9 March 2018

Toby Andres
STC Project Management
Reserve Bank of New Zealand
P O Box 2498
Wellington 6140

By email: stcproject@rbnz.govt.nz

Dear Toby

**ANZ submission on the review of mortgage bond collateral standards**

Thank you for the opportunity to respond to the consultation paper: ‘Review of mortgage bonds collateral standards’ *(mortgage bond paper)* released in November 2017.

ANZ Bank New Zealand Limited (ANZ) submits that New Zealand mortgage bond standards should be based on structures that already exist and are well understood in the New Zealand and Australian markets (among others), rather than a prescriptive model which introduces concepts from European mortgage bond markets that have different underlying mortgage markets and legal frameworks.

Together with other issuers of retained RMBS (iRMBS), we have separately proposed an alternative RMBS structure which we think can meet the RBNZ’s objectives within existing structures. We would welcome the opportunity to discuss this proposal with the RBNZ.

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**Key messages**

1. ANZ submits that the structure of the RMO standard is overly prescriptive, contains features which are not consistent with market practice in the Australasian market, includes portfolio limits and mandatory structuring requirements that would severely limit issuance, and would not contain sufficient flexibility to adapt to changing market conditions.

2. ANZ submits that the term sheet prepared on behalf of iRMBS issuers (submitted separately) provides a better basis for meeting RBNZ objectives while conforming more closely to Australasian market norms, regulatory/legislative requirements and international guidelines.
Format of submission

This submission comprises seven parts.

- Section I provides more detail around each of the above key messages.
- Section II provides responses to the specific questions from the consultation paper.

- Appendix III - Comparison of RMO Requirements with Australian and ECB Repo-Eligibility Criteria and Simple, Transparent and Standardised Rules.

Publication of submission

ANZ consents to the publication of this submission, with certain aspects withheld to protect the privacy of natural persons or on the grounds of commercial sensitivity, under the RBNZ’s publication of submissions policy. ANZ considers that the redacted information should be withheld if a request for it is made under the OIA on the basis that:

1. The information has been supplied to the Reserve Bank in connection with a consultation on the possible exercise of its powers under Part 5 of the Reserve Bank of New Zealand Act, and therefore may not be disclosed pursuant to sections 105(1)(c) and 105(2) of the Reserve Bank of New Zealand Act 1989
2. Making available the information would be likely to unreasonably prejudice ANZ’s commercial position, and therefore the information may be withheld under section 9(2)(b) of the Official Information Act 1982.

About ANZ

ANZ is the largest financial institution in New Zealand, and offers a full range of financial products and services including a significant range of financial advisory services, personal banking, institutional banking and wealth management products and services. ANZ is a Qualifying Financial Entity and employs one of the largest QFE Adviser networks as well as Authorised Financial Advisers.
Contact for submission

ANZ is keen to discuss our responses directly with RBNZ officials. Please contact me on [Redacted] to arrange, or email [Redacted]

Once again, we thank RBNZ for the opportunity to provide feedback on the mortgage bond paper.

Yours sincerely

[Redacted]

Paul Daley
Treasurer
Section I - Key messages

ANZ addresses each of the key messages in turn:

1. **ANZ submits that the structure of the RMO standard is overly prescriptive, contains features which are not consistent with market practice in the Australasian market and includes portfolio limits and mandatory structuring requirements that would severely limit issuance, and would not contain flexibility to adapt to changing market conditions.**

   ANZ submits:
   - The RMO Standard goes far beyond simple, transparent and comparable guidelines ("STC Guidelines") and the requirements of comparable jurisdictions such as Australia, under which none of the following features of the RMO Standard are required: standard documentation, standardised tranching, portfolio parameters, inability for the originator to provide bank accounts and hold collections while it has the requisite credit rating, mandatory use of the moderate balance principle, mandatory trapping of excess spread, cross-collateralisation across series, mandatory alternative servicing, dedicated servicing personnel, minimum experience criteria and so forth;
   - A common set of documents is impractical and will be difficult to implement because of differences between loan products and origination and servicing processes and systems among banks;
   - Certain features of the RMO Standard such, as the moderate balance principle, borrow heavily from other markets which have mortgages that are quite different from those of New Zealand. Many elements of the proposed mandatory structuring are not suitable for the NZ market;
   - Some features of the RMO Standard do not sit well under New Zealand law and could preclude bankruptcy-remoteness from the originator;
   - A rating will be essential for marketability and liquidity. RMO is proposed as an unrated instrument, some of the features of which may not be compatible with obtaining a rating;
   - Investor appetite is unlikely to be constant regardless of market conditions. Originators need the ability to structure to meet investor demand;
   - The proposed portfolio limits and restrictions around replenishment are likely to severely reduce potential issuance and will not allow scalability;
   - Many elements of the RMO standard appear to be designed to create a risk-free asset, which is likely to distort markets by providing a level of support not normally permitted by regulators under securitisation standards and result in the cherry-picking of assets to the detriment of unsecured creditors and depositors.

2. **ANZ submits that the term sheet prepared on behalf of iRMBS issuers (submitted separately) provides a better basis for meeting RBNZ objectives while conforming more closely to Australasian market norms, regulatory/legislative requirements and international guidelines.**
ANZ submits that a mortgage bond structure based more closely on existing market norms is capable of meeting the RBNZ’s objectives without introducing concepts from European mortgage bond jurisdictions that may not be compatible with the New Zealand market and regulatory environment.

ANZ believes that the jointly submitted term sheet would:

- be acceptable to current iRMBS issuers, current external RMBS issuers and investors;
- meet STC criteria
- be consistent with rating agency criteria
- allow RBNZ’s objectives to be achieved via setting suitable eligibility criteria and subordination levels
- be easier and less costly to implement
- be compatible with international standards
**Section II – ANZ’s responses to the questions raised in the RBNZ’s consultation paper: ‘Review of mortgage bonds collateral standards’**

<table>
<thead>
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<th>Part A</th>
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<td><strong>Section 1.1</strong></td>
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<tr>
<td><strong>Existing iRMBS programmes</strong></td>
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<tr>
<td>1. ANZ, along with other major banks, understands the Reserve Bank of New Zealand (&quot;RBNZ&quot;)’s desire to improve the design of mortgage-based repo-eligible collateral.</td>
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<td>2. Existing iRMBS programmes were established during the GFC and were not established with the intention of bonds being distributed externally. This was understood by the RBNZ at the time.</td>
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<td>3. Given this, some of their characteristics were intended for ease of administration.</td>
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<td>4. However, the underlying quality of the iRMBS portfolios and the amount of subordination in the structures (which together define ‘safety’) are not materially different to that implied by the proposed RMO criteria (See Appendix 1).</td>
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<td>5. The ‘technology’ on which ANZ’s programme is based (the charitable trust owned SPV model) is ‘market standard’ in Australasia (and other common law countries) and the existing programme largely conforms to STC criteria.</td>
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<td>6. In ANZ’s view, existing iRMBS programmes could be modified relatively easily to meet the RBNZ’s objectives and STC criteria.</td>
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<td>7. We think this would provide a better starting point for achieving the RBNZ’s objectives than a mortgage bond model based on different mortgage products than those offered in New Zealand and a different legal framework to New Zealand’s.</td>
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<td><strong>Question A1</strong></td>
<td>A1: Do you agree these characteristics are appropriate to seek in eligible capital?</td>
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<td>8. These characteristics (high quality, liquid, scalable and non-distortionary) would obviously be desirable in any repo-eligible asset.</td>
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<td>9. However, in ANZ’s view, the RMO structure is not the only way to achieve them and, in fact, the RMO would not achieve them (see our comments on ‘Scalable’ below, paras 34-38).</td>
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<td>10. We believe it would be better for the RBNZ to adopt a principles based</td>
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10. This approach, which provided high level guidelines in relation to key criteria and left it up to each originator to make changes to their iRMBS programme to bring it into line.

11. Guidelines would reflect alignment between regulators, investors and issuers regarding the characteristics of the mortgage bonds created in respect of their safety, risk versus return and cost. We don’t think the performance or complexity of New Zealand mortgages, or the nature or performance of iRMBS, warrants the regime proposed under the RMO standard.

12. A principles based approach would be consistent with comparable jurisdictions and reduces the risk of unforeseen outcomes through the introduction of an untested standard, which draws heavily from jurisdictions with mortgage markets which are quite different from New Zealand’s. We see greater benefits in trying to develop a set of New Zealand, high level guidelines harmonised with those already successfully operating in Australia, rather than introducing something completely new which is far more onerous than anything currently required internationally.

13. However, given the RBNZ’s desire to see some uniformity in RMBS, we have worked with other major iRMBS banks to produce a high level terms sheet based on standard RMBS structures which we think gives an acceptable base for discussion with the RBNZ. This has been provided separately to the RBNZ.

