The Treasury

Reviewing the Reserve Bank Act Information Release

Release Document January 2018

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

to prevent prejudicing the entrusting of information to the Government of New Zealand on a basis of confidence by an international organisation	6(b)(ii)
to protect the privacy of natural persons, including deceased people	9(2)(a)
to prevent prejudice to the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied	9(2)(ba)(i)
to avoid prejudice to the substantial economic interests of New Zealand	9(2)(d)
to maintain the effective conduct of public affairs through the free and frank expression of opinions	9(2)(g)(i)
to maintain legal professional privilege	9(2)(h)
to prevent the disclosure of official information for improper gain or improper advantage	9(2)(k)

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) and section 18 of the Official Information Act.

Reserve Bank Prudential Regulation of Banks

August 2017

Dr James Every-Palmer QC[1]

1 Introduction and Executive Summary

You have sought my views on the present framework for the Reserve Bank to set prudential requirements for banks under the Reserve Bank of New Zealand Act 1989 (**RBNZ Act**).

The present framework is centred around conditions of registration which are imposed on banks under the RBNZ Act. The detailed rules are, however, contained in a series of documents known as the Banking Supervision Handbook.

You have asked me to consider whether the present framework:

- strikes the right balance between the need to ensure democratic accountability for matters of significant policy versus the desires to delegate matters of technical detail to regulatory agencies;
- enables the Government to credibly commit to the long-term objective of maintaining a stable financial system; and
- provides sufficient protection that decisions that pertain to individuals are taken impartially.

These questions arise in the context of a legislative framework that has remained the same for nearly three decades while the practice of prudential regulation has changed significantly. Prudential regulation has become much broader in scope and more prescriptive over time. In addition, the corresponding frameworks for insurers and non-bank deposit takers have put more emphasis on standards and regulations than on conditions of registration.

In my view, an accountability deficit has arisen as these prudential requirements operate as laws imposed by administrative decision-making without sufficient Parliamentary oversight. This issue could potentially be addressed in a number of ways such as treating the Banking Supervision Handbook as a disallowable instrument subject to review by the Regulations Review Committee or by treating the Handbook as a determination which is subject to a merits appeal to the Courts (like input methodologies determined by the Commerce Commission).

But my preferred approach is to continue to give the Reserve Bank a high degree of autonomy in relation to prudential requirements given the technical nature of the subject matter, the need to frequently update the requirements over time and the importance of certainty as to their legal effectiveness. However, I consider that the *quid pro quo* should be more tightly prescribing the range of matters in relation to which the Reserve Bank may impose prudential requirements and providing the Minister of Finance with a clear mandate to advise the Reserve Bank of policy matters to be taken into account in operating the prudential regulatory regime.

---

[1] With assistance from Jonathan Orpin-Dowell.

In addition, I have made recommendations in relation to creating express statutory processes for tailoring rules, granting exemptions and exercising ongoing administrative decision-making functions, including the creation of appeal rights.

The remainder of this report is structured as follows:

- Part 2 discusses the current framework for prudential regulation;
- Part 3 introduces a number of legal issues arising from the current framework;
- Part 4 contains a broad discussion of the regulatory options available; and
- Part 5 contains my recommendations as to the framework for prudential regulation.

2 Current framework for prudential regulation

2.1 Introduction

In this Part, I discuss the key aspects of the current framework for prudential regulation being: conditions of registration; public disclosure requirements; and the memorandum of understanding between the Governor of the Reserve Bank and the Minister of Finance (**MOU**) in relation to macro-prudential policy.[2]

2.2 Conditions of registration

The present regime of imposing prudential requirements on banks through conditions of registration dates back to 1987 (Reserve Bank Amendment Act 1986).

The basis for prudential regulation is the divergence between the costs that would be suffered by a bank's shareholders and creditors if the bank failed and the broader costs to the economy that would result. This divergence means that a bank will tend to take more risk than is socially optimal because the full impact of a bank's actions on the wider public might not be taken into account. Prudential regulation responds to this market failure.

The framework of conditions of registration has remained the same, even though the prudential regulation regime has evolved from a light-handed approach based on self-discipline and very limited prudential rules to much greater prescription about how registered banks are to behave.

The 1986 Amendment Act (and the RBNZ Act today) provided that a bank could be registered "unconditionally" or subject to conditions specified by the Reserve Bank.[3] The original conditions imposed under this regime pertained to the maintenance of adequate levels of capital for a bank's operations, as well as various internal controls.[4]

---

[2] There are a number of other important aspects of prudential regulation that are outside the scope of this report including directions; enforcement procedures; crisis management; deregistration procedures; the Reserve Banks' day-to-day practice in implementing the regime; and the Reserve Bank internal governance.

[3] Reserve Bank of New Zealand Act 1964, s 38D(3) (inserted by s 10 of the Reserve Bank Amendment Act 1964). See also s 74(1) of the RBNZ Act.

[4] Chris Hunt "A Short History of Prudential Regulation and Supervision at the Reserve Bank" Reserve Bank of New Zealand *Bulletin* Vol 79, No 14, August 2016 at 6.

One of the changes made by the introduction of the RBNZ Act in 1989 was to give the Reserve Bank a "greater ability to impose conditions on the registration of an institution and to vary these conditions if necessary".[5] The Act expressly states what the conditions may relate to,[6] with provision for the specified matters being expanded by the legislature over time.[7] Further, a broad interpretation has been taken of these specified matters such as risk management systems. They have been seen as authorising matters not specifically referred to, such as debt to income, loan to value and liquidity requirements.

Today conditions are imposed on banks through the setting of requirements that the bank comply with parts of a larger handbook document (the Banking Supervision Handbook) that sets out the content of the requirements.

The Reserve Bank is currently in the process of reformatting and restructuring the Banking Supervision Handbook.[8] The Banking Supervision Handbook is "a collection of documents that sets out a range of different matters relating to the Reserve Bank's regulatory requirements for banks".[9] Only some parts of the Banking Supervision Handbook are referred to in conditions of registration, other parts take the form of explanation of requirements imposed directly by the Act and provide explanatory guidance.[10]

In the Reserve Bank's own words the Banking Supervision Handbook has grown "organically" over time.[11] It has expanded rapidly in recent years. For instance, prior to 2006 the Banking Supervision Handbook consisted of about ten documents. Between January 2006 and October 2013, a further nine documents were added to the Banking Supervision Handbook and some of the original documents were replaced with multiple documents.[12]

There has been growth not only in the size of the Banking Supervision Handbook but also in the range of matters covered and an increase in the detail of the regulation included within it. Changes within the last 10 years include the introduction of minimum liquidity and corporate governance requirements, the implementation of the Basel II and III capital adequacy frameworks, and the development of the Open Bank Resolution policy.[13]

2.3 Public disclosure requirements

Sections 81 to 83 of the RBNZ Act contain a regime for financial disclosure by registered banks. In particular, disclosure requirements may be set by Orders

---

5 Report of the Finance and Expenditure Committee on the Reserve Bank of New Zealand Bill (December 1989) at 8.

6 Reserve Bank of New Zealand Act 1989, s 74(4).

7 See the amended s 74 inserted into the Act by s 16 of the Reserve Bank of New Zealand Amendment Act 2003.

8 Reserve Bank of New Zealand *Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks: summary of submissions and policy decision* (18 December 2015).

9 Reserve Bank of New Zealand *Consultation Document: Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks* (July 2015) at [110].

10 Ibid at [112].

11 Ibid at [114].

12 Ibid at [114]–[115].

13 Ibid at [1].

in Council made under s 81(1) made on the advice of the Minister of Finance in accordance with a recommendation of the Reserve Bank.

2.4 Macro-prudential regulation

In 2013, the Governor of the Reserve Bank and the Minister of Finance entered a MOU intended to provide "clarity over the purpose and instruments of macro-prudential policy, so that emerging systemic risks are able to be addressed in a timely manner".

The MOU provides that the objective of macro-prudential policy is "to increase the resilience of the domestic financial system and counter instability in the domestic financial system arising from credit, asset price or liquidity shocks".

The MOU goes on to list four macro-prudential instruments that are "considered useful in the New Zealand context for addressing the systemic risks of financial instability". These instruments are: adjustments to the core funding ratio; countercyclical capital buffer; adjustments to sectoral capital requirements; and quantitative restriction on the share of high LVR loans.

Under the MOU, the decision on macro-prudential intervention is one for the Governor. But the MOU provides that development of any additional macro-prudential instruments "will be undertaken in consultation with the Treasury".

In addition, the Bank agrees to keep the Minister and the Treasury "regularly informed on its thinking on significant policy developments relating to macro-prudential policy, and of emerging risks to the financial system". To this end, the Bank is obliged to consult with the Minister and Treasury "from the point where macro-prudential intervention is under active consideration" and to inform the Minister and Treasury "prior to making any decision on deployment of a macro-prudential policy instrument".

3 Issues arising in relation to the current framework

3.1 Introduction

In the time since the current framework for conditions of registration was set, significant changes have occurred in the practice of prudential regulation of banks.

Prudential regulation has become much broader in scope and more prescriptive over time than appears to have been envisaged when the framework was established in the 1980s. Today the requirements contained in the Banking Supervision Handbook and imposed through the conditions of registration have a very significant impact on a bank's organisation and operations. Yet, the RBNZ Act provides more oversight for information disclosure requirements (set by Order in Council) than it does for the prudential requirements (determined and imposed by administrative decision-making). Similarly, while the RBNZ Act envisages a "handbook" of sorts (under s 75, the Reserve Bank is required to "publish the principles on which it acts" in determining applications for registration and imposing/varying conditions) it seems unlikely that the inclusion of such an extensive set of prudential requirements was envisaged.

