

# The Treasury

## Reserve Bank of New Zealand Institutional Arrangements Information Release

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Chair,  
Cabinet Economic Development Committee

## **Reserve Bank Act Review: Further policy matters for the Institutional Bill**

### **Proposal**

1. This paper seeks agreement on further matters relating to the institutional settings of the Reserve Bank (the Bank), in relation to the Reserve Bank Institutional Bill (the Bill), currently being drafted.

### **Executive summary**

2. In December 2019 Cabinet agreed to replace the Reserve Bank of New Zealand Act 1989 (the Act) with a Reserve Bank Institutional Act and a Deposit Takers Act [CAB-19-MIN-0675]. Cabinet also agreed to the broad parameters of these Acts.
3. This paper seeks additional decisions in relation to the Reserve Bank Institutional Bill. It is intended that this Bill be introduced into Parliament in mid-2020. The Deposit Takers Bill is intended to be introduced into Parliament in 2021. The main additional decisions that this paper seeks are in respect of: the Bank's powers to gather and share information, protections from liability and foreign exchange reserves management. Decisions are also sought on a number of more minor matters.

#### *Information powers*

4. The Bill will carry over the Bank's current power to gather information for the purpose of its central banking functions, with minor amendments. The Bank generally makes use of this power to do surveys of financial institutions, for example, for monetary policy purposes. Cabinet has agreed to broaden the scope of entities that the Bank can collect information from under this power [CAB-19-MIN-0675]. I recommend that the Bank be able to seek information from: financial service providers and entities involved in the distribution and management of cash, as well as entities related to these entities, and anyone who holds information on behalf of those persons. I also recommend that the Bill provide an infringement offence for unintentional non-compliance with information gathering requirements, with more serious intentional non-compliance subject to a criminal offence with higher penalties.

5. I recommend that the Bill include a power for the Bank to share information with a defined set of domestic public agencies involved in financial regulation, and with international agencies with comparable functions. This will support coordination and cooperation of financial sector regulation by reducing administrative burdens to cross agency information sharing.

#### *Protection from Liability*

6. I recommend that individuals acting for the Bank be protected from liability when acting in good faith in the course of the Bank's operations. This is the status quo, and consistent with other Crown entities and protections afforded to state sector employees. I also recommend that the Bank itself be protected from liability when acting in good faith in the course of its operations. This will ensure that the Bank can act without fear of litigation, ensuring it does not act in an overly risk averse manner. This may be important in a failure resolution scenario, where the Bank may need to act quickly and with limited information.
7. The Bank, and individuals acting for the Bank, currently have an indemnity from the Crown for all liabilities arising from actions taken in good faith in the course of the Bank's operation. This indemnity is provided in the legislation. Given the broad protection from liability recommended, this broad indemnity is unnecessary. However, I recommend that an indemnity be retained for liabilities arising in the exercise of the Bank's statutory management powers. This will also apply to statutory managers exercising statutory management powers on behalf of the Bank. This indemnity is justified due to the difficulty in effecting insurance for statutory management activities.

#### *Foreign exchange management*

8. The Bank deals in foreign exchange in order to meet the monetary policy objectives, and also to respond to foreign exchange market dysfunction. In the latter case the Bank currently acts under ministerial direction. Cabinet has agreed that the Bank will have an overarching financial stability objective [CAB-19-MIN-0675]. This will enable the Bank to act independently in a wider range of situations of foreign exchange market disorder. Nevertheless, such actions need to be subject to an appropriate governance framework.
9. I recommend that the Bank's use of foreign exchange reserves be subject to a Reserves Management and Coordination Framework, agreed between the Bank and the Minister of Finance. This framework would clarify the objectives of the Bank holding foreign exchange reserves, set the total level of reserves, and set out how any trade-offs in the use of reserves are managed. This framework would provide greater transparency and accountability as to how the Bank is using reserves, and clarify expectations between the Bank and the Minister. It would replace the power in the Act for the Minister to set the total level of foreign reserves held by the Bank.

## *Other matters*

10. I recommend that the remuneration of the Governor of the Bank be set by the Remuneration Authority. This will ensure the Governor's remuneration is based on objective criteria and consistent with broader state sector practice. The Governor's other terms and conditions of appointment will be set by the Board.
11. I also recommend that the Bank have an enhanced cash management function, to enable it to take a system oversight role in the management of the cash system, including monitoring of the system. This role is important at this point of time given the impacts on society of the declining transactional use of cash.
12. I am also recommending further detail in relation to the decisions Cabinet took in December regarding: the appointment of Board members; the decision-making principles; and the legislative mandate for the Council of Financial Regulators (CoFR).

## **Background**

13. Cabinet agreed in December 2019 to replace the Reserve Bank of New Zealand Act 1989 (the Act) with two new pieces of legislation: a Reserve Bank Institutional Act and a Deposit Takers Act [CAB-19-MIN-0675]. The Institutional Act will provide the Reserve Bank's (the Bank) overarching objectives, governance, operational and accountability framework and central banking functions.
14. This report addresses a number of supplementary decisions required to progress the Reserve Bank Institutional Bill (the Bill). It covers matters that relate to:
  - 14.1. information gathering powers;
  - 14.2. information sharing;
  - 14.3. protection from liability;
  - 14.4. indemnities;
  - 14.5. the management arrangements for foreign exchange reserves;
  - 14.6. the Governor's remuneration and terms and conditions of appointment; and
  - 14.7. the Bank's responsibilities in relation to bank notes and coins.
15. This report also provides further details in relation to previous decisions on:
  - 15.1. the legislative mandate for CoFR;
  - 15.2. the appointment process for the Board; and
  - 15.3. the regulatory decision-making principles.
16. The intention is for the Bill to be introduced in mid-2020.