14. **High Quality:** ‘Quality’ in the context of the senior tranches of a securitisation is defined by:

   - The quality (i.e. expected credit performance) of the underlying collateral;
   - The amount of subordination in place (whether it is in the form ‘capital’, over-collateralisation (in the case of covered bonds) or subordinated debt) to absorb unexpected losses in the loan pool.

15. These factors are not independent of each other. In a typical securitisation, the minimum amount of subordination is determined in conjunction with the relevant rating agency or agencies, following an analysis of the collateral (amongst other factors), to achieve the desired rating for the senior tranches. In general, issuers want to achieve the highest quality (AAA/Aaa) available for the senior tranche.

16. We agree that it is appropriate for mortgage bond collateral to be high quality. In the case of ANZ’s iRMBS, there is no material difference in performance between the loans backing the iRMBS and the wider ANZ mortgage portfolio which has performed very well historically.

17. Further, we note that the portfolio composition and the credit support (subordination) of ANZ’s current iRMBS is largely equivalent to the level being...
sought for the RMO. We don’t see the RMO being materially safer (i.e. of higher quality) than our current iRMBS, when the actual risk is assessed.

19. We understand that the RBNZ is looking for consistent collateral standards across all originators. We think this is reasonable, in principle, and that this would be best achieved via some strengthening of the minimum eligibility criteria. However, we have concerns that some elements of the proposed standard will lead to cherry-picking of the least risky loan assets leading to the collateral pool not broadly reflecting the overall portfolio (which is also seen as desirable by the RBNZ) to the detriment of unsecured creditors and depositors. Homogeneity in the context of the STC criteria refers to the assets in a given pool rather than comparisons across different securitisations.

22. We note that many elements of the RMO standard seem to borrow from Danish mortgage bonds. However, we also note that the Danish mortgage market and New Zealand mortgage market are quite different. Danish mortgages appear to be either long term fixed rate loans or floating rate loans at a constant spread over a wholesale short term index. Loans can be repaid at par (similar to the US market).

23. This type of mortgage lends itself to the ‘moderate balance’ principle outlined in the paper, as minimal hedging is required.

24. However, Danish mortgage bonds also leave the investor with considerable interest rate and option risk, as the investor has effectively written an interest rate put to the mortgage borrower/mortgage bond issuer.

25. New Zealand originators offer borrowers mortgage loan products with differing features and borrower ability to significantly change interest rate profiles over the life of the loan. Originators have different systems and credit underwriting and servicing processes. The underlying loans themselves will be similar but they are not fungible. They are not consistent with a ‘moderate balance’ principle.

26. The New Zealand mortgage market is also quite different from markets such as the United States which experienced problems during the global financial crisis. In general, we do not have an “originate to distribute” model in New Zealand. Originators are largely originating loans for their own balance sheets and already retain the risk on them.

27. The composition of the portfolio backing securities will change over time due to amortisation and prepayments regardless of the parameters which apply at transaction closing. Therefore, the risk characteristics could change significantly. We believe investors will be focused on the composition of the portfolio at the
time of purchase of the securities and the performance track record of the originator when assessing comparability and the quality of the portfolio.

29. **Liquid**: The deficiencies noted by the RBNZ in relation to liquidity reflect that the current iRMBS structures were designed as safe collateral for the RBNZ to allow it to provide contingent liquidity to originators during liquidity crises. This does not mean that current iRMBS programmes cannot be amended to improve their marketability. We don’t think it is necessary to introduce a completely new standard to achieve this.

30. We do not believe the only way of obtaining pricing indications is to place the securities with the market. The Reserve Bank of Australia has an established model for valuation which could be adopted. Investors will generally look to the more active Australian market for pricing comparisons.

31. The RBNZ also assumes that investor appetite for the proposed structure will remain constant regardless of market conditions. Typically, this is not the case. We think it is important to be able to structure securities to meet investor demand and market conditions at the time of placement.

32. The lack of a rating is likely to limit potential investors as investor mandates usually require a public rating. We note that iRMBS already have AAA ratings and reflect rating agency criteria with which investors are already familiar. We question the cost, time and effort of obtaining a new rating for an untested structure which would never be able to achieve a rating higher than AAA.

33. ANZ acknowledges that it has not issued RMBS securities to the market. The reasons for this are:
   - **Cost**: The weighted average yield at which prime RMBS securities are typically issued in the Australasian market is generally higher than equivalent unsecured funding levels.
   - **Administrative overhead**: Given that the issue costs are higher than alternatives, the administrative time and complexity associated with any securitisation is not warranted
   - **Crowding out**: The combined major-bank balance sheets exceed the size of the managed funds market in New Zealand by some way. It is likely that purchases of RMBS would result in lower purchases of senior debt by some investors.

34. **Scalable**: We agree that residential mortgages provide the largest pool of potential collateral to support secured borrowing. However, the imposition of the RMO pool level limits, in addition to eligibility criteria and discrete pools, will prevent transactions occurring at short notice and severely limit issuance volume.

35. As noted above, banks will still need to apply their own filters for operational and practical reason
38. In order to maximise scalability, ANZ’s proposed solution is that existing iRMBS programmes be maintained as open pools under an agreed framework, but that they become closed pools whenever repo-ed with the RBNZ. External RMBS would be undertaken periodically to demonstrate liquidity and marketability and provide pricing transparency. Pool level limits should not apply as portfolios should be reasonably consistent with those of the originator to avoid situations where assets are cherry-picked. This is similar to the Australian approach where self-securitisations do not have to meet the APS120 funding-only securitisation criteria until they are repo-ed with the RBA. This is the approach we think would best allow the amendment of iRMBS to better meet the RBNZ’s objectives, without adversely impacting on depositors and unsecured creditors.

39. **Non-Distortionary:**

42. We do not agree that iRMBS are ‘distortionary’.

**Lack of liquid assets in New Zealand**

43. A theme in the consultation paper is a supposed shortage of safe or ‘liquid’ (i.e. repo-eligible) assets in New Zealand.

44. In a liquidity crisis situation ‘liquid’ is defined by the central bank’s willingness to purchase or lend against an asset. What is ‘liquid’ in ‘normal times’ is largely irrelevant during a crisis. Therefore, in answer to question A2, banks will generally hold any asset as a ‘liquid asset’ that the central bank deems to be repo-eligible. The proportion of each asset that banks will hold will be a function of its availability and cost.

45. We understand that Figure 2 shows:

- Total bank liquid assets, which total approximately $62bn
• Divided by the total balance sheet assets of banks, fund managers and insurance companies (~$750bn)
• This gives a ratio of bank liquid assets to total financial market assets of ~8%.

46. In ANZ’s view, this ratio gives a misleading picture of available NZ dollar liquid assets. The major banks hold:
• $11bn of ~$75bn outstanding NZGB
• $10bn of ~$25bn outstanding Kauri bonds
• $4bn of ~$10bn outstanding local authority bonds

47. Adding other outstanding repo-eligible assets to bank holdings gives total outstanding repo-eligible assets of at least $147bn, which is a ratio of ~19% of the total balance sheets above. (If NZGB/Kauris held offshore are excluded the ratio is ~13%).

48. While substantial volumes of NZGB and Kauris may be held offshore, this is simply a function of individual market participants’ views on returns and risks. Very large volumes of ‘liquid’ assets exist in NZ dollars.

49. Question A2

A2: Do you see scope for RBNZ counterparties to hold other satisfactory collateral?

51. In a liquidity crisis, the only securities that can be defined as ‘liquid’ are securities that are repo-eligible at the central bank. Other non-NZGB assets that the RBNZ will accept on repo, and are therefore ‘liquid’, include: Kauri bonds, local authority bonds and some SOE bonds. In ANZ’s view these are satisfactory as repo eligible assets.

52. However, banks would not be able to liquidate these types of securities into the market in anything like the volumes that might be required by the banking system. It is only their status as repo-eligible instruments that encourages banks to hold them in current volumes.

53. In a liquidity crisis we also doubt whether the market would be able to absorb NZGB in the volumes the banking system might seek to liquidate given non-banks’ asset positions at any point in time. To purchase or repo securities from the banks, market participants would need to raise cash from either their bank accounts (which defeats the purpose from banks’ viewpoint) or themselves liquidate other assets somehow.

54. The RBNZ determines which entities can use access its repo facilities. It can increase the scope of that if it wishes. In ANZ’s view, the particular instruments that each entity might repo are not relevant to the proposition the RBNZ is
A3: Do you agree that i-RMBS and covered bonds are unlikely to meet the Reserve Bank’s ‘ideal’ criteria for eligible collateral set out above?

55. No

56. We think iRMBS with some structural amendments can meet the criteria as well as RMO. ANZ does not see a lot of difference between iRMBS and the RMO in this regard.