These observations are not intended to be critical of the Reserve Bank. Rather, the divergence between the statutory framework and the current practice of prudential regulation that has arisen over 30 years indicates that it is an appropriate time for a stocktake to assess the robustness of the statutory framework.

In this regard, I note that the introduction of prudential regulation in relation to insurance and non-bank deposit takers in recent years has relied on different statutory instruments for some of the regulatory tools provided in those Acts:[14]

- Under the Insurance (Prudential Supervision) Act 2010 (**IPS Act**) prudential requirements for insurers are contained in "standards" (fit and proper standards and solvency standards). Standards are drafted by the Reserve Bank and made by a notice signed by the Governor.[15] However, they are a "disallowable instrument" and so are subject to scrutiny by the Regulations Review Committee (**RRC**) and may be disallowed by Parliament.[16] Standards must be publicly notified and the IPS Act provides for a consultation process in relation to their making.[17] There is also considerable scope for conditions to be imposed on a licensed insurer.[18]
- Non-bank deposit takers are regulated under the Non-bank Deposit Takers Act 2013 (**NBDT Act**). That Act requires non-bank deposit takers to be licensed by the Reserve Bank.[19] Prudential requirements take the form of regulations that are drafted by the Parliamentary Counsel Office (**PCO**) and made by Order in Council by the Governor General on the advice of the Minister given in accordance with a recommendation of the RBNZ.[20] The NBDT Act imposes consultation obligations on the RBNZ before it makes a recommendation for the making of a regulation.[21] Regulations are a type of "legislative instrument" and legislative instruments are disallowable instruments, so they are subject to scrutiny by the RRC and Parliament.[22] In addition, the NBDT Act allows the Reserve Bank to issue licenses subject to conditions.[23] Conditions may modify any of the prudential requirements imposed by regulations.[24]

Looking at other sectors where participants are subject to similar (if not entirely analogous) regulatory powers:

- The Financial Markets Conduct Act 2013 provides a process for making regulations covering a wide variety of matters.[25] In each case the regulations

---

[14] Although it is outside the scope of this report to consider these other regimes in detail, I note that there are significant differences between those regimes and the way that banks are regulated. It is possible that those differences are justified. However, the differences appear to be largely accidents of history rather than the result of deliberate policy choices.

[15] Insurance (Prudential Supervision) Act 2010, ss 36 and 55.

[16] Insurance (Prudential Supervision) Act 2010, s 233.

[17] Insurance (Prudential Supervision) Act 2010, ss 234–235.

[18] Insurance (Prudential Supervision) Act 2010, ss 20-21.

[19] Non-bank Deposit Takers Act 2013, s 11(1).

[20] Non-bank Deposit Takers Act 2013, ss 24, 30, 33, 36 and 39.

[21] Non-bank Deposit Takers Act 2013, s 76.

[22] Legislation Act 2012, ss 4 (defintition of "legislative instrument") and 38.

[23] Non-bank Deposit Takers Act 2013, s 18.

[24] Non-bank Deposit Takers Act 2013, s 19(1)(c).

[25] Financial Markets Conduct Act 2013, ss 543–548.

may be made by the Governor-General, on the recommendation of the Minister. However, the Minister is required to consult with the Financial Markets Authority (**FMA**) before making the recommendation.[26] The FMA also has a power to grant exemptions from provisions of these regulations (and certain provisions of the Act).[27] The Productivity Commission has observed that under the conditions of registration regime the Reserve Bank, unlike the FMA, is able to determine regulatory requirements of significant matters without requiring the approval from Ministers or Cabinet.[28]

- Under amendments made in 2008, price control under Part 4 of the Commerce Act 1986 proceeds by way of the Commerce Commission determining various "input methodologies" in advance of price control being applied to particular entities. The input methodologies are subject to merits review in the High Court with two subject matter experts sitting with the Judge.[29]

In Australia, I understand that prudential regulation of banks and insurance companies is generally implemented through prudential standards that are a form of delegated legislation. Under the governing legislation, the Australian Prudential Regulation Authority has a broad power to determine standards in relation to prudential matters.[30] Most standards are deemed to be legislative instruments,[31] which are subject to a parliamentary disallowance regime.[32] Decisions affecting individual entities may also be appealed to the Administrative Appeals Authority and subsequently, on a question of law, to the Federal Court.[33]

For all these reasons, it is timely to review whether the statutory framework for prudential regulation of banks remains consistent with best practice, or whether changes should be considered.

The remainder of this part of the report considers the following potential legal/regulatory issues that arise in relation to the present framework (and which I have been asked to address) in more detail:

- The main prudential rules sit outside the conditions of registration;
- There is limited or no Ministerial or Parliamentary scrutiny of the rules;
- There is no express process for the general rules to be tailored to the circumstances of a particular bank;
- The Reserve Bank has retained an ongoing administrative decision-making function through the "notice of non-objection" process;
- The macro-prudential MOU is not envisaged by the RBNZ Act and may operate in practice to constrain the Reserve Bank's powers;
- The regulatory perimeter presently evolves in an ad hoc function; and
- The accessibility of the prudential requirements.

I discuss each in turn.

---

[26] Financial Markets Conduct Act 2013, ss 549.
[27] Financial Markets Conduct Act 2013, ss 556–557.
[28] New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 223–224.
[29] See *Wellington International Airport Ltd v Commerce Commission* [2013] NZHC 3289.
[30] Banking Act 1959 (Cth), s 11AF.
[31] Banking Act 1959 (Cth), s 11AF(7A).
[32] Legislation Act 2003 (Cth), ss 36–48.
[33] See fn 43 and 44 below and the accompanying text.

3.2 The main regulatory rules now sit outside the conditions

The practice of prudential regulation of banks has evolved in such a way that the detailed requirements are to be found in the Banking Supervision Handbook. The conditions of registration give effect to the Handbook by stipulating which parts apply to the bank in question. In most cases the same requirements apply to all banks, although in some areas (particularly capital requirements) there is variation among entities.

The organic development of the Banking Supervision Handbook as the substantive rulebook for prudential regulation gives rise to a number of issues.

The first is whether the statutory framework should focus on the Banking Supervision Handbook as the principal regulatory instrument in the framework rather than on the conditions of registration. That is, in contrast to the standards and regulations that apply in relation to insurer and non-bank deposit takers respectively, the prudential "rules" for banks sit in a policy document that is not referred to in the statutory framework.[34]

As the rules sit outside the statutory framework, there are no prescribed statutory processes in relation to consultation or oversight of the Banking Supervision Handbook other than general administrative law principles.

In terms of consultation, the RBNZ Act prescribes that the Reserve Bank must consult with an affected bank before imposing or varying a condition of registration.[35] However, because the Banking Supervision Handbook sits outside the legislative framework, there are no statutory requirements to, for example, undertake public consultation in relation to the content of the Handbook. I understand that the Reserve Bank's practice has been for conditions to refer to the Handbook as it existed on a particular date and to consult on changes to the Handbook.[36] While this means that consultation occurs in practice in order to incorporate the updated Handbook requirements into the conditions, a good case can be made that the process protections should be enshrined in legislation as is the case with the IPS Act and the NBDT Act.[37]

3.3 Absence of Ministerial or Parliamentary scrutiny

Conditions of registration are treated as a form of administrative instrument rather than subordinate legislation. As a result they are neither a legislative instrument nor a disallowable instrument under the Legislation Act.[38] They are therefore made by the

---

[34] Section s 75 of the RBNZ Act does require the Reserve Bank to publish certain principles. However, the role the Banking Supervision Handbook plays is much broader in scope.

[35] Reserve Bank of New Zealand Act 1989, s 74(3).

[36] Reserve Bank of New Zealand *Consultation Document: Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks* (July 2015) at [111].

[37] Insurance (Prudential Supervision) Act 2010, s 235 and Non-bank Deposit Takers Act 2013, s 76.

Footnote withheld under sections 9(2)(d), 9(2)(g)(i) and 9(2)(h)

Reserve Bank without the Minister of Finance or Parliament having any decision rights or right of veto.

Over recent years there has been a significant growth in the breadth and complexity of prudential regulation and with this comes a wider range of impacts on the wider economy. This raises the question as to whether there are appropriate safeguards in place as to the setting of regulatory requirements. While it is desirable to delegate matters of technical detail to regulatory agencies, the question is whether the prudential requirements are subject to too little scrutiny, particularly in comparison with the IPS Act, the NBDT Act and the financial markets regime.

3.4 Process for tailoring prudential requirements

As noted above, the Reserve Bank's practice is to generally impose the common rules in the Banking Supervision Handbook to all registered banks, but with some tailoring (for example, around capital requirements).

Because the standard set of rules contained in the Banking Supervision Handbook exists as a policy document with the conditions being the primary focus of the statutory framework, there are no statutory provisions dealing with tailoring these rules to a particular bank. Presently, this just occurs through the Reserve Bank's administrative discretion in determining the conditions which will apply to a particular bank.

If one accepts, however, that the standard set of rules contained in the Banking Supervision Handbook is like a default code, then it may be desirable to deal with

---

Footnote withheld under sections 9(2)(d), 9(2)(g)(i) and 9(2)(h)

tailoring through an express process of granting exemptions, as is the case with the IPS Act, the NBDT Act and the FMC Act.[39]

One of the issues that would be addressed if there was an express framework for tailoring (or exemption granting) is whether a bank should have any ability (beyond the right to seek judicial review) to challenge such a decision.

