

# Departmental Disclosure Statement

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Financial Market Infrastructures Bill
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The departmental disclosure statement for a government Bill seeks to bring together in one place a range of information to support and enhance the Parliamentary and public scrutiny of that Bill.

It identifies:

- the general policy intent of the Bill and other background policy material;
- some of the key quality assurance products and processes used to develop and test the content of the Bill;
- the presence of certain significant powers or features in the Bill that might be of particular Parliamentary or public interest and warrant an explanation.

This disclosure statement was prepared by the Reserve Bank of New Zealand.

The Reserve Bank of New Zealand certifies that, to the best of its knowledge and understanding, the information provided is complete and accurate at the date of finalisation below.

4 December 2019

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## Part One: General Policy Statement

Financial market infrastructures (**FMI**s) are multilateral systems that provide trading, clearing, settlement, and reporting services in relation to payments, securities, derivatives, and other financial transactions. FMI

s include payment systems, securities settlement systems, central securities depositories, central counterparties, and trade repositories.

Well-managed and well-operated FMI

s are essential to the operation of a sound and efficient financial system, and the day-to-day operation of the economy. In particular, they provide much of the underlying infrastructure that enables non-cash payments and the settlement of financial market transactions. They also reduce transaction costs by supporting the management of counterparty risks and fostering transparency. Given the key role they play, the disruption or failure of important FMIs could have significant negative impacts on the financial system, businesses, and consumers.

The Financial Market Infrastructures Bill (the **Bill**) establishes a new regulatory regime for FMI

s. It also provides certain FMIs with legal protections relating to settlement finality, netting, and the enforceability of their rules.

The purposes of the Bill are to:

- promote the maintenance of a sound and efficient financial system;
- avoid significant damage to the financial system that could result from problems with an FMI, an operator of an FMI, or a participant of an FMI;
- promote the confident and informed participation of businesses, investors, and consumers in the financial markets; and
- promote and facilitate the development of fair, efficient, and transparent financial markets.

The Bill will replace Parts 5B and 5C of the Reserve Bank of New Zealand Act 1989 (the **RBNZ Act**).

### Regulator

The role of the regulator under the Bill is carried out by the Reserve Bank of New Zealand (the **Reserve Bank**) and the Financial Markets Authority (the **FMA**) acting jointly, except in relation to payment systems, where the Reserve Bank acts as the sole regulator.

Powers under the Bill will be exercised by the joint regulators and joint Ministers (that is, the Minister of Finance and the Minister of Commerce and Consumer Affairs), except in relation to pure payment systems, where powers will be exercised by the Reserve Bank and Minister of Finance alone.

### Designated and non-designated FMIs

The Bill provides for different treatment of designated and non-designated FMI

s. Designated FMIs will be FMIs that:

- are identified as systemically important and brought into the regime (as discussed further below); or
- have opted into the regime to access the settlement finality and netting protections that are currently included in Part 5C of the RBNZ Act and that will be carried across into the new legislation.

## **Regulation of designated FMIs**

### *Designation process*

Under the Bill, joint Ministers have the power to declare, on the recommendation of joint regulators, that an FMI is a designated FMI for the purposes of the Bill. The joint regulators may make this recommendation on their own initiative if they are satisfied that the FMI is systemically important (taking into account prescribed matters such as the concentration of financial risks in the FMI, and the nature and scope of the FMI's activities). Alternatively, an FMI may apply to the joint regulators for a recommendation to be made if it wishes to access the legal protections for designated systems (in this case the joint regulators will assess whether the FMI and its rules are sufficiently robust to justify the application of these legal protections).

### *Standards*

The Bill provides joint regulators with the power to make legally binding standards that apply to designated FMIs. The matters standards may relate to are designed to allow standards to be made in relation to any of the matters covered in the CPSS/IOSCO Principles for Financial Market Infrastructures. Standards may apply to all FMIs, a class of FMIs, or an individual FMI.

Standards are also disallowable instruments. These reason for these requirements being set by standards issued by the regulator rather than by regulations made by Order in Council are that:

- The requirements are relatively detailed technical matters, that are not subject to criminal sanctions;
- The requirements apply to a narrowly defined, clearly identifiable group (that is, designated FMIs); and
- The requirements are best made by the regulators given the technical expertise required and international best practice indicating that these types of requirements should be made by an independent body (or bodies).

