The Treasury

Additional Documents Related to Phase 2 of the Reserve Bank Act Review - December 2019 to April 2021 - Proactive Release

June 2021

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Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

[7] 6(e)(ii) - to prevent serious damage to the economy of New Zealand by disclosing prematurely decisions to change or continue government economic or financial policies relating to the regulation of banking or credit

[27] 9(2)(ba)(ii) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely otherwise to damage the public interest

[29] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment

[36] 9(2)(h) - to maintain legal professional privilege

[39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [39] appearing where information has been withheld in a release document refers to section 9(2)(k).

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RESERVE BANK OF NEW ZEALAND
TE PŪTEA MATUA

TE TAI ŌHANGA
THE TREASURY

Report: Reserve Bank Institutional Act, outstanding policy issues

Date:	14 February 2020	**Report No:**	T2020/251
		File Number:	MC-1-7-3-1-13

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	**Agree** to the recommendations in this report **Refer** this report to the Associate Ministers of Finance, the Minister of Commerce and Consumer Affairs and the Minister of Justice	18 February 2020

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Felicity Barker	Principal Advisor, Reserve Bank Act Review- Phase 2	[35]	✓
Tamiko Bayliss	Director, Reserve Bank Act Review- Phase 2	[39]	

Minister's Office actions (if required)

Return the signed report to the Treasury

Refer the report to the Associate Ministers of Finance and the Minister of Commerce and Consumer Affairs

Refer this report to the Minister of Justice, in regards to recommendation dd

Enclosure: Yes

Report: Reserve Bank Institutional Act, outstanding policy issues

Executive Summary

In December 2019 Cabinet agreed to replace the Reserve Bank of New Zealand Act 1989 (the Act) with a new Reserve Bank Institutional Act and a Deposit Takers Act [CAB-19-MIN-0675]. Cabinet also agreed to the broad parameters of these Acts.

This report seeks additional decisions in relation to the Reserve Bank Institutional Bill (the Bill). Following your decisions on these matters, we will provide you with a draft Cabinet paper. Officials are aiming for decisions to be made at the Cabinet Economic Development Committee meeting on 18th March enabling the Bill to be introduced into Parliament in mid-2020. Key matters addressed in this report are summarised here.

Information gathering and sharing powers

The Bill will carry over the Reserve Bank's (the Bank) 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 survey financial institutions, for example, for monetary policy purposes. The key recommended amendments are:

- broadening the scope of entities from which the Bank can collect information to ensure the information gathering power supports all the Bank's central banking and financial sector monitoring functions; and

- updating penalties, including by making it an infringement offence to fail to provide information.

It is also recommended that the Bank has a specific power enabling it to share information with a defined list of public sector agencies, which have related functions. This will support the co-ordination of financial sector regulation.

Protection from liability and indemnity

The Crown entities framework provides a framework for protection from liability for directors, employees and office holders. This framework is broadly intended to apply to the Bank. Individuals will be protected from liability in the course of their duties, when acting in good faith. However, an exception to this protection is that individuals will not be protected from liability for certain specified crimes. Further, directors of the Bank will be able to be removed from office for breach of a statutory duty, and the Bank may bring an action against a director for breach of certain statutory duties.

It is recommended that the Bank have statutory protection from liability across all its functions when it acts in good faith. The Bank currently has such a protection in its role as prudential regulator of the insurance and non-bank deposit taking sectors. This ensures that the Bank is able to act without fear of litigation. That may be important in, for example, a failure resolution situation where the Bank may need to act quickly.

The Bank and certain individuals currently have an indemnity from the Crown, provided through a permanent legislative authority, for liabilities arising in the exercise of the Bank's powers. Such a broad indemnity is considered unnecessary in light of the broad protection from liability discussed above. It is proposed that for directors, employees and office holders, the approach in the Crown Entities Act 2004 apply. This would allow the Bank to indemnify or effect insurance for these individuals when they are acting in good faith. An indemnity,

provided through a permanent legislative authority, is however recommended for the Bank and statutory managers, when acting in good faith, for liabilities arising when exercising statutory management powers. This is because of the need to act quickly, and the likely difficulty of effecting insurance, in these circumstances.