3.5 The Reserve Bank's ongoing administrative decision-making function

Under the conditions of registration framework, the Reserve Bank may set requirements that call for approvals or other administrative decision making on the part of the Reserve Bank on an ongoing basis.

For instance, in the case of capital requirements it is a condition of registration of locally incorporated registered banks that they receive a notice of non-objection from the Reserve Bank before treating any capital instrument (aside from ordinary shares) as regulatory capital.[40] Other examples include approvals for internal ratings-based models, permission to repay a capital instrument, permission for significant acquisition, and non-objection in relation to a director or senior manager.

This ongoing administrative decision-making function has received recent attention in the Kiwibank issue. According to media reports, the Reserve Bank had previously provided Kiwibank with letters of non-objection in relation to two bond instruments (collectively worth $250 m) being treated as regulatory capital. However, in May 2017 the Reserve Bank came to the view that the bond instruments did not comply with its capital requirements. In order to rectify the situation, Kiwibank shareholders had to inject new equity.[41] I am informed, by the Reserve Bank, that this change in position was the result of new information which came to light. The Reserve Bank has since issued a letter of non-objection after changes were made to to address its concerns.[42]

In exercising these powers the Reserve Bank is functioning as an administrative decision-maker and not as a judicial tribunal. However, many such administrative decisions are subject to appeals to the Courts. Under the Insurance (Prudential Supervision) Act 2010, the Reserve Bank's decision that a director or officer of a licensed insurer is not a fit and proper person may be appealed to the High Court and then, on a question of law, to the Court of Appeal.[43]

---

39 Insurance (Prudential Supervision) Act 2010, ss 38, 59, 60(2A), 119, 204(4), 220(4), 232 and 238; Non-bank Deposit Takers Act 2013, ss 70–72; and Financial Markets Conduct Act 2013, ss 556–557.

40 "Information relating to the capital adequacy framework in New Zealand" Reserve Bank of New Zealand <www.rbnz.govt.nz>; and RBNZ "Application requirements for capital recognition or repayment and notification requirements in respect of capital" (BS16, November 2015).

41 "Reserve Bank of New Zealand confirms decision on Kiwibank's convertible capital instruments held by Kiwi Capital Funding Limited (KCFL)" (30 May 2017) Kiwibank Ltd <www.kiwibank.co.nz>; and Hamish Rutherford "Reserve Bank spat forces Kiwibank to ask shareholders for $247m" *Stuff* (online ed).

42 Sophie Boot "Reserve Bank changes its mind on Kiwibank bonds" *NBR* (online ed) (10 August 2017).

43 Insurance (Prudential Supervision) Act 2010, ss 42 and 43.

Other similar administrative decisions are also subject to appeals to the Court. For example, a party who applies to the Commerce Commission for a merger clearance can appeal the decision to the High Court where the Court reaches its own view based on the evidence that was before the Commission. Similarly, appeal rights exist in relation to various administrative decisions of the Registrar of Companies and the Taxation Review Authority.

Further, in Australia many decisions of the Australian Prudential Regulation Authority may be appealed to the Administrative Appeals Tribunal (usually after a request has first been made to APRA to reconsider its decision).[44] There is then a right of appeal, on a question of law, to the Federal Court of Australia.[45]

Appeal rights from regulatory decisions are often seen as desirable to ensure quality decision-making and accountability, and to ensure that those subject to administrative discretions can hold decision-makers to account.

A number of issues arise in relation to ongoing administrative decision-making powers:

- Are such ongoing powers appropriate?
- Should a bank have appeal rights?
- Should a bank be able to disregard the Reserve Bank's view and force the Reserve Bank to take enforcement action?

3.6 The status of the MOU re macro-prudential regulation

As discussed above, a MOU has been put in place between the Minister of Finance and the Reserve Bank for macro-prudential requirements with a set of four agreed tools (LVR restrictions, the counter-cyclical capital buffer, sectoral capital requirements and the core funding ratio). At the time it was agreed, the then Minister described it as providing for "four new measures".[46] Accordingly, a distinction now exists between prudential and macro-prudential requirements, even though both types of requirement are empowered by s 74 of the RBNZ Act. The MOU does not have an express legislative basis.

The Banking Supervision Handbook refers to the MOU and states that "decisions to impose these conditions, and subsequently to vary or remove them, are taken within the framework set out in the Reserve Bank's Memorandum of Understanding on macro-prudential policy".[47]

---

[44] Banking Act 1959 (Cth), s 51C(1); Financial Institutions Supervisory Levies Collection Act 1998 (Cth), s 27(6); Financial Sector (Business Transfer and Group Restructure) Act 1999 (Cth), s 45; Financial Sector (Collection of Data) Act 2001 (Cth), s 25D(1); Insurance Act 1973 (Cth), s 63(7); Life Inusrance Act 1995 (Cth), s 236(8); Medical Indemnity (Prudential Supervision and Product Standards) Act 2003 (Cth), s 14; Private Health Insurance (Prudential Supervision) Act 2015 (Cth), s 168(7); Retirement Savings Accounts Act 1997 (Cth), s 189(7); and Superannuation Industry (Supervision) Act 1993 (Cth), s 344(8). A list of decisions reviewable by the Administrative Appeals Tribunal is available at www.aat.govt.au/applying-for-areview/when-we-can-help/jurisdiction.

[45] Administrative Appeals Tribunal Act 1975 (Cth), s 44.

[46] Bill English "New tools agreed to enhance financial stability" (press release, 16 May 2013).

[47] Statement of Principles: Bank Registration and Supervision (BS1, December 2016) at [97A].

Under the RBNZ Act the Reserve Bank has power to impose conditions relating to the matters specified in the Act or in regulations made by Order in Council. The MOU cannot constrain the Reserve Bank from exercising powers that already exist under the Act. If it purported to do this it could be argued that the Reserve Bank was taking into account irrelevant considerations or impermissibly delegating its statutory responsibilities by seeking the Minister's consent.

While I do not consider that the wording of the MOU constrains the Reserve Bank, public communications about it have appeared to imply that it does.[48] For instance, the Reserve Bank has recently summarised the effect of the MOU in a consultation paper as follows: "In 2013, the Bank and the Minister of Finance agreed that direct, cyclical controls of this sort would not be imposed without the tool being listed in the [MOU]. Hence, cyclical DTI limits will only be possible in the future if an amended [MOU] is agreed."[49] If this is how the MOU is being applied in practice it would, in my view, give rise to public law concerns.

Aside from those concerns, the application of the MOU (on its own terms) is unclear. The distinction between macro-prudential and prudential tools is not clearly defined and there is no clear statement of which tools that are empowered by ss 74 and 78 are required to be in the MOU before they can be used.

3.7 Issues in relation to evolution of the regulatory perimeter

The scope of areas subject to conditions of registration and the Banking Supervision Handbook has grown over time.

The RBNZ Act describes and controls the "regulatory perimeter" (that is, the set of matters in relation to which prudential requirements may be set) by:

- setting out in ss 73-73B, 78 and 81 the range of matters that conditions of registration may relate to (s 74(4)); and
- allowing for regulations to be made on the advice of the Minister to extend that range of matters (in particular under s 78(2)).[50]

I note that within the regulatory perimeter, the Reserve Bank acts with a large degree of autonomy as the prudential requirements are not presently subject to any Parliamentary or judicial oversight (other than through judicial review). This would suggest that the statutory intention is to leave the Reserve Bank relatively unconstrained, but that the boundaries should not be interpreted openly to expand the scope for regulation beyond that which has been clearly authorised. In my view the issues of oversight and the nature of the regulatory perimeter are closely connected: the narrower the scope of the empowering provision the more independence will be allowable.

---

[48] Steven Joyce "Finance Minister requests cost-benefit analysis on DTIs" (press release, 8 February 2017).

[49] Reserve Bank of New Zealand *Consultation Paper: Serviceability Restrictions as a Potential Macro-prudential Tool in New Zealand* (8 June 2017).

[50] Section 78 lists a range of matters related to carrying on business in a prudent manner including, as a final item, "such other matters as may from time to time be prescribed in regulations" (s 78(2)). Such regulations are made by Order in Council "on the advice of the Minister given in accordance with a recommendation from the [Reserve Bank]" (s 78(2)).

This statutory intention could arguably be frustrated by the Reserve Bank taking a broad interpretation of the matters that conditions may relate to under the current Act. In particular, the Reserve Bank has adopted a broad interpretation of s 78(1)(fa) which, in combination with s 74, empowers it to make conditions relating to "risk management systems and policies or proposed risk management systems and policies". Recent topics that have been subject to conditions of registration that are not expressly referred to in the RBNZ Act include LVRs (including the inclusion of Auckland-specific restrictions) and liquidity requirements. This can be seen as giving the Reserve Bank the power to independently expand the regulatory perimeter.

Sections 9(2)(d), 9(2)(g)(i) and 9(2)(h)

3.8 Are the prudential requirements appropriately accessible?

Finally, there is a question whether the regulation of banks is appropriately accessible. There are a number of aspects to this:

- At present the relevant "rules" of prudential regulation are divided between the Act, conditions, the Banking Supervision Handbook and Reserve Bank decisions in relation to notices of non-objection and other ongoing administrative decision-making functions.
- There is presently no central registry of the particular conditions that have been imposed on a particular bank. Conditions are disclosed by individual banks but are difficult to locate and it is not obvious if any special conditions have been imposed. Should the Reserve Bank have a role in maintaining a publicly available register of conditions?
- The Reserve Bank does not presently publicly publish its decisions.
- The Banking Supervision Handbook is, as the Reserve Bank has acknowledged, not drafted in the clearest way.[51]

4 Regulatory options and factors to weigh up

4.1 Introduction

The purpose of this part of the report is to provide an account of the different choices to be considered in relation to how prudential regulation is to be imposed and the factors that need to be weighed up.

