Exposure Draft of the Deposit Takers Bill.

Full submission of the non-bank deposit takers

11 March 2022

This is a joint submission of the following non-bank deposit takers (**NBDT**s):

- Christian Savings Limited
- Credit Union Auckland Incorporated
- Finance Direct Limited
- Fisher & Paykel Credit Union Incorporated
- General Finance Limited
- Gold Band Finance Limited
- Heretaunga Building Society
- Mutual Credit Finance Limited
- Nelson Building Society
- Steelsands Credit Union Incorporated
- Unity Credit Union
- Wairarapa Building Society
- Xceda Finance Limited

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Introduction

This is the full submission made on behalf of the NBDTs expanding on our initial submission made 21 February 2021.

As noted in our initial submission, the NBDTs support the move to update New Zealand's prudential framework and acknowledge the enormity and complexity of this task for the Reserve Bank Act Review Team (**Review Team**). We also understand the very tight time pressures the Review Team is under (in particular to implement the new depositor compensation scheme and bank resolution framework) and the large number of decisions that have needed to be made as part of the review.

In recognition of the significance of the review to the NBDT sector and the potential benefits of a single prudential framework, the NBDTs have spent considerable time and money engaging with the Review Team on the development of a Deposit Takers Act (**DT Act**) since the consultation began in 2019. This has been done in the spirit of collaboration and genuine consultation – both assisting the Review Team to understand some of the particular challenges for NBDTs but also, in so doing, putting forward constructive suggestions on how a DT Act could be used to foster a more inclusive and diverse financial sector that ultimately would improve the wellbeing of all Kiwis.

Though we acknowledge this is not driven by the Review Team, we are concerned with the impact of the timeframe on meaningful consultation throughout this process. The Review team has engaged well with our sector and rapidly increased its understanding of our businesses and regulatory challenges. It was pleasing to hear at the Hui on 3 February that the Reserve Bank of New Zealand (**Reserve Bank**) understands the importance of the NBDTs in a more inclusive, varied and innovative financial sector. However, we do not see any evidence of this sentiment, or our previous submissions on how to foster this sentiment, in the Exposure Draft of the Deposit Takers Bill (**Bill**).

As was discussed at the Hui, the NBDTs' primary concern with the Bill is the level of regulatory uncertainty. There is simply not enough detail in the Bill for us to meaningfully consult on important matters of policy or plan for this significant regulatory transition. The NBDTs had anticipated that the Bill would give direction on how proportionality would be applied by the Reserve Bank, how the Financial Policy Remit would be taken into account and the extent to which the existing prudential requirements applying to them would be grandfathered across in transitional provisions. None of these matters have been addressed in the Bill. Unfortunately, we suspect this is a result of the Review Team being subjected to unrealistic deadlines. However, we note that the Legislation Guidelines created by the Legislation Design and Advisory Committee state that:

"*it is not appropriate to empower secondary legislation that involves significant policy to fill any gaps in an Act that may have occurred as a result of a rushed or unfinished policy development process; to avoid full debate and scrutiny of politically contentious matters in Parliament; or solely to speed up a Bill's passage through Parliament.*"[1]

We would like to thank the Review Team for allowing us a two week extension on making our full submission. It has been essential in order to enable us to better understand the potential impact of the Bill on our sector and businesses and we have used the time to consult more widely with our organisations (including with our boards) and to talk to some of our peers in Australia on what has and has not worked for them under a single deposit taker regime.

[1] LDAC Legislation Guidelines at 69.

We make this submission with the same collaborative and constructive approach we have taken to date, with a focus on providing practical suggestions. The focus of our submission will be on the key matters that we think must be included in the Bill (rather than standards) to support a diverse and vibrant financial sector where smaller deposit takers can thrive and which might mitigate some of the regulatory uncertainty and consequent anxiety we are experiencing. As kaitiaki we think it is important that you ensure the whole system flourish – both local institutions as well as the large foreign owned banks.

We hope that the consultation on these matters will not end with this submission, but that the Reserve Bank will, in the spirit of genuine consultation more akin to the principles of Te Ao Māori, continue to engage with a series of more focussed hui on areas of particular concern to our sector. We again suggest setting up a working group including members of the Review Team and NBDTs to work through the matters discussed in this submission on an ongoing basis. We envisage this as an informal arrangement where we make appropriate representatives available to work through issues with the Reserve Bank as they arise.

