

Payment Systems and Netting Act 1998

No. 83, 1998

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**An Act to make provision in relation to payment
and settlement systems and netting contracts, and
for related purposes**

Contents

Part 1—Preliminary	1
1 Short title.....	1
2 Commencement	1
3 Crown bound by this Act.....	2
4 Application of <i>Criminal Code</i>	2
5 Definitions.....	2
Part 2—Integrity of approved RTGS payment systems	7
6 External administration not to affect transactions carried out on the day of appointment	7
7 Obligation to notify system administrator of external administration.....	7
8 Application for approval of payment system	8
9 Reserve Bank may approve payment system	8
Part 3—Integrity of approved netting arrangements	11
10 Effectiveness of approved multilateral netting arrangements.....	11
11 Application for approval of netting arrangement	13
12 Reserve Bank may approve netting arrangement	13
13 Qualified privilege	14
Part 4—Close-out netting contracts	15
14 Effectiveness of close-out netting contracts.....	15
15 Declaration that section 14 does not apply.....	17
Part 5—Market netting contracts	18
16 Effectiveness of market netting contracts	18
Part 6—Administration	20
17 Prescribed forms	20
18 Regulations.....	20

Payment Systems and Netting Act 1998

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An Act to make provision in relation to payment and settlement systems and netting contracts, and for related purposes

[Assented to 2 July 1998]

The Parliament of Australia enacts:

Part 1—Preliminary

1 Short title

This Act may be cited as the *Payment Systems and Netting Act 1998*.

2 Commencement

This Act commences on the day on which it receives the Royal Assent.

3 Crown bound by this Act

This Act binds the Crown in all its capacities, but does not make the Crown liable to be prosecuted for an offence.

4 Application of *Criminal Code*

The *Criminal Code* applies to all offences against this Act.

5 Definitions

In this Act, unless the contrary intention appears:

approved futures clearing house means a clearing house approved under section 1131 of the Corporations Law.

approved netting arrangement means a netting arrangement approved under section 12.

approved RTGS system means a payment or settlement system approved under section 9.

approved special stock market means a stock market approved under section 770A of the Corporations Law.

close-out netting contract means:

- (a) a contract under which, if a particular event happens:
 - (i) particular obligations of the parties terminate or may be terminated; and
 - (ii) the termination values of the obligations are calculated or may be calculated; and
 - (iii) the termination values are netted, or may be netted, so that only a net cash amount (whether in Australian currency or some other currency) is payable; or
- (b) a contract declared by the regulations to be a close-out netting contract for the purposes of this Act;

but does not include:

- (c) a contract that constitutes, or is part of, an approved netting arrangement; or
- (d) a contract in relation to which a declaration under section 15 is in force; or
- (e) a contract declared by the regulations to not be a close-out netting contract for the purposes of this Act.

Commonwealth constitutional reach: a contract or arrangement is entered into in circumstances that are within Commonwealth constitutional reach if:

- (a) a constitutional corporation is a party to the contract or arrangement; or
- (b) the contract or agreement has a significant effect on the business affairs, or an activity, of a constitutional corporation; or
- (c) the contract or arrangement is entered into in the course of, for the purposes of or in relation to one or more of the following:
 - (i) dealings in currency, bills of exchange or promissory notes;
 - (ii) money borrowed on the public credit of the Commonwealth;
 - (iii) trade and commerce between Australia and places outside Australia or between places outside Australia;
 - (iv) trade or commerce among the States;
 - (v) trade or commerce within a Territory, between a State and a Territory or between 2 Territories;
 - (vi) banking (other than State banking);
 - (vii) insurance (other than State insurance); or
- (d) the contract or arrangement is entered into by means of or in relation to, postal, telegraphic, telephonic or other like services.

constitutional corporation means:

- (a) a foreign corporation; or
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Section 5

- (b) a trading or financial corporation formed within the limits of the Commonwealth.

external administration: a person goes into external administration if:

- (a) they become a body corporate that is an externally administered body corporate within the meaning of the Corporations Law; or
- (b) they become an individual who is an insolvent under administration within the meaning of the Corporations Law; or
- (c) someone takes control of the person's property for the benefit of the person's creditors because the person is, or is likely to become, insolvent.

