

ANNUAL REPORT 2012

NEW ZEALAND MARKETS DISCIPLINARY TRIBUNAL



CONTENTS

| | |
|----|---|
| 05 | CHAIRMAN'S REPORT |
| 12 | MEMBERS |
| 16 | STATEMENTS OF CASE, FINDINGS AND PENALTIES |
| 29 | NZX REGULATION ANNUAL REPORT TO NZMDT |
| 39 | NEW ZEALAND CLEARING ANNUAL REPORT TO NZMDT |
| 44 | REPORT ON SPECIAL DIVISION ACTIVITIES |
| 53 | DIRECTORY |



CHAIRMAN'S REPORT

CHAIRMAN'S REPORT

REPORTING PERIOD

This report covers the period 1 January 2012 to 31 December 2012.

FUNCTION OF NZ MARKETS DISCIPLINARY TRIBUNAL

The NZ Markets Disciplinary Tribunal (*the Tribunal*) is an independent regulatory body established under the NZ Markets Disciplinary Tribunal Rules (*Tribunal Rules*).

The Tribunal's principal role is to determine whether there has been a breach of the NZX Conduct Rules¹, the NZX Derivatives Market Rules and the Clearing and Settlement Rules of New Zealand Clearing Limited (*CHO*) in matters referred to it by NZX Limited (*NZX*).

In addition, during the reporting period, the Tribunal's role was extended to include determining whether there has been a breach of the Fonterra Shareholders' Market (*FSM*) Rules in matters referred to it by NZX. Launched on 30 November 2012, the FSM is a private registered market operated by NZX on which farmer shareholders can trade Fonterra Co-operative Group Limited shares among themselves.

In the event that the Tribunal finds a breach, its secondary role is to assess and impose penalties. Those penalties are set out in the Tribunal Rules. The Tribunal, in conjunction with NZX, has established Procedures to give guidance to parties dealing with the Tribunal. These Procedures also inform Tribunal members when determining the appropriate penalty to be imposed.

The Tribunal Rules and Procedures can be viewed at <https://www.nzx.com/market-supervision/rules/nz-markets-disciplinary-tribunal-rules>.

The Tribunal serves in an adjudicative role. It is not an inspectorate of market conduct. That role is performed by NZX Regulation. The Financial Markets Authority (*FMA*) is responsible for reviewing how well NZX is meeting its obligations.

The Tribunal also has authority under the Tribunal Rules to:

- a) review decisions made by NZX, CHO or New Zealand Depository Limited (*CDO*), as the context requires, in respect of a waiver or ruling application made under the Rules on referral from the applicant; and
- b) review decisions made by CHO in respect of a claim for compensation under the Clearing and Settlement Rules where the claimant alleges that CHO has failed to determine its claim in good faith.

1. The NZX Conduct Rules comprise 1) the NZX Participant Rules, which govern the conduct of market participants in NZX's three markets – the NZSX Market, the NZAX Market and the NZDX Market; and 2) the NZX Listing Rules governing the conduct of issuers whose securities are listed on NZX's markets.

The Tribunal does not deal directly with members of the public.

DIVISIONS

The Tribunal sits in divisions of three. The Tribunal Chairman normally only chairs divisions hearing cases under the Full Hearing Procedure. No matters were heard under the Full Hearing Procedure during the 2012 reporting period. All matters were heard under the Summary Hearing Procedure.

Tribunal Rule 3.2 establishes a Special Division. The Role of the Special Division is to administer the NZX Conduct Rules as they apply to NZX as a listed company and the five listed funds managed by Smartshares Limited, a subsidiary of NZX. A separate report of the Special Division's activities can be found at page 44 of this annual report.

RELATIONSHIP WITH NZX

The Tribunal is funded by NZX and members of the Tribunal are appointed by NZX (subject to confirmation by the FMA). Apart from that, the Tribunal is wholly independent of NZX.

While it is independent from NZX, the Tribunal and NZX must maintain a constructive working relationship to ensure each can perform their role effectively. I am pleased to report that the Tribunal's working relationship with NZX has strengthened over the course of this past year. This has resulted particularly from increased regular dialogue between NZX Regulation and the Chair and Executive Counsel of the Tribunal to ensure better co-ordination of, and communication regarding, operational matters.

NZX Regulation also consulted with the Tribunal during its development of their Enforcement Procedures, an internal NZX document outlining NZX's approach to enforcing the rules of the markets it operates (*the Market Rules*). The Enforcement Procedures are intended to guide and inform NZX staff on the general policies, procedures and decision-making processes of NZX Regulation when investigating possible breaches of the Rules, including with regard to the referral of matters to the Tribunal. The Tribunal is advised that the Enforcement Procedures were implemented by NZX Regulation in December 2012.

MATTERS HANDLED BY THE TRIBUNAL

During the reporting period five matters were referred to the Tribunal. All were completed during the reporting period and each was completed within two months of referral by NZX. Details of each of these matters can be found in the section of this annual report entitled 'Statements of Case, Findings and Penalties' at page 16.

The Tribunal was not called on to consider any matters arising under the NZX Derivatives Market Rules, the Clearing and Settlement Rules or the FSM Rules during the reporting period.

Delay in referral of matters

The processes of the Tribunal are designed to be efficient and expedient in order to meet the requirements of the market for speed and certainty of interpretation and administration of the NZX Market Rules. The Tribunal's Rules contain strict deadlines in which actions must be taken by it once a matter is referred by NZX. However, this objective is frustrated when a significant period of time elapses between when NZX becomes aware of the alleged breach and when the matter is ultimately referred to the Tribunal.

In relation to those matters referred to the Tribunal in 2012, the average time between when NZX became aware of the alleged breach and when the matter was referred to the Tribunal was approximately 6 months. In one case, this period was approximately nine months. In two cases referred to the Tribunal in 2012 involving NZX Advisors, NZX took several months from the date of its last correspondence with the respondent to refer the matter to the Tribunal. Both Advisors expressed their concern at the length of the process and the effect this had on their professional and personal lives.

The Tribunal is also aware of other matters, one of which has not been referred to the Tribunal, involving possible breaches which occurred over a year ago and another which has taken more than a year from the time that NZX became aware of the breach until it decided not to refer the matter to the Tribunal.

As noted above, NZX has now developed Enforcement Procedures. The Tribunal's hope is that this will lead to better processing times in the coming year.

Number of referrals

NZX has provided the Tribunal with its regulatory report at page 29. That report identified a number of breaches of the Rules detected by NZX. The matters being referred to the Tribunal represent only around 10% of the breaches being identified.

The Tribunal understands that the matters currently being referred to it represent serious breaches of the Rules. The Tribunal is an equally effective forum for addressing more minor or technical breaches. The summary hearing procedure is, in fact, designed to deal with minor breaches. It is recognised that in many cases, referral of minor matters to the Tribunal is not warranted and that those matters are better addressed by NZX in other ways. However, referral of minor breaches to the Tribunal may, on occasion, be beneficial, both to signal to participants that NZX is focussed on particular breaches (especially where such breaches are occurring reasonably frequently) and to avoid the risk of participants becoming complacent in complying with what they may perceive to be less significant obligations under the Market Rules.

MEMBERSHIP

I noted in my report last year that for the future effective operation of the Tribunal, the on-going review of the Tribunal's membership is essential. I also identified several areas of need in our membership. I am pleased to say that nine new Tribunal members were appointed in 2012.

Richard Bodman is the Head of Compliance at First NZ Capital Securities Limited, and is a Market Participant, Clearing Appointee and Derivatives Market Appointee to the Tribunal. Following Richard's appointment, the Tribunal now has the requisite Clearing Appointee and Derivatives Market Appointee required under our Rules.

Trevor Janes, a company director and independent financial consultant, and James Ogden, also a company director and consultant, are Issuer Appointees to the Tribunal.

Kevin Baker, CFO of Infratil Limited and its manager, HRL Morrison & Co, Danny Chan, a company director, Susan Peterson, at that time General Manager Business and Performance for ANZ's Global Wealth and Private Banking business, Mariëtte van Ryn, General Manager Regulatory Affairs & General Counsel NZ for Westpac, and Leonard Ward, lawyer, are Public

Appointees to the Tribunal. Nick Hegan, a partner at law firm Russell McVeagh, is a Legal Appointee to the Tribunal.

The Tribunal also farewelled a number of its founding members who retired at the 2012 annual meeting. I express my gratitude to Patsy Reddy, Michael Jeffs, Simon McArley, Stephen Moir and Paul Ridley-Smith for their service to the Tribunal over a number of years.

