

# The Treasury

## Reserve Bank Act Review Phase 2 Review Update Proactive Release

March 2020

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- [33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
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## Report: Reserve Bank Act Review: Institutional Act follow ups

<b>Date:</b>	18 October 2019	<b>Report No:</b>	T2019/2766
		<b>File Number:</b>	MC-1-7-3-1-3

### Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	<b>Agree</b> the recommendations. <b>Note</b> the additional information provided.	Tuesday, 22 October 2019

### Contact for telephone discussion (if required)

Name	Position		Telephone	1st Contact
Felicity Barker	Principal Advisor, Reserve Bank Act Review – Phase 2	[39]	N/A (mob)	✓
Bernard Hodgetts	Director, Reserve Bank Act Review – Phase 2	[39] (wk)	n/a (mob)	

### Minister's Office actions (if required)

Return the signed report to Treasury.  
Refer a copy of this paper to the Associate Ministers' of Finance.

**Enclosure:** No

## **Report: Reserve Bank Act Review: Institutional Act follow ups**

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### **Executive Summary**

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This report seeks further decisions to be incorporated into the November Cabinet paper on the Reserve Bank Institutional Bill (the 'bill'). The decisions in this report relate in the main to: the Reserve Bank's (the 'Bank') information gathering powers, its balance sheet management, foreign exchange management and transition provisions. The report also provides supplementary information that you have sought in relation to a number of matters.

#### *Supplementary information*

You have requested supplementary information on the following matters:

- **Legislating the Council of Financial Regulators (CoFR):** our recommendation is that the Cabinet paper seeks agreement to create a legislative mandate for CoFR, and subsequent to that, officials will work with CoFR members to determine how that mandate will be included in the legislation. Officials will report back once the specification is determined.
- **Criteria for the removal of the Governor:** under the bill the Governor will continue to be able to be removed from office by the Governor-General on the advice of the Minister if specified grounds are met. These grounds will be similar to the 'just cause' grounds in the Crown Entities Act (Table 1 paragraph 43). Compared to the current Act, two grounds will be removed as these are now responsibilities of the Board. These are the duty to adequately carry out the functions of the Bank and to manage the resources of the Bank effectively.
- **Scope of review by the Ombudsman:** the Ombudsman may investigate any decision that affects a person in their personal capacity relating to a matter of administration by an organisation named in the schedule to its Act. The Ombudsman cannot investigate conduct which is legislative, judicial, or ministerial in nature. In addition, the Ombudsman cannot investigate a matter where there is a statutory right of appeal, and has the discretion to not investigate complaints where the complainant has no greater interest in the matter than any other person (such as is the case with monetary policy decisions). As part of the development of the Deposit Takers Bill, it is intended that a statutory right of appeal apply for banks subject to resolution.
- **Performance reviews of the Bank:** it is proposed that the Bank be subject to the requirements of the Public Audit Act, which allow the Auditor-General to examine the extent to which a public entity is carrying out its activities effectively and efficiently, and that the Minister also be able to review the operations and performance of the Bank in the same manner as Crown entities can be reviewed. We do not recommend a legislated frequency of reviews, as this would reduce flexibility. However, the frequency of reviews could be addressed in the memorandum of understanding to be agreed between the Minister and the Treasury that will set out how the Treasury will conduct its monitoring activities.

- **Process for reviewing deposit insurance scheme:** it is recommended that the deposit insurance scheme be reviewed at a suitable interval post implementation and from time to time thereafter. The Regulatory Impact Assessment will commit to undertaking the post-implementation review of the wider package of reforms in the Deposit Takers Bill.
- **Government funding backstop for deposit insurance:** you will receive further advice on the details of a prearranged and guaranteed government funding backstop for the deposit insurance scheme before the end of this year as part of preparation for consultation early next year.

