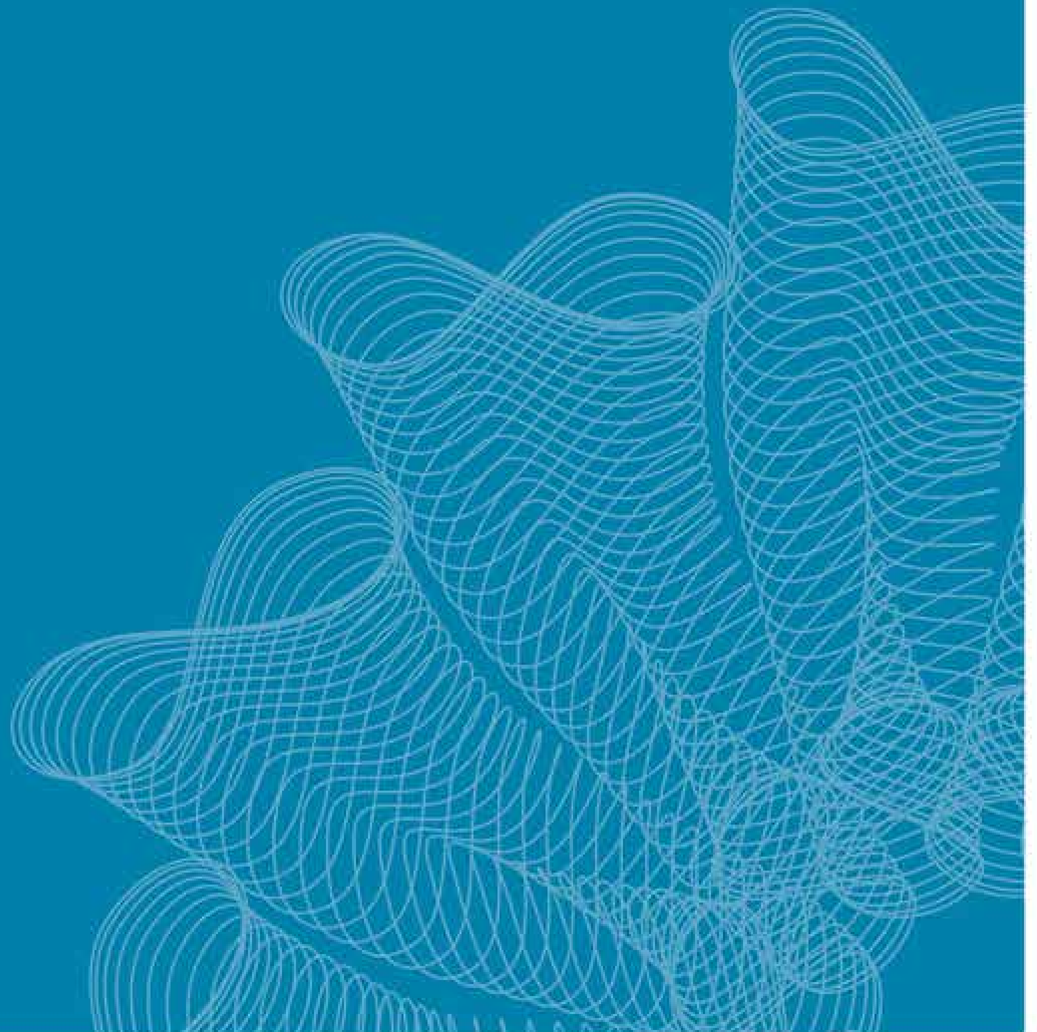
Safeguarding the future of our financial system

Glossary Document

Consultation 2

Phase 2 of the Reserve Bank Act Review

June 2019



Glossary

Abbreviations, acronyms and key terms

ACC – Accident Compensation Corporation. A Crown entity that provides personal injury compensation.

ACE – an autonomous Crown entity as defined by the Crown Entities Act 2004.

Activities-based regulation – regulation of entities based on the fact that they undertake certain activities, such as taking deposits.

Actuarial gains/losses – actuarial valuations resulting in gains or losses. Valuations change over time. Key valuation assumptions include price inflation, earnings growth, employee retirement dates and investment returns.

ADI – authorised deposit-taking institution. An institution authorised by Australia's prudential regulator, APRA, to carry on banking business, such as a bank, credit union, or building society.

Administrative instrument – an instrument that allows for the implementation, within the legal framework, of the actions or decisions of a regulatory body.

Agent – a party acting on behalf of someone else (the 'principal'). The Reserve Bank's Board is currently the monitoring agent for the Reserve Bank, acting on behalf of the Minister of Finance.

AML/CFT – anti-money laundering and countering financing of terrorism.

Annual report (as used in this document) – a statutory accountability document in which an agency reports on its operations and financial performance during the last year.

APRA – Australian Prudential Regulation Authority. The prudential regulator of the Australian financial services industry.

