The Treasury

Reserve Bank Act Review Phase 2 Consultation 3 Submission Information Release

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Questions for consultation

Chapter 2: Purposes of the Deposit Takers Act

2.A Do you agree with the proposed purposes? If not, what changes would you propose to the purposes? Are there any other purposes that we should be considering?

purpose 1: promote safety and soundness. Consultation 1 extensively covered issues with the term 'soundness' and for this very reason proposed that it not be used. Re-introducing it as a principle in the deposit-takers' act is entirely inconsistent with all of this previous work and should not occur. Stability is a better word for all of the reasons you have outlined in consultation 1. Bonus, it is less jargon-ey.

purpose 2: I agree with this principle

purpose 3: I agree with the essence of this principle, however I think it needs to be broader. The RBNZ should regulate and supervise to protect the financial system (in aggregate) from both:

- risks that may originate *outside* the financial system eg cyber risks, covid and
- risks from within the financial system ie reflecting the interlinkages and macroprudential element

It is important to mitigate the risks both to and from the financial system. For example, Brexit was a political risk that materialized, but the BoE lowered the CCyB to protect the financial system *from an outside risk*, rather than to protect the economy from a financial system risk. The Covid episode has been another risk emerging from outside the system.

Perhaps use your own wording – (page22) "to strengthen the resilience of the financial system as a whole" ?

2.B Do you agree with the proposed decision-making principles? If not, what changes would you propose to the principles? Are there other principles that should be considered?

I agree with these principles. The principle on "the desirability of sectors regulated by the Reserve Bank being competitive, taking account of the size of the market" could more clearly articulate that the RBNZ has a role in *considering* the implications of its actions on competition, but that it has no role in *promoting/increasing* competition . This has been a point of *significant* confusion between agencies in the past with relation to other Bills that should be avoided in future.

Chapter 3: Regulatory perimeter

3.A Do you agree with the proposed approach to defining the overall regulatory perimeter? If not, what approach would you suggest? Yes

3.B Do you support the proposed exclusion for wholesale-only funded lenders? If not, what approach would you suggest?

Yes as described in the diagram (Ie with a maximum size threshold)

3.C Do you support a maximum size threshold for the wholesale exclusion? If so, what would be

an appropriate measure of size? Yes but no comment on what the appropriate size is

3.D Do you agree with the proposed territorial scope of the legislation? If not, what approach would you suggest? *Yes*

3.E Do you have any comments on the application of the Deposit Takers Act to associated persons?

Overall, I agree with setting the regulatory perimeter as described in the decision tree diagram.

3.F Do you agree with retaining the restriction on the use of the words 'bank', 'banker' and 'banking', but limiting it to persons providing 'financial services'? If not, what approach would you suggest? Yes

3.G Do you agree that the use of the words 'deposit', 'deposit taker' and 'deposit-taking' should be restricted? What restrictions would you suggest? yes

3.H Do you support the proposed approach to foreign bank branches? If not, what approach would you suggest?yes

3.I Do you agree that prudential regulation should be retained for finance companies funded via retail debt securities? yes

3.J Would you support the approach of creating a restricted licence category for finance companies funded via retail debt securities (option 1)? What do you think would be the benefits and costs of this approach? Yes, if there are strong and considered restrictions on the sale and labelling of these products. I think the pros of this approach include supporting the diversity of the financial system and financing options, and also future proofing the regulatory regime. The cons relate to complexity. It is hard to know in advance how much extra regulatory complexity would be associated with a separate licensing regime, so any primary legislation should be worded in a way that does not restrict the RBNZ from applying similar standards to those faced by deposit takers.

3.K Under option 1, what restrictions should be placed on the services that a licensed finance company could offer without becoming a full licensed deposit taker?

3.L Should licensed financial market supervisors undertake the frontline supervision of finance companies under this model? If not, what approach would you suggest? Yes

3.M Alternatively, would you support requiring finance companies to have full deposit taking licences to issue retail debt securities (option 2)? What do you think the benefits and costs of this approach would be? No, not flexible or future proofed.

