The Treasury

Reserve Bank Act Review Phase 2 Second Consultation Information Release

July 2019

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Office of the Minister of Finance

Chair,
Cabinet Economic Development Committee

Phase 2 of the Reserve Bank Act Review – In-principle decisions and the release of the second consultation

Proposal

1. This paper seeks agreement to in-principle decisions for Phase 2 of the Reserve Bank Act Review. It also seeks agreement to the release of the two attached consultation documents (titled 'Safeguarding the future of our financial system' – Documents 2A and 2B), which will form part of the Review's second consultation.

Executive Summary

2. Phase 2 of the Reserve Bank Act Review is considering the Reserve Bank's financial policy framework, which provides the basis for prudential regulation and supervision. It is also reviewing the Reserve Bank's broader governance and accountability arrangements. This second phase follows Phase 1 of the Review, which focused on improving the Reserve Bank's monetary policy framework. Changes from Phase 1 came into force on 1 April 2019.

3. The first consultation document for Phase 2 was released in November 2018 and the consultation closed in late January 2019. It covered topics that are crucial in shaping the Review's overall outcome, including the Reserve Bank's high-level financial policy objectives, governance arrangements and regulatory perimeter, the case for depositor protection in New Zealand, and the case for separating prudential functions from the Reserve Bank.

4. I am seeking Cabinet's endorsement to in-principle decisions taken on these topics, which draw on feedback received during the first consultation. These in-principle decisions were needed to provide clarity on the expected direction of travel for the Review given interdependencies with the remaining topics in the Review's terms of reference, which form part of the second consultation. These in-principle decisions are to:

- retain the prudential regulation and supervision functions within the Reserve Bank
- replace the Reserve Bank's existing 'soundness' and 'efficiency' financial policy objectives with a single over-arching 'financial stability' objective
- establish a new governance board, which is given statutory authority over all Reserve Bank decisions (except for those reserved for the Monetary Policy Committee), including prudential policy decisions
- (in light of the above) not establish a new Financial Policy Committee
- appoint the Treasury as the external monitor of the Reserve Bank
- merge New Zealand's two existing prudential regimes for regulating banks and non-bank deposit takers into a single regime for deposit takers
- establish a depositor insurance scheme with a coverage limit in the range of $30,000 - $50,000.

5. I am also seeking agreement to release the Review's second round of consultation. The second consultation sets out the above in-principle decisions and seeks further feedback on more detailed elements of these topics (attached Consultation Document 2A refers). It also seeks feedback on the remaining topics set out in the Review's terms of reference (attached Consultation Document 2B refers). These remaining topics include:

- what prudential regulatory tools and powers the Reserve Bank should have, and what role it should have in macro-prudential policy
- how the Reserve Bank should supervise and enforce prudential regulation
- how the Reserve Bank's balance sheet function should be formulated
- what features New Zealand's crisis management regime should have
- how the Reserve Bank should coordinate with other agencies
- how the Reserve Bank should be funded and resourced.

Background to the Review

6. A well-functioning and efficient financial system is important for improving the wellbeing and living standards of New Zealanders. The regulatory framework is a key driver of the performance of the financial system.

7. In 2017, the Government announced it would undertake a Review of the Reserve Bank of New Zealand Act 1989 (the Review) to modernise the monetary and financial stability policy frameworks and the Reserve Bank's governance and accountability settings. This Review is one of the Government's initiatives under the 'grow and share more fairly New Zealand's prosperity' priority outcome, supporting the development of a productive, sustainable and inclusive economy.