## Information gathering powers

### *Scope of information gathering powers*

17. Section 36 of the Act allows the Bank to collect information from financial institutions for the purpose of carrying out its central banking functions— such as undertaking monetary policy, dealing in foreign exchange and acting as lender of last resort. The Bank generally makes use of this power through surveying financial institutions.
18. Cabinet agreed [CAB-19-MIN-0675] that this power will be carried over to the Bill, but that the scope of entities that the Bank can gather information from will be broadened. The current restriction to ‘financial institutions’ has proved too narrow at times to enable the Bank to collect all the information it may need to fulfil its central banking functions. For example, it cannot collect information from securities registries, and the power is not sufficiently broad for the Bank to have oversight of entities involved in the distribution of bank notes and coins.
19. In accordance with this Cabinet decision, I recommend that the Bank be able to require, by written notice, the following individuals and entities (persons) to provide information pertaining to the exercise of the Bank’s central banking and financial system oversight functions:
  - 19.1. any financial service provider;
  - 19.2. any person involved in the distribution and management of bank notes and coins;
  - 19.3. any person who holds information relating to, or acts on behalf of, those individuals or entities; or
  - 19.4. a body corporate that is a related party of another body corporate named in 19.1 or 19.2, or was formally a person named in 19.1 or 19.2 in respect of actions of that former person.
20. The information collected must relate to the business of the person, and not to the affairs of a particular customer or client.
21. I recommend that the power will be able to be used by the Bank to collect information for the purpose of its central banking and financial system oversight functions. That is, broadly for the purpose of fulfilling its responsibilities in relation to monetary policy, general central banking functions, monitoring of the cash system and producing the Financial Stability and Monetary Policy Reports. It is intended, however, that the Bank will be able to use the information collected to assist in the performance of any of the Bank’s other functions.

22. The Bank will retain information gathering powers in the sectoral Acts,<sup>1</sup> which allow for collecting information from regulated entities for the purposes of prudential regulation. These information gathering powers will be reviewed, and possibly consolidated into the Institutional Act, as part of work on the Deposit Takers Act.

### *Compliance and confidentiality*

23. I recommend that individuals or entities that fail to supply information when required will be subject to an infringement fee of \$1,000 for individuals, and \$3,000 for entities, with maximum fines of \$3,000 and \$9,000 respectively.<sup>2</sup> These amounts are consistent with Ministry of Justice guidance on infringement offences. Infringement offences provide a mechanism to enforce compliance without subjecting individuals to a criminal conviction. Infringement offences are justified as non-compliance tends to be low level (e.g. missing out information), but can be frequent, and such non-compliance can impact on the quality of data from the survey.
24. For more serious non-compliance, where action is intentional, I recommend keeping a full criminal offence.<sup>3</sup> This would apply in the case of provision of false or misleading information, or failure to provide information where an element of intent is shown. It is recommended that the penalty be between \$100,000 - \$200,000 for an entity and \$20,000 - \$50,000 for an individual. Final penalties will be determined following consultation with the Ministry of Justice during drafting of the Bill.
25. The Act allows the Bank to require that information collected under this power be audited, where the Bank considers that information to be inadequate or inaccurate. It is an offence not to comply with a requirement that the information be audited. I recommend that this provision be amended to allow the Bank to require the person who provided the information to either have the information audited or “reviewed”, if the Bank reasonably considers it to be inadequate or inaccurate. This would be by an auditor or suitably qualified reviewer approved by the Bank, and at the expense of the person providing the information. This allows for a broader range of types of review than just an audit. It would continue to be an offence to, without excuse, fail to undertake the audit or review. It is recommended that the maximum penalty for this offence be the same range as discussed in paragraph 24.
26. I recommend that standard legal protections, such as protection of legal privileges, and the privilege against self-incrimination, will apply to the providers of the information. This would be in a manner similar to that which applies for the Bank’s information gathering powers under the sectoral Acts. This is consistent with the Evidence Act, which provides that no person can be required to provide information which would self-incriminate.

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<sup>1</sup> Deposit Takers Act, Insurance (Prudential Supervision) Act, Financial Markets Infrastructures Act.

<sup>2</sup> The fee is the amount payable on issuance of an infringement notice, and the fine the amount payable if the matter is proved in Court.

<sup>3</sup> A full criminal offence will need to be proved on conviction.

27. The Act currently provides that a person is not excused from supplying any information on the grounds that it would incriminate that person (sections 175A and 175B). It is recommended that these provisions be repealed as they are inconsistent with modern practice.
28. The Bank will be required to keep any information collected confidential, unless grounds for release, similar to those currently applying, are met. These grounds include that the information is in a statistical or summary form, the consent of the person to whom the information relates has been obtained, or release is to someone who has a proper interest.
29. It is recommended that the offence provision for breaching this confidentiality provision be updated in the Bill, such that a person will only commit an offence if they intentionally release confidential information. This is a higher threshold than in the Act, which does not currently require intention. Requiring intent is considered appropriate for constituting a criminal offence, and will also support a more collaborative information sharing culture between agencies. Requiring intent is consistent with the Financial Markets Infrastructure (FMI) Bill.
30. I recommend that the confidentiality provision would overrule where information would otherwise be required to be released under the Official Information Act (OIA). This information would only be able to be released under the OIA if one of the confidentiality grounds discussed above is met. If, however, a ground for release is met, and none of the grounds to withhold in the OIA apply, then the information would be required to be released.
31. The OIA is an important part of New Zealand's public law framework, and should not be limited without good reason. This information gathering power in the Bill will be mostly used to collect statistical information from financial institutions through surveys. Much of this information is sensitive. The proposed approach provides better assurance to respondents that their data is confidential, which will in turn encourage cooperation from respondents. It also ensures that the quality of the statistical results based on the data are high, and not influenced by premature release of preliminary results. The standard withholding grounds in the OIA are not sufficiently tailored to the issues which arise when dealing with statistical data. This is a similar approach taken for Statistics New Zealand. The Office of the Ombudsman has been consulted, and recognises there are countervailing considerations that may justify a limited application of the OIA in this case.