Management arrangements for foreign exchange reserves

The Bank may deal in foreign exchange to meet its monetary policy objectives and to respond to foreign exchange market dysfunction. In the latter case, the Bank currently acts under ministerial direction. It is recommended that the Bank's use of foreign exchange reserves be subject to a Reserves Management and Co-ordination Framework, agreed between the Bank and the Minister of Finance. This would clarify the objectives of the Bank holding foreign exchange reserves, set the total level of reserves, recognise each party's interests and how trade-offs 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.

Governor's remuneration and terms and conditions of appointment

Under the Act, decisions on the Governor's remuneration and terms and conditions of appointment are made by the Minister in agreement with the Governor, following consultation with the Board. This is inconsistent with state sector practice. It does not formally reference objective decision-making criteria. It has the potential for actual or perceived conflicts of interest. And it may not support the Board's governance role. Alternatively, decisions regarding the Governor's remuneration could be taken by the Board, or the Remuneration Authority. The first option (Board) is recommended by the Bank and the second option (Remuneration Authority) is recommended by the Treasury. In addition, the Treasury and the Reserve Bank recommend moving the decision regarding the Governor's terms and conditions of appointment to the Board.

Cash management function

The Bill will include the Bank's powers in relation to the issuance and oversight of bank notes and coins (cash). This report recommends a number of matters to be included in the Bill that recognise an expanded stewardship role for the Bank in relation to the cash system. These matters relate to the specification of the Bank's functions, monitoring responsibilities and information gathering powers. These matters are discussed in this report as they are integral to the Bill. The Bank will be providing you with a separate paper that addresses more substantive policy issues in response to the declining transactional use of cash.

Council of Financial Regulators

Cabinet previously agreed to "establish a legislative mandate for the Council of Financial Regulators (CoFR) that enhances coordination while retaining flexibility and regulators' statutory independence" [CAB-19-MIN-0675]. To achieve this, it is recommended that the Bill provide that the Bank and the FMA must 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.

Other matters

This report recommends some minor amendments, or further detail, relating to the December Cabinet decisions regarding: the appointment of Board members; in which Acts the decision-making principles are placed; and the scope of capital expenditure to be included in the funding agreement.

Recommended Action

We recommend that, in relation to the Bill, you:

Information gathering

a. **agree** that the Bank may collect information for the purpose of performing its central banking and financial system oversight functions from any:

   i. financial service provider

   ii. person involved in the distribution and management of bank notes and coins

   iii. person who holds information relating to, or on behalf of, those persons

   iv. a body corporate that is a related party of a body corporate named in (i) or (ii), or was formally a person named in (i) or (ii) in respect of actions of that former person

agree/disagree

b. **agree** that the information collected must relate to the business of the person, and not to the affairs of a particular customer or client

agree/disagree

c. **agree** that a person who fails to supply required information would be subject to an infringement offence with a maximum:

   i. fee of: $1,000 for individuals, and $3,000 for corporates

   ii. fine of: $3,000 for individuals, and $9,000 for corporates

agree/disagree

d. **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:

   i. $20,000 - $50,000 for an individual

   ii. $100,000 - $200,000 for a body corporate

agree/disagree

e. **agree** that persons who provide information will have standard legal protections from self-incrimination and protection of profession privilege

agree/disagree

f. **agree** that the provisions of the Act that remove person's protections against self-incrimination be repealed (sections 175A, 175B)

agree/disagree

g. **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

agree/disagree

h. **agree** that the indicative maximum penalty for the offence in recommendation (g) be broadly aligned with a level 3 offence under the FMI Bill ($50,000 for an individual)

agree/disagree

i. **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

agree/disagree

j. **agree** that the indicative penalty for the offence in recommendation (i) be in the range of:

   i. $20,000 - $50,000 for an individual

   ii. $100,000 - $200,000 for a body corporate

Information sharing

k. **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

agree/disagree

l. **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

agree/disagree

m. **agree** that the Bank be able to set conditions in relation to shared information, with the penalty for wilful breach of conditions in line with the penalty in section 61 of the Financial Markets Authority Act 2011 (FMA Act), being up to $300,000