8. The Review has been split into two phases:

   a. Phase 1 focused on improving the Reserve Bank's monetary policy framework. Cabinet agreed policy changes in March 2018 [CAB-18-MIN-0086 refers] and I announced the final decisions on 26 March 2018. These included a decision to add maximum sustainable employment as an objective of monetary policy alongside the existing objective of price stability. In addition, Phase 1 instituted a Monetary Policy Committee (MPC), which will make decisions on monetary policy and include a minority of external members. These changes came into force on 1 April 2019.

   b. Phase 2 (the focus of this Cabinet paper) considers the Reserve Bank's financial policy framework, which provides the basis for prudential regulation and supervision, as well as the Reserve Bank's broader governance and accountability arrangements. Cabinet agreed the Terms of Reference for Phase 2 in May 2018 [DEV-18-MIN-0082 refers], and I released these to the public on 7 June 2018.

9. A joint Review team comprising members of both the Treasury and the Reserve Bank is carrying out Phase 2 of the Review. The Review team has prepared the attached consultation documents.

Independent Expert Advisory Panel

10. In Phase 1 of the Review, an Independent Expert Advisory Panel played an important role in supporting and advising the officials undertaking the Review. This role has continued in Phase 2. The Panel also provides advice directly to me, as appropriate.

11. For Phase 2, the Panel consists of Suzanne Snively (Chair), Malcolm Edey, and Girol Karacaoglu (the original members of the Phase 1 Panel), and Barbara Chapman, Belinda Moffat, and John Sproat (Cabinet agreed in August to add the latter three members to broaden expertise on the Panel [APH-18-MIN-0155 refers]).

Review Timeline

12. Public consultation and engagement is a central feature of the Review. This is a once-in-thirty-year opportunity and requires a comprehensive approach. There will be three rounds of public consultation during which we will seek feedback from a broad range of stakeholders. The number of consultations also reflects the breadth of topics set out in the Review's terms of reference. Figure A sets out the planned timeline for the Review below.

13. The first consultation was released in November 2018 [DEV-18-MIN-0240 refers] and closed in late January 2019. It covered topics that are crucial in shaping the Review's overall outcome, including:

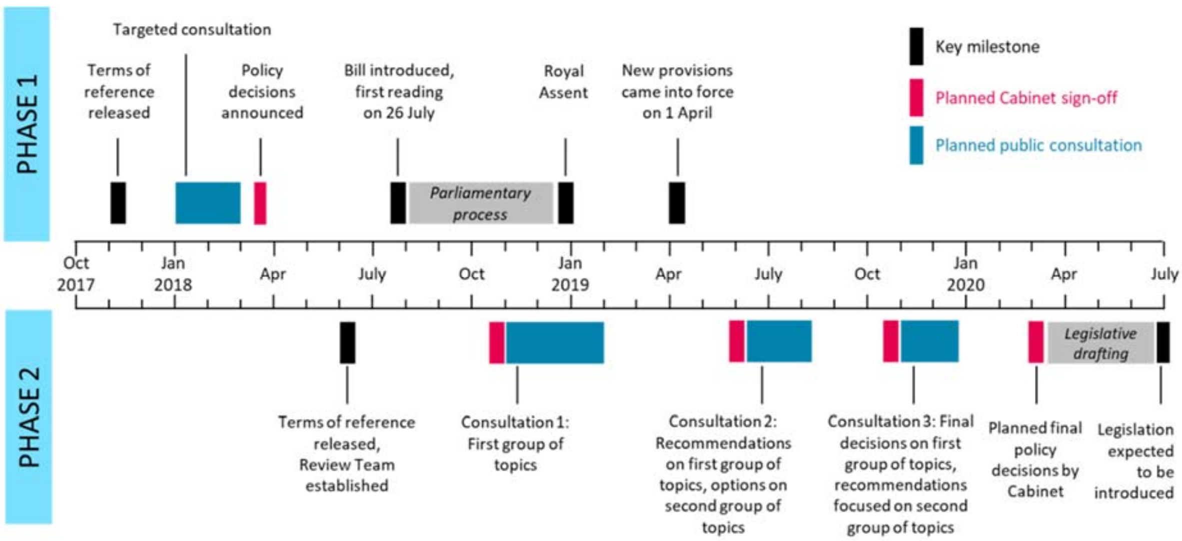
    - the case for separating prudential functions from the Reserve Bank
    - the Reserve Bank's high-level financial policy objectives
    - the Reserve Bank's governance arrangements
    - the Reserve Bank's regulatory perimeter
    - the case for depositor protection in New Zealand

14. A total of 67 formal submissions (around 40% of which were from individuals/members of the public) were received during the first round of consultation alongside a programme of stakeholder engagement, workshops and interviews undertaken by the Review team.

