
Reserve Bank of New Zealand

Statement of Intent

For the period 1 July 2010 to 30 June 2013

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Introduction

Under section 162A of the Reserve Bank of New Zealand Act 1989 (the Act), the Reserve Bank must, in each financial year, provide to the Minister a *Statement of Intent (SOI)* for the Bank for that financial year and at least the next two financial years. Section 162B requires the *SOI* to contain the following information for the full period to which it relates:

- a) key background information about the Bank and its operating environment;
- b) the nature and scope of the Bank's functions and its principal areas of operation;
- c) the specific impacts, outcomes, or objectives that the Bank seeks to achieve or contribute to;
- d) how the Bank intends to perform its functions and conduct its operations to achieve those impacts, outcomes, or objectives;
- da) if a direction has been given under section 68B, how the Bank has had regard to the direction;
- e) the proposed strategies for managing the organisational health and capability of the Bank;
- f) a statement of the projected income and expenditure for the first financial year in the period to which the *SOI* relates;
- g) a statement of the principles in accordance with which the Bank must determine the amount it recommends to the Minister as appropriately payable by the Bank to the Crown as an annual dividend;
- h) the main financial and non-financial measures and standards by which the future performance of the Bank may be judged;
- i) the matters on which the Bank will consult or notify the Minister before making a decision, the matters on which it will report to its Minister, and the frequency of reporting;
- j) any other matters that are reasonably necessary to achieve an understanding of the Bank's intentions and direction.

What we do

The Reserve Bank of New Zealand is the nation's central bank, established by an Act of Parliament, the Reserve Bank of New Zealand Act. The Bank has three main functions, which are designed to promote a sound and dynamic monetary and financial system and meet the goal of improving New Zealand's economic performance. These functions are: (1) the management of monetary policy to maintain overall price stability; (2) the maintenance of a sound and efficient financial system; and (3) the supply of legal tender to meet the currency needs of the public.

The functions and operations that the Bank performs to achieve these objectives are described in the following pages. In performing them, the Bank ensures that it works effectively with Ministers, the Treasury, other relevant government departments and the private sector on all matters where there is a shared interest.

Vision

We promote a sound and dynamic monetary and financial system.

Values

Integrity – Being professional and exercising sound judgement

Innovation – Actively improving what we do

Inclusion – Working together for a more effective Bank

Foreword

Recovery from the global financial crisis and recession is underway, yet there are almost daily reminders that conditions remain fragile and volatile.

New Zealand has emerged from its recession, benefiting from stronger growth in our major trading partners in China, Australia and emerging Asia. However, recovery remains sluggish in the UK and Europe, and sovereign debt concerns hovering over several European economies are disturbing financial markets.

Compared to other countries, New Zealand has been less scarred than most from the crisis. Our financial system is much simpler than in other parts of the globe, our banks were not as exposed to toxic assets and our firms were not as highly leveraged as elsewhere, though our households are highly leveraged.

Funding has been accessible for the banking system over the past year but has been more expensive than before the crisis. More recently, the sovereign debt concerns in Europe have impacted the cost and availability of funding. As an externally indebted country, New Zealand remains exposed to any deterioration in global debt markets, despite good quality fiscal management.

Conventional monetary policy, coupled with temporary emergency liquidity measures, has been sufficient to bring New Zealand through the crisis without the need for the radical policies adopted in several major economies.

The Strategic Priorities outlined in this *SOI* capture the work we have underway to navigate through these conditions.

There is a lively debate in New Zealand regarding the role of monetary policy in managing financial misalignments. For its part, the Bank is investigating the potential for macro-prudential policy tools for New Zealand. Unlike many of our counterparts overseas, as a 'full service' central bank we can engage staff in this work from across our policy departments, who are specialists in monetary policy, financial markets and banking supervision.

As the domestic economic recovery continues, we expect to begin unwinding the degree of monetary policy stimulus. While we have been able to unwind some of the emergency liquidity support provided to the financial system during the financial crisis, our facilities remain under review given current financial market turbulence. Our financial market staff and economists are directing this work.

Our banking supervisors are also engaging in global discussions on what type of bank supervision regime may be necessary to ward against such catastrophes in future. We expect to make further changes to the Basel capital regime. Our approach will be to ensure that New Zealand adopts those measures that improve the soundness of the financial system while not undermining its efficiency.

At the same time, work initiated in previous years is continuing. In the period covered by this *SOI*, we will advance the implementation of the new Non-Bank Deposit Taker (NBDT) regime. A gradual rationalisation of the finance company sector continues, with the expiry of the original term of the retail deposit guarantee scheme

and a more stringent regulatory regime resulting in further consolidation. We will continue to develop and implement the new prudential regime for Insurance.

In our Priorities, we also recognise the need to ensure that our staff can meet the challenges of our evolving responsibilities. We will provide adequate development and support.

It is not only financial crises that we must guard against. In recent years the Bank has refreshed or replaced systems to ensure we can withstand physical crises or biohazards. A key initiative in this *SOI* will be the establishment of a business support centre in Auckland to improve business continuity and disaster recovery capability.

Our budget reflects the emerging environment. As the Bank's last Five-Year Funding Agreement was due to expire on 30 June 2010, we have negotiated a new Funding Agreement with the Minister for the period to 30 June 2015. While ensuring that funding is available to carry out existing functions and the new responsibilities outlined above, we have also been particularly conscious of the need to maintain strong financial disciplines and to carefully prioritise expenditure proposals.

The Bank's budget for 2010–11 shows operating expenditure of \$47.8 million, an increase of \$0.9 million over last year's Funding Agreement of \$46.9 million, reflecting the building of capacity in the Prudential Supervision Department.

This *SOI* reflects our ongoing commitment to ensure stability in New Zealand's financial system and growth in our economy in the face of a fragile environment.



Alan Bollard
Governor



Grant Spencer
Deputy Governor

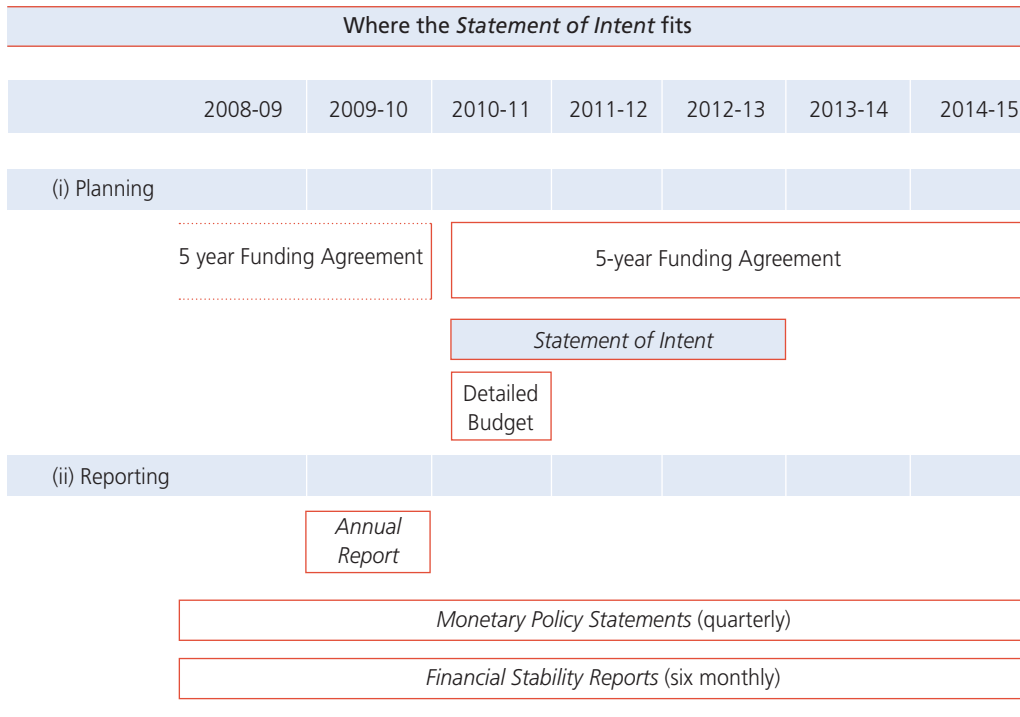
Reserve Bank Strategic Priorities for 2010-11