At the end of the reporting period, the Tribunal comprised six Public Appointees, six Issuer Appointees, eight Legal Appointees, four Market Participant Appointees and one member who qualifies as both a Clearing Appointee and Derivatives Market Appointee.

The Tribunal will again lose a number of its most experienced members who must retire at the annual meeting this year. The Tribunal is working with NZX on a public nominations process to attract suitably qualified candidates.

Remuneration Review

Members' remuneration was reviewed this year as required under the Tribunal Rules. Following a process of consultation between the Head of Regulation and I, the NZX Board set new rates for members.

RULES SUB-COMMITTEE

At the Tribunal's 2012 annual meeting, members agreed to convene a Rules Sub-Committee to consider a number of matters to determine whether certain amendments to the Tribunal Rules were desirable and the implications of such amendments.

The Tribunal agreed, as a result of the Rules Sub-Committee's review, to recommend one Rule change to NZX to enable members who are part of a division to complete any case they are sitting on at the time of their retirement from the Tribunal. There is already a provision in the Tribunal Rules to permit members who have resigned to continue to consider matters before a division on which they are sitting at the time of their resignation. I am pleased that NZX agreed to our suggested amendment and has submitted the Rule change to the FMA for its approval.

RESOURCING

Tribunal Rule 14.1.2(d) requires a statement from the Tribunal confirming whether or not it believes that adequate resources have been made available to it to undertake its role under the NZMDT Rules. I so confirm. NZX has provided all the assistance which the Tribunal has needed in the performance of its role.

I note that NZX has formalised Rachel Batters' role as Executive Counsel to the Tribunal and has retained the services of Stephen Layburn to act as Executive Counsel should Rachel be unavailable.

DISCIPLINARY FUND

The Tribunal Rules restrict the use that may be made of money paid into the Disciplinary Fund to enforcement action, the costs of the Tribunal and Appeals Panel (and their staff), educational initiatives relevant to the regulation of NZX's markets and the futures and options industry, rules revision and any other use approved by the FMA.

The Disciplinary Fund accounts are to be found at page 37 of this annual report.

During the year, NZX wrote off \$22,703 in bad debts. This amount relates to two cases from 2008 involving individuals who are no longer NZX Advisors. NZX considered that it was unlikely to recover this money.

The Tribunal receives regular reports from NZX regarding the recovery of penalties and costs imposed by the Tribunal. I am pleased to say that all of the amounts imposed in respect of cases referred to the Tribunal in 2012 have been recovered in full.

APPEALS PANEL

The Appeals Panel is responsible for determining appeals made against determinations of the Tribunal. The Appeals Panel is independent of both NZX and the Tribunal. Members of the Appeals Panel are appointed by the FMA.

During the reporting period, no appeals have been made against determinations of the Tribunal requiring referral to the Appeals Panel.

Resources

Mr Euan Abernethy, the Chairman of the Appeals Panel, also confirms that it has had adequate resources to undertake its role under the NZMDT Rules during the reporting period.

I express my appreciation to all members of the Tribunal who have sat in 2012.

I wish to acknowledge the valuable contribution which Falcon Clouston, Phillip Meyer and Tim Williams, all of whom have been members of the Tribunal since its establishment and who will be retiring at this year's annual meeting, have made over a period of many years. In particular, I wish to thank the Deputy Chairman, William Stevens and the Chairman of the Special Division, Peter Wilson. Both gentlemen were also foundation members of the Tribunal and will also retire from the Tribunal this year. Their contribution over the years has been significant and they will be sorely missed.



Derek Johnston | CHAIRMAN
12 April 2013



MEMBERS

MEMBERS

MEMBERS OF THE TRIBUNAL AS AT 31 DECEMBER 2012

LEGAL

Derek Johnston (Chairman), Andrew Beck, David Boldt, David Flacks, Mark Freeman, Nick Hegan, Don Holborow and Tim Williams.

LISTED ISSUER

Peter Wilson (Special Division Chairman), Jo Appleyard, Falcon Clouston, Trevor Janes, James Ogden and Alison Paterson.

MARKET PARTICIPANTS

William Stevens (Deputy Chairman), Richard Bodman, Shane Edmond and Campbell Stuart.

MEMBERS OF THE PUBLIC

Kevin Baker, Danny Chan, Phillip Meyer, Susan Peterson, Noeline Munro*, Mariëtte van Ryn and Leonard Ward.

CLEARING PARTICIPANTS

Richard Bodman

DERVIATIVES PARTICIPANTS

Richard Bodman

* Noeline Munro's membership classification changed with the consent of NZX from Market Participant to Public Appointee in December 2012 following her retirement from Craigs Investment Partners Ltd.

MEMBERS OF THE SPECIAL DIVISION AS AT 31 DECEMBER 2012

Peter Wilson (Chairman), Kevin Baker, Andrew Beck and Shane Edmond**.

Rachel Batters acts as Executive Counsel to the Tribunal and the Special Division.

MEMBERS OF THE APPEALS PANEL AS AT 31 DECEMBER 2012

Euan Abernethy (Chairman), Brian Allison, Bill Thurston and John Upton QC.

** Kevin Baker and Shane Edmond were appointed to the Special Division in June 2012 following the retirement of Michael Jeffs and Paul Ridley-Smith from the Tribunal.



STATEMENTS OF CASE, FINDINGS AND PENALTIES

THIS SECTION OF THE REPORT ADDRESSES THOSE MATTERS
REQUIRED BY TRIBUNAL RULE 14.1.3(a) - (c) WHICH PROVIDES:

“14.1.3 The Tribunal shall create and provide an annual regulatory report (the Annual Regulatory Report) to the public by the end of April of the following year using as a minimum the information from the report in respect of each year provided to the Tribunal by NZX and CHO above, and that collated by itself below:

- a) number of statements of case issued by NZX and CHO and the type of matters addressed in those statements of case;
 - b) the findings of the Tribunal and the Appeal Panel in respect of each statement of case issued by NZX and CHO, provided such disclosures are consistent with any decision on publication made by the Tribunal;
 - c) any penalties imposed by the Tribunal and the Appeal Panel; and..”
-

NZMDT 01/12 NZX V INSURED GROUP LIMITED (INS)

Division: Wilson (chair), Holborow and Appleyard

Statement of Case served: 27 January 2012

Date of Determination: 21 February 2012

MATERIAL FACTS

The statement of case alleged that INS had breached NZSX Listing Rules 10.5.1, 6.1.1 and 6.2.3.

Rule 10.5.1 requires an Issuer to release its annual report to the market within three months of its financial year end. INS' 2011 financial year ended on 30 June 2011. INS was therefore required to release its annual report by 30 September 2011. INS did not release its annual report until 25 November 2011.

Rule 6.1.1 requires a notice of meeting to an Issuer's quoted security holders, regarding matters other than those listed in Rule 6.1.2, to be approved by NZX. Rule 6.2.3 requires a notice of meeting to security holders to contain or be accompanied by sufficient explanation to enable a reasonable person to understand the effect of the resolutions proposed in the notice of meeting.

On 24 October 2011, INS submitted a draft notice of annual meeting (*Notice*) to NZX for review. The explanatory statement accompanying the Notice stated that the annual report was available on the INS website. NZX approved the Notice on the basis that the information provided by INS was complete and accurate. NZX understood that, at the time the Notice was to be sent to shareholders, the annual report would be available on the INS website. On 1 November 2011, INS released the Notice with the statement that the annual report was available on its website, when it was not.

TRIBUNAL FINDINGS

An Issuer's compliance with the periodic reporting requirements in the Listing Rules is fundamental. Information in relation to the performance and financial position of an Issuer must be promptly made available to the market. Any breach of these Rules, and the resulting trading halt, brings the market into disrepute.

The Tribunal has signalled that it will increase the penalties it imposes for such breaches to act as a deterrent.

The Tribunal considered that there were a number of aggravating factors in this case. INS did release its preliminary announcement on 29 August 2011, within the time allowed under the Rules. However, following this release, INS shareholders remained uninformed as to the financial position of INS for approximately two months. During that period there was uncertainty as to whether INS' auditors would be able to issue an unqualified opinion on INS' financial statements. This heightened the need for timely advice to shareholders and in the Tribunal's view elevated the seriousness of the breach.

The Tribunal did not find the matters noted in mitigation by INS for its failure to provide its annual report when due to be compelling. To the contrary, the undertaking of numerous complex transactions, the migration to Australia and change in key personnel were all reasons for ensuring that shareholders and the market were fully informed of INS' position in a timely manner.

