

# The Treasury

## Reserve Bank Act Review - Deposit Takers Bill Information Release

April 2021

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### Cabinet Document Details

Title: **Cabinet Minute DEV-21-MIN-0077: Cabinet Economic Development Committee: Minutes of Decisions for Reserve Bank Act Review**

Date: **14 April 2021**

Creator: Cabinet Office

**No information has been withheld**

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# Cabinet Economic Development Committee

## Minute of Decision

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### Reserve Bank Act Review - Deposit Takers Bill: Prudential Framework (Paper 2)

Portfolio                      Finance

On 14 April 2021, the Cabinet Economic Development Committee (DEV):

#### Purposes and principles

- 1        **noted** that:
  - 1.1     Phase 1 of the Review of the Reserve Bank of New Zealand Act 1989 (the RBNZ Act) introduced a new purpose statement to ‘promote the prosperity and well-being of New Zealanders and contribute to a sustainable and productive economy’;
  - 1.2     this purpose statement will remain in the new RBNZ Act, and recognise that monetary and financial policy are not ends in themselves, but are means to improve the prosperity and well-being of New Zealanders;
- 2        **noted** that on 11 December 2019, DEV agreed that the new RBNZ Act’s financial policy objective will be to ‘protect and promote the stability of New Zealand’s financial system’ [DEV-19-MIN-0345];
- 3        **noted** that on 11 December 2019, DEV agreed that the new RBNZ Act will require the Minister of Finance to issue a Financial Policy Remit, and that the board of the Reserve Bank must have regard to it when pursuing the financial stability objective – specifically when acting in relation to the Reserve Bank’s strategic intentions and the setting of prudential requirements [DEV-19-MIN-0345];
- 4        **agreed** that the purposes of the proposed Deposit Takers Bill (the DTA) be designed to achieve the following objectives:
  - 4.1     the promotion of the safety and soundness of deposit takers;
  - 4.2     the promotion of the public confidence in the financial system;
  - 4.3     the mitigation of risks that arise to and from the financial system;

and that, in doing so, contribute to protecting and promoting the stability of New Zealand's financial system;

- 5 **noted** that in addition to the general purposes in the DTA, there will be part-specific purposes (for example, the protection of depositors in the context of deposit insurance);
- 6 **agreed** that the Reserve Bank be required to take into account principles (to the extent they are relevant) when exercising its powers under the DTA. It is anticipated that the principles would be along the following lines:
- 6.1 the desirability of minimising unnecessary costs of regulatory actions;
  - 6.2 the desirability of taking a proportionate approach to regulation and supervision, and ensuring that similar institutions are treated consistently while recognising the diversity of institutions;
  - 6.3 the need to maintain competition within the deposit taking sector;
  - 6.4 the value of transparency and public understanding of the Reserve Bank's objectives and how the Reserve Bank's functions are exercised;
  - 6.5 consideration of the practice by relevant international counterparts carrying out similar functions, as well as guidance and standards from international bodies;
  - 6.6 the desirability of ensuring that long-term risks to financial stability are well managed;

### **Regulatory perimeter**

- 7 **confirmed** Cabinet's in-principle decision to merge New Zealand's two existing prudential regimes for regulating banks and non-bank deposit takers into a single deposit-taking regime [DEV-19-MIN-0161];
- 8 **agreed** that the DTA provide for a single, flexible licensing regime that requires deposit takers to be licensed by the Reserve Bank;
- 9 **agreed** to an activity-based regulatory perimeter that captures as deposit takers persons carrying on the business of borrowing and lending, excluding some types of wholesale funded lenders and firms subject to existing Non-Bank Deposit Takers Act 2013 exclusions and exemptions;
- 10 **noted** that while the scope of the wholesale lender exclusion will be further tested and refined through the drafting process, it is expected to exclude lenders that solely borrow on wholesale capital markets, from financial institutions, or from associated persons;
- 11 **agreed** that a financial service provider that is not licensed as a deposit taker may not hold itself out to be a licensed deposit taker;
- 12 **agreed** that no financial service provider may use the words 'bank', 'banking' and 'banker' (restricted words) when carrying on activities in New Zealand, except for licensed deposit takers or persons licensed or registered as a bank in a country other than New Zealand that, in each case, have been authorised by the Reserve Bank to use restricted words;
- 13 **agreed** that the Reserve Bank will publish a policy framework under which it will authorise the use of restricted words, including setting out the minimum authorisation requirements for deposit takers (such as financial strength requirements);

