

Financial Market Infrastructure Regulatory Reforms

Submission to Consultation on Exposure Draft Legislation

February 2024

Executive Summary

The Reserve Bank of Australia (RBA) strongly supports reform to modernise the regulatory framework for Financial Market Infrastructures in Australia.

Enhanced supervisory powers

The proposed reforms transfer powers to enforce the Financial Stability Standards (FSS) to the RBA, strengthen powers to gather information to support compliance assessments and provide the RBA with new direction powers to allow intervention where there is a threat to financial stability.

The RBA considers these new powers to be appropriate and proportionate given the central role that clearing and settlement (CS) facilities play in the modern financial system and the need for authorities to effectively monitor compliance and protect financial stability.

New crisis management powers

The proposed reforms include new powers to allow the RBA to respond to an acute crisis at a CS facility to prevent a disorderly wind-down of the facility and protect the continuity of services that are critical to the functioning of the Australian financial system and financial stability.

The proposed crisis management framework is based on internationally agreed principles and includes tools to stabilise a distressed CS facility and restore it to viability.

The RBA supports the inclusion of appropriate crisis management powers that are consistent with international best practice. These powers fill a gap in the existing regulatory architecture and will give the RBA the tools to effectively resolve a crisis at a CS facility and, in coordination with other regulators, safeguard the stability of the Australian financial system.

1. Introduction

The Reserve Bank of Australia (RBA) welcomes the modernisation of the regulatory framework for Financial Market Infrastructures (FMIs) embodied in these proposed reforms to the *Corporations Act 2001* (Corporations Act) and other legislation. The RBA supports the effort to strengthen the regulatory powers of the Australian Securities and Investments Commission (ASIC) and the RBA and better align the powers with the agencies' respective responsibilities for the regulation of FMIs. The proposed new

crisis powers will be an important addition to the regulatory toolkit and greatly improve the RBA's ability to respond effectively to a threat to the viability of a CS facility, which could otherwise pose risks to the stability of the Australian financial system. While this submission focuses on the changes to the powers and responsibilities of the RBA, the RBA also supports the enhancements to ASIC's powers included in the proposed reforms. The Australian financial system will benefit from a modern regulatory framework with the necessary powers, aligned to the responsibilities of the various regulators.

Under the proposed reforms the RBA will retain its role as co-regulator of CS facilities (with ASIC) with a mandate for financial system stability. The RBA will continue to have responsibility for setting and assessing compliance with Financial Stability Standards (FSS) and advising ASIC on certain decisions including licensing. To allow it to fulfil its supervisory role, the RBA will be given new powers to enforce compliance with the FSS and stronger powers to gather information. In addition, the RBA will have new powers to engage experts to undertake detailed reviews to inform its supervision.

The interconnected nature of CS facilities and their central role in the modern financial system means that the disorderly failure of one of these entities would likely lead to disruption to the wider financial system. Such a failure could result in the unwinding of payments, a delay or failure of settlement of transactions and/or a disruption to asset markets as large amounts of margin collateral is liquidated. CS facilities are required to have access to financial resources to protect against disorderly failure in a wide range of extreme but plausible circumstances. Nonetheless, it is globally recognised that further intervention would be required in the exceptional circumstance that these primary arrangements fail. The international consensus on appropriate resolution arrangements is expressed in the Financial Stability Board Key Attributes of Effective Resolution Regimes for Financial Institutions (FSB Key Attributes) complemented by the 2017 Guidance on CCP Resolution and Resolution Planning (FSB Resolution Guidance).¹

2. Specific comments on some key provisions

The proposed package is substantial and has been the subject of previous consultation and analysis. The RBA supports the package in full. This submission is not intended to comment on the reforms exhaustively or in detail. However, the RBA welcomes the opportunity to make the following comments on some of the key proposals.

Crisis management and resolution powers

As part of the proposed reforms the RBA will receive powers for crisis management and resolution of CS facilities. These powers are proposed for the effective management and resolution of certain threats arising from or relating to CS facilities. Specifically, these are threats posed to:

- the stability of the financial system in Australia; or
- the continuity of clearing and settlement facility services that are critical to the functioning of the financial system in Australia.

(Schedule 1: s830B)

The proposed reforms also specify the triggers for the use of crisis and resolution powers. (Schedule 1: s831B)

1 See [Key Attributes of Effective Resolution Regimes for Financial Institutions](#) and [Guidance on Central Counterparty Resolution and Resolution Planning](#).