external administrator for a person who goes into external administration is the person who takes control of the person's property under the administration.

general participant in a payment or settlement system means a participant who cannot, under the operating rules for the system, settle transactions on their own account through the system.

market netting contract means:

- (a) a contract:
 - (i) entered into in accordance with the rules that govern the operation of a netting market; and
 - (ii) under which obligations between parties to the contract are netted; or
- (b) a contract declared by the regulations to be a market netting contract for the purposes of this Act;

but does not include:

- (c) a contract that constitutes, or is part of, an approved netting arrangement; or
- (d) a contract declared by the regulations not to be a market netting contract for the purposes of this Act.

multilateral netting arrangement means an arrangement that has more than 2 parties and under which the obligations owed by the parties to each other are netted.

netting market means:

- (a) an arrangement that is:
 - (i) a stock exchange, approved special stock market, exempt stock market, securities clearing house, futures exchange, exempt futures market or approved futures clearing house under the Corporations Law; and
 - (ii) approved by the Minister for the purposes of this definition; or
- (b) an arrangement declared by the regulations to be a netting market for the purposes of this Act.

operating rules for a payment or settlement system means the rules governing the operation of the system.

participant in an approved RTGS system means a person who is a participant in the system in accordance with the rules governing the operations of the system.

party to an approved netting arrangement is a person who is a party to the arrangement in accordance with the rules governing the arrangement.

provable: an obligation is provable in an external administration if:

- (a) for an external administration that is a winding up under the Corporations Law—the obligation is a debt or claim that is admissible to proof against the body being wound up; or
- (b) for an external administration that is a bankruptcy under the *Bankruptcy Act 1966*—the obligation is a debt or liability provable in the bankruptcy; or
- (c) in any other case—the person to whom the obligation is owed is entitled to share in any distribution of property to creditors under the administration on the basis of the obligation if the obligation is properly established.

Section 5

Reserve Bank means the Reserve Bank of Australia.

settling participant in a payment or settlement system means a participant who, under the operating rules for the system, can settle transactions through the system on their own behalf and for other participants.

specified provisions means:

- (a) section 11F and subsection 13A(3) of the *Banking Act 1959*; and
- and
- (b) section 187 of the *Life Insurance Act 1995*; and
- (c) section 86 of the *Reserve Bank Act 1959*; and
- (d) sections 437D and 468 and Division 2 of Part 5.7B of the Corporations Law; and
- (e) sections 120, 121 and 122 of the *Bankruptcy Act 1966*; and
- (f) section 142 of the *Superannuation Industry (Supervision) Act 1993*; and
- (g) a law prescribed by the regulations for the purposes of this definition.

voidable: a payment is voidable in an external administration if it is:

- (a) for an external administration that is a winding up under the Corporations Law—voidable under Division 2 of Part 5.7B of the Corporations Law; or
- (b) for an external administration that is a bankruptcy under the *Bankruptcy Act 1966*—void as against the trustee in bankruptcy; or
- (c) in any other case—void as against the external administrator or voidable under the law governing the external administration.

Part 2—Integrity of approved RTGS payment systems

6 External administration not to affect transactions carried out on the day of appointment

- (1) If:
 - (a) a participant in an approved RTGS system goes into external administration; and
 - (b) a payment or settlement transaction is executed through the system at any time on the day on which the external administrator is appointed; and
 - (c) the transaction involves the payment of money, or the transfer of an asset, by the participant;the payment or transfer has the same effect it would have had if the participant had gone into external administration on the next day.
- (2) This section has effect despite any other law.

7 Obligation to notify system administrator of external administration

- (1) A participant in an approved RTGS system must notify the system administrator if:
 - (a) the participant; or
 - (b) another participant whose transactions the participant settles through the system;goes into external administration. The participant must give the notice as soon as practicable after the participant becomes aware of the external administration.
- (2) A person does not contravene subsection (1) if:
 - (a) they took reasonable steps to comply with that subsection; or

Section 8

- (b) the system administrator was already aware of the external administration by the time the person was required to notify the administrator under subsection (1).
- (3) A person must not contravene subsection (1).

Penalty: Imprisonment for 5 years.

