



SEPTEMBER 2023

Market operator obligations review

Catalist

Findings from the FMA's review of how well Catalist is meeting its licensed market operator obligations, for the period 1 April 2022 to 31 March 2023

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Executive summary

About this report

Catalist Markets Limited (**Catalist**) is licensed under section 316 of the Financial Markets Conduct Act 2013 (**FMC Act**) to operate Catalist Public Market.

The FMC Act requires the Financial Markets Authority – Te Mana Tātai Hokohoko (**FMA**) to carry out a review and report on how well Catalist is meeting its licensed market operator obligations. We may carry out this review at any time but must do so at least once a year.

This report covers our second obligations review of Catalist, for the period from 1 April 2022 to 31 March 2023 (referred to as **the review period**).

The Catalist Public Market is aimed at small and medium-sized businesses (**SMEs**) seeking liquidity or seeking to raise capital up to \$20m, with a view that once these entities reach a certain scale and size, they would transition on to the next phase of their growth, which may be a listing on the NZX. It was designed to be a lower-cost and simplified financial products market, offering trading by way of an online auction platform with periodic (rather than continuous) trading and disclosure.

Details of Catalist's licence are on [our website](#).

How we approached this review

As with other market operator obligations reviews, we selected certain areas of focus. The scope of our review was influenced by this being Catalist's second period of licensed activity, the scale of the activity undertaken on its licensed market, and the particular conditions of its licence.

The scope of this review focused on, but was not limited to, the following key areas:

1. Governance arrangements and oversight
2. Monitoring of conduct
3. Conflict management
4. Enquiries, investigations, and enforcement
5. Technology

In assessing these areas and overall compliance, we reviewed and considered how Catalist is structured and governed by reviewing policy and process documents, Board reporting and minutes, and risk management frameworks. Additionally, we spoke to Catalist's key personnel and members of the Board.

We employ a risk-based approach to monitoring. While this review is of Catalist's overall compliance with its licensed market operator obligations, we have exercised our judgement in selecting focus areas, and the level and detail of work performed in each. This report highlights our main observations from the review and, as with any risk-based approach, has inherent limitations. Our assessment, recommendations and observations are based on the information we have received, collected and reviewed.

Overall assessment

Our overall conclusion is that Catalist has complied with its licensed market operator obligations during the review period. In making this assessment we considered specific conditions of Catalist's licence and obligations of a licensed market operator under the FMC Act¹, in particular the general obligations under section 314 to:

- Do all things necessary to ensure, to the extent that is reasonably practicable, that each of its licensed markets is fair, orderly and transparent
- Have adequate arrangements for notifying disclosures made to it under a disclosure obligation, and for continuing to make those disclosures available
- Have adequate arrangements for handling conflicts between its commercial interests and the need to ensure its markets operate in a fair, orderly and transparent manner
- Have adequate arrangements for monitoring the conduct of participants in its markets
- Have adequate arrangements for enforcing compliance with relevant market rules
- Have sufficient resources (including financial, technological and human resources) to operate its licensed markets properly.

Observations

Our key observations for the review period include the following:

- Catalist has maintained proactive engagement with issuers, investors, and the regulator.
- Catalist has adopted a guidance-based and educative approach to support issuers to meet the onboarding standards.
- Catalist has continued to embed processes and controls, applying enhancements that were appropriate.
- We observed a maturing of Catalist, with the trading platform performing well and coping with an increase in volumes, and note the organisation is well positioned for further growth.
- Catalist demonstrated that it is managing key person risk adequately for the exposure it has and the activities it is undertaking.
- Catalist continued to be supported by a stable and engaged Board. Through discussions and information gathered we observed sound communication channels and a good level of challenge.

We acknowledge and thank Catalist staff for their constructive engagements during 2022 and our on-site review in 2023.

¹ Refer to Appendix 1 for further details on obligations.