Transitional Uncertainty

The NBDTs anticipate that the shift to the new regime could require a lot of work for the NBDTs which would require significant time and cost that we will need to plan for.

The Bill gives almost no indication of what the regime will look like for us in practice. As noted in our initial submission, this level of uncertainty has serious implications for our businesses now, including our ability to make strategic plans and raise capital to grow, as well as our ability to prepare for compliance with the new regime. In our initial submission we set out at a high level the areas where the Bill creates significant uncertainty that potentially challenges the viability of our businesses. We expand on these matters and provide some potential solutions below.

At present we are each supervised by Trustees in accordance with our individual trust deeds. Each of these trust deeds have different terms, for example, relating to capital and liquidity ratios, related party exposures and resolution powers of the supervisor. The Bill gives us no clarity on which of these requirements will apply to us going forward and how we will be expected to transition to these requirements.

As noted in previous submissions, many of our trust deeds provide for a charge over our assets in favour of our depositors. We need to understand how this will be approached under the new regime which does not provide for depositor preference. Perhaps some of us may need to retain the charge over our assets so that our customers with deposits over the amount covered by depositor compensation still have priority in the event of a liquidation (this would likely require ongoing involvement of our trustees, but solely as security trustee and not in a supervisory capacity). That will have the double benefit of effectively giving the Deposit Compensation Scheme security through its rights of subrogation. In any event we believe the Bill needs to deal with either the process of putting many depositors with NBDTs in a worse position (something very much at odds with the no creditor worse off principle adopted elsewhere in the Bill) or include a mechanism for security to be retained.

Some matters that we have certainty on under the current regime have now been made subject to Reserve Bank discretion with no indications of how this discretion will be exercised. Under the current regime, NBDTs below a certain size are exempted from the requirement to have a credit rating (provided they maintain a minimum capital ratio). This exemption has not been carried over into the Bill but instead gives the Reserve Bank complete discretion to waive this requirement. In addition, the fine for contravening this requirement is $2.5 million – an amount that would cause many of us to be in breach of their capital requirements and therefore become unviable.

Similarly, NBDTs are not currently subject to macro-prudential policy. This has not caused any harm and to some extent, has provided a safety valve for the unfortunate cases of hardship that can be created by these policies. However, the Bill provides that the Reserve Bank may apply lending standards to any licenced deposit taker, including macro prudential standards. We believe applying the policy only to prudentially regulated entities is not a fair approach. The policy should apply to all lenders over a certain size threshold irrespective of whether they are prudentially regulated or not. Our Australian counterparts have reported that smaller deposit takers are disproportionately impacted by any macro prudential lending control because, with much smaller balance sheets, it can only take a couple of loans tipping over LVR restrictions to cause them to be in breach. This has caused significant barriers to growth for smaller deposit takers. It would be good to learn from this experience. While there seems to be some mechanisms to allow smaller deposit takers to be exempted from these requirements in the Bill, there is no guarantee that they would be used – another factor creating regulatory uncertainty.

We believe that the Reserve Bank should be required to impose macro prudential regulation in a way that is proportionate and fair across all mortgage lenders – not just prudentially regulated entities. As a matter of practice, given their market share there is a good case for limiting macro prudential policy to the domestic systemically important bank only – at least at first instance.

Finally, the power to impose lending standards seems to go beyond what is required for macro prudential regulation. This is of significant concern for NBDTs. They are already subject to lending standards effectively imposed by the Commerce Commission, potentially subject to lending policies imposed by the Financial Markets Authority (**FMA**) as part of conduct licencing and the CUBS have lending restrictions imposed on them by their incorporating legislation. The Reserve Banks role in imposing lending standards should be limited to macro prudential standards and indirectly through capital adequacy rules.

The move to a new regime is intended to modernise the regulatory framework for deposit takers. We emphasise that as far as we are aware there have been no issues identified with the NBDT regime (or the NBDTs themselves) for prudential purposes. As such, the level of regulation imposed on us by the new regime should be no more burdensome than what we are currently subject to and indeed carry some benefits because it should enable a deposit taker to access Reserve Bank liquidity and other support in a proportionate way. Our existing standards and regulation should be retained in substance unless there is a good reason to modify them (for example, to take a more proportionate approach).

