ISDA Safe, Efficient Markets

September 26, 2019

BY E-MAIL& HAND

The Reserve Bank of New Zealand
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Wellington
New Zealand
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Dear Sirs

New Zealand: Exposure Draft – Financial Market Infrastructures Bill

Introduction

The International Swaps and Derivatives Association, Inc.[1] ("**ISDA**") is grateful for the opportunity to provide feedback on the exposure draft of the Financial Market Infrastructures Bill (the "**Bill**') published by the Reserve Bank of New Zealand ("**RBNZ**") on 1 August.

We note that the Bill is intended to establish a standalone Act for the regulation and supervision of financial market infrastructures ("**FMIs**") in New Zealand. This will replace the current regime in New Zealand, which is contained in Parts 5B and 5C of the Reserve Bank of New Zealand Act 1989. We also understand that the New Zealand Government has previously decided to adopt a new regulatory regime for FMIs and has made various supplementary policy decisions in this regard. The Bill has been published specifically to seek views on the granular and technical details of the Bill itself.

ISDA is supportive of the efforts made by the RBNZ to provide a robust framework for the regulation and supervision of FMIs. Whilst ISDA has provided comments in this submission on certain aspects of the Bill, we note that our members and other trade associations may choose to make their own individual submissions to the RBNZ on the Bill. In providing these comments, we have ensured that they are consistent with the feedback provided by Bell Gully, ISDA's netting and collateral opinion counsel in New Zealand, on the very same points.

[1] Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 900 member institutions from 71 countries. These members comprise a broad range of derivatives markets participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter @ISDA.

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We set out our comments below.

Comments

- Section 113: Statutory Management does not place any person in contravention of enactment, etc

As you are aware, the appointment of a statutory manager to a counterparty is a standard and important event of default in derivatives documentation. Section 5(a)(vii) of the 2002 ISDA Master Agreement ("**ISDA MA**"), for instance, provides for a Bankruptcy Event of Default. This provision of the ISDA MA applies to each party, any Credit Support Provider of a party and any applicable Specified Entity of a party. The Bankruptcy Event of Default in the ISDA MA has been drafted to be broad enough to be triggered by analogous proceedings or events under any bankruptcy or insolvency laws pertaining to a particular party. If a party is subject to insolvency proceedings under the laws of its jurisdiction of incorporation, those insolvency laws will apply even if another jurisdiction's laws govern the ISDA MA.

We note that, whilst section 113(2) is intended to uphold the enforceability of such a provision in the statutory management of an FMI operator, the drafting suggests that this is only in the case where that FMI operator is a central counterparty ("**CCP**"). Section 113(2) states that "This section does not apply to a right to which section 116 applies" - and section 116(1)(c) refers to an FMI that is a CCP.

It appears then that the current drafting does not apply to *other* types of FMIs - only CCPs. Section 113(2) should be amended to provide for the inclusion of other FMIs, as these are also able to enter into derivatives transactions.

We would therefore suggest that the reference to section 116 in section 113(2) be amended to refer to section 116(1)(a) and (b) instead.

- Section 116: Certain rights relating to derivatives may be exercised after stay

Subpart 4 - Supplementary Provisions of the Bill sets out rights relating to derivatives which may be exercised after the imposition of a stay. It is critical therefore that the drafting of this Subpart 4 is clear in order to assess the effect of these provisions on the derivatives industry.

Section 116(2) states that section 42 of the Corporations (Investigation and Management) Act 1989 ("**CIMA**") (as applied by section 102 of the Bill) does not limit or prevent the exercise of the "right" described in section 116(1) if that right is exercised after the specified time. The use of the words "limit or prevent" in section 116(2) appears to mean that anything not already prohibited by section 42 of CIMA is unaffected by the Bill.

