Chris Dalton | Chief Executive Officer

3 Spring Street, Sydney NSW 2000

T +61 (0)2 8243 3906
M +61 (0)403 584 600
E cdalton@securitisation.com.au

www.securitisation.com.au

9 March 2018

Mr Toby Andres
Adviser
Reserve Bank of New Zealand
2 The Terrace
Wellington 6011
New Zealand

By email: STC.Project@rbnz.govt.nz

Dear Toby

Consultation - New Zealand STC Collateral Standard – Review of mortgage bond collateral standards

We refer to the RBNZ's public consultation released on 17 November 2017 seeking responses to the proposed new collateral standards following the RBNZ's review of domestic and international mortgage bond collateral standards.

The Australian Securitisation Forum (ASF) was formed in 1989 to promote the development of securitisation in Australia. As the peak industry body representing both the Australian and New Zealand securitisation market, the ASF performs a pivotal role in the education of government, regulators, the public, investors and others who have an interest or potential interest in the benefits of securitisation and aspects of the Australian and New Zealand securitisation industry.

We outline below key comments we have in relation to the RBNZ's mortgage bond collateral standards review (as described in Parts A, B and C of the Consultation Papers) and provide in the attached tables more specific comments to the list of questions in both Parts A and B. Our comments reflect both the ASF's experience of more than 30 years of operation in Australia's securitisation market and incorporates significant feedback from our New Zealand membership.

1. General observations of the proposed mortgage bond standards

The ASF understands that the objective of the proposed mortgage bond standards is to promote a stock of domestic high quality, liquid, non-distortionary, scalable assets via the use of appropriately structured mortgage bonds. However, we believe certain proposals in the standard are likely to:

a) limit the potential benefit of the initiative because Residential Mortgage Obligation (RMO) bonds cannot be tailored to meet specific investor requirements. Investor preferences may include high yield as well as lower risk exposures;

b) continue to reduce the attractiveness for banks to issue RMO bonds because investors will be less familiar with this form of security.

The RMO structure should be flexible to encourage the participation of investors who seek high quality securities but want to have the opportunity to seek a high yield. Mortgage backed exposures are not entirely risk free. There are other high-quality liquid assets such as government bonds and bonds issued by the New Zealand Local Government Funding Agency that do already provide the type of liquidity the RBNZ is promoting through the RMO structure.

In addition to missing an opportunity to foster the growth of a market which might otherwise increase the diversity of sustainable funding sources for the New Zealand financial system, the overall limited investor participation and issuance relating to RMO bonds (in both primary issuance[1] and secondary market trading) is likely to reduce price transparency for this product. This may result in a higher reliance on the RBNZ, particularly in times of stress, with the potential unintended consequence of higher risk borne by the RBNZ and the New Zealand financial system. We recommend the RBNZ take a more principles-based approach to repo eligibility rather than the proposed prescriptive rules and the resultant constraining RMO structure.

There is talk of alternative liquidity providers in the Consultation Papers without any analysis on who might realistically invest in or trade these bonds. Key issues such as risk weights and capital impact have not been considered in the papers but are critical matters for liquidity and tradability. In fact, capital relief as an option is not available or at the very most remains uncertain which surely is in direct contrast to the objective of the RBNZ to improve market depth and participation in the sector.

The key to creating an active securitisation market is to attract and create incentives for both new domestic investors (such as Kiwisaver and super funds) and non-domestic investors to enter the New Zealand market. Those who already have deep RMBS investments in Australia, US, Europe and even in Asia are more likely to participate in a security they are familiar with

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[1] *Based on the experience in the Australian Securitisation market; in calendar years 2016-2017 major banks have issued 8 RMBS in aggregate totalling A$13.2bn, representing circa 28% of the total market issuance of 60 RMBS with an aggregate volume of A$46.5bn across the Australian RMBS market. Source: Bloomberg*

rather than a RMO in which they have never previously invested in nor which has demonstrated any performance history.