Do you support the proposed approach to small deposit takers, under which the Reserve Bank would be expected to calibrate its regulatory approach in light of the proposed purposes, the decision-making principles, and the contents of the Remit? If not, what changes would you suggest? Yes

3.O Alternatively, would you support creating a separate tier in legislation for small deposit takers? If so, how would you suggest drawing this distinction? No, this would be essentially inconsistent with the decision to create an activities based regime for all.

3.P Do you think the use of the words 'bank', 'banker' and 'banking' should be restricted to a subset of deposit takers? If so, what criteria would be appropriate for their use? No, I think any *deposit taker* should be able to use the term, for the reasons discussed in the Con Doc. Smaller ones arguably do have lower credit ratings, but it is the job of the regulator to balance risks and benefits. Furthermore, presumably all ADIs will need to be part of the DI scheme and (hopefully) also required to implement depositor preference.

3.Q Should current NBDTs have the same supervision, governance and disclosure exemptions from the FMC Act as banks? If not, what approach would you suggest? Yes they should

3.R Should current NBDTs be subject to a disclosure regime that is similar to that for banks? If not, what approach would you suggest? Yes they should

3.S Do you support the proposed approach to perimeter monitoring? If not, what approach would you suggest? I support it

3.T Do you support the proposed designation power? If not, what approach would you suggest? I support the power

3.U Do you support the proposed exemption power? If not, what changes or alternative approaches would you suggest? Yes, and this should be in the act, not in regulations.

3.V What should the criteria be for the Reserve Bank granting an exemption? What other limitations or safeguards should be placed on the power?

Suggesting:

Restriction on RBNZ's exemption power

The RNBZ must not grant an exemption under this subpart unless it is satisfied that—

(a) granting the exemption is necessary or desirable in order to promote the principles and purposes of this Act

(b) the extent of the exemption is not broader than is reasonably necessary to address the matters that gave rise to the exemption.

I don't think that it needs to specifically call out onerous or burdensome requirements, as in the NBDT act, since this is reflected in the purposes and principles (in line with your explanation for why small NBDTs don't need their own subsection).

I do think that (unlike the FMC Act) the section needs to refer to both the purposes and principles, rather than just the purposes. This is because under the proposed DT Act, there is no reference to 'efficiency' etc in the purposes (as there is in the FMC Act). Instead, it is in the principles.

Chapter 4: Standards and licensing

4.A Do you agree that the proposed scope of standards is appropriate? If not, what changes would you suggest? Seems like a reasonable list.

4.B Do you agree with the proposed power for the Reserve Bank to set lending standards (such as LVRs and DTIs) in relation to mortgages? If not, what changes to the scope or additional safeguards would you suggest? Yes, absolutely 100%. And it should be possible to introduce new tools via regulations. I think it's important not to limit the discussion to just DTIs, but to include serviceability instruments more generally.

The government should not be able to limit the RBNZ in the use of these tools, due to housing affordability considerations and the like. An ability to do so would create undesirable incentives for the government, and potentially restrict the RBNZ in achieving its objectives (for example, the government should be incentivized to address difficult issues such as supply constraints, rather than incentivized to limit the RBNZ).

I don't think that 'distributional' consequences are a good justification for government involvement in the use of these tools *for clear financial stability purposes.* There are certainly also 'distributional consequences' associated with financial crises, and also with the government not taking action with the tools *it* has available. The RBNZ would use the tools in accordance with clearly defined objectives, purposes and principles.

4.C Do you agree that the Reserve Bank should be able to issue differing standards for different entity classes? If not, what approach would you suggest? Yes

4.D Do you agree that the Reserve Bank should be able to make standards that enable it to exercise supervisory discretion on matters and within ranges specified in the standards? If not, what approach would you suggest? Yes absolutely.

4.E What procedural requirements and protections should apply to the Reserve Bank's use of supervisory adjustment? There needs to be more detail regarding what would qualify as "circumstances where discretion needs to be exercised urgently in which case these [notification and right of reply] requirements would not necessarily apply". Ie, there need to be clearly defined triggers for operating outside the normal procedure, in the same way that there are triggers for putting entity into resolution.