Priority	Explanation	Department
1	Investigate the potential for macro-prudential policy tools for New Zealand.	Financial Markets Economics Prudential Supervision
2	Begin unwinding special financial system support and monetary policy stimulus.	Financial Markets Economics
3	Identify any appropriate changes to the bank supervision regime, including those based on international regulatory reforms.	Prudential Supervision
4	Advance the implementation of the new Non-Bank Deposit Taker (NBDT) regime.	Prudential Supervision
5	Develop and implement the new prudential regime for Insurance.	Prudential Supervision

Reserve Bank Strategic Priorities for 2010-11

Priority	Explanation	Department	
6	Engage, develop and support staff to meet the challenges of the Bank's evolving responsibilities.	As the Bank's role evolves, the contribution of every staff member is important to the successful carrying out of the Bank's functions. Through quality feedback, appropriate training and targeted development plans, we can increase staff's individual contribution to the Bank's overall success in fulfilling its functions.	Bank-wide
7	Improve business continuity and disaster recovery capability through the establishment of a business support centre in Auckland.	The Bank ensures that it has systems in place to enable it to continue functioning in the event of a range of crises. It will establish a small office in Auckland to provide business continuity in payments and market functions in the event of a regional disaster in Wellington.	Operational

Planning and reporting framework



Our *SOI*, which traverses three years, is set in the context of our longer-term planning and funding. The Bank is funded through a five-year funding agreement between the Governor and the Minister of Finance, which is ratified by Parliament. The funding agreement specifies how much of the Bank's income can be retained by the Bank to meet its operating costs.

The 2005/06–2009/10 Funding Agreement expires on 30 June 2010. This *SOI* covers the first three years of the new Funding Agreement, which had yet to be ratified by Parliament at the time of writing.

Governance and structure

Board of Directors

The Reserve Bank has a Board of Directors whose primary function is to review the performance of the Governor and the Bank. The Board holds regular meetings at which it receives extensive briefings on the Bank's activities, decisions and policies. At these meetings, the Board also provides advice to the Governor on a range of Bank functions.

The Board, through an Audit Committee, reviews the Bank's financial statements and internal audit activity. Each year, the Board writes an assessment of the Bank's and the Governor's performance, which is provided as advice to the Minister of Finance and made public later in the Bank's *Annual Report*.

When required, the Board makes recommendations to the Minister on the appointment or reappointment of the Governor. The Minister can only appoint a Governor recommended by the Board. The Board can recommend to the Minister that the Governor be dismissed if the Board believes that the Governor's performance or conduct has been 'inadequate' or inappropriate in any one of various respects. The Board appoints the Deputy Governor on the Governor's recommendation.

The Board typically meets formally nine times a year, with provision for additional meetings. The current Board members are Dr Arthur Grimes (Chair); Mr Hugh Fletcher (Deputy Chair, and Chair of the Board's Audit Committee); Dr Chris Eichbaum; Professor Neil Quigley; Ms Sue Sheldon CNZM; Mr Keith Taylor; Ms Kerrin Vautier CMG; and Dr Alan Bollard (Governor). Board members are appointed for five-year terms and are eligible for reappointment.

Management structure

Under the Act, the Governor – who is also the Bank's Chief Executive – is accountable for the Bank's actions. In monetary policy, and in many other matters, decision-making authority resides with the Governor alone, although in practice he receives widespread advice, and takes monetary policy decisions based on the formal advice of the Official Cash Rate Advisory Group.¹ The Governor is appointed for a five-year term and can also be reappointed for further terms of up to five years. The Act sets specific procedures for the appointment, reappointment and dismissal of the Governor.

The Reserve Bank's senior management team is made up of the Governor, a Deputy Governor/Deputy Chief Executive, two Assistant Governors and the heads of the Bank's various departments, as outlined on page 9. The positions of Governor and Deputy Governor are required and their roles defined by statute. Currently, the Deputy Governor is also the Head of Financial Stability. The two current Assistant Governors are the Head of Operations and the Head of Economics.

The Governor receives advice from a number of internal committees within the Bank.

¹ This group includes key economic advisers within the Bank and two external monetary policy advisers.

Reserve Bank organisational structure

Governors	Department/Heads	Functions	Internal services	
Governor <i>Alan Bollard</i>	Assistant Governor/ Head of Economics <i>John McDermott</i>	Economics	Monetary policy formulation	
	Deputy Governor/ Head of Financial Stability <i>Grant Spencer</i>	Financial Markets <i>Simon Tyler</i>	Market operations Foreign reserves management	
		Prudential Supervision <i>Toby Fiennes</i>	Financial system surveillance and policy	
		Currency and Building services <i>Alan Boaden</i>	Currency operations	Property management Security
		Financial services <i>Mike Wolyncewicz</i>	Settlement services Registry and depository services	Accounting services Treasury services
		Knowledge services <i>Tanya Harris</i>		Library services Technology services Project management Web publishing
	Assistant Governor/ Head of Operations <i>Don Abel</i>	Human Resources <i>Lindsay Jenkin</i>		Human resources strategy and services
		Communications/ Board secretary <i>Mike Hannah</i>		Communications strategy and services Reputation management Board secretariat
		Risk assessment and assurance <i>Steve Anderson</i>		Risk assessment and assurance Audit services Legal services

Functions and operations

Monetary policy formulation

Outcome

Stability in the general level of prices.

Objective statement

To achieve and maintain stability in the general level of prices. The current Policy Targets Agreement (PTA)² requires that the Bank “keep future CPI inflation outcomes between 1 and 3 percent on average over the medium term”. It also requires that: “In pursuing its price stability objective, the Bank shall ... seek to avoid unnecessary instability in output, interest rates and the exchange rate.”

Environment

- The global economy is recovering from its worst recession in many decades, but growth is variable across countries. Australia and economies in Asia are growing solidly, but growth remains low and fragile in many advanced Western economies. Global inflation is rising again. There remains considerable uncertainty and risk around the global economic outlook.
- Central banks are turning attention to when and how fast they exit their highly accommodative positions, including low or zero official interest rates and any credit or quantitative easing.
- Growth in the New Zealand economy has been weak, but it is expected to pick up through 2010, only regaining the past peak in activity in late 2010.
- Inflation pressures are likely to increase somewhat. The risks to the inflation outlook are broadly balanced.
- The Bank is expected to be independent and accountable for its actions, and to make sound, credible and transparent judgements.