2. The RMO Structure

Certain aspects of a RMO might raise additional challenges or concerns for issuers resulting in an ultimately undeveloped market. For example:

a) The excessive 10% capital or credit enhancement requirement (to RMO) means that there will be more underlying assets that are required to become encumbered to secured funding vehicles. We would query whether this raises depositor protection issues? Similarly, we recall that this is one of the reasons why there is a 10% limit on covered bond issuance in NZ.

b) The requirement to "cherry pick" the highest quality assets in RMO pools is particularly restrictive and will inevitably result in the exclusion of certain product types from eligible pools and cause loans with higher risk characteristics to remain on balance sheet. The setting of RMO criteria and resultant selection of assets in this way is not a reasonable representation of the market and it is arguable whether it will encourage an active mortgage backed market in New Zealand. Australian regulations seek to avoid cherry picking of prime assets from a bank balance sheet to be sold into a securitisation. The general principle is that the pools should be representative of the lender's entire mortgage book.

c) One of the options noted in paragraph 52.3 of the Part B Consultation Paper is the adoption of a "Retained RMO" option which is expected to come with a 19% haircut. We query how the Retained RMO option can be any different to I-RMBS in real terms? Adopting APRA's approach to I-RMBS, by classifying these as funding only securitisations with date-based calls enabled, would work better.

d) There is a unique opportunity for non-bank lenders to access the RBNZ's repo facility and contribute to liquidity in this market. However, a non-bank lender's mortgage portfolio is unlikely to fit within the RBNZ's proposed restrictive eligibility criteria for RMOs. In addition, the high capital requirements of a RMO issue are not aligned with the non-bank business model. The non-bank sector benefits the financial system and functioning of the economy through competition and niche-lending. The originate-to-securitise model of the non-bank lender caters for a more diverse range of funding sources and therefore a broader allocation of risk amongst investors which can improve the liquidity of RMBS.

We would like to understand the RBNZ's appetite to discuss alternate proposals that would provide the RBNZ with the safety and security it requires for repo-eligible collateral, but also deliver greater competition and price transparency via a functioning RMBS market.

3. Mortgage bond /RMO operating framework

The RBNZ should consider the cost implications of a complex and unique framework and one which requires an originating seller (who is the most familiar with the performance of its assets) to be excluded from or have limited involvement in the establishment of the trust, servicing functions, management of the trust and providing market-based derivatives to the trust. The servicing functions can no doubt be dealt with through legal division of responsibilities under the documentation. Control rights in Australian and New Zealand securitisations are clearly documented in the trust documents and are balanced in favour of creditors.

4. Structural requirements

a) Our view is that there is no particular benefit from having highly prescriptive and unique structures as it limits the flexibility of issuers in terms of being able to meet investor demand for risk and other characteristics to suit their investment portfolio needs. Although it is beneficial for the underlying pools to comprise of homogenous assets (mortgages are generally viewed this way), the RBNZ's proposal prescribes the types of mortgage characteristics which will ultimately drive what assets will qualify for funding and this could possibly create difficulties for home owners obtaining mortgage finance.

b) The risk retention requirements (of 10%-35%) are well in excess of those required in other markets (i.e. 5% in EU/US, no risk retention requirements in Australia and the exemption of "qualified residential mortgages" in the US). It is not a preference of investors to require this level of risk retention and requirements over and above 5% effectively minimise the funding benefit to issuers.

c) The default structure is too conservative, restrictive and uneconomic to appeal to a wide variety of investors. Some investors will typically seek AAA rated low risk positions while others will seek mezzanine positions with an enhanced yield. The proposed RMO structure does not offer this.

d) Where there is no principal pass through but rather principal is collected or trapped until another class of notes is due for repayment, the RBNZ needs to be mindful of the negative carry this could potentially have on the transaction adding to the overall return to investors in the market. If the NZ banks with whom the principal is trapped and held on deposit were to be downgraded this could have an adverse ratings impact on the senior notes under standard ratings methodology.

The introduction of a RMO standard will create a bifurcated mortgage bond market with issuance to a limited investor base inhibiting the participation of non-bank lenders and new entrants and thereby restricting market competition.

We hope that the comments in this letter and in the annexed responses to the list of questions in Parts A and B of the Consultation Papers are of some help to you. We would be more than happy to discuss any aspect of our submission with you if you require further supporting information or clarity.