Arbitrage – a situation where market inefficiency creates differences in the costs of similar products, allowing providers to benefit from the inefficiency. Regulatory arbitrage is where regulated entities structure themselves to minimise their regulatory compliance costs.

ASIC – Australian Securities and Investments Commission.

Asset – a resource controlled by a person or enterprise (an 'investor') from which future economic benefits are expected to flow to the investor. Cash, bank deposits, and KiwiSaver funds are common 'assets' held by New Zealanders. An instrument held as an asset by an investor is a 'liability' for the institution that has issued the instrument. For example, cash held by New Zealanders is an asset to them but is a liability of the Reserve Bank, while bank deposits are assets for the deposit holders but liabilities of the banks holding the deposits.

Auditor-General inquiry – under section 18 of the Public Audit Act 2001, the Controller and Auditor-General is able to "inquire, either on request or on their own initiative, into any matter concerning a public entities use of its resources".

Auditor-General performance audit – under section 16 of the Public Audit Act 2001, the Controller and Auditor-General examines "the extent to which a public entity is carrying out its activities effectively and efficiently".

Bail-in – restructuring mechanisms that enable loss absorption and the recapitalisation of a bank in resolution or the effective capitalisation of a bridge institution through the cancellation, write-down or termination of equity, debt instruments, and other senior or subordinated unsecured liabilities of the bank in resolution, and the conversion or exchange of all or part of such instruments or liabilities into or for equity in or other instruments issued by that bank, a successor (including a bridge institution) or a parent company of that bank.

Bail-out – any transfer of funds from public sources to a failed bank or a commitment by a public authority with a view to sustaining a failed bank (for example, by way of guarantees) that results in benefit to the shareholders or uninsured creditors of that bank, or the assumption of risks by the public authority that would otherwise be borne by the firm itself, where the value of the funds transferred is not recouped from the bank, its shareholders and creditors or, if necessary, the financial system more widely, or where the public authority is not fully compensated for the risks assumed.

Basel Committee on Banking Supervision (BCBS) – the primary global standard setter for the prudential regulation of banks, and a forum for regular cooperation on banking supervisory matters. It has 45 members comprising central banks and bank supervisors from 28 jurisdictions. New Zealand is not one of these jurisdictions. The BCBS produces the BCPs.

Basel III – the international standard for capital requirements.

BCPs – Basel Core Principles for effective banking supervision. BCPs are used by the IMF in their Financial Sector Assessment Programmes. The BCPs were first issued in 1997, and last updated in 2012 to reflect lessons from the GFC.

Beneficiary theory – a theory based on the principle that those who benefit from a good or service should bear the cost of providing it. The beneficiary theory requires the regulator to consider whether the goods or services it provides are public, private, club, or merit and to apportion user charges on the basis of these characteristics. Public goods should typically be funded wholly from taxation, club goods and private goods from the goods' users or beneficiaries, and merit goods potentially through a mixture of both public and private sources.

BIS – Bank for International Settlements. An international financial institution owned by central banks that "fosters international monetary and financial cooperation and serves as a bank for central banks".

BoE – Bank of England.

Bridge bank – an entity created by authorities to operate a failed bank until a buyer can be found for its operations.

BRRD – European Bank Recovery and Resolution Directive (Directive 2014/59/EU).

Budgetary independence – funding arrangements that protect the regulator from external pressure (Productivity Commission, 2014).

CA – a Crown agent as defined by the Crown Entities Act 2004.

Capital – in the banking context, capital refers to the type of funding that a bank uses to finance its assets. 'Common Equity Tier 1' capital primarily includes ordinary shares and retained earnings. 'Additional Tier 1' capital includes preference shares. 'Tier 2' capital consists mainly of long-dated subordinated debt. Capital is not cash reserves or money set aside for an emergency.

Capital ratio – an amount of capital (expressed as a ratio of capital to exposures/investments) that regulated entities must hold in order to protect against losses on those exposures/investments.

CDGS – Crown Retail Deposit Guarantee Scheme. An emergency measure to support the financial sector implemented by the New Zealand Government during the GFC. The CDGS was put in place in October 2008 and ended in December 2011. At its peak the scheme covered 96 institutions, including 12 banks, 60 NBDSs, and 24 investment firms. The Government paid out $2 billion to 42,000 depositors under the scheme. The largest single pay-out was for South Canterbury Finance ($1.6 billion), one of nine failures under the scheme.

CEO – Chief Executive Officer. The highest-ranking senior manager in a company or other institution, acting as a point of communication between the board and corporate operations. The Governor is the CEO of the Reserve Bank.

CIMA – Corporations (Investigation and Management) Act 1989.

Closed bank resolution – the resolution of a failed bank in a manner that does not keep the bank operating as a going concern. Parts of the bank may be transferred to another owner with other parts passed to another type of management vehicle or liquidated. Compare with 'open bank resolution'.