Scope of operations

- Setting an Official Cash Rate (OCR) eight times a year, or as required, with the aim of keeping inflation within the target band.
- Publishing the Bank’s quarterly *Monetary Policy Statements (MPSs)* at the same time as four of the OCR decisions. The MPSs set out the Bank’s views on the economy and inflationary pressures, and the basis for the OCR decision.
- Announcing the other four OCR decisions approximately halfway between each *MPS*.
- Intervening in the foreign exchange market, where appropriate and feasible, to influence the level of the exchange rate, consistent with the objectives of the PTA.

Issues

- The speed/extent of deleveraging by New Zealand households and firms in response to high levels of debt.
- Considerable uncertainty about the pace and durability of the current recovery of the global economy, given the variability of growth across countries, still-impaired financial sectors and high household debt levels in some countries, and the widespread need for fiscal consolidation.

² The PTA specifies the monetary policy target agreed by the Governor and the Minister of Finance.

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- As global and domestic economic conditions permit, monetary policy stimulus will need to be withdrawn. The pace of this withdrawal will need to take into account how low interest rates have fallen and uncertainties about what will constitute 'normal conditions' in the future.
 - International re-examination of macroeconomic stabilisation policy and of how inflation-targeting monetary policy can be augmented by appropriate modifications to prudential policy and fiscal policy, taking into account New Zealand's particular circumstances with respect to the importance of asset prices and the exchange rate.
 - The central role of housing, credit and the financial sector in the current downturn, reinforcing the need for ongoing judgement to be applied to our economic models.

Initiatives and strategies

- Support our business-as-usual monetary policy advice will be our core objective. This includes providing advice on the withdrawal of monetary policy stimulus in light of current and prospective financial market conditions, and any changed economic behaviour on the part of households and firms as a result of the global financial crisis.
- Leverage new modeling and forecasting capability through exploiting KITT, the Bank's new primary forecasting model, and refining and using more extensively our alternative models.
- Monitor and evaluate international thinking about how monetary policy and financial stability policy should interact, particularly the ways in which flexible inflation targeting may be augmented to take account of the effects of asset-price cycles, leverage and prudential and fiscal policy on economic activity and inflation.
- Improve the quality, accessibility, relevance and reliability of Reserve Bank statistics, including by completing the implementation of the Financial Sector Information System (FSIS).

Key performance indicators

- Reserve Bank forecasts of CPI inflation should be comfortably within the target range in the second half of our forecast horizon.
- Measures of underlying inflation should generally lie within the target range.
- Unnecessary instability in output, interest rates and the exchange rate should be avoided.
- The Bank's reputation for comprehensive knowledge about the economy, thorough analysis and credible judgment, should be maintained or enhanced.
- The *MPS* provides a basis for assessment of the Bank's performance in pursuing its price stability target as defined in the PTA.

Domestic market operations

Foreign reserves management

Outcomes

- Adequate banking system liquidity; short-term interest rates consistent with monetary policy; confidence in the efficient functioning of New Zealand financial markets.
- Foreign reserves available for efficient foreign exchange intervention and crisis management.

Objective statement

To support the effective implementation of monetary policy; to assist in the efficient functioning of the New Zealand financial system; to manage official foreign reserves; to provide effective support and execution for the Bank's foreign exchange market intervention policy; to manage the Crown's financial liquidity; and to maintain an effective crisis intervention capability.

Environment

- Changes to the financing and management of New Zealand's foreign currency reserves and our liquidity management regime continue to focus the Bank's market operations towards foreign exchange and swaps markets.
- Relatively low interest rates in the major markets are reducing the earnings on unhedged foreign reserves.
- Although banks have been able to improve levels of liquidity and raise term funds over the past year, sovereign debt concerns in parts of Europe are continuing to affect the cost and availability of funds.

Scope of operations

- Providing advice on financial market developments and issues for the formulation of monetary policy.
- Ensuring the effective implementation of monetary policy through the level of the OCR.
- Managing official foreign reserves for use in times of financial distress or when foreign exchange intervention is needed for monetary policy purposes.
- Managing liquidity in the banking system.
- Providing and managing the Crown Settlement Account.
- Acting as lender of last resort to the financial system if necessary, as well as assisting in the resolution of any financial market or banking crisis.

Issues

- Determining the future of the exceptional facilities put in place to help financial market participants through the credit crisis and what facilities will be sufficient to cope with post-crisis 'normal' conditions.
- Maintaining and continuing to develop the Bank's foreign exchange intervention capability to enhance the effectiveness of monetary policy implementation and the maintenance of orderly foreign exchange markets.
- Managing the liquidity management regime so that the payments system continues to operate, the banking system has adequate liquidity, and risks (both to the Bank and the market) are balanced appropriately.

Initiatives and strategies

- Continue to review and adjust the provision of temporary back-up liquidity facilities put in place through the crisis as warranted by financial market conditions.
- Implement the review of foreign reserves asset allocation and management approach.
- Promote the development of capital markets in areas where the Bank has powers and responsibilities (i.e., in money, bond and foreign exchange markets).

Key performance indicators

- Short-term wholesale interest rates should be relatively stable and maintained at levels consistent with the OCR.
- There is no evidence of payment failures due to shortage of cash in the banking system.
- Domestic market operations are expected over the medium term to generate a positive return for the domestic markets function, as an indicator that operations are running effectively.
- Foreign reserves are held at the level agreed with the Minister.
- Foreign reserves are held in a liquid and secure form, suitable for foreign exchange market intervention.
- The FRM portfolio is managed efficiently, yielding a net return that meets or exceeds that of its benchmark portfolio.³

³ The Bank is developing a new benchmark portfolio, which would include an open exchange position of 1 billion SDRs.

Financial system surveillance and policy

Outcomes

- A sound and efficient financial system in New Zealand.
- International and local confidence in New Zealand's financial system.

Objective statement

To register and supervise banks so as to promote the maintenance of a sound and efficient financial system, and to limit damage to the financial system that could result from a bank failure. To regulate non-bank deposit takers (NBDTs) and, assuming legislation is passed, to regulate and supervise the insurance sector. This will be done in a manner that will be relevant to New Zealand and that delivers a cost-effective balance between regulatory requirements and self- and market-discipline.

Environment

- Given the ongoing turbulence in global financial markets, there remain relatively high risks to the balance sheets of banks, NBDTs and insurance providers.
- In the wake of the global financial crisis, a number of changes to international prudential standards and codes are expected, especially in the areas of capital and liquidity requirements.
- It is yet to be determined what arrangements, if any, will be in place past the scheduled expiry of the Government's guarantees on retail deposits in December 2011.
- The prudential regulatory regime for NBDTs being progressively implemented currently requires deposit takers to comply with risk management and credit ratings requirements and, over time, will require compliance with requirements related to capital, liquidity, governance and restrictions on related-party exposures.
- Legislation to give the Bank additional power to complete the NBDT prudential regime, including crisis management and licensing powers in relation to NBDTs, is expected to be introduced to the House in late 2010.
- Legislation giving the Reserve Bank regulatory and supervisory powers in relation to insurers is expected to be enacted in late 2010.
- Through legislation enacted in October 2009, the Bank became the supervisor, for anti-money laundering and countering the financing of terrorism (AML/CFT) purposes, of banks, life insurers and NBDTs.
- The Bank increased its payment systems oversight responsibilities to include the oversight and designation of settlement systems (alongside the Securities Commission) following amendments made to Part 5C of the Reserve Bank Act in November 2009.