agree/disagree

n. **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 a similar penalty to that in section 61 of the FMA Act for a wilful contravention of an order

agree/disagree

Liability and indemnity

o. **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

agree/disagree

p. **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

agree/disagree

q. **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

agree/disagree

r. **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

agree/disagree

s. **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

agree/disagree

t. **note** that the matter in recommendation (s) will be reviewed again as part of the development of the resolution framework for the Deposit Takers Act

u. **agree** that the indemnity and liability provisions be consolidated into the Institutional Act

agree/disagree

Foreign Exchange Reserves

v. **agree** that the Minister of Finance and the Bank be required to agree a Foreign Reserves Management and Co-ordination Framework (RMCF), providing matters along the lines of those set out in paragraph 58

agree/disagree

w. **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)

agree/disagree

x. **agree** that the RMCF be subject to transitional arrangements, and that the existing arrangements apply until a RMCF is agreed

agree/disagree

y. **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

agree/disagree

z. **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

agree/disagree

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

aa. **agree** that the Governor's remuneration be determined by either:

i. the Board following consultation (recommended by the Bank), or

agree/disagree

ii. the Remuneration Authority (recommended by the Treasury)

agree/disagree

bb. **agree** that the Governor's terms and conditions of appointment be determined by the Board

agree/disagree

Bank notes and coins

cc. **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

agree/disagree

dd. **agree** to recommend to the Minister of Justice that consideration be given to incorporating offences relating to banknote and coins into the Crimes Act at an appropriate time

agree/disagree

ee. **note** that current offence provisions in relation to bank notes and coins will be carried over to the Institutional Bill pending any review by the Ministry of Justice

The Council of Financial Regulators (CoFR)

ff. **agree** that a legislative mandate for the CoFR 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

agree/disagree

gg. **agree** that the Bill and the FMA Act reference respectively the Bank's and the FMA's roles as Chairs of CoFR in the respective coordination functions

agree/disagree

hh. **agree** that the core CoFR agencies be designated in the Bill so as to include the Treasury, FMA, Ministry of Business Innovation and Employment and the Bank, with other agencies invited by the Chairs

agree/disagree

Appointment of Board members

ii. **note** Cabinet's previous decision to retain the current process for the appointment of Reserve Bank Board members [CAB-19-MIN-0675]

jj. **agree** to recommend that Cabinet rescind the decision referred to in recommendation (ii), and instead provide that Board members be appointed by the Governor-General on the advice of the Minister, consistent with the process for Independent Crown Entities

agree/disagree

Funding

kk. **note** that items included in capital expenditure, for the purposes of the funding agreement, will be based on the definition of capital expenditure contained in the Public Finance Act but excluding certain volatile items

Decision-making principles

ll. **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 (the Deposit Takers Act, the Insurance (Prudential Supervision) Act (IPSA), and the Financial Markets Infrastructures Act)

mm. **agree** to recommend that Cabinet rescind the decision referred to in recommendation (ll), and instead provide that the decision-making principles broadly agreed by Cabinet be located in the Deposit Takers Act

agree/disagree

nn. **agree** that IPSA 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

agree/disagree

oo. **note** that the recommendations in this paper may be further refined prior to submission of a paper to the Cabinet Economic Development Committee on 18 March 2020, based on advice from the Parliamentary Counsel Office or Ministry of Justice

Tamiko Bayliss
Director,
Reserve Bank Act Review – Phase 2

Hon Grant Robertson
Minister of Finance

Report: Reserve Bank Institutional Act, outstanding policy issues

Purpose of Report

1. This report seeks agreement to a number of recommendations on outstanding policy issues in relation to the Institutional Bill (the Bill) for the Reserve Bank (the Bank).

Background

2. 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 Bank's over-arching objectives, governance and accountability framework and central banking functions.

3. This report addresses a number of supplementary decisions required to progress the Institutional Bill (the Bill). It covers matters that relate to:

   - information gathering powers;
   - information sharing;
   - protection from liability;
   - indemnities;
   - the management arrangements for foreign exchange reserves;
   - the Governor's remuneration and terms and conditions of appointment;
   - matters relating to the Bank's responsibilities in relation to bank notes and coins; and
   - the legislative mandate for the Council of Financial Regulators (CoFR).