The Tribunal agreed with NZX that given the annual report was not available at the time the Notice was distributed to shareholders, INS breached Rule 6.1.1.

The Tribunal also considered that INS had breached Rule 6.2.3. The Tribunal noted that it is imperative that shareholders are presented with timely and accurate information in order to make informed decisions when asked to vote at meetings. Accordingly, Issuers are obligated under the Rules to ensure that notices contain or are accompanied by sufficient information. By not having its annual report available to shareholders, as INS had advised them in its Notice, until 3 Business Days before its meeting, INS did not meet this obligation. The annual report was critical information for shareholders, particularly given INS' financial circumstances and the number of changes occurring at the company.

PENALTY:

The penalties imposed by the Tribunal were:

- a) An order to pay **\$50,000**, being \$30,000 for the breach of Rule 10.5.1, \$15,000 for the breach of Rule 6.2.3 and \$5,000 for the breach of Rule 6.1.1.
- b) A public censure of INS.

COSTS

INS was required to pay the costs of the Tribunal and NZX in considering the matter.

PUBLICATION

The Tribunal's determination was released in full to the market.

NZMDT 02/12 NZX V HERITAGE GOLD NZ LIMITED (HGD)

Division: Flacks (chair), Paterson and Meyer

Statement of Case served: 16 March 2012

Date of Determination: 26 April 2012

MATERIAL FACTS:

The statement of case alleged that HGD had breached:

- a) Rule 3.3.1(c) from 6 April 2011 until 2 August 2011, because its Board did not include at least two Independent Directors; and
- b) Rule 3.6.2(b) from 31 March 2007 until 15 November 2011, because its Audit Committee was not comprised of at least three members.

HGD did not dispute the breaches but made submissions in mitigation, including that it took active steps to rectify them before the case was brought before the Tribunal.

TRIBUNAL FINDINGS:

Any breach by an Issuer of the corporate governance provisions in the Rules is serious. The Rules provide confidence to shareholders and prospective investors that the Issuer is abiding by the principles of corporate governance expected of a Listed entity. In addition, an appropriately comprised audit committee is critical in ensuring that an Issuer maintains a robust audit process.

The Tribunal noted that where an Issuer has only the minimum number of Independent Directors on its Board, as HGD did, it is imperative that the Board have a succession plan in place should one of these members resign. HGD did seek a waiver from Rule 3.3.1(c), but the Tribunal gave little weight to that, as the waiver was sought several months after the breach had first occurred.

With respect to the breach of Rule 3.6.2(b), the Tribunal was very concerned about the significant period of time – approximately four and a half years – that HGD was in breach. It was fortunate in this case that the HGD Audit Committee had remained in compliance with Rule 3.6.2(c) – having a majority of members who are Independent Directors – and that the Managing Director was generally in attendance. However, the Tribunal noted that being unaware of the Rules is not a satisfactory reason for non-compliance. It is beholden on all Issuers and their Directors to understand the obligations the Rules impose and to ensure compliance with them.

PENALTY:

The penalties imposed by the Tribunal were:

- a) An order to pay **\$15,000**, being \$10,000 for the breach of Rule 3.3.1(c) and \$5,000 for the breach of Rule 3.6.2(b).
 - b) A public censure of HGD.
-

COSTS:

HGD was required to pay the costs of the Tribunal and NZX in considering the matter.

PUBLICATION:

The Tribunal's determination was released in full to the market.

NZMDT 03/12 NZX V CRAIGS INVESTMENT PARTNERS LIMITED (CRAIGS)

Division: Boldt (chair), Janes and Stuart

Statement of Case served: 17 May 2012

Date of Determination: 9 July 2012

MATERIAL FACTS:

The statement of case alleged that Craigs had breached Participant Rules 4.5.2, 8.8, 10.2.2 and 10.8.1 as a result of two separate orders which were directly entered into the NZX Trading System by its client in error. Each error created considerable market disruption.

Under the Rules, a Trading Participant may provide Direct Market Access (*DMA*) to a client who is designated as a DMA Authorised Person. This status allows authorised clients to submit orders directly into the NZX Trading System without first passing them through the Participant's trading desk.

Craigs provided DMA to a client under an access agreement which authorised the client to access Craigs' own trading system, provided by IRESS (NZ) Limited (*IRESS*), to submit trading messages to NZX through a process known as Direct Client Order Processing.

On 2 August 2011, using Craigs' trading system, the client entered a market order into the NZX Trading System to buy 640,000 Telecom Corporation of New Zealand Limited (*TEL*) shares (*the TEL order*). No price was specified for the TEL order. The TEL order was immediately matched against more than 17 sell orders and resulted in a change to the traded price of TEL shares from \$2.68 to \$3.31, a 23.5% increase.

NZX Market Surveillance (*NZXMS*) initiated an investigation and was advised by Craigs that the client had entered the TEL order in error. The client had intended to place an order for execution by Craigs' trading desk and had not intended that the order be entered directly into the NZX Trading System. NZXMS put TEL into a trading halt and cancelled the trades directly arising from the TEL order, along with all the trades in TEL that occurred between the TEL order and the trading halt. This resulted in 52 trades being cancelled.

On 15 November 2011, again using Craigs' trading system, the (same) client entered a market order into the NZX Trading System to buy 30,000 Rubicon Limited (*RBC*) shares (*the RBC order*). The RBC order immediately matched against three sell orders, resulting in a change to the traded price of RBC from \$0.39 to \$0.58, a 48% increase.

On becoming aware of the RBC order, NZXMS halted trading in RBC and contacted Craigs who advised NZXMS that the RBC order had again been entered in error. The client had intended to place an order for execution by Craigs' trading desk and had not intended that order be entered directly into the NZX Trading System. NZXMS cancelled the relevant trades resulting from the RBC order.

TRIBUNAL FINDINGS:

Craigs admitted that it failed to have appropriate – or indeed any – filters in place at the time of the TEL order, and that the market disruption which

followed was a consequence of this. The Tribunal noted that it was Craigs' responsibility under the Participant Rules to ensure that proper filters were in place for its DMA clients. Appropriate filters would have rejected an order of this kind before it was routed to the NZX Trading System.

Craigs denied it was responsible for the market disruption which followed the RBC order. While it acknowledged that the order entered by its client led to disorder in the market, it did not accept it was responsible for this. The RBC order was not rejected by the new filters put in place at the request of Craigs following the TEL order. In correspondence with NZX, IRESS accepted that the RBC order was a result of a software error on its part. Craigs submitted that the latent software error was something it did not know about, and could not have known about, and sought to rely on a defence of total absence of fault.

The Tribunal noted that in light of Rule 4.5.2, a participant cannot avoid responsibility for errors in its trades by pointing to the actions or inactions of a third party supplier. Participants are responsible for their own trades. While Craigs was entitled to contract part of its order processing to an outside provider, the effect of the Rules is that each participant is responsible for errors associated with its trades. Because Craigs chose to use IRESS to complete a transaction which was its responsibility, it must also accept responsibility for the error in the IRESS system. However, the fact Craigs had taken steps to ensure filters were in place after the TEL order was a mitigating factor relevant to determining the appropriate penalty.

NZX asked the Tribunal to impose a concurrent penalty for both the TEL order and RBC order, but submitted that the penalties for the breach of each of the Rules should be accumulated. The Tribunal agreed with Craigs that this was an inappropriate way to construct the penalty. The Tribunal considered that all of the offences which were established as a result of the TEL order and the RBC order arose from the same acts and omissions. Craigs was no more culpable because its conduct happened to infringe four Participant Rules than it would have been if it had breached only one. The correct focus is on the acts and omissions which led to the breach (together with the serious consequences which flowed), rather than the number of provisions which were breached. The Tribunal determined it should assess the appropriate level of penalty for the most serious of the breaches and then apply it concurrently across all four Rules.

PENALTY:

The penalties imposed by the Tribunal were:

- a) An order to pay **\$40,000**, being \$30,000 in respect of the breaches regarding the TEL order and \$10,000 for the breaches regarding the RBC order.
- b) A public censure of Craigs.

COSTS:

Craigs was required to pay the costs of the Tribunal and NZX in considering the matter.

PUBLICATION:

The Tribunal's determination was released in full to the market.

NZMDT 04/12 NZX V A NZX ADVISOR

Division: Holborow (chair), Bodman and Ward

Statement of Case served: 9 November 2012

Date of Determination: 14 December 2012

MATERIAL FACTS:

In 2011, a personal relationship developed between the NZX Advisor and a client of the firm. That personal relationship meant that the client should have been classed as a Prescribed Person under the Participant Rules. However, the NZX Advisor failed to do so.