### *Information gathering*

It is proposed that the Bank's current, relatively narrow, information-gathering power that applies in regards to collecting information for the purpose of its central banking and financial system monitoring functions be replaced by a broader power. The proposed power would enable the Bank to collect any information from any person (but not from individuals in their private capacities) for the purpose of enabling these functions. This would enable the Bank to collect information from any financial service provider, as well as other entities that support the financial sector, rather than be restricted to collecting information from a defined set of financial institutions. The Bank has separate information gathering powers for its regulatory functions. The precise specification of this power will need to be considered by the Ministry of Justice to ensure compliance with the Bill of Rights. Information collected under this power would be subject to the Bank's confidentiality provisions.

### *Balance Sheet Management*

The Bank transacts in financial markets in undertaking its central banking activities, giving rise to financial risk. To increase transparency, it is proposed that the Board be required to publish its framework for balance sheet management. It is also proposed that an additional function be added to the bill that captures many of the Bank's balance sheet operations, such that the Bank can "*conduct market transactions in support of its economic and financial stability objectives*".

It is possible that the Bank may, at some point in time, use unconventional monetary policy to meet its economic objectives. This gives rise to a number of issues, including how any resulting profits and losses from such policies are shared between the Bank and the Crown, and how to reconcile the Board's balance sheet management with the Monetary Policy Committee's decisions. The Treasury and the Bank are working together to clarify the details of any programme that the Bank may undertake and will report back to you on these issues, and if there are any resulting implications for the legislation.

### *Foreign Exchange Market Intervention*

Many of the provisions in the current Act on foreign exchange management relate to the nature of the economy and policy tools in place when the current Act was passed in 1989. It is recommended that sections that are no longer able to be practically used to meet their original policy objectives in modern financial markets are repealed.

## *Transitional Provisions*

It is recommended that provisions of the bill enabling the establishment of the Board, including the nominations committee, would commence on Royal Assent. Other parts of the bill would commence twelve months after Royal Assent to allow time to appoint the Board.

The proposed model for the Minister to retain the appointment of the Governor gives rise to a number of legislative and operational complexities. In particular, the Board will be responsible for the day-to-day monitoring and performance management of the Governor, but not for the person's appointment or dismissal. Operational complexities include: whether the Governor will be an employee of the Bank and who determines the Governor's remuneration. The Review will report back on these matters.

## Recommended Action

We recommend that you:

- a. **note** the additional information we have provided in response to your request in paragraphs 40-63.

*Noted*

- b. **agree** that the bill for the Institutional Act (the bill) broaden the Bank's existing information gathering power in relation to its central banking functions, allowing it to collect any information from any person (other than personal information) for use in relation to these functions.

*Agree/disagree*

- c. **agree** that the bill require that the Board publish its framework for balance sheet management.

*Agree/disagree*

- d. **agree** that, in addition to the functions agreed in T2019/2764, the Bank have a function to capture the Bank's balance sheet operations, such as: *Conduct market transactions in support of its economic and financial stability objectives*.

*Agree/disagree*

- e. **agree** to repeal the following sections of the Reserve Bank Act on foreign exchange dealing that are no longer able to be practically implemented to meet their objectives or are redundant:

1. **Section 18** – That the Minister can direct that all foreign exchange dealings by the Bank shall be at a fixed rate of exchange;
2. **Section 22** – That the Governor can direct New Zealand-registered banks to stop dealing in the foreign exchange market;
3. **Section 23** – That the Bank advises the Minister on foreign exchange matters.

*Agree/disagree*

- f. **agree** that the legislative provisions enabling the establishment of the Board, including the nominations committee, commence on Royal Assent.

*Agree/disagree*

- g. **agree** that the other parts of the bill commence twelve months following Royal Assent.

*Agree/disagree*

- h. **agree** to add the Bank to the list of organisations in Schedule 1 of the Ombudsmen Act 1975.