Scope of operations

- Setting specific criteria for bank registration.
- Subjecting banks to a specific monitoring regime.
- Publishing regular *Financial Stability Reports (FSRs)* assessing the soundness and efficiency of the New Zealand financial system.
- Strengthening the Bank's capacity to respond in times of financial crisis.

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- Monitoring the Crown's exposures in relation to the Deposit Guarantee Scheme (DGS) on behalf of the Treasury.
 - Overseeing and setting specific criteria for designation of payment and settlement systems.
 - Progressively developing and implementing the prudential regulatory framework for NBDTs and insurers, throughout 2010 and 2011.
 - Developing an AML/CFT supervisory framework, throughout 2010 and 2011.

Issues

- Ensuring that banks maintain adequate capital, through close monitoring of asset quality and prompt supervisory responses.
- Ensuring the international examination of macroprudential policy tools to assist monetary and prudential policy takes into account New Zealand's particular circumstances.
- The extent to which the current General Disclosure Requirements required of banks match stakeholder needs in a way that minimises compliance costs.
- Implementing and enforcing the regulatory regime for the NBDT sector, through appropriate consultation with the sector and trustees.
- Ensuring the Crown's exposures under the DGS are actively monitored and that the Treasury is promptly advised of any potential issues.
- Implementing the Insurance (Prudential Supervision) Bill when enacted.
- Implementing the prudential liquidity regime for banks.
- International re-examination of macroeconomic stabilisation policy and of how appropriate modifications to prudential policy may support and interact with monetary policy.

Initiatives and strategies

- Enhance the Bank's monitoring of risks to bank balance sheets and profitability.
- Reviewing disclosure requirements of banks as part of the Bank's continuous review of compliance costs.
- Develop, with the Treasury as required, the high-level features of post-deposit guarantee regulatory arrangements, if any.
- Continue implementing regulatory arrangements for the NBDT sector, and review the effectiveness of these regulatory arrangements by the end of 2012.
- Identify any appropriate changes to the bank supervision regime, especially in the areas of capital and liquidity requirements, including those based on international regulatory reforms.
- Refine our crisis preparedness, focusing on practical solutions and enhancing trans-Tasman coordination.
- Develop and implement the supervisory framework for the insurance sector.
- Develop and implement the AML/CFT supervisory regime.
- Monitor and evaluate international thinking about how monetary and financial stability policy should interact, and investigate the potential for macroprudential policy tools to assist existing prudential and monetary policy approaches.

Key performance indicators

- Banks comply with Conditions of Registration and maintain the required minimum capital ratios and liquidity requirements.
- NBDT regulations in place and NBDTs comply with the regulatory regime.
- The Treasury is promptly notified of and consulted with on:
 - any issues with any entities in the DGS;
 - significant policy developments, in particular in prudential and macroprudential regulation.
- The Bank has in place the people, procedures and systems to implement the Insurance (Prudential Supervision) Bill when it comes into force.
- The Bank has in place the people, procedures and systems to implement the AML/CFT supervisory regime and has publicly communicated the core features of its proposed regulatory arrangements.
- Measures included in the *FSR* provide a basis for assessment of the New Zealand financial system's stability and efficiency and the performance of the surveillance function.

Currency operations

Outcomes

Legal tender that meets the currency needs of the public.

Objective statement

To meet the currency needs of the public by ensuring, as the sole issuer of currency, the supply and integrity of bank notes and coins.

Environment

- The demand for notes and coins continues to grow each year. Cash remains an important means of making payments in New Zealand.
- The Bank's cash operations have changed considerably over the last decade and a new management information system is now required for more efficient and secure management of cash processes.
- The rate of counterfeiting in New Zealand is very low by international standards. However, the current bank note series is 10 years old and is due for review of security features.
- Surveys of notes in circulation have shown that the quality of most denominations is very good, but that many \$5 notes are showing considerable wear.

Scope of operations

- Procuring, storing, processing and issuing bank notes and coins to the banking system.
- Maintaining the quality, and verifying the authenticity of, currency in circulation.
- Issuing legal tender collectors' currency through an outsourcing arrangement.

Issues

- The currency operations inventory management system needs replacing to enable more effective management of cash-handling operations.
- The current polymer bank note series is 10 years old and the security features are due for review.
- The Currency Operations 'wholesale' business model has been in place for 10 years and is due for review of effectiveness and efficiency.
- The quality of \$5 notes in circulation is falling below the desired standard.

Initiatives and strategies

- Implement a new Currency Management System for the management of currency operations.
- Review the effectiveness and efficiency of the Currency Operations 'wholesale' business model.
- Investigate possible enhanced security features for bank notes.
- Lift the quality of \$5 notes in circulation through a 'swap' programme.

Key performance indicators

- All orders for notes and coins from banks that meet the Reserve Bank's guidelines are supplied within agreed times.
- Notes and coins in general circulation are of a good quality as indicated by surveys of the condition of currency in circulation.
- The number of counterfeit notes in circulation should be fewer than 10 per million notes in circulation.

Depository and settlement services

Outcomes

An efficient, reliable and secure payments system that supports the smooth functioning of the economy.

Objective statement

To ensure that payments system infrastructure services are provided efficiently and meet international standards.

Environment

- The Government's Capital Markets Development Task Force has recommended that the Reserve Bank and NZX should work together to improve New Zealand's clearing infrastructure.
- The upgraded Exchange Settlement Account System (ESAS)/NZClear⁴ system is allowing the Bank to deliver a stream of functional enhancements to users.
- International standards for system performance and resilience are being lifted.

Scope of operations

Operating the ESAS and NZClear systems, including the infrastructure required for settlement of foreign exchange transactions through Continuous Linked Settlement (CLS) Bank.

Issues

- Reviewing how the Bank and NZX should deliver clearing and settlement services.
- Enhancing ESAS and NZClear system functionality.
- Improving business continuity planning and disaster recovery capabilities, and responding to higher international operating standards.
- Facilitating the industry decision to move to 'Settlement Before Interchange' for intraday bilateral settlement and interchange of retail transactions.

Initiatives and strategies

- Complete the technical and business analysis of working with NZX in regard to clearing systems and decide on a course of action.
- Continue to make enhancements to NZClear and ESAS as agreed with industry representatives.
- Establish interfaces that will facilitate inter-operability between ESAS/NZClear and other providers' payment and settlement systems, to increase efficiency and reduce risk.
- Improve business continuity planning and disaster recovery capability for the payments system through the establishment in Auckland of a business support centre.
- Build 'Settlement Before Interchange' functionality within ESAS to replace the retail settlement function performed by ISL⁵, so reducing payment settlement risk.

Key performance indicators

- Availability of ESAS/NZClear during core hours is at least 99.95 percent, as measured over a year.
- Customer satisfaction with operations and with system development is demonstrated through an annual customer survey in which an approval level of 90 percent or more is achieved.
- All risks are well managed, as demonstrated by quarterly external audits.
- International standards for payment and settlement systems (CPSS and IOSCO⁶) are complied with.