15. I am now seeking agreement to release the Review's second round of consultation documents. The second round of consultation will set out in-principle decisions on topics covered in the first consultation and seek further feedback on more detailed elements of these topics. It will also seek feedback on the remaining topics set out in the Review's terms of reference. These remaining topics are outlined in paragraphs 59-70 below.

16. A third and final consultation will take place later in 2019 and will seek feedback on preferred options developed relating to these remaining topics.

Figure A: Planned timeline for the Review



Second Consultation

17. The proposed material for the second consultation is attached. There are two consultation documents:

    a. <u>Consultation Document 2A</u>: *'In-principle decisions and follow up questions on: the role of the Reserve Bank and how it should be governed'.* This document sets out the proposed in-principle decisions outlined above along with relevant follow-up issues for further consultation relating to these topics. These in-principle decisions are set out in paragraphs 24-57 below.

    b. <u>Consultation Document 2B</u>: *'The Reserve Bank's role in financial policy: tools, powers, and approach'.* This document explores all remaining topics covered in the Review's terms of reference. These remaining topics are outlined in paragraphs 59-70 below.

18. Additional papers will be published alongside this consultation paper to provide further background on some of the topics discussed. This includes a paper on the role of the Reserve Bank in responding to climate risk, which links to several topics being considered in the second consultation, and a paper on macro-prudential policy.

19. In preparing the consultation document the Review team has been mindful of the need for the consultation to be accessible to non-specialist audiences. An external editor has been engaged to ensure the readability of the document.

20. The Independent Panel considers the two consultation documents are of good quality overall and suitable for consultation. They note that topics have been covered well and in a balanced way, and that consultation questions are focused on the right issues.

In-Principle Decisions on Topics from First Consultation

21. Following the conclusion of the first consultation round in January, I made some in-principle decisions, outlined below in paragraphs 24-57, relating to topics covered in the first consultation. These in-principle decisions were needed to provide clarity on the expected direction of travel for the Review given interdependencies with the remaining Review topics being covered in the second consultation. For example, it would be difficult to progress work on the crisis management framework for the second consultation without a clear indication about whether depositor protection is expected to be pursued.

22. Final decisions will be sought on recommendations for these topics after the second consultation has concluded later in 2019. More detail on each of these is set out in Consultation Document 2A.

23. The attached consultation documents have been prepared on the basis of the in-principle decisions, which are described further in paragraphs 24-57 below. I seek Cabinet's endorsement of these in-principle decisions.

Should prudential regulation remain with the Reserve Bank?

24. The Reserve Bank is currently the prudential regulator for New Zealand's financial system. This Review has been considering whether the Reserve Bank should continue to have this prudential mandate, or whether this function should be moved to a separate agency, as is the case in Australia (where prudential responsibilities are with the Australian Prudential Regulation Authority). While the first consultation set out the Government's initial preference that prudential responsibilities should continue to sit with the Reserve Bank, I tasked this Review with exploring this question further, and what underlies it, given the strong interest from some external stakeholders.

25. I recommend that an in-principle decision is taken to retain responsibility for prudential functions at the Reserve Bank. This will maximise synergies between the Reserve Bank's prudential regulation and other functions. It will also avoid the transition costs of setting up a new prudential agency and is a cost-effective regulatory model given New Zealand's size. The decision is consistent with international trends since the global financial crisis, with a number of jurisdictions shifting responsibility for prudential regulation to their central banks.

