulness of the QDS, particularly the fourth quarter statements (for the 12-month period ended 31 March 2012) which will contain fees and costs information that is over a year old.

49 We are interested in feedback on the likely benefits of providing more up-to-date fees and costs information in the QDS and also the likely additional burden on providers of providing this information. For example, some providers may need to calculate fees and costs quarterly in any case, in order to calculate gross returns.

### ***Clause 30 – Information about asset allocation and portfolio holdings***

- 50 Information on the composition of assets held by the fund will assist members to assess the suitability of the fund's investment strategy and level of risk. The regulations require the fund to disclose a list of the top 10 assets held by the fund, in addition to a pie graph showing the composition of assets in the fund. To assist comparison between funds, providers must use the prescribed list of asset categories. We welcome feedback on whether any changes should be made to the prescribed asset categories.
- 51 Providers must also disclose the target asset allocation in the same categories.

### ***Clause 31 – Portfolio turnover***

- 52 As discussed in paragraph 30 above, portfolio turnover provides an indication of comparative trading expenses between funds and an aspect of the fund's investment strategy over the period.
- 53 We understand that there are other methods for calculating portfolio turnover which may be more appropriate. For example, the methodology used by the UK removes the effect on portfolio turnover resulting from member contributions and withdrawals (e.g. by subtracting contributions to the fund from the fund's purchases, and subtracting withdrawals from the fund from the fund's sales). This may be more appropriate as some turnover may be required following member contributions and withdrawals, which are outside of the fund manager's control.

### ***Clause 32 – Additional information about assets that must be included in annual disclosure statement***

- 54 The regulations require funds to disclose a full list once per year of all assets held by the fund. Full disclosure of the assets held by underlying funds is also required, unless that information is already available to the public or represents less than 5% of the total asset value of the fund.

### ***Clause 34 and 35 – Liquidity and debt ratio***

- 55 The liquidity ratio is calculated as the proportion of assets that could be liquidated within 5 working days without materially affecting the price of any asset. We invite feedback on whether there is a better summary measure of fund liquidity and/or whether a different timeframe would be more appropriate.
- 56 We also invite feedback on whether or not the disclosure statements will provide sufficient information on the assets held by the fund to assess the liquidity of underlying assets, particularly when a fund holds unlisted managed funds which fall below the 5% threshold for full disclosure.
- 57 It is not expected that all investors will be interested in the liquidity and debt ratios. However, disclosure will enable advisers, commentators and regulators to assess the fund's strategy and alert investors to funds with high leverage ratios or large holdings of illiquid assets and the risks associated with them.

### ***Clause 37 – Information about key personnel***

- 58 A fund's performance is dependent on the people making the investment decisions regarding the fund. The experience and history of the managers may therefore influence investors' decision making, particularly in the case of funds that market themselves based on their personnel.

### ***Clause 43 – Formatting***

- 59 The draft regulations prescribe how the reports are required to be formatted. Reports must use the same headings, explanatory words, layout and borders as in the example disclosure statements (except where information specific to the report itself is required). In addition, the reports must not include any information that is not required by the regulations.
- 60 In some cases, minor variations from the required format may be necessary to ensure that the statements are not misleading. The regulations also allow minor variations for different fonts and font sizes and the extension of tables and graphs to provide sufficient space for the completion of the information required.
- 61 There may be additional areas of presentation that need flexibility for minor variations, such as the inclusion of branding and use of different borders. We invite comment on areas where this may be the case.

### ***Schedules***

- 62 We welcome feedback on changes that can be made to the tables in Schedule 1, and the example ADS and QDS in Schedule 2 and 3, to improve the usefulness and comprehensibility of the statements to potential readers.