## Information sharing

32. I recommend that the Bank be empowered to share any information (including prudential information) it holds with a defined set of public sector agencies and with equivalent overseas agencies, where it may assist the agency in its functions. This would enable, for instance, the sharing of time-critical information with the Treasury easily in a resolution scenario, or the sharing of information with the Financial Markets Authority (FMA) where both agencies have an interest in a matter. The power would be modelled off the information sharing power in the Financial Markets Authority Act 2011 (FMA Act). The Ministry of Business Innovation and Employment (MBIE) has recommended an equivalent power for the Commerce Commission as part of changes to the Commerce Act.
33. The Bank can currently share information with agencies where it considers that the agency has a proper purpose. This ability is currently provided through an exception to the requirement that would otherwise require the Bank to keep the information confidential. Providing a positively framed information sharing power is considered to enhance the status quo for two main reasons. First, the legislation would provide a defined set of agencies that by default are assumed to have a proper purpose to receive information. This would reduce administrative procedures to information sharing and therefore allow information to flow quickly. Second, providing a positively framed power is likely to support a more open information sharing culture. This power supports the Bank's function to cooperate with other public sector agencies, which Cabinet agreed to in December [CAB-19-MIN-0675].
34. The Bank would not be required to share information with other agencies if it did not consider this appropriate. Further, it is recommended that the Bank be able to impose conditions when sharing that information with another agency, including continued confidentiality, storage, copying, or use, of the information in question. The Bank would also be able to make confidentiality orders, as discussed below. Where information is shared with an overseas agency, the Bank must be satisfied that there are sufficient protections in place to protect the confidentiality of the information. In imposing conditions the Bank must have regard to what is desirable to protect the privacy of any individual. The Office of the Privacy Commissioner considers this sufficient to protect the privacy of personal information.
35. The legislation would define a core set of domestic agencies that the Bank could share information with. This would include, at least: CoFR agencies; Statistics New Zealand and the Director of the Serious Fraud Office.<sup>4</sup> Further agencies would be able to be set by Order in Council, following a recommendation from the Minister. The sharing of this information would be permitted under the confidentiality provisions in the Bank's Acts.

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<sup>4</sup> At the drafting level, Government departments could be set through reference to those departments responsible for the administration of specific pieces of legislation. This list will be refined in drafting.



36. I also recommend that the Bank will have the power to make confidentiality orders. This would be similar to the FMA's power to make confidentiality orders in section 44 of the FMA Act. This would allow the Bank to, on its own initiative or on the application of any person, make an order prohibiting the release of certain information.
37. The indicative penalty recommended for wilful breach of conditions on released information or a breach of a confidentiality order is a penalty similar to equivalent provisions in the FMA Act (\$200,000 - \$300,000).

### **Protection from liability**

38. I recommend that the following persons have a statutory protection from liability when acting in good faith in the course of the Bank's operations, except in relation to certain specified crimes:
  - 38.1. individuals: employees, directors, MPC members, the Governor, statutory managers and investigators acting for the Bank, and
  - 38.2. the Bank.

#### *Protection from liability for individuals acting in good faith*

39. The Act provides that individuals acting on behalf of the Bank will be protected from any liability arising in the exercise of powers under the Act, except when acting in bad faith. Similar protections are provided in the Insurance (Prudential Supervision) Act 2010 (IPSA) and the Non-Bank Deposit Takers Act (NBDT Act) 2013. Such a protection from liability is consistent with the Crown entities framework in regards to directors, employees and office holders, and with protections afforded to public sector employees. It ensures officials acting in good faith can undertake their duties without fear of litigation. I recommend that this protection from liability for individuals be carried over to the Bill. It is also recommended that the Bill consolidate the protection of liability for individuals, and apply across all the Bank's functions, to ensure a consistent approach to all the Bank's functions.
40. One amendment is, however, recommended to the protection from liability for individuals. It is recommended that individuals not be protected from liability for certain criminal offences including: espionage, corrupt use of official information, and corruption or bribery. This would align with the exclusions to the liability afforded in the FMA Act.
41. As is the case for Crown entities, directors would still be able to be removed from office, and are liable to the entity (the Bank) for breach of individual statutory duties. These duties include the duty to act with reasonable care and the duty not to improperly disclose information.

### *The Bank's protection from liability*

42. The Bank itself is protected from liability when acting in good faith, in its capacity as a regulator of insurers or non-bank deposit takers (this is also the position in the FMI Bill). The Bank has no statutory protection when acting as a central bank, or banking regulator (although it does have a Crown indemnity, discussed below). I recommend that the Bill provide the Bank with protection from liability for all its functions. This will ensure that the Bank can undertake its functions without fear of litigation.
43. As discussed, under IPSA and the NBDT Act the Bank is protected from liability when acting in good faith. The FMA and the Commerce Commission, in contrast, are protected from liability, unless shown to have acted in bad faith or *without reasonable care*.
44. I recommend that the Bill provide the Bank with a protection from liability, unless it is shown to have acted in bad faith. This will consolidate the provisions in IPSA, the NBDT Act and FMI Bill into the Institutional Act, and extend the protection to the Bank's banking regulation and central banking functions. However, I recommend that the Bank should not have statutory protection from certain specified crimes, as with the FMA Act. Further, any protection from liability will need be drafted in such a way that it does not reduce parties' incentives to contract with the Bank, or otherwise damage the Bank's commercial activities.
45. Protections from liability must be carefully considered as they impair the ability of individuals and companies to seek redress from the courts when wronged, and could reduce incentives on the Bank to act with reasonable care. Guidance from the Legislation Design Advisory Committee is that any immunity from civil liability should be separately justified and should not be overly broad, as immunities conflict with the central principle that the Government should be subject to the same law as everyone else. If immunities are given, consideration should be given to other ways in which those exercising a power can be held to account.
46. Treasury legal advice is that, if the Bank's protection from liability only applies when the Bank acts with reasonable care (as for the FMA), the Bank would be exposed to a risk of being found liable in negligence under common law. This risk would likely be very small due to the difficulty of bringing successful negligence claims against regulators and supervisors. However, the nature and extent of the risk may change depending on how the law in this area evolves.
47. As noted, I recommend that the Bank have protection from liability, unless shown to have acted in bad faith. This would protect the Bank from actions in negligence. This broad protection from liability is considered justified as it may be particularly important in the context of a crisis event, such as a banking crisis. In such a scenario swift action may be needed on the basis of limited information, and potential liability may be significant. This is different from the situation other regulators may be exposed to, who generally do not deal with systemic crises.