In addition to the observations noted above, we identified five areas Catalist will need to continue to focus on as it grows:

Area	Recommendation
Adequacy of resourcing	Catalist is cognisant of market operator obligations, and of the importance of maintaining sufficient capacity and capability while ensuring these are also appropriate to scale and activities. We recommend that Catalist maintains regular oversight of any outsourced arrangements, with measured appraisals, to ensure this resourcing structure continues to work effectively and provides access to capacity and capability in a timely fashion.
Financial resilience	Providing cashflow forecasting and re-forecasting for capital planning is crucial for any company in start-up or growth phase. Catalist performs regular forecasting as well as scenario-based testing as part of its internal reporting and capital management activities. Given the stage of its growth, and the importance of managing financial resilience risks, Catalist should maintain its focus in this regard.
On-boarding of issuers	Catalist is aware of and actively considers regulatory obligations and the purpose for which the market was created. We recommend Catalist continues to embed robust controls to maintain an appropriate level of segregation between its role as market operator and the facilitation of new issuance. While Catalist retains evidence to demonstrate the process followed and that the requirements for listings are met, it should ensure that its records include more comprehensive evidence of qualitative analysis undertaken regarding new issuer requirements, in accordance with the relevant internal policies.
Technology platform	Catalist trading platform was stable and coped well with increased activity. We note the implementation of additional controls since our last review. Catalist should continue the development of its control framework to minimise risk of potential technology issues.
Cyber and security	Cyber and security is a key area to stay abreast of, as the cyber environment is continually evolving. Catalist undertakes regular risk-based testing. We recommend ongoing vigilance with regular assessment of IT security risk posture and mitigation plans.

Focus areas

Governance arrangements and oversight

Background and review

We concentrated our review of governance arrangements and oversight in three key areas: understanding the level of reporting and oversight, monitoring and assessing sufficiency of resourcing, and oversight of risk management framework and outputs. We reviewed logs, protocols and controls, Board minutes, and held discussions with key staff and Board members.

Catalist has a Board of four directors, representing a range of industry and regulatory knowledge and experience, with three independent Board members. The Catalist Board composition has remained unchanged since the licence was granted. As part of this review, we considered whether the composition of the Board remains appropriate, as Catalist continues to grow. We also looked at the type and frequency of reporting the Board receives, and the consistency of engagement, both formal and informal.

FMA observations

Review of key documents and discussions with Board members showed an appropriate level of escalation on complex matters, challenge, and oversight. We found the Board to be stable, with robust and mature governance, and a good mix of skills. However, while the current Board members are well-versed in technology matters, there is not a technology specialist on the Board. This places additional director responsibility on continued learning in this space.

The Board is kept informed across all areas of sufficiency of resources. The Board has good visibility over the recently adopted outsourcing model, with two executive positions held by contractors, the Head of Regulation, and the Chief Financial Officer, which has resulted in an overall uplift in key areas. The outsourcing model will require regular engagement, with measured appraisals, to ensure this resourcing structure continues to work effectively and provides access to capacity and capability in a timely fashion, so expectations continue to be met. Further, providing cashflow forecasting and regular re-forecasting for capital planning and management purposes are necessary requirements for sound risk and capital management in any business. We consider that Catalist pays appropriate attention to managing risks relating to financial resilience. Catalist should continue with its current process of forecasting and scenario modelling that ensures these risks are being regularly modelled under a number of assumptions with the results regularly reported.

Having reviewed the risk management framework, we observed it is fit for purpose for this stage of the business. We observed Catalist is alert to the detection and monitoring of new risks as the business grows.

Monitoring of conduct

Background and review

Catalist must have adequate arrangements for monitoring the conduct of market participants in its markets. Conduct monitoring is the responsibility of all directors, staff and contractors who are involved in any market surveillance, investigations, or enforcement action against any Catalist issuer or investor, or who are involved in any trading activity on the Catalist Public Market (including restricted auctions). Therefore, we concentrated our monitoring of conduct review in three key areas: on-boarding of issuers during the review period, monitoring activity that took place during the review period, and monitoring of issuer compliance with disclosure obligations. We reviewed relevant processes, checklists, and policies, such as the Catalist Market Surveillance, Investigations and Enforcement Policy (**MSIE policy**), and the Catalist Compliance Assurance Programme. We also selected a sample of two issuer on-boarding files for closer inspection. In addition, we reviewed two relevant guidance notes: Information Memorandum – for issuers of equity securities / shares, and Disclosure of material information. Both guidance notes aim to assist with education for new issuers in the Catalist Public Market.