26. The Independent Panel, the Reserve Bank and the Treasury support this recommendation. The majority of stakeholders also supported prudential functions remaining at the Reserve Bank in their feedback through the first consultation.

27. A minority of stakeholders were concerned about issues such as a lack of focus from the Reserve Bank on its prudential role, a lack of capacity to fulfil its role, and potential conflicts with different policy functions. Wider reforms being considered by this Review (including around the Reserve Bank's governance arrangements, objectives, and resourcing) can help address these concerns.

What high-level financial policy objectives should the Reserve Bank have?

28. The Reserve Bank's high-level financial policy objective to '*promote the maintenance of a sound and efficient financial system*' has been in place for almost 30 years and defines the Reserve Bank's role in financial regulatory policy. The key question for the Review is whether the existing objectives are still the most appropriate goals for the Reserve Bank, or whether they should be refreshed.

29. I recommend an in-principle decision is taken to replace the Reserve Bank's existing 'soundness' and 'efficiency' financial policy objectives with a single over-arching 'financial stability' objective. 'Financial stability' is seen as a clearer, more modern, internationally accepted term that is more relevant to the Reserve Bank's broad role in safeguarding the financial system. It provides direction for all of the Reserve Bank's financial policy functions, from prudential regulation to crisis management. It also unites the most relevant aspects of soundness and efficiency in a singular objective, removing ambiguity in how objectives are weighed, and providing clarity of focus.

30. This high-level objective will be complemented by a fuller set of objectives that includes relevant aspects of both 'soundness' and 'efficiency'. These are being consulted on further in the second consultation.

31. The Independent Panel, the Reserve Bank and the Treasury all support this in-principle decision. Most stakeholders supported this change while recognising that the high-level financial stability objective should be complemented by a fuller 'objective set' to guide the Reserve Bank in undertaking its financial policy functions. In particular, stakeholders noted that it would be important to retain and clarify the Reserve Bank's role in supporting 'financial system efficiency' when developing the objective set. Options around a wider objective set are set out in more detail in Chapter 2 of Consultation Document 2A.

Should the Reserve Bank have a governance board?

32. The governance arrangements of the Reserve Bank play an important role in determining how the Reserve Bank pursues its policy objectives. A key question covered by the Review is whether any of the Reserve Bank's governance arrangements could be enhanced, including whether the Reserve Bank's current single decision-maker model should be replaced by a board.

33. I recommend an in-principle decision is taken to establish a new governance board, which is given statutory authority over all Reserve Bank decisions (except for those reserved for the MPC). The board governance model is already used by all New Zealand Crown entities (including the Financial Markets Authority), is well understood domestically and internationally, and is underpinned by robust legal and corporate governance frameworks.

34. Through the new governance board, group decision-making will be embedded at the highest level of the Reserve Bank. This will help to bring diverse perspectives and experiences to key decisions and protect against individual biases and preferences. It will also enable more robust accountability for

decisions by creating a clearer split between the governance and management functions (with the latter remaining the Governor's responsibility).

35. The new governance board will need to be designed carefully to ensure it can manage its broad mandate, particularly in details such as its composition (the balance of executive and non-executive members), skills and expertise of board members, and appointment/removal processes. Chapter 3 of Consultation Document 2A consults further on some of these key design features. It broadly assumes that the MPC will continue in its current form, although it suggests options for change in the MPC governance arrangements if they are consistent with the direction of reform for financial policy.

36. The Independent Panel, the Reserve Bank and the Treasury support the establishment of a governance board. In addition, the vast majority of submissions from the first consultation supported a new governance board being established to replace the single-decision-maker model.

Should the Reserve Bank have a separate Financial Policy Committee?

37. The Review's first consultation also considered whether a Financial Policy Committee (FPC) should be introduced alongside the new Monetary Policy Committee being established from Phase 1.

38. I recommend an in-principle decision is taken not to establish an FPC. Instead the proposed new governance board will be responsible for Reserve Bank decisions relating to prudential policy.