48. Providing a broader immunity would also protect the Bank from future changes in the scope of public authority liability under the common law, and would make clear that the Bank is not subject to the risk of litigation and threats of litigation if exercising its powers in good faith.
49. A number of mechanisms have been included in the Bill to ensure that the Bank can be held to account for its actions, including bringing the Bank within the scope of review by the Auditor-General. Further, the Bank would still be subject to judicial review, and directors would have duties to act in accordance with the legislation the Bank acts under, and with reasonable care. Hence, the overall regime provides sufficient mechanisms to hold decision-makers to account even with this broad protection from liability.

### **Indemnities**

50. I recommend that the Crown indemnify the Bank and statutory managers, through a permanent legislative authority, against any liability that may arise in the good faith exercise of statutory management powers.
51. Under the Bank's Acts, individuals acting for the Bank and the Bank itself are currently indemnified by the Crown, through a permanent legislative authority, for liabilities arising in the course of their duties, provided they act in good faith.
52. The scope of this indemnity is unclear. Further, given the broad scope of the protection from liability for individuals and the Bank proposed above, such a broad indemnity is considered unnecessary.

#### *Indemnities for individuals*

53. For directors, employees and office holders (including the Governor and members of the MPC), it is recommended that the approach in the Crown Entities Act to indemnities and insurance for individuals apply. Individuals would be able to be indemnified or insured by the Bank for all actions, except those done in bad faith.
54. However, I recommend that statutory managers acting in good faith on behalf of the Bank continue to have a permanent legislative indemnity from the Crown when exercising their powers on behalf of the Bank, similar to the provision in section 63 of the Corporations (Investigation and Management) Act 1989 (CIMA). This is because it may be necessary to engage a statutory manager quickly, and it may be difficult to obtain adequate insurance for them. Statutory managers play an important role in the resolution of failed entities, and need to be able to act quickly without fear of personal liability.

### *Indemnity for the Reserve Bank*

55. While a broad indemnity for the Bank is unnecessary, provided the Bank is broadly protected from liability, I recommend that the Bank be indemnified by the Crown for any liabilities that may arise in the good faith exercise of statutory management powers. This indemnity would be provided through a permanent legislative authority.
56. This indemnity would be similar to the existing indemnity for the FMA under section 63 of CIMA. It would apply to the exercise of statutory management powers in respect of any of the Bank's Acts. In the future it could potentially apply to other specified powers that may be exercised in a resolution, such as the bail-in power that is expected to be included in the Deposit Takers Act. It is not intended that this indemnity apply to any liabilities that the Bank may create on its balance sheet to fund loans to financial institutions when, for example, acting as lender of last resort.

### **Foreign exchange reserves**

#### *Current arrangements*

57. Under section 16 of the Act the Bank is empowered to deal in foreign exchange in order to perform its functions and fulfil its obligations. This provision recognises that the Bank may deal in foreign exchange to achieve the monetary policy objectives. In this case dealing in foreign exchange is a monetary policy tool, and the Bank is operationally independent in these dealings.
58. In addition, the Minister of Finance may issue a direction to the Bank under section 17 of the Act to deal in foreign exchange within guidelines prescribed by the Minister. This direction may require the Bank to deal in foreign exchange for an objective different to the monetary policy objectives<sup>5</sup>. If such a direction is considered by the Bank to be inconsistent with the monetary policy objectives, the MPC and the Bank are not required to comply with that direction unless the Governor-General also issues an Order in Council that changes the objectives so that they are consistent with the direction.
59. A direction was issued in 2004 under section 17 of the Act, providing the Bank with delegated authority from the Minister of Finance to intervene in the foreign currency market for the purpose of "stabilising the currency market in situations of extreme disorder". That authority allows the Bank to intervene up to a specified amount (SDR175 million, equal to around 3% of the Bank's foreign currency intervention capacity) for this purpose without further authority from the Minister. The authority only applies when intervention is urgently required, and the Minister is unavailable to be contacted quickly to otherwise give a direction. Under current arrangements, it is expected that non-urgent action to address foreign exchange market disorder would generally be undertaken under the authority and approval of the Minister.

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<sup>5</sup> Maintaining price stability and supporting maximum sustainable employment.

60. In addition, under section 24 of the Act the Minister of Finance is required to set the level of foreign exchange reserves that the Bank holds. The reserves are held for both purposes above; that is for monetary policy and to manage disorder in the foreign exchange market (this is referred to as the 'shared pool').
61. The most recent review of the Bank's foreign exchange market intervention strategy and the level of reserves was in 2004, when the Minister issued the direction discussed above.
62. There are two key issues to address with the current legislative provisions:
  - 62.1.** Current arrangements do not provide clarity on the responsibilities of the Treasury and the Bank in the process for setting reserves, and in particular which agency is responsible for providing advice to the Minister.
  - 62.2.** Cabinet has agreed that the Bank will now have an overarching financial stability objective. In some instances, stabilising the foreign exchange market will be considered a sub-objective of financial stability. Hence the Bank will have greater power to act independently to stabilise the foreign exchange market. However, there needs to be an appropriate governance and accountability framework in regards to foreign exchange management.