FMA observations

Catalist has prepared guidance notes to assist with education for new issuers in the Catalist Public Market. These provide guidance on required disclosure information and preparing Information Memorandums, in compliance with the Catalist Issuer Rules and all relevant legislation. We observed that enhancements to Catalist's overall strategy for on-boarding of issuers focused on improving the efficiency of the 'issuer journey', by standardising the process so it is more scalable and repeatable. We observed that improvements to processes were in line with a maturing of Catalist's business model.

There are risks associated with an educational approach, and they need to be balanced with the role market operators play in the oversight of activity on their markets. We recommend Catalist continues to embed robust controls to maintain an appropriate level of segregation between its role as the market operator and facilitating potential new issuances. While Catalist retained evidence to demonstrate the process followed and that the requirements for the listing are met, it should ensure that its records include more comprehensive evidence of qualitative analysis undertaken regarding new issuer requirements, in accordance with the relevant internal policies.

Catalist has adopted a guidance-based and educative approach, in addition to its processes and controls utilised for monitoring and testing issuer compliance with disclosure obligations. During the review period, secondary market trading on the Catalist Public Market commenced. Trading was monitored in accordance with Catalist's MSIE policy, and no activity that warranted escalation under this policy was identified. We are overall satisfied that Catalist had adequate arrangements in place for monitoring of conduct during the review period.

Conflict management

Background and review

Catalist is required to have adequate arrangements for handling conflicts between commercial interests and the need to ensure its licensed market is fair, orderly, and transparent. To understand how well Catalist manages conflict management, we reviewed relevant registers and policy documents, such as Catalist's

Conflicts of Interest and Regulatory Decisions Policy. We also had discussions with key staff, noting that Catalist's size and level of activity mean individuals within the organisation continue to undertake a broad range of activities.

FMA observations

During the review period, there were several issuer-related items recorded on Catalist's Conflicts and Regulatory Decisions register. Each matter was appropriately escalated, in line with the relevant policy. We are satisfied that Catalist has adequate measures in place to identify, record and escalate conflicts.

During the review period we engaged with Catalist on its roadmap for gradual separation of compliance and regulatory oversight roles from commercial activity as the business grows. For completeness, this is in reference to Licence Condition 8(7) (Licence Condition): "Catalist must have a dedicated regulatory and compliance resource, which is separate to its commercial function when the Catalist Public Market exceeds its initial year trading projections as notified to the FMA at the time of licence application". Although the Licence Condition has not yet been triggered; we observed Catalist has worked on segregation of duties and effective management of risks and controls to ensure that commercial imperatives do not override regulatory obligations. We will continue to review how Catalist further segregates roles to enhance conflict management arrangements, in line with its growth and the maturing of its operations.

Enquiries, investigations, and enforcement

Background and review

Catalist is required to have adequate arrangements for enforcing compliance with market rules. Enforcement procedures are set out in Catalist's MSIE Policy and are summarised for market participants in Catalist's Issuer Rules Enforcement Policy. To understand how well Catalist continues to manage enforcement, we reviewed relevant process and policy documents and had discussions with key staff. We considered Catalist's approach to investigation of potential breaches, and the process Catalist followed.

FMA observations

There was no enforcement activity over the review period, and no breach of the Issuer Rules. There was one unusual activity; however, upon investigation no further action was taken. We noted the system tools Catalist can utilise, including the alerts relating to unusual activity, and these seem appropriate for the current size and scale of Catalist. Based on the information available, we are satisfied that Catalist has appropriate measures in place to undertake enquiries and enforcement.