Yours sincerely,

Chris Dalton

RESERVE BANK OF NEW ZEALAND
TE PŪTEA MATUA

Review of mortgage bond collateral standards

PART A

The role of mortgage bonds in funding and liquidity operations

November 2017

List of Questions

Section		**Question**
1.2	A1	Do you agree these characteristics are appropriate to seek in eligible mortgage collateral? While we understand that the principal purpose of the mortgage bond is to promote liquidity for both RBNZ lending operations by accepting only high-quality collateral and to enable deeper markets in mortgage bonds to emerge, extreme care should be taken in seeking to restrict the type of collateral eligible for inclusion. This could lead to significant "cherry picking" of loans to meet the standard. In an effort to homogenise the asset type (which does not necessarily mean that quality is enhanced) the mortgage bond itself may not be representative of loan originations of a diversified asset class thereby creating a much larger category of ineligible loans that are not capable of being sold into the public markets. The key is to ensure that any standard proposed by the RBNZ is not so conservative that it does not represent the characteristics of underlying mortgage books and therefore does not lead to pricing distortions (i.e. to avoid a subset of "super prime loans").
	A2	Do you see scope for Reserve Bank counterparties to hold other satisfactory collateral? Other satisfactory collateral will be largely dictated by the funding programmes of issuers. SSA's are one high level (highly rated) asset class where issuance is much less constrained.
	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? Existing I-RMBS and covered bonds are unlikely to meet the RBNZ's 'ideal criteria' for eligible collateral as proposed. Covered bonds might if issuances were regular and there was an increase in the cap on issuance. While the ASF membership largely agree with the objectives of the RBNZ's review as a means of improving the stability of the NZ financial system and economy as a whole, particularly if this also promotes greater mortgage bond issuance and competition through the levelling of the playing field between banks and non-banks, it is not in favour of the introduction of a new security that may have the effect of undermining existing securities or inhibiting a wider securitisation market as an alternative funding source for New Zealand lenders.

		It is unlikely that in a time of stress that there will be sufficient liquidity in a product which is not globally traded and therefore limited to the demand of the New Zealand market.
	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 stress? As demonstrated during the GFC in Australia, the Australian Government provided various means of ensuring that an asset backed mortgage market would be sustainable even in periods of stress. One key initiative was the Government's directive to use the Australian Office of Financial Management (AOFM) to invest in up to A$20 billion of new issues of prime RMBS issued by smaller banks and non-banks. This temporary initiative ensured that all lenders could continue to operate their businesses to finance home loans through the capital markets at reasonable rates and ensure the continuity of competition in the Australian home loan market. The sustainability of the market with the temporary support of government initiatives is as much a contributor to liquidity as are central bank liquidity schemes. As demonstrated in Australia, the market was able to re-establish itself and no longer rely on temporary government investment support of the AOFM. The regulatory capital framework of the Australian banks obviously had positive features that made the mortgage market attractive. However ultimately the market has had to analyse the risk and return profile of bonds on offer. Investors have the ability and desire to price for this risk. By pricing in risk, the market is in many ways instrumental in shaping the criteria for loan eligibility. Australian non-banks rely predominantly on securitisation for funding and through the promotion of the securitisation market are able to provide genuine competition to the banks and therefore a competitive offering to the end borrower. The proposed NZ mortgage bonds are focussed on structural features that may limit the flexibility of issuers in terms of not being able to meet investor requirements for particular risk characteristics, tranche size, tenors etc. If the mortgage bonds are unable to be tailored to meet specific investor needs this will reduce the attractiveness of mortgage bond issuance which in turn is likely to reduce price transparency for this product. This may then result in a higher reliance on the RBNZ particularly in times of stress, with the potential (albeit unintended) consequence of a higher risk borne by the RBNZ and the NZ financial system.
1.3	A5	Do you agree that it is feasible to create more resilient mortgage bond markets?