57. We think covered bonds would better meet the criteria than RMO.

58. iRMBS can be amended relatively easily to comply with a set of guidelines without going down the route of a highly prescriptive standard and it would be preferable to do that rather than introducing RMO. We also question whether RMO is the correct solution for some of the RBNZ’s perceived problems, as follows:

a. iRMBS are already structured to be bankruptcy remote from the seller. Some of the aspects of iRMBS which were specifically put in place to facilitate bankruptcy remoteness are not included in the proposed RMO structure and may adversely impact on it. For example:
   i. the trust manager should not be an “associated party” of the originator,
   ii. the beneficiary should be a charity, and
   iii. a bankruptcy remote issuer in New Zealand wouldn’t have any employees.

The alternatives proposed for the RMO may in fact result in it not being bankruptcy remote.

New Zealand covered bonds use the same ownership structure of an SPV as iRMBS. We note that specific legislation was necessary to remove any ambiguity in relation to bankruptcy remoteness.

b. The RBNZ finds current documentation too complex. We doubt that the documentation will be less complex for RMO than for iRMBS, given that RMO are effectively RMBS.

It is highly likely that some customisation between issuers will be required due to the different systems, operational processes and loan products of the different originators, which will mean that different originators will end up with different documents or one set of documents will need to cover multiple permutations to accommodate all originators.

It would be much simpler for originators to amend and align their existing documentation to meet high level guidelines than to try and negotiate a common set of documents which satisfies all originators, the RBNZ and the
c. The proposed “capital centre” for each series (with excess spread from one series supporting other series) is not used in New Zealand securitisation transactions. If such a feature can be incorporated (we have doubts it would comply with APS120) it is likely to make RMO more complex rather than less complex than iRMBS.

d. Para 16 of Part A: We disagree with your assumption that our existing transaction would not be attractive to investors:

- The ANZ iRMBS is AAA rated with a sequential payment structure. This is more conservative than typical RMBS and more conservative than the payment structure proposed under the RMO. This would undoubtedly be attractive.

- Amending existing iRMBS structures to become a closed pool as soon as securities are repo-ed with the RBNZ would mean that the analysis of their expected life, portfolio composition, etc. would be no more complex than traditional RMBS.

e. We do not think it is appropriate for the RBNZ to assume a structuring role. The RMO standard includes a rigid structure but has no methodology articulated behind what is proposed and why this is appropriate for all loan products and portfolios in the New Zealand market now and in the future.

Who is going to undertake the investor education process regarding the rationale for this structure and why the proposed tranching is appropriate in all current and future circumstances and for all portfolios? Is this a function that the RBNZ is proposing to undertake itself?

f. iRMBS reflect rating agency methodology, with which investors are already familiar, tailored to the New Zealand market. The consultation paper does not refer to a similar basis to support the RMO structure and the paper does not seem to see a role for rating agencies in this market. As discussed above (in para 32), most investors would require a rating to invest in any new instrument.

60. However, we note that the RMO includes issuance of a shorter term security to fund longer term assets, or, in any event, a security that is marketed to investors as short term. The amount of this tranche is based on an arbitrary range of portfolio outstandings rather than any analysis of payment rates, delinquencies, defaults, prepayment speeds, etc. and is further complicated by the requirement that such a tranche be supported exclusively by fixed rate loans. The amount of a fast pay tranche, if this is mandatory, has to be based on the characteristics of
the assets rather than arbitrary structuring standards. (See also our response in para 82 on investor mandates.)

61. As discussed in paragraphs 22 to 24 above, given the nature of mortgage products in the New Zealand market, the concept of ‘moderate balance’ would be very difficult to implement and would further limit the potential portfolio to support RMO transactions.

62. Para 16c of Part A: common guidelines for minimum reporting could be agreed and incorporated into iRMBS documentation. You do not need the RMO structure to do this.

63. Para 16d of Part A: we would propose to deal with the issue of minimum collateral quality through a common set of eligibility criteria. Again, this can be done through amending existing documentation. The time, expense and complexity of RMO are not warranted in order to make this change.

**Question A4**

**A4: Would there be benefits from making mortgage bonds tradable to liquidity providers other than the Reserve Bank including in normal times or periods of distress?**

64. No, other than some price transparency.

65. In ANZ’s view, ‘liquidity providers other than the Reserve Bank’ is a misnomer with respect to any entity in the New Zealand market.

66. During normal times, domestic buyers of ANZ securities are simply providing funding in the normal course of business, based on their own flows of funds and asset allocation criteria. They are no different from depositors in this regard.

67. During times of liquidity stress, by definition, normal lenders to banks become unwilling to lend. If a non-bank entity purchased repo-eligible securities from a bank it must either liquidate another asset, which would be difficult to do, or itself be able to liquefy the repo eligible asset with RBNZ.

68. In ANZ’s view, the only liquidity provider in the New Zealand system in a stress situation is RBNZ. (We assume that offshore funders will also be unwilling to fund New Zealand banks in a liquidity crisis.)

69. However, we agree that having repo-eligible mortgage backed securities traded in the market would provide some price transparency.

**Question A5**

**A5: Do you agree that it is feasible to create more resilient mortgage bond markets?**

70. We believe it could be feasible to create a more resilient mortgage bond market and it would be beneficial to continue to develop New Zealand securitisation markets.
71. However, we do not agree that the reason one has not emerged to date is because investors would not be willing to invest in traditional RMBS. Some New Zealand investors already invest in traditional RMBS. The Australian RMBS market developed without having standard documentation, a standardised structure, etc. That market demonstrates good demand for bank originated RMBS and we would expect similar, limited, appetite from New Zealand investors.

72. There has been little incentive for banks to issue residential mortgage securities historically for reasons including:
   a. More expensive than unsecured funding and relatively short tenor due to high prepayment rates of the underlying mortgages.
   b. Some concerns about investor capacity to absorb both RMBS and unsecured funding and desire to maintain maximum level of unsecured funding onshore.
   c. Cheaper funding and longer tenor available through covered bonds as well as other advantages such as investor diversification and increased market access.

73. Figure 5, after paragraph 29 of Part A, has a summary of the features of covered bonds, RMBS and covered mortgage bonds. In the New Zealand context, the table exaggerates the differences between covered bonds and RMBS. Covered bond programmes in New Zealand were established prior to any specific New Zealand legislation. While they are structured to replicate the essence of European ‘legislative’ covered bonds, they are similar to RMBS in that bonds are guaranteed by bankruptcy remote special purpose vehicles structured as charitable trusts under common law and general legislation.

74. New Zealand covered bond structures are very similar to covered bond programmes in other common law jurisdictions, but different to those in civil law jurisdictions (which are the ones described in Figure 5 of Part A), which tend to be highly prescriptive in nature. The New Zealand legislation is ‘light touch’ compared to that in civil law jurisdictions.

75. Covered bonds have been issued in significant volumes by New Zealand banks. Their key attractions to issuers are:
   a. The tenor that can be achieved;
   b. The access to a very large pool of funds in Europe separate from normal unsecured funds; and
   c. The market tends to operate better in difficult conditions than unsecured markets.

76. While their issuance costs are slightly below unsecured levels, their main attractions are diversification and market resilience.

**Question A6** What would be the critical features required to achieve this?
77. We believe the critical features required to achieve this are:
   
a. RMO would need to provide a competitive source of funding (vis a vis unsecured funding and covered bonds) or other advantages to originators (e.g. longer tenor, capital relief, investor diversification) in order to incentivise originators to issue, without adversely impacting on originators’ depositors and unsecured creditors and existing funding markets.
   
b. Flexibility for originators to tailor transactions to meet their own and investor objectives (while remaining within guidelines agreed with the RBNZ). We are not in favour of adopting a rigid, untested structure on the basis of its assumed liquidity in all circumstances.
   
c. AAA public ratings for securities from at least one rating agency.
   
d. Good performance history for the relevant assets supported by asset performance data and portfolio reporting. We note that this is already the case.
   
e. Investor appetite, which is likely to vary depending on market conditions.

Question A7  What would be the challenges creating such products in the New Zealand market?

78. Higher pricing on RMBS versus covered bonds and unsecured debt.
   
   In this regard, we have doubts around cost savings of RMO because they are effectively RMBS, albeit with pre-determined tranching and portfolio parameters and minimum capital requirements.

79. High prepayment rates make it difficult to achieve longer tenor on RMBS making them unattractive versus covered bonds or unsecured debt.
   
   ANZ does not generally issue any term debt with maturities less than three years.

80. It is highly unlikely that capital relief would be achievable with the RMO because of the constraints around the seller retaining the full amount of the subordinated note and the trapping of excess spread in the structure.

81. Concerns around impact on unsecured ratings through increased use of secured debt.

82. Lack of liquidity in normal market conditions
   
   This is a major barrier to investment for some investors. However, we have doubts that repo-eligibility will necessarily be the solution. Some investors are precluded from leveraging assets. If the RBNZ were prepared to make a market in RMO and purchase the RMO outright, this would likely provide the level of liquidity sought by investors to bring new investors into the market.
83. *We don’t think the RMO is inherently different from iRMBS*

If investors cannot invest in iRMBS because of extension risk, for example, it is unlikely that they will be able to invest in RMO.