*Agree/disagree*

- i. **agree** that the Cabinet paper seek agreement to create a legislative mandate for the Council of Financial Regulators, with the design of the mandate to be determined subsequently.

*Agree/disagree*

- j. **agree** to move requirements relating to commercial banks' retention of documents to the Bills of Exchange Act.

*Agree/disagree*

- k. **Note** that we do not recommend a statutory requirement to regularly review the Bank. Rather the nature and frequency of any reviews can be addressed in the MOU between the Minister of Finance and the Treasury (as monitor).

*Noted*

Bernard Hodgetts  
**Director, Reserve Bank Act Review – Phase 2**

Hon Grant Robertson  
**Minister of Finance**

## **Report: Reserve Bank Act Review: Institutional Act follow ups**

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### **Purpose of Report**

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1. The purpose of this report is to seek further decisions on matters relating to the Reserve Bank Institutional bill (the 'bill') and to provide you with information that you have requested.
2. Decisions on the policy issues in this report will be included in the Cabinet paper seeking approval to the proposed content of the bill. We will provide you a draft of this Cabinet paper on 29 October, to allow submission to the Cabinet Economic and Development Committee meeting on 20 November.

### **Analysis**

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#### ***Background***

3. You have made a number of decisions in relation to the Institutional bill [T2019/2764]. This paper addresses the following remaining issues: information gathering powers, legislating a mandate for the Council of Financial Regulators, requirements in relation to the management of balance sheet risks, foreign exchange intervention and transitional matters. This report also discusses the setting of the Governor's remuneration.
4. You have also asked for additional information in relation to adding the Bank to the list of entities the Ombudsman can review, changes to the provisions relating to removal of the Governor, requirements relating to reviews of the Bank's operations and performance, how the framework will ensure regular review of the deposit insurance scheme, and the Government funding backstop for deposit insurance.
5. There is one remaining substantive issue that needs to be addressed in regards to the bill. This relates to the Bank's powers in relation to the issuance of currency and stewardship of the currency system. The Bank is currently consulting on the legislative requirements in regards to currency management and reviewing the technical aspects of its currency function. The Review will provide further advice on the powers in regards to currency management in early 2020. Changes to the bill in regards to the currency powers are likely to need Cabinet approval.
6. There are a number of more minor issues that will need to be addressed as the bill is drafted. This includes provisions relating to immunity and indemnity and penalties in relation to failure to comply with information requests. The Review will report back on any further substantive issues in the early 2020.

## ***Information gathering***

7. The Bank can currently require financial institutions to provide information for the purposes of enabling it to carry out its functions under Part 2 of the Act. It uses this power to conduct a range of surveys which are critical to the formulation and implementation of monetary policy, as well as monitoring the financial system and undertaking other central banking functions, and for general information requests of financial institutions.
8. While the Bank's current information gathering power is fit for purpose in most cases, its restriction to information held by "financial institutions" has been problematic. The legal meaning of financial institutions is relatively narrow and limited in practice to entities that offer "bank-like" services. This means that it cannot be used by the Bank to collect some information that is important to central banking functions, such as information about securities holdings from securities registries.
9. We propose that this information collection power be replaced by a broad and enabling information gathering power, enabling the Bank to collect any information from any person for the purposes of enabling its central banking and financial system monitoring functions. This would enable the Bank to collect information from any financial service provider, as well as other entities that support the financial sector, to support these functions. It would not be used for the Bank's regulatory functions, which have separate information gathering powers. It would be specified so as not to enable the Bank to collect information from individuals in their private capacities. The current ability to require information provided to be audited would be retained, clarified and made more flexible.
10. The precise specification of this power will need to be assessed against the provisions of the Bill of Rights Act and be vetted by the Ministry of Justice. In particular, consideration will need to be given to the right to be secure against unreasonable search or seizure. Our view is that the power is reasonable due to the link to the Bank's objectives and functions and the limitations on the types of information that the Bank can collect as set out in paragraph 9. We note that the Financial Markets Authority (FMA) has a similarly broad power, relating to all of its functions, which the Ministry of Justice assessed as constituting a reasonable search and seizure power.
11. The Act currently provides that failure to supply information under section 36 is an offence, and sets penalties for this. Our initial view is that it would be desirable to update the penalties associated with this offence and provide for an infringement offence. We will report back on this following discussions with the Ministry of Justice.