Furthermore, if an entity submits a response to the proposed action, the Reserve Bank should be required to address entity's submission and why it agrees or disagrees when making its final decision.

4.F Do you support the proposed approach to allowing the Reserve Bank to set reporting standards and lending standards in relation to categories of non-deposit-taking lenders that have been prescribed via regulations? Why or why not? Yes, in accordance with the above discussion on who to license.

4.G Do you agree that the proposed procedural requirements for standards are appropriate? If not, why not? Should any other requirements be considered? Broadly, yes, with the caveat below:

The requirement to consult the government and other government agencies (and take on their feedback) should be no stronger than the requirement to publicly consult (and take on the public's feedback). It should also be limited to issues of substance, as described in the public consultation paragraph. It should only be on the standard (as described in the condoc) and not on the actual setting.

4.H Do you support the proposed licensing test for deposit takers? If not, what approach would you suggest? No comment

4.I Are the proposed procedural requirements for licensing appropriate? If not, why not? Should any other requirements be considered? No comment

4.J What scope of appeal rights should be provided for in relation to licensing decisions and why? I don't know, but agree there is a risk that the High Court would not have the necessary expertise for any review looking at more than just whether processes were followed.

4.K Do you agree with the proposed approach to de-licensing? If not, what changes would you suggest? yes

4.L Do you agree with the proposed use of the register to record and apply standards and other requirements on deposit takers? If not, what approach would you suggest? yes

Chapter 5: Liability and accountability

5.A Do you agree with the general categorisation of the contraventions that should give rise to criminal and civil liability in the Deposit Takers Act? No comment

5.B Do you agree with the specification of the new positive duties for directors of deposit takers? If not, why not? Yes

5.C Do you agree that directors should not be indemnified or insured against loss in the performance of their duties? yes

5.D Do you see any specific issues with the relationship between the existing director duties in the

Companies Act, and the new duties being proposed here? No comment

5.E Do you agree that deemed liability should be retained for false and misleading disclosure? If not, what approach would you suggest? No comment

5.F Do you agree with the proposed approach to maximum civil penalties on bodies corporate, including the use of maximum penalties based on the size of the institution or any benefit gained (or loss avoided)? If so, what specific metrics or amounts should be considered for these penalties? No comment

5.G Should a lower tier of civil penalties be established for some contraventions, for example, those that do not adversely affect the deposit taker's prudential standing? Yes

5.H What maximum level of individual civil penalty should be provided for and why? No comment

5.I Should criminal offences relating to the obstruction of routine supervisory powers be subject to monetary penalties, but not imprisonment terms for an individual? If so, what level of maximum penalty would be appropriate and why? No comment

5.J What monetary and imprisonment penalties should be considered for more serious criminal offences and why? No comment

Chapter 6: Supervision and enforcement powers

6.A Do you agree that the on-site power for the AML/CFT regime is an appropriate comparator for a similar power for the Reserve Bank's prudential functions? Yes

6.B Should this power be a generic power in the new Institutional Act, or specified in the Deposit Takers Act? Generic

6.C Do you think any additional safeguards are necessary for the on-site power? No comment

6.D Do you think the FMA's on-site inspection power should be expanded in the same way that is proposed for the Reserve Bank? Yes

6.E Should an expanded FMA on-site inspection power apply in all circumstances and to all FMAregulated entities or only some (e.g. in high-risk circumstances or for dual prudential-conduct regulated entities)? No comment

6.F Do you have any comment on the appropriate legislative location of supervisory powers such as information gathering and sharing, on-site inspections, and other related powers? Do you

see merit in consolidating similar powers from sectoral Acts into the Institutional Act? Yes I see merit in consolidating BAU powers that apply across sectors in a single Act.

6.G Should a breach-reporting requirement be directly provided for in legislation? Should this be provided for in the Deposit Takers Act, or located in the Institutional Act as a requirement for all entities regulated by the Reserve Bank? I am not convinced this needs to be in primary legislation.