84. *As noted in our responses to Part B, there are some features in the RMO structure which may not sit well with rating agency criteria.*

85. *Imposing a rigid, prescriptive structure leaves no room for development of the market*

This leaves the RBNZ exposed to the risk of liquidity drying up in circumstances where investor appetite and market conditions change in unforeseen ways.

86. *System changes to meet enhanced reporting requirements, aligning banks’ key points of difference, the costs of which will be passed on to customers.*

**Question A8**

Do you agree that RMOs broadly meet the criteria set out by the Reserve Bank for ‘ideal collateral’ (a more detailed description of RMO being provided in Part B)?

| 87. No. |
| 88. We think it is appropriate that the RBNZ requires a consistent standard of iRMBS across originators, but this would be better achieved through amending existing iRMBS based on agreed set of high level guidelines. |
| 89. The spirit of the RMO appears to go far beyond the intention of the “simple, transparent and comparable” guidelines and looks to be an attempt to create a risk free asset. |
| 90. In this regard we note that the iRMBS are already AAA rated, the highest potential rating. Minimum capital requirements in excess of the rating agency requirement at AAA, coupled with trapping of excess spread (including cross collateralisation across series), conservative eligibility criteria and portfolio parameters, cash collateralised liquidity reserves, investment of principal collections in RMT eligible assets, etc. all suggest the originator would be providing capital far in excess of the amount required to cover the risk on the portfolio at an AAA level. |
| 91. Such an approach could well distort markets and be inconsistent with APS120: |
| i. How would the RBNZ treat other securities which are currently repo-eligible if the requirements for the RMO are the benchmark for repo-eligibility? Will the current repo-eligibility of other securities be withdrawn if the RMO standard is introduced? |
| ii. There is a New Zealand securitisation market, albeit with intermittent public issuance. This market has been developing in terms of the range of assets securitised and the sophistication of investors and appetite for risk. We think the RMO standard suggests that the appropriate way to develop the market is to start again and that investors should only invest in securitisations if they are risk free and they don’t need to analyse them. |
Such an approach sends the wrong message to investors and could well have a negative impact on the existing market and issuers.

iii. Creation of a risk free security would ultimately penalise unsecured creditors and depositors because it would involve originators providing support far in excess of the amount required to create low risk collateral for repo-eligible transactions, compared with other jurisdictions.

iv. We don’t believe the proposed standard is in the spirit of APS120. Creating a structure which achieves “no principal loss even in severe stress scenarios” is likely to run into implicit support issues. Some of the features of the RMO may be acceptable prior to repo, if the transaction is a self-securitisation. However, the RBNZ is also considering compelling originators to issue concurrently into the market. In this case we believe we would need to meet APS120 requirements for a funding-only securitisation from the outset.

92. Para 46 of Part A: see our response on Scalability (paras 34-38). We believe that to maximise the potential portfolio of loans, existing iRMBS programmes should be maintained as open pools under an agreed framework, but that they should become closed pools whenever repo-ed with the RBNZ. Only loan eligibility criteria should be mandatory.

93. Liquidity in the New Zealand fixed income market is generally supplied by banks. Given their repo-eligibility, RMO liquidity would likely be similar to Kauri bonds.

94. However, the extent to which they are traded in normal times would not be a good guide to how they would trade during a liquidity stress situation.

95. Given that banks hold iRMBS to meet regulatory liquidity ratios, if they are compelled to issue before a liquidity crisis by selling RMO in normal market conditions, they would then have to invest the proceeds in other repo-eligible assets which they would need to buy from the market.

96. This will either encourage reciprocal placement of RMO among originators (to minimise negative carry), or result in a transfer of value from banks to other market participants (through market participants switching out of low yielding New Zealand Government bonds (“NZGB”), for example, into RMO and originators switching out of RMO into NZGB). Neither scenario actually creates new system liquidity.

97. The RBNZ’s assumptions regarding superior liquidity for the RMOs appear to be based on them being risk free and therefore equivalent to NZGB. We don’t believe a risk free security is the correct approach for the reasons set out above. Otherwise, we would expect the liquidity and pricing of the RMO to be similar to traditional RMBS, which historically have been more expensive and less liquid than covered bonds.

98. Some of the RBNZ’s liquidity and market assumptions appear erroneous. In
particular:

a. Placement of securities is not typically done by way of auctions, but by a book build approach, in New Zealand.

b. Demand for fast pay versus amortising longer term RMBS tends to vary depending on market conditions.

c. Some investor mandates preclude funds being leveraged (e.g. via repo transactions).

99. See our response under para 30 above concerning the RBA valuation system.

<table>
<thead>
<tr>
<th>Question A10</th>
<th>A10: Are there alternative instruments the Reserve Bank could consider as eligible collateral in order to reduce reliance on iRMBS?</th>
</tr>
</thead>
</table>

100. The international track record for covered bonds by New Zealand issuers is already well established. New Zealand dollar denominated covered bond issues have been well received by domestic investors. The lack of New Zealand dollar issues reflects issuer funding market preferences, given New Zealand’s reliance on offshore funding, rather than a perceived lack of New Zealand investor demand.

101. We do not believe an increase in covered bond issuance (in the context of reduced iRMBS issuance) would prejudice depositors and unsecured creditors as the levels of over-collateralisation required under covered bonds are generally consistent with what is sought as a minimum for the RMO without the requirement for additional trapping of excess spread.

102. Covered bonds are also more homogenous in that they all share the same security rather than the discrete pool approach proposed under the RMO standard. Covered bond pricing is also more transparent.

<table>
<thead>
<tr>
<th>Question A11</th>
<th>A11: Do you think RMO would be in principle compliant with APS120? Are the requirements therein reasonable in the New Zealand regulatory and financial market context?</th>
</tr>
</thead>
</table>

103. There appears to be a desire under the RMO to push recourse to originators beyond what would be acceptable under APS120. See our response under paras 89 and 91.

104. The requirements do not look reasonable in comparison with existing repo-eligibility criteria here and in Australia.

<table>
<thead>
<tr>
<th>Question A12</th>
<th>A12: Are there any other areas that should potentially be addressed in the context of developing the Reserve Bank’s ability to lend to eligible parties in the</th>
</tr>
</thead>
</table>
105. Non-bank New Zealand investors currently hold approximately $33bn (35%) of outstanding repo-eligible securities not held by domestic banks or offshore holders.

106. If the RBNZ wished, it could offer its repo facilities to these holders now. However, given that the fund management industry holds various asset classes based on investor demand, assets in one fund cannot generally be used to provide liquidity in another, and leverage in funds may also not be permitted, the usefulness of this facility may be limited for many market participants.

107. ANZ has concerns about:

a. An untested model being applied without addressing potential impacts on banks’ costs and current funding arrangements. The RMO would lead to increased funding costs for New Zealand borrowers and substantial additional offshore funding requirements to finance alternative repo-eligible assets; and

b. Impact on the existing New Zealand securitisation market (see para 98).

**Question A13**

**A13: Are there other essential requirements to developing secured funding markets?**

108. Adequate time to develop the depth of the market. There seems to be an assumption that large volumes of RMO instruments can be placed immediately. This is unlikely to be the case.

109. Investor mandates would need to allow the purchase of these instruments if they are being presented as a new “risk free” asset class which is neither a RMBS nor a covered bond. We would see a substantial investor education programme being required.
### Part B

#### Question B1

**B1: Do you agree that safety, risk versus return, and cost are the most important considerations when appraising a mortgage bond standard? Are there other aspects of mortgage bonds that should also be considered?**

<table>
<thead>
<tr>
<th>110. We agree that safety, risk versus return and cost are important considerations when appraising a mortgage bond standard. However, the intention of the RMO appears to be to create a risk free instrument. This goes far beyond the approach adopted under the “simple-transparent-comparable” guidelines and the RBA repo-eligibility criteria. Refer to Appendix 4 which compares the RMO Standard with the RBA and ECB eligibility criteria and the simple, transparent and standardised regulations.</th>
</tr>
</thead>
<tbody>
<tr>
<td>111. We believe it is possible to create an acceptable low risk instrument, where the RBNZ and investors can have a high degree of confidence about performance in a range of adverse environments, without having to create a risk free instrument.</td>
</tr>
<tr>
<td>112. The creation of a risk free instrument in itself is likely to distort markets as it implies a level of support beyond what is normally permitted under securitisation standards. It will potentially result in the cherry-picking of assets to the detriment of unsecured creditors and depositors and/or impact on mortgage markets through restriction of new originations.</td>
</tr>
<tr>
<td>113. In our view, there is also some confusion as to what is actually proposed under the standard. The consultation paper refers to a tradable domestic “covered mortgage bond”. However, covered bonds typically allow for adjustment of the loan portfolio to top up security to the agreed minimum level (which is contrary to the principle of discrete pools).</td>
</tr>
<tr>
<td>114. What appears to be proposed under the standard is in fact an RMBS with additional restrictions regarding the tranching, portfolio parameters, eligibility criteria, etc. We cannot see any benefit in introducing a completely new standard when the existing iRMBS could be adjusted to meet stricter requirements, if necessary.</td>
</tr>
<tr>
<td>115. We also find it hard to understand some of the assumptions behind Figure 1 of Part B.</td>
</tr>
<tr>
<td>a. How do you conclude that covered bonds for which there has already been substantial issuance and which have a proven track record during the GFC, have medium liquidity whereas an untested RMO structure will have high liquidity? The RMO is simply a more conservative form of RMBS. RMBS have not historically been more liquid than covered bonds.</td>
</tr>
<tr>
<td>b. We question your assumption concerning economies of scale.</td>
</tr>
<tr>
<td>116. We note that a role for rating agencies has not been included in the</td>
</tr>
</tbody>
</table>
consultation paper. We don’t believe it would be possible for many investors to invest in these securities without a rating. Consequently, they should also be part of the consultation process in order to confirm that it would be possible to achieve an AAA rating on the basis of the proposed structure.