## ***Council of Financial Regulators***

12. You have indicated that you would like to create a legislative mandate for the Council of Financial Regulators (CoFR). We recommend any mandate for the CoFR be flexible and enabling, and avoid prescribing the CoFR's structures or functions in any detail, instead focusing on its purpose. It is also important that the CoFR's role does not conflict with the statutory independence of the Bank, Financial Markets Authority and Commerce Commission. We propose that you seek agreement from Cabinet to provide a legislative mandate for the CoFR and that we subsequently provide you with further advice on the design of the mandate, incorporating advice from other CoFR agencies.



13. We consider that the primary value added by the CoFR relates to system monitoring and operational co-ordination, particularly in regards to regulatory actions and the legislative mandate should be consistent with this.
14. You have also indicated that you see the CoFR playing a key role in ensuring coordinated stewardship across the financial regulatory system. All CEOs of agencies subject to the State Services Act 1988 (SSA) have stewardship obligations in respect of their agency and the legislation administered by them. The Bank is not subject to the SSA. "Stewardship" under the SSA means active planning and management of medium- and long-term interests, along with associated advice.
15. We agree that a more integrated and coordinated approach to system stewardship is critical. However, we do not consider the CoFR should itself have system stewardship responsibilities. This could potentially reduce role clarity for the agencies that administer the legislation. We will provide you with further advice in 2020 on developing a more integrated and coordinated approach to stewardship of the financial regulatory system.

### ***Balance Sheet Management***

16. The exercise of many of the Bank's powers requires it to undertake financial market transactions. For this reason the Bank's activities give rise to financial risks. There should therefore be a level of oversight and transparency as to how the Bank is managing its balance sheet, and the benefits that are being obtained from financial risks that are taken.
17. For this reason, it is proposed to require the Board to publish its framework for balance sheet management. This would provide greater transparency as to the Board's approach to the management of balance sheet risks, and assist the Treasury in its role as monitor. The framework would include the Bank's management of financial risks arising from foreign reserves, lender of last resort activities and unconventional monetary policy tools if they are used by the Bank in the future. The framework document would be a living document that the Bank would update at appropriate intervals.
18. Further, it is important that the Bank is sufficiently empowered to transact in financial markets to meet its objectives. It is recommended that in addition to the functions recommended in the previous Joint Report [T2019/2764], the bill include a function that captures many of the Bank's balance sheet operations, such as the Bank can *conduct market transactions in support of its economic and financial stability objectives*.
19. Sections of the legislation impacting the Bank's balance sheet, such as management of foreign reserves and lender of last resort activities, will need to be updated as a result of changes to the Bank's objectives.
20. It is possible that the Monetary Policy Committee (MPC) may decide to implement a form of unconventional monetary policy, such as large scale asset purchases ('quantitative easing' (QE)) or credit easing in the future. If it did, this could have significant implications for the size and composition of the Bank's balance sheet. The decision to use unconventional monetary policy tools sits with the MPC, but a key issue will be how to reconcile the Board's responsibilities for balance sheet management with the MPC's decision-making for asset purchases.

21. Our preferred option to address this issue is through the monetary policy remit. This remit could require the MPC to have regard to the Board's framework for balance sheet management in the formulation of monetary policy.
22. Another issue is how much market and credit risk will be taken on as a result of these unconventional monetary policy tools, and how resulting profits or losses will be shared between the Bank and the Crown. The Bank and the Treasury are working together to clarify the details of any programme the Bank may undertake should unconventional monetary policy be required at some point, including:
  - the costs and benefits of the types of tools that the Bank may choose to use
  - the institutional arrangements required to govern the use of those tools, and
  - how any assets or derivatives held by the Bank for monetary policy purposes should be accounted for on the Bank's balance sheet.
23. Depending on the outcome of this work, we may provide further advice on legislative implications at a later date.