#### *Reserves Management and Coordination Framework*

63. To address these issues, I recommend that a modified governance structure for foreign reserves management be included in the Bill. The objectives that this governance structure seeks to achieve are:
  - 63.1.** Ensuring that the Bank has operational independence, and capacity, to deal in foreign exchange to advance all of its statutory objectives (including providing liquidity to disorderly markets, smoothing the exchange rate cycle and potentially undertaking unconventional monetary policy).
  - 63.2.** Ensuring that there is a sound governance framework, and sufficient capacity, to manage foreign exchange market dysfunction.
  - 63.3.** Ensuring that the Government of the day can make choices over the framework for economic policy to maintain democratic legitimacy.
64. I recommend that the Minister and the Bank be required to agree a 'Foreign Reserves Management and Coordination Framework' (RMCF) for the shared pool of foreign reserves that the Bank holds and manages. This would replace the Minister's power to set the total pool of reserves that the Bank holds and manages.

65. The Minister would retain the power in the Institutional Act to issue directions to the Bank to deal in foreign exchange within guidelines. This would now explicitly include a power to direct the Bank to hold a certain level of reserves in order to meet a current or potential direction (in addition to the reserves held in order for the Bank to meet its statutory objectives). Retaining the ministerial direction power recognises the right of the Government of the day to manage economic policy, and provides flexibility to manage unexpected future economic situations or extreme events with broad economic impacts.
66. The purpose of the RMCF is to provide a transparent framework for the management of foreign exchange reserves, the use of which is aimed at advancing the Bank's statutory objectives, and any ministerial direction. The RMCF would therefore be required to be consistent with the Bank's statutory objectives, and any ministerial direction – that is it sets out a framework to achieve those higher level purposes.
67. Broadly the RMCF would be able to cover the following:
  - 67.1.** A framework for the use of the shared pool of foreign reserves in order to advance the statutory objectives, or any ministerial direction.
  - 67.2.** The level of the reserves necessary to advance the statutory objectives and meet any current or potential ministerial direction.
  - 67.3.** Any coordination arrangements with the Debt Management Office.
  - 67.4.** Requirements relating to the publication of information on the management, use and performance of the reserves.
  - 67.5.** The impact of reserve levels on the Bank's capital adequacy, and any associated arrangements.
  - 67.6.** Any other matters agreed between the Minister and the Bank.
68. The RMCF may provide a framework around when a ministerial direction may be issued. This could anticipate, for example, that a direction may be issued in the case of extreme market disorder where there were wide spread economic impacts. However, this would not limit the Minister's power to issue a different direction.

#### *Process for constituting the framework*

69. Transitional arrangements will be included in the Bill in regards to the transition to a RMCF. Broadly, it is intended that current arrangements remain extant until the first RMCF is in place and that the Bill contain procedural requirements relating to the first RMCF, such as requirements as to when the RMCF should be in place by.
70. When the first RMCF is agreed, section 24 of the current Act, which requires the Minister to set the total level of reserves will be repealed. The Bank and the Treasury will work collaboratively to develop advice on the first RMCF, including whether any ministerial directions would be required once the framework is in place.
71. Once a RMCF is in place it will have continued existence but may be amended and would be subject to regular review.

72. The RMCF would also be required to be reviewed if a new foreign exchange ministerial direction is issued. Both parties would be required to take reasonable steps to ensure that the framework is consistent with the direction. The Minister would, however, be able to require changes to the framework if necessary to implement a direction, if changes in regards to a direction were not agreed.
73. In regards to the Minister's power to issue a direction, I recommend that this direction be subject to process requirements regarding review and publication similar to those that apply to directions under section 115 and 115A of the Crown Entities Act.

## **The Governor's remuneration and terms and conditions of appointment**

### *Remuneration*

74. The Act provides that the Governor's remuneration is determined by agreement between the Governor and Minister, following consultation with the Board. This is inconsistent with wider state sector practice. The salaries of all other chief executives that are statutory appointments are determined by the Remuneration Authority. The salaries of the chief executives of Crown entities are determined by the entities' boards, with the consent of the State Services Commission (SSC). Departmental chief executives' salaries are set by the SSC. Furthermore, the current arrangements do not require formal reference to an objective set of criteria.
75. I recommend that the Remuneration Authority determine the Governor's remuneration. The Governor's position will continue to be a statutory position appointed by the Minister. Shifting the Governor's remuneration to the Remuneration Authority would be consistent with state sector practice for statutory appointments. It would also ensure that the salary is based on the objective criteria set out in the Remuneration Authority Act 1977. The Remuneration Authority will also determine the salaries of Reserve Bank Board members. The SSC supports this approach and the Remuneration Authority has advised that this would be consistent with its role.

### *Terms and conditions of appointment*

76. Under the Act, the Minister and the Governor agree on the Governor's terms and conditions of appointment. This is after consultation with the Board. In practice, the Minister relies on advice from the Board in relation to the Bank's policies and procedures and details such as car parking entitlements. The terms and conditions of appointment will generally include organisational policies and procedures.
77. I recommend that in the Bill the Board determine the Governor's terms and conditions of appointment, other than remuneration. This will ensure that the terms and conditions of appointment align with organisational practice and support the Board's governance role, as the Board will largely be determining the role and responsibilities of the Governor.

## **Matters relating to the Bank's responsibilities in relation to bank notes and coins**

78. The Bank's powers and functions in relation to the issuance and oversight of bank notes and coins (cash) will be incorporated into the Bill. This paper addresses some matters in relation to the management of bank notes and coins (the cash system) that are integral to the Institutional Bill.