All NBDTs should also be automatically transitioned to the new regime as licences deposit takers based on meeting existing standards without having to go through the time consuming and expensive process (for us and the Reserve Bank) of needing to reapply. There seems little value in a reapplication process for anyone given all NBDTs have been supervised already for a decade or more. We support the submission of the Trustee Corporations Association of New Zealand Inc, which urges the Reserve Bank to work with the trustees to ensure that transitional provisions operate as intended. The trustees have an in depth understanding of our businesses and our processes for complying with our duties and regulation. They have worked with us to get comfortable with these processes while ensuring they do not disproportionately impact our businesses. They will be a useful resource for the Reserve Bank in determining both the appropriateness of future standards and supervisory approaches and how best to transition to them. Good regulatory practice will be to work collaboratively with them, and us as the supervised entities, to enable the lowest impact transition possible (especially given no problems have been identified with the current regime – just improvement opportunities).

Finally, NBDTs have found the trustees to be quite responsive when decisions have been needed under our trust deeds. The NBDTs believe it will be important that responsiveness in decision making should not be adversely affected by the transition to the Reserve Bank as supervisor. We note that in the Bill where timeframes are provided the Reserve Bank has significantly longer to respond than deposit takers to provide the information in the first place. While it may be difficult to quantify time periods for decisions, we believe there should be a statutory obligation on the Reserve Bank to make decisions as soon as reasonably possible to mitigate the risks of delayed decisions on deposit takers.

Purpose

We are concerned that the purpose of the Bill has a singular focus on financial stability. There will be circumstances where improving financial stability will need to be weighed against other societal benefits, such as competition, innovation and financial inclusion.

We suggest that the Reserve Bank adopt an approach similar to that of Australia in its Banking Act 1959 where the prudential objectives include both financial stability and objectives which counterbalance this to promote a thriving financial sector:

(1) The main objects of this Act are:

(a) to protect the interests of depositors in ADIs in ways that are consistent with the continued development of a viable, competitive and innovative banking industry; and

(b) to promote financial system stability in Australia.

A new clause 3(1) could read:

The main purposes of this Act are:

a) to promote the financial well-being of New Zealanders and a sustainable and productive economy through the development of a competitive, innovative and inclusive deposit taking industry; and

b) to promote the stability of the financial system.

The additional purposes in clause 3(2) should then be expanded to reflect the dual main purposes of the Bill. Such additional purposes could include, for example, promoting financial inclusion, competition, the co-operative economy, innovation and increasing domestic capability.

The Prudential Regulation Authority (**PRA**) in the United Kingdom have a secondary purpose of competition embedded in their governing legislation. This (in concert with certain accountability measures, such as the requirement to develop and publish strategy) has driven initiatives such as the New Bank Start-up Unit, consultation on changes to capital requirements for credit unions to remove barriers to growth and, currently, its "Strong and Simple" consultation on developing a simplified prudential framework for non-systemically important banks.[2] All of these things should not just be enabled by the Deposit Takers Act but required.

We are also concerned that clause 3(2) gives undue weight to the soundness of each individual deposit taker. We do not think it serves the objective of financial stability to elevate the safety and soundness of each individual deposit taker (other than DSIBs) above other considerations such as, for example, promoting competition, which has instead been something noted in the principles in clause 4 as something that is 'desirable'.

There is a serious risk that this will be interpreted as a zero-fail regime when we do not believe that is the intention and which lends itself to over regulation that can only be sustained by the largest financial institutions. This will inevitably eliminate options for customers and increase concentration risk in overseas owned banks and in particular, the Australian-owned banks. Adding additional sub-purposes as noted above will support a more comprehensive view of financial stability. We also suggest the sub-purpose in clause 3(2)(a) be amended to read:

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[2] United Kingdom Prudential Regulation Authority *DP1/21 – A strong and simple prudential framework for non-systemic banks and building societies* 29 April 2021.

"*to promote the safety and soundness of each deposit taker having regard to their systemic importance and consequence of failure on the whole financial system*".

Finally, we suggest that an additional principle be included in clause 4, being the need to give effect to the Financial Policy Remit. Where such wide discretion is given to a regulator such that the regulation could intrude into politically contentious matters especially in circumstances where economic goals could conflict with social, legal or political outcomes it is vital that it is clear the Minister can and should set the priorities.

Proportionality

Our primary concern with the move to a single deposit taker regime is the potential regulatory burden. The concept of proportionality of regulation is mentioned only once in the entire Bill in clause 4 (Principles to be taken into account under the Act) and provides simply that the Reserve Bank must take into account the desirability of taking a proportionate approach to regulation when exercising its functions, powers and duties. If this is the extent of the statutory requirement it is easy to see particularly over time how it could become a low priority for the Reserve Bank.