### *General monitoring and oversight*

Under the Bill, joint regulators also have powers for monitoring and investigative purposes, including:

- the power to require operators or participants to provide information; and

- the power to require an operator to obtain a report from an independent expert on aspects of the FMI's business or operations; and
- the power to appoint an investigator to examine the financial position or operation of the FMI; and
- the power to seek a warrant to enter premises to obtain evidence relevant to an investigation.

#### *Oversight of rules*

The Bill provides that designated FMIs must provide any amendments to their rules to the joint regulators, and that rule changes for domestic designated FMIs must be approved by the joint regulators. The joint regulators also have the power to require the operator to prepare a rule change to ensure compliance with relevant standards and, where they consider the rule change is not adequate to ensure compliance, direct the operator to change the FMI's rules.

#### *Crisis management: FMI contingency plans*

Under the Bill, FMIs are required to have contingency plans for how they will deal with operational or financial failure. The crisis management powers in the Bill are expected to be used only in cases where these contingency plans are not being appropriately implemented or are inadequate to deal with the situation. The contingency plans to deal with financial failure are also expected to provide for rules for loss allocation among participants.

#### *Crisis management: direction powers*

The Bill provides joint regulators with the power to direct the operators of designated FMIs. The threshold for being able to issue directions includes the actual or potential insolvency of the operator, carrying on business in a manner that is prejudicial to the soundness of the financial system, or carrying on business fraudulently or recklessly. Directions may, for example, require participants to comply with the rules of the FMI, or appoint or remove the directors of an operator.

#### *Crisis management: statutory management*

The Bill establishes a tailored statutory management regime for FMIs, which also includes new powers such as the ability to transfer the FMI to a new operator under a new operator scheme.

### **Regulation of non-designated FMIs**

The joint regulators' powers in respect of non-designated FMIs are limited to information gathering and the ability to require operators of these FMIs to obtain an independent report in respect of the business or operation of the FMI. This reflects the fact that these FMIs are not systemically important and do not have access to the legal protections afforded to relevant designated FMIs.

These powers are intended to be used mainly for the purpose of monitoring the broader sector, and identifying whether an FMI has become systemically important (and so may need to be designated under the regime).

### **Enforcement and penalties**

The Bill provides for a graduated and flexible range of remedies for breaches of legal requirements imposed by or under the Bill. Specifically, -

- breaches of requirements imposed directly by the Bill result in criminal offences or civil pecuniary penalties depending upon the requirement in question, and breaches of requirements set in standards result in civil pecuniary penalties; and
- joint regulators have the ability to issue remedial notices requiring breaches to be corrected; and
- joint regulators have the ability to enter into enforceable undertakings.

### **Transitional arrangements and commencement**

Most of the Bill will come into force on a date or dates specified by 1 or more Orders in Council, but no later than 3 years after the date of Royal assent. This is necessary to give effect to the intended arrangements for implementing the Bill.

The following powers (and associated enforcement provisions) will come into force immediately:

- powers to require information, reviews, and independent reports (*Part 2*):
- power to designate FMIs for the purposes of the Bill (*clauses 20 to 29*):
- power to set standards (*clauses 31 to 34*).

A transitional period will then be used to designate relevant FMIs and issue the relevant standards. At the end of this period, the provisions relating to designation notices, standards, and settlement finality and the remaining provisions of the Bill will come into force and Parts 5B and 5C of the RBNZ Act will be repealed.

## Part Two: Background Material and Policy Information

### Published reviews or evaluations

<b>2.1. Are there any publicly available inquiry, review or evaluation reports that have informed, or are relevant to, the policy to be given effect by this Bill?</b>	<b>YES</b>
<p>The International Monetary Fund (IMF) carried out a Financial System Assessment Programme (FSAP) review of New Zealand in 2016/17. As part of that process, the IMF reviewed the current regulation and supervision of FMIs in New Zealand, and an earlier version of the proposals which are now included in the Bill. This resulted in the IMF publishing a technical note <a href="#">Regulation and Oversight of Financial Market Infrastructures</a> in May 2017, along with other reports arising out of the FSAP review.</p>	

### Relevant international treaties

<b>2.2. Does this Bill seek to give effect to New Zealand action in relation to an international treaty?</b>	<b>NO</b>

<b>2.2.1. If so, was a National Interest Analysis report prepared to inform a Parliamentary examination of the proposed New Zealand action in relation to the treaty?</b>	<b>NO</b>