Also proposed are powers to allow the RBA to effectively plan for crisis scenarios and maximise the likelihood that resolution will be executed successfully when such intervention is required.

Some of the proposed crisis management and resolution powers are stronger than powers which are generally available to regulators for use in day-to-day supervision. This is because crisis management and resolution powers are designed to be used to respond to the serious threats set out in proposed s830B. The powers may only be used in the circumstances set out in proposed s831B. The suite of powers is consistent with recognised international best-practice as expressed in the FSB Key Attributes and FSB Resolution Guidance and are comparable to similar powers being implemented in peer jurisdictions.

The circumstances in which these powers might be utilised are expected to be very unusual. CS facilities are required to have robust risk management arrangements and access to sufficient financial resources and recovery tools to protect against shocks including failure of participants to meet their obligations to the facility. It is generally expected that these arrangements will be sufficient to protect the financial system from stability risks posed by CS facilities. Even in a major (but plausible) downside scenario a CS facility would be expected to withstand adverse conditions without intervention from regulators. The proposed reform package also provides the RBA with powers, including direction powers, which are intended to further reduce the likelihood that the full range of crisis and resolution powers will need to be utilised.

The proposed reforms include a range of powers to be used by the RBA in the management of a crisis. To effectively manage a crisis situation posing the threats set out in proposed s830B, it will be important for the RBA to have the flexibility to choose the most appropriate response. This cannot be determined in advance because it is not possible to foresee the full range of scenarios that may result in the threats set out in proposed s830B. In responding to a crisis scenario arising from a CS facility, the RBA's objective will be to formulate the most appropriate response to the specific situation based on the information available to the RBA at that time.

It is likely that a crisis scenario involving a CS facility will include a range of complex factors that will need to be considered by the RBA. Within the context, the RBA will seek to formulate the least intrusive response that is appropriate and effective in responding to threats to financial stability and the continuity of critical clearing and settlement services.

Resolution is most likely to occur where the viability of the CS facility is threatened and the resources and tools at the facility's disposal are insufficient or fail to address losses as expected. It will also be considered in circumstances where the use of recovery tools could itself be harmful to financial stability. This is reflected in the conditions for resolution (Schedule 1: s831A).

In conducting resolution, the RBA will endeavour to follow loss allocation procedures as established in the CCP's rulebook wherever possible but must give priority to financial stability.

The RBA appreciates the value of transparency and predictability in helping stakeholders plan for a crisis scenario. Acknowledging the difficulty of predicting what might trigger a crisis, and the need to be prepared for any shocks that arise, no matter the source, the RBA's intention is to use methods such as published policy statements to provide appropriate transparency. The RBA expects that these might explain matters such as its approach to determining what constitutes a threat to financial stability, the circumstances that might trigger resolution and the factors that might be considered in deciding which tools it would use.

Scope of powers crisis and resolution powers: applicability to related bodies corporate

In certain circumstances, the proposed resolution powers may be applied to other entities within a CS facility's corporate group. Facilities often operate as part of a larger group that provides a range of financial services. In such groups, it is common for individual entities to rely on other parts of the corporate group (related bodies corporate (RBC)) for the provision of services and financial support. To execute resolution effectively and safeguard the continuity of clearing and settlement services the RBA must be able to influence and, at the extreme, control these related services providers. These resolution powers for non-CS entities will only be used where it is deemed necessary to effectively resolve the CS facility.

Clarifying the regulatory perimeter (Schedule 2: s820D, s820e)

The RBA supports the clarification of the test to determine if a CS facility is required to be licensed in Australia. In our view, the current test has given rise to an undesirable level of uncertainty.

The reforms provide ASIC with the power to declare that a CS facility has a material connection to Australia. The reforms will also establish detailed criteria for determining if such a material connection exists. An entity that is covered by an ASIC declaration will be required to hold a CS licence or be exempted.

The RBA considers that the proposed clarification will provide greater certainty that will assist both the regulators and CS facilities. The proposed reform will help to ensure that CS facilities which have the potential to affect Australian financial stability are appropriately regulated in Australia.

Reserve Bank of Australia
9 February 2024

References

Financial Stability Board (2014), [Key Attributes of Effective Resolution Regimes for Financial Institutions](#).

Financial Stability Board (2017), [Guidance on Central Counterparty Resolution and Resolution Planning](#).

Exposure draft

[Schedule 1 – FMI: resolution authority](#)

[Schedule 2 – FMI: new and enhanced regulatory powers](#)