- 14 **agreed** that the disclosure, governance and trustee supervision exclusions from the Financial Markets Conduct Act 2013 that currently apply to registered banks should be extended to all licensed deposit takers;
- 15 **agreed** that the DTA will allow the Reserve Bank to monitor, through information gathering powers, non-deposit taking lenders for financial stability risks and identify entities that should be designated as deposit takers for the purposes of the DTA;
- 16 **agreed** that the Reserve Bank be empowered to designate an entity as a deposit taker for the purposes of the DTA where the services it provides are the same, or substantially similar, in economic substance to carrying on the business of borrowing and lending;

## Standards and licensing

- 17 **noted** that on 11 December 2019, DEV agreed in principle, subject to further policy development, that:
- 17.1 ‘standards’ set by the Reserve Bank will be the primary tool for imposing regulatory requirements on deposit takers, with a high degree of flexibility to tailor requirements to individual deposit takers and classes of deposit takers;
- 17.2 the prudential framework will provide the scope of matters that the Reserve Bank will be able to set standards on, with the ability for the Minister to add additional matters to which standards can relate via regulations;
- 17.3 requirements that impact on the rights of individuals to be provided for in primary legislation, in particular, fit and proper requirements for directors and senior executives;

[DEV-19-MIN-0346]

## Scope of standards

- 18 **confirmed** Cabinet’s in-principle decision that the Reserve Bank be empowered under the DTA to set regulatory requirements for deposit takers by secondary legislation (prudential standards);
- 19 **agreed** that the subject matter of prudential standards be specified in the DTA, and may encompass:
- 19.1 the current conditions of registration;
- 19.2 the matters listed in sections 73-73B and section 78 of the current Reserve Bank of New Zealand Act 1989;
- 1.1 compliance with the range of matters in the Reserve Bank’s Banking Supervision Handbook;
- 19.3 the Basel Core Principles of Effective Banking Supervision;
- 19.4 any other matters prescribed by regulations;
- 20 **noted** that it is anticipated that the subject matter of standards will include the matters that are to be taken into account when licensing deposit takers;
- 21 **agreed** that the subject matter of prudential standards will include lending requirements (e.g. loan-to-value and debt-to-income ratios);

- 22 **agreed** that the permitted scope of lending standards be set by regulation, and that this will be confined to types of lending (e.g. residential mortgage, rural, commercial property);
- 23 **agreed** that a regulation pertaining to lending standards can be made by the Governor-General by Order-in-Council on the advice of the Minister of Finance after consultation with the Reserve Bank;
- 24 **confirmed** Cabinet's in-principle decision that additional matters that may be covered by prudential standards may be prescribed by regulations recommended by the Minister;
- 25 **agreed** that the DTA should allow the Reserve Bank to set reporting and lending standards in relation to categories of non-deposit-taking lenders prescribed by regulation;
- 26 **noted** that the DTA will not provide the Reserve Bank with the power to impose standards on associated persons of licensed deposit takers, except in relation to paragraph 25 above;
- 27 **agreed** that standards may apply to all licensed deposit takers, specified classes of licensed deposit takers, or one or more specified licensed deposit takers;
- 28 **agreed** that the requirements imposed on a licensed deposit taker under standards may be modified by administrative instruments (e.g. licence conditions or exemptions), subject to appropriate safeguards;

### Process for setting standards

- 29 **agreed** that the following procedural requirements would apply before a standard may be issued by the Reserve Bank:
- 29.1 a requirement to consult with members of the Council of Financial Regulators;
- 29.2 a requirement to consult affected persons (except for minor amendments to standards, when consultation could be limited to substantially affected persons);
- 30 **noted** that standards, as secondary legislation, will be subject to Parliamentary disallowance (section 115 of the Legislation Act 2019);
- 31 **noted** that the Reserve Bank of New Zealand Bill:
- 31.1 requires the Reserve Bank to assess and publish the expected regulatory impact of any policy adopted under prudential legislation, which will include the development of standards under the DTA (except of a minor or technical nature);
- 31.2 sets requirements around the content of the regulatory impact assessment for standards, including how the Board has had regard to the Minister of Finance's Financial Policy Remit;
- 32 **agreed** that there be a statutory requirement for the Reserve Bank to inform the Minister of Finance of key policy changes, other than those of a minor or technical nature;

### Licensing

- 33 **agreed** that a person will be entitled to be issued with a licence if the Bank is satisfied as to specified matters, such as the ability to comply with the DTA, applicable standards, and any proposed licence conditions;