117. Originators need more flexibility to manage their own operational processes. Prescriptive requirements around elements such as the frequency of top ups seem excessive and do nothing to enhance safety.

Question B2

**B2: Do you agree with the considerations underlying the merits of a high quality liquidity substitute? Are there other considerations that should be included?**

118. The RMOs are essentially RMBS.

119. We do not agree that investors are likely to treat them as requiring no analysis because of the additional conditions imposed by the RBNZ and the standardised tranching.

120. We think it is highly likely that investors will want to analyse portfolio composition, loan performance history including delinquencies, defaults, recoveries, prepayment speeds, origination and servicing processes and loan characteristics.

121. In addition, the requirement for discrete pools means that it would be highly unlikely that portfolio composition would be consistent with the initial parameters when the RBNZ may wish to have RMOs placed with investors. Our expectation is that investors will be interested in the composition of the portfolio at that time and the performance of that pool rather than relying on the initial parameters.

122. There does not appear to be any matching of the tenor of RMT eligible liquidity assets with the expected maturity of the fast pay 2 year tranche. If that is the case, then investors in this tranche will also be exposed to adverse market movements in the value of such securities, as there are no limitations proposed on their maturity to ensure that they are converted to cash prior to the soft bullet maturity date, and consequently would need to be liquidated to allow repayment. If this is the RBNZ’s intention, then losses on liquidation would also need to be taken into account by investors.

123. There appears to be an assumption that RMOs will be more liquid because they have a standardised structure. We doubt that this would be the case because investors will still be exposed to the same risks that apply to RMBS: prepayment speeds, extension risk, obligor defaults, declines in property values, etc.

124. Para 12.1: There appears to be an assumption that investors will be able to repo these securities. See our comments under para 82 above.

125. Para 13: The Draft Practice Guide (“DPG”) indicates that fast pay notes are to be between 20% and 45% of the aggregate initial invested amount. See our comments under para 60 above.
<table>
<thead>
<tr>
<th>Question B3</th>
<th>B3: Do you agree that the proposed RMO default capital structure could help to address current impediments to develop safer assets and a deeper market?</th>
</tr>
</thead>
<tbody>
<tr>
<td>126. No.</td>
<td>127. As noted above, RMBS are generally not issued by domestic banks due to cost and tenor considerations rather than investor concerns around safety.</td>
</tr>
<tr>
<td>128. Investor demand and structural preferences will vary depending on market conditions. We do not agree with prescribing a structure upfront assuming that it will always meet investor demand. We believe a principles-based approach, similar to Australia, is more prudent and versatile than the proposed RMO Standard. (Also see our comments under para 60 above).</td>
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</tr>
<tr>
<td>129. If a prescribed structure is mandatory:</td>
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</tr>
<tr>
<td>a. We query the purpose of the fast pay tranche. RMT eligible assets are confined to government and local government securities, deposits with the RBNZ and other RMO AA notes (which banks would not normally use as eligible assets in a securitisation transaction because they would be treated as a re-securitisation). Therefore, given this note effectively would ‘convert’ into government/local government securities (through reinvestment of principal collections into RMT eligible assets), all this note does is provide investors with a premium over direct investment in government securities.</td>
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</tr>
<tr>
<td>b. If a fast pay tranche is required at all, it would be safer, for the reasons set out under para 122, for principal to be passed through to investors rather than being trapped in the structure (i.e. an amortising structure). Fast pay notes would be floating rate and fixed rate loans swapped to floating rate to hedge any mismatch.</td>
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<tr>
<td>c. We think the AB Note will be more expensive if the pool can potentially be replenished and new AA Notes can be issued. Investors would need to price on the basis that subsequent top ups occurred, whereas in fact we believe this would be unlikely because of the requirements attaching to the AA tranche (20% to 45% of the issue amount). We believe, instead, that it would be preferable for external RMBS to be closed pools, in line with market practice and that iRMBS pools should remain open until repo-ed with the RBNZ.</td>
<td></td>
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<tr>
<td>Question B4</td>
<td>B4: Do market participants agree with the principles used to align the capital note structure and waterfall payment priorities? Are there any further considerations to include?</td>
</tr>
</tbody>
</table>
130. While some of the principles are consistent with RMBS, there are a number which are excessively conservative or contrary to rating agency methodology and normal RMBS market practice and are likely to cause problems if adopted. In particular:

a. The transaction provides for all excess spread being locked up in the Trust Reserve Account and, according to the structure diagram, shared between series. This is not New Zealand market practice and we would not want this to become an investor expectation for securitisations as it would inhibit development of the market.

We also see it causing regulatory problems under APS120. Banks are not permitted to provide additional support to securitisations and support under this structure would be open-ended with support from one series potentially being available to future unrelated series;

b. The structure provides for pro rata payment occurring when note outstandings reach 20% of the initial invested amount. Pro rata payment is typically triggered when fast pay tranches are fully repaid and credit support as a percentage of outstandings increases to a specified level (e.g. 15% to 20% of outstandings if initial support levels are 10%). Pro rata payments typically cease when the transaction becomes callable. They would also typically be subject to satisfaction of performance criteria.

Investors may not be comfortable with the proposed pro rata repayment mechanism which has pro rata being triggered at the tail end of the transaction potentially prolonging the tail out to 30 years. This may also preclude the notes from getting an AAA rating.

131. No post default waterfall is contemplated

**Question B5**

*B5: Do you agree the above portfolio limits strike a balance between being conservative enough while providing enough depth in eligible mortgage loans? Are there any technical hurdles to access data or select loans based on the criteria above the Reserve Bank should be aware of? Should any additional limits be incorporated to reduce risks?*

132. No.

134. To maximise availability and scalability, we would prefer that the Australian approach be adopted whereby the portfolio would remain open to further sales, with any securities repo-ed with the RBNZ needing to meet the relevant securitisation standards at that time. More severe haircuts could apply for securities where the underlying portfolio diverged from the benchmark portfolio.
135. ANZ’s iRMBS programme has been operating for around 10 years. In our view, the pool has continued to be representative of ANZ’s mortgage pool, once ineligible loans have been excluded. In our view, the proposed eligibility criteria would result in a ‘cherry-picked’ portfolio rather than a poor quality one, to the detriment of unsecured lenders and depositors.

Question B6  
**B6: Do you agree with the proposed underwriting standards? Are the guidelines flexible enough to support a safe and robust collateral standard.**

137. We generally agree with the underwriting standards.
138. The requirements in relation to performance history should be articulated, as it is not clear over what prior period of time performance history is required.

Question B7  
**B7: Do you agree that discrete pools are the most transparent way to guarantee transparency or enforce control over a mortgage pool when necessary? Would you consider replenishing pools as an alternative conditional on the necessary amount of risk governance and control could be undertaken? Would you regard the cost involved in establishing replenishment criteria and monitoring processes as feasible in that context?**

139. Para 45 of Part B: it is not market practice that replenishing structures require higher levels of independence, governance and control. If investors can rely on eligibility criteria for initial sale without independent review, why do they need it for replenishment?

140. In ANZ’s view, an open pool under which originators had flexibility to maintain portfolios in accordance with high level guidelines prior to securities being repo-ed with RBNZ, whereupon they will become discrete pools, would be better.

141. Para 49 of Part B: we wouldn’t consider this regulatory capital relief as the underlying assets are depleting. Capital is simply being maintained at the normal level required for the portfolio. Capital relief refers to the situation where the originator is able to hold a lower amount of capital than the full amount required for the assets. We don’t believe true capital relief would be possible under the RMO standard based on the requirement that the originator hold the full capital note. We recommend that the RBNZ considers establishing a regime similar to Australia which allows for both funding only and capital relief securitisations.

142. Para 53.1 – see our response under para 94 above.

143. We think it would be possible to propose a simpler structure (see our proposal under paras 10-12 above) without going down the route of having numerous
discrete portfolios which will be expensive and administratively cumbersome and will severely limit potential issuance.