79. The cash system is a complex network comprised of the Bank and a number of commercial agents, that all contribute to the supply of bank notes and coins to the public. Currently, there are no formally defined roles and responsibilities in the cash system, and no agency has responsibility for taking a system-wide view. It is important that the Bank have a clear role in ensuring the end-to-end functioning of the cash system on a sustainable basis going forward.
80. Further, transactional use of cash has been declining over recent years. This will make it more important for the Bank to have a system oversight role going forward, but may also mean that in the future the Bank might play a larger role in the distribution of cash, for example by owning and operating cash depots.
81. To support the Bank having this system oversight role, I recommend that the Bill contain an expanded function in relation to bank notes and coins. This will recognise the Bank's role in the issuance of bank notes and coins, and also enable the Bank to participate in the distribution of bank notes and coins as necessary to meet the needs of the public. The Bank will also have a function to monitor the financial system, which is intended to also include monitoring of the cash system.
82. The Act contains a number of offences in relation to counterfeit and defacement of bank notes and coins. These will be carried over to the Bill. I intend to recommend to the Minister of Justice that consideration be given to shifting these offences to the Crimes Act at an appropriate time.

### **Further detailed decisions**

#### *Legislative mandate for the Council of Financial Regulators (CoFR)*

83. Cabinet previously agreed [CAB-19-MIN-0675] to “establish a legislative mandate for CoFR that enhances coordination while retaining flexibility and regulators’ statutory independence”. This would ensure that CoFR has an enduring and effective role in achieving good outcomes for New Zealand through the financial regulatory system.
84. Consistent with this decision, the Bill will provide a provision along the lines that the Bank and the FMA must chair CoFR. CoFR would have the purpose of facilitating cooperation and coordination between financial regulators and other agencies to enable effective and responsive financial system regulation.
85. Core CoFR members will be established in legislation and will be the: Reserve Bank, FMA, MBIE and Treasury. Other members, such as the Commerce Commission, will be able to be invited by the Chairs on a permanent or temporary basis.
86. Previously, Cabinet decided that the Bank would have a function to cooperate with other relevant public sector agencies. This function will reference the Bank's role as chair of CoFR. The FMA's function to cooperate will also be amended similarly to reflect its role as co-chair. This will make clear that the Bank and the FMA are expected to exercise their functions to cooperate through CoFR, but not exclusively through CoFR.



### *Appointment of Board members*

87. In December 2019, Cabinet considered a recommendation to establish a nominating committee. The nominating committee would have nominated candidates to the Minister for appointment to the Board by the Governor-General. Cabinet decided to retain the current process for the appointment of Reserve Bank Board members. The current Reserve Bank Board is appointed by the Minister.
88. While the Bank will not be a Crown entity, it will to the extent appropriate be modelled on an Independent Crown Entity (ICE). One of the aims of the review is to harmonise the governance and accountability arrangements for the Bank with wider state sector practice. This is intended to ensure consistency with other state sector entities and provide clarity with regard to the roles and responsibilities of the various parties.
89. I recommend aligning the process for the appointment of Board members with the model for appointing members of an ICE. This involves an additional step in the process previously agreed. ICE board members are appointed by the Governor-General on the recommendation of the Minister.
90. Appointment by the Governor-General on the advice of the Minister would also align with the removal process for Board members. Cabinet agreed that Board members will only be able to be removed by the Governor-General for 'just cause' on the advice of the Minister, and following consultation with the Attorney-General.

### *Decision-making principles*

91. In December 2019, Cabinet agreed [CAB-19-MIN-0675] that the Bill contain decision-making principles that the Bank must have regard to in exercising its regulatory powers under all the sectoral Acts.
92. During drafting a question of legislative design has arisen. This is whether the principles should be located in the sectoral Acts or the Institutional Act. IPSA and the FMI Bill already contain a set of decision-making principles, which address most of the principles that were proposed for inclusion in the Bill. The principles in the FMI Bill would apply to the Bank and FMA as joint regulators.
93. I recommend that the decision-making principles be located in each of the sectoral Acts. This means that the decision-making principles in the December Cabinet paper would be included in the Deposit Takers Act (Annex 1). This ensures that the principles are located in the same Act as the relevant regulatory powers, and allows for differences in principles across those Acts.
94. The current principles in IPSA and the FMI Bill will be retained.<sup>6</sup> These already broadly address most of the decision-making principles that had been proposed for inclusion in the Bill. However, one key principle is not contained in IPSA and the FMI Bill. This is the principle that the Bank consider "long-term risks" when exercising its financial policy powers. A key long-term risk is climate change.

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<sup>6</sup> While the NBDT Act has principles, this Act will be consolidated into the Deposit Takers Act and the principles in the Deposit Takers Act then apply.

95. Risks arising from climate change are highly relevant to the insurance sector, which can, for example, be exposed to property damage coastal erosion. It is less relevant to FMIs, which provide services such as payments and settlements systems. It is therefore recommended that an additional decision-making principle be included in IPSA that requires the Bank to consider long-term risks to the sector. This amendment would be made through the Institutional Bill.

## **Consultation**

96. Treasury and the Reserve Bank jointly developed this policy and provided advice for this paper.
97. The Ministry of Business, Innovation and Employment; the Ministry of Justice, the Office of the Ombudsman; the State Services Commission; the Financial Markets Authority; the Department of Prime Minister and Cabinet; the Parliamentary Counsel Office; the Office of the Privacy Commissioner, and the Commerce Commission were consulted on the proposals in this Cabinet paper.
98. In its feedback the Office of the Ombudsman noted the importance of the OIA within New Zealand's constitutional arrangements, and the principle that the OIA should apply to all new and existing bodies. It also noted the relatively narrow scope of the proposed regime and the specific requirements of statistical information, and understands the exceptional circumstances provide a rationale for limiting the availability of information under the OIA.
99. Two rounds of public consultation have been undertaken on the broad parameters of the Institutional Act.

## **Financial Implications**

100. This paper recommends that the Bill include a permanent legislative authority for a Crown indemnity for liabilities of the Bank and statutory managers that may arise through the good faith exercise of statutory management powers. The existing permanent legislative authority for a Crown indemnity for all liabilities of the Reserve Bank, and Reserve Bank employees and officers, directors, advisory committee members, and appointees will be removed. The proposed indemnity is of narrower scope than the existing indemnity.