In October 2011, the NZX Advisor lent the client \$42,000, which the client used to purchase 30,000 shares in the initial public offering undertaken by Summerset Group Holdings Ltd (*SUM*). In November 2011, the client sold the *SUM* shares. Using the funds from the sale of the *SUM* shares, and some additional funds deposited by the client, the client purchased 18,700 shares in the initial public offering undertaken by Trade Me Group Ltd (*TME*). In December 2011, the client transferred 15,000 *TME* shares to the NZX Advisor, via an off-market transfer.

The statement of case alleged that in doing so:

1. the client, a Prescribed Person, participated in the *SUM* and *TME* initial public offerings in breach of Rule 10.5.3;
 2. the client and the NZX Advisor acquired securities without obtaining written authority from the Firm, in breach of Rule 10.5.1; and
 3. the NZX Advisor did not refrain from conduct that was detrimental to NZX and its markets, and failed to comply fully with all applicable Rules, and at all times observe Good Broking Practice, in breach of Rules 5.8.1 and 8.1.1.
-

TRIBUNAL FINDINGS:

The Tribunal approved a settlement agreement between the parties under which the NZX Advisor accepted the breach of Rules 5.8.1, 8.1.1, 10.5.1 and 10.5.3. As contemplated by section 10 of the Tribunal Rules, the settlement agreement became the determination of the Tribunal.

The Tribunal noted the following mitigating circumstances when considering the appropriateness of the penalty agreed between the parties:

1. No client had suffered any direct loss as a result of the breaches.
2. The NZX Advisor had faced disciplinary action from the Firm.
3. The NZX Advisor had not been involved in repeated offences (as substantiated by a review conducted by the Firm).
4. The NZX Advisor had admitted to the breaches.

PENALITY:

Under the terms of the settlement agreement, the NZX Advisor was ordered to pay **\$16,000**.

COSTS:

The NZX Advisor was required to pay the costs of the Tribunal and NZX in considering the matter.

PUBLICATION:

A public statement in the form attached to the settlement agreement and approved by the Tribunal was released to the market. The public statement did not name the NZX Advisor.

The Tribunal has published guidelines to explain its policy on the naming of respondents who are market participants (*the Policy*). In developing the Policy, the Tribunal took into account the need to ensure that its process was transparent and parties brought before it were named. However, the Tribunal also took into account the punitive effect of naming parties, regardless of the seriousness of their breach. The Policy seeks to strike a balance between the public interest in naming respondents and the detriment to the respondent from being named.

Under the Policy, the name of a respondent is most likely to be published when:

- a. The public has been harmed, or public confidence in the sector has been damaged.
- b. The Respondent has been involved in repeated offences, and shown disregard for the NZX Participant Rules.
- c. The penalty for the Respondent falls within Penalty Bands 4 to 8 of the Procedures.

The Tribunal considered that in this case no member of the public had been harmed by the breaches. The Tribunal had also been advised that the NZX Advisor's Firm had conducted a review of the Advisor's files and found that the Advisor had adhered to good practice and that there was no reason to take any further action beyond the disciplinary action already taken by the Firm.

The Tribunal noted that while the breaches did fall within Penalty Band 5 of the Tribunal Procedures, it must exercise its discretion on a case by case basis.

In this case, the Tribunal considered that the likely detrimental consequences of publicly naming the NZX Advisor were too severe when given the nature and circumstances of the breaches. The Tribunal considered that mitigating circumstances (as outlined above) meant that the public interest in naming the NZX Advisor did not outweigh the detriment to being named.

In this case, a market announcement designed to have both an educational benefit and a deterrent effect for other NZX Advisors regarding a similar breach of the Rules would serve the public interest. The release of the NZX Advisor's name was not necessary to achieve that objective.

NZMDT 05/12 NZX V A NZX ADVISOR

Division: Holborow (chair), Bodman and Ward

Statement of Case served: 9 November 2012

Date of Determination: 7 December 2012

MATERIAL FACTS:

The NZX Advisor transferred funds to a client. The client used those funds to acquire 1,500 shares in the initial public offering undertaken by Trade Me Group Ltd (*TME*). These shares were subsequently transferred, via an off-market transfer, to the NZX Advisor.

The statement of case alleged that in doing so the NZX Advisor:

1. participated in the TME initial public offering in breach of Rule 10.5.3;
 2. acquired securities without obtaining written authority from the Firm, in breach of Rule 10.5.1; and
 3. did not refrain from conduct that was detrimental to NZX and its markets, and failed to comply fully with all applicable Rules, and at all times observe Good Broking Practice, in breach of Rules 5.8.1 and 8.1.1.
-

TRIBUNAL FINDINGS:

The Tribunal approved a settlement agreement between the parties under which the NZX Advisor accepted the breach of Rules 5.8.1, 8.1.1, 10.5.1 and 10.5.3. As contemplated by section 10 of the Tribunal Rules, the settlement agreement became the determination of the Tribunal.

The Tribunal noted the following mitigating circumstances when considering the appropriateness of the penalty agreed between the parties:

1. The breaches were a one-off offence (as substantiated by a review conducted by the Firm).
 2. No client suffered as a result of the breaches.
 3. There was an early admission of fault by the NZX Advisor.
 4. The NZX Advisor has faced disciplinary action from the Firm.
-

PENALITY:

Under the terms of the settlement agreement, the NZX Advisor was ordered to pay **\$10,000**.

COSTS:

The NZX Advisor was required to pay the costs of the Tribunal and NZX in considering the matter.

PUBLICATION:

A public statement in the form attached to the settlement agreement and approved by the Tribunal was released to the market. The public statement did not name the NZX Advisor.

The Tribunal's guidelines on the naming of respondents who are market participants is described on page 25.

The Tribunal considered that in this case no member of the public had been harmed by the breaches. The Tribunal had also been advised that the NZX Advisor's Firm had conducted a review of the Advisor's files and found that the breaches were a one-off offence.

The Tribunal noted that while the breaches did fall within Penalty Band 5 of the Tribunal Procedures, it must exercise its discretion on a case by case basis.

In this case, the Tribunal considered that the likely detrimental consequences of publicly naming the NZX Advisor were too severe when given the nature and circumstances of the breaches. The Tribunal considered that mitigating circumstances (as outlined above) meant that the public interest in naming the NZX Advisor did not outweigh the detriment to being named. The public statement agreed by the parties would have both an educational benefit and a deterrent effect for other NZX Advisors. The release of the NZX Advisor's name was not necessary to achieve that objective.



NZX REGULATION ANNUAL REPORT TO NZ MARKETS DISCIPLINARY TRIBUNAL

THIS SECTION OF THE REPORT ADDRESSES THOSE MATTERS
REQUIRED BY NZMDT RULE 14.1.1 (a) - (c) WHICH PROVIDES:

"14.1.1 Following the end of each calendar year NZX shall collate the following information for that year and provide to the Tribunal as a report by the end of February of the following year:

- a) breaches of the NZX Market Rules identified by NZX;
 - b) complaints received by NZX in respect of Participants (other than Clearing Participants, Lending Clearing Participants or Depository Participants);
and
 - c) the use of the proceeds of the Disciplinary Fund."
-

1. INTRODUCTION

NZX Regulation (“**NZXR**”) is the regulatory body of NZX Limited (“**NZX**”). NZXR is responsible for the front line regulation of NZX’s markets in accordance with its Market Rules as required by section 36G of the Securities Markets Act 1988 (“**SMA**”) and the NZX Derivatives Market Rules (the “**Derivatives Rules**”).

The NZ Markets Disciplinary Tribunal (the “**Tribunal**”) is an independent disciplinary body charged with determining and providing remedies for referrals made to it by NZXR.

NZXR provides this report, dated 28 February 2013, to the Tribunal pursuant to Rule 14.1.1 of the NZ Markets Disciplinary Tribunal Rules (the “**NZMDT Rules**”). Pursuant to NZMDT Rule 14.1.1, NZX must submit to the Tribunal by 28 February 2013 a report for the 2012 calendar year, which contains the following information:

- a) breaches of the NZX Market Rules (including the NZSX/NZDX Listing Rules and NZAX Listing Rules, the Fonterra Co-operative Group Limited FSM Rules (together the “**Listing Rules**”) and the NZX Participant Rules), the Derivatives Market Rules and any other rules or regulations of NZX from time to time identified by NZX;
- b) complaints received by NZX in respect of Participants (other than Clearing Participants, Lending Clearing Participants or Depository Participants); and
- c) the use of the proceeds of the Discipline Fund.