144. We also don’t think discrete pools will be consistent with the RBNZ’s objectives of availability, scalability and homogeneity. Potentially the RBNZ could find itself holding numerous small transactions at different stages of amortisation. Investors would have to analyse each deal given that their recourse is limited to the loans in the relevant series and may not wish to invest in non-market size parcels.

145. Our suggestion would be that we follow the Australian model whereby the originator can add and remove loans into one self-securitisation until such time as the securities are repo-ed with the RBNZ. This would allow the RBNZ to apply criteria regarding portfolio composition when it was actually exposed to the iRMBS and the underlying portfolio would be more reflective of the originator’s wider portfolio with less risk of cherry-picking.

**Question B8**

**B8: Do you agree with the incentive scheme outlined above? Should there be any compulsory risk retention in senior notes? Is there a need to support regulatory capital relief beyond the capital relief mechanism described above?**

146. We agree that risk retention by the originator is considered an important incentive to maintain the quality of underwriting and servicing. However, the risk retention proposed by the RBNZ again goes far beyond what is required in other jurisdictions and in this case is compounded further with the trapping of excess spread in the structure. Retention requirements should not go beyond those of comparable jurisdictions such as Australia.

147. Issues arose in offshore markets which had an “originate to distribute” model. This is not the case in New Zealand. Banks are the largest mortgage originators and hold and fund the mortgages on balance sheet.

148. We don’t think risk retention of senior notes is required for RMO or iRMBS. Originator risk retention in both types of structures is already substantial.

**Question B9**

**B9: Do you agree that repo-eligibility would support RMO to become in principle accepted financial instruments in domestic markets? What would markets be able to accommodate as an initial market placement?**

149. In general, yes. But it would equally assist standard RMBS

150. As mentioned above under para 98, we do not think repo-eligibility benefits all investors. There are some investors who will not have (nor will be able to enter into) repo agreements with the RBNZ or other parties.
<table>
<thead>
<tr>
<th>152. Private placements still involve negotiation of pricing with investors. We think private placements should be eligible.</th>
</tr>
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<tbody>
<tr>
<td><strong>Question B10</strong></td>
</tr>
<tr>
<td><strong>B10: Do you agree the information disclosure as outlined would be sufficiently comprehensive? Are there other disclosure requirements that should be included? Would an external data repository as outlined above provide an adequate solution for NZ markets?</strong></td>
</tr>
<tr>
<td>153. The information disclosure requirements are comprehensive. However, we have some issues with the proposed disclosure regime as follows:</td>
</tr>
<tr>
<td><strong>a.</strong> We don’t think a data repository is required. We propose that each bank posit initial and ongoing disclosure information on their own website.</td>
</tr>
<tr>
<td><strong>b.</strong> Para 55.3 of Part B: we do not think this is practical. If the RBNZ wishes to define the information that must be released, issuers will strive to meet those requirements. However, any further information on the pool would need to be released simultaneously to all investors via the same mechanism, otherwise one investor would be in a privileged position. But if responses to ad hoc queries are loaded onto websites then you are potentially not going to have the same information for all originators anyway because it will be dependent on what questions investors ask each originator. We wouldn’t expect that all information potentially requested by investors would be suitable to load onto a website, e.g. if an investor asked for CVs of relevant personnel in the originations or servicing area.</td>
</tr>
<tr>
<td><strong>c.</strong> Para 55.4 of Part B: it is not clear what sort of information the RBNZ has in mind. How far back would such information need to be provided?</td>
</tr>
<tr>
<td><strong>d.</strong> Para 56.2 of Part B: some of the information required as part of the asset criteria would not necessarily be captured in the loan management system.</td>
</tr>
<tr>
<td><strong>e.</strong> Para 58 of Part B: originators should have the flexibility to have publicly available materials uploaded to their websites.</td>
</tr>
<tr>
<td><strong>Question B11</strong></td>
</tr>
<tr>
<td><strong>B11: Do you agree the above Servicer requirements strike a balance in protecting creditors’ interest and allowing for cost efficiency in the required operations?</strong></td>
</tr>
<tr>
<td>154. Investors would find it very strange if the beneficiaries of a trust exercised</td>
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</tbody>
</table>
control over the trust. This may also make a rating impossible. Typically the consent of the majority of senior noteholders would be required, rather than the beneficiaries.

155. We wonder whether these requirements would be consistent with all legislation

<table>
<thead>
<tr>
<th>Question B12</th>
<th>B12: Do you agree these operations could be established at a reasonable cost?</th>
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<tbody>
<tr>
<td></td>
<td>156. We estimate the proposed costs would be substantial.</td>
</tr>
<tr>
<td></td>
<td>157. Principal collections in respect of the iRMBS currently can be held by the seller/servicer, subject to them having the minimum required short term rating. Under the RMO, collections will need to be invested in RMT eligible assets.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Question B13</th>
<th>B13: Do you consider a more active role for the Reserve Bank as beneficial? Would there be other functions the Reserve Bank would need to consider to support the creation of lower risk assets and a future market development effectively?</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>158. See our response to para 58 above. We don’t see a structuring role being consistent with the RBNZ’s mandate.</td>
</tr>
<tr>
<td></td>
<td>159. Para 75 of Part B: we would not propose that the RMO be listed. These securities will not be placed with retail investors.</td>
</tr>
<tr>
<td></td>
<td>160. Para 75.2 of Part B: our preference would be for investors to make initial and ongoing disclosure information available via their websites, similar to existing arrangements with covered bonds.</td>
</tr>
<tr>
<td></td>
<td>161. Para 75.5 of Part B: we don’t think external investors would be comfortable with a situation where RMOs could cease to be repo-eligible following replenishment. Repo-eligibility would need to be a condition precedent to replenishment occurring.</td>
</tr>
</tbody>
</table>

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<thead>
<tr>
<th>Question B14</th>
<th>B14: Do you agree with the Reserve Bank’s view that the potential benefits from RMO could be high? Are there any other benefits not mentioned in here?</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>162. No.</td>
</tr>
<tr>
<td></td>
<td>163. From an issuer’s perspective, iRMBS are simpler and cheaper than RMO. Amending iRMBS to align with high level guidelines is our preference. We don’t see any intrinsic benefits in RMO.</td>
</tr>
</tbody>
</table>
164. We also query some of your assumptions:

a. **Figure 10 of Part B**: As set out above, we believe some of the variations you have proposed for the RMT would hamper its ability to be bankruptcy remote. Our expectation is that RMT will be equivalent to special purpose vehicles under the iRMBS. Consequently it would be preferable to amend existing iRMBS structures than to implement a whole new model.

b. The RMO structure wouldn’t result in disaggregation of assets from an originator’s balance sheet. Originators will be exposed to all the risk (credit, operational, compliance, legal, etc.) on the relevant portfolios. Consequently, we don’t see the RMO standard reducing systemic risks.

165. Comments on Figure 10:

a. **Issuer**: In a New Zealand context, the issuer, or guarantor in the case of covered bonds, would need to be a bankruptcy remote SPV in all cases.

b. **Legal Framework**: New Zealand covered bonds are largely documented under general legislation and common law. New Zealand RMBS legal structures are not ‘bespoke’. They are documented under general legislation and common law and are, in essence, similar.

c. **Asset Quality**: Under current RBNZ iRMBS requirements, loans with an LVR over 80% can only be included if the ‘first loss’ is insured. Most covered bond programmes give zero collateral value to security above 80% LVR.

d. **Nature of Pool**: RMBS can have replenishing pools for a period.

e. **Loss Buffer**: In practice, these equate to the same thing.

f. **Liquidity Value**: We doubt whether RMO will be more liquid than RMBS in a New Zealand context.

<table>
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<tr>
<th>Question</th>
<th>B15: Do you agree with the cost components and scenarios above? Are there other costs or risks the Reserve Bank should be aware of in this context?</th>
</tr>
</thead>
<tbody>
<tr>
<td>B15</td>
<td><strong>No.</strong></td>
</tr>
</tbody>
</table>

166. No.

167. First, Figure 11 of Part B does not present the relevant counterfactual for moving from iRMBS to RMO. Secondly, the figures in the Figure 11 are speculative.
171. Paragraph 86.3 seems to suggest that banks would need to modify their mortgage products to conform to the RMO criteria. Is this correct?

Question B16  

**B16: Do you agree that a period of 12 months would be sufficient to restructure existing legal documentation for non-tradable**

172. No.

173. We do not consider that 12 months is feasible given the scale of the changes being proposed

Question B17  

**B17: Do you agree with the proposed incentive scheme? Are the incentives sufficient to encourage market development and to reduce distortions?**

174. The RMO standard is highly unattractive for issuers for the reasons outlined above. It:

   a. goes far beyond the requirements of any comparable jurisdiction and is not warranted based on the nature of the New Zealand mortgage market and the performance of New Zealand mortgages;
   
   b. is overly prescriptive and will substantially reduce potential issuance;
   
   c. will be expensive without offering any offsetting benefits vis a vis iRMBS;
   
   d. will be complex to implement and maintain;
   
   e. is doubtful whether it will achieve greater liquidity than RMBS or allow investor diversification or market development;
   
   f. is potentially detrimental to depositors and unsecured creditors and may impact adversely on consumers through further tightening of lending standards; and
   
   g. does not appear to be compliant with APS120.