### Regulatory impact analysis

<b>2.3. Were any regulatory impact statements provided to inform the policy decisions that led to this Bill?</b>	<b>YES</b>
<p>The Reserve Bank has prepared the Regulatory Impact Statement <a href="#">An Enhanced Oversight Framework for Financial Market Infrastructures</a> (published in April 2017) and the Summary Impact Statement <a href="#">Financial Market Infrastructures Bill: Additional Policy Decisions</a> (published in December 2019).</p>	

<b>2.3.1. If so, did the RIA Team in the Treasury provide an independent opinion on the quality of any of these regulatory impact statements?</b>	<b>NO</b>
<p>The Regulatory Impact Statement and Summary Impact Statement did not meet the threshold for Treasury RIA Team assessment.</p>	

<b>2.3.2. Are there aspects of the policy to be given effect by this Bill that were not addressed by, or that now vary materially from, the policy options analysed in these regulatory impact statements?</b>	<b>NO</b>

## Extent of impact analysis available

<b>2.4. Has further impact analysis become available for any aspects of the policy to be given effect by this Bill?</b>	<b>NO</b>

<b>2.5. For the policy to be given effect by this Bill, is there analysis available on:</b>	
<b>(a) the size of the potential costs and benefits?</b>	<b>YES</b>
<b>(b) the potential for any group of persons to suffer a substantial unavoidable loss of income or wealth?</b>	<b>NO</b>
Analysis of the costs and benefits of the policy to be given effect by this Bill is included in the Regulatory Impact Statement and Summary Impact Statement referred to in question 2.3.	

<b>2.6. For the policy to be given effect by this Bill, are the potential costs or benefits likely to be impacted by:</b>	
<b>(a) the level of effective compliance or non-compliance with applicable obligations or standards?</b>	<b>YES</b>
<b>(b) the nature and level of regulator effort put into encouraging or securing compliance?</b>	<b>YES</b>
<p>The Bill establishes a regulatory regime for Financial Market Infrastructures (FMIs) which imposes certain obligation on designated FMIs (as well as more minimal obligations on non-designated FMIs). The purposes of the Bill are to:</p> <ul style="list-style-type: none"> <li>• promote the maintenance of a sound and efficient financial system; and</li> <li>• avoid significant damage to the financial system that could result from problems with an FMI, an operator of an FMI, or a participant of an FMI; and</li> <li>• promote the confident and informed participation of businesses, investors, and consumers in the financial markets; and</li> <li>• promote and facilitate the development of fair, efficient, and transparent financial markets.</li> </ul> <p>In order to achieve these purposes the regulators (the Reserve Bank and Financial Markets Authority) will need to monitor compliance with, and enforce obligations imposed by or under the Bill. Initial estimates of the resourcing implications for the Reserve Bank and FMA are in paragraphs 115-118 of the Cabinet paper <a href="#">An Enhanced Oversight Framework for Financial Market Infrastructures</a>. Work on the detailed design of the regulators' supervisory approach under the Bill is ongoing.</p>	

## Part Three: Testing of Legislative Content

### Consistency with New Zealand's international obligations

#### 3.1. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations?

No policy measures in this Bill have been identified, as part of the normal policy process, as raising any questions of consistency with our international obligations. As a result, no separate formal steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations.

The global standard for the regulation of financial market infrastructures (the [Principles for Financial Market Infrastructures](#)) have been taken into account during the policy development process.

### Consistency with the government's Treaty of Waitangi obligations

#### 3.2. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with the principles of the Treaty of Waitangi?

The provisions of the Bill affect the New Zealand public as participants in financial markets and payment systems, and do not impact on the principles of the Treaty of Waitangi.

### Consistency with the New Zealand Bill of Rights Act 1990

#### 3.3. Has advice been provided to the Attorney-General on whether any provisions of this Bill appear to limit any of the rights and freedoms affirmed in the New Zealand Bill of Rights Act 1990?

YES

Advice provided to the Attorney-General by the Ministry of Justice is generally expected to be available on the Ministry of Justice's website at: <https://www.justice.govt.nz/justice-sector-policy/constitutional-issues-and-human-rights/bill-of-rights-compliance-reports/advice/>.

### Offences, penalties and court jurisdictions

#### 3.4. Does this Bill create, amend, or remove:

(a) offences or penalties (including infringement offences or penalties and civil pecuniary penalty regimes)?

YES

(b) the jurisdiction of a court or tribunal (including rights to judicial review or rights of appeal)?

YES

The Bill establishes criminal offences or pecuniary penalties for the breach of different requirements imposed by or under the Bill.