- 34 **agreed** that the fitness and propriety of directors and senior managers of an applicant be a matter that the Reserve Bank must be satisfied of before a person is entitled to be issued with a deposit taking licence;
- 35 **agreed** that the Reserve Bank be required to follow appropriate procedural requirements before deciding on entitlement to a license, including consultation with the Financial Markets Authority;
- 36 **agreed** that the Reserve Bank will have powers to establish licensing conditions, specific to licensed deposit takers, and that it is anticipated that licensing conditions may be used to apply to standards and relate to the licensing matters and the types of conditions that may be imposed under the Non-Bank Deposit Takers Act 2013 and Insurance (Prudential Supervision) Act 2010;
- 37 **agreed** that Reserve Bank approval be required before a person (or persons acting together) obtains a controlling interest in a licensed deposit taker;
- 38 **agreed** that the DTA will include appropriate de-licensing powers, including the circumstances under which the licence of a deposit taker may be revoked;

### **Transparency requirements**

- 39 **noted** that the Reserve Bank of New Zealand Bill requires the Reserve Bank to publish Statements of Prudential Policy in order to provide transparency about how it acts as a prudential regulator and supervisor under prudential legislation;
- 40 **agreed** that the Reserve Bank be required to publish in its Statement of Prudential Policy its policies in relation to how it acts, or proposes to act, in relation to its administrative decision-making, such as imposing, modifying or removing conditions of licence or granting exemptions from requirements imposed by standards;
- 41 **agreed** that the Reserve Bank must keep a public register of licensed deposit takers, with prescribed content requirements;

### **Fit and proper**

- 42 **agreed** that the DTA provide fit and proper requirements for directors and senior managers of deposit takers in line with the fit and proper framework contained in the Insurance (Prudential Supervision) Act 2010, with any necessary or desirable modifications, for example:
- 42.1 that the Reserve Bank's approval be required prior to the appointment by the deposit taker of a director or senior manager;
- 42.2 that deposit takers be required to notify the Reserve Bank of significant issues that may affect the fitness and propriety of directors and senior managers as and when they occur;

### **Previous decisions on liability, accountability, supervision and enforcement**

- 43 **noted** that on 11 December 2019, DEV agreed in principle, subject to further policy development, that:
- 43.1 accountability requirements will be enhanced for directors of deposit takers established through broad positive duties, with civil penalties as the primary sanction for non-compliance;

- 43.2 subject to further advice from a cross-agency process separate from the Phase 2 Review, integrated prudential-conduct executive accountability regime which extends accountability requirements to include certain senior employees of deposit takers and insurers will be developed;
- 43.3 the Reserve Bank will have a power to undertake on-site inspections of any licensed deposit-taker, and any other regulated entity as appropriate;
- 43.4 the Reserve Bank will be able to issue directions to a deposit taker without Ministerial consent but subject to appropriate thresholds, and to delicense a deposit taker without a ministerial direction;
- 43.5 a more graduated enforcement and penalty framework will apply, with a broader range of potential sanctions than the current Reserve Bank Act, such as statutory public notices, infringement fees, enforceable undertakings, and civil pecuniary penalties;

[DEV-19-MIN-0346]

### Director accountability

- 44 **agreed** that directors of licensed deposit takers will have a new due diligence duty to ensure there are adequate systems, processes and policies in place so that the deposit taker complies with its prudential obligations, and that there will be a civil pecuniary penalty for breach of this duty, subject to appropriate defences;
- 45 **agreed** that a licensed deposit taker will not be able to insure or indemnify a director against a breach of the due diligence director duty, and that any such insurance or indemnification would be ineffective;
- 46 **noted** that directors would be able to insure themselves personally against insurable risks (such as a civil pecuniary penalty) in their capacity as directors of a licensed deposit taker;
- 47 **noted** that this duty will exist alongside other director duties, including fiduciary duties to the company under the Companies Act 1993, and duties under the Financial Markets Conduct Act 2013 and the Credit Contracts and Consumer Finance Act 2003;
- 48 **agreed** that licensed deposit takers may be liable to a civil pecuniary penalty if false or misleading information is given to the Reserve Bank or publicly disclosed and that, if such a penalty is imposed on a licensed deposit taker, the directors of that licensed deposit taker will be treated as having contravened the requirement in such a case and be liable for a pecuniary penalty, subject to appropriate defences;
- 49 **noted** that this due diligence duty may be incorporated into a future executive and director accountability regime agreed to in principle by Cabinet, to be progressed by Council of Financial Regulators agencies separately from the Review of the Reserve Bank Act;