CMDT – Capital Market Development Taskforce. An industry-led taskforce appointed by the Government in 2008 to investigate issues with New Zealand capital markets. It was commissioned following the Review of Financial Products and Providers (RFPP).

CoFR – Council of Financial Regulators. An information-sharing body for New Zealand's main financial regulatory agencies (the Reserve Bank, the Treasury, the Ministry of Business, Innovation and Employment, and the Financial Markets Authority).

Collateral – an asset or commitment that is used by a borrower (a collateral provider) to secure a loan.

Conditions of registration – a set of criteria that banks registered in New Zealand must meet in order refer to themselves as banks. A registered bank's conditions of registration are controlled by the Reserve Bank, and are the primary way that prudential requirements are applied. They are designed to promote banking system stability by constraining, but not completely removing, banking risk in certain key areas.

Contagion – a situation where difficulties facing one participant in the financial system spread to other participants.

Countercyclical capital buffer (CCYB) – a macro-prudential tool imposed by a regulator, which requires banks to maintain higher levels of capital (or face limits on their ability to pay dividends).

Covered bond – a bond where the holder's right to payment is secured by specific assets, known as 'collateral'.

Creditor – someone who has lent money to a firm, which the firm has undertaken to repay. For example, a depositor is a creditor of a bank. In contrast, a shareholder is an owner of a bank.

Creditor hierarchy – the order in which creditors or classes of creditors are paid out in a liquidation.

Creditor property rights –

- in relation to a debt and a creditor prior to liquidation, the right to be repaid on time without deduction and without being subordinated to another competing claim of equal rank.
- in relation to a debt and a creditor during the course of a liquidation, the right to share in the proceeds of the liquidation in accordance with the rules set by the applicable insolvency laws.

Crisis management – a process by which authorities deal with an unexpected and disruptive event (or the risk of a disruptive event) that threatens the stability of the financial system (e.g. the failure of a major bank).

Crown (the) – the meaning of 'the Crown' varies according to the context in which it is used. Generally, it describes executive government conducted by Ministers and their departments. It does not normally include organisations that have their own corporate identities, such as state-owned enterprises. The Reserve Bank is not part of the Crown.

Crown entity – where referred to in this document, means a Crown-owned organisation, a legal entity in its own right that has been established under legislation as "statutory entity" and is subject to the Crown Entities Act 2004. Crown entities perform functions on behalf of government at varying degrees of independence from government.

De minimis (as used in this document) – an optional function that could protect small bank deposits under OBR.

Debt instrument/security – a bond or other form of liability creating a contractual obligation on the issuing institution that the bond must be repaid. These instruments are traded in debt markets.

Debt security – a right to be repaid money or paid interest on money that is lent or deposited with a person. Examples include deposits, debentures, or bonds.

Debt-to-income limits (DTI) – limits on loans relative to borrower income. May be part of a lender's risk management policies, or imposed by a regulator as part of macro-prudential policy.

Delegated legislation – rules made under an empowering provision in primary legislation that create, alter or remove rights or obligations of all, or a class, of the public. For the purposes of this consultation document, the term 'delegated legislation' captures both 'legislative instruments' and 'disallowable instruments' under the Legislation Act 2012.

Democratic legitimacy – public support for, belief in, and understanding of an institution's powers and processes, which should reflect and support the will of the people.

Deposit taker – a financial institution that takes deposits, such as a bank or NBDT. Deposit takers are commercial entities that act as interfaces between lenders and borrowers, for example by collecting deposits from the general public and extending loans to households and businesses.

Depositor – someone who has money in a deposit account with a bank or NBDT, either because they have placed funds in that account or from temporary situations deriving from normal banking transactions. This person becomes a creditor to the institution holding their deposit, and the institution is contractually required to repay them.

Director attestation regime – the way the Reserve Bank underpins self-discipline by placing responsibility for prudent outcomes with directors of registered banks. Directors attest in public disclosure statements that their bank is adequately managing risks, and whether the bank has complied with its conditions of registration.

Disallowable instrument – delegated legislation that must be presented to Parliament and can be disallowed by Parliament.

DNB – the Dutch National Bank, the central bank of the Netherlands.

Economic cycle – fluctuations in the economy. An economy may be in a boom, or in a downturn also known as a 'recession'. A severe downturn is a 'depression'.

Emergency demand management planning – emergency demand management planning refers to how the Reserve Bank and the Treasury may plan to coordinate to stimulate demand in the economy when there has been a crisis, and there is a highly constrained ability for monetary policy to be used to stimulate demand. In such a scenario, the Treasury may use fiscal policy to stimulate demand.

Enforcement – corrective action undertaken by a prudential authority to address financial institutions' non-compliance with regulatory requirements, or to address any emerging areas of concern (before formal non-compliance). Tools include formal powers such as court-based action, as

well as the use of various supervisory actions such as persuasion, more supervisory oversight, or changing license conditions.