39. As noted above, the board model is also well understood domestically and internationally, and underpinned by robust legal and corporate governance frameworks. In contrast to monetary policy where committees are common practice, a statutory FPC is seldom used for prudential policy internationally (with the Bank of England being a notable exception) and no Crown entities have statutory committees. The prudential policy framework is less mature than the monetary policy framework, and differences between monetary and prudential policy mean that the optimal decision-making structure is not necessarily the same for both.

40. While stakeholders strongly supported the establishment of a new board, views differed on whether the board or a separate statutory FPC would provide the best governance arrangements for prudential policy. The Independent Panel members' views differed on the establishment of a statutory FPC, with four favouring the board controlling prudential policy (to avoid diluting its role and introducing additional complexity) and two supporting an FPC (to increase the prominence and focus of prudential policy decisions).

Who should monitor the Reserve Bank's performance?

41. The existing Reserve Bank board currently serves as the Reserve Bank's monitor.[1] The existing Reserve Bank board is not well placed to monitor and assess the Reserve Bank's operational performance. It has no formal decision-making rights (outside appointments), no independent resourcing and limited financial policy expertise, and there are practical challenges in balancing its duties to the Minister with its relationship with the Reserve Bank.

42. I recommend an in-principle decision is taken to establish the Treasury as the Reserve Bank's monitoring agent. This will align the Reserve Bank's monitoring arrangements with those of a Crown entity and make the Treasury responsible for assessing and reporting on the Reserve Bank's performance (including the Monetary Policy Committee).

43. Moving to a Crown entity-style monitoring framework will address issues with the current monitoring arrangements and delineate monitoring roles more clearly. The move will see the new governance board providing greater oversight of the Reserve Bank's day-to-day operations and the Treasury providing an independent cross-check of the Reserve Bank's overall performance, as the external monitor acting on behalf of the Minister. The Reserve Bank's operational independence will be protected and the Treasury will not be evaluating or second-guessing decisions made by the board or MPC. The Treasury is well placed for this role given its existing close relationship with the Minister and independence from the Reserve Bank.

44. The Independent Panel, the Reserve Bank, the State Services Commission and the Treasury support the Treasury becoming the external monitor for the Reserve Bank. Submissions received through the first consultation indicated strong stakeholder support that the Treasury should monitor the Reserve Bank.

45. Given that the board model and monitoring arrangements share common features with Crown entities' governance arrangements, the Chapter 3 of Consultation Document 2A also consults on the merits in reclassifying the Reserve Bank as an independent Crown entity. Any shift to an independent Crown entity model would have to accommodate distinctive features (such as the MPC) needed by the Reserve Bank to fulfil its functions and protect its operational independence.

How should the regulatory perimeter be set?

46. The 'regulatory perimeter' refers to the firms or activities that the Reserve Bank regulates and how the boundary between regulated and unregulated firms is defined. The current perimeter for deposit-taking entities could be redrawn to create a more unified, simple and future-proofed regulatory regime. The key question for the Review is whether the potential benefits of redrawing the perimeter are worth the transition costs.

[1] 'Monitoring' refers to the processes in which a Minister oversees an agency and ensures that it is meeting its legislative duties, using taxpayer funds appropriately, and acting in line with agreed strategic directions.

47. I recommend an in-principle decision is taken to bring together the currently separate regulatory regimes for banks and non-bank deposit takers (deposit-taking institutions that are not registered banks, such as finance companies and building societies) into a single 'licensed deposit taker' perimeter.

48. This move to a single regime will more clearly align regulatory activities with the Reserve Bank's 'financial stability' objective, and also support good regulatory outcomes through greater regulatory efficiency (minimising duplication across regimes) and neutrality (treating similar activities in the same way). The new framework will continue to be risk-based, allowing it to be growth-compatible and support innovation. It will also be more flexible and adaptable, and enable new entrants and new business models to be accommodated where appropriate (this was a strong theme in stakeholder feedback). Chapter 4 of Consultation Document 2A seeks feedback on further development of this new approach.