⁴ Formerly known as Austraclear. The name changed on 26 June 2010.

⁵ ISL (Interchange Settlement Limited) is the major retail payment processing switch in New Zealand. The system is used to interchange cheques, direct debits, direct credits, automatic payments, ATM transactions, telephone banking, and internet banking. These payments are settled on a deferred net basis via NZClear during the morning settlement session.

⁶ Committee on Payment and Settlement Systems; and the International Organisation of Securities Commissions.

Organisational health and capabilities

Human resources

Objective statement

To provide strategic human resource advice and support services.

Environment

- The evolving role of the Bank and the recovering financial and economic conditions create new challenges for Bank staff.
- Staff need appropriate support, tools and resources to perform at their best during this period of change.
- The Bank will continue to provide leadership development opportunities for current and emerging leaders.
- The Bank will be continuing to recruit additional staff to carry out its expanded prudential regulation functions.

Scope of operations

- Providing strategic human resource advice and support to senior management.
- Organising specific bank-wide training and development programmes, key-role risk planning, succession planning and secondment arrangements.
- Assisting departments with change management, recruitment, employee development, contract negotiation, employment relations, legislative advice and terminations.
- Facilitating the annual remuneration review and performance management programme.

Issues

- In times of change, staff are both motivated and challenged. They need extra support and leadership as well as opportunities to extend themselves.
- Ensuring high-quality staff for the Bank through training and recruitment.
- Identifying areas where skills can be enhanced and developed to meet current and future business requirements.
- Maintaining staff wellbeing and Bank operations in the event of a crisis.

Initiatives and strategies

- Engage, develop and support staff to meet the challenges of the Bank's evolving responsibilities.
- Support management in further developing their values-based leadership competencies.
- Continue an annual review of key-role risk within the Bank and mitigation strategies.
- Enhance the Bank's staff appraisal and personal development programme.
- Facilitate excellent management processes and decision making throughout the Bank; provide a supportive environment for staff to perform at their best; and continue to develop the skills and knowledge required.
- Ensure the Bank's Values of integrity, innovation and inclusion are central to all staff initiatives.
- Complete the biennial staff satisfaction survey in 2011.
- Ensure staff are adequately informed to cope with a crisis, and that there is sufficient back-up to ensure Bank operations are maintained.

Knowledge services

Objective statement

To provide knowledge management and information technology services, direction and support.

Environment

- The technology platforms must provide a high level of uninterrupted service, functionality and security.
- The Knowledge Centre must provide easy access to a broad range of relevant information sources.

Scope of operations

- Developing and maintaining the Bank's core technology infrastructure.
- Providing business analysis and applications development.
- Delivering help desk and web support.
- Maintaining library, museum, information and records management services.
- Providing project and programme management services.
- Providing payments system support.

Issues

Managing capital expenditure to:

- maintain and upgrade information technology, information management and applications;
- provide efficient payments system services;
- enhance data management and reporting systems; and
- improve business continuity.

Initiatives and strategies

- FSIS implementation will ensure key business benefits are realised by completing the migration of remaining surveys, and developing new surveys for NBDTs and the insurance sector and for other external data.
- Ensure that users can use Bank systems effectively and efficiently. Develop systems to make our management of the information technology environment more efficient.
- Continue developing the Bank's IT Security systems to maintain industry best practice and improve our ability to respond to increasing threats.
- Refresh the Bank's website to better deliver content and services.
- Extend the Intranet and make more use of personalised and collaborative tools.
- Establish a managed information architecture and sound information management platform.
- Review and, where appropriate, upgrade or replace older internally supported computer applications.
- Improve management and archival processes around documents, email, network drive files and physical records, in line with the Public Records Act.
- Enhance and develop museum services as part of a wider public education programme.
- Continue to enhance the Bank's business continuity infrastructure, through the establishment in Auckland of a business support centre for critical functions and other back-up computing arrangements.

Internal financial services

Objective statement

To provide support services for the Bank's key financial operations, including financial reporting and management reporting; compliance with corporate governance and accountability responsibilities; settlement operations; and treasury accounting and compliance reporting.

Environment

The Bank's financial systems must be of a high standard to enable management of a very large and complex balance sheet.

Scope of operations

- Settling transactions and treasury accounting and compliance reporting in support of the Bank's domestic market operations and foreign reserves functions.
- Preparing financial statements, and carrying out monthly management and Board reporting.
- Facilitating the Bank's strategic planning and annual budgeting processes.
- Delivering financial support services and balance sheet management advice.
- Liaising with external auditors.

Issues

- Ensuring systems are constantly developed to meet changes to the Bank's financial operations and environment.
- Maximising efficiency through process improvement and systems changes.

Initiatives and strategies

- Continue to enhance workflows, reports and processes for financial operations and securities transactions.
- Revise reporting for financial market operations to give effect to portfolio management changes.
- Replace the Bank's own financial management information system during 2011.

Communications

Objective statement

To provide strategic advice and management for the Bank's external and internal communications and for the maintenance of its reputation and credibility.

Environment

- The Bank's messages and actions across its policy functions require broad public understanding to be most effective.
- This will be particularly so in the Bank's contribution to the financial and economic recovery, the development of any new macroprudential policy tools, and its expanding prudential supervision powers.
- Emerging media technologies may provide new opportunities as well as risks that require management.

Scope of operations

- Supporting the Bank's functions with communication and relationship strategies for key audiences.
- Editing and publishing Bank statements and documents.
- Sponsoring education initiatives.
- Coordinating responses to Official Information Act requests, ministerial correspondence, parliamentary questions and public inquiries.
- Supporting the Board by providing Board secretariat and administrative services.

Issues

- Ensuring the Bank's messages are informed, well constructed, easily understood, timely and delivered to target audiences through the most appropriate channels.
- Maintaining preparedness in a volatile environment by monitoring developments, news and commentaries, and coordinating with other agencies.
- Improving New Zealanders' financial literacy.
- Further enhancing internal communications.

Initiatives and strategies

- Monitor media, maintain communication relationships, and provide timely information and strategies to ensure the Bank's key messages are delivered and understood, and to address credibility risks and opportunities.
- Develop appropriate communication vehicles for the Bank's expanded role in the prudential supervision of non-bank financial institutions.
- Provide communications services for crises, including simulation.
- Enhance financial literacy, through promotion of the Bank's role as prudential regulator and support for inter-agency financial literacy programmes.

Risk assessment and assurance

Objective statement

To assist in the identification of risk and the maintenance of effective and efficient risk management; to provide assurance over operations, procedures and internal control systems; and to provide legal advice.

Environment

The Bank's financial exposure from changes in its balance sheet structure and regulatory exposure from changes in its regulatory responsibilities increase overall risks faced by the Bank.

Scope of operations

- Assisting management to identify and analyse sources of risk.
- Assisting management to design risk management systems and processes.
- Monitoring risk management implementation and providing risk management advice to Governors and the Board.
- Providing ongoing internal audit review and evaluation of the Bank's operations and control systems.
- Providing legal advice and services.