EQC – Earthquake Commission. A Crown entity that compensates for natural disaster damage to residential land and buildings.

ESRB – European Systemic Risk Board.

Externality – a consequence of an industrial or commercial activity which affects other parties without this being reflected in market prices, because it does not directly affect the producer/seller.

Externality theory – a theory that externalities should be internalised. For example, that the entities that produce negative externalities (such as systemic risk in the case of financial institutions) should bear the costs of mitigating them.

Failing bank – a bank (or financial institution) that is, or is likely to become, unviable. For example, a bank may be unviable because it is unable to honour its debts and liabilities, or because it is in breach of its conditions of registration.

FCA – Financial Conduct Authority (UK).

FCIC – Financial Crisis Inquiry Commission (US).

Fee – a charge imposed on a specified party in return for the provision of a good or service, which directly benefits that party (e.g. a bank registration fee).

Finance and Expenditure Committee (FEC) – a select committee of Parliament that examines business related to economic and fiscal policy, taxation, revenue, banking and finance, superannuation, insurance, government expenditure and financial performance, and public audit.

Financial cycle – the process where financial markets fluctuate from upturns/booms to downturns/disruptions over time. The financial cycle can affect real economic activity (and the economic cycle).

Financial market – a generic term for markets in which financial instruments are issued, invested, and traded, and where those who have a surplus of funds lend to those who have a shortage. The four main financial markets trade in foreign exchange, debt or bonds, shares or equities, and derivatives. These can be broken down into subsets – for example, the 'money market' is a market for short-term debt using instruments that generally have a maturity of up to one year.

Financial policy – the approach, decisions, choices, and rules related to the regulation, supervision, and oversight of the financial system. Financial policy seeks to achieve various outcomes for the financial system, including financial stability, efficiency, and the protection of consumers. Note that in the case of the Reserve Bank, financial policy includes prudential supervision policy, macro-prudential policy, and crisis management policy.

Financial regulation – the laws and rules that govern what various participants in the financial system can and cannot do. Regulation is necessary because of the existence of various market failures that prevent the financial system achieving socially optimal outcomes on its own. Regulation seeks to achieve various outcomes outlined in policy. These outcomes for the financial system may include financial stability, efficiency, and the protection of consumers.

Financial safety net – a set of five distinct but mutually supportive regulatory tools and powers that help keep banks safe and sound. The financial safety net comprises regulations, prudential supervision and monitoring, system liquidity support, deposit protection, and resolution.

Financial sector – the collective class of financial system participants (e.g. banks and insurers).

Financial system – the network of participants in an economy that collectively undertake various finance-related functions and activities. A financial system includes financial institutions (such as deposit takers and insurers), markets, market infrastructures, and the everyday people who use them. Financial systems operate at various geographical levels: regional, national, and global.

FinTech – technology-enabled innovation in financial services that could result in new business models, applications, processes, or products with associated material effect on provision of financial services.

FMA – Financial Markets Authority. The New Zealand government agency responsible for promoting fair, efficient, and transparent financial markets by enforcing securities, financial reporting, and company law as they apply to financial services and securities markets. The FMA also regulates securities exchanges, financial advisers and brokers, auditors, trustees, and issuers, including issuers of KiwiSaver and superannuation schemes.

FMI – Financial Market Infrastructure. A channel through which financial transactions are cleared, settled, and recorded, including payment systems and trading platforms. FMIs are the 'plumbing' of the financial system, providing services critical to the smooth functioning of financial markets.

FMS – Financial Markets Supervisor. A private sector company that supervises licensed non-bank deposit takers. FMSs are licensed by the FMA.

FPC – Financial Policy Committee. An option considered in this Review for the governance arrangements for financial policy.

FSA – Financial Services Authority. The agency that regulated financial services in the UK between 2001 and 2013. The FSA was split in 2013 into the Financial Conduct Authority and the Prudential Regulation Authority of the Bank of England.

FSAP – Financial Sector Assessment Programme. An IMF programme that seeks to identify the strengths and vulnerabilities of countries' financial systems (including regulatory frameworks, which it assesses against various international standards, including those for banks, insurers, FMIs and securities markets. It also seeks to determine how key sources of risk are being managed. The most recent FSAP mission to New Zealand was in 2016/17.

FSB – Financial Stability Board. An international body with membership comprising the G20 countries (New Zealand is not a member). It has a mandate to assess the vulnerabilities affecting the financial system, identify and oversee action to address them, and promote cooperation and information sharing among authorities responsible for financial stability.

FSR – Financial Stability Report. A six-monthly Reserve Bank report required by legislation reporting on the soundness and efficiency of the financial system and containing the information necessary to enable an assessment of the Reserve Bank's activities in pursuing its prudential purposes.

G20 – Group of Twenty. An international forum for the governments and central bank governors from 19 countries and the European Union. New Zealand is not a member of the G20.