49. The Independent Panel, the Reserve Bank and the Treasury support this recommendation. Stakeholders almost universally supported this decision in their feedback through the first consultation.

Should there be depositor protection in New Zealand?

50. New Zealand does not currently have a depositor protection regime, so customer deposits are at risk if banks fail. The first consultation looked at mechanisms that are used around the world to protect depositors, set out the potential benefits and costs of protecting depositors in New Zealand, and sought views on whether the arguments supported a case to progress work on developing a depositor protection regime for New Zealand.

51. I recommend an in-principle decision be taken to start developing a formal scheme to protect depositors in New Zealand in the event that the institutions holding their deposits fail. I recommend this work proceed on the basis that eligible depositors' savings in registered deposit-taking institutions are protected up to an insured limit, currently proposed to be $30,000-$50,000 per depositor per institution. The scheme will protect, with certainty and consistency, ordinary New Zealanders from the risk of losing their savings in the bank – and in doing so contribute to public confidence and the stability of New Zealand's financial system.

52. The first consultation showed that a broad cross-section of stakeholders are in favour of introducing depositor protection for New Zealanders. Those in favour included a significant majority of the general public, industry practitioners and experts, special interest groups, past governors of the Reserve Bank, and three of the five largest banks in New Zealand.

53. Stakeholders generally agreed that an insurance scheme would be the best way to protect depositors, possibly supported by a depositor preference (which puts protected depositors in failed banks higher in the creditor hierarchy so they are closer to the front of the queue to be repaid).

54. However, stakeholders had mixed views on the objectives of depositor protection, and many – including the Independent Expert Advisory Panel – asked for more information on where depositor protection might fit within New Zealand's broader prudential regulatory architecture, and the economic consequences of protecting depositors. Chapter 5 of Consultation Document 2A follows up on these issues in more detail.

55. The design of New Zealand's depositor protection scheme will require significant further work and consultation to ensure that it is the best for New Zealand. Among other things, the work programme will have to address:

    a. the public policy objectives that the protection scheme should meet

    b. how the protection scheme should function (its role, scope, coverage and pay-out procedure)

    c. how the protection scheme should be financed to support these functions (including whether industry will finance the scheme, the size of the scheme, and when funding for the scheme should be collected)

    d. whether the protection scheme should be complemented by a 'depositor preference' for protected claims.

56. Chapter 5 of Consultation Document 2A seeks feedback on some of these issues.

57. Final decisions on these issues will be made later in the Review process, when they can be considered in the context of decisions on New Zealand's wider prudential framework.

Remaining Review Topics

58. The second consultation also explores the remaining topics set out in the Review's terms of reference. These remaining topics, which are covered in Consultation Document 2B, are outlined briefly in paragraphs 59-70 below.

What prudential regulatory tools and powers should the Reserve Bank have?

59. 'Prudential regulation' is the set of rules and requirements (such as capital, liquidity and corporate governance requirements) that apply to New Zealand's banks, insurers and other financial institutions. In New Zealand, prudential regulation is implemented either through primary legislation or instruments delegated to the Reserve Bank. Key questions for the Review are whether the right balance has been struck between the use of primary legislation and delegated instruments, and whether the delegated instruments used to regulate the banking sector are fit for purpose.

60. The Review also considers the arguments for and against New Zealand adopting elements of the Banking Executive Accountability Regime (BEAR) framework, which would increase the responsibilities and accountabilities of senior executives of the new licensed deposit-takers (see paragraph 47).

Potential changes to executive accountability are currently being considered in conduct regulation: it would be desirable that the design of both conduct and prudential regulation in this area is clearly aligned.

What role should the Reserve Bank have in macro-prudential policy?

61. Macro-prudential policy is the subset of prudential regulation that emphasises a system-wide approach to risk assessment rather than just on the stability of individual institutions. Since the GFC, most advanced countries have adopted a macro-prudential overlay to their prudential work and have used new tools to help mitigate excessive variability in the financial cycle.