Issues

- Ensuring risks are being managed in a proactive, coordinated, prioritised and cost-effective manner.
- Identifying and managing the increased exposure to implementation risks from the expanded prudential regulatory regimes.

Initiatives and strategies

- Monitor the Bank's approach to risk management, utilising the enterprise-wide risk map.
- Continue a comprehensive internal audit programme to provide assurance on the Bank's control environment.
- Continue to provide quality legal advice.

Property management Security

Objective statement

To provide appropriate accommodation for the Bank to ensure that all functions, including cash operations, can be conducted unimpeded in a secure environment.

Environment

- An additional site is to be established in Auckland by January 2011 to ensure business continuity.
- For efficiency and environmental reasons, the Bank needs to maintain and extend energy-saving and recycling programmes.

Scope of operations

- Maintaining the Bank-owned building at 2 The Terrace, and managing leases on eight of the 14 floors.
- Maintaining a secure working environment and the safe custody of currency reserves.
- Maintaining business continuity sites in Wellington and, in the future, Auckland.

Issues

- The Bank has agreed to establish and maintain an Auckland business continuity site.
- The infrastructure of the Bank's building must be maintained at a level that promotes efficiency, soundness, effectiveness and security.

Initiatives and strategies

- Refurbish Bank accommodation as required to meet the business needs of staff.
- Assist in locating and setting up a suitable Auckland office.
- Implement cost-effective measures to further enhance energy efficiency.

Financial management

Financial structure

Balance sheet overview and funding of the Bank's operations

The Reserve Bank is both a statutory agency and a financial institution. It receives no direct funding through the central government budgetary process. Instead, the Bank's main source of income is the return on the substantial investments the Bank holds, which are funded by the issue of currency and by the Bank's equity. Currency in circulation is a liability on which no interest expense is incurred. The funds received when currency is issued are invested and earn interest income which is known as seigniorage.

The nature and extent of the Bank's principal activities impacting on its balance sheet are described in the *Annual Report 2008–2009* (pages 68–69). Foreign reserves management, New Zealand dollar liquidity management and currency operations materially impact the size and structure of the Bank's balance sheet.

Under the Reserve Bank Act, the Minister and the Governor are required to enter into a funding agreement to specify the amount of the Bank's income that may be used to meet expenses in each financial year. The funding agreement comes into force only after it is ratified by Parliament. The Act provides for each funding agreement to apply for a period of five consecutive financial years. This contrasts with the arrangements for government departments, which are funded on an annual basis. The Bank's funding arrangements are designed to strike an appropriate balance between providing a high degree of operational independence, and providing strong incentives for effective management of operating expenditure, while ensuring accountability for use of resources. Capital expenditure is funded by the Bank, with depreciation of fixed assets included in annual operating expenses. If operating expenses (net of specified revenue) in any year exceed the amount provided in the funding agreement, the Bank is required to fund that excess from equity.

The current Funding Agreement ends on 30 June 2010. The Bank and the Minister of Finance have signed a new Funding Agreement for the next five years starting 1 July 2010. At the time of writing, the new Funding Agreement is still to be ratified by Parliament.

Annual distributions paid by the Bank

Under the Reserve Bank of New Zealand Amendment Act, the Bank's annual dividend is determined using the principles listed below in the Statement of dividend principles. The Bank applies the dividend principles and makes a recommendation to the Minister of Finance of the amount to be paid. The Minister then decides how much should be paid having regard for the recommendation of the Bank, the views of the Board of the Bank and any other relevant matters.

Statement of dividend principles

The Bank should maintain sufficient equity for the financial risks of performing its functions. Equity in excess of that required to cover those risks will be distributed to the Crown.

In general, unrealised gains should be retained by the Bank until they are realised in New Zealand dollars. However, the Bank may recommend the distribution of unrealised gains where the Bank believes that the probability of the gain being realised is high.

New Funding Agreement

The 2005–10 Funding Agreement ends on 30 June 2010.

The Governor and the Minister of Finance have signed a new Funding Agreement for the next five years commencing 1 July 2010. The new agreement provides for \$47.8 million in the first year (2010–11) increasing to \$56.4 million in year five (2014–15).

The 2005–10 Funding Agreement focused on getting the Bank 'fit-for-purpose' by replacing and upgrading systems, improving business continuity capability, building capacity for new regulation and surveillance policy outputs, replacing nickel/copper coins with plated steel coins and renovating the building at No 2 The Terrace.

The new Funding Agreement, commencing 1 July 2010, has a focus of extending capacity in new regulatory and surveillance areas, and completing unfinished work upgrading information technology, business continuity and building infrastructure, in particular, establishing the Auckland office.

The new Funding Agreement was developed in an environment where central government expected its agencies to have strong expenditure control and to minimise growth in operating costs. The Bank has carefully prioritised its expenditure proposals and minimised increases in costs, without undermining the ability to deliver on the Bank's existing and new responsibilities over the term of the new Funding Agreement.

The introduction of a new series of bank notes is potentially a large project for the new Funding Agreement with a considerable cost attached to it. However, at this stage, much of the cost will fall into the subsequent five-year funding agreement period (i.e., from 1 July 2015 onwards).

Drivers of the Bank's financial performance and financial position

The principal drivers of the Bank's financial performance are:

- *The size of the Bank's open foreign exchange position and related changes in foreign exchange rates.*
In 2007, the Bank changed its exposure to foreign exchange risk after concluding that it could better meet its statutory responsibilities by holding a portion of foreign currency reserves on an unhedged basis. The Bank established a benchmark holding of SDR 1.0 billion unhedged foreign reserves with the ability to hold more or less than the benchmark over the exchange rate cycle. During the financial crisis, the benchmark was temporarily increased to SDR 1.5 billion.

The unhedged foreign reserves position was initially held in three currencies – US dollars, euro and Japanese yen. The range of currencies has since been expanded to also include British pounds, Australian dollars and Canadian dollars.

Holding unhedged foreign reserves means that the Bank's net equity will fluctuate with changes in the exchange rate: foreign exchange losses may be incurred when the New Zealand dollar is strong and gains may be recorded when the New Zealand dollar is weak. The unhedged foreign reserves position in particular will cause increased volatility in the Bank's financial performance and financial position.

At 30 April 2010, the Bank held an open foreign exchange position of SDR 1.46 billion (NZD 3.03 billion), down from SDR 1.62 (NZD 3.88 billion) at 30 June 2009.

- *The value of currency in circulation.*

Currency in circulation is a non-interest-bearing liability. Trading banks are charged for currency issued to them and the Bank earns interest on investment of these amounts paid by trading banks. Currency in circulation typically grows by around 4 percent per annum. In 2008, currency in circulation increased by 14 percent to \$3.9 billion. The sharp increase in currency issued occurred due to a short-lived and temporary surge in the public's demand for bank notes that occurred prior to announcement of the government's Retail Deposit Guarantee Scheme. Annual growth in currency in circulation has now returned to more typical levels, but as noted above can vary sharply from year to year.

At 30 April 2010, currency in circulation was \$3.98 billion.

- *Interest rates earned on the Bank's investment in government securities and other securities.*

Under the New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), the Bank's holdings of New Zealand government securities are valued at market value, with unrealised gains and losses on those holdings booked to equity.

This valuation methodology for the Bank's holdings of New Zealand government securities results in more variability in the Bank's financial performance and financial position than under previous valuation methodology.