GDP – Gross Domestic Product. A measure of the value of economic production in the economy.

Global financial crisis (GFC) – the GFC occurred between mid-2007 and early 2009 and was a period of extreme and widespread stress in global financial markets and banking systems. The GFC was an example of systemic risks crystallising and damaging the financial system and wider economy.

Governance – the system by which an organisation is controlled and operates, and the mechanisms by which it, and its people, are held to account. Governance captures who makes policy and regulatory decisions, who makes organisational decisions, and how decision-makers are held to account.

ICE – An independent Crown entity as defined by the Crown Entities Act 2004.

IMF – International Monetary Fund. An international organisation of 189 member countries established to ensure the stability of the international monetary system. Its remit includes the system of exchange rates and international payments, as well as all macro-economic and financial sector issues that affect global stability.

INC – Independent Nominating Committee. A nominating committee appointed by the Minister. The committee would nominate candidates to the Minister, who would make appointments after consulting with other political parties. This is a model similar to the Guardians of the New Zealand Superannuation Fund, and was recommended by stakeholders in Phase 1 of the Review.

Independence – in relation to a public institution such as the Reserve Bank, the provision that ensures the institution can carry out its tasks and duties without political interference.

Independent Expert Advisory Panel – a panel appointed by the Minister of Finance to provide independent and expert advice on the Review of the Reserve Bank Act.

Insolvency – when the value of a firm's assets falls below the value of the liabilities it owes, and the firm is therefore unable to pay its debts. An insolvent firm is a 'failing' firm.

International Association of Deposit Insurers (IADI) – a forum of 83 deposit insurance scheme managers that was formed in 2002 to share knowledge and promote international cooperation on

deposit insurance systems. IADI works with the BCBS to develop guiding principles for effective deposit insurance systems.

Investor – someone who has invested their money in a financial institution. Anybody providing funds to a financial institution in whatever form is an investor, from shareholders to depositors to professional investors in more sophisticated debt instruments.

IOD – New Zealand Institute of Directors.

IPSA – Insurance (Prudential Supervision) Act 2010.

Issuer – an entity that issues, and therefore becomes obligated for, a security or other financial instrument. For example, a bank that writes a debt in exchange for funding is the 'issuer' of that debt.

Key Attributes – the FSB's 'Key Attributes of Effective Resolution Regimes for Financial Institutions', a set of 12 attributes developed by the FSB and endorsed by the OECD as an international standard for bank resolution regimes.

LDAC – Legislation Design and Advisory Committee.

Lending standards – rules banks use when deciding whether to lend to a prospective borrower. May include limits on loans relative to collateral (such as loan-to-value or LVR limits) or borrower income (such as debt to income or DTI limits). May be influenced by regulation.

Leverage – a measure of indebtedness relative to asset holdings. Assets can be purchased through equity or through borrowed funds, or a combination of both. A person who takes out a mortgage to buy a house is 'leveraged'. An excessive build-up of leverage among banks and households was seen as one of the causes of the GFC.

Levy – a charge imposed on a particular party or group, as a proxy for those that benefit from a specific good or service or regulation.

Liability – a debt or legal obligation to be repaid, by either cash or another type of financial instrument. Examples include customer deposits held by banks, and bonds and other debt securities issued by banks. As previously noted, one entity's asset is another entity's liability.

Liquidation – the process of closing a firm where the assets are sold (realised) and the proceeds allocated to creditors and shareholders in accordance with the hierarchy of claims.

Liquidity – the capacity to sell an asset quickly and easily without significantly affecting the price of that asset. 'Liquidity' is also sometimes used to refer to assets that are highly liquid.

LoLR – Lender of Last Resort. The central bank acting in its function to provide emergency liquidity assistance to a solvent financial institution facing temporary liquidity problems in order to maintain the soundness of the financial system.

LVR – Loan to Value Ratio. A tool used by financial sector regulators to influence lenders' credit policies and the availability of loans to borrowers, by specifying the proportion of an asset's value that may be financed through borrowing.

Machinery of government – includes the set of organisations within government, their functions and governance arrangements, and how they work together to deliver results for Ministers and the public.

Macro-prudential policy – the use of prudential tools (such as capital buffers and loan-to-value restrictions) to manage the system-wide (systemic) risks that can develop during boom-bust financial cycles. Macro-prudential policy aims to promote greater financial system stability by building additional resilience in the financial system during periods of rapid credit growth and rising leverage or abundant liquidity, and by dampening excessive growth in credit and asset prices. In New Zealand, macro-prudential policy is used to address systemic risks as they change over time (across the financial cycle). Systemic risks arising at a point in time are managed through 'traditional' prudential policy in New Zealand. However, internationally, macro-prudential policy is often defined as the management of systemic risk both over time and cross-sectionally.