There is a large body of literature on the theory of regulation. However, because of the variety of circumstances in which regulation is imposed and the limitless range of

[51] Reserve Bank of New Zealand *Consultation Document: Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks* (July 2015) at [20] and [21].

options, the guidance is inevitably high level. Nevertheless, it is a useful process to go through in order to identify the factors that need to be weighed up in a particular regulatory problem.

An important point to stress is that regulatory instruments such as "regulations", "standards" and administrative "conditions" are flexible terms of art. While they can be seen as sitting on different parts of a spectrum from more to less Parliamentary oversight, they do not imply a particular setting in terms of oversight, appeal rights or ongoing administrative decision-making functions. Accordingly, it is important to ask what characteristics or qualities should the regulatory framework possess, rather than to ask should we use instrument X or instrument Y.

I have started by identifying what I see as the four key high level issues to be considered in relation to prudential regulation:

- Should prudential requirements be in primary or delegated legislation?
- If the power to make prudential requirements is delegated, should the requirements be set by the regulator, by a Minister or Order in Council, or somewhere in between?
- What is the appropriate balance between one-size-fits-all rules and administrative discretion in particular cases?
- What oversight should there be of the prudential rules and of particular decisions?

The following sections discuss each of these topics in turn. The discussion starts off by abstracting away from bank supervision and the particular instruments that might be used, and focuses instead on identifying factors that will tell for or against a particular approach in particular circumstances. I then make some general observations about how the analyses might inform prudential regulation of bank by the Reserve Bank. This approach then informs the specific design recommendations in part 5 of this paper.

4.2 Should prudential requirements be in primary or delegated legislation?

The topic of the appropriate use of "primary" versus "delegated" legislation has been well traversed in the literature.[52]

I use the term "primary legislation" to refer to Acts passed by the House of Representatives. It should not be confused with "legislative instrument" as defined in the Legislation Act 2012 which includes both Acts of Parliament and some delegated legislation.

The term "delegated legislation" is an umbrella term to capture laws made by bodies other than Parliament. Here I intend the phrase to capture administrative decisions such as conditions of registration as well as regulations and standards.

---

[52] See, for example, New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 228–220; *Legislation Advisory Committee Guidelines* (2014 edition) chpt 13; *Cabinet Manual* (2017) at [7.82]–[7.101]; UK Cabinet Office *Guide to Making Legislation* (July 2017); *Standing Orders of the House of Representatives* (2014), at 318–325.

The phrase is helpfully explained in the *Legislation Advisory Committee Guidelines* which provide that:[53]

> Parliament makes laws by enacting primary legislation (Acts); however, it is not always appropriate or possible for Parliament to deal with all of the detailed underlying systems and structures that give effect to an Act. In these cases Parliament often includes in an Act a provision that authorises another body, usually part of the executive, to exercise some of its law-making functions to deal with those detailed underlying systems. The Act that delegates this law-making power is known as the "empowering Act". … The product of the exercise of this power is known as "delegated legislation".
>
> Delegated legislation can be made by different bodies or officers within or outside the executive. These include the Governor-General in the Executive Council (the most common), a Minister, or a statutory body or officer. Delegated legislation is referred to by a range of terms, including secondary legislation, tertiary legislation, regulation, Proclamation, Order in Council, bylaw, rule, code, notice, or warrant.

As a general rule, primary legislation should be used for matters of policy and principle. Delegated legislation should deal with technical matters of implementation and operation of primary legislation. The table below illustrates matters that may fall on either side of the divide.

Matters that are generally appropriately addressed by primary legislation	**Matters that are generally appropriately addressed by delegated legislation (including administrative decision-making)**
Significant policy matters	Matters of detail or implementation
Provisions affecting fundamental rights and freedoms	Technical issues
Rights of appeal	Matters that are best addressed by a non-political body
Provisions that vary the common law	Allowing for potential, but as yet, unknown contingences
Creation of offences or the possibility of significant penalties	Matters likely to require frequent updating
Imposition of taxes	Responding to emergencies or situations that require speedy responses
Creation of new agencies	Rules which will be better made after some experience with new legislation
Retrospective changes	Matters that need to be consulted on before they are finalised or changed

In terms of applying these factors to prudential regulation of banks, there are some factors that would suggest primary legislation is the appropriate vehicle. In particular, the regulatory requirements may have significant financial consequences for registered banks and very important interests (financial stability) are being protected.

---

[53] *Legislation Advisory Committee Guidelines* (2014 edition), chpt 13.

However, against this, the subject matter is very technical, the rules may need to change over time and the rules should generally be set in a way that is free from political bias. Consistently with our present practice, the second set of factors would seem to dominate and suggests that prudential requirements should generally be in delegated rather than primary legislation.

4.3 If the power to make prudential requirements is delegated, should the requirements be set by the regulator, by a Minister or Order in Council, or somewhere in between?

The next issue to consider is, if prudential requirements are to be set by delegated legislation, should they be set by the regulator, by a Minister or Order in Council,[54] or by some combination?

The following table sets out factors in favour of delegated rules being set by either a Minister or by the Governor General in Council, or by an independent regulator:[55]

Factors in favour of rules being set by Governor-General in Council or Minister	Factors in favour of rules being set by an independent regulator
Matters that significantly affect the population, a large number of people or human rights	Issues where a credible commitment to a stable long term framework is important
Decisions which involve value judgments which are more appropriately made by elected representatives	More consistent and stable decision-making
Where political control is necessary to guard against "regulatory capture" by the regulated sector	Avoidance of conflicts of interest (political expediency and focus on the electoral cycle)
Decisions with significant fiscal implications or that are otherwise integral to the Government's economic strategy	Subject matter is highly technical or specialised
Creation of criminal sanctions or pecuniary penalties	Decisions which impact on particular interests should be made impartially
Decisions involving significant exercise of the coercive powers of the state (for example, taxation or expropriation of property)	Independent decision-making may be important for public confidence in the regime
	Decisions that may need to be taken urgently

[54] Note that in practice, there may not be much difference between rules being made by the relevant Minister (acting, when exercising the power, independently from Cabinet) or by the Governor General in Council. This is because as a matter of Cabinet's procedures, Cabinet expects to be informed of significant decisions that a relevant portfolio Minister intends to take (see Cabinet Office *Cabinet Manual* (2017) at [5.11]–[5.13] and [5.34]–[5.37]). Nevertheless, if the rule-making power is delegated to the Minister, it is for the Minister (and not Cabinet) to take the decision.

[55] See New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 216–220; *Legislation Advisory Committee Guidelines* (2014 edition), chpt 13, part 3.

Here I observe that, in relation to prudential regulation, there are factors in favour of traditional regulations (financial implications for banks and the importance of financial stability) and factors in favour of independent regulatory decision-making (the importance of long-term stability and impartial decision-making). Furthermore, it may be that the balance is affected by the particular area of prudential regulation. For example, macro-prudential regulation which may affect access to borrowing for house buyers may be seen as involving important value judgments.

If there is a preference for decision-making by the Reserve Bank as the independent regulator, that does not imply that political influence needs to be entirely excluded.

While the Productivity Commission recognises that political intervention in independent regulators is generally undesirable, as it will tend to undermine the authority of the regulator and encourage lobbying, trying to create complete independence may be just as problematic:[56]

> Absolute constraints on ministers may not lead to a more stable regulatory environment. Ad hoc legislation to substantially reform or override regulatory regimes as a result of temporary political frustration is deleterious to a stable, predictable and effective regulatory environment that encourages investment. There is also a risk that without clarity about how to manage such political imperatives, a regulator will be subject to more informal and insidious political pressures.

Where some form of political intervention may be appropriate (and/or inevitable), it should occur in a way that maintains the regulator's authority and does not invite future interventions. In particular, a political channel of influence or direction should be expressly provided for and exercised transparently. This both allows the regulator to more easily resist informal political pressure and means that, where politicians do intervene, they can be held to account.

As set out in the following table, there are a number of existing models that somewhere between the two extremes of delegation to Minister / Order in Council and delegation to an independent regulator.

Empowering model	**Examples**
Governor-General by Order in Council (with no involvement from the relevant Minister)	RBNZ Act, s 173 – power to make a miscellaneous range of regulations
Governor-General, on the advice of the Minister	RBNZ Act, s 12 – power to direct the Reserve Bank to formulate and implement monetary policy for any economic objective (other than maintaining price stability)
Governor-General, on the advice of the Minister but only after consulting with the specialist regulator	Financial Markets Conduct Act, ss 543-549 – power to make a range of regulations relating to disclosure financial product offers, governance of financial products, dealing in financial products on markets and market services

[56] New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 236–237.