This report provides information for the period 1 January 2012 to 31 December 2012 (the “**Period**”). Capitalised terms used in this report that are not otherwise defined in this report have the meanings given to them in the NZMDT Rules.

This report does not refer to referrals made by NZXR to the Financial Markets Authority (“**FMA**”) for breaches of the SMA NZXR detects while carrying out its regulation and surveillance duties (for example, in respect of suspected insider trading, market manipulation or director and officer disclosure).

If a matter was referred to the FMA, it is also included in this report if the matter was either a breach of the Listing Rules or the NZX Participant Rules, or was a complaint received by NZXR in respect of a Market Participant, Derivative Participant or a Listed Issuer.

2. MARKET PARTICIPANTS AND DERIVATIVES MARKET PARTICIPANTS

This section 2 summarises:

- i) breaches of the NZX Participant Rules and the Derivatives Market Rules identified by NZXR; and
- ii) complaints received by NZXR in respect of Market Participants and Derivatives Participants.

A. SUMMARY OF BREACHES OF THE NZX PARTICIPANT RULES IDENTIFIED BY NZXR

- i) **Significant breaches of the NZX Participant Rules referred to NZMDT**
There were 3 cases representing significant breaches of the NZX Participant Rules referred to the Tribunal during the Period. 2 of these breaches were identified during the Period, and 1 was identified during 2011. These cases are described under the heading "Statement of Case, Findings and Penalties" in NZMDT's Annual Report.
- ii) **Other breaches of the NZX Participant Rules**
In addition to the above cases, NZXR identified 28 breaches of the NZX Participant Rules 26 of which were not considered sufficiently serious to warrant a referral to the Tribunal and 2, in respect of which a referral is to be made, or which are under investigation.

Of these 28 cases, 19 were identified during NZXR's onsite inspections, capital adequacy reviews and other targeted investigations. These breaches were subsequently highlighted to the relevant Market Participant, either as part of an NZXR inspection report or in correspondence (containing, as appropriate, action points for Market Participants to resolve, or implement, within specified timeframes). The other breaches were identified through NZXR's other monitoring work.

A total of 13 breaches of NZX Participant Rule 18.6.1 (d) (Client Funds Account overdrawn) were identified. These were largely self-reported by the relevant Market Participant. 12 of these breaches were the result of an error in processing bank transactions by the Market Participant's employees and one error was the result of a bank error. Where the breach was a one-off and had been remedied by the Market Participant, no further action was taken by NZXR. Two Market Participants received warning letters in relation to repeated breaches of Rule 18.6.1 (d).

There were 6 breaches of Section 19 of the NZX Participant Rules relating to capital adequacy. No further action was taken in respect of 3 of these breaches that related to late reporting of daily movements in capital where the liquid capital ratios exceeded 120% of the minimum requirement. These breaches were resolved promptly and NZXR reminded the Market Participants of the requirement to ensure reporting deadlines are met. The other 3 breaches resulted in warning letters being issued to Market Participants; 1 in relation to the Market Participant overstating its liquid capital ratio and failing to notify NZXR of changes in its capital ratio; and 1 in relation to the Market Participant failing to comply with a waiver condition to immediately notify NZXR of significant transactions. 1 related to the Market Participant's capital ratio falling to 97% of the minimum requirement. In this case NZXR and CHO were monitoring the Market Participant's capital position closely during the course of a significant transaction. Given that these 3 matters related to a singular breach of the capital adequacy requirements and the Market Participants did not have a history of similar breaches, NZXR and CHO decided not to refer these matters to NZMDT. However, NZXR and CHO have reserved the right to refer to these matters in any future disciplinary proceedings if subsequent breaches arise.

1 breach of NZX Participant Rules 9.1.1(c)(d) and 9.10.2 (Duty of Care and Discretionary Accounts) resulted in a warning letter being issued to the Advisor concerned.

2 breaches of NZX Participant Rule 10.5.1 (Employee Trading) were self-reported. Both of these breaches were in relation to individuals that did not have direct contractual relationships with NZX and so could not be referred to the Tribunal. 1 incident resulted in a warning letter being issued to the Director concerned, noting NZX's concern at the behavior, and the other incident is currently under investigation.

1 breach of NZX Participant Rule 15.17.1 (Failure to Dispatch Contract Notes) is currently under investigation.

1 alleged breach of NZX Participant Rules in relation to trading in an Issuer's securities. 1 is currently under investigation and is expected to be completed by the end of Q2 2013.

Other minor breaches noted during the Period included:

- Late notification of a new Director;
- Late notification of an Advisor's resignation;
- An algorithmic trading system error where the Participant's system failed to process the current best offer price and which resulted in a large number of passive buy orders being submitted into the central order book, in breach of NZX Participant Rules 4.5.2, 8.8, 10.8.1 and 10.8.2. The orders were not executed, and the Participant cleared the order book. No further action was taken by NZXR in relation to this one-off incident; and
- Failure of an Advisor to comply with the 10 Business Day holding period before selling securities, in breach of Rule 10.5.9.

B. SUMMARY OF COMPLAINTS RECEIVED BY NZXR IN RESPECT OF MARKET PARTICIPANTS

NZXR received a total of 4 written complaints in respect of Market Participants during the Period. Of these complaints 3 were determined not to be a breach of the NZX Participant Rules.

1 complaint was in relation to trading in an Issuer's securities. NZXR's investigation into this is ongoing.

C. SUMMARY OF BREACHES OF THE DERIVATIVES MARKET RULES IDENTIFIED BY NZXR

NZXR did not identify any breaches in respect of the Derivatives Rules during the period.

D. SUMMARY OF COMPLAINTS RECEIVED BY NZXR IN RESPECT OF DERIVATIVES MARKET PARTICIPANTS

NZXR did not receive any complaints in respect of Derivatives Participants during the period.

3. NZX ISSUERS

This section 3 summarises:

- i) breaches of the Listing Rules identified by NZXR; and
- ii) complaints received by NZXR in respect of Listed Issuers.

A. SUMMARY OF BREACHES OF THE LISTING RULES IDENTIFIED BY NZXR

- i) **Significant breaches of the Listing Rules referred to NZMDT**
There were 2 cases representing significant breaches of the Listing Rules by Issuers that were referred to the Tribunal during the Period. Both of these cases were Identified in 2011 and are described under the heading "Statement of Case, Findings and Penalties" in NZMDT's Annual Report.
- ii) **Other breaches of Listing Rules**
3 cases representing significant breaches of the Listing Rules by Issuers have been referred to the Tribunal in January and February 2013. 2 of these cases related to periodic reporting breaches. 1 case related to the corporate governance provisions and a failure to obtain NZXR approval to a Notice of Meeting.

In addition to the above breaches, NZXR identified 39 breaches of the Listing Rules; 38 of which were not considered sufficiently serious to warrant referral to the Tribunal, and 1 of which is under investigation at the end of the Period.

Of the 39 breaches, the majority related to a minor breach of the disclosure requirements under the Rules. 21 breaches related to Issuers' failures to make announcements to the market at the same time as information was sent to shareholders. 5 breaches related to Issuers' failures to make announcements to NZX at the same time as the information was sent to the Issuer's Home Exchange. NZXR wrote to these Issuers, noting there has been a breach of the Listing Rules and reminding the Issuer of its obligations under the Listing Rules.

2 breaches related to periodic reporting requirements under the Listing Rules, particularly in regards to delay in releasing half-year reports and preliminary results. For each of these, NZXR communicated with the Issuers and ensured that the reports and results were released to the market as soon as possible. NZXR wrote to each of the Issuers, reminding them of the importance of the periodic reporting requirements in ensuring the symmetry of information in the market and of the periodic reporting obligations under the Listing Rules.

4 breaches related to Issuers' failures to provide all of the information required by the Listing Rules in the annual report. In respect of each breach, NZXR sent a letter of enquiry asking about the processes which the Issuer has in place to ensure compliance with the Listing Rules governing the content of the annual reports and enquiring as to why the breaches occurred.

1 breach related to an Issuer's failure to obtain NZX approval before executing amendments to a trust deed required as a result of a required legislative change. NZXR reminded the Issuer of the requirement under the Rules that the trust deed be approved prior to execution.

1 breach related to an Issuer's failure to provide information required as a condition of a waiver granted. NZXR wrote to the Issuer, reminding it of the waivers conditions.