175. We recommend RBNZ looks to introduce greater simplicity, transparency and comparability through adoption of a set of high level guidelines suitable for the
176. Comments on Figure 12

a. The table confuses ‘distribution’ with ‘liquidity’. At present ‘liquidity’, i.e. the ability to buy or sell securities, is provided to the market largely by banks. Placing more (or less) of a series externally will not of itself determine ‘liquidity’.

b. **High Liquidity**: The low haircut on high liquidity notes is of little value to the issuer if more than 80% of them are held elsewhere, unless banks were permitted to hold high volumes of each other’s paper (as someone else will benefit from the low haircut).

c. **Limited Liquidity**: Banks are unlikely to list RMO or RMBS

d. **Low Liquidity**: With respect to the Liquidity Premium, we do not understand what the paper means by ‘potential cost advantage’ or over whom iRMBS issuers would have an advantage?
Comparison of RMO Requirements with Australian and ECB Repo-Eligibility Criteria and Simple, Transparent and Standardised Rules

| Class | Item | RMO Standards | Equivalent Australian Standard | Reserve Bank of Australia Repo Eligibility Criteria | Equivalent RMO Standard | Simple Transparency and Standardised
|------|------|----------------|-------------------------------|-----------------------------------------------|------------------------|----------------------------------|
|      |      | Minimum size  | Yes or No?                     | No requirement for fast pay tranche            |                         | No requirement for fast pay tranche
| AA   | Size | <min 20 and max 45]/100 |                               |                                               |                         |                                  |
|      | Rating | No | Yes-AAA rating required | No | Guidelines EU 2018/1/1 | No |
|      | Legal Maturity | <= 30y | No | Not applicable |                         | No |
|      | Expected Life | >= 2.0y | No | Not applicable |                         | No |
|      | Call Rights | Not callable | No | Not applicable |                         | No |
|      | Income Payable | Fixed rate, Quarterly | No | No |                         | No |
|      | Principal Payable | Soft Bullet | No | No |                         | No |
| AB   | Size | <min 45 and max 70]/100 | No | Not applicable |                         | No |
|      | Rating | Yes-AAA rating required | No | Guidelines EU 2018/1/1 | No |
|      | Legal Maturity | <= 30y | No | Guidelines EU 2018/1/1 | No |
|      | Expected Life | > 10 years | No | Guidelines EU 2018/1/1 | No |

1. The title of the underlying exposures shall be acquired by the SSPE by means of a true sale or assignment or transfer with the same legal effect in a manner that is enforceable against the seller and any other third party. The transfer of the title to the SSPE shall not be subject to severe clawback provisions in the event of the seller’s insolvency.

2. For the purpose of paragraph 1, any of the following shall constitute severe clawback provisions:

(a) provisions which allow the liquidator of the seller to invalidate the sale of the underlying exposures solely on the basis that it was concluded in a manner that does not comply with the rules of evidence in the jurisdiction of the seller.

(b) provisions where the SSPE can only prevent the invalidation referred to in point (a) if it can prove that it was aware of the insolvency of the seller at the time of sale.

3. For the purpose of paragraph 1, clawback provisions in national insolvency laws that allow the liquidator or a court to invalidate the sale of underlying exposures in cases of fraudulent transfers, unfair prejudice to creditors or transfers intended to improperly favour particular creditors over others shall not constitute severe clawback provisions.

4. Where the seller is not the original lender, the true sale or assignment or transfer with the same legal effect of the underlying exposures to that seller, whether that true sale or assignment or transfer with the same legal effect is direct or through one or more intermediate steps, shall meet the requirements set out in paragraphs 1 to 3.

5. Where the transfer of the underlying exposures is performed by means of an assignment and perfected at a later stage than the closing of the transaction, the triggers to effect such perfection shall include at least the following events:

(a) securitisation of the seller credit quality standing;

(b) insolvency of the seller; and

(c) unremedied breaches of contractual obligations by the seller, including the seller’s default.

6. The seller shall provide representations and warranties that, to the best of its knowledge, the underlying exposures included in the securitisation are not encumbered or otherwise in a condition that can be foreseen to adversely affect the enforceability of the true sale or assignment transfer with the same legal effect.

7. The underlying exposures transferred from, or assigned by, the seller to the SSPE shall meet predetermined, clear and documented eligibility criteria enforced by the SSPE that, in turn, shall meet the eligibility criteria applied to the initial underlying exposures.

8. The securitisation shall be backed by a pool of underlying exposures that are homogenous in terms of asset type, taking into account the specific characteristics relating to the cash flows of the asset type including their contractual, credit-risk and prepayment characteristics. A pool of underlying exposures shall comprise only one asset type. The underlying exposures shall contain obligations that are contractually binding and enforceable, with full recourse to debtors and, where applicable, guarantors.
### Comparison of RMO Requirements with Australian and ECB Repo Eligibility Criteria and Simple, Transparent and Standardised Rules

#### Appendix 4

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**Note:** The underwriting exposures shall have defined periodic payment streams, the instalments of which may differ in their amounts, relating to rental, principal, or interest payments, or to any other right to receive income from assets supporting such payments. The underlying exposures may also generate proceeds from the sale of any financial or leased assets.

- The underlying exposures shall not include transferable securities, as defined in point (4)(a) of Article 4(1) of Directive 2014/59/EU, other than corporate bonds that are not listed on a trading venue.

- The underwriting standards pursuant to which the underlying exposures are originated and any material changes from prior underwriting standards shall be fully disclosed to potential investors without undue delay.

- In the case of securitisations where the underlying exposures are residential loans, the pool of loans shall not include any loan that was marketed and underwritten on the premise that the loan applicant or, where applicable, intermediaries were made aware that the information provided might not be verified by the lender.

- The assessment of the borrower’s creditworthiness shall meet the requirements set out in Article 8 of Directive 2008/48/EC and paragraphs 1 to 4, point (a) of paragraph 5, and paragraph 6 of Article 18 of Directive 2014/77/EU where, or applicable, equivalent requirements in third countries.

- The originator or original lender shall have expertise in originating exposures of a similar nature to those securitised.

- The underwriting exposures shall be transferred to the SSPE after selection without undue delay and shall not include, at the time of selection, exposures in default within the meaning of Article 178(1) of Regulation (EU) No 575/2013 or exposures to a credit-impaired debtor or guarantor, who, to the best of the originator or original lender’s knowledge:

- (a) has been declared insolvent or has had a court grant its creditors a final non-appealable right of enforcement or material damages as a result of a missed payment within three years prior to the date of origination or has undergone a debt-restructuring process with regard to his non-performing exposures within three years prior to the date of transfer or assignment of the underlying exposures to the SSPE; and

- (b) was, at the time of origination, where applicable, on a public credit registry of persons with adverse credit history or, where there is no such public credit registry, another credit registry that is available to the originator or original lender; or

- (c) has a credit assessment or a credit score indicating that the risk of contractually agreed payments not being made is significantly higher than for comparable exposures held by the originator which are not securitised.

---

### 2. Applications and Reporting Requirements

- 2.1 Ongoing Reporting (Asset-Backed Securities) **System**

  - The Reserve Bank and the public must be provided with reliable data on the composition of the assets underlying all eligible asset-backed securities on an ongoing basis.

  - The reporting requirements reflect the need to receive comprehensive and standardised information on these securities and to promote broader transparency in the securitisation market. Compliance with these ongoing reporting requirements is necessary for asset-backed securities to be considered eligible securities by the Reserve Bank.

  - Any securities that fail to comply with the mandatory reporting requirements will be considered ineligible for repo operations. A list of these securities can be found on the list of Outstanding Repo Eligibility Applications and Ineligible Securities.

- Prior to 1 March 2018, reporting through the Securitisation System must be lodged within 7 calendar days of the monthly anniversary of the distribution date for the asset-backed securities. From 1 March 2018, reporting through the Securitisation System must be lodged by the monthly anniversary of the distribution date for the asset-backed securities. Securities that lose eligibility due to late reporting will remain ineligible until all outstanding submissions related to that security have been made and a subsequent submission has been lodged successfully by the due date. Information Providers can contact the Securitisation System before the deadline to request an extension if they anticipate having trouble meeting the reporting deadlines.

  - These requests will be assessed on a case-by-case basis and will typically only be granted under exceptional circumstances.

