

GILBERT ' SWAN

Barristers & Solicitors

06 July 2001

Mr John Farrell
Chief Executive
Securities Commission
12th Floor
Reserve Bank Building
2 The Terrace
WELLINGTON

Dear Sir

Re: Trustees & Statutory Supervisors - Invitation to Comment
OurRef: ASF039/2

We refer to your letter of 25 May 2001 addressed to the Association of Superannuation Funds of New Zealand (ASFONZ).

We submit with this letter comments prepared on behalf of ASFONZ.

Yours sincerely

ASSOCIATION OF SUPERANNUATION FUNDS OF NEW ZEALAND

**Comments on Review of Policy for the Appointment of
Trustees and Statutory Supervisors**

General

ASFONZ represents employer sponsored superannuation schemes. These schemes have trustees and are governed by trust deeds. However, the functions of such trustees are different from the statutory role given to trustees (and statutory supervisors) appointed under section 48 of The Securities Act 1978 ("the Act").

In this paper, a reference to a "trustee" is therefore a reference to a company appointed as a trustee under the Act. To differentiate between such a trustee, and the form of trustee familiar to superannuation schemes, we shall include the latter in the generic term "superannuation schemes".

ASFONZ's interest in the discussion is therefore as a representative of a group of investors. Superannuation schemes have investment responsibilities under The Trustee Act and under the trust deeds by which they are constituted. They represent professional investors concerned to see a properly regulated market.

As an overview, ASFONZ has the following comments concerning trustees appointed under the Act:

1. Such a trustee is more concealed than the usual trustee. In their initial offering of an investment its role is less clearly defined than that of the promoter.
2. The trustee is invariably one of the few authorised limited liability companies, and the use of the company structure makes the trustee less conspicuous or approachable than an individual trustee.
3. The individuals managing the operating company are more mobile than would be the case if individual persons were the trustees.
4. Recent experience has seen trustee companies sold and the function of the trustee assumed by a second company, the process undermining the individual investor's view of the stability of the trustee.
5. The use of a limited liability company diminishes the accountability of the individuals running the company.

The growth in emphasis on the use and content of investment statements and prospectuses are providing more information to the investing public, and thereby imposing a requirement for more professionalism from the trustee.

The trustees are seen not only as a vehicle for the aggregation of investors in one entity, but also as placing a control or brake on the activities of managers.

Discussion Questions

Part II

I. Is there a useful role for trustees and statutory supervisors to play in representing the interests of security holders?

Answer: There is perceived to be a very useful role for trustees and statutory supervisors to play in representing the interest of security holders.

II. If yes, in respect of question I, do the prescribed rights and duties of trustees and statutory supervisors empower them to adequately represent the interests of security holders?

Answer: There will always be a tension between the function of the trustee and that of the promoter of the particular investment. The promoter will inevitably seek to push the boundaries of any statutory or constitutional restraints.

It is the promoter that appoints the trustee. Thus the promoter can shop around for a compliant trustee. The promoter is also able to negotiate a soft trust deed that may well be of minimal assistance to investors. The trust deed will be negotiated at a time before investors are apparent, and it may be all too easy for minimal standards to be implemented.

Part III

III. Is there a need for a regulatory body to consider applications for approval of persons to act as trustees and statutory supervisors?

Answer: There is a clear need for a regulatory body to approve trustees and statutory supervisors. Under the present regime there is a degree of competition between the qualified entities. To dilute the number by opening the range must of necessity dilute the quality and experience of those available.

IV. If yes, in respect of question III, is the Commission the appropriate regulatory body to manage this process?

Answer: The Commission does seem appropriate to be the regulatory body to manage the process.

V. Are there more desirable alternatives to the present system of approval?

Answer: No comment.

Part IV

VI. Are the Commissioner's current criteria for the approval of trustees and statutory supervisors satisfactory?

Answer: The provision of professional indemnity cover should be one of the criteria for competence and financial capacity. Not only should there be supervision of a minimum level of PI cover, but there should also be ongoing supervision of its currency. Such supervision could be achieved by direct linkage to the underwriters.

VII. Are the Commission's current procedures for the approval of trustees and statutory supervisors necessary?

Answer: It is not apparent whether the Commission's current procedures place sufficient control over the continuity of directors and key management personnel through the vetting of new officers. The perception is that more should be done to supervise the maintenance of a level of relevant skills, qualifications and experience.

VIII. Should the Commission require an applicant to have a minimum amount of paid up capital?

Answer: There seems to be an inconsistency between the legislation dealing with the insurance industry, which requires a minimum amount of capital and a bond, and the subject legislation. This is especially true in view of the fact that the trustee companies are more often than not aligned with an insurance company.

IX. Should the Commission approve individuals to act as trustees?

Answer: It is difficult to see a situation where an individual would have the substance, skill and back-up necessary to function as a trustee.

X. *Is the dishonesty criterion (paragraph 38) satisfactory?*

Answer: One questions why the criteria only excludes someone who has been a bankrupt at any time during the last five years, where the other criteria do not have that time limit. One also questions how the expression "key management staff" is determined. What if an undesirable person was exercising control over a trustee, albeit indirectly? There should be a facility for the Commission to disqualify a trustee (and appoint a replacement) in circumstances where the trustee does not measure up.

XI. *Should the professional membership criterion (paragraph 39) be amended to allow applicants a greater level of flexibility in terms of their board membership?*

Answer: With the deregulation of the professions, a greater level of flexibility would seem appropriate.

XII. *Does the independence criterion (paragraphs 44 and 45) impose an unnecessary entry barrier to potential applicants or a business barrier to established trustees and statutory supervisors?*

Answer: The independence criterion seems desirable, and there seems to be no theoretical reason why new businesses should not enter the market.

XIII. *Should personal guarantees be required from applicants?*

Answer: The ability to seek personal guarantees, bonds or other such securities should be available to cover the circumstances of some applicants.

XIV. *Is the duration period of approvals (five years) too short, about right or too long?*

Answer: If there is ongoing oversight, a duration period for approvals is not appropriate.

XV. *Should approvals, of either trustees or statutory supervisors, be for an unlimited duration?*

Answer: Circumstances and personnel will change, and approvals should be reviewed.

Part V

XVI. *Is there a need for ongoing oversight of trustees and statutory supervisors?*

Answer: Yes, see above.

XVII. If yes, in respect of question XVI, is the Commission the appropriate body to conduct this role ?

Answer: There needs to be some statutory body overseeing the role. There seems no reason to change from the Commission as being the appropriate body to provide the oversight.

XVIII. If yes, in respect of question XVII, should the trustee/statutory supervisor be required to report to the Commission on the occurrence any change in matters material to the Commission's approval of that person and in any event, on an annual basis to the Commission?

Answer: Given the premise that there should be ongoing oversight, then it would be desirable to require reports of any changes in circumstances and in any event on an annual basis.

XIX. If yes, in respect of question XVIII, should such an annual report be made available to investors on request?

Answer: To better assure the confidence of the investing public, an annual report should be made available to investors on request, and in any event as an annexure to the annual report of the particular venture. There is a need for greater accountability and transparency in the function of trustees.