8 Application for approval of payment system

- (1) A person may apply to the Reserve Bank for approval of a payment or settlement system.
- (2) The application must:
 - (a) be in the prescribed form; and
 - (b) be accompanied by the documents:
 - (i) specified in the regulations; or
 - (ii) required by the Reserve Bank.

9 Reserve Bank may approve payment system

- (1) The Reserve Bank may approve the system if it is satisfied that:
 - (a) systemic disruption in the financial system could result if a participant went into external administration and the system were not approved under this section; and
 - (b) the system is supported by a legally enforceable arrangement between participants in the system for the irrevocable settlement of transactions in real time; and
 - (c) the rules governing the system establish a system administrator for the arrangement; and
 - (d) the system administrator has the resources, competency and integrity needed to administer the system; and
 - (e) the system rules provide that if a settling participant goes into external administration, the system administrator may suspend from the system:
 - (i) the participant; and

- (ii) any general participant for whom that participant is the sole sponsor; and
 - (f) the system rules provide that if a general participant goes into external administration, the system administrator may suspend that participant from the system; and
 - (g) the system rules require a settling participant to assume the obligations of any participant whose transactions they settle through the system if the participant fails to fulfil those obligations;and of any other matters specified in the regulations.
- (2) In deciding whether to approve a system, the Reserve Bank must have regard to the following:
 - (a) whether the system rules:
 - (i) allow all participants to settle transactions on their own account; or
 - (ii) provide both for participants who can settle transactions on their own account and for other participants (*settling participants*) and for participants who cannot settle transactions on their own account (*general participants*);
 - (b) whether the system rules provide for different obligations for settling participants and general participants and, if they do, whether they:
 - (i) require a general participant to have a settling participant to settle their transactions through the system; and
 - (ii) require a participant who goes into external administration to notify its settling participant (if any) of the external administration as soon as practicable; and
 - (iii) require a settling participant to notify the system administrator as soon as practicable if it becomes aware that a participant whose transactions it settles through the system has gone into external administration;

Section 9

- (c) whether the system rules require participants to notify the system administrator as soon as practicable if they go into external administration;
 - (d) any other matters specified in the regulations;
 - (e) any other matters the Reserve Bank considers relevant.
- (3) An approval:
- (a) must be given in writing; and
 - (b) may be given subject to the terms and conditions specified in the approval; and
 - (c) is a disallowable instrument for the purposes of section 46A of the *Acts Interpretation Act 1901*.

Part 3—Integrity of approved netting arrangements

10 Effectiveness of approved multilateral netting arrangements

- (1) If an approved netting arrangement is entered into in circumstances that are within Commonwealth constitutional reach:
 - (a) obligations may be terminated, termination values may be calculated and a net amount become payable in accordance with the arrangement; and
 - (b) paragraph (a) applies despite:
 - (i) any disposal of rights that may be netted under the arrangement; or
 - (ii) the creation of any encumbrance, or any other interest, in relation to those rights; or
 - (iii) the operation of any encumbrance, or any other interest, in relation to those rights that is created after the commencement of this section;
in contravention of a prohibition in the arrangement; and
 - (c) for the purposes of any law, the assets and liabilities of a party to the arrangement are taken:
 - (i) to include any net obligation owed to a party under the arrangement; and
 - (ii) not to include obligations terminated under the arrangement.
- (2) If a party to an approved netting arrangement goes into external administration:
 - (a) the party may do anything permitted or required by the arrangement in order to net:
 - (i) obligations incurred before or on the day on which the party goes into external administration; and

Section 10

- (ii) net obligations if the obligations that are directly or indirectly netted are incurred before or on the day on which the party goes into external administration; and
- (b) the obligations that are, or have been, netted under the arrangement are to be disregarded in the external administration (but see subsection (4)); and
- (c) any net obligation owed by the party under the arrangement that has not been discharged is provable in the external administration; and
- (d) any net obligation owed to the party under the arrangement that has not been discharged may be recovered by the external administrator for the benefit of creditors; and
- (e) the netting and any payment made by the party under the arrangement to discharge a net obligation is not to be voidable in the external administration.

Note 1: Paragraph (a)—This paragraph only authorises the party to take any action to arrive at a net obligation; it does not authorise the party to settle the net obligation by payment.

Note 2: By giving express recognition to approved netting arrangements, subsections (1) and (2) remove the basis for arguing that the arrangements are void as contrary to public policy embodied in the laws dealing with insolvency.