4. This report also provides further details in relation to previous decisions on:

   - the appointment process for the Board;
   - definitions for the purposes of the funding agreement; and
   - the Acts in which regulatory decision-making principles are placed.

5. It is intended that the decisions in this paper will be taken to the Cabinet Economic Development Committee meeting on 18 March, and Cabinet subsequent to that. This will allow for the Bill to be introduced in mid-2020.

6. The Treasury and the Bank will provide you with a report on the Financial Policy Remit next week. We understand that the Bank will also be providing you with a draft Cabinet paper on matters relating to the Future of Cash, which are not within the scope of the Reserve Bank Act Review.

7. The Treasury and the Bank will shortly undertake further public consultation on the design of the Deposit Takers Act and deposit insurance. Matters in the consultation, such as the Financial Policy Remit, are relevant to both Acts.

Analysis

Information gathering powers

Scope of information gathering powers

8. Section 36 of the Act allows the Bank to collect information from financial institutions for the purpose of carrying out its non-regulatory 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.

9. Cabinet agreed [CAB-19-MIN-0675] that this power will be transferred 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.

10. In order to implement this Cabinet decision, we 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 over-sight functions:

    i. any financial service provider;

    ii. any person involved in the distribution and management of bank notes and coins;

    iii. any person who holds information relating to, or acts on behalf of, those individuals or entities; or

    iv. a body corporate that is a related party of another body corporate named in (i) or (ii), or was formally a person named in (i) or (ii) in respect of actions of that former person.

11. It is intended that the information collected must relate to the business of the person, and not to the affairs of a particular customer or client.

12. We 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.

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

[1] Deposit Takers Act, Insurance (Prudential Supervision) Act, Financial Markets Infrastructures Act.

Compliance and confidentiality

14. We recommend that institutions that fail to supply information when required will be subject to an infringement fee of $1,000 for individuals, and $3,000 for corporates, with maximum fines of $3,000 and $9,000 respectively.[2] 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.

15. For more serious non-compliance, where action is intentional, we recommend keeping a full criminal offence. 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 a body corporate 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.

16. 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. It is recommended 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 15.

17. We 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.

18. 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.

19. 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. Officials are considering the application of the Official Information Act to confidential information and will report back on this.

[2] 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.

20. The Act provides that it is an offence for a person to disclose information, unless the specified grounds for release are met. It is recommended that the offence provision be updated in the Bill, such that a person will only commit an offence if they intentionally release confidential information. This higher threshold 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.

21. It is intended that the penalty for breach of the confidentiality provisions be broadly aligned with the existing penalty in the Act for this offence ($50,000 fine and 3 months imprisonment for individuals). This is the same financial penalty for the same offence as in the FMI Bill.

Information sharing

22. We 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 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.

23. The Bank can currently share information with agencies where it considers that the agency has a proper purpose. 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.

24. 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.

25. The legislation would define a core set of domestic agencies that the Bank could share information with. This would include, at least, the agencies in the Council of Financial Regulators; Statistics New Zealand and the Director of the Serious Fraud Office.[3] 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.

[3] 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.

26. We 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 Financial Markets Authority Act 2011 (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 any information relating to an ongoing inquiry or investigation of the Bank. The order would apply for as long as the inquiry or investigation is taking place. It is envisaged that this would apply to the Bank's regulatory functions, but we are seeking a decision on this now as it relates to the proposed information sharing power.

27. The indicative penalty recommended for wilful breach of conditions on released information or a breach of a confidentiality order is a penalty similar to section 61 of the FMA Act (up to $300,000), which applies to similar powers.

Protection from liability

28. We 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 crimes:

    i. individuals: employees, directors, MPC members, the Governor, statutory managers and investigators acting for the Bank, and

    ii. the Bank.

Protection from liability for individuals acting in good faith

29. 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. It is recommended 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.

30. 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.

31. 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

32. The Bank itself is protected from liability under IPSA and the NBDT Act 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 – as discussed below). It is recommended that the Bill consolidate these provisions, and

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.