Governor-General, on the advice of the Minister given in accordance with a recommendation of a specialist regulator	Insurance (Prudential Supervision) Act 2010: • Section 103 – power to make regulations specifying: what constitutes income of a statutory fund; what constitutes outgoing of a statutory fund; and providing for the apportionment of amounts of income and outgoings, and liabilities • Section 170 – power to put licensed insurers and associated persons into statutory management • Section 191 – power to reduce the value of contracts of insurance of a licensed insurer in statutory management Non-bank Deposit Takers Act 2013: • Section 24 – power to make regulations relating to credit ratings • Section 30 – power to make regulations relating to minimum capital requirements
Specialist regulator, subject to approval by the Minister	Electricity Act 1992 (repealed), ss 36–38 – power of WorkSafe to issue an electrical code of practice that does not come into force until approved by the Minister (who was required to undertake consultation before approving Code)
Specialist regulator, but required to have regard to a Government Policy Statement	Commerce Act 1986, s 26 – Commission to "have regard to" the economic policies of the Government as transmitted in writing from time to time. See also RBNZ Act, s 68B.
Specialist regulator	RBNZ Act, s 74 – Reserve Bank's power to impose conditions

As set out in the table above, there are many intermediate positions between a regulation made by the Governor-General and a decision made by an independent regulator.

4.4 What is the appropriate balance between one-size-fits-all rules and administrative discretion (including exemptions) in particular cases?

Allowing for exemptions and other means of tailoring general rules has the advantage of providing flexibility for the best outcome in particular cases. However, on the other hand, exemption regimes can reduce the accessibility of the law because the law is spread across primary legislation and specific exemptions.[57] This is particularly problematic if the exemptions are not publicly accessible.

[57] *Legislation Advisory Committee Guidelines* (2014 edition) at chpt 14, part 14.1.

The following table sets out some of the factors in favour of discretions and exemptions and some of the factors in favour of rules:[58]

Factors in favour of discretions	**Factors in favour of rules**
Ability to adapt a regime to a wide variety of circumstances Providing for unforeseen events, especially in a complex and evolving field Allows for a focus on outcomes rather than prescribing how those outcomes are to be achieved Allows for urgent action Allows for exceptional or "one off" issues to be dealt with (eg where compliance is impractical or unduly expensive) without having to amend the underlying rules	Certainty and predictability Respect for the rule of law: the exercise of state power should be in accordance with rules known in advance and set with sufficient specificity to allow individuals to know with tolerable certainty their rights and obligations.

In considering the balance between certainty and flexibility, it is important to include the overlay of administrative law principles that will govern decisions about exemptions in particular cases.[59] In exercising discretionary powers, the decision-maker must:

- use discretionary powers in good faith and for a proper purpose (i.e. honestly and only within the scope and purpose for which the powers are given);
- base their decision on logically probative material (i.e. logical reasons, information that proves the issues in question, relevant and reliable evidence);
- consider only relevant considerations and not consider irrelevant considerations;
- give adequate weight to a matter of great importance but not give excessive weight to a relevant factor of no great importance;
- exercise their discretion independently and not act under the dictation or at the behest of any third person or body;
- give proper, genuine and realistic consideration to the merits of the particular case, and not apply policy inflexibly; and
- observe the basic rules of procedural fairness (i.e. natural justice).

Conversely, the decision-maker must not:

- make decisions in matters in which they have an actual or reasonably perceived conflict of interest;
- improperly fetter their own discretion (or that of future decision-makers) by, for example, adopting a policy that prescribes decision-making in certain circumstances;

---

[58] See New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 274; *Legislation Advisory Committee Guidelines* (2014 edition) at 56–58 regarding exemptions from legislation.

[59] "Reviewing the Exercise of Discretionary Powers" (2004) 10:2 Ombudsman Quarterly Review.

- exercise a discretion in a way that is so unreasonable that no reasonable person would have exercised the power in that way;
- exercise a discretionary power in such a way that the result is uncertain;
- act in a way that is biased or conveys a reasonable perception of bias;
- make decisions that are arbitrary, vague or fanciful;
- refuse to exercise a discretionary power in circumstances where the decision-maker is under a duty to do so; or
- unreasonably delay the making of a decision that the decision-maker is under a duty to make.

Best practice is to make exemption powers and other discretions subject to safeguards such as the following:[60]

- the empowering legislation should clearly define the purposes for which the discretion may be exercised;
- legislation should set out criteria for granting an exemption;
- legislation should include a requirement to give reasons for the exemption and to make these publicly available;
- exemptions should be subject to an expiry date to ensure regular review of the exemption; and
- the right to seek judicial review of the exercise of the exemption power should be preserved.

It may also be appropriate for the decision-maker to issue guidance as to how discretion will be exercised. Such guidance should be straightforward, flexible and explain relevant considerations.[61]

4.5 What oversight should there be of the rules and particular decisions?

Introduction

The final topic is what, if any, oversight regime(s) apply to the prudential requirements generally or to the exercise of any powers of exemption (or other discretions).[62]

In terms of oversight of the prudential requirements, the two main options are scrutiny by the RRC if they are a disallowable instrument or judicial scrutiny through judicial review or appeal rights created by legislation.

In terms of oversight of the exercise of discretionary powers, options include: internal review;[63] complaint to the Ombudsman;[64] judicial oversight through judicial review or appeal rights; and/or oversight by a specialist tribunal such as a rulings panel.

---

60 *Legislation Advisory Committee Guidelines* (2014 edition) at chpt 14, part 14.2.

61 Office of the Ombudsman *Good Decision Making* (2012) at p 3. See also s 75 of the RBNZ Act.

62 See generally New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 286; David Goddard *"Regulatory Error: Review and Appeal Rights"* (paper presented to Legal Research Foundation. Conference, Auckland, September 2006).

63 An internal review is sometimes provided for in empowering legislation (see New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 298). In addition, many bodies operate internal review procedures without legislative provision although it is preferable for such review procedures to be provided for in legislation (see

In this section I discuss oversight by the RRC, judicial oversight and a specialist rulings panel.

Regulations Review Committee

The RRC has jurisdiction in relation to all regulations, defined as "any delegated legislation, including legislative instruments and disallowable instruments within the meaning of the Legislation Act 2012".[65]

In considering a regulation, the RRC considers whether it ought to be drawn to the attention of the House on one or more of the following grounds, namely it:[66]

(a) is not in accordance with the general objects and intentions of the statute under which it is made;
(b) trespasses unduly on personal rights and liberties;
(c) appears to make some unusual or unexpected use of the powers conferred by the statute under which it is made;
(d) unduly makes the rights and liberties of persons dependent upon administrative decisions which are not subject to review on their merits by a judicial or other independent tribunal;
(e) excludes the jurisdiction of the courts without explicit authorisation in the enabling statute;
(f) contains matter more appropriate for parliamentary enactment;
(g) is retrospective where this is not expressly authorised by the empowering statute;
(h) was not made in compliance with particular notice and consultation procedures prescribed by statute; or
(i) for any other reason concerning its form or purport, calls for elucidation.

Note that the RRC does not concern itself with (or offer opinions on) matters of policy.

If one or more of these grounds are met, the RRC may refer the regulation to the attention of the House.[67] The House has a power, by resolution, to disallow any disallowable instrument or provisions of a disallowable instrument.[68] If a notice of motion to disallow an instrument or any provisions of an instrument is given by a

---

Legislation Advisory Committee Guidelines (2014 edition) at 25.2). At present, internal review tends to be available for low level decisions rather than cases of complex economic regulation (see New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 298–299).

64 The Ombudsmen can investigate "any decision or recommendation made, or any act done or omitted" by certain named departments and organisations (see Ombudsmen Act 1975, s 13(1)). However, the RZBNZ is not one of the listed organisations (see Ombudsmen Act 1975, sch 1). Accordingly, absent an amendment to the Ombudsmen Act, Ombudsmen oversight will not apply. Note that the Banking Ombudsman Scheme does not have oversight of the Reserve Bank.

65 Standing Orders of the House of Representatives, o 315 and the definition of "regulation" in o 3(1).

66 Standing Orders of the House of Representatives, o 319(2).

67 Standing Orders of the House of Representatives, o 319(1).

68 Legislation Act 2012, s 42(1).

member of the RRC, the instrument or provisions is automatically disallowed if the motion is not otherwise disposed of within 21 sitting days.[69]

Treating prudential requirements as a disallowable instrument and subject to RRC scrutiny can be an important check on the exercise of regulatory powers and adds an element of democratic accountability. However, it would also add an element of uncertainty to the prudential requirements as there would be some risk that the Committee took exception to a particular requirement.

Judicial oversight

In terms of judicial oversight, the exercise of public power (in particular statutory power, which includes the making of regulations, rule, bylaws, orders or giving any notice or direction that has effect as subordinate legislation)[70] is subject to judicial review. In addition, there may also be appeal rights if those are provided for in the empowering legislation.

Judicial review provides oversight as to process and legality. It is a supervisory jurisdiction that enables the courts to ensure that public powers are exercised lawfully.[71] In judicial review, the court typically defers to the expertise of a specialist regulator in terms of the substance (there is a very high standard to show a decision is unreasonable). The court's focus is on ensuring the subject is treated fairly and in accordance with the law.

Appeal rights allow a challenge as to merits and correctness. These only exist if provided for in the statue. Where appeal rights are conferred, there are a range of options: de novo (hears afresh), re-hearing (based on evidence before the first decision maker, although can be updating evidence), pure appeals (no new evidence) and case-stated or appeals on points of law only (narrow legal questions, typically as to interpretation of the governing statue).

The following table sets out factors in favour of and against judicial oversight:

Factors in favour of more judicial oversight	**Factors in favour of less judicial oversight**
Improvement of decision-making through review process Protection of rights of regulated entities	Regulator has better information and expertise than the Courts Cost Delay Need for finality

Specialist rulings panel

A specialist rulings panel is an option for oversight of the exercise of discretionary powers. For example, a rulings panel is provided for in the Electricity Industry Act

[69] Legislation Act 2012, s 43.
[70] Judicial Review Procedure Act 2016, s 5.
[71] *Ririnui v Landcorp Farming Ltd* [2016] NZSC 62, [2016] 1 NZLR 1056 at [1].