- (3) Subsections (1) and (2) have effect despite any other law (including the specified provisions).

Note: Section 5 defines *specified provisions*.

- (4) If:
 - (a) a party to an approved netting arrangement goes into external administration; and
 - (b) an obligation owed by the party to another party to the arrangement has been netted under the arrangement; and
 - (c) a direct payment by the party owing the obligation to the other party would have been voidable in the external administration if it had been made to settle the obligation on the day on which the netting occurred;

the external administrator may recover from the other party for the benefit of creditors an amount equal to the amount of the obligation.

11 Application for approval of netting arrangement

- (1) A person may apply to the Reserve Bank for approval of a multilateral netting arrangement.
- (2) The application must:
 - (a) be in the prescribed form; and
 - (b) be accompanied by the documents specified in the regulations or required by the Reserve Bank.

12 Reserve Bank may approve netting arrangement

- (1) The Reserve Bank may approve the arrangement if it is satisfied that:
 - (a) systemic disruption in the financial system could result if a participant went into external administration and the arrangement were not approved under this section; and
 - (b) the arrangement provides for netting to occur at least once on each business day; and
 - (c) the rules governing the arrangement establish a coordinator for the arrangement; and
 - (d) the coordinator of the arrangement has the resources, competency and integrity needed to administer the arrangement; and
 - (e) the rules governing the arrangement provide that if a party to the arrangement goes into external administration:
 - (i) the party must notify the coordinator as soon as practicable; and
 - (ii) the coordinator may exclude the party from the arrangement; and
 - (f) the rules governing the arrangement require a party to the arrangement to notify the coordinator as soon as practicable

Section 13

if they have reasonable grounds to suspect that another party to the arrangement is insolvent;
and of any other matters specified in the regulations.

- (2) An approval:
- (a) must be given in writing; and
 - (b) may be given subject to the terms and conditions specified in the approval.

13 Qualified privilege

A party to an approved netting arrangement has qualified privilege for a notice they give the coordinator under the rules governing the arrangement that they have reasonable grounds to suspect that another party to the arrangement is insolvent.

Part 4—Close-out netting contracts

14 Effectiveness of close-out netting contracts

- (1) If:
- (a) Australian law governs a close-out netting contract; and
 - (b) the contract is entered into in circumstances that are within Commonwealth constitutional reach;
- the following provisions apply:
- (c) obligations may be terminated, termination values may be calculated and a net amount become payable in accordance with the contract;
 - (d) paragraph (c) applies despite:
 - (i) any disposal of rights that may be netted under the contract; or
 - (ii) the creation of any encumbrance, or any other interest, in relation to those rights; or
 - (iii) the operation of any encumbrance, or any other interest, in relation to those rights that is created after the commencement of this section;in contravention of a prohibition in the contract;
 - (e) for the purposes of any law, the assets of a party to the contract are taken:
 - (i) to include any net obligation owed to the party under the contract; and
 - (ii) not to include obligations terminated under the contract.
- (2) If:
- (a) a person who is, or has been, a party to a close-out netting contract goes into external administration; and
 - (b) Australian law governs either:
 - (i) the external administration; or
 - (ii) the contract;

Section 14

the following provisions apply:

- (c) obligations may be terminated, termination values may be calculated and a net amount become payable in accordance with the contract;
- (d) obligations that are, or have been, terminated under the contract are to be disregarded in the external administration (but see subsection (5));
- (e) any net obligation owed by the party under the contract that has not been discharged is provable in the external administration;
- (f) any net obligation owed to the party under the contract that has not been discharged may be recovered by the external administrator for the benefit of creditors;
- (g) the termination of obligations, the netting of obligations and any payment made by the party under the contract to discharge a net obligation are not to be void or voidable in the external administration.

Note: By giving express recognition to close-out netting contracts, subsections (1) and (2) remove the basis for arguing that the contracts are void as contrary to public policy embodied in the laws dealing with insolvency.

- (3) A person may not rely on the application of subsection (2) to a right or obligation under a close-out netting contract if the person acquired the right or obligation from another person with notice that that other person was at that time unable to pay their debts as and when they became due and payable.
- (4) Subsections (1) and (2) have effect despite any other law (including the specified provisions).