Other breaches included 1 relating to an Issuer's incorrect use of an

embargo when announcing price sensitive information; 3 relating to Issuers' failures to provide the market with information regarding changes to their credit ratings; and 1 relating to an Issuer's failure to notify the market regarding a change to its registered office. NZXR wrote to each Issuer, noting the breach of the Listing Rules and reminding the Issuer of its obligations under the Listing Rules.

B. SUMMARY OF COMPLAINTS RECEIVED BY NZXR IN RESPECT OF NZX ISSUERS

NZXR received a total of 32 complaints in respect of Issuers during the Period. In all cases, NZXR acknowledged the receipt of these complaints by contacting the complainants.

For 24 of these, NZXR undertook a review to arrive at the determination that there were no breaches of the Listing Rules and/or relevant securities legislations and regulations. Of these:

- 3 related to alleged insider trading;
- 4 related to enquiries as to the movement in price of shares;
- 1 related to Issuers' alleged failure to pay a shareholder the proceeds from share capitalisation;
- 2 related to complainants questioning Issuers' solvency;
- 4 related to Issuers' compliance with the continuous disclosure requirements of the Listing Rules;
- 1 related to a takeover of an Issuer;
- 1 related to a complainant challenging the Independence of a director of an Issuer;
- 1 related to an Issuer's alleged failure to comply with International Financial Reporting Standards in preparing its half-year report;
- 1 related to whether an independent report for underwriting was required for an Issuer. NZXR referred this matter to the Takeovers Panel;
- 1 related to whether an Issuer was in compliance with the restrictions in respect of material transactions with related parties;
- 4 related to an Issuer's suggested delisting and the implications of this for shareholders;
- 1 related to actions by non-listed entities

From the complaints received, 6 breaches of the Listing Rules were identified.

- 1 related to information not being provided to market at the same time it was sent to shareholders. NZXR communicated with the Issuer and the information was subsequently made available to market.
- 1 related to an Issuer's failure to release information in respect of its intended capital raising. NZXR discussed the complaint with the Issuer concerned, and the Issuer released a clarifying announcement to the market.
- 2 related to an Issuer's statements being misleading and/or inaccurate. NZXR's investigation into this matter is on-going.
- 1 related to incorrect statements made by an Issuer in its Notice of Meeting provided to shareholders. NZXR raised this with the Issuer and the Issuer made an announcement correcting the incorrect statements.
- 1 related to calculations contained in a Notice of Meeting by an

Issuer provided to shareholders. NZXR contacted the Issuer and the Issuer issued a correcting statement to the market. NZXR sent a letter reminding the Issuer of its obligations under the Listing Rules in this regard.

The remaining 2 complaints were in the process of being reviewed as at 31 December 2012.

Of these:

- 1 related to an Issuer's failure to meet forecasts. NZXR's investigation into this matter is ongoing.
- 1 related to an Issuer's failure to return surplus cash and shares to shareholders in respect of a takeover. NZXR referred the complaint to the Takeovers Panel and also sent letters of enquiry to the Issuer.

4. USE OF PROCEEDS OF THE DISCIPLINE FUND

This section 4 details the use of the proceeds of the Discipline Fund, as set out in the Discipline Fund Accounts. Proceeds of the Discipline Fund may be used in accordance with NZMDT Rule 11.21.1.

STATEMENT OF INCOME AND EXPENDITURE

| | 4 Months to 30- Apr-08 | 8 Months to 31- Dec-08 | 12 Months to 31- Dec-09 | 12 Months to 31- Dec-10 | 12 Months to 31- Dec-11 | 12 Months to 31- Dec-12 |
|---|------------------------------|------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| Fines and costs | 13,000 | 230,629 | 411,237 | 341,957 | 196,617 | 179,838 |
| Expenses of NZ Markets Disciplinary Tribunal | | | | | | |
| Appeal Member costs | - | - | - | - | - | - |
| Executive Counsel costs | - | 60,087 | 109,112 | 136,192 | 136,192 | 34,714 |
| NZ Markets Disciplinary Tribunal Member costs | 14,248 | 105,282 | 44,171 | 166,919 | 101,567 | 88,554 |
| Legal Advisory costs | - | - | - | 8,145 | - | - |
| Rules Review costs | 44,752 | 1,360 | 595 | 5,161 | - | 2,310 |
| Disbursements | - | 3,717 | 11,234 | 6,711 | 5,295 | 1,497 |
| Educational Expenditure | - | - | - | 61,109 | 5,000 | - |
| Other Incidentals | - | - | - | 1,440 | 1,524 | 2,027 |
| Bad Debts | - | - | - | 342,728 | - | 22,703 |
| Total Expenses | 59,000 | 170,446 | 165,112 | 728,405 | 176,603 | 151,805 |
| Interest Income | - | - | - | 3,844 | 70 | 1,270 |
| Surplus (Deficit) for the period | (46,000) | 60,183 | 246,125 | (382,604) | 20,084 | 29,303 |
| Accumulated Surplus (Deficit) | 236,054 | 296,237 | 542,362 | 159,758 | 179,842 | 209,145 |



**NEW ZEALAND CLEARING ANNUAL
REPORT TO NZ MARKETS
DISCIPLINARY TRIBUNAL**

THIS SECTION OF THE REPORT ADDRESSES THOSE MATTERS
REQUIRED BY NZMDT RULE 14.1.2 (a) - (b) WHICH PROVIDES:

“14.1.2 Following the end of each calendar year CHO shall collate the following information for that year and provide to the Tribunal as a report by the end of February of the following year:

- a) breaches of the Clearing and Settlement Rules identified by CHO; and
 - b) complaints received by CHO in respect of Clearing Participants or Lending Clearing Participants.”
-

1. INTRODUCTION

New Zealand Clearing Limited ("CHO") provides clearing and settlement services to Clearing Participants and Lending Clearing Participants under the Clearing and Settlement Rules. The NZCDC Settlement System is a designated settlement system pursuant to the Reserve Bank of New Zealand (Designated Settlement System – NZCDC) Order 2010.

The NZ Markets Disciplinary Tribunal (the "Tribunal") is an independent disciplinary body charged with determining and providing remedies for referrals made to it by CHO under the Clearing and Settlement Rules.

CHO provides this report, dated 28 February 2013, to the Tribunal pursuant to Rule 14.1.2 of the NZ Markets Disciplinary Tribunal Rules (the "NZMDT Rules"). Pursuant to NZMDT Rule 14.1.2, CHO must submit to the Tribunal by 28 February 2013 a report for the 2012 calendar year which contains the following information:

- a) breaches of the Clearing and Settlement Rules identified by CHO; and
- b) complaints received by CHO in respect of Clearing Participants and Lending Clearing Participants.

This report provides information for the period 1 January 2012 to 31 December 2012 (the "**Period**"). NZX also provides information about CHO in its Annual Report, available on its website, www.nzclearingcorp.com.

Capitalised terms used in this report which are not otherwise defined in this report have the meaning given to them in the NZMDT Rules.

2. BREACHES OF THE CLEARING AND SETTLEMENT RULES

This section 2 summarises breaches of the Clearing and Settlement Rules by Clearing Participants and Lending Clearing Participants identified by CHO during the Period.

A. SIGNIFICANT BREACHES OF THE NZX PARTICIPANT RULES REFERRED TO NZMDT

No significant breaches of the Clearing and Settlement Rules were referred to the Tribunal during the Period.

B. OTHER BREACHES OF THE CLEARING AND SETTLEMENT RULES

There were five minor, inadvertent or technical breaches of the Clearing and Settlement Rules, which were not considered sufficiently serious to warrant referral to the Tribunal. These breaches were identified during CHO's onsite inspections of Clearing Participants and the Participants were required to rectify the cause of the breach within a given timeframe. In all cases this requirement was met. These breaches were subsequently highlighted to the relevant Clearing Participant as part of a CHO inspection report (containing, as appropriate, action points for Clearing Participants to resolve, or implement, within specified timeframes).

There were two breaches of Clearing and Settlement Rule 3.12.3; on each occasion due to a Clearing Participant's late delivery of Eligible Collateral to CHO. In each instance sufficient surplus cash was held by CHO to cover the margin call.

There were three breaches of Rule 2.17 of the Clearing and Settlement Rules relating to monthly reporting of capital adequacy calculations by a Clearing Participant. There was one breach of Rule 2.19 relating to calculation of capital, and one breach of Rule 2.15 where the Clearing Participant's capital ratio fell to 97% of the minimum requirement. Further information relating to these breaches is provided in NZX Regulation's report to NZMDT.

3. SUMMARY OF COMPLAINTS RECEIVED BY CHO IN RESPECT OF CLEARING PARTICIPANTS AND LENDING CLEARING PARTICIPANTS DURING THE PERIOD

This section 3 summarises complaints received by CHO in respect of Clearing Participants and Lending Clearing Participants during the Period.