In this respect, we would be grateful for the RBNZ's clarification that the intention of the Bill is to provide that the exercise of certain rights relating to derivatives *would* be stayed for a period, regardless of whether that is currently permitted under CIMA. If this is indeed the case, we would ask that RBNZ considers whether the current drafting of section 116 supports this intention.

We note that the exercise of termination rights is generally considered *not* to be prohibited by section 42(1) of CIMA. Also, whilst the exercise of netting and secured creditor rights *is* generally considered to be prohibited by section 42(1) of CIMA, section 42(7) and (8) allow for the exercise of those rights under certain circumstances.

Therefore, we would suggest that section 116 of the Bill be amended to broaden the current stay in section 42 of CIMA as it applies to a designated FMI that is a CCP. If such an amendment is made, it should also state that it does not affect the application of section 42 to a designated FMI that is not a CCP.

- Inter-relation between the Bill and the Financial Markets (Derivatives Margin and Benchmarking) Reform Amendment Act 2019

Part 1 of the Financial Markets (Derivatives Margin and Benchmarking) Reform Amendment Act 2019 ("**Derivatives Margin Act**") came into force on 31 August 2019. We note that the inter-relation between the Bill and the Derivatives Margin Act could not have been previously provided for in the Bill, seeing that the Bill pre-dates the enactment of the Derivatives Margin Act.

However, we believe that the Bill will need to describe how it affects the new section 42(9) of CIMA (as inserted by section 16 of the Derivatives Margin Act). Presumably, the effect would be that section 42(9) would apply in the statutory management of an operator of a designated FMI in the unlikely event that this statutory management occurs under CIMA. However, in the more likely event that this statutory management occurs under the Bill, we would suggest that the position would be as we have described in the preceding section.

- Section 5 – Interpretation

We note that Section 5 of the Bill provides, among others, the definition of an "FMI" and this "includes (without limitation) a system that is commonly regarded, within financial systems that are in New Zealand or elsewhere, as a financial market infrastructure…".

We also note that Section 14 provides that the regulator may, by notice, require an operator, a participant, or an indirect participant of an FMI to give to the regulator any information relating to the FMI that the regulator reasonably requires for the purposes of, or in connection with, its functions. Section 16 of the Bill further provides for the regulator's power to require information which has been submitted to be reviewed. Section 18 also states that the regulator may, by notice, require an operator of an FMI to give to the regulator an independent report. We understand that these information provision obligations would extend to all FMIs, even without a designated status.

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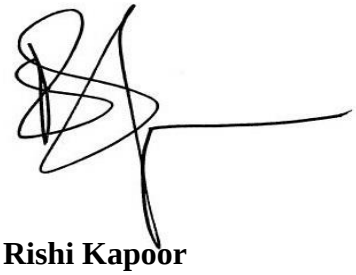
We note that the Explanatory Note to the Bill provides, among others "that the joint regulators' powers in respect of non-designated FMIs are limited to information gathering and the ability to require operators of these FMIs to obtain an independent report in respect of the business or operation of the FMI. This reflects the fact that these FMIs are not systematically 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 the FMI has become systemically important (and so may need to be designated under the regime)."

We have received comments urging that the Bill should be carefully drafted to only capture FMIs and their direct and indirect participants which are relevant to New Zealand financial markets (in the case of an FMI, irrespective of whether it is designated).

ISDA thanks the RBNZ for the opportunity to respond to the Bill and welcomes dialogue with the RBNZ on any of the points raised. Please do not hesitate to contact Rishi Kapoor, Director, Public Policy, Asia-Pacific (rkapoor@isda.org, +852 2200 5900) or Erryan Abdul Samad, Assistant General Counsel (eabdulsamad@isda.org, +65 6653 4170).

Yours sincerely,

For the International Swaps and Derivatives Association, Inc.



Rishi Kapoor
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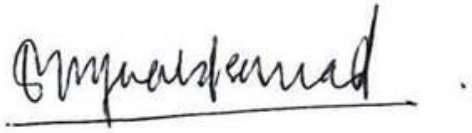

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