## **Legislative Implications**

101. The policy decisions in this Cabinet paper will be implemented through the Reserve Bank Institutional Bill. Parliamentary Counsel Office has started drafting this Bill on the basis of previous decisions made by Cabinet [CAB-19-MIN-0675]. The Bill is planned to be introduced in July 2020.
102. A bid for legislative priority 4 (to be referred to a select committee in the year) was submitted for the Bill.

## Impact Analysis

### *Regulatory Impact Assessment*

103. A Regulatory Impact Assessment has been completed, and has been provided alongside this Cabinet paper. This assessment is an updated version of the Assessment provided alongside the December Cabinet decisions [CAB-19-MIN-0675].
104. This updated Regulatory Impact Assessment includes a Section 3A. This section contains regulatory impact analysis on the Reserve Bank's information gathering and sharing powers, the new Foreign Exchange Reserves Management and Coordination Framework, and the liabilities and indemnities of the Bank. The Assessment also contains new paragraphs on the Reserve Bank's new function in relation to the cash system, and the remuneration of the Governor.
105. Content in the Regulatory Impact Assessment which was used to support December 2019 Cabinet decisions remains unchanged.
106. A Quality Assurance Panel with representatives from the Ministry of Business, Innovation & Employment and the Treasury has reviewed the Regulatory Impact Assessment for the above legislative/regulatory proposal in accordance with the quality assurance criteria set out in the [CabGuide](#). The Quality Assurance Panel considers that the Regulatory Impact Assessment **meets** the Quality Assurance Criteria.

### Climate implications of policy assessment

107. A Climate Implications of Policy Assessment has not been completed as decreasing greenhouse gas emissions is a not key policy objective, and these proposals will not have an impact on emissions.

## Human Rights

108. Policy recommendations in this Cabinet paper have implications for the New Zealand Bill of Rights Act (BoRA). All possible steps have been taken to mitigate inconsistencies with the BoRA, while still allowing for the policy intent. The Ministry of Justice has been consulted, and will be consulted further as the legislation is drafted.
109. I have considered these implications carefully, and I consider any infringements are reasonable limits which are demonstrably justified in a free and democratic society and no broader than necessary. The final Bill will undergo a New Zealand Bill of Rights Act vetting and any unjustified inconsistencies reported to Parliament.

### *The Reserve Bank's information gathering power*

110. The proposed information gathering power of the Bank *prima facie* infringes on the right to free expression, and the right against unreasonable search and seizure. This is justified as an information gathering power is essential for the Bank to perform its central banking functions. Without this power the Bank would not be able to effectively monitor the financial system.

111. It is not intended that the Bank use this power for regulatory purposes. However, it is possible that information gathered under this power will be used to inform the Bank's regulatory functions. To ensure consistency with the New Zealand Bill of Rights Act the Bank will not be able to compel information which is protected by legal privilege, or which would serve to self-incriminate. The existing provisions in the Reserve Bank of New Zealand Act which allows self-incriminating information to be gathered will be repealed. Process requirements will also limit the Bank's use of this power, and information will not be able to be gathered which relates to a particular individual.

#### *The Reserve Bank's protection from liability*

112. The proposed broad protection from liability for the Bank *prima facie* infringes on the right to justice. This would protect the Bank from any civil or non-exempt criminal liability when acting in the course of its functions, powers, or duties. This is a justified limitation, as it is important that the Bank can act without fear of litigation as a regulator. A protection broader than similar regulators is justified due to the particular nature of the Bank's role as a central bank, and the need for it to act swiftly in resolution scenarios.
113. This has been mitigated by the limitation that the protection does not apply where the Reserve Bank has been shown to have acted in bad faith. It also does not apply for certain criminal offences where a protection from liability would not be appropriate. Decisions of the Bank will be amenable to judicial review and the accountability of the Bank has been enhanced through subjecting the Bank to review by the Auditor-General and the Ombudsman. Directors of the Reserve Bank will be accountable to the Bank for a failure to act without reasonable care.

#### **Gender Implications**

114. There are no gender implications for these proposals.

#### **Disability Perspective**

115. There are no disability implications for these proposals.

#### **Publicity**

116. There is no plan for further publicity relating to the decisions in this paper other than as discussed next.

#### **Proactive Release**

117. I am recommending that this paper and Cabinet's decisions be proactively released.

## Recommendations

118. The Minister of Finance recommends that the Committee:

### *Information gathering*

1. agree that the Bank may collect information for the purpose of performing its central banking and financial system oversight functions from any:
  - 1.1. financial service provider
  - 1.2. person involved in the distribution and management of bank notes and coins
  - 1.3. person who holds information relating to, or on behalf of, those persons
  - 1.4. body corporate that is a related party of a body corporate named in 1.1 or 1.2, or was formally a person named in 1.1 or 1.2 in respect of actions of that former person
2. agree that the information collected must relate to the business of the person, and not to the affairs of a particular customer or client
3. agree that a person who fails to supply required information would be subject to an infringement offence with a maximum:
  - 3.1. fee of: \$1,000 for individuals, and \$3,000 for body corporates
  - 3.2. fine of: \$3,000 for individuals, and \$9,000 for body corporates
4. agree that a person who purposefully provides false or misleading information, or purposefully fails to provide information, shall be subject to a criminal conviction with indicative penalties in the range of:
  - 4.1. \$20,000 - \$50,000 for an individual
  - 4.2. \$100,000 - \$200,000 for a body corporate
5. agree that persons who provide information will have standard legal protections from self-incrimination and protection of profession privilege
6. agree that the provisions of the Act that remove person's protections against self-incrimination be repealed (sections 175A, 175B)
7. agree that collected information will be required to be kept confidential, with disclosure being permitted only if specified grounds are met, and that it is an offence for a person to otherwise intentionally disclose confidential information
8. agree that information otherwise required to be released under the Official Information Act would only be able to be disclosed by the Reserve Bank if the specified disclosure grounds referred to in recommendation (7) are met
9. agree that the indicative maximum penalty for the offence in recommendation (7) be broadly aligned with a level 3 offence under the FMI Bill (\$50,000 for an individual)