33. The Treasury and the Bank have considered the specification of the Bank's protection from liability. 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 it is shown that they have acted in bad faith or without reasonable care.

34. We 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, we 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.

35. 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 Legislative 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.

[36]

37. As noted, we recommend that the Bank have a broader protection from liability than the FMA and Commerce Commission. A high level of protection from liability for the Bank 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. Failure to protect the Bank from potentially vexatious litigation may result in an overly risk adverse culture or costly delays in action.

38. The Bank has provided strong feedback that it views such a protection from liability as necessary and desirable. 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.

39. 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 still have duties to act in accordance with the legislation the Bank acts under, and with reasonable care. Hence, we consider that the overall regime provides sufficient mechanisms to hold decision-makers to account even with this broad protection from liability.

Indemnities

40. We recommend that the Crown indemnify the Bank and statutory managers, through a permanent legislative authority, against any liability that may arise in the exercise of statutory management powers.

41. 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 do not act in bad faith.

42. 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

43. 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.

44. However, we 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. 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.

The Reserve Bank's legislative indemnity

45. While a broad indemnity for the Bank is considered unnecessary, provided the Bank is broadly protected from liability as recommended above, an indemnity for the Bank is considered appropriate in regards to any liabilities that may arise in the exercise of statutory management powers.

46. This indemnity would apply only if the Bank were acting in good faith. This would provide a 'backstop' to the protection from liability. This would be similar to the existing indemnity for the FMA under section 63 of the Corporations (Investigation and Management) Act 1989. It would apply to the exercise of statutory management powers. 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 liabilities that the Bank has on its balance sheet to fund loans to financial institutions.

47. This indemnity would be consolidated in the Institutional Act, and limit the existing Crown indemnity provisions that currently sit in the Act, IPSA and the NBDT Act. This would require retaining the current permanent legislative authority for an appropriation in relation to the indemnity.[4]

[4] The wording of the permanent legislative authority would be updated to reflect modern accounting practice.

48. The Treasury and the Bank will work to develop a clear understanding of how the indemnity will apply to the exercise of broader resolution powers as part of further work on the Deposit Takers Act.

Foreign exchange reserves

Current arrangements

49. 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.

50. 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 (the economic objectives[5]). If such a direction is considered by the Bank to be inconsistent with the economic 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 economic objectives so that they are consistent with the direction.

51. 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.

52. 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').

53. 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.

54. We see that there are two key issues to address with the current legislative provisions:

- Current arrangements do not provide clarity on the responsibilities of the Treasury and the Bank in the process for setting reserves. It is not clear which agency is responsible for advising the Minister on the level of reserves that is necessary and adequate to advance the objectives for the reserves. In addition, there is no process to review foreign exchange directions or the level of reserves. The level of reserves has not been reviewed for an extended period.

- Cabinet has agreed that the Bank will now have an over-arching financial stability objective, in addition to its existing economic objectives. It is likely that in some

[5] Maintaining price stability and supporting maximum sustainable employment.

instances, stabilising the foreign exchange market will be considered a sub-objective of financial stability, and hence under the Bank's new objectives and functions we consider the Bank has greater power to act independently to stabilise the foreign exchange market. However, there continues to be a need for an appropriate governance and accountability framework, including assigning clear objectives, roles and responsibilities in regards to managing foreign exchange market dysfunction, and in an extreme case where coordinated action across official agencies may be necessary, intervention would more properly be undertaken under Government direction.

A new Reserves Management and Co-ordination Framework

55. To address these issues, we 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:

- 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);
- Ensuring that there is a sound governance framework, and sufficient capacity, to manage foreign exchange market dysfunction;
- Ensuring that the Government of the day can make choices over the framework for economic policy to maintain democratic legitimacy.

56. The key recommended change is that the Minister and the Bank would be required to agree a "Foreign Reserves Management and Co-ordination 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. The Minister would retain the power in the Institutional Act to issue directions to the Bank to deal in foreign exchange within guidelines, and 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 as agreed in the RMCF). 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.

57. 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.

