



**MEMORANDUM OF UNDERSTANDING**

**BETWEEN**

**FINANCIAL MARKETS AUTHORITY**

**AND**

**RESERVE BANK OF NEW ZEALAND**

**(on designation and oversight of settlement systems)**

7 December 2011

## MEMORANDUM OF UNDERSTANDING

BETWEEN

RESERVE BANK OF NEW ZEALAND

AND

FINANCIAL MARKETS AUTHORITY

### 1. Background

- 1.1 The Reserve Bank has responsibility for:
- (a) promoting the maintenance of a sound and efficient financial system; and
  - (b) avoiding significant damage to the financial system that could result from the failure of a participant in a settlement system.
- 1.2 The Financial Markets Authority ("FMA") has responsibility for:
- (a) promoting the integrity and effectiveness of settlement systems and related markets; and
  - (b) enhancing the confidence of investors and other market participants in settlement systems and related markets.
- 1.3 The new Part 5C of the Reserve Bank of New Zealand Act 1989 ("the Act") came into force on 24 November 2009. Its intention is to signal that trades in securities and other products can be cleared and settled in New Zealand through systems that meet the expectations of international and domestic participants.
- 1.4 The new law provides for the designation and oversight of settlement systems, replacing the regime that previously existed under the old Part 5C which was just concerned with the designation of payment systems. The new law makes the Reserve Bank and FMA jointly responsible for the designation and oversight of settlement systems (known as joint regulators in the legislation). Sole responsibility is however virtually given to the Reserve Bank in respect of a settlement system that is deemed to be a pure payment system.
- 1.5 This memorandum of understanding lays down guidance on how the joint work of the Reserve Bank and FMA will be conducted. In particular, it outlines the terms of liaison between the two agencies and the parameters that apply to this.

### 2. Designation

- 2.1 The designation of a settlement system is done by Order in Council on the advice of the two responsible Ministers (the Minister of Finance for the Reserve Bank, and the Minister of Commerce for FMA) and this, in turn, is based on a joint recommendation of the Reserve Bank and FMA.
- 2.2 The procedure for making a designation is laid down in sections 156Y to 156ZA of the Act. In this regard, the Reserve Bank and FMA agree as follows:
- (a) to notify the other of a formal application for designation within two (2) working days of the application being received (should they not be both notified at the time);

- (b) to meet with each other within ten (10) working days of receipt of the application to discuss:
  - (i) the matters specified in section 156Z(2)(a) – (f);
  - (ii) any other matters that are considered appropriate;
  - (iii) whether the proposed settlement system may constitute a pure payment system;
- (c) to meet or confer thereafter as required in order to make a joint recommendation to the Ministers that the settlement system be declared a designated settlement system, or to decide to refuse to make such a recommendation;
- (d) to promptly inform the applicant of a refusal to make a recommendation, together with the reasons for the refusal.

### **3. Amendments to the Rules/Disallowances**

3.1 Part 5C makes provision for amendments to the rules of a designated settlement system. An amendment may be disallowed by the Reserve Bank and FMA if notice of disallowance is given within twenty (20) working days after the date the notice of the proposed amendment is first received.

3.2 In this regard, the Reserve Bank and FMA agree as follows:

- (a) to notify the other of a notice of proposed amendment within two working days of the notice being received (should they not be both notified at the time);
- (b) to meet or confer with each other within five working days of receipt of the notice to consider the matter;
- (c) to decide within fifteen (15) working days of the notice being received whether the proposed amendment should be disallowed;
- (d) to promptly inform the contact person of the designated settlement system of the decision.

### **4. Variation/Revocation**

4.1 Part 5C makes provision for the variation or revocation of a designation, whether initiated by the operator of the settlement system or initiated by the joint regulators. The variation or revocation is done by Order in Council on the advice of the two Ministers and this, in turn, is based on a joint recommendation of the Reserve Bank and FMA.

4.2 In relation to a variation or revocation initiated by an operator, the Reserve Bank and FMA agree as follows:

- (a) to notify the other of a formal application within two (2) working days of the application being received (should they not be both notified at the time);
- (b) to meet or confer with each other to discuss:
  - (i) the matters specified in section 156ZI(1) (a) – (h);
  - (ii) any other matters that are considered appropriate;
- (c) to decide whether to make a joint recommendation to the Ministers to vary or revoke the designation;
- (d) to promptly inform the contact person of the designated settlement system of the decision.

4.3 In relation to a variation or revocation initiated by a joint regulator, the Reserve Bank and FMA agree as follows:

- (a) to confer with the other before the commencement of a review;
- (b) to meet or confer with each other as needed to discuss:
  - (i) the matters specified in section 156ZL(1) (a) – (h);
  - (ii) any other matters that are considered appropriate;
- (c) if proceeded with, to notify the contact person (on behalf of the operator) of the proposed action (together with the reasons for the action) and to afford the contact person an opportunity of making submissions;
- (d) in light of any submissions received, to decide whether a joint recommendation should be made to the Ministers to vary or revoke the designation;
- (e) to promptly inform the contact person of the designated settlement system of the decision.