- *The size and performance of the Bank's foreign reserve management and market operations functions.*

The Bank has increased its holdings of foreign reserves that can be liquidated at short notice to support its functions, including monetary policy objectives and the maintenance of orderly markets. The composition of the Bank's foreign currency assets is also likely to change in light of information on asset liquidity during stress times gained during the financial crisis.

Since 2006, the Bank has managed its New Zealand dollar liquidity management operations by significantly increasing the level of settlement cash held by financial institutions.⁷ This change added around \$7 billion

⁷ See RBNZ *Annual Report 2006-2007*, page 25.

to assets and liabilities reported on the Bank's and Crown's balance sheets.⁸ In 2008, the Bank introduced a range of temporary measures to support New Zealand dollar liquidity in response to global market disruptions. Some of these measures were removed as market conditions improved during 2009 and early 2010 and the New Zealand banks gained improved access to funding.

- *Operating expenditure incurred by the Bank.*

As noted in the previous section about the new Funding Agreement, the level of operating expenditure is expected to increase over the next five years, reflecting further expansion of the Bank's financial system regulatory and surveillance capacity, improvement of business continuity capabilities, commencement of changes to currency in circulation and the renewal and replacement of systems.

- *The level of equity available for investment and the dividend paid by the Bank.*

The Bank requires equity to absorb any losses arising from carrying out its functions. In 2004, the Bank received an equity injection of \$1 billion to give it the financial capacity to intervene in foreign currency markets. In 2008, the Bank received an additional \$600 million as a buffer to protect reported equity from potential changes in the valuation of New Zealand government securities under NZ IFRS.

Equity is reviewed annually during the process to determine the Bank's annual dividend with equity in excess of that required to cover the Bank's risks paid to the Crown. In August 2009, the Bank paid a dividend for the 2008–09 year of \$630 million to the Crown. This dividend amount included realised foreign exchange gains of \$434 million.

In March 2010, an interim capital review was conducted and a voluntary payment of \$45 million was made to the Crown.

Principal financial risk management considerations

As a financial institution with more than \$20 billion in assets, the Bank faces a wide range of financial risks. These arise mainly because of the Bank's operations in the domestic financial system and because of the Bank's holdings of foreign exchange reserves. The risks include:

- credit risks and market risks associated with day-to-day dealings with financial institutions, in the process of managing liquidity in the financial system;
- risks associated with the Bank's holdings of foreign currency reserves, including credit risk, liquidity risk, interest rate risk and exchange rate risk; and
- operational risks in the transactions and processing areas of the Bank.

More detailed information on the Bank's approach to managing these risks is outlined on pages 83–95 in the *Annual Report 2008–2009*.

⁸ The rationale for this change is explained in the document *Reform of the Reserve Bank of New Zealand's Liquidity Management Operations, June 2006*, which is available on the Bank's website: www.rbnz.govt.nz.

Financial projections

The following table outlines the Bank's budgeted income and expenditure for 2010–11. The budgeted income and expenditure have been prepared using the accounting policies used in the preparation of the Bank's financial statements for the year ended 30 June 2009.

The key assumptions underlying the budget for the year ended 30 June 2011 are that:

- the Bank's current functions will continue, with the Bank commencing prudential supervision of non-bank financial institutions and insurers;
- the Bank will maintain an open foreign currency position during the year equal to \$3.03 billion, being the position at 30 April 2010;
- interest and exchange rates will be those prevailing as at 30 April 2010;
- there will be no change in the credit worthiness of the Bank's counterparties; and
- there will be no material changes to the Bank's liquidity management operations.

The following table sets out projected income and expenditure for the Bank for the year ended 30 June 2011.⁹

Projected financial performance 2010 – 2011

	Budget
<i>For the year ended 30 June</i>	2010-11
	\$m
Operating income:	
Net investment income	246.5
Other income	7.8
Total operating income	254.3
Operating expenses:	
Personnel	28.4
New currency issued	5.4
Asset management	7.5
Administration	1.4
Other	12.8
Total operating expenses	55.5
Operating surplus	198.8

⁹ The Bank's accounting policies are disclosed in its *Annual Report 2008–2009* on pages 61–67.

The budget is based on an assumption that no changes to interest rates or foreign exchange rates will occur during the financial year and the Bank retains for the full year its open foreign exchange position that it held at 30 April 2010.

It is important to note that the Bank's assets and liabilities are sensitive to changes in interest rates and exchange rates, and that actual financial results could differ materially from those budgeted.

At 30 April 2010, a 10 percent appreciation in the value of the New Zealand dollar would reduce the Bank's comprehensive income¹⁰ by \$276 million, and conversely a 10 percent depreciation in the value of the New Zealand dollar would add \$337 million to comprehensive income. A 1 percent across-the-board increase in interest rates would reduce comprehensive income by about \$149 million, and a 1 percent across-the-board reduction in interest rates would increase comprehensive income by about \$154 million.

Net expenditure by function

<i>For the year ended 30 June</i>	Net Expenditure [†]	
	Budget	
	2010-11	
	\$000s	
Functions:		
Monetary Policy Formulation		10,203
Market Operations		6,900
Financial System Surveillance/Policy		13,328
Currency Operations		9,655
Foreign Reserves Management		6,781
Settlement Services		702
Registry and Depository Services		(382)
Other Outputs		573
Net expenditure		47,760
Net expenditure provided for in the Funding Agreement		47,800
Funding Agreement Under-Expenditure		40

† Net Expenditure comprises operating expenses less income earned from certain Bank operations as specified in the Funding Agreement.

¹⁰ Comprehensive income includes earnings booked to the Bank's Income Statement and also changes booked directly to equity. The majority of sensitivity to changes in foreign exchange rates is booked to the Income Statement, whereas the majority of interest rate sensitivity arises on the Bank's portfolio of New Zealand government securities and is booked directly to equity. Refer to page 88 of the Bank's *Annual Report 2008-2009* for a detailed sensitivity analysis as at 30 June 2009.

Regulatory Plan

As part of the Government's commitment to improving the quality of regulation, the Bank will undertake systematic and ongoing scanning of its existing legislation and regulation to identify whether it may be unnecessary, ineffective or excessively costly in achieving the Bank's objectives.

The Bank has for many years been charged with prudential oversight of New Zealand banks. New Zealand has a light-handed regulatory regime for its banks that relies for much of its force on the regular public disclosure of prudential information to all investors. We have begun a review of the General Disclosure Statements that are published by banks under this regime, with a view to reducing the reporting requirements and compliance costs, while ensuring the reporting still serves its purpose of keeping investors adequately informed.

We have also undertaken an initial review of legislation and regulations administered by the Bank and identified some that are no longer required and could be revoked.

The Bank has recently been mandated to expand its prudential regulation role beyond banks to NBDTs and the insurance sector. The purpose of this regulatory expansion is to promote the maintenance of a sound and efficient financial system, and avoid significant damage to the financial system that could result from the failure of a non-bank deposit taker.

In the period covered by this *SOI*, the Bank intends to introduce regulations to implement the NBDT regime covering NBDT capital and liquidity; and will seek new legislation to provide for licensing of NBDTs, enhanced information gathering by the Bank, and direction-giving powers. The Bank will also develop regulations necessary to implement the prudential supervision regime for the insurance sector.