10. agree that the Bank will be able to require that information collected under this power be audited or reviewed by an auditor, or other suitably qualified reviewer approved by the Bank, where it reasonably considers that information to be inadequate or inaccurate, and that it will be an offence to fail to comply with this requirement
11. agree that the indicative penalty for the offence in recommendation (10) be in the range of:
  - 11.1. \$20,000 - \$50,000 for an individual
  - 11.2. \$100,000 - \$200,000 for a body corporate

#### *Information sharing*

12. agree that the Bank be enabled to share any information it holds with a defined set of agencies, where that information would assist those agencies in the performance of their functions. This would include members of the Council of Financial Regulators, Statistics New Zealand, the Serious Fraud Office, as well as other prescribed agencies
13. agree that release of such information will be permitted under the confidentiality provisions in the Bank's Acts, subject to any conditions the Bill provides for that release
14. agree that the Bank be able to set conditions in relation to shared information, with the penalty for wilful breach of conditions in the range of \$200,000 - \$300,000
15. agree that the Bank be able to put in place confidentiality orders in respect of any information it has released under any provision in the Bank's Acts, with penalties in the range of \$200,000 - \$300,000

#### *Liability and indemnity*

16. agree that individuals acting for the Bank be protected from liability in the course of their duties when acting in good faith, except in relation to specified crimes
17. agree to apply the Crown entities framework for indemnities and insurance to employees, directors and office holders, which allows the Bank to provide an indemnity or effect insurance for civil liability when the person is acting in good faith
18. agree that statutory managers be indemnified by the Crown, through a permanent legislative authority, for any liability arising in the exercise of their statutory management functions when acting in good faith
19. agree that the Bank be protected from any liability when exercising its powers or performing its policy and regulatory functions in good faith, except in relation to specified crimes
20. agree that the Bank be indemnified from liability by the Crown, through a permanent legislative authority, for any liability arising in the exercise of statutory management powers when acting in good faith

21. note that the matter in recommendation (20) will be reviewed again as part of the development of the resolution framework for the Deposit Takers Act
22. agree that the indemnity and liability provisions be consolidated into the Institutional Act

#### *Foreign Exchange Reserves*

23. agree that the Minister of Finance and the Bank be required to agree a Foreign Reserves Management and Coordination Framework (RMCF)
24. agree that the RMCF, once in place, will replace the requirement on the Minister to set the total level of foreign exchange reserves that the Bank holds (section 24 of the Act)
25. agree that the RMCF be subject to transitional arrangements, and that the existing arrangements apply until a RMCF is agreed
26. agree that, the RMCF notwithstanding, the Minister retain the power to direct the Bank to deal in foreign exchange within guidelines, and that such a direction may specify the level of reserves the Bank shall hold to meet this direction or a potential direction
27. agree that this direction power be subject to similar process requirements that apply to directions under section 115 and 115A of the Crown Entities Act

#### *Determining the Governor's remuneration and terms and conditions of appointment*

28. agree that the Governor's remuneration be determined by the Remuneration Authority
29. agree that the Governor's other terms and conditions of appointment be determined by the Board

#### *Bank notes and coins*

30. agree that the Bill recognise an expanded mandate for the Bank in relation to oversight of the system of bank notes and coins, including through the specification of its functions relating to bank notes and coins and monitoring
31. note that current offence provisions in relation to bank notes and coins will be carried over to the Institutional Bill

#### *The Council of Financial Regulators (CoFR)*

32. note that, in accordance with previous Cabinet decisions [CAB-19-MIN-0675], a legislative mandate for the CoFR will be provided along the lines of requiring that the Bank and the Financial Markets Authority (FMA) chair the CoFR with the purpose of facilitating cooperation and coordination between financial regulators and other agencies to enable effective and responsive financial system regulation
33. agree that the Financial Markets Authority Act and the Bill reference the respective roles of the FMA and Bank as Chairs of CoFR in their coordination functions

### *Appointment of Board members*

34. note Cabinet's previous decision to retain the current process for the appointment of Reserve Bank Board members, which involves ministerial appointment [CAB-19-MIN-0675]
35. agree to build upon the decision noted in (34), by providing that the Governor-General will undertake the appointment of Board members, following the advice of the Minister, consistent with the process for Independent Crown Entities

### *Decision-making principles*

36. note Cabinet's previous decision that the Bill contain decision-making principles that the Bank must have regard to in exercising its regulatory powers under the sectoral Acts
37. agree to amend the decision referred to in recommendation (36), to provide that the decision-making principles broadly agreed by Cabinet be located in the Deposit Takers Act and that the existing principles in other sectoral Acts be retained
38. agree that IPISA include an additional decision-making principle that requires the Bank to have regard to long-term risks to the insurance sector when exercising its powers under the Act, to ensure climate change considerations are captured in this Act

### *Further matters*

39. invite the Minister of Finance to issue further drafting instructions to the Parliamentary Counsel Office to give effect to the proposals in this paper
40. agree that the Minister of Finance be authorised to further clarify and develop policy matters relating to the proposals in this Cabinet paper in a manner not inconsistent with the policy recommendations contained in the paper
41. agree that Cabinet's decisions and this paper be publicly released.

Authorised for lodgement

Hon Grant Robertson

**Minister of Finance**



## Annex 1:

### Decision-making principles in the December Cabinet paper

The desirability of minimising unnecessary costs from regulatory actions, taking into account the value of outcomes to be delivered

The desirability of taking a proportionate approach to regulation and supervision, and ensuring consistency of treatment of similar institutions

The desirability that sectors regulated by the Bank are competitive

The value of transparency and public understanding

Practice by relevant international counterparts carrying out similar functions, as well as guidance and standards from international bodies

The desirability of taking into account long term risks to financial stability