6.H Do you agree that the Deposit Takers Act should provide for the Reserve Bank to accept a voluntary undertaking from a deposit taker that is enforceable in court? Yes

6.I Should the Deposit Takers Act provide a statutory basis for the Reserve Bank to issue a formal notice to a deposit taker? Yes

6.J Do you see any role for infringement notices in the Deposit Takers Act? No comment

6.K Do you see a useful role for remedial notices and/or action plans in the Deposit Takers Act? Yes

Chapter 7: Resolution and crisis management

7.A What are your views on the proposed triggers for placing a deposit taker into resolution and exercising resolution powers? I agree with them, but the FSB Key Attributes wording is fine, it does not need to be reframed as a 'viability and necessity test'.

7.B What should be the scope of statutory bail-in in New Zealand? What liabilities should be expressly included or expressly excluded? How should deposits be treated? New Zealand should take a 'broad' approach, ie have a 'negative list' of what is excluded from bail in. It would be a more future-proofed approach, and also arguably more transparent. This also decreases the case for retrospective application.

Uninsured deposits can be subject to bail in (assuming that the only alternative is liquidation, and that a NCWO safeguard applies).

7.C Should statutory bail-in have retrospective application? Firm no.

7.D Is there still a role for a ministerially-appointed advisory committee to a statutory manager? If so, should legislation be more specific about the purpose and the composition of that committee? No.

- Firstly, it is unclear what the purpose of this committee would be – it seems backward to decide that there should be a committee before deciding what it would do.
- Second, at best it seems like duplication of expertise – surely the resolution authority would appoint the most capable statutory manager possible. Furthermore, as far as I understand, there is also nothing stopping the RA from obtaining external advice?

- Third, it seems an inappropriate political encroachment on the independence of both the resolution authority and the statutory manager (also impractical given the legal duty of the statutory manager to the interests of the company in SM).
- Fourth, it seems unnecessarily complex with no clear benefit. Having another actor could slow a lengthy resolution down even further. There would be no benefit due to points 2 and 3 and the fact that this committee would have no statutory powers. (If it were given statutory powers, this would contradict the FSB Key attributes).

7.E Should the Reserve Bank have the power to demutualise a building society or credit union that meets the criteria for being placed into resolution? No comment

7.F Do you agree that deposit takers should only be subject to one statutory management and resolution regime? Not necessarily, see question 7G. I don't think that retaining the status quo would be inconsistent with international best practice of guidance, as long as the RBNZ's powers are aligned with such guidance. There is no 'harm' in leaving the power in CIMA, acknowledging that it is very unlikely it will ever be used ahead of the RBNZ's powers. Conduct issues that may lead to statutory management are *unlikely* to not also affect prudential viability, however, the two regimes seem more future proof at low 'cost'.

7.G Do you favour option 1, option 2, or some other approach (including the status quo)?

I favour either option 2 or the status quo.

Chapter 8: Depositor protection

8.A What are your views on the benefits and costs of a preference for insured depositors compared to no preference? I strongly support depositor preference.

8.B If a preference for depositors is introduced, do you agree it should only cover insured deposits (not all deposits)? I do not think it should be limited to insured deposits, because the insurance limit in New Zealand will be low (and is arguably not very future proof). Not limiting preference would enhance financial stability because:

- It would shift market discipline responsibility towards those that are actually equipped with the expertise to exert it. If anything, large retail account balances would indicate a *lack* of financial literacy, as those that are literate would split accounts!
- It would reduce run risk (retail deposits form a large part of bank funding, but there does not seem to be much evidence of retail depositors exerting market discipline, or even *knowing* their deposits might be at risk).

Another example/ reason is that the more time goes by, the more people will have high kiwisaver balances, potentially resulting in a greater number of large account balances for New Zealanders 65+. These are people who will have next to no employment prospects, and almost certainly won't be 'exerting market discipline by monitoring their banks on balances over $50,000'. For retirees, being left with 50,000 to last an increasingly large number of retirement years would result in financial hardship.

8.C Do you agree with the proposed prescribed product approach for coverage under the new

scheme? If not, what approach would you suggest?

Yes to both the approach (outlining coverage in regulations) and the description. The scheme should not cover investment products that are subject to FMC Act disclosure requirements, such as retail bonds, debentures, and capital notes. These are reasonably sophisticated investment options, make up a small portion of retail liabilities, and are not used for everyday spending.