### ***Foreign Exchange Market Intervention powers***

24. The Act provides a number of provisions in regards to the management of foreign exchange. Many of these provisions related to the nature of the economy and tools of economic management in place when the Act was passed in 1989. In particular, New Zealand had recently moved from a fixed exchange rate regime, to a floating exchange rate regime with the central bank focussed on price stability.
25. It is recommended that several sections of the current legislation related to foreign exchange market intervention are repealed, as they are no longer able to be used to meet the original policy objective. These are:
  - Section 18 – provides a residual power for the Minister of Finance to direct the Bank to deal in foreign exchange at a fixed rate of exchange. We consider this power is unnecessary and undesirable as:
    - the Minister can also direct the Bank to deal in foreign exchange within guidelines for the purpose of influencing the exchange rate through section 17. A direction under this section is currently in place giving the Bank authority to act at its own initiative in the event of disorder in the foreign exchange market where urgent action is required;
    - the Governor-General can on the advice of the Minister change the objective of monetary policy to be something other than achieving price stability and maximum sustainable employment (the economic objectives), including moving to a currency objective; and
    - a fixed exchange rate regime is not consistent with independent monetary policy.
  - Section 22 – provides the Governor the power to direct all registered banks to stop dealing in the foreign exchange market. Most foreign exchange market trading of New Zealand dollars now takes place overseas by financial institutions that are not New Zealand-registered

banks, meaning this provision could not be practically implemented to meet the policy objective. Furthermore, stopping New Zealand banks from participating in the foreign exchange market would likely cause significant economic disruption.

- Section 23 – provides that the Bank will advise the Minister on foreign exchange matters. This section is redundant, as under Section 33, the Bank may provide advice to the Minister on any matter connected to its functions.

### ***Transitional provisions***

26. The following sections address transitional matters in regards to the enactment of the new Act.
27. It is anticipated that the Act commence prior to the Deposit Takers Act. During the intervening period, it will be necessary for Parts 4 and 5 of the current Act to remain in force, pending the enactment of the Deposit Takers Act.
28. In the interim period, sections 2, 3 and certain sections in Part 7 that are not transferred to the Institutional Act will also need to remain in force. Sections 2 and 3 contain definitions that assist with the interpretation of Parts 4 and 5.
29. Currently the Act provides certain requirements that commercial banks must meet in relation to the retention of documents (such as retention of cheques). It is recommended that these requirements be moved to the Bills of Exchange Act as they are more relevant to that Act.
30. Transitional arrangements will be needed to enable the appointment of the Board. This is so that it can be established and undertake its duties under the new Act from the time that it comes into effect. To enable this, it is recommended that the legislative provisions providing for the establishment of the Board commence twelve months prior to the rest of the Act. This will include enactment of the provisions relating to the nominating committee, who will nominate Board members, as well as provisions that set out the features of the Board (such as the size of the Board).
31. Consideration has been given to the establishment of an interim Board prior to the enactment of the legislation via administrative means. The legislation, however, will require that Board members are nominated to the Minister by the nominating committee. The process will also require consultation with other parties in Parliament. Members will then be appointed by the Governor-General on the advice of the Minister. Even if Board members were to be appointed prior to the enactment of the legislation, the procedural requirements would still need to be followed, resulting in an inefficient process.
32. Candidates for the nominating committee could, however, be identified prior to the legislation receiving Royal Assent to enable the nominating committee to commence as soon as the Act passes.
33. The Treasury's Appointments Team advises that the appointment process for Board members is likely to take nine to twelve months. This is because a relatively large board is proposed of not fewer than five members, and no more than nine. Due to the proposed Board's wide range of responsibilities, it is recommended that the Board operates as close to nine as possible. It is

recommended that twelve months be allowed for the establishment of the Board, to ensure that a Board of sufficient size and expertise is in place at the commencement of the rest of the Act.