The Bank will introduce new regulation only when we are satisfied that it is required, reasonable and robust in terms of its efficiency and effectiveness.

Monitoring the Bank's performance

The Bank has been, and will continue to strive to be, a world leader in the openness and transparency of its processes and policies. Transparency assists the Bank to achieve its policy and operational goals effectively and efficiently, while allowing others to scrutinise the Bank's performance and to provide feedback, so helping the Bank improve the way it works.

The principal mechanisms for externally communicating the Bank's views each year include:

- eight OCR decisions, four of them in the quarterly *Monetary Policy Statements*;
- two *Financial Stability Reports*;
- the Bank's *Statement of Intent*, *Annual Report* and financial statements;
- four *Bulletins*;
- the Bank's website (www.rbnz.govt.nz);
- occasional publications and issue-specific books and brochures; and
- addresses given by the Governor and other senior Bank staff.

The Bank formally assesses its performance or is externally assessed in the following ways.

The Board reviews the Bank's performance and the discharge of its statutory obligations. In addition to providing the Governor with ongoing advice and feedback, the Board is also required to report annually on the Bank's performance. The Board's report is published in the Bank's *Annual Report*.¹¹

The Audit Committee of the Board reviews the Bank's financial statements and provides advice to the Governor before the Governor and Deputy Governor sign the related management statements. It also monitors the Bank's internal audit function.

The Bank publishes its *SOI* at the commencement of each financial year. The *SOI* sets out the Bank's principal functions, objectives, strategies and key performance indicators for the next three years; comments on strategies for managing organisational health and capability; sets out initiatives and projected income and expenditure for the first year of that three-year period; includes a statement of principles determining the annual dividend payable to the Minister; and outlines the Bank's Regulatory Plan for the year.

The *Annual Report* includes both the financial statements and an assessment of the performance of the Bank's various functions, in terms of both the day-to-day responsibilities and progress against priorities and key performance indicators published in the *SOI*. It is tabled in Parliament.

Parliament's Finance and Expenditure Committee reviews the quarterly *MPS*, the six-monthly *FSR* and the Bank's *Annual Report*, and can ask the Bank to appear before it on request.

Under section 167 of the Act, the Minister may, from time to time, initiate an assessment of the Bank's performance and how it has exercised its powers under the Act.

¹¹ For example, see pages 6–9 in the *Annual Report 2008–2009*.

The Bank is subject to Cabinet's Regulatory Impact Analysis requirements, ensuring that proposals involving regulatory options are subject to careful and robust regulatory analysis, and that a regulatory solution is required in the public interest. The Bank undertakes extensive consultation on proposed legislation and regulation.

The Bank's financial statements are audited by external auditors who are the agent of the Controller and Auditor-General. The critical payment systems operated by the Bank are subject to review by external auditors quarterly in respect of the NZClear depository system, and annually in respect of ESAS. An annual report is presented to NZClear members.

From time to time, the Bank engages experts to assess the Bank's processes, research and technical performance. In the past, assessments have been provided in the fields of monetary policy development; financial system policy; forecasting processes; bank-failure management; computer systems and network security; management; and leadership assessment and development. The Bank funds a Professorial Fellowship in Monetary and Financial Economics at Victoria University of Wellington. Also, two external advisers assist in the provision of advice to the Governor regarding his interest rate decisions. Prior to the release of the *MPS*, these two advisers participate in the deliberations leading to the formulation of the *MPS*.

The Bank's performance is also subject to international scrutiny. Every 12 to 18 months, the International Monetary Fund (IMF) undertakes an 'Article IV' assessment of the New Zealand economy, which includes sections on monetary policy and financial system stability. The resultant report is made public. Likewise, every two years, the Organisation for Economic Co-operation and Development undertakes a similar assessment, which is also published. The IMF is expected to undertake a Financial Sector Assessment Programme investigation every six or seven years; the last was in 2003.

Appendix A

Key document references

Title	Purpose	Location
Policy Targets Agreement	Agreement between the Governor and the Minister of Finance required under s9 of the Act, specifying the monetary policy target in detail	http://www.rbnz.govt.nz/monpol/pta/index.html
<i>Monetary Policy Statement*</i>	Quarterly publication of the Bank's view of how it proposes to meet its monetary policy targets, including extensive economic projections, required under s15 of the Act	http://www.rbnz.govt.nz/monpol/statements/
<i>Financial Stability Report*</i>	Six-monthly publication of the Bank's view on the soundness and efficiency of the New Zealand financial system, required under s165A of the Act	http://www.rbnz.govt.nz/finstab/fsreport/index.html
<i>Annual Report*</i>	Key accountability document, plus presentation of financial statements, required under ss163-165 of the Act	http://www.rbnz.govt.nz/about/whatwedo/0094054.html
Board of Directors' <i>Annual Report</i>	Board of Directors' report on the Bank's performance required under s53A of the Act	Reproduced in the Bank's Annual Report http://www.rbnz.govt.nz/about/whatwedo/0094054.html
Briefing on the Reserve Bank of New Zealand*	Description of the role and functions of the Reserve Bank, prepared for an incoming government	http://www.rbnz.govt.nz/about/whatwedo/0122541.html
Reserve Bank of New Zealand Act 1989	Reserve Bank's statutory authority	www.rbnz.govt.nz/about/ourlegislation/
Funding Agreement	Basis of Bank's funding, setting how much of the Bank's revenues can be retained by the Bank, in accordance with ss159-161 of the Act	http://www.rbnz.govt.nz/about/whatwedo/1845734.html
<i>Statement of Intent*</i>	A statement of what the Bank intends to achieve over the next three years, with forecast income and expenditure for one financial year, in accordance with ss162A-E of the Act	http://www.rbnz.govt.nz/about/whatwedo/1764296.html
Letter to Minister of Finance on foreign exchange market intervention policy	Description of how the Bank may intervene in the foreign exchange market under section 16 of the Act to influence the exchange rate	http://www.rbnz.govt.nz/finmarkets/foreignreserves/intervention/0148214.html
Memorandum from the Minister of Finance to the Bank on foreign exchange intervention	Provision of delegated authority for the Bank to intervene in the foreign exchange market under section 17 of the Act, should that market become dysfunctional	http://www.rbnz.govt.nz/finmarkets/foreignreserves/intervention/0148293.html
Reserve Bank <i>Bulletin*</i>	Quarterly publication of articles relevant to central banking in New Zealand	http://www.rbnz.govt.nz/research/bulletin/
Statement of Principles	Explanation of the Reserve Bank's approach to bank registration and supervision under s75 of the Act	http://www.rbnz.govt.nz/finstab/banking/regulation/3272066.pdf
<i>Annual Report for the NZClear NZ System</i>	Accountability document on the performance of the NZClear NZ system	http://www.rbnz.govt.nz/payment/austraclear/3748533.pdf
Vision Statement and Values	Expression of the Bank's vision and culture	Inside front cover of <i>Annual Report</i> http://www.rbnz.govt.nz/about/whatwedo/0094054.html

* Also available in print from: the Knowledge Centre, Reserve Bank of New Zealand, PO Box 2498, Wellington, New Zealand. knowledge@rbnz.govt.nz, www.rbnz.govt.nz