The offences in the Bill are established by clauses 15(1), 17(1), 19(1), 30(2), 44(1), 49, 53(1), 66(1) or (2), 70(1), 83(1), 83(2), 85(1), and 113(1) or (3), 137(2) or (4), 140(1), and 143(1), (with the relevant penalty levels set out in clause 124).

The pecuniary penalties in the Bill are established by clauses 27, 34, 46, and 48(2) (with the relevant penalty levels set out in clause 128).

The Bill also establishes the High Court's jurisdiction to, on the application of the regulators, enforce a voluntary undertaking entered into under the Bill, and impose any of the pecuniary penalties established by the Bill.

<b>3.4.1. Was the Ministry of Justice consulted about these provisions?</b>	<b>YES</b>
The Ministry of Justice has been consulted and has not raised any concerns about these provisions.	

### Privacy issues

<b>3.5. Does this Bill create, amend or remove any provisions relating to the collection, storage, access to, correction of, use or disclosure of personal information?</b>	<b>NO</b>
The information gathering provisions in the Bill apply to the operators, participants, and indirect participants of FMs. It is extremely unlikely that any of these entities would be a natural person, and that personal information would ever be collected under the Bill.	

<b>3.5.1. Was the Privacy Commissioner consulted about these provisions?</b>	<b>NO</b>
See the response to question 3.5.	

### External consultation

<b>3.6. Has there been any external consultation on the policy to be given effect by this Bill, or on a draft of this Bill?</b>	<b>YES</b>
<p>Two separate rounds of consultation on an enhanced FMI oversight framework were carried out in late 2013 and mid-2015. Submitters broadly supported the proposal as outlined in the second of these consultations, but made a number of technical comments and suggestions. Where appropriate, these were reflected in the final proposal for the entire framework (except the specific design of crisis management powers) that was published in December 2015. An additional round of consultation on the design of crisis management powers under the proposed framework was carried out in early 2016. Submitters remained supportive of the proposal as outlined in the consultation, although a number of technical comments and suggestions were incorporated into the final proposal.</p> <p>An exposure draft of the Bill was published in August 2019. Where appropriate, the Bill was amended to take into account technical comments and suggestions from submitters.</p>	

### Other testing of proposals

<b>3.7. Have the policy details to be given effect by this Bill been otherwise tested or assessed in any way to ensure the Bill's provisions are workable and complete?</b>	<b>YES</b>
<p>The International Monetary Fund (IMF) carried out a Financial System Assessment Programme (FSAP) review of New Zealand in 2016/17. As part of that process, the IMF reviewed the current regulation and supervision of FMs in New Zealand, and an earlier version of the proposals which are now included in the Bill. This resulted in the IMF publishing a technical note <a href="#">Regulation and Oversight of Financial Market Infrastructures</a> along with other reports arising out of the review. The technical note was supportive of the proposed framework and considered that it would bring New Zealand broadly into alignment with international best practice.</p>	

## Part Four: Significant Legislative Features

### Compulsory acquisition of private property

<b>4.1. Does this Bill contain any provisions that could result in the compulsory acquisition of private property?</b>	<b>YES</b>
<p>Powers that can be exercised in statutory management include the ability to sell the business of an FMI operator to a third party, or transfer that business to a new operator under a new operator scheme. These powers are only exercisable in cases where the FMI is distressed (i.e. has been subject to a financial, operational or governance failure). As such, they only apply when all, or a substantial part, of the operator's business has failed and/or where it is necessary to protect the stability of financial system (and achieve the purposes of the Bill).</p>	

### Charges in the nature of a tax

<b>4.2. Does this Bill create or amend a power to impose a fee, levy or charge in the nature of a tax?</b>	<b>NO</b>
<p>The Bill allows for regulations to be made setting fees and charges payable by operators in connection with the carrying out by the regulator of any function under the Bill, or on an application or request to the regulator to carry out any function under the Bill. Fees are expected to be set for only a small number of matters (possibly just for applications by an FMI to opt-in to the regime), will be set at no more than a cost recovery basis, and because they can only be set by regulations, will be subject to standard Cabinet processes.</p>	

### Retrospective effect

<b>4.3. Does this Bill affect rights, freedoms, or impose obligations, retrospectively?</b>	<b>NO</b>