Technology

Background and review

During the review period, we engaged with Catalist on management and 'business as usual' matters, which included relevant updates on the technology space such as initiatives and reporting. We reviewed logs, protocols and controls and Board minutes, and held discussions with key staff and Board members. We reviewed relevant policies, such as the Catalist Cyber and Information Security Policy and the Business Continuity Policy.

The Catalist internal technology team comprises developers and the Chief Technology Officer, who are further supported by external providers where required. Given the small size of Catalist, there continues to be a high degree of cross-functional agility when it comes to technology development.

FMA observations

We consider that Catalist has continued to focus on technology capability as the business grows, and to support compliance with its market operator obligations. This was demonstrated through continued improvement and updates of Catalist's application and platform. We note however that as Catalist grows, it will need to continually reinforce its technology strategy to deliver appropriate business function, such as usability, workflow, data integrity and reconciliation, as well as the non-functions, such as accessibility, performance, and security.

Catalist should continue to develop its control framework to minimise the risk of issues, and where possible Catalist should continue to work on further automation of some aspects. Catalist's technology security posture is appropriate for its exposure and activities.

Follow up on observations from September 2022 report

Background and review

In our September 2022 report we provided three recommendations for Catalist in relation to key person risk, risk management and conflicts management, and financial capability and resilience. Leading up to and during this review, we discussed each of these areas. Steps were taken to mitigate each; these actions were also evident in the materials we reviewed.

FMA observations

Regarding key person risk, we noted an uplift in documented policies and procedures to strengthen transfer of knowledge, which is vital to smooth operations. We observed during the review period the continued focus on quality of documentation in this area, as a means to mitigate key person risk.

Concerning risk management and conflicts management, we note that as Catalist matures, it is our expectation that there is further segregation of activities so functions can be given a more tailored focus. The Licence Condition has not yet been triggered; however, Catalist is cognisant of the requirements, and shows active consideration of how to effect separation in the context of its current scale, with a plan to further mature arrangements as the business grows.

Our prior-year observations on financial capability and resilience included a need for continued focus in this area given Catalist was in the early stages of growth. We note senior finance staffing changes at Catalist during the review period with a partial outsourcing model adopted. An uplift in the financial reporting and engagement with the Board has been observed under this approach. Financial resilience is a key risk to start-ups, so providing regular cashflow forecasting and re-forecasting for capital planning is crucial to manage available capital well, with the recent uplift in financial function supporting this goal.

Appendix 1: Our role in reviewing Catalyst

Our role

The FMA is an Independent Crown Entity and one of two main regulators of New Zealand's financial markets. Our purpose is to promote and facilitate the development of fair, efficient and transparent financial markets.

Under the FMC Act, we are required to review, at least annually, how well a licensed market operator is meeting its obligations. We are also required to publish a written report of the review.

If we consider, after conducting a review, that a licensed market operator has failed or is failing to meet any one or more of its market operator obligations, we may, by written notice, require the licensed market operator to submit an action plan to the FMA.

Market operator obligations

In the FMC Act, 'market operator obligations' means:

- the general obligations in respect of licensed markets (section 314):
 - to ensure, to the extent that is reasonably practicable, that each of its licensed markets is a fair, orderly and transparent market
 - to have adequate arrangements for notifying disclosures made to it from participants in its markets, and for continuing to make those disclosures available
 - to have adequate arrangements for handling conflicts between its commercial interests and the need to ensure its markets operate in a fair, orderly and transparent manner
 - to have adequate arrangements for monitoring the conduct of participants in its markets
 - to have adequate arrangements for enforcing compliance with market rules
 - to have sufficient resources (including financial, technological, and human resources) to operate its licensed markets properly
- an obligation to respond to a request from the FMA to make changes to market rules (section 333)
- an obligation to give the FMA an annual self-assessment of compliance with its obligations (section 337)
- an obligation to act on the directions of the FMA or the Minister, if the operator is found to be failing to meet any of its obligations (sections 340 to 342)
- any obligation imposed as a condition of a market operator's licence.