The experience of our Australian counterparts is that matters like how proportionality will be exercised need to be clearly set out in legislation to incentivise regulators to understand the impact of regulation on smaller entities. Smaller entities may seem inconsequential from an immediate financial stability perspective and without a clear mandate to support them, the focus of regulators simply goes elsewhere. In Australia, the government had to intervene to force regulators to consider the impact of regulatory change on "market competition".

In the United Kingdom, the PRA are undertaking a significant consultation on the simplification of prudential frameworks for small and non-systemically important banks.[3] There is a strong movement internationally towards developing approaches that do not apply full Basel standards (developed for complex and internationally active banks) to all deposit takers due to the unintended consequences of over-regulation.

It is important for the Reserve Bank to understand that there are NBDTs with as few as one full time employee and who have not had a loan default in their entire history – who have limited capacity to deal with the existing regulatory regime let alone any significant additional change and where there is simply no need to add to their regulatory burden.

Furthermore, some of the penalties set out in the Bill would make some of the NBDTs immediately unviable. We noted the penalty relating to credit ratings in the section on transitional uncertainty. Similarly, clause 152 provides that breach of a standard or condition could result in a pecuniary penalty of up to $5 million or 0.1% of consolidated assets *if higher* (thus this would not apply to the NBDTs). A penalty of $5 million is simply unsustainable for most of the NBDTs and there is no guidance on how these penalties should be applied proportionately. For many NBDTs, $5 million is between 5% and 10% of assets, significantly greater than the 0.1% that is the maximum payable by any large bank. This is simply unfair.

In the Hui, the Reserve Bank noted that clause 4 was inserted to give greater detail and context on how the Reserve Bank will implement efficiency principles in practice, on the basis that "efficiency" can be a nebulous concept and mean different things to different people. Similarly, we feel that this type of detail and clarity is needed to articulate the operation of the concept of proportionality. We also note that the FMA has begun work on articulating how it will apply conduct regulation proportionately, pointing to features of the regulated entity such as:

- nature, size and complexity;
- services and products offered;
- how services and products are offered; and
- types of consumer.

[3] Ibid.

We request that the FMA and the Reserve Bank (along with the rest of Council of Financial Regulators) work together to articulate the details of how regulatory proportionality will operate in practice and that this detail be translated into the Bill.

We have provided more specific suggestions on proportionality in later sections where we think it is most critical for the success of smaller, non-systemically important deposit takers, but ideally directives and details on how proportionality will apply in practice would be included throughout the Bill:

- in part 2 relating to criteria for applying for a licence, imposing conditions of licence (including the application of standards) and the process for assessing whether a director or senior manager is fit and proper;
- in part 3 relating to whether the Reserve Bank will exempt a deposit taker from the requirement to get a credit rating, when creating classes of deposit takers for the purposes of issuing standards, when issuing standards;
- in part 4 relating to the Reserve Bank's approach to supervision of deposit takers;
- in part 6 relating to the levies imposed on deposit takers (discussed further below); and
- in part 7 relating to the use of resolution tools (including the need for resolution plans and assuming additional resolution tools are included that would work for small deposit takers which is discussed further below).

The application of proportionality will be critical for the success of the NBDTs and it certainly does not seem consistent with trying to create a competitive, inclusive and diverse financial sector to effectively force these entities to merge and in doing so lose their unique value. The experience of the Australian sector and the impact of the PRA's secondary competition objective clearly show that a statutory mandate and appropriate accountability mechanisms are required to ensure proportionality of regulation – notwithstanding the best of intentions at the outset.

Standards and Conditions

The Bill should set out principles that the Reserve Bank must have regard to when making decisions relating to the establishment of classes, conditions of licence and standards, including that standards should be proportionate to the risk the entity or class poses to New Zealand's financial stability.