58. Broadly the RMCF would be able to cover the following:

- A framework for the use of the shared pool of foreign reserves in order to advance the statutory objectives, or any ministerial direction;
- The level of the reserves necessary to advance the statutory objectives and meet any current or potential ministerial direction;

- Any co-ordination arrangements with the Debt Management Office (who also hold foreign exchange reserves that could be used in a currency crisis);
- Requirements relating to the publication of information on the management, use and performance of the reserves;
- The impact of reserve levels on the Bank's capital adequacy, and any associated arrangements;
- Any other matters agreed between the Minister and the Bank.

59. 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

60. Transitional arrangements are intended to 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 (this includes the Minister's power to set reserves and foreign exchange directions under the Act). It is recommended that the Bill contain procedural requirements relating to the first RMCF, such as requiring that:

- the Board will be required to provide advice on the first RMCF within 4 months of taking up their legislative responsibilities;
- the Board and the Minister will be required to take reasonable steps to ensure that a RMCF is in place within six months of the Board taking up their legislative duties;
- the RMCF would be in force from the point the Minister consents to a framework proposed by the Board.

61. 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. Existing directions will be in place until revoked.

62. Once a RMCF is in place it will have continued existence but may be amended. The RMCF would be required to be reviewed every five years (from the last amendment). Further, the Minister or the Bank would be able to seek to review the RMCF at any time. Both parties must agree to amendments arising from these reviews.

63. The RMCF would also be required to be reviewed if a new foreign exchange ministerial direction is issued. As discussed both parties must take reasonable steps to ensure that the framework is amended in a manner 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.

64. It is proposed that the legislation specify that the Minister may request the Bank to provide advice on the RMCF at any time. The Treasury and the Bank would work together on any proposed revisions. This would allow for a flexible process over time, as compared to prescribing the process in legislation.

65. In regards to the Minister's power to issue a direction, we 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. These requirements will, however, be tailored to recognise that foreign exchange directions may need to be issued quickly at times. Changes to the direction power would take effect from main commencement of the Act.

The Governor's remuneration and terms and conditions of appointment

Remuneration

66. 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.

67. Furthermore, the current arrangements do not require formal reference to an objective set of criteria. There is also a risk that the current arrangements could result in an actual or perceived conflict of interest. The Bank for International Settlements (BIS) advises that the potential for conflicts of interest is the reason why central bank governors' salaries are often set by an independent body or reference point. The Bank will also have a new governance board. The inability of the Board to determine the Governor's remuneration may undermine the Board's governance role and is inconsistent with the Crown entity framework.

68. The Treasury and the Bank agreed that having the Board set the Governor's remuneration would best support its governance role. The Treasury also considers it important for remuneration decisions to be consistent with broader state sector practice. Both agencies would therefore support an option for the Board to set the Governor's remuneration following consultation with the States Services Commission (SSC) or the Remuneration Authority. However, the SSC advised that it is inappropriate for it to be legislatively required to consent to, or provide advice on, the Governor's remuneration. This is on the basis that "it would be constitutionally inappropriate for SSC to be statutorily involved in setting the remuneration for an independent position such as this". The Remuneration Authority does not act in an advisory role. Rather, it provides determinations.

69. As neither the SSC nor the Remuneration Authority are able to provide a formal check, and as there are competing considerations, which the agencies weight differently, the Bank and the Treasury support different recommendations.

70. The Bank's preferred option is that the Board determine the Governor's remuneration. The Board could set the salary by reference to the scope of the Governor's role and responsibilities, which the Board will be responsible for determining. Moving the decision regarding remuneration to the Board would also avoid the potential for actual or perceived conflicts of interest. Enabling the Board to set remuneration would be consistent with the Board's governance role. Setting the remuneration of its key agent is an important lever for a Board. It is also consistent with the Crown entity model which the review has sought to align the Bank's governance structure with where possible.

71. The Treasury's preferred option is that the Remuneration Authority determine the Governor's remuneration. Despite the new governance framework, 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. The Remuneration Authority has advised that determining the Governor's remuneration would be consistent with this role. It would also ensure that the salary is based on the objective criteria set out in the Remuneration Authority Act 1977. Using the Remuneration Authority would avoid any actual or perceived conflicts of interest. The role is also similar to other positions that the Remuneration Authority determines remuneration for. The Remuneration Authority

will also determine the salaries of Reserve Bank board members. The SSC supports this approach.