A. SUMMARY OF COMPLAINTS RECEIVED BY CHO IN RESPECT OF CLEARING

CHO did not receive any complaints in respect of Clearing Participants during the Period.

B. SUMMARY OF COMPLAINTS RECEIVED BY CHO IN RESPECT OF LENDING CLEARING PARTICIPANTS

CHO did not receive any complaints in respect of Lending Clearing Participants during the Period.



REPORT ON SPECIAL DIVISION ACTIVITIES

The Special Division considered thirty matters during the year. A summary of each matter follows this report.

SMARTS SURVEILLANCE SYSTEM ALERTS

As with the previous year, the majority of matters referred to the Special Division related to SMARTS surveillance system alerts regarding trading in the quoted securities of NZX and the listed funds managed by its subsidiary, Smartshares. A number of the alerts referred to the Special Division reflected, in part, general movements in the market during 2012. Others, however, required some investigation. Of note are:

- 1) The Special Division investigated the circumstances surrounding NZX's announcement on 30 July 2012 regarding its first half performance and the impact that announcement had on the NZX share price, triggering a SMARTS surveillance system alert. Following its review of the actions of NZX, and confirmation from NZX that it had complied, and remained in compliance, with the Listing Rules, the Special Division determined that no further action on its part was necessary. The Special Division informed the FMA of its review and findings.
- 2) Further to its referral regarding trading in NZX shares on 30 July 2012, NZXMS wrote to advise the Special Division of trading conducted by a market participant which it considered required investigation. As the trading potentially involved market manipulation, the Special Division referred the matter to the FMA for review. The FMA conducted a review and shared its findings with the Special Division.
- 3) The Special Division received referrals from NZXMS on 4 July 2012 and again on 27 December 2012 regarding several SMARTS alerts involving abnormally large trading in the units of the smartTENZ Fund managed by Smartshares. The Special Division investigated the circumstances of the alerts, which arose as a result of Smartshares releasing an incorrect NTA calculation to the market on the first occasion and an incorrect basket composition notice on the second occasion. The Special Division sought, and obtained, confirmations from Smartshares that it has undertaken a review of the incidents to identify how the errors occurred and has rectified its procedures.

The Special Division fulfils its role of monitoring trading in the quoted securities of NZX and the units in the funds managed by Smartshares with assistance from NZXMS. I thank NZXMS for its prompt attention to these matters in 2012.

PERSONNEL

Paul Ridley-Smith and Michael Jeffs both retired from the Special Division at the Tribunal's annual general meeting in June 2012. I sincerely thank Paul and Michael for their service on the Special Division. Both brought considerable insight into the market and served the Special Division very well. We welcomed Shane Edmond and Kevin Baker as members of the Special Division in June 2012. Both have already made a significant contribution.



Peter Wilson | CHAIRMAN
12 April 2013

NZMDT SPECIAL DIVISION MATTERS – 1 JANUARY TO 30 DECEMBER 2012

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|-----------------|--|--|
| 6/1/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Volume Inter-Day" for trading in TNZ on 6 January 2012. The alert resulted from volume of 2,181,604 TNZ units trading over 3 days (the threshold is 2,000,000).</p> <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |
| 10/1/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-Day" for trading in NZX shares on 9 January 2012. The alert resulted from an increase in the price of NZX shares from \$2.25 to \$2.40 from 8 December 2011 to 9 January 2012.</p> |
| 12/1/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-Day" for trading in NZX shares on 12 January 2012. The alert resulted from an increase in the price over:</p> <ul style="list-style-type: none"> a) 3 days of \$0.19 (7.9%) from \$2.40 to \$2.59; b) 10 days of \$0.27 (11.6%) from \$2.32 to \$2.59; and c) 20 days of \$0.39 (17.7%) from \$2.20 to \$2.59. <p>The Special Division investigated the circumstances surrounding the alerts referred on 10 and 12 January 2012 and sought an explanation from NZX for the price movements and confirmation of compliance with the NZSX Listing Rules, including regarding continuous disclosure. Following its review of the material and confirmations from NZX, the Special Division determined that no further action on its part was necessary.</p> |
| 20/1/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Volume Inter-Day" for trading in TNZ on 20 January 2012. The alert resulted from volume of 3,017,671 TNZ units trading over 20 days (the threshold is 3,000,000).</p> |
| 24/1/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-Day" for trading in NZX shares on 23 January 2012.</p> <p>The alert resulted from an increase in the price of NZX shares over 20 days from \$2.30 to \$2.68 (16.5%). The benchmark rise over 20 days is 0.36 (16%). \$2.68 is an all time high closing price for NZX (previous high of 2.66 occurred in June 2007).</p> <p>The Special Division investigated the circumstances surrounding this alert and sought an explanation from NZX for the price movements and confirmation of compliance with the NZSX Listing Rules, including regarding continuous disclosure. Following its review of the material and confirmations from NZX, the Special Division determined that no further action on its part was necessary.</p> |

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|---------|--|---|
| 10/2/12 | NZX Ltd | Application for waiver from Listing Rule 7.6.1 | <p>On 10 February 2012, NZX applied to the Special Division for a waiver from Listing Rule 7.6.1.</p> <p>In 2009, NZX acquired rural media company Country-Wide Publications (CPL). Under the agreement, NZX issued \$500,000 of shares to a nominee company with the shares to vest in CPL on completion of NZX's 2012 financial statements and subject to certain criteria being met, including that two specified individuals remain employees of NZX on 31 December 2012. One of the individuals ceased employment with NZX and accordingly NZX was required to redeem 50% of the shares.</p> <p>Listing Rule 7.6.1 sets out the permitted methods available to Issuers for the redemption of Equity Securities. The redemption of the shares by NZX did not fall within the permitted methods.</p> <p>The Special Division granted NZX the waiver requested. In coming to its decision, the Special Division considered that:</p> <ul style="list-style-type: none"> a) the redemption was not detrimental to NZX shareholders and allowed NZX to deal with those shares in a commercial manner; b) it was satisfied the redemption was not inconsistent with the policy objective of Rule 7.6.1; and c) there was precedent for this policy approach. <p>The Special Division's decision on the waiver was released to the market in full on 20 February 2012.</p> |
| 14/2/12 | NZX Ltd | Review of Notice of Meeting under Rule 6.1 | <p>The Special Division received an application from NZX for approval of the notice for NZX's 2012 AGM. The Special Division's approval was required because the notice included a resolution seeking shareholder approval to undertake a capital repayment to distribute the proceeds of the sale of NZX's shareholding in Markit to shareholders under a scheme of arrangement.</p> <p>The Special Division approved the notice on 5 March 2012.</p> |
| 17/2/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-Day" for trading in NZX shares on 16 February 2012.</p> <p>The alert resulted from the price of NZX shares decreasing from \$2.74 to \$2.60 between 14 February 2012 and 16 February 2012.</p> |