62. New Zealand introduced a new macro-prudential framework in 2013 and the Reserve Bank immediately made use of a new macro-prudential tool – Loan-to-Value Ratio (LVRs) restrictions on residential mortgage lending. The use of LVRs has attracted more scrutiny than standard prudential tools because they have affected individual borrowers more directly. The key question for the Review is how effective New Zealand's macro-prudential framework has been over the past five years and whether changes to the governance of macro-prudential decisions and the macro-prudential toolkit should be considered.

How should the Reserve Bank supervise and enforce prudential regulation?

63. The Reserve Bank adopts a light-handed approach to supervision and enforcement of prudential regulation instead emphasising the importance of creating incentives for a bank's own directors and a bank's creditors to ensure that banks are being run in a safe and sound manner.

64. Although the Reserve Bank has followed the trend overseas and increased the intensity of its supervision since the GFC, by international standards New Zealand's supervisory regime remains light-handed with relatively little independent verification of supervisory information, largely tied to the absence of an 'on-site' inspection regime. Key questions for the Review are whether this approach remains appropriate and whether the Reserve Bank has a sufficient range of enforcement powers to ensure that regulatory standards are being met.

How should the Reserve Bank's balance sheet function be formulated?

65. In times of stress, when banks are struggling to obtain funding from private creditors, the Reserve Bank can use its balance sheet to act as the Lender of Last Resort (LoLR) – providing short-term loans to solvent banks to contain market panic. This function is a crucial part of New Zealand's financial safety net, but current legislation says little about when and how the Reserve Bank can undertakes this LoLR role. The key question for the Review is how both the purpose and boundaries of the LoLR function can be clarified, which could include a mixture of changes to primary legislation and/or requirements to publish framework documents.

66. The Reserve Bank can use its balance sheet for a number of other functions, including implementing monetary policy decisions (including quantitative

easing or unconventional monetary policy) and foreign exchange intervention. A related question for this Review is whether there is a case to alter the extent of the Reserve Bank's powers or independence in specific areas.

What features should New Zealand's crisis management regime have?

67. Banks, like any type of business, can fail. However, unlike other businesses, a bank failure can have severe economic impacts on its depositors and can cause widespread contagion to other financial institutions which can threaten financial stability and economic prosperity. It is for this reason that the prudential regulation of banks needs to be complemented by a 'resolution regime' that provides sufficient powers for the Reserve Bank to resolve failed banks in an orderly way. The key question for the Review is whether New Zealand's existing resolution regime is fit-for-purpose, and to consider options to address any issues and align with international best practice as appropriate.

How should the Reserve Bank coordinate with other agencies?

68. The Reserve Bank is part of a broader eco-system of domestic and international financial regulators and economic policymakers. Effective coordination with other agencies is important to improve the quality of policy, identify and address overlaps or underlaps in the regulatory framework and ensure an optimal mix of policies throughout the system. Coordination can also facilitate better planning for extraordinary events, which are likely to require more intensive cooperation between agencies. The key question for the Review is whether existing mechanisms to facilitate policy and regulatory coordination in New Zealand could be enhanced by formal statutory requirements to support effective coordination arrangements.

How should the Reserve Bank be funded and resourced?

69. The way the Reserve Bank receives its funding has a key influence on how and whether it can achieve its statutory objectives. A well-designed funding mechanism balances budgetary independence with transparency and accountability (to ensure that the public is getting good value for money). The key question for the Review is whether the current funding mechanism is effective in achieving this balance and whether other models could be more appropriate.

70. The particular level of funding the Reserve Bank receives is outside the scope of the terms of reference for this Review and will instead be considered through the existing funding agreement mechanism with the Reserve Bank (with preparation currently underway for the next funding agreement due in 2020).