2010.[72] The functions of the rulings panel include hearing and determining: complaints about breaches or possible breaches of the Electricity Industry Participation Code; and appeals from certain decisions made under the Code.[73] The members of the panel are appointed by the Governor-General on the recommendation of the Minister, after the Minister has consulted with the Minister of Justice and the Electricity Authority.[74] This allows for the appointment of members with subject matter expertise. A similar rulings panel could be set up to hear appeals in relation to the exercise of the Reserve Bank's discretionary powers.

4.6 How are these policy choices implemented in practice?

There is a large variety of ways in which prudential requirements might be imposed and scrutinised.

While it is difficult to provide a complete list of options, the following table sets out the broad categories available. It is important to note that labels like "conditions" and "standards" (and even "regulations") do not have precise meanings within this taxonomy and that there is a large amount of variety within each option as empowering statutes can (and often do) customise the regime to suit the particular issue at hand. It is, therefore, best to focus on the features that are desired rather than on a particular label.

Type of instrument	Decision Maker	Drafting	Publisher	Executive / Parliamentary scrutiny	Judicial scrutiny
Legislation	Parliament	PCO	PCO	Government Bills require Cabinet approval for introduction. Bills must be passed by the House.	Making of Acts not subject to either judicial review or appeal rights. But decisions made under legislation may be reviewable/ appealable.
Regulations					
Regulations by Order-in-Council	Governor-General in Council But empowering provision may require advice of Minister and also a recommendation from regulator.	PCO	PCO	*Executive*: Cabinet approves most matters for consideration by Executive Council.[75] *Parliament:* if a legislative or disallowable instrument, • Laid before House (in case of legislative instruments and some disallowable instruments)[76] • Subject to Regulations Review Committee scrutiny[77] • Parliament may disallow (in the case of a disallowable	Exercise of power to make regulations may be subject to judicial review.

[72] Electricity Industry Act 2010, ss 23–26 and Electricity Industry (Enforcement) Regulations 2010.
[73] Electricity Industry Act 2010, s 25.
[74] Electricity Industry Act 2010, s 24.
[75] Cabinet Office *Cabinet Manual* (2017) at [1.39]–[1.41].
[76] Legislation Act 2012, s 41.
[77] Standing Orders of the House of Representatives, o 318 and the definition of "regulations" in o 3(1).

				instrument)[78]	
Regulations that are confirmable instruments Eg: *RBNZ Act, s 152*	Governor-General in Council and Parliament	PCO	PCO	*Executive*: Cabinet approves most matters for consideration by Executive Council. *Parliament*: revoked unless confirmed by Parliament[79]	Exercise of power to make regulations may be subject to judicial review.
Regulations subject to affirmative resolution	Governor-General in Council and Parliament	PCO	PCO	*Executive*: Cabinet approves most matters for consideration by Executive Council *Parliament*: regulations require approval of Parliament either before being made[80] or in order to come into force.[81] Before being approved, such regulations are first referred to a select committee.[82]	Exercise of power to make regulations may be subject to judicial review.
Other delegated legislation					
Instruments made by Minister NB: *Will be a legislative instrument if empowering Act requires publication under Legislation Act and a disallowable instrument if they are a legislative instrument or have "significant legislative effect"*	Minister	Ministry	PCO (if a legislative or disallowable instrument). Otherwise, Ministry.	*Executive*: Minister will inform Cabinet of significant decisions.[83] *Parliament*: if a legislative or disallowable instrument, • Laid before House (in case of legislative instruments and some disallowable instruments) • Subject to Regulations Review Committee scrutiny • Parliament may disallow (in the case of a disallowable instrument)	Exercise of power to make instrument may be subject to judicial review.
Instruments made by regulator	Regulator	Regulator	PCO (if a legislative or disallowable instrument). Otherwise, regulator.	*Parliament*: if a legislative or disallowable instrument,[84] • Laid before House (in case of legislative instruments and some disallowable instruments) • Subject to Regulations Review Committee scrutiny • Parliament may disallow (in the case of a disallowable instrument)	Exercise of power to make instrument may be subject to judicial review. Some instruments may be subject to a merits review appeal (eg input methodologies)
Instruments	Regulator	Regulator	Regulator[85]	None	Exercise of power to make

[78] Legislation Act 2012, s 42.
[79] Legislation Act 2012, Part 3, subpart 1A.
[80] See, for example, Public Finance Act 1989, s 82(5).
[81] See, for example, Misuse of Drugs Act 1975, s 4A and Dog Control Act 1996, s 78B(2). The relevant regulations under both these Acts have the effect of amending schedules to the Act.
[82] Standing Orders of the House of Representatives, o 322.
[83] Cabinet Office *Cabinet Manaul* (2017) at [5.11]–[5.13] and [5.34]–[5.37].
[84] Compare, for example, s 52W(4) of the Commerce Act 1986 which provides that input methodoligies are neither legislative instruments nor disallowable instruments.

specific to individual entities (eg conditions of licence, notices)					instrument may be subject to judicial review.
Administrative decision-making instruments (eg notice of non-objection)	Regulator	Regulator	Regulator	None	Exercise of power to make instrument may be subject to judicial review and appeal rights.

5 Appropriate legal framework for setting prudential requirements

5.1 Introduction

In this part of the report I set out my recommendations as to the appropriate framework for setting prudential requirements for banks having regard to the issues raised in Part 3 and the options and considerations identified in Part 4.

Prudential regulation of banks touches on number of different law-making tensions.

On the one hand, financial stability is a vital interest and this suggests that democratically elected members of Parliament should retain control over the content of the law. On the other hand, the subject matter is technical, long term stability is important, and the costs of prudential requirements are concentrated but the benefits diffuse such that political actors may not always have strong incentives to act in a timely manner.

Oversight mechanisms could enhance accountability under the regime, but on the other hand they may add delay and create uncertainty as to whether purported requirements are legally effective. This could undermine the financial stability objective.

I am conscious that there is no "correct" way of imposing prudential requirements and that my recommendations involve evaluative judgments as to the correct balance to be struck between competing factors. I note that in making these recommendations, I have conducted a desktop exercise without consultation with regulated entities and other interested parties. Also, I have confined my analysis to the issues of principle rather than working through the detail of the various prudential requirements; I see that as a second stage to be undertaken as part of the drafting of any new legislative framework. Finally, I note that I have conducted my review on a 'blank sheet' basis. That is, in making my recommendations I have not sought to achieve consistency with the existing IPSA, NBDT or APRA regimes. I do not consider that designing the regime for prudential regulation of banks with the aim of achieving consistency with those other regimes would be particularly helpful given (among other factors) that those regimes have their own inconsistencies and reflect different characteristics in those sectors.

---

[85] If instruments are truly specific to individual entities (unlike the Banking Supervision Handbook) they are unlikely to legislative instruments or disallowable instruments.

Section 3 identified a number of issues with the Act that it would be desirable to consider in an updated statutory framework, including that :

- some of the prudential requirements (for example, LVR restrictions) are not listed in section 78 of the Act Sections 9(2)(d), 9(2)(g)(i) and 9(2)(h)
- whether conditions of registration together with the Banking Supervision Handbook amount to a disallowable instrument despite the practice to the contrary;
- the MOU provides for Ministerial input in a way not envisaged by the RBNZ Act;
- whether exemptions may be granted; and
- whether greater process protections should be put in place around the Reserve Bank's administrative role.

Any updated statutory framework should address these issues expressly to remove any doubt.

I set out my recommendations by addressing the following questions in turn:

- What is the appropriate regime for imposing prudential requirements?
- Should there be additional process steps for "policy-heavy" requirements?
- What should the process be for tailoring and exemptions?
- What should the process be for ongoing approvals?
- How should the regulatory perimeter evolve over time?
- How should the rules be disclosed?

5.2 What is the appropriate regime for prudential requirements?

Introduction: An accountability deficit in the present regime?

Notwithstanding their current form, prudential requirements are in substance a type of law (or at least "law like") in that they involve the application of general rules to a specific class of entities. In this sense, they are (in type, if not detail) not unlike the general rules provided for in the Financial Markets Conduct Act 2013 or the solvency standards set under the Insurance (Prudential Supervision) Act 2010. If prudential regulation is a type of law, it (like other types of law) should be subject to accountability mechanisms.

Against this, I note that the rules in the Financial Markets Conduct Act relate to types of conduct and the IPS Act and the NBDT Act provide compulsory regimes for insurers/non-banks. By contrast, prudential regulation applies on an opt-in basis to institutions that voluntarily register as banks. That distinction, however, is not inconsistent with prudential regulation being a type of law (or at least "law like"). The same point could be made about the rules in the Financial Markets Conduct Act – if one chose not to engage in conduct in financial markets, the rules would not apply. In this narrow sense, much regulation is "opt-in". Of course, in practice it is not really practical for large banks to opt out of the prudential regulation regime by deciding not to register as banks. Further, even if banks did have a real choice, that does not justify setting up a regime that is not subject to accountability mechanisms.

The desirability of having accountability mechanisms for the prudential regulation regime is strengthened by the following considerations:

- Prudential settings affect the risk levels taken by banks, which in turn affect the likelihood of the government stepping in to guarantee or otherwise support bank activities (either informally or through Open Bank resolution).
- Prudential settings affect life choices of borrowers.

