

FMI STANDARD 5: COLLATERAL

FS5



DOCUMENT VERSION HISTORY

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INTRODUCTION

Application

- i. This standard applies to every operator of a designated FMI that was specified in its designation notice under section 29(2)(f) of Financial Market Infrastructures Act 2021 (the **Act**) as falling within one or more of the following classes of designated FMIs:
 - (a) a pure payment system; or
 - (b) a securities settlement system; or
 - (c) a central counterparty.

Legal powers

- ii. Under section 8 of the Act the regulator is defined as the RBNZ and the FMA acting jointly (or the RBNZ acting on its own in respect of pure payment systems).
- iii. Section 12 of the Act provides the regulator's functions. These include regulating designated FMIs, dealing with designated FMIs that are distressed, and other functions under the Act.
- iv. Subject to certain statutory prerequisites, section 31 of the Act empowers the regulator to make standards for designated FMIs.
- v. Section 34 sets out the matters that standards may deal with or otherwise relate to. Section 34(1)(e)(iii) provides that a standard may deal with, or otherwise relate to, the management by operators of credit risk. The use of collateral is one way to manage credit risk.

Interpretation

- vi. Words and phrases used in this standard have the same meaning as in the Act.
- vii. **Internal systems** means mechanisms within an FMI or operator to implement policies, procedures, or controls.
- viii. **Haircut** is defined as a risk control measure applied to underlying assets where the value of those underlying assets is calculated as the market value of the assets reduced by a certain percentage.

Commencement

- ix. This standard comes into force on 1 March 2024.

REQUIREMENTS

- 1) An operator that requires collateral for the purposes of operating the FMI, to manage the FMI's or its participants' credit exposure, must ensure it only accepts collateral with low credit, liquidity, and market risks. An operator must also set, and enforce appropriately, conservative haircuts and concentration limits.
- 2) Further to the requirements in clause (1) an operator must ensure that:
 - a) it establishes prudent valuation practices and develops haircuts that are tested at least annually, and that take into account stressed market conditions; and
 - b) stable and conservative haircuts for collateral are established, and that these haircuts are calibrated to include periods of stressed market conditions, to the extent practicable and prudent, to reduce the need for procyclical adjustments; and
 - c) it avoids concentrated holdings of any assets where this would significantly impair its ability to liquidate such assets quickly without significant adverse price effects; and
 - d) where an operator accepts cross-border collateral for the FMI, it mitigates the risks associated with the use of that collateral, and ensures the collateral can be used in a timely manner; and
 - e) it uses an internal system that is well-designed and operationally flexible for managing collateral.

(See Guidance for Standard 5: 'Collateral', in Guidance for the FMI Standards for more detail).