Consultation

71. The joint Review team, comprising staff from the Treasury and the Reserve Bank, prepared the attached consultation documents. The following agencies were consulted: the Ministry of Business, Innovation and Employment, the Financial Markets Authority, the Commerce Commission, the Ministry of Justice, the State Services Commission, the Reserve Bank, and the Treasury.

72. Workshops and discussions have also been held with Associate Ministers of Finance and the Minister for Housing and Urban Development.

73. The Department of the Prime Minister and Cabinet was informed.

Financial Implications

74. This paper has no direct financial implications.

Human Rights

75. There are no human rights implications arising from this paper.

Legislative Implications

76. There are no legislative implications arising directly from this paper. Final policy decisions made later in the Review are expected to result in changes to the Reserve Bank of New Zealand Act 1989.

Regulatory Impact Analysis

77. A regulatory impact statement is not required at this stage. The consultation document incorporates elements of regulatory impact analysis, and a regulatory impact statement will be prepared when final policy decisions are sought. The Independent Panel has also provided a quality assurance function for the consultation documents, consistent with quality assurance requirements for regulatory impact analysis.

Gender Implications

78. There are no gender implications arising from this paper.

Disability Perspective

79. There are no disability implications arising from this paper.

Publicity

80. The consultation documents will be made available on the Review section of the Treasury website. A media release will be issued when the consultation documents are released. A programme of stakeholder engagement is planned to follow the release.

Proactive Release

81. I propose to proactively release this Cabinet paper, in full, as part of a wider proactive release of material (such as policy advice reports) relating to the development of the set of second consultation documents. This will be made available within 30 days of releasing the consultation documents, on the Review section of the Treasury website.

Recommendations

82. I recommend the Committee:

1. **note** that Phase 2 of the Reserve Bank Act Review was announced in June 2018 and is focusing on reviewing the financial policy provisions of the Reserve Bank Act 1989 as well as broader governance arrangements for the Reserve Bank

2. **note** the first consultation document for Phase 2 was released in November 2018 and consultation concluded in January 2019

In-principle decisions around topics from the first consultation

3. **note** in-principle decisions are being sought at this stage on topics covered in the first consultation

4. **note** these in-principle decisions are needed to provide clarity on the expected direction of travel for the Review given the interdependencies with the topics being covered in the second consultation

5. **agree in principle** to:

   5.1. Retain the prudential regulation and supervision functions as part of the Reserve Bank

   5.2. Replace the Reserve Bank's existing 'soundness' and 'efficiency' financial policy objectives with a single over-arching 'financial stability' objective

   5.3. Establish a new governance board, which is given statutory authority over all Reserve Bank decisions (except for those reserved for the Monetary Policy Committee), including prudential policy decisions

   5.4. (in light of 5.3) Not establish a new Financial Policy Committee

   5.5. Appoint the Treasury as the external monitor of the Reserve Bank

   5.6. Merge New Zealand's two existing prudential regimes for regulating banks and non-bank deposit takers into a single deposit-taking regime

   5.7. Establish a depositor insurance scheme with a coverage limit in the range of $30,000 - $50,000

6. **note** that the attached consultation documents have been prepared on the basis of these in-principle decisions

7. **note** that final decisions will be sought on these topics after the second consultation has concluded later in 2019

Release of second consultation

8. **note** the focus of the second consultation is to:

    8.1. Set out the proposed in-principle decisions on topics from the first consultation and consult on relevant follow-up issues relating to these topics (covered in Consultation Document 2A), and

    8.2. Explore all remaining topics covered in the Review's terms of reference (covered in Consultation Document 2B)

9. **agree** that the Minister of Finance release the attached Consultation Documents 2A and 2B

10. **authorise** the Minister of Finance to approve minor amendments and refinements to these consultation documents

11. **note** the second consultation period will run for eight weeks commencing mid-June 2019 and concluding in August 2019

12. **note** that the Minister of Finance will report back to Cabinet on the outcome of this consultation in October 2019.

Authorised for lodgement

Hon Grant Robertson
Minister of Finance