### Supervisory powers

- 50 **noted** that:
- 50.1 the Reserve Bank will be empowered with flexible regulatory tools, which can be used expeditiously and with efficacy to promote financial stability;
- 50.2 the extent, scope, and use of these powers will need to be clear and well justified to provide certainty and legitimacy;

- 51 **noted** that:
- 51.1 the Reserve Bank's functions under the Reserve Bank of New Zealand Bill will include acting as a prudential regulator and supervisor, and that the supervisory powers under the DTA can be exercised as necessary or desirable to carry out this function;
- 51.2 the Reserve Bank will also be able to use these powers in its deposit insurance role;
- 52 **agreed** that the Reserve Bank will have a power to gather information from financial service providers, associated persons of financial service providers, and other appropriate persons;
- 53 **agreed** that the Reserve Bank will have a power to require a licensed deposit taker to produce a report on a matter relating to its business, operations, or management, or those of an associated person, to be carried out by a qualified person approved by the Reserve Bank;
- 54 **agreed** that the Reserve Bank will have a power, at any reasonable time, to, without notice, enter and remain on the premises of a licensed deposit taker for the purpose of conducting an on-site inspection to carry out prudential supervision and monitor the deposit-taker's compliance with obligations imposed under the DTA;
- 55 **agreed** that the Reserve Bank will have the power to carry out on-site inspections of insurers licensed under the Insurance (Prudential Supervision) Act 2010 comparable to the on-site inspection power for licensed deposit takers;
- 56 **noted** that the power to conduct on-site inspections is not intended to be a search and seizure power;
- 57 **agreed** that, during an on-site inspection, an employee, an officer or agent of a licensed deposit taker may be required to answer questions and provide any other information that may reasonably be required for the purpose of the inspection;
- 58 **noted** that the Ministry of Business, Innovation and Employment will seek the Minister of Commerce and Consumer Affairs' approval to undertake further targeted consultation on a potential on-site inspection power for the Financial Markets Authority, for the purpose of alignment between twin peaks regulators, with a view to seeking final policy decisions through the second tranche of DTA policy decisions;
- 59 **agreed** that the Reserve Bank may require the production of information and appoint a qualified person to carry out an investigation into the affairs of a licensed deposit taker or associated person for the purpose of investigating conduct that constitutes, or may constitute, a contravention of an obligation imposed under the DTA;
- 60 **agreed** that a person appointed by the Reserve Bank to investigate whether a person is contravening, or has contravened, an obligation imposed under the DTA, may enter and search any place if the occupier of the place consents or the person obtains a warrant;
- 61 **agreed** that licensed deposit takers be required to report to the Reserve Bank breaches of obligations imposed under the DTA;
- 62 **noted** that the Reserve Bank will not be permitted under the DTA to compel privileged, or self-incriminatory information from individuals;
- 63 **agreed** that information connected with the use of the Bank's powers, and derived information that a licensed deposit taker is required to provide to the Reserve Bank must be kept confidential, and only be released in prescribed circumstances;



- 64 **noted** that the Reserve Bank will be able to share information with relevant agencies, such as the Financial Markets Authority, using the information sharing power in the Reserve Bank of New Zealand Bill;
- 65 **noted** that the exercise of supervisory powers will be subject to appropriate procedural constraints, in accordance with natural justice requirements;

### Enforcement powers

- 66 **agreed** that the Reserve Bank have a power to direct licensed deposit takers to take specified actions (the scope of this power is discussed in Paper 4 under DEV-21-SUB-0079);
- 67 **agreed** that the Reserve Bank have the power to make an order prohibiting the publication or communication of any information relating to the exercise of supervisory and enforcement powers under the DTA;
- 68 **agreed** that the Reserve Bank may require the preparation and implementation by a licensed deposit taker of a plan setting out how it would avoid, mitigate or remedy a contravention, or potential contravention, of its prudential obligations under the DTA;
- 69 **agreed** that the Reserve Bank may accept a written undertaking from any person in connection with compliance with any obligation imposed under the DTA, and have the power to apply to the court to enforce the undertaking and order appropriate remedies for breach of the undertaking, including the payment of an amount up to the amount of any benefit that the person obtained that is reasonably attributable to the breach;
- 70 **agreed** that the Reserve Bank be able to require that a licensed entity publicly display a notice or warning issued by the Reserve Bank;