34. Consistent with your in-principle decision in the Joint Report [T2019/2764], the current Board will be disestablished on the close of the day before the commencement date for the new Board. Members will cease to hold office at that time.

### ***Governor's terms of appointment***

35. You have made the decision to retain the power to appoint the Governor. This model is bespoke and carries a number of legislative and operational challenges. The Board would be responsible for the day-to-day monitoring and performance management of the Governor, but not for the person's appointment and dismissal.
36. One issue that will need to be resolved is whether the Governor is an employee. Another issue is who sets the Governor's remuneration and terms of appointment.
37. Currently the Governor's remuneration is agreed between the Governor and the Minister, following consultation with the Board. In the Crown entity model the Board sets the chief executive's remuneration, although this requires the consent of the State Services Commissioner. Alternatively other statutory heads of institutions that are appointed by the Governor-General or the Minister generally have their remuneration determined by the Remuneration Authority. In either case, this ensures remuneration levels are set through standardised processes.
38. There would be benefits to ensuring the Governor's remuneration is set through a process that results in consistency with state sector practice. Two alternatives to the current model are:
  - a. The Remuneration Authority could set the Governor's remuneration. In this case the Governor would not be an employee of the Bank.
  - b. The remuneration of the Governor be set by the Board. If a decision were made to shift remuneration decisions to the Board, consideration would need to be given to whether the SSC must consent to the remuneration level.
39. Officials will report back on these matters.

### ***Other information***

40. You have asked for advice on what provisions will be included in the bill regarding removal of the Governor, additional information on subjecting the Bank to review by the Ombudsman, the requirements around performance review for the Bank and information on the process for review of the deposit insurance scheme and implementation of a Government backstop for deposit insurance.

## Governor removal provisions

41. The following paragraphs detail what change will be made to the provisions that allow removal of the Governor under the new legislation. Under the current legislation and in the bill, the Governor-General is able to remove the Governor from office on the advice of the Minister if specified grounds are met. The Board currently has, and will continue to have, a duty to advise the Minister if they consider that the grounds for removal have been met. The Minister currently can, and will continue to be able to, tender advice to the Governor-Governor that the grounds for removal have been met whether or not the Board have provided such advice.
42. Under the current Act, the grounds for removal extend to the Bank not adequately carrying out its functions and improper management of the Bank's resources. Under the bill, the Board will be responsible for ensuring that the entity acts in a manner consistent with its objectives and functions and will be required to ensure that the entity operates in a financially responsible manner. The grounds for removal of the Governor will need to be amended to recognise the shift of these obligations from the Governor to the Board.
43. Table 1 below provides a comparison of the current grounds for removal of the Governor and the proposed grounds under the bill.

Current	Institutional Bill
The Bank is not adequately carrying out its functions	This will be a duty of the Board
The Governor has not adequately discharged the responsibilities of office	This ground will be retained but relate to the responsibilities delegated by the Board
The Governor has breached a duty as a member of the MPC or the MPC has breached a collective duty	This ground will be retained
The Governor has obstructed or prevented the Board or the MPC from discharging its responsibilities	This ground will be retained
The resources of the Bank have not been properly or effectively managed	This will be a duty of the Board
The Governor has held another office for profit, or has an ownership interest in a regulated entity	This ground will be retained
The Governor is unable to carry out the responsibilities of office, or has been guilty of serious neglect of duty, or has been guilty of misconduct.	These removal grounds will be retained (these elements align with the definition of just cause under the Crown Entities Act)