### 3. Income Payable

- **Income Payable**

  - **Callable or pool <=10%**

    - **No**

  - **Callable if pool <10%**

    - **No**

  - **Callable if pool >=10%**

    - **No**

- **Step-Up Coupon**

  - **Min of 0.25%**

    - **No**

- **Income Payable**

  - **3% KB3M + Fixed margin**

    - **No**

- **Minimum capital support**

  - **No**

### 4. II. LEVEL OF REQUIRED DETAIL

- **1. After the date of application of loan-level data reporting requirements for the specific class of cash-flow generating assets backing the ABSs as specified on the European Central Bank’s (ECB) website, detailed loan-by-loan information must be provided for ABSs to become or remain eligible.**

- **2. Within a period of three months, the ABSs must achieve a compulsory minimum compliance level, assessed by reference to the availability of information, which provides a complete picture of the loan-level data reporting template.**

- **3. To capture non-available fields, a set of six “no data” (ND) options are included in the loan-level data templates and must be filled in whenever data cannot be submitted in accordance with the loan-level data template.**

- **4. A set of ND options, which only applies to the loan-level data template for commercial mortgage-backed securities (CMBSs)**

---

### 5. Rating

- **Rating**

  - **Standard**

    - **No**

- **Legal Maturity**

  - **No**

### 6. Call Rights

- **Callable if pool <10%**

  - **No**

### 7. Income Payable

- **Floating rate**

  - **No**

### 8. Principal Payable

- **Pass through**

  - **No**

### 9. Minimum capital support

- **No**

### 10. Size

- **No**
### Comparison of RMO Requirements with Australian and ECB Repo-Eligibility Criteria and Simple, Transparent and Standardised Rules

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<tbody>
<tr>
<td></td>
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<td></td>
<td>Yes or No?</td>
<td>For more information on the Reserve Bank’s reporting requirements, see the RBA Securitisations Industry Forum.</td>
<td>Yes or No?</td>
<td>Yes or No?</td>
<td>Yes or No?</td>
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<td>Principal Payable pass through No</td>
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<td>Principal draw Yes No</td>
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<td>Liquidity reserve balance Yes No</td>
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<td>Capital reserve Yes No</td>
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<td>Trust reserve Yes No</td>
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<td>Eligible liquidity assets Yes No</td>
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<td>Loan eligibility criteria Yes No</td>
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<td>Moderate balance principal Yes No</td>
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<td>Replenishment restrictions Yes No</td>
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<td>Transfer of mortgage loan pool and rights Yes Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

**Mandatory structuring**

- Model legal documentation
- Waterfalls
- Principal draw
- Liquidity reserve
- Capital reserve
- Trust reserve
- Eligible liquidity assets
- Loan eligibility criteria
- Moderate balance principal
- Replenishment restrictions
- Transfer of mortgage loan pool and rights

### Underwriting standards

- Some criteria in relation to assets.

- Some criteria in relation to assets.

- Some criteria in relation to assets.

- Some criteria in relation to assets.

### Requirements relating to standardisation

1. The originator, sponsor or original lender shall satisfy the risk-retention requirement in accordance with Article 6.
2. The interest-rate and currency risks arising from the securitisation shall be appropriately mitigated and any measures taken to that effect shall be disclosed. Except for the purpose of hedging interest-rate or currency risk, the SPE shall not enter into derivative contracts and shall ensure that the pool of underlying exposures does not include derivatives. Those derivatives shall be underwritten and documented according to common standards in international finance.
3. Any referenced interest payments under the securitisation assets and liabilities shall be based on generally used market interest rates, or generally used sectoral rates reflective of the cost of funds, and shall not reference complex formulae or derivatives.
4. Where an enforcement or an acceleration notice has been delivered:
   - (a) no amount of cash shall be trapped in the SPE beyond what is necessary to ensure the operational functioning of the SPE or the orderly repayment of investors in accordance with the contractual terms of the securitisation, unless exceptional circumstances require that an amount be trapped to be used, in the best interests of investors, for expenses in order to avoid the deterioration in the credit quality of the underlying exposures;
   - (b) principal receipts from the underlying exposures shall be passed to investors via sequential amortisation of the securitisation positions, as determined by the seniority of the securitisation position;
   - (c) repayment of the securitisation positions shall not be reversed with regard to their seniority; and
   - (d) no provisions shall require automatic liquidation of the underlying exposures at market value.
### Comparison of RMO Requirements with Australian and ECB Repo-Eligibility Criteria and Simple, Transparent and Standardised Rules

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<th>Equivalent STS Standard?</th>
<th>Yes or No?</th>
<th>Simple Transparent and Standardised</th>
</tr>
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<tbody>
<tr>
<td>Transferability</td>
<td>First ranking and performing residential mortgages in New Zealand</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>6. Transactions which feature non-sequential priority of payments shall include triggers relating to the performance of the underlying exposures resulting in the priority of payments reverting to sequential payments in order of seniority. Such performance-related triggers shall include at least the deterioration in the credit quality of the underlying exposures below a predetermined threshold.</td>
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<tr>
<td>Consistency</td>
<td>Originated by a single seller based on consistent and robust lending standards</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>(a) a deterioration in the credit quality of the underlying exposures to or below a predetermined threshold;</td>
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<tr>
<td>Performance</td>
<td>Full tranche information and performance history provided</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>(b) the occurrence of an insolvency-related event with regard to the originator or the servicer;</td>
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</tr>
<tr>
<td>Documentation</td>
<td>Documented and sustainable employment or self-employment income</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>(c) of the underlying exposures held by the SSPE falls below a predetermined threshold (early amortisation event); and</td>
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<tr>
<td>Jurisdiction</td>
<td>Issued in accordance with NZ law and conditions of registration</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>(d) a failure to generate sufficient new underlying exposures that meet the predetermined credit quality (trigger for termination of the revolving period).</td>
<td></td>
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<tr>
<td>Transferability</td>
<td>Transferability of financial claims and security titles under New Zealand law</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>7. The transaction documentation shall clearly specify:</td>
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<td>Experience</td>
<td>Issuer/originator/warehouse with &gt;=5 years experience in mortgage lending</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>(a) the contractual obligations, duties and responsibilities of the servicer and the trustee, if any, and other ancillary service providers;</td>
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<tr>
<td>Currency</td>
<td>Receivable or payable denominated in NZD</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>(b) the processes and responsibilities necessary to ensure that a default by or an insolvency of the servicer does not result in a termination of servicing, such as a contractual provision which enables the replacement of the servicer in such cases; and</td>
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<tr>
<td>RMO Portfolio Limits Pool-Level</td>
<td>Nature of pool</td>
<td>discrete pool / no replenishment</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>8. The servicer shall have expertise in servicing exposures of a similar nature to those securitised and shall have well-documented and adequate policies, procedures and risk-management controls relating to the servicing of exposures.</td>
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<td></td>
<td>Loan to value ratio</td>
<td>max 60%</td>
<td>Actual value proxy</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>9. The transaction documentation shall set out in clear and consistent terms definitions, remedies and actions relating to delinquency and default of debtors, debt restructuring, debt forgiveness, forbearance, payment holidays, losses, charge offs, recoveries and other asset performance remedies. The transaction documentation shall clearly specify the priorities of payment, events which trigger changes in such priorities of payment as well as the obligation to report such events. Any change in the priorities of payments which will materially adversely affect the repayment of the securitisation position shall be reported to investors without undue delay.</td>
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<td>Interest cover ratio</td>
<td>&gt;= 2.0</td>
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*(Note: Equivalent STS Standard? Yes or No? and Simple Transparent and Standardised columns are placeholders for the actual standards and requirements.*
### Appendix 4

#### ECB Repo Eligibility Criteria

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</table>

#### Loan-Level (not weighted)

- **Nature of pool**
  - Verified NZ Resident / Borrower Unit: Yes
- **Loan to value ratio**
  - <=80%: Yes
- **Borrower concentration ratio**
  - <=NZD 1 M: No
- **Interest-only loan ratio**
  - <= 20%: No
- **Investment loan ratio**
  - <= 20%: No
- **Fixed rate loan ratio**
  - <= 45%: No
- **Remaining loan term**
  - <=360 calendar months: No
- **Loan seasoning**
  - <= 90 days: No

#### Operational standards

- **Issuer**
  - NZ registered trust, bankruptcy remote non-recourse legal entity: Yes
- **Servicer**
  - Employees with >=5 years experience: No
<table>
<thead>
<tr>
<th>Class</th>
<th>Item</th>
<th>RMO Standards</th>
<th>Equivalent Australian Standard Yes or No?</th>
<th>Reserve Bank of Australia Repo Eligibility Criteria Yes or No?</th>
<th>Equivalent ECB Standard Yes or No?</th>
<th>Equivalent STS Standard? Yes or No?</th>
<th>Simple Transparent and Standardised</th>
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<tr>
<td></td>
<td>Ability to replace Servicer for any reason at RMT’s discretion</td>
<td>No</td>
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<td>Separation of servicing of securitised loans</td>
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<td>Back-up Servicer</td>
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<td>Data requirements</td>
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<td>Central Data repository</td>
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