As an example, we refer you to section 393 of the Financial Markets Conduct Act 2013 (**FMCA**) which sets out the principles that must guide the FMA in exercising its powers relating to licencing. These include that the exercise of licencing powers should promote the purposes of the FMCA and should not unnecessarily restrict the licencing of persons. The FMCA also sets out procedural requirements for exercising these powers including requiring that certain matters be taken into account.[4] In the submission of 23 October 2020 made by the credit unions and building societies (**CUBS**), the CUBS set out matters that should be taken into account when considering whether less complex regulatory approaches are warranted, being:

(a) whether the institution has cross-border operations;

(b) the complexity of the institution's assets and liabilities;

(c) the asset size of the institution;

(d) the extent of the institution's leverage;

(e) the institution's connectedness with the financial system;

(f) the degree to which the institution reports to multiple prudential supervisors;

(g) the extent and nature of the institution's off-balance sheet exposures; and

(h) the mix of business activities of the institution, such as whether it engages in community banking, commercial banking and/or investment banking.5

The submission dated 23 October 2020 of the Reserve Bank regulated finance companies recommended that classes of deposit takers be provided in the primary legislation itself based on market share (including a suggested statutory class of "Restricted Deposit Taker" similar to Australia's RADI regime). Providing for certain classes of deposit takers in the legislation itself as a starting point, based on factors such as market share of deposits (percentage of banking assets), corporate form (eg profit-maximising company, mutual or charity), a class for DSIBs, a class for deposit takers with cross-border operations and even classes based on sources of funding (exclusively retail or a mix of retail and wholesale) would give the NBDTs more comfort that standards will be fit for purpose and the NBDTs will not automatically be subject to standards based on those applied to larger banks by default without proper analysis of whether they really were appropriate or not. The Bill could require the Reserve Bank to tailor standards to those classes unless there were good reasons not to do so. The Bill could then enable the Reserve Bank to create additional classes (either standalone or within the statutory classes) based on characteristics that may change over time such as dollar value of deposits or assets, customer niches, complexity of business and financial products offered.

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[4] FMCA, s 397.

[5] World Council of Credit Unions Submission to Basel Committee on Banking Supervision *Proportionality in Regulation at the Global Level* (3 April 2019).

We also think there is some value in considering the approach in Australia, which is a graduated approach to regulation in terms of life stage and size that we understand to be operating well in many respects.

Figure 1. Summary of the key differences in applying APRA's prudential framework to each category of ADI

Restricted ADI (where applicable)	New ADI	Established ADI
• *Initial capital* - ongoing capital requirement plus 3 months' operational expenses • *Ongoing capital* - \$3m plus \$1m resolution reserve • *CCB* - none • *Contingency plan* – primary focus on return of deposits • *Deposit limit* - \$2m aggregate cap on deposits	• *Initial capital* - higher of \$15m or 9 months' operational expenses • *Ongoing capital* - higher of \$10m, rolling 6 months' operational expenses or percentage of RWAs • *CCB* - \$2.5m or 25% of 6 months' rolling operational expenses or 2.5% of RWAs • *Contingency plan* – Evolving with business: likely to be return of deposits in early stages • *Deposit limit* – may apply some controls on deposit growth	• *Capital* - calculated on a risk weighted basis as per APRA standards • *CCB* – 2.5% of RWAs • *Contingency plan* – must demonstrate how ADI can recover or exit • *Deposit limit* – no limit or controls on deposit growth

There is a restricted ADI category that allows certain ADIs testing their business model to operate under a simplified regime for a limited time. Such a simplified approach might also be appropriate for the smaller NBDTs who are not necessarily focused on scaling rapidly, but whose proven and non-complex business models justify simplified regulation and supervision. This framework might perhaps still rely on trustee supervision and would probably not have the benefit of the depositor compensation scheme.

Outside of the restricted ADI regime in Australia, there is a minimum size to become an ADI and that is calculated by reference to regulatory capital. Currently the minimum capital required to be an authorised deposit taker in Australia is A\$10 million, with new entrants being required to have A\$15 million in regulatory capital to account for the possibility of losses while getting their business off the ground. This seems to us like a reasonable level of commitment from new players to justify access to benefits such as the deposit compensation scheme, while not subjecting smaller and new deposit takers to the same requirements as long-established and systemically important banks.

If this approach were adopted, we would expect that all current NBDTs would be grandfathered into the fully licenced category, even where they do not meet the minimum capital requirements, on the basis that they have been prudentially regulated and supervised in most cases for a decade or more. However, to the extent that an NBDT did not meet the minimum capital requirements, they should be given the option to opt out of either:

- being fully licenced and be subject to a simplified regime, or
- just the depositor compensation scheme on the basis they make it very clear their deposits are not subject to the scheme.