		A resilient mortgage bond market will require an active group of issuers and investors to participate to provide a frequent pattern of issuance and multiple investors to invest and set prices for senior and junior tranches of the bonds. The current RBNZ proposal mandates a particular structure and an overly rigid and restrictive eligibility criteria which will inhibit the development and evolution of a more active and resilient mortgage bond market. We doubt whether the proposed RMO is likely to be more robust and resilient over time, particularly during periods of stress, than standard RMBS.
	A6	What would be the critical features required to achieve this? Broad based investor participation and a motivation for NZ lenders to issue. Standardisation requires regular issuance, repo eligibility, marketing/education to domestic and offshore investors (including asset consultants, investment advisers) and pricing that attracts investors.
	A7	Which are the challenges creating those in the New Zealand market? Complete mortgage bond standardisation may be difficult to achieve as different issuers (and their mortgage books) have differences in risk profiles. There will always be tension in pricing between issuers and investors at the outset of issuance and until a particular programme is established and investors become comfortable with the asset class and programme itself.
2.1	A8	Do you agree that RMO broadly meet the criteria set out by the Reserve Bank for 'ideal collateral' (a more detailed description of RMO being provided in Part B)? Certain aspects of the requirements in Part B seem to be contradictory and may create practical issues for lenders to provide collateral which satisfy the requirements of an RMO. For example, collateral criteria should not be overly prescriptive. There is more scope to adjust credit enhancement to address differences in collateral.
	A9	How much weight should the Reserve Bank put on RMO securities being traded relative to the other characteristics discussed? The 'ideal' characteristics for mortgage bond collateral as outlined in Figure 3 emphasises the RBNZ's desire to ensure that the quality of the mortgage collateral is such that there are no principal losses experienced even in severe stress scenarios. This could mean that less risky assets (non-representative) are pledged away to secured funding vehicles and riskier (e.g. high LVR loans) will remain with the bank.

		As a general point, the RMO standard appears to be a lot more focussed on structural features (such as tranching, waterfalls, specific credit enhancement requirements) in contrast to the EU's STS standards which do not appear to have specific requirements in this respect. There is little benefit from having highly prescriptive structures (as proposed in the Consultation Papers). This will limit the flexibility for issuers in being able to meet varied investor preferences. Many investors in RMBS will have the systems and knowledge to be able to analyse and understand a range of different structures and risks and it follows that it should be left to the industry (including the investor base) to determine which structures best work for their portfolio needs and risk appetite.
	A10	Are there alternative instruments the Reserve Bank could consider as eligible collateral in order to reduce reliance on I-RMBS? An alternative may be to make I-RMBS more standardised across the various lenders.
	A11	Do you think RMO would be in principle compliant with APS 120? Is the requirement therein reasonable in the New Zealand regulatory and financial market context? A key philosophy of APS 120 is that a securitisation undertaken by a bank should be backed by assets that are generally representative of similar assets held on the bank's balance sheet i.e. no cherry picking of good assets that benefit a particular class of creditors. The proposed eligibility criteria set out in Part B is contrary to the spirit of APS 120 as the lowest risk assets would be pledged for the benefit of capital market investors to the detriment of other creditors of the bank. Other than depositor protection concerns, it is doubtful that a RMO product can be structured guaranteeing 'no principal losses' in a drive to promote what would seem to look like a risk- free product. Therefore, this could be problematic under APS 120.
2.2	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 financial system? It is suggested that the RMO structure be reconsidered to provide more flexibility for additional tranching to be incorporated to meet demand from capital market investors and the collateral pools to be more representative of the characteristics of assets funded on balance sheet. The RBNZ

		can still meet its objectives and mitigate risk by only providing funding and liquidity to a bank by purchasing the senior securities in a RMO that are protected from credit loss by a very significant seller interest.
	A13	Are there other essential requirements to developing secured funding markets? It is vital that a new market does not inadvertently degrade existing markets, notably that of senior unsecured bank debt, covered bonds or RMBS. The ratings agencies' opinions are likely to play a key role but there is no mention of them in the consultation papers and the ratings agencies' own methodology papers do not provide a clear signal. Is the RMO no-pass through structure robust enough to pass ratings criteria? It should be noted that the majority of investors do require a formal rating before they will even consider participating in a transaction. Given that the RBNZ framework proposes the introduction of a more senior credit instrument (and to an extent cherry picking higher quality mortgage collateral) this could lead to a downgrade of senior unsecured debt which would be a very poor outcome and likely raise funding costs for the NZ banking system from the unsecured channels. The consultation papers mention that there is usually a legislative limit on the volume of covered bonds which appears to be portrayed as a negative. However, it does protect senior unsecured creditors and provides clarity for investors and ratings agencies. It would be our expectation that the volumes would be insufficient to crowd out the rating, but without any quantification of volumes or a limit on volumes, this is but an expectation. We think the system would benefit from having this clarified. It is also not desirable to alter the competitive landscape for lenders. While standardisation is likely to assist liquidity, reduce costs and facilitate volume creation in times of need, too much standardisation can alter the competitive landscape and inhibit the provision of tailored or innovative lending and funding solutions. For example, prescribing 45% of fixed rate mortgages may impact the underlying mortgage market. Although it is arguable that the volumes of RMOs issued are unlikely to provide distortions this should be clarified and not inhibit or penalise other funding options acceptable to or even sought by the market.