Market discipline – one of the 3 pillars of the Reserve Bank's prudential framework. Refers to the way in which market participants influence a financial institution's behaviour by monitoring its risk profile and financial position.

Market failure – a situation where the allocation of goods and services by a free market is not efficient, and leads to a net social welfare loss. The existence of market failures provides the rationale for the regulation and supervision of the financial system, and its component parts (financial institutions, markets etc.).

MoU – Memorandum of Understanding. A non-binding agreement or expression of common understanding between two or more parties.

Monetary policy – action undertaken by a central bank to affect the cost of money and credit to meet objectives such as price stability or maximising sustainable employment. While monetary policy is generally implemented using a policy interest rate (such as the Official Cash Rate), it can also involve the use of extraordinary measures such as quantitative easing/asset purchasing.

Monetary Policy Statement (MPS) – a formal statement from the Reserve Bank, issued four times a year, setting out how it intends to achieve its monetary policy objectives, how it proposes that monetary policy will be formulated and implemented for the next five years, and a review of its monetary policy in the last quarter.

Monitor – a body that is responsible for monitoring the performance of an entity on behalf of a responsible Minister.

Monopoly power – when a person or enterprise is the only supplier of a particular good or service, and therefore has extraordinary control or power over the market for that good or service. Monopoly power can result in higher profits for the producer, and higher prices for the consumer, than would be the case in a competitive market.

Moral hazard – a situation where one party has an incentive to take risks without taking responsibility or having to bear the consequences to themselves or society. For example, expectations of government bail-out creates moral hazard by encouraging financial institutions to take more risks than they would otherwise.

MPC – Monetary Policy Committee. A committee that is responsible for the formulation of monetary policy in New Zealand. The committee has been established as an outcome of Phase 1 of the Review of the Reserve Bank Act.

Name-based regulation – regulation of entities based on their use of certain restricted words (e.g. 'bank').

NBDT – Non-Bank Deposit Taker. An institution that carries on the business of borrowing and lending money, or providing financial services, or both, but is not a registered bank. Examples of NBDTs are some finance companies, credit unions, and building societies. NBDTs are currently prudentially regulated by the Reserve Bank under the Non-bank Deposit Takers Act 2013. The Reserve Bank does not, however, supervise this sector. Supervision is undertaken by trustees, who are in turn supervised by the FMA.

NBER – National Bureau of Economic Research (US).

NCWO – No Creditor Worse Off than in liquidation. The principle that no creditor should incur greater losses than they would have incurred if an institution had been wound up under normal insolvency proceedings. 'NCWO compensation' is financial compensation to a creditor whose actual incurred losses are greater than what they would have incurred in liquidation.

NDLI – Non-Deposit-taking Lending Institution. An institution that writes loans but is not funded from retail deposits.

Non-zero-failure banking regime – an approach to banking regulation that is used in all advanced economies, including New Zealand, whereby banks are allowed to fail.

Northern Rock – a British bank that suffered a major liquidity crisis during the global financial crisis, causing the Bank of England to provide it with special liquidity assistance which precipitated a retail depositor run, ultimately forcing the government to nationalise the bank to protect taxpayer interests. Northern Rock's retail operations were eventually returned to private ownership when they were acquired by Virgin Group in 2012. The failed bank's mortgage book was subsequently sold to private interests in 2016.

NZClear – a real-time settlement system which provides the financial markets with clearing and settlement services for high-value debt securities and equities.

NZFSA – New Zealand Financial Services Authority. Creating an NZFSA is an option that was introduced in Consultation Document 1 in considering whether prudential regulation should remain with the Reserve Bank. This option will not be progressed.

NZPRA – New Zealand Prudential Regulation Authority. Creating an NZPRA is an option that was introduced in Consultation Document 1 in considering whether prudential regulation should remain with the Reserve Bank. This option will not be progressed.

OBR – Open Bank Resolution. A Reserve Bank policy designed to help manage a bank failure. Open bank resolution more generally is a strategy whereby authorities stabilise and resolve a failed bank in such a way that it is able to continue operating as a going concern, providing continuity of the bank's critical functions and services. Compare with 'closed bank resolution'.

OCR – Official Cash Rate. The OCR is an interest rate set by the Reserve Bank. It influences all other interest rates and is, in effect, the wholesale price of borrowing or lending money in New Zealand. It allows the Reserve Bank to meet its goal of ensuring price stability for New Zealand.

OECD – Organisation for Economic Cooperation and Development. An intergovernmental economic organisation that represents industrial market countries and contributes to the economic development of less-advanced members and non-member countries.

Off-site supervision – set of supervisory activities undertaken by the prudential authority at its premises (also called desk-based monitoring). Typically used to complement on-site supervision. The Reserve Bank relies on off-site supervision to monitor and assess regulatory compliance.

OIA – Official Information Act 1982.