### Penalties and offences

- 71 **agreed** that civil pecuniary penalties may be imposed by the court (with a civil standard of proof) for a contravention of a requirement or obligation under the DTA;
- 72 **agreed** that the Reserve Bank may apply for a civil pecuniary penalty order against any person who has contravened, or has been involved in a contravention, of a requirement or obligation under the DTA;
- 73 **agreed** that the DTA include guidance to assist the court in determining the size of a pecuniary penalty in individual cases, including factors such as the extent of cooperation with regulators, or the recommendation of the Reserve Bank;
- 74 **agreed** that intentional or reckless non-compliance with the Reserve Bank's supervisory and enforcement powers be a criminal offence;
- 75 **agreed** that the DTA include a criminal offence for intentionally misleading the Reserve Bank;
- 76 **agreed** that the DTA provide for administrative penalties (i.e. infringement notices imposed under the procedure provided in the Summary Proceedings Act 1957) to deter conduct that is of relatively low seriousness, such as failure to supply information to the Reserve Bank;
- 77 **agreed** that further detail of the proposed offences and penalties be developed by the Minister of Finance under Cabinet's delegated authority provided in Paper 1 under DEV-21-SUB-0076, and that penalty levels would be comparable with the conduct and competition regimes and could be significant;

## Appeal rights

### Appeals from fit and proper decisions

78 **agreed** that the decision by the Reserve Bank to not approve a proposed director or senior manager, or to remove a director or senior manager, be subject to appeal by the affected person to the High Court and that the appeal be by way of a rehearing;

### Appeals from decisions to decline a licence

79 **agreed** that the decision by the Reserve Bank to not grant a deposit taker licence be subject to appeal by the licence applicant to the High Court, and that the appeal be by way of a rehearing;

### Appeals from decisions affecting the rights and interests attaching to deposit taking licences

80 **agreed** that decisions under the DTA affecting the rights and interests that attach to deposit taking licences (i.e. conditions of licence, changes to the licence holder (approvals of change of ownership, corporate form etc) and approvals to carry on or cease carrying on certain activities) be subject to appeal on questions of law, with the decision appealed against continuing in effect until the appeal has finally been disposed of, unless the Court orders otherwise;

### Appeals from decisions by the Resolution Authority

81 **noted** that appeal rights for decisions made by the resolution authority will be considered once the no creditor worse off framework has been confirmed, but that officials consider that appeals should likely be limited to no creditor worse off compensation;

### Judicial review

82 **noted** that the inherent power of the High Court to review the lawfulness of a decision taken under the DTA will be available, including in respect of the exercise of powers for which an appeal right is not provided for in the DTA (e.g. powers to make secondary legislation through setting standards and exemptions or designations);

### Associated persons

83 **agreed** that the definition of an associated person be along the lines of that used in section 10 of the Insurance (Prudential Supervision) Act 2010;

84 **agreed** that the Reserve Bank is able to require an associated person to provide the Reserve Bank with information for the purposes of the Reserve Bank's prudential supervision of licensed deposit takers;

### Miscellaneous matters

85 **agreed** that the following provisions of the RBNZ Act be carried across to the DTA (subject to drafting modifications):

85.1 section 68A (Trans-Tasman cooperation);

85.2 section 139A – 139J (covered bonds);

86 **agreed** that comparable provisions to sections 60, 62-63, and 67-71 of the Insurance (Prudential Supervision) Act 2010 (relating to financial strength ratings) be included in the DTA (subject to necessary drafting changes or modifications);

87 **noted** that Paper 1 under DEV-21-SUB-0076 seeks authority for the Minister of Finance to make further policy decisions required to finalise drafting instructions for the DTA (including matters outlined in Annex 1 of that paper) in consultation with the Associate Ministers of Finance and the Minister of Commerce and Consumer Affairs.

Janine Harvey  
Committee Secretary

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**Present:**

Hon Grant Robertson (Chair)  
Hon Dr Megan Woods  
Hon David Parker  
Hon Nanaia Mahuta  
Hon Poto Williams  
Hon Damien O'Connor  
Hon Stuart Nash  
Hon Willie Jackson  
Hon Michael Wood  
Hon Dr David Clark  
Hon Phil Twyford  
Rino Tirikatene, MP  
Dr Deborah Russell, MP

**Officials present from:**

Office of the Prime Minister  
Officials Committee for DEV

**Hard-copy distribution:**

Minister of Finance