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|-----------------|--|---|
| 21/2/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of SMARTS alerts for "Unusual Price Movement Inter-Day" for trading in NZX shares on 20 February 2012.</p> <p>The alerts resulted from the price of NZX shares increasing from \$2.59 to \$2.84 or 9.7% between 10:00am and 10:55am and the price of NZX shares increasing from \$2.62 to \$2.84 or 8.4% between 16 February 2012 and 20 February 2012.</p> <p>The referral also included an alert for "Unusual Volume Inter-Day" which resulted from 1,144,243 NZX shares trading between 31 January 2012 and 20 February 2012.</p> <p>The Special Division investigated the circumstances surrounding the alert referred on 17 and 21 February 2012 and sought an explanation from NZX for the price movements and confirmation of compliance with the NZSX Listing Rules, including regarding continuous disclosure. Following its review of the material and confirmations from NZX, the Special Division determined that no further action on its part was necessary.</p> |
| 21/2/12 | Smartshares Ltd | Review of waivers | <p>The Special Division released to the market a report on its review of waivers it granted on 14 October 2004 and 29 March 2005 so that the Board of Smartshares is not required to include a minimum number of Independent Directors under Rule 3.3.1(c) or to comply with the associated procedural requirements in Rules 3.3.2 to 3.3.4 for determining independence and the appointment process.</p> |
| 21/3/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received referrals from NZXMS of SMARTS alerts for "Unusual Price Movement Inter-Day" and "Unusual Volume Inter-Day" in the days following the alerts which fired on 20 February 2012 for trading in NZX shares showing incremental changes in the price and volume traded against the initial alert.</p> <p>The Special Division investigated the circumstances surrounding the alerts which fired following 20 February 2012 and sought an explanation from NZX for the price and volume movements and confirmation of compliance with the NZSX Listing Rules, including regarding continuous disclosure. Following its review of the material and confirmations from NZX, the Special Division determined that no further action on its part was necessary.</p> |
| 13/4/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Volume Inter-Day" for trading in TNZ on 12 April 2012. The alert resulted from volume of 2,026,789 TNZ units trading over the last 10 days (the threshold is 2,000,000).</p> <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|-----------------|--|---|
| 16/4/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Volume Inter-Day" in trading of NZX shares on:</p> <ul style="list-style-type: none"> i) 12 April 2012 - 1,164,466 volume in the last 10 days (the threshold is 1,000,000). ii) 13 April 2012 - 1,029,676 volume in the last 3 days (the threshold is 1,000,000). iii) 13 April 2012 - 1,208,727 volume in the last 10 days (the threshold is 1,200,000). <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |
| 26/4/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received referrals from NZXMS of SMARTS alerts for "Unusual Volume Inter-Day" in the days following the alert referred on 13 April 2012 for trading in TNZ showing incremental changes in volume traded against the initial alert.</p> <p>The Special Division considered the nature of the alert and sought advice from Smartshares. It determined that no further investigation was necessary.</p> |
| 26/4/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alerts in trading of NZX shares on:</p> <ul style="list-style-type: none"> i) 18 April 2012 for "Unusual Price Movement Inter- Day". The price change over 20 days was -\$0.17 (6%) from \$2.84 to \$2.67 and the bench mark is \$0.13 (5%). ii) 19 April 2012 for "Unusual Price Movement Inter-Day". The price change over 20 days was -\$0.16 (5.6%) from \$2.84 to \$2.68 and the benchmark is \$0.14 (5%). iii) 20 April 2012 for "Price Driver Down" where a trader decreased the price of NZX 3 times on 20 April 2012 out of a total of 6 downward movements. <p>The Special Division also received a referral from NZXMS of a SMARTS alerts in trading of NZX shares for "Unusual Volume Inter-Day" between 18 and 26 April 2012.</p> <p>The Special Division investigated the circumstances surrounding the alerts, including seeking an explanation from NZX for the price and volume movements and confirmation of compliance with the NZSX Listing Rules, and obtained advice from the market participant involved. Following its review of the material and confirmations from NZX, the Special Division determined that no further action on its part was necessary.</p> |

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|-----------------|--|---|
| 2/5/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of SMARTS alerts fired on 2 May 2012 which resulted from a Large Bid Order involving 345,941 units of FNZ with a value of \$446,610 (the volume threshold is 200,000 units and the value threshold is \$250,000). This alert was followed by a Bait and Switch with the same trader deleting a large bid order for 345,941 units.</p> <p>The Special Division investigated the circumstances surrounding the alerts and obtained advice from the market participant involved. Following its review of the material the Special Division determined that no further action on its part was necessary.</p> |
| 8/5/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received referrals from NZXMS of SMARTS alerts for "Unusual Volume Inter-Day" which fired between 27 April 2012 and 7 May 2012 showing incremental changes in volume traded of NZX shares.</p> <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |
| 18/5/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-Day" for units in OZY which resulted from a price change over 10 days of \$0.177 (5.2%) from \$3.427 to \$3.25 and benchmark is \$0.15 (5%).</p> <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |
| 18/6/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alerts for Unusual Price and Volume Movement Inter-Day in trading of NZX shares between 9 May 2012 and 14 June 2012.</p> <p>The Special Division considered the nature of the alerts and announcements made during that period and determined that no further action on its part was necessary.</p> |
| 4/7/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of SMARTS alerts fired on 29 June 2012 "Unusual Price Rise: Intra-day" triggered following an on-market trade in MZY units by a market participant with a wholesale client on the buy side and a wholesale client on the sell side.</p> <p>The Special Division investigated the circumstances surrounding the alerts and conducted an investigation into errors made by Smartshares Ltd in the calculation of the NTA for the fund and information it provided to market participants.</p> <p>The Special Division sought, and obtained, confirmations from Smartshares that it had undertaken a review of the incident to identify how the errors occurred and had taken steps to ensure they did not reoccur.</p> |

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|-----------------|---|---|
| 4/7/12 | NZX Ltd | Review of SMARTS surveillance system alert | The Special Division received a referral from NZXMS of SMARTS alerts for "Unusual Volume Inter-Day" which fired between 29 June 2012 and 2 July 2012. The alerts were directly attributable to a single off market special crossing of 9,500,000 NZX shares. This volume represents 3.7% of the issued share capital of NZX Limited. The Special Division was provided with a copy of the Ongoing Disclosure Notice relating to this transaction which involved the disposal of NZX shares by its former CEO. |
| 30/7/12 | NZX Ltd | Review of SMARTS surveillance system alert and timing of announcement | <p>The Special Division conducted an investigation of circumstances surrounding an announcement released by NZX on 30 July 2012 regarding aspects of the first half performance of NZX and a SMARTS alert referred by NZXMS on 30 July 2012 regarding trading in NZX shares following that announcement.</p> <p>The Special Division obtained advice from NZX including confirmation that the information contained in the announcement was released within the time required under NZSX Listing Rule 10.1.1. The Special Division was satisfied with the response it received from NZX. The Special Division consulted with the FMA regarding its investigation.</p> |
| 1/8/12 | NZX Ltd | Review of SMARTS surveillance system alert | Further to its referral regarding trading in NZX shares on 30 July 2012, NZXMS wrote to advise the Special Division of trading conducted by a market participant which it considered required investigation. As the trading potentially involved market manipulation, the Special Division referred the matter to the FMA for review. |
| 24/8/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alerts for "Unusual Price Movement Inter-Day" which fired on 24 August 2012 and resulted from a price change in NZX shares over 20 days of -\$0.25 (18.9%) from \$1.32 to \$1.07 and the benchmark is \$0.24 (18%).</p> <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |
| 28/8/12 | Smartshares Ltd | Application for approval under Rule 6.1 | The Special Division reviewed and approved the amended Prospectuses and the Investment Statement for each of the ETF funds managed by Smartshares Ltd. |
| 18/10/12 | NZX Ltd | Application for approval under Rule 6.1 | The Special Division reviewed and approved the Prospectus and the Investment Statement for the NZX employee share scheme. |

| DATE REFERRED | ISSUER | MATTER | SUMMARY OF MATTER |
|---------------|-----------------|--|---|
| 18/10/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert on 17 October 2012 for trading in MDZ. The alert was for "Unusual Price Movement Intra-Day" and resulted from MDZ trading at \$3.45, a price \$0.96 (38.8%) higher than the previous trade of \$2.48. The alert resulted from a market participant bid order for 5,000 MDZ units at a price of \$3.45. Immediately following the order, 5 trades occurred at a price of \$3.45. NZXMS contacted the participant involved who advised that he had entered four buy orders with an incorrect price. NZXMS cancelled five trades resulting from the error.</p> <p>The Special Division received a summary of the review undertaken by NZXMS into this matter. The Special Division investigated the circumstances of the alert and sought, and obtained, advice from the market participant involved.</p> |
| 23/10/12 | NZX Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-day" which resulted from a price change in NZX shares over 10 days of +\$0.10 (8.8%) from \$1.14 to \$1.24 and the benchmark is \$0.08 (8%).</p> <p>The Special Division considered the nature of the alert and obtained advice from NZX. It determined that no further investigation was necessary.</p> |
| 23/10/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of a SMARTS alert for "Unusual Price Movement Inter-day" which resulted from a price change in MZY units over 10 days of +\$0.24 (5.2%) from \$4.60 to \$4.84 and the benchmark is \$0.20 (5%).</p> <p>The Special Division considered the nature of the alert and determined that no further investigation was necessary.</p> |
| 27/12/12 | Smartshares Ltd | Review of SMARTS surveillance system alert | <p>The Special Division received a referral from NZXMS of SMARTS alerts relating to abnormally large trading in the units of TNZ. The Special Division investigated the circumstances of the alerts, which arose as a result of Smartshares releasing an incorrect basket composition notice. The Special Division sought, and obtained, confirmations from Smartshares that it has undertaken a review of the incident to identify how the error occurred and has rectified its procedures.</p> |

DIRECTORY

RACHEL BATTERS | EXECUTIVE COUNSEL
PO BOX 105 269 AUCKLAND 1143
EMAIL rachel.batters@nzmdt.com