Terms and conditions of appointment

72. 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.

73. We recommend that the Board determine the Governor's terms and conditions of appointment. This would be consistent with the Crown entity model. The terms and conditions of appointment would align with organisational practice, ensuring that these are based on objective criteria. Shifting the decision regarding terms and conditions of appointment to the Board would also support the Board's governance role. The Board will largely be determining the role and responsibilities of the Governor. It will, therefore, be well placed to align the terms and conditions of appointment with the role and responsibilities of the Governor.

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

74. 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. These powers include that the Bank has the sole right to issue bank notes and coins in New Zealand, which is legal tender in New Zealand. The Act also provides a number of offences in relation to defacement and counterfeit, for which the Bank may take enforcement action.

Oversight of the cash system

75. The Bank has been reviewing its powers and responsibilities in relation to the cash system over recent months. The Bank will be providing you with a draft Cabinet paper recommending some additional provisions to be incorporated in the Bill, which are outside the scope of the Reserve Bank Act Review. However, there are a number of matters relating to the Bank's functions as set out in the Bill that are addressed in this report as they are integral to the Bill.

76. The cash system is a complex network comprised of the Bank and a number of commercial agents (banks, cash-in-transit operators, and ATM operators) 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. The Treasury and the Bank support the Bank having a clear role in ensuring the end-to-end functioning of the cash system on a sustainable basis going forward.

77. 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 than it does presently, for example by owning and operating cash depots.

78. To support the Bank having this system oversight role, we 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.

79. In order for the Bank to have oversight of the cash system, it will be important for the Bank to monitor the cash system. As agreed by Cabinet, it is intended that one of the Bank's functions will be to undertake monitoring activities in relation to its objectives. It is recommended that this monitoring function be broad enough to cover monitoring of the cash system. As discussed earlier, it is recommended that the Bank's information gathering power be expanded to allow the collection of information from entities involved in the distribution of cash. This will ensure that the Bank is enabled to collect information so as to undertake monitoring in relation to the cash system.

Offences relating to cash

80. The Act makes it an offence to counterfeit and deface currency. The Crimes Act also provides an offence for counterfeit of coins. We consider that counterfeit, and potentially other cash offences, would be best contained in the Crimes Act. Furthermore, the penalty for counterfeit offences is low compared to the seriousness of the crime. It is recommended that you recommend to the Minister of Justice that the Ministry of Justice give consideration to consolidating offences relating to bank notes and coins into the Crimes Act, and reviewing the penalties in light of the Crimes Act penalties, at an appropriate time. Pending this review the offence provisions will be carried over to the Institutional Bill.

Council of Financial Regulators

Legislative mandate

81. Cabinet has previously agreed to "establish a legislative mandate for CoFR that enhances coordination while retaining flexibility and regulators' statutory independence". The purpose of the mandate would be to ensure that CoFR has an enduring and effective role in achieving good outcomes for New Zealand through the financial regulatory system.

82. To achieve this we recommend, subject to drafting advice from the Parliamentary Counsel Office, that the Bill 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.

83. This approach reflects the government's expectations of good regulatory stewardship, which include monitoring existing regulatory systems, providing analysis and support for changes to the system, and good regulatory practice. Good regulatory practice includes developing relationships with other regulators to coordinate activities to help manage regulatory gaps or overlaps, minimise regulatory burdens on regulated parties, and maximise effective use of scarce regulator resources.

84. We recommend that the core members of CoFR recognised in the Bill be The: Bank, FMA, MBIE and Treasury, with others able to be invited by the Chairs. The Commerce Commission would remain a member, but would not be listed in the Bill as it is not a core part of the 'twin peaks' financial regulatory architecture.

85. Each agency has its own separate role in the financial regulatory system, and has existing responsibilities and functions. The CoFR mandate should encourage and enable cooperation and coordination between agencies but should not crowd out existing arrangements, confuse existing responsibilities, or be overly prescriptive. The mandate should make clear that it does not limit any agency's ability to exercise its statutorily independent functions, powers or duties.