## Strict liability or reversal of the usual burden of proof for offences

<b>4.4. Does this Bill:</b>	
<b>(a) create or amend a strict or absolute liability offence?</b>	<b>YES</b>
<b>(b) reverse or modify the usual burden of proof for an offence or a civil pecuniary penalty proceeding?</b>	<b>YES</b>
<p>The Bill established three strict liability offences which reverse the normal burden of proof. Specifically:</p> <ul style="list-style-type: none"> <li>• Clause 15(1) (Offence for failure to give information);</li> <li>• Clause 17(1) (Offence for failure to obtain review); and</li> <li>• Clause 143(1) (Offence for unauthorised disclosure or use).</li> </ul> <p>The strict liability offences in clauses 15(1) and 17(1) are necessary in order to ensure that the regulators ability to identify when FMIs should be brought into the regime via a designation notice is not compromised. In an extreme case, the committing of an offence under these clauses could result in a systemically important FMI failing while not being designated, with material disruption and cost to a significant part of the financial system.</p> <p>The strict liability offence in clause 143(1) is necessary in order to provide a high level of protection to confidential information, which if inappropriately disclosed could, in an extreme case result in significant adverse impacts on all or a substantial part of the financial system.</p> <p>Potential adverse effects of these strict liability offences are mitigated by the defence provided for in the Bill. This defence applies where the person charged with the offence (“A”) can prove that both of the following criteria are met:</p> <ul style="list-style-type: none"> <li>• The contravention was due to: <ul style="list-style-type: none"> <li>– The conduct of another person, other than a director, an employee, or an agent of A; or</li> <li>– An accident of some other cause beyond the control of A and A’s directors, employees, and agents; and</li> </ul> </li> <li>• A took reasonable precautions and exercised due diligence to avoid the contravention.</li> </ul>	

## Civil or criminal immunity

<b>4.5. Does this Bill create or amend a civil or criminal immunity for any person?</b>	<b>YES</b>
<p>The Bill extends the existing protections from liability for Reserve Bank staff and certain other persons in the Reserve Bank of New Zealand Act 1989, so that it also covers Reserve Bank staff and these other persons in relation to acts or omissions when exercising powers under the Bill. These protections only apply where the act or omission occurred in good faith. The FMA’s existing protection from liability in section 22 of the Financial Markets Authority Act 2011 (which applies unless it can be shown that the FMA or its staff have acted in bad faith, or that the FMA has failed to exercise reasonable care) will also apply to the FMA’s exercise of powers under the Bill.</p>	

## Significant decision-making powers

<b>4.6. Does this Bill create or amend a decision-making power to make a determination about a person’s rights, obligations, or interests protected or recognised by law, and that could have a significant impact on those rights, obligations, or interests?</b>	<b>YES</b>
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The statutory management framework in the Bill permits the statutory manager of a distressed FMI to:

- Following consultation with the regulators, disapply a provision of that FMI's rules if they are satisfied that this is necessary for one of the purposes in clause 78 (broadly speaking, where it is necessary to ensure the continuity of essential services and/or avoid or mitigate threats to the stability of, or confidence in, the financial system); and
- With the consent of the regulators, not be required to take into account the desirability of consistency in the treatment of creditors within the same class (if they provide consent, the regulators must set out the reasons for doing so in a report which is tabled in the House).

These powers are necessary to order to ensure the stability of the financial system in extreme cases, and are subject to the safeguards noted above in order to ensure they are properly constrained and used appropriately.

### Powers to make delegated legislation

<b>4.7. Does this Bill create or amend a power to make delegated legislation that could amend an Act, define the meaning of a term in an Act, or grant an exemption from an Act or delegated legislation?</b>	<b>NO</b>

<b>4.8. Does this Bill create or amend any other powers to make delegated legislation?</b>	<b>YES</b>
<p>The Bill contains provisions for the Reserve Bank and FMA to make legally binding standards that would apply to designated FMIs. These standards are disallowable instruments, and may set requirements relating to various topics including risk management, financial resources, governance, and contingency planning.</p> <p>These reasons for these requirements being set via deemed regulations are that:</p> <ul style="list-style-type: none"> <li>• The requirements are relatively detailed technical matters, that are not subject to criminal sanctions;</li> <li>• The requirements apply to a narrowly defined, clearly identifiable group (i.e. designated FMIs); and</li> <li>• The requirements are best made by the regulators given the technical expertise required and international best practice indicating that these types of requirements should be made by an independent body (or bodies).</li> </ul> <p>The Bill also includes various safeguards around this power including the requirement to consult with affected parties before standards are made, the requirement for standards to relate to certain matters, and the requirement for the regulators to have regard to certain principles when making standards.</p>	

### Any other unusual provisions or features

<b>4.9. Does this Bill contain any provisions (other than those noted above) that are unusual or call for special comment?</b>	<b>No</b>