While it is understandable that responsibility has been delegated to the Reserve Bank to set the prudential requirements, the absence of greater checks and balances is out of step with comparable regulatory regimes. Presently it is only subject to judicial review, and given the high policy content of the Reserve Bank's decision it may be difficult for a bank to successful challenge its decisions.

I also note the understandable wish of the Government to influence prudential regulation as reflected in the MOU. However, the MOU appears to be the wrong regulatory tool given the public law issues raised. This therefore gives rise to the question as to how the legal framework can be better designed to:

- Give the Government or Minister some say in articulating the policy objectives/target at a more granular level (see points on a GPS); and/or
- Give the Government or Minister some say in the choice of tools that are outside the standard tool kit.

One way of dealing with these issues would be to include the rules concerning prudential regulation of banks in primary legislation. In my view, however, this would be inappropriate for the majority of prudential rules for a variety of reasons including that: the subject matter calls for the technical expertise of a subject matter expert; a legislative regime would be less adaptable (an issue of particular importance in financial markets); and if rules were included in primary legislation, prudential regulation may become a more partisan political issue.

In determining the appropriate regime, I consider that there is a broad choice between:

- Keeping a flexible scope, but oversight through Parliament (through scrutiny by the Regulations Review Committee) or the Courts (merits review).
- Reducing the flexibility (that is, have a more tightly defined scope of regulation) but without being subject to direct Parliamentary or judicial oversight (although with the possibility of Government Policy Statements).

There are pros and cons associated with each option. Ultimately, the need for technical expertise and also for certainty/finality led me to favour option #2. But I also recommend including process protection around the development of the Banking Supervision Handbook and having a Government Policy Statement as the *quid pro quo* for giving significant power to an independent regulator.

Recommendation #1: Retain conditions of registration and give statutory recognition to the Banking Supervision Handbook

In terms of the basic regulatory "architecture", I consider that there should be a common core set of requirements contained in the Banking Supervision Handbook (or equivalent) and that the conditions of registration should continue as the means of imposing those requirements on a particular bank.

I consider that the common prudential requirements should be contained in the Banking Supervision Handbook rather than implemented by way of legislation to ensure that the regime is adaptable and politically neutral.

Although it might be possible to remove the concept of conditions of registration (that is, the Banking Supervision Handbook could apply automatically to all registered banks, subject to any exemptions to deal with issues of tailoring), I see advantages for retaining the conditions. Conditions allow for flexibility, especially to deal with transitional arrangements or matters that are unique to a particular bank. However, in order to ensure transparency I recommend that:

- The Reserve Bank maintain a public register of all conditions of registrations.
- The register should clearly identify situations where bespoke conditions (ie conditions other than those contained in the Banking Supervision Handbook) have been imposed on banks or the conditions in the Handbook have been overridden.
- The Reserve Bank give publicly available reasons for its decisions to impose bespoke conditions on banks or to override conditions in the Handbook.

If the Banking Supervision Handbook is given statutory recognition and conditions of registration remain, that raises the question of the Banking Supervision Handbook's status. In particular, should it be a disallowable instrument? As discussed below, I recommend that the legislation deem the Banking Supervision Handbook not to be a disallowable instrument and to make it clear that it can be overridden by conditions (on the later point, see recommendation #6 below).

Recommendation #2: The prudential requirements should be drafted and made by RBNZ

The prudential requirements are highly technical and in my view should be prepared by the Reserve Bank rather than by Parliamentary Counsel's Office.

For similar reasons, subject to the restriction set out in recommendation #9, I consider that the prudential requirements should be made by the Reserve Bank, rather than by a Ministerial decision or by the Governor General through an Order in Council.

I also recommend that the governing legislation require the prudential requirements to be made publicly available. To make the requirements accessible, the Banking Supervision Handbook should be published in the "Other Instruments" section of the New Zealand Legislation website as well as on the RBNZ's website.

I note the Productivity Commission's suggestion that it is anomalous that the FMA has many regulatory requirements determined through regulations made by Governor-General in Council, while the Reserve Bank is able to determine regulatory requirements of a similar significance administratively without requiring approval from ministers or Cabinet.[86] However, in my view the technical nature of prudential requirements, the need for frequent updating and the importance of high degree of certainty as to their legal effectiveness justify a different approach for the core set of requirements.

---

[86] New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 223–224.

In order to ensure that prudential requirements meet best drafting practice and for the purposes of quality improvement, I also recommend that:

- The Reserve Bank is formally required to consult with Parliamentary Counsel's Office in relation to drafting matters when it prepares the Banking Supervision Handbook; and
- When drafting the Banking Supervision Handbook, the Reserve Bank look at Commerce Commission input methodology determinations and the Electricity Industry Participation Code as useful comparators.

Recommendation #3: Oversight by way of judicial review, rather than RRC or appeals

The Banking Supervision Handbook could be subject to Regulations Review Committee scrutiny like the standards under the IPS Act. However, in my view the need for finality and the subject matter expertise of the Reserve Bank mean that the Handbook should not be classified as a legislative instrument or a disallowable instrument.[87] Similarly, I do not consider that any special appeal rights should be created in relation to the setting of the core prudential requirements.

While this approach may be criticised as giving insufficient weight to the values of democratic accountability and error correction, I note the following recommendations at least partly address this issue by proposing:

- a more tightly prescribed regulatory perimeter (recommendation #9);
- the Government should be able to issue a Government Policy Statement that the Reserve Bank is required to have regard to in setting and updating the Banking Supervision Handbook.

This approach would leave only judicial review as a formal means of challenging the requirements. I am conscious of criticisms of the efficacy of judicial review and the view that "the house always wins" because success in review almost always involves the matter being remitted back to the decision-maker. This leaves an applicant vulnerable to the possibility that the decision-maker corrects a procedural deficiency but reaches the same substantive outcome.

I also note the comment from a financial institute to the Productivity Commission that judicial review of the Reserve Bank would be a "nuclear option".[88] However, as the Commission also noted, judicial review is employed more widely in other regulatory fields. For instance, firms regularly challenge Commerce Commission decisions.[89] It would seem that if banks want to establish clear ground rules, they may need to change their thinking about judicial review.

---

87 See s 52W(4) of the Commerce Act 1986 which provides that: "A published input methodology is neither a legislative instrument nor a disallowable instrument for the purposes of the Legislation Act 2012".

88 New Zealand Productivity Commission *Regulatory Institutions and Practices* (June 2014) at 308.

89 Ibid.

Recommendation #4: Changes should require public consultation and the process should be set out in the Act

Because there is no statutory recognition of the Banking Supervision Handbook, there are no process rules or consultation requirements around making changes to the Handbook. However, the present practices of the Reserve Bank (in particular, the incorporation of parts of the Banking Supervision Handbook as at a particular date through conditions of registration) result in consultation obligations applying.

In my view consultation obligations should exist as a statutory right, rather than as a matter of practice. Exceptions may be appropriate for trivial changes and a special process for urgent situations.

If there are robust process requirements around changes to the Banking Supervision Handbook then, in my view, it would be appropriate for the conditions of registration to refer to requirements in the Handbook as amended from time to time.

5.3 Should there be additional process requirements for policy-heavy rules?

Introduction

To the extent that "policy-heavy" rules (that is, rules that go beyond the conventional requirements of capital adequacy, liquidity, governance, fit and proper persons and exposure limits and have greater than usual distributional consequences for individual households and firms) are treated separately in the current regulatory framework, that is done by way of the MOU between the Reserve Bank and the Minister of Finance. Sections 9(2)(d), 9(2)(g)(i) and 9(2)(h)

Sections 9(2)(d), 9(2)(g)(i) and 9(2)(h) the scope of the tools falling within the MOU is also unclear. I understand that the Reserve Bank's view is that the MOU's scope is limited to instruments of macro-prudential policy that are designed to provide additional buffers to the financial system (eg through changes in capital, lending and liquidity requirements) that *vary with the macro-credit cycle*.

The Reserve Bank is currently in the process of consulting about the prospect of including debt to income ratio (DTI) limits in the Reserve Bank's macro prudential toolkit. As part of that consultation, the Reserve Bank has stated that the result of the MOU is that "cyclical DTI limits will only be possible in the future if an amended MoU is agreed".[90] Non-cyclical DTI limits would not fall within the MOU.

Recommendation #5: The Government should be able to issue a Government Policy Statement that the Reserve Bank is required to have regard to in setting and updating the Banking Supervision Handbook

The recent experience with macro-prudential requirements shows that there are some requirements that can significantly impact on consumer life choices (for example, the ability to borrow and house prices) that ought to have input from elected representatives.

While the MOU appears motivated by this concern, it is potentially problematic in that it provides for Ministerial input in a way not envisaged by the RBNZ Act.

---

[90] Reserve Bank *Consultation Paper: Serviceability Restrictions as a Potential Macroprudential Tool in New Zealand* (June 2017) at 2.

I have considered whether it is possible to isolate certain types of prudential requirements that could be subject to their own separate approval process with Ministerial involvement and/or decision rights. This approach risks creating uncertainty as to the mechanism that should be used to set a particular requirement which could give rise to a vires challenge that a particular requirement was approved through the wrong channel. Hence my recommendation to de-lineate the channel used to set requirements is limited to that set out in recommendation #9.