Another option could be that a class of small deposit taker is included in the legislation itself, for example with assets of less than 0.5% of total financial system assets, with the ability of the Reserve Bank to create additional categories or sub-categories. In the short term, this would create a category to which the transitional provisions for NBDTs would apply. This would also be similar to the approach taken in the

United Kingdom (following the European Union), where smaller and less complex firms are subject to simplified and less burdensome requirements.[6] Within this group there are standards specifically tailored, for example to credit unions, this includes the credit union rulebook and supervisory statements providing guidance on how to comply. Though, as noted above, the PRA are currently in the process of consulting on a graduated approach to prudential supervision whereby the full Basel standards will only be applied to large and internationally active banks.[7] We see no reason why a similar approach could not be applied in New Zealand.

[6] Non-CRR firms.
[7] Above, n2.

Supervision

In previous submissions we expressed a preference to be supervised directly by the Reserve Bank, rather than by Trustees. This preference was based primarily on the fact that trustee supervision was a considerable expense for the NBDTs. However, we would like to note that most of our experience working with the trustees has been positive. Our current supervisors have made efforts to understand our business and regularly update their understanding.

The NBDTs experience of direct supervision to date has been more limited (largely in the context of COVID-19), but we immediately noticed a more process driven and broad-brushed approach, requiring significant amounts of documentation, which for the NBDTs was very resource intensive (and we believe surplus to requirements).

While we have also had some very high-quality engagement with Reserve Bank officials on certain important issues, we are concerned that a fit for purpose approach to supervision on a day-to-day basis is not likely to be prioritised by the Reserve Bank and it could revert to a one-size fits all approach involving a modified version of bank supervision, rather than one specifically targeted at the risks and characteristics of NBDT's based on what has worked with trustees. This would be very burdensome for us, adding what we believe could be significant direct and indirect cost for us, especially in a transition period. In some cases this could have a material impact on profitability. This has certainly been an issue reported to us by our counterparts in Australia. While on-site supervision has been recognised as an important part of APRA's toolkit, it has proven to be very burdensome for smaller deposit takers, largely due to standardisation of internal policies, risk appetite statements and other documentation, with very arduous processes if the ADI wishes to take an alternative approach.

Principles for exercising these powers should clearly set out that the intensity of supervision should be proportionate to the risk the deposit taker poses to the financial stability of New Zealand and that the Reserve Bank must weigh up the materiality of supervisory measures for the purposes of financial stability against the impact on the deposit taker. We suggest that guidelines should also be included around the intensity of supervision, particularly information gathering powers under clause 95 and onsite inspection powers under clause 110.

While the Reserve Bank increases its understanding of our businesses and risk management infrastructure, we strongly suggest that the Reserve Bank utilise the industry knowledge and experience of the trustees.

Benefits of being prudentially regulated

If the Reserve Bank wishes to promote a diverse and competitive deposit taking sector that serves all New Zealanders, it must ensure that prudential regulation supports new and existing business. In our previous submissions, we have noted that the regulatory burden of the NBDT regime currently far outweighs the benefits and that we would like to see this remedied – as part of promoting a dynamic and inclusive financial system. Unfortunately, the Bill does not appear to have done much to address this.

One benefit that we advocated for has been accepted in the Bill – that there should be no cost of supervision. All NBDTs have been exempted from the requirement to have a supervisor under the FMCA (we note that the Trustee Supervision Act 2011 will still reference "licensed deposit takers" which we assume is in error). However, the following benefits that we asked for have not been provided with no explanation as to why and in some cases, contrary to decisions indicated in the April 2021 cabinet paper entitled Reserve Bank Act Review – Deposit Takers Bill (**Cabinet Paper**):

Use of the word "Bank"

"Bank" remains a restricted word that can only be used by financial service providers with the Reserve Bank's authorisation. The Bank has complete discretion over whether to authorise use of the word and the Bill suggests that it may adopt a policy that it will only authorise deposit takers that comply with higher financial strength requirements.