8.D Do you agree that both retail and wholesale investors in insured deposit products should be

covered up to the $50,000 coverage limit? If not, what approach would you suggest? No. Absolutely not. This should be a retail insurance scheme. Wholesale investors are equipped to exert market discipline. Including them in an insurance scheme would increase moral hazard. Also! This is an even more outrageous suggestion in the context of the preference discussion in 8A and 8B. It would mean that wholesale depositors' first $50,000 would be preferred over ordinary retail depositors' savings above $50,000!!

8.E Is the list of excluded deposit products appropriate? If not, what approach would you suggest? Yes.

8.F Do you agree with the proposed narrow mandate for the deposit insurer? Yes

8.G Do you agree that the deposit insurer should be able to provide funding for resolutions other

than a liquidation? Yes

8.H If yes, do you agree with the limit on the amount of funds that can be used? What are your

views on the appropriate safeguards? Yes

8.I What are your views on the appropriate decision authority for the coverage limit? Regulations, ie Ministerial control. In all likelihood, the circumstances in which the Government may wish to change the coverage limit would be in the heat of a crisis, when time is of the essence. In these instances, the regulation model would be more efficient. It would of course be possible to make changes under the primary legislation model too. However, in my opinion this would be inferior as it would introduce unnecessary complexity and process, with little practical gain in terms of accountability.

For example, in a crisis, any changes to primary leg would likely be passed under urgency anyway. Ie, it would still have to go through the house (extra process) without going through select committee (where genuine policy debate may occur), as was the case with the RDGS (appropriate at the time). Furthermore, if the government did wish to change the limit, this would likely be in the interests of financial stability (since the original $50k already covers short term hardship). The ability to maintain financial stability and prevent runs is paramount in a crisis.

8.J If a deposit insurance fund is established, should changes to the target size and the levies be

made by ministers via regulations or by the deposit insurer itself? I don't know – the paragraph doesn't really outline pros and cons. As you say, it depends on how tightly the criteria can be described. I think there is a case for investigating whether it would be possible to describe criteria tightly enough to delegate decisions to the independent regulator. Otherwise, decisions should be by the Minister on the recommendation of the regulator/ insurer. What do other countries do? Either way, I do agree that there should be strict decision-making criteria, as there may be a risks of lobbying and 'disaster myopia'.

8.K Should there be a legislated requirement to review the deposit insurance scheme? If so, how often should it be reviewed (e.g., every five years)? Yes, every 10 years. Every 5 years would be too frequent – these things can take a while and doing them too frequently runs the risks of either

- of being in a near constant state of review, or
- disruptive to organizations (requiring a new team every couple of years), or
- turning reviews into a check-box exercise.

8.L Do you agree that the insurer should build a deposit insurance fund ahead of a failure? If not, what approach would you suggest? Absolutely yes.

8.M What are your views on the appropriate size of any deposit insurance fund? …. ? I think that this should be decided in accordance with the decision in 8J. It (obviously ?) shouldn't be to cover the entire banking system, or even the expected LGD of all NZ banks. The fund should maybe aim to cover the expected LGD of one major bank, accounting for fund investments and operating costs of the fund.

8.N Should the insurer charge higher levies to higher risk deposit takers? What are your views on how risk should be assessed? No. What is a 'high risk deposit-taker' in the context of an ADI regime? They will all be under equivalent prudential regimes (as much as possible, accounting for competition etc considerations). It would be the role of the prudential regulator to make an appropriately 'safe' prudential regime.

8.O Do you agree that the insurer should build a deposit insurance fund ahead of a failure? If not, what approach would you suggest? Repeated question

8.P What are your views on the appropriate size of any deposit insurance fund? Repeated question

8.Q Should the insurer charge higher levies to higher risk deposit takers? What are your views on how risk should be assessed? Repeated question

8.L Has the Review identified the appropriate criteria for assessing the best organisational form of the insurer? No comment

8.M Do you agree that the insurer should be located within the Reserve Bank? If not, what approach would you suggest? Yes.