

# New Derivatives Regulations in Effect for Issuers to NZ Clients

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Photo: Bloomberg

Starting today, all derivatives issuers (issuers) who make regulated offers to New Zealand clients must be licensed by the New Zealand Financial Markets Authority (FMA).

Previously, financial services entities were able to obtain Financial Services Provider (FSP) registration and offer short-term derivative contracts (i.e. those that are settled within 3 days) to both retail and wholesale clients based in New Zealand without the need to be formally licensed by the FMA.

This meant that these entities could operate a trading platform with limited regulation in a respected jurisdiction. However, the lack of regulation around short-term derivative trading and other derivative products led to a vast number of retail client complaints to the FSP.

The FMA attributes this large number of client complaints to the number of unlicensed issuers, such as online foreign exchange traders, who targeted the New Zealand retail market. The lack of licensing meant that it was very difficult for clients to recover their money from these entities and the lack of regulation meant that the FMA did not have the jurisdiction to assist clients with this recovery.

The FMA has addressed these issues through new licensing requirements for short-term Issuers.

## Who must be licensed?

Any issuer who wishes to make a regulated offer of derivatives (including short-term derivatives) to one or more New Zealand clients, regardless of whether the issuer itself is based in New Zealand or abroad, must be licensed by the FMA.

An offer of derivatives exclusively to wholesale clients in New Zealand will not be a regulated offer under the Financial Markets Conduct Act 2013 ("the Act"). However, if even one client in a group of clients to whom an offer is made is a type that would require disclosure, for example a retail client, then the whole offer will be regulated and the issuer must be licensed as well as registered with the FSP.

It is therefore possible to offer derivatives to New Zealand-based wholesale clients, without requiring a FMA license, however the issuer would need to have compliance protocols in place to ensure that the offer is only made to wholesale clients and that there were no circumstances in which a retail client could receive and accept such an offer, and this may be rather an onerous exercise for the Issuer.

### What is a derivative?

Section 8(4) of the Act provides a broad definition of 'derivatives' that includes:

- Futures contracts and forwards;
- Options (except options to acquire an equity security, a debt security, or a managed investment product by way of issue);
- Swaps;
- Contracts-for-difference (CFDs), margin contracts and rolling spot contracts; and
- Caps, collars, floors and spreads.

### What is a regulated offer?

A regulated offer, as defined by s41 of the Act, is any offer of derivatives where disclosure must be made to one or more investors, Pursuant to the Act an 'offer' includes:

- Inviting applications for the issue of financial products; and
- Inviting applications to purchase financial products.

### What steps do issuers need to take?

Given the new rules, issuers with New Zealand-based clients who are not currently licensed by the FMA have two options:

1. Close the accounts of all New Zealand based clients and not on-board any future New Zealand clients. This is likely to be the simplest approach depending on the number of clients and their trading volume.
2. Apply to the FMA for an Issuer license and comply with the relevant FMC Act obligations.
3. FMA had previously advised issuers to start their licensing process by 1 August 2017, on the basis that it would not be possible to start the licensing process now and meet the December deadline. That being said, issuers may still apply for a license but cannot make a regulated offer of derivatives to New Zealand clients from 1 December 2017 until their license is granted.

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