Statutory function to cooperate

86. Cabinet agreed that in the Bill, the Bank would have a function to cooperate with other relevant public sector agencies, including in relation to its role as a member of CoFR. We propose that this function also reference the Bank's role as chair of CoFR. The FMA's function to cooperate is also recommended to 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.

Further detailed decisions

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.

88. The current Reserve Bank Board is appointed by the Minister. The Board also includes the Governor. Appointments must be notified in the Gazette.

89. 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. Aligning the appointment process with the legislative process for the appointment of ICE members would support this approach.

90. We recommend aligning the process for the appointment of Board members with the model for appointing members of an ICE. ICE board members are appointed by the Governor-General on the recommendation of the Minister.

91. 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.

Funding Agreement – definitions

92. Cabinet has agreed to retain a five yearly funding agreement between the Bank and the Minister of Finance. Cabinet also agreed that the agreement would cover defined operating and capital expenditure. Currently the funding agreement only covers operating expenditure. The Bank and the Minister will also be able to agree expenditure items that would not be covered by the funding agreement, even if they are *prima facie* covered by the legislative definition.

93. The Treasury and the Bank have considered the appropriate scope of capital expenditure that would *prima facie* be included in the funding agreement. The working definition for capital expenditure is based on the definition of capital expenditure used in the Public Finance Act.[6] It is consistent with capital expenditure as reported in the Bank's financial statements, and includes the purchase of tangible assets and intangible assets, but excludes:

    i. inventories (the largest component of which is bank notes and coins);

[6] This definition may be further developed through drafting of the Bill.

ii. purchases of financial instruments; and

iii. purchases of ownership interests in entities that are not subsidiaries.

Decision-making principles

94. In December 2019, Cabinet agreed that the Bill contain decision-making principles that the Bank must have regard to in exercising its regulatory powers under all the sectoral Acts. These principles are provided in the Annex (Table 1, column 1).

95. As discussed in joint report: Draft Consultation Paper on the Deposit Takers Act (T2020/83), the Treasury and the Bank have considered further 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 (see Annex (Table 1, column 2 and 3). The principles in the FMI Bill would apply to the Bank and FMA as joint regulators.

96. We now recommend that the decision-making principles be located in each of the sectoral Acts. This means the decision-making principles approved by Cabinet would be included in the Deposit Takers Act. 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. The consultation document on the Deposit Takers Act (C3) proceeds on this basis.

97. The current principles in IPSA and the FMI Bill will be retained. 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.

98. 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.

Next steps

99. Following your decisions on the matters in this report, we will provide you with a draft Cabinet paper for consultation with your Ministerial colleagues. We are targeting decisions on these matters being made at the Cabinet Economic Development Committee meeting on 18 March. This will enable these matters to be incorporated into the Bill in time for introduction into Parliament in mid-2020.

Annex 1:

Table 1: Comparison of decision-making principles in the FMI Bill and IPSA to those proposed for the Deposit Takers Act

Proposed for the DTA	FMI	IPSA
The desirability of minimising unnecessary costs from regulatory actions, taking into account the value of outcomes to be delivered	The need to avoid unnecessary compliance costs and unnecessary constraints on innovation	The need to avoid unnecessary compliance costs
The desirability of taking a proportionate approach to regulation and supervision, and ensuring consistency of treatment of similar institutions	No equivalent [this principle is less applicable to FMIs as small operators may still be critically important and operators diverse]	The desirability of consistency in the treatment of similar institutions (while recognising that the New Zealand insurance market comprises a diversity of institutions)
The desirability that sectors regulated by the Bank are competitive	No equivalent [this principle is less applicable FMIs as the sector has quasi-monopoly like properties]	The importance of maintaining the sustainability of the New Zealand insurance market The need to maintain competition in the insurance market
The value of transparency and public understanding	Timely, accurate, and understandable information being available to participants to assist them in making informed decisions about their interaction with the FMI	The desirability of providing to the public adequate information to enable members of the public to make informed decisions
Practice by relevant international counterparts carrying out similar functions, as well as guidance and standards from international bodies	The importance of regulating FMIs in a way that is consistent with international standards for their regulation where those standards are appropriate for conditions in New Zealand:	
The desirability of taking into account long term risks to financial stability		