On-site supervision – a set of supervisory activities undertaken by the prudential authority at the premises of financial institutions. Used to obtain independent verification that a financial institution has adequate policies, procedures and controls in place. Also called on-site inspections or examinations. The Reserve Bank does not undertake on-site supervision, instead relying on off-site supervision.

OSFI – Office of the Superintendent of Financial Institutions, Canada's prudential authority.

Parliamentary appropriation – the authority (in the form of an Act) of Parliament to expend public money.

Payment and settlement systems – a type of FMI. Payment and settlement systems support the exchange of payments for products and services. They may be cash payment systems (such as the Reserve Bank's Exchange Settlement Account System) or securities settlement systems.

Phase 1 – the first phase of the Review of the Reserve Bank Act. The outcomes of Phase 1 updated the Reserve Bank's high-level objectives for monetary policy, adding employment to the price stability objective of the Reserve Bank and providing for a committee decision-making model for monetary policy decisions (the MPC).

Phase 2 – the current phase of the Review of the Reserve Bank Act. It is primarily focused on a comprehensive review of the financial policy provisions of the Reserve Bank Act that provide the legislative basis for prudential regulation and supervision, and will also consider the broader

governance arrangements of the Reserve Bank. It will be broken up into three consultations, of which this is the first.

Policy instrument – a policy tool that is available to the regulator to achieve its objective. The Official Cash Rate is a policy tool available to the Reserve Bank to effect monetary policy.

Productive capacity – the maximum output that can be produced in an economy that is working efficiently and without friction.

Prudential regulation – rules that support the prudent operation of financial entities licensed by the prudential authority. In New Zealand, prudential regulation focuses on the soundness and efficiency of the financial system by imposing regulatory requirements at the level of individual institutions. Capital requirements, liquidity requirements, and disclosure requirements are among the prudential requirements currently implemented by the Reserve Bank.

Prudential supervision – a set of activities directed at both individual financial institutions and the wider financial system. Activities include licensing individual entities, collecting and analysing information, assessing compliance against prudential regulatory requirements, and cooperating and coordinating with other domestic and international agencies.

Quantitative easing – expanding the balance sheet of the central bank (often by buying safe assets like Government debt) to provide monetary stimulus (increase the money supply), often once interest rates have already been reduced to near zero.

Real economy – the part of the economy that is concerned with producing goods and services, as opposed to the part of the economy that is concerned with buying and selling on the financial markets.

Recapitalisation – restoration of a firm's depleted financial resources following a significant loss or other type of asset write-down.

Regulated entity – a financial service provider falling within the scope of the Reserve Bank's supervisory and/or regulatory powers. This currently captures registered banks, NBDTs, and insurers.

Regulations Review Committee – a committee of Parliament that applies technical scrutiny to delegated legislation.

Regulator – a body mandated by the Government to oversee a particular industry or sector. The Reserve Bank is the prudential regulator for the financial sector in New Zealand.

Regulatory discipline – one of the 3 pillars of the Reserve Bank's prudential framework. Refers to the role of mandated rules and requirements set by the Reserve Bank to support the soundness of individual financial institutions and the stability of the financial system as a whole. See also: prudential regulation.

Regulatory framework – a system of rules and requirements that govern the way regulators and regulated entities interact. The financial sector regulatory framework is made up of regulatory requirements, guidance, and Memoranda of Understanding.

Regulatory leakage – the shifting of activities to products, markets or entities so that they fall outside the regulatory perimeter.

Related party exposure – an entity's investment in another entity, where the first entity is a parent or subsidiary of the second. For example, investments in a subsidiary or parent company are related party exposures. Also known as 'intragroup exposures'.

Reserve Bank of New Zealand – New Zealand's central bank, established in 1934. The Reserve Bank manages monetary policy to maintain price stability, promotes the maintenance of a sound and efficient financial system, and supplies New Zealand banknotes and coins.

Resolution – the restructuring and/or orderly wind-down of all or part of a deposit taker's business in a way that adequately safeguards the public interest.

Resolution authority – a public authority that, either alone or together with other authorities, is responsible for the resolution of banks established in its jurisdiction (including resolution planning functions).

Resolution fund – financing set up in advance of a crisis so that authorities are not constrained to rely on public ownership or bail-out funds as a means of resolving a failed institution. A deposit insurance scheme can perform the function of a resolution fund, but stand-alone funds can also be established.

Retail depositors – households and small businesses with deposit accounts. Retail depositors are not professional investors or wholesale creditors.

RFPP – Review of Financial Products and Providers. A review carried out between 2005 and 2008, leading to a number of new pieces of legislation, including the Financial Service Providers (Registration and Dispute Resolution) Act 2008, the Reserve Bank of New Zealand Amendment Act 2008, and the Insurance (Prudential Supervision) Act 2010.

Risk pricing – when the amount that investors earn from/borrowers pay for a loan is calculated in relation to the risk that the loan will not be repaid. The return an investor earns on their investment is the 'risk price'. Accurate risk pricing is a key part of the risk management process. Risk mispricing is believed to have caused a build-up of systemic risks that led to the GFC.