44. Additionally, a person is disqualified from acting as Governor (and deemed to have resigned) if any of the following grounds are met (this will be continued in the bill). The person:

- is a member of Parliament
- is a director or an employee of a regulated entity;
- is a chief executive of a government department or an employee of a government department
- is an undischarged bankrupt
- is a person who is convicted of any offence punishable by imprisonment for a term of 2 years or more
- is a person who is convicted of any offence punishable by imprisonment for a term of less than 2 years and is sentenced to imprisonment for that offence
- is prohibited from being a director, or being concerned or taking part in the management of, an incorporated or unincorporated body, or
- is subject to a property order under the Protection of Personal and Property Rights Act 1988.

*Adding the Bank to Schedule 1 of the Ombudsmen Act*

45. You have asked for more information on the proposal to add the Bank to Schedule 1 of the Ombudsmen Act.

46. The Ombudsmen Act allows the Ombudsman to investigate any decision, act, omission, or recommendation relating to a matter of administration by an organisation in Schedule 1 of the Act. The decision, act, omission or recommendation must affect a person in their personal capacity (this includes non-natural persons). The Ombudsman cannot investigate conduct which is legislative, judicial, or ministerial in nature. In addition, the Ombudsman does not have the authority to investigate a matter where there is a statutory right of appeal or review on the merits to a court or tribunal.

47. An investigation can be due to a complaint, or on the initiative of the Ombudsman. An Ombudsman may obtain information and make inquiries. After having investigated, the Ombudsman must report to the agency in question any conduct which they believe to be:

- contrary to law
- unreasonable, unjust, oppressive, or improperly discriminatory, or was in accordance with a rule of law or a provision of any Act, regulation, or bylaw or a practice that is or may be unreasonable, unjust, oppressive, or improperly discriminatory
- based wholly or partly on a mistake of law or fact, or
- wrong.

48. The Ombudsman may make any recommendations to that agency as they see fit. If the agency does not take appropriate action, the Ombudsman may provide the recommendation to the Prime Minister and the House of Representatives. There is no power for the Ombudsman to compel an agency to take an action.
49. The Ombudsman has a statutory discretion not to investigate complaints in certain cases. This includes if the complainant does not have a sufficient personal interest in the subject matter of the complaint. It cannot be determined in advance how the Ombudsman would exercise this discretion in a particular case. The Office of the Ombudsman has advised that it typically declines to investigate complaints where the complainant has no greater personal interest in the subject-matter than an average New Zealander. For example, the Ombudsman would be able to exercise this statutory discretion in relation to a complaint regarding a decision that does not obviously affect a person in their 'personal capacity', such as a monetary policy decision. Furthermore, it is proposed that the resolution decisions of the Bank in relation to failing entities will be subject to a statutory right of appeal for banks. The statutory right of appeal would limit the Ombudsman's ability to investigate resolution decisions.
50. The Legislative Design Advisory Committee guidelines state that all public bodies should be subject to the Ombudsmen Act unless there is a compelling reason otherwise. This is because the Ombudsmen Act is an important way to hold public bodies to account. A small number of public sector agencies are outside of the Ombudsman's remit for specific reasons, such as where:
- a specific investigatory body exists: for example, the Independent Police Conduct Authority
  - the agency provides legal advice to the Crown, such as the Parliamentary Counsel Office, or
  - the agency is in the form of a trust.
51. None of these reasons apply to the Bank. As the Bank makes a number of administrative decisions, we consider there is a strong rationale to include the Bank in the schedule of entities that can be reviewed by the Ombudsman.