## **5. Pure Payment System**

5.1 Where a proposed system is considered by the joint regulators to be a pure payment system, the Reserve Bank will then assume full regulatory responsibility. FMA will not have a role save for involvement in the decision process (as required by the legislation), or unless the character of the system should subsequently change. It is acknowledged that the Reserve Bank will be expected to undertake all the work that is required to process an application which is considered to relate to a pure payment system (as provided for by section 156Z (4)). In the event of a refusal to make a recommendation, the applicant will be promptly informed together with the reasons for the refusal.

## **6. Reliance on Others Work**

6.1 Part 5C enables each of the joint regulators to rely on the work of the other regulator when considering applications for designation, variation or revocation. Each of them records that they will seek to optimise the use of overall regulatory resources in a way that takes into account their respective interests and which makes use of each regulator's comparative advantage and knowledge base.

## **7. Supply of Information**

7.1 There is provision in Part 5C for the joint regulators to require the supply of information from an operator of, a participant in, or a contact person of, a designated settlement system. The Reserve Bank and FMA will confer with each other before exercising this power in any case and agree on the taking of such action.

## **8. Disclosure of Information/Sharing of Information**

8.1 Section 156ZN prescribes situations when information compulsory required under section 156ZL (as contemplated by clause 7.1 above) may be disclosed to a third party. The Reserve Bank and FMA will keep each other informed about such disclosures, in particular, they will confer with each other at least two working days before any final decision is made about the disclosure. Where appropriate they will agree arrangements to protect the confidentiality of the information to be disclosed.

- 8.2 Should information come into the possession of a joint regulator which may have relevance to the administration of Part 5C, or to the performance of the joint regulators' functions and duties under Part 5C, then that joint regulator will promptly inform the other regulator.

## **9. Exercise of Powers Under Securities Act**

- 9.1 Section 156L permits FMA to exercise its powers under the Securities Act 1978 in performing its work under Part 5C. This is circumscribed in the case of the exercise of its inspection powers against the Reserve Bank, in particular, it may only exercise such powers if the Reserve Bank is a participant in, or operator of, a settlement system.

- 9.2 FMA agrees to inform the Reserve Bank in advance if it intends to exercise its powers for the purposes of Part 5C including its powers of inspection, such to be done at least two (2) working days before any final decision on the exercise of the powers. They will endeavour to reach agreement on the way such action is to be carried out.

## **10. Conferral**

- 10.1 There are various references in Part 5C which contemplate conferral between the Reserve Bank and FMA on certain matters. These arise in relation to:

- (a) information to support an application for designation (section 156Y (3) (a));
- (b) the application fee for designation (section 156Y (3) (c));
- (c) guidelines for the application procedure (section 156Y (4));
- (d) the application fee for variation or revocation (section 156ZG (3)).

The Reserve Bank and FMA have conferred already in relation to these matters. They acknowledge that further conferral may be necessary both to finalise outstanding issues and to review the matters in the future as and when required.

- 10.2 The Reserve Bank and FMA will confer with each other on any other matter relating to the designation and oversight of a settlement system including, but not limited to:

- (a) determining whether any proposed rule change(s) should more properly be treated as a variation of the designation;
- (b) the nature and timing of any self-assessment;
- (c) the nature and timing of any stress testing (where there is a central counterparty);
- (d) any replenishment of capital that may be required;
- (e) the need for any third party verification or audit;
- (f) the preparation and publication of any report of an operator or the publication of any other commentary by a joint regulator on matters relating to a designated settlement system;
- (g) any other formal contact with a designated settlement system (beyond what is contemplated already under the MOU), in particular, to keep each other informed about the reasons for such contact, how it should be done and who should participate.

## **11. Communications/Meetings**

- 11.1 The Reserve Bank and FMA will endeavour to communicate with a settlement system by letter or email (as opposed to telephone or other personal contact), in particular, on

matters of substance. They expect a settlement system to do the same when it comes to its dealings with the joint regulators.

- 11.2 The joint regulators themselves will confer with each other before communicating with a settlement system, in particular, on matters of substance.
- 11.3 Meetings with a settlement system should be conducted with both the Reserve Bank and FMA present unless the circumstances do not warrant this.
- 11.4 Where either the Reserve Bank or FMA is contacted in its capacity as a joint regulator under Part 5C, other than by an email or letter to both joint regulators, the joint regulator who has been contacted will promptly advise the other joint regulator of the contact made and the matters discussed or raised.
- 11.5 This clause will apply for the purposes of an application for designation as well as relations in the post-designation stage.

## 12. Time Limits

- 12.1 The time limits expressed in this memorandum of understanding may be amended in any case by agreement between the Reserve Bank and FMA.

## 13. Review

- 13.1 The arrangements under this memorandum of understanding will be kept under review and modified where the Reserve Bank and FMA deem it necessary.

## 14. Contacts

- 14.1 The Reserve Bank and FMA will nominate liaison persons for the purposes of Part 5C and for the purposes of this memorandum of understanding. The initial liaison persons for each are specified below.

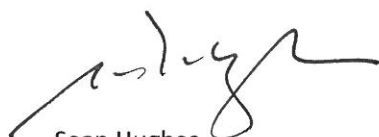
### Reserve Bank

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Dated this 7<sup>th</sup> day of December 2011



Sean Hughes  
 CEO  
 Financial Markets Authority



Alan Bollard  
 Governor  
 Reserve Bank of New Zealand