Risk-based supervision – the allocation of supervisory resources focusing on the areas of highest risk (typically the largest and most systemically important financial entities). It is supported by an explicit risk identification and assessment methodology.

Securities exchange – a marketplace where financial securities such as stocks and bonds are traded. In New Zealand, securities exchanges – such as the New Zealand Stock Exchange – are regulated by the FMA.

Securitisation vehicle – an instrument for pooling various types of debt instrument, such as mortgages, and selling their related cash flows to third-party investors as tradeable securities.

Seigniorage – revenue that is created through the Reserve Bank's monopoly power to create physical cash. The cost of printing notes and minting coins is much lower than their face value. Commercial banks buy this cash from the Reserve Bank at face value. The Reserve Bank invests the difference in a portfolio of low-risk assets and earns a return known as seigniorage income.

$$Seigniorage = (Face\ value\ of\ currency\ created - Cost\ of\ creating\ currency) \times investment\ return$$

Self-discipline – one of the 3 pillars of the Reserve Bank's prudential framework. Refers to the responsibility of senior management and board directors for an institution's own processes and risk management frameworks.

Shareholder – someone who has invested money in a firm to become a partial owner of that firm.

Single decision-maker – under the Reserve Bank's current governance arrangement, the Governor is the single decision-maker ultimately responsible and accountable for all financial policy decisions. An alternative model may place responsibility with a board.

Social capital – one of the four capitals in the New Zealand Treasury's Living Standards Framework.

SOI – Statement of Intent. A statutory accountability document setting out the strategic objectives that an entity intends to achieve in the future reporting period and other matters intended to promote the public accountability of the entity.

Special bank resolution – the exercise of powers and tools under the legal framework that applies to failing financial institutions by a public resolution authority tasked with preserving financial stability.

State sector – a term used to cover all organisations that report to the Crown. The State sector is separate from local government (city, district, and regional councils).

Statutory management – one of several legal mechanisms available in New Zealand to deal with a failing bank, set out in the Reserve Bank Act.

Statutory manager – an individual appointed by the Governor-General (on the advice of the Minister of Finance in accordance with a recommendation of the Reserve Bank) to run a commercial bank in the interest of the New Zealand public when the bank is failing. The statutory manager has wide powers to deal with the failing bank, such as assuming all powers of the board and management, and exercising many of the powers of a liquidator. The statutory manager may choose to suspend or make payments to creditors, or organise to sell the bank.

System/Regulatory stewardship – the responsibility for ensuring that the legislative and regulatory frameworks within which a regulator (and the sectors it regulates) operates remain fit for purpose.

Systemic risk – the risk that issues at one point in the financial system (perhaps due to operational disruption or a participant's financial difficulties) will cause issues at other points in the system, generating spill-over effects that could threaten the wider operation and stability of the system and have negative consequences for the real economy.

TCFD – Task Force on Climate-Related Financial Disclosures. The TCFD seeks to develop recommendations for voluntary climate-related financial disclosures that are consistent, comparable, reliable, clear, and efficient, and provide decision-useful information to lenders, insurers, and investors. The TCFD's 31 members were chosen by the FSB to include both users and preparers of disclosures from across the G20's constituency covering a broad range of economic sectors and financial markets.

Trans-Tasman Council on Banking Supervision – also known as the Trans-Tasman Banking Council (TTBC); a trans-Tasman forum comprising the New Zealand Treasury, the Reserve Bank of New Zealand, the Financial Markets Authority, the Australian Treasury, the Australian Prudential Regulation Authority, the Reserve Bank of Australia, and the Australian Securities and Investments Commission which meets regularly to support the development of a single economic market in banking services. The TTBC has a particular focus on enhancing cooperation on the supervision of trans-Tasman banks and other financial institutions, promoting and reviewing trans-Tasman banking crisis response preparedness, and guiding the development of policy advice to both governments, underpinned by the principles of policy harmonisation, mutual recognition, and trans-Tasman coordination.

The Treasury – the Minister of Finance's policy department and the Government's lead economic and financial adviser.

Twin peaks – a model of financial regulation where financial market conduct and prudential regulation are separated.

Unsecured credit – funds that have been lent (e.g. to a financial institution or consumer) that are not backed by specific assets. In the event of failure, unsecured creditors will be paid out from a general pool of assets. In contrast, some funding (such as covered bonds) is secured with specific assets.

Unsecured liabilities – a debt or other liability that is not secured by an asset or lien. An unsecured liability carries no collateral. In case of bankruptcy, the creditor of an unsecured liability is considered a general creditor. Bonds (other than 'covered bonds') and deposits are unsecured liabilities.

Wholesale participants – professional (non-retail) financial market players, such as sophisticated investors in capital market instruments and participants in interbank money markets.