Note: Section 5 defines *specified provisions*.

- (5) Subsection (1) or (2) does not apply to an obligation owed by a party to a close-out netting contract to another person if:
 - (a) the party goes into external administration; and
 - (b) the obligation is, or has been, terminated under the contract;and

- (c) either:
- (i) the other person did not act in good faith in entering into the transaction that created the terminated obligation; or
 - (ii) when the transaction that created the terminated obligation was entered into, the other person had reasonable grounds for suspecting that the party was insolvent at that time or would become insolvent because of, or because of matters including:
 - (A) entering into the transaction; or
 - (B) a person doing an act, or making an omission, for the purposes of giving effect to the transaction; or
 - (iii) the other person neither provided valuable consideration under, nor changed their position in reliance on, the transaction.

15 Declaration that section 14 does not apply

- (1) The Reserve Bank may declare in writing that section 14 does not apply to a close-out netting contract if it is satisfied that systemic disruption in the financial system could result if a party to the contract went into external administration.

Note: This section is intended to allow the Reserve Bank to require an economically significant multilateral netting arrangement to meet the standards in Part 3 of this Act. It may be necessary to amend the rules governing the arrangement before it can be approved under that Part.

- (2) A declaration under subsection (1):
- (a) may only relate to a contract entered into after the declaration is made; and
 - (b) is to be made by notice published in the *Gazette*; and
 - (c) ceases to have effect 6 months after it is made.

Part 5—Market netting contracts

16 Effectiveness of market netting contracts

(1) If:

- (a) Australian law governs a market netting contract; and
- (b) the contract is entered into in circumstances that are within Commonwealth constitutional reach;

the following provisions apply:

- (c) obligations may be terminated, termination values may be calculated and a net amount become payable in accordance with the contract;
- (d) paragraph (c) applies despite:
 - (i) any disposal of rights that may be netted under the contract; or
 - (ii) the creation of any encumbrance, or any other interest, in relation to those rights; or
 - (iii) the operation of any encumbrance, or any other interest, in relation to those rights that is created after the commencement of this section;in contravention of a prohibition in the contract;
- (e) for the purposes of any law, the assets of a party to the contract are taken:
 - (i) to include any net obligation owed to the party under the contract; and
 - (ii) not to include obligations terminated under the contract.

(2) If:

- (a) a party to a market netting contract goes into external administration; and
- (b) Australian law governs either:
 - (i) the external administration; or
 - (ii) the contract;

the following provisions apply:

- (c) obligations may be netted or terminated, termination values may be calculated and a net amount become payable in accordance with the contract;
- (d) obligations that are, or have been, netted or terminated under the contract are to be disregarded in the external administration;
- (e) any net obligation owed by the party under the contract that has not been discharged is provable in the external administration;
- (f) any net obligation owed to the party under the contract that has not been discharged may be recovered by the external administrator for the benefit of creditors;
- (g) none of the following is to be void or voidable in the external administration:
 - (i) the netting or termination of obligations under the contract;
 - (ii) a payment by the party to discharge a net obligation under the contract;
 - (iii) a payment, or a transfer of property (whether absolutely or by way of security), by the party to meet an obligation under the contract to pay a deposit or margin call.

Note: By giving express recognition to market netting contracts, subsections (1) and (2) remove the basis for arguing that the contracts are void as contrary to public policy embodied in the laws dealing with insolvency.

- (3) Subsections (1) and (2) have effect despite any other law (including the specified provisions).

Note: Section 5 defines *specified provisions*.

Part 6—Administration

17 Prescribed forms

A document that this Act requires to be in a prescribed form must be:

- (a) if a form for the document is prescribed in the regulations—in the prescribed form; or
- (b) if a form for the document is not prescribed in regulations but the Reserve Bank has approved a form for the document—in the approved form.

18 Regulations

The Governor-General may make regulations prescribing matters:

- (a) required or permitted to be prescribed by this Act; or
- (b) necessary or convenient to be prescribed for carrying out or giving effect to this Act.

*[Minister's second reading speech made in—
House of Representatives on 1 April 1998
Senate on 29 May 1998]*

(45/98)

Payment Systems and Netting Act 1998 No. 83, 1998 1