#### *Regular review process*

52. You have requested additional information on whether the bill should provide for a regular process for review of the Bank's operations and performance.
53. It is proposed that the bill brings into force two mechanisms to review the operations and performance of the Bank. First, the Bank would be made subject to the requirements of the Public Audit Act, which allow the Auditor General to examine:
- the extent to which a public entity is carrying out its activities effectively and efficiently
  - a public entity's compliance with its statutory obligations
  - any act or omission of a public entity, in order to determine whether waste has resulted or may have resulted or may result

- any act or omission showing or appearing to show a lack of probity or financial prudence by a public entity or 1 or more of its members, office holders, and employees, and
  - the use of a public entity's resources.
54. It is also intended that a provision equivalent to section 132 of the Crown Entities Act be applied that would allow a responsible Minister to review the operations and performance of a Crown entity at any time. These are standard requirements for Crown entities.
55. While a legislative requirement to regularly review the Bank's performance could have benefits, it could also have a number of downsides – such as the commissioning of more generic reviews not targeted at areas of interest or concern. There are benefits to a flexible approach to monitoring and review, including the timing and nature. This would be consistent with a permissive and flexible approach to the legislation.
56. The proposed power of the Minister to review the operations and performance of the Bank would provide a flexible tool for the Treasury, as monitoring agency, to review the Bank's performance on your behalf. The Treasury will be the monitor for the Bank in the same manner as if the Bank were a Crown entity. The Treasury intends to adopt a robust programme of monitoring – including providing ongoing assurance around the performance of the Bank's functions. The MOU that you sign with the Treasury will outline the approach to monitoring, which may include details as to the regularity of any performance reviews and the nature of on-going monitoring.
57. We do, however, see merit in reviewing the overall institutional framework for the Bank once it has been in force for a period. This will allow us to evaluate the effectiveness of the new institutional arrangements and to ensure no unexpected issues have arisen. To this end, and as part of its role in administering the new Act, the Treasury intends to commit in the Regulatory Impact Assessment to review the institutional framework five years after it has come into force. This approach would be more flexible than a statutory review requirement, allowing the size and scope of the review to adjust to fit the circumstances at the time.

#### *Process for review of the deposit insurance scheme*

58. The Review recommends that the deposit insurance scheme (DIS) should be reviewed several years after the regime has been in place. This would allow for an assessment of how depositors have responded to the new regime, and better measurement of how many depositors are covered. A process for ongoing review of the coverage limit and other aspects of the scheme is also desirable, to ensure that it continues to be aligned with its objectives (including covering the vast majority of depositors).
59. The initial review of the DIS could be part of a wider post-implementation review of the Deposit Takers Act. Following the model proposed for the Institutional Act, the Regulatory Impact Assessment could commit to undertaking a review after a certain timeframe. We will also provide further advice as part of the next stage of public consultation regarding the best approach to ensuring that the



DIS is reviewed from time to time. For example, the agency tasked with governing the scheme and/or the monitoring agency could be required to undertake such reviews, with the Minister of Finance agreeing to any recommended changes.

#### *Government backstop for deposit insurance*

60. A supplementary government funding backstop is necessary to maintain public confidence that the scheme will be able to fulfil its obligations, particularly as it may be many years before industry funding has reached a sufficiently large size. Lessons from the GFC suggest that the backstop should include guaranteed and pre-arranged sources of funding, in order to support public confidence in the scheme during periods of financial stress. A government backstop would also support the usual approach internationally of targeting an industry fund size that is only a portion the total insured deposit base (normally enough funding to pay depositors at a few small banks).
61. The provision of the government funding backstop would be prescribed in legislation. Overseas, sources of emergency funding have included a funding agreement with the government, the central bank, or an authority for the scheme to borrow from the market with a government guarantee. The legislation should also provide that any funds advanced through such an authority could be recouped through recoveries from the failed deposit-taker's assets and, if necessary, additional levies on the remaining industry.
62. We plan to consult on the details of a prearranged and guaranteed government funding backstop early next year. You will receive further advice on the details of this before the end of the year as part of preparation for consultation early next year.
63. A preference for insured depositors would significantly increase recoveries from a failed deposit taker. However this could have unintended consequences and needs to be considered in more detail. We will provide advice on depositor preference next year.