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Review of mortgage bond collateral standards

PART B

Residential Mortgage Obligations

List of Questions

Section		Question
3.1	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 to consider? We believe that the aspects set out in paragraphs 7.1 to 7.10 are relevant for a mortgage bond standard. An additional aspect to consider is achieving the support and participation by a variety of investors in the market for RMO which will be essential to achieve the object of the standard, to create a liquid and tradeable security. We query paragraph 7.10 as it is not clear how a bank can achieve capital relief by issuing an RMO. We also point out that a RMO bond standard may have an adverse impact on the ability of an issuer to issue a less standardised product because it would be economically more punitive and possibly restrict access for such an issuer to a more traditional RMBS market. This outcome may be viewed as anti-competitive. In addition, the RBNZ assumes that the highly structured RMO product will be attractive to investors. However, as the RBNZ will be paid out first and the AA note fast pay this will possibly render the structure inactive within 12 months.
3.2	B2	Do you agree with the considerations underlying the merits of a high-quality liquidity substitute? Are there other considerations that should be included? We do not think the Residential Mortgage Trust (RMT) structure is optimal and query why a pass-through or master trust structure, which would be more familiar to domestic, Australian and international credit investors, should not be used. We believe creating a unique New Zealand structure will be less well perceived by investors. The RBNZ could use the senior notes in a pass through or master trust structure to provide liquidity to the financial system as well as provide a high quality low risk exposure for the RBNZ. More work needs to be done to understand whether there is demand from investors for a shorter term (fast pay) note rather than the traditional RMBS where the issue has a longer term to maturity and the investor takes on pre-payment risk.
	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?

		We believe the default structure is overly conservative and restrictive and could be an impediment to the development of a deeper market. In particular, the requirement in paragraph 24 that principal received will be held in the trust until the AA- notes became due for repayment will make the structure inefficient from a cost perspective with the consequence that the yield that can be paid to investors will be less than if it were passed through on receipt. Given the extension risk in the Class AB notes, it will be difficult for investors to price unless there is an ability to replenish the collateral pool. However, this in itself creates complexity. A pass-through structure, which is familiar to and preferred by investors, may be more suitable to develop the New Zealand market. There are also investors in New Zealand and offshore that would be prepared to invest in lower rated non-repo eligible notes and their participation could help in the development of a deeper market and arguably a safer market as these investors will often undertake a more detailed analysis of the mortgage loans.
	B4	Do you agree with the principles used to align the capital note structure and waterfall payment priorities? Are there any further considerations to include? Paragraph 36 specifies a purely sequential allocation of cash flows. We believe a pro-rata allocation could be incorporated in the waterfall in circumstances where the protection of the AA and AB Note holders is not compromised (i.e. the minimum levels of subordination are preserved and defaults are below expected levels). Although pro-rata allocation is contemplated in section 35 of Part C, the prescribed allocation is materially more conservative than traditional RMBS. In addition, the current waterfalls do not allow excess spread to be returned to the lender, which is common in RMBS. Instead, such amounts are trapped in various reserves, including the trust reserve which is only released when the RMT is wound up. Lenders must have a mechanism to remove excess spread (for example, as deferred consideration or as an excess servicing fee).
	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?