Accordingly, my preferred approach is for the Government to be able to issue a Government Policy Statement that the Reserve Bank is required to have regard to in setting and updating the Banking Supervision Handbook.[91] This would apply in relation to all requirements, however, the obligation on the Reserve Bank would be to "have regard" to the Statement and it would not be a direction.[92]

I note that at present s 68B of the RBNZ Act provides that the Minister may "direct the Reserve Bank to have regard to a government policy that relates to the Bank's functions" under Part 5 (registration of banks and prudential supervision of registered banks), Part 5B (oversight of payment systems) and Part 5C (designated settlement systems).[93] I note that this section has some differences to the similar provision in the Commerce Act (s 26).[94] In particular:

- Section 68B contemplates the Minister giving the Reserve Bank a particular direction that it should have regard to "a government policy". By contrast, s 26 of the Commerce Act requires the Commission to have regard to the government's economic policies as transmitted in writing from time to time. In other words, the Commission is under a standing obligation to consider the Government Policy Statement whereas the Reserve Bank must be specifically directed to do so.
- Section 68B only applies to the "functions" of the bank. By contrast, s 26 of the Commerce Act applies more generally to the exercise of its powers under the Act.

It is my intention that allowing for a Government Policy Statement like that provided for in s 26 of the Commerce Act would make the mechanism more effective than the existing power in s 68B of the RBNZ Act.

---

[91] Note that there are a number of different options regarding the transmittal of Government policy, including by notice in the Gazette, tabling in Parliament, or signed off through an Order in Council.

[92] See s 26 of the Commerce Act 1986 which provides that" "In the exercise of its powers under this Act, the Commission shall have regard to the economic policies of the Government as transmitted in writing from time to time to the Commission by the Minister."

[93] I understand that the scope of s 68B has been subject to debate and the section has been seen, at least in some quarters, as being significantly narrower than s 26 of the Commerce Act. In particular, it appears that the reference to "functions" has constrained the sections use in practice. The fact that the Minister and the Reserve Bank entered into the MOU tends to suggest that the government took the view that it could not give the Reserve Bank a GPS in equivalent terms under s 68.

[94] Section 104 of the Crown Entities Act 2004 closely follows the language of s 68 of the RBNZ Act.

In order to promote transparency and accountability, I also recommend that the Reserve Bank is under an obligation to include within its statement of intent an explanation for how it has had regard to the Government Policy Statement.[95]

5.4 What should the process be for tailoring, exemptions and ongoing approvals?

Recommendation #6: The Reserve Bank should have an express power to grant exemptions or otherwise modify the application of the standard prudential requirements to a particular bank and to maintain an ongoing administrative decision-making function

I recommend that the Reserve Bank should:

- have an express power to grant exemptions or otherwise modify the application of the standard prudential requirements (contained in the Banking Supervision Handbook) to a particular bank,[96] including at the request of the bank; and
- maintain its ongoing ability to make administrative decisions.

I consider that these functions are important to allow the standard prudential requirements to be modified to the circumstances of a particular bank, and to having clarity as to how the requirements apply in particular circumstances.

Allowing the Reserve Bank the power to grant exemptions from the Banking Supervision Handbook could be seen as giving rise to Henry VII issues. Henry VIII issues arise where Parliament allows delegated legislation to override primary legislation.[97] However, that is not proposed here as I propose that the standard prudential requirements (in the Banking Supervision Handbook) would themselves be contained in delegated legislation. In my view, all that is required is legislative clarity as to the intended powers and no problematic points of administrative law principles arise.

The power to grant exemptions and the like should be subject to safeguards. In particular, the Act should:

- Provide that the power to grant exemptions or variations must be exercised consistently with the purposes of the RBNZ Act and the framework contained in the Banking Supervision Handbook.[98]
- Set out the criteria to be applied by the Reserve Bank in determining whether to grant an exemption or variation.[99] The criteria should provide a threshold that ensures exemptions do not become so numerous that the accessibility of the law is impaired.[100]

---

[95] See Reserve Bank of New Zealand Act 1989, s 162B(1)(da).
[96] New legislation would specify the functions of exemptions and conditions. I envisage that the same process requirements would apply to both.
[97] *Legislative Advisory Committee Guidelines* (2014) at [13.5].
[98] Ibid at [14.2].
[99] Ibid.
[100] Ibid at [14.1].

- Require the Reserve Bank to give reasons for its decision to grant or decline to grant an exemption or variation and that these reasons be published on the Reserve Bank's website.[101]
- Provide that exemptions are subject to an expiry date to ensure regular review of the exemption unless, exceptionally, the nature of the exemption is such that it should be granted permanently.[102]
- Expressly preserve the right to seek judicial review.

I recommend that the Act also provide that the exemption instrument is not a disallowable instrument. Instead, the bank should have a right of appeal relating to the exemption (see recommendation #8 below).

Recommendations #7 and #8 proceed on the assumption that the Reserve Bank will continue to customise standard requirements and undertake an ongoing administrative decision-making function, and asks what protections are required in relation to those functions.

Recommendation #7: The Act should set out the process for decision-making around exemptions, other modifications to the standard prudential requirements and ongoing administrative decision-making

The Act should set out the process for decision-making around exemptions and other modifications to the standard prudential requirements and ongoing administrative decision-making. This should include the right to be heard (either on the papers or orally) and an opportunity for the bank/person to respond to any adverse findings.

The precise scope of the requirements is a level of detail that can be worked through in the drafting stage but key issues to be considered include:

- Who decisions are made by – should they be made by a body with some independence (eg a rulings panel)?
- If the power to grant exemptions is given to an officer of the Reserve Bank, the legislation should specify whether that power may be delegated.[103]
- If the decisions are made by a body with some independence, whether the decisions are binding or by way of guidance only.

Recommendation #8: A bank should have the right to appeal a decision relating to an exemption, other modifications to the standard prudential requirements and ongoing administrative decision-making

A bank (or other individual directly affected, eg a director subject to a fit and proper assessment) should have the right to appeal a decision relating to an exemption or other modification of the standard prudential requirements, and as to ongoing approvals/administrative decisions.

Where the Reserve Bank carries out a function that involves a determination in respect of a person's rights, obligation or interests, the Reserve Bank is under an obligation to observe the principles of natural justice.[104] The requirements of natural

---

[101] Ibid at [14.2].
[102] Ibid.
[103] Ibid at [13.5].
[104] New Zealand Bill of Rights Act 1990, s 27(1).

justice vary with the circumstances. In short, the Reserve Bank is required to act fairly. The basic requirements are that Reserve Bank must give the bank/person an opportunity to be heard and must be disinterested and unbiased. It is also likely to require the Reserve Bank to put the case (and relevant information and documents) against the bank/person to it so that it has an opportunity to answer it. In some cases, it may also require the Reserve Bank to give reasons for its decision.

One example of an administrative decision-making function is the decision whether a person is a fit and proper person to be a director of senior manager of a bank. Under the RBNZ Act, this is a factor that the Reserve Bank must have regard to in determining whether a bank should be registered.[105] The RBNZ Act, however, does not provide a process for assessing this issue or any appeal rights. By contrast, under the IPSA the Reserve Bank's decision that a director or officer of a licensed insurer is not a fit and proper person may be appealed to the High Court and then, on a question of law, to the Court of Appeal.[106] Although the fit and proper regime under IPSA takes place in a different regulatory context, the treatment of appeal rights in that Act provides a useful point of reference particularly given that under both regimes decisions about whether a person can or cannot be a director have a significant impact on individual freedoms.

I note that the present notice of non-objection process risks vesting undue discretion in the Reserve Bank as being both the maker and the interpreter of rules. That is, if a bank disagrees with the Reserve Bank's interpretation of the prudential requirements in relation to a matter requiring the Reserve Bank's approval, it will not be able to act on its view as the Reserve Bank would not provide a notice of non-objection. The bank's only recourse would be in seeking judicial review. In my view, a broader appeal right is a more appropriate check and balance.

While there may be some matters which are not appropriate for appeal rights, my starting presumption would be to make all decisions affecting individual banks (or individual people within a bank) subject to a right of appeal to the courts.

5.5 How should the regulatory perimeter be set and how should it evolve over time?

Recommendation #9: The Act should set out a core set of areas for prudential regulation, but new areas would require regulation by Governor General in Council

As discussed above, in my view it is appropriate for the Reserve Bank to maintain a high degree of autonomy in setting requirements in relation to prudential mattes specified by Parliament, but that Ministerial and/or Parliamentary oversight should be required in relation to matters not specifically referred to in the Act.

This recommendation would see the framework contained in s 78 of the RBNZ Act amended to clarify that the matters subject to prudential requirements at a particular point in time were to be strictly interpreted. This could be achieved by: refreshing the specific categories of prudential regulation that are within the initial regulatory permitter; specifying that these categories are to be strictly construed; and providing a power to supplement the list by adding new categories over time (for example by Order in Council).

---

[105] Reserve Bank of New Zealand Act 1989, s 73(2)(e).
[106] Insurance (Prudential Supervision) Act 2010, ss 42 and 43.

While this might be seen as creating a vires risk if it was unclear whether a proposed requirement came within the statutory list, the risk would be removed by the ability to add a new matter to avoid doubt.

5.6 Disclosure

Recommendation #10: The Act should impose new disclosure requirements on the Reserve Bank so that the prudential requirements applying to a particular bank are as accessible and transparent as possible

As set out in section 3.8 of this report, there are a number of aspects in which the accessibility of prudential requirements could be improved. While these could be dealt with by the Reserve Bank changing its practices, I would recommend that they are also spelt on in legislation. In particular, I recommend that:

- The Reserve Bank should be required to maintain a central registry of the particular conditions that have been imposed on a particular bank.
- The Reserve Bank should be required to give reasons for and publish its decisions in relation to conditions, exemptions and ongoing approvals.