		We believe that the combination of portfolio and loan level limits is overly conservative and will provide practical difficulties for lenders to adhere to the limits particularly in circumstances where prepayment speeds vary, or borrower preferences change. We suggest greater flexibility can be introduced. We see that the limits will require lenders to cherry pick loans to meet the standard to the potential detriment of other creditors and investors in senior unsecured securities issued by the lender. Should any additional limits be incorporated? Consider the following examples: A restriction of <=20% investment loans would require cherry picking. Given the level of home ownership, the need for investment properties is greater than 20% and therefore the demand for investment loans is also greater than contemplated by the RMO restriction. In the case of newly originated loans, unlike traditional bank sponsored RMBS they would need to be seasoned regardless of whether they meet LVR criteria on day one. Therefore, the RMO prescriptive limits could mean that new mortgages may not be able to meet the RMO portfolio criteria. The proposed portfolio limits for RMOs are indeed one of the most contentious aspects of the proposal. With respect to paragraph 40.6, the general experience with investment loans in Australia (refer to data evidence collected by the Reserve Bank of Australia) is that over all they have not shown default and losses rates significantly different to owner-occupied loans. In any case, investors typically determine, based on the level of exposure to investment loans, whether or not a premium will be applied.
	B6	Do you agree with the proposed underwriting standards? Are the guidelines flexible enough to support a safe and robust collateral standard? The proposed underwriting standards seem reasonable. We would submit that the RBNZ may wish to have some discretion to allow loans written by a lender with less than 5 years' experience to be acceptable in circumstances where a new lender may be acquired by an established lender.
	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 as feasible in that context? We believe that the standard should permit a lender to use a pass-through or master trust structure. Similarly, investors also tend to have a preference for pass-through structures as it allows them to assess the risk of the portfolio more easily. Although short periods of asset substitution have been acceptable at certain stages of the credit cycle, replenishing type structures are not standard for external RMBS and do generally attract a pricing premium and may even reduce participation.
	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? We believe that there are other alternatives to holding capital notes in a structure to avoid the risks of the "originate to distribute" business model. We note that the 10% value of the C-Note is arbitrary and seems exceedingly high compared to historical experience of New Zealand mortgages particularly in light of the proposed very conservative collateral requirements. The requirement to hold C-Notes will also mean a bank will not achieve capital relief under APS 120.
	B9	Do you agree that repo eligibility would support RMO to become more widely accepted financial instruments in domestic markets? What would markets be able to accommodate as an initial market placement? We believe that liquidity is a relative concept. Liquidity exists in normal or good conditions but disappears in difficult market conditions. This is true for all debt securities other than government bonds. We fully agree that repo eligibility will create and support liquidity in the market for RMOs. We understand from investor feedback that any initial offerings of RMO securities would need to be carefully managed and marketed well and that much of the demand would come from real money managers who invest in RMBS and banks.
	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 provide an adequate solution for NZ markets?

		The key to having meaningful information available to investors is working with issuers to agree standardised definitions and guidelines to be provided to investors and other stakeholders. We would suggest that investors have indicated a preference for a “one-stop-shop” for gathering mortgage pool information. The European Data Warehouse which has established templates for mortgage data from various countries is an example of such a centralised service.
	B11	Do you agree the above Servicer requirements strike a balance in protecting creditors’ interests and allowing for cost efficiency in the required operations? The circumstances under which the Servicer can be replaced needs more careful consideration as it is loosely defined in the Consultation Paper. We would query whether the “back up servicing” requirements outlined in the paper add benefit to creditors, given that these will add to the costs of the RMO structure.
	B12	Do you agree these operations could be established at reasonable cost? The ASF doesn’t have a view on this question.
3.3	B13	Do you consider a more active role of 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? We don’t foresee what further role the RBNZ could play.
	B14	Do you agree with the Reserve Bank’s view that the potential benefits from RMO could be high? Are there benefits not mentioned in here? The potential benefits are significant but the RMO framework needs to be recalibrated to avoid possible disruption in the underlying mortgage market.
4.1	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? The ASF doesn’t have a view on this question.
4.2	B16	Do you agree that a period of 12 months would be sufficient to restructure existing legal documentations for non-tradable I-RMBS?

		Experience in transitioning a market to new regulatory standards in Australia and elsewhere indicate that 12 months is a very ambitious timeframe and a longer period may allow a more orderly transition to occur and for investors to inform clients of the new asset class to seek approval to invest in RMO. The RBNZ should also be open to considering some form of “grandfathering” of existing repo securities such as I-RMBS.
4.3	B17	Do you agree with the proposed incentive scheme? Are the incentives sufficient to encourage market development and to reduce distortions? Although section 116.2 states that there will be no formal requirement for a credit rating from an external credit rating agency for RMO notes to be approved as “repo eligible”, there is little doubt that most market participants will in fact require a credit rating to invest in such securities. Without a credit rating, RMO notes would be extremely illiquid. Section 116.3 states that the “Reserve Bank may require issuance of capital notes in RMO to be greater than 10% of aggregate invested amounts”. How will this be determined? This creates uncertainty for the issuer and means the Standard is not fixed, but dynamic. This does raise an interesting issue of the risk that RMO AA and AB notes do not obtain the highest possible credit rating of AAA even with subordination of 10% due to the quality of the mortgage pool or the economic environment. In order to encourage investors in times of stress, subordination may need to be increased which may not be possible in that stressed environment.