At present the use of the word depends on the deposit taker's prudential regime, which is not per se an indication of its financial strength. Nor, is it an indicator of what is a bank and what is not – that is a function of what an entity does not its financial strength. If the Reserve Bank is determining who can use the word based on higher "financial strength" requirements, there is an even greater risk than under the current regime of presenting the mutual and specialist deposit takers as unsophisticated and/or unsafe. This approach seems out of step with global developments in the banking space (for example, the emergence of neo-banks/challenger banks) and certainly the approach that has been taken in Australia and which we had understood the Review Team had initially supported. We suggest that the Bill follow the Australian approach, which allows all authorised deposit takers to call themselves banks unless APRA determines otherwise.[8] From enquires we have made in Australia there have been no issues with regulated ADIs using the term bank and it is widely used amongst ADIs (with the exception of some credit unions). The use of the term bank is of particular importance to the RBNZ regulated finance companies. With the stigma still associated with the term "finance company" arising out of failures of unsupervised finance companies in the GFC, being able to rebrand incorporating the term bank could enable the RBNZ Regulated Finance Companies to make a more meaningful contribution to the competitiveness and ultimately the stability of New Zealand's financial systems.

There should be guidance around the use of discretion by the Reserve Bank to restrict a licenced deposit taker from using a restricted word, for example, the Reserve Bank should only be able to limit a deposit taker from using a restricted word in its name to the extent that this is necessary to further the purposes of the Bill.

Proportionate regulation

As mentioned above, smaller deposit takers have no certainty that their regulatory burden (both in terms of standards and supervision) will be proportionate to the risk they pose to financial stability. While this is

[8] Banking Act 1959 (Aus), 66AA.

enabled by the Bill, it is not guaranteed, and the Bill equally enables a much heavier handed approach to regulation of smaller deposit takers.

Depositor compensation

While all prudentially regulated deposit takers will have access to deposit insurance, we are concerned that the costs of this will disproportionately fall on smaller deposit takers, despite the fact that we pose a relatively minor risk to financial stability (this is discussed further in the next section).

Liquidity and counter cyclical support

We have submitted on a number of occasions on the need for liquidity support in times of stress on the financial system. In the submission of 12 May 2020 made by the credit unions and building societies and supported by the deposit taking finance companies, we explained to you the realities of expecting the larger banks to provide that liquidity support to smaller deposit takers (it simply does not happen) and the effect of a low or negative OCR on our non-interest margin (**NIM**). We have suggested that the Reserve Bank take steps to:

- provide liquidity support itself (through liquidity facilities with appropriate modifications to acceptable collateral and by holding deposits).
- reclassify our deposits with banks so we can earn retail rates (a very low risk for bank liquidity balanced against a much higher prudential benefit for NBDTs given the high level of deposits they have). If the Reserve Bank is not prepared to modify its risk appetite to offer to take deposits from NBDTs directly (removing the largely uninsured risk NBDTs must take and given the size of the sector a very low risk for the Reserve Bank) then we believe, if it is to actively encourage a diverse economy, it needs to ensure that NBDTs can maximise returns by not being penalised by regulatory settings.

Under a single regime, all deposit takers should have access to the same support in a crisis. We believe that if this is not enshrined in legislation, then while the Reserve Bank can provide this support in theory, collateral requirements may rule this sector out in practice (which was the case in both New Zealand and Australia during the COVID-19 crisis). The Reserve Bank should be required to extend equal liquidity support to all deposit takers in a crisis. To the extent we cannot have this included in the Bill itself, this is an issue we would like to work closely with the Reserve Bank on as part of a working group. While RBNZ is currently consulting on liquidity, including with NBDT, we still believe the requirement to provide liquidity to all regulated entities on a proportionate basis (including as to security) should be enshrined in the Bill.

It is not uncommon in other sectors for large dominant entities to be required to provide services at a fair and even discounted rate to other participants. To the extent the Reserve Bank is not prepared to provide liquidity support or deposit facilities for NBDTs, then we believe the Bill should empower them to compel DSIBs to provide (perhaps capped at a certain level) that support on terms approved by the Reserve Bank and/or put in place regulatory settings that encourage and support DSIBs to do so (eg classification of deposits and risk weighting for standby facilities for NBDTs – something we believe other regulators may do).

Yet another option could be to allow the NBDTs to access the depositor compensation scheme at no cost in a financial crisis. This would allow us to improve liquidity by seeking funds from the retail market with no increased cost.

It is important the NBDTs have confidence they have access to support in a crisis – something that was a concern with the initial Covid lockdown – when banks received significant support from the Reserve Bank but then would not necessarily pass the benefit of that support to NBDTs (eg by allowing them to break term

deposits and by giving signals that standby liquidity facilities may not be available because pre conditions may not have been met). Certainly there is no evidence the cheap funding provided by the Funding for Lending scheme was ever passed on to NBDTs.

This support will also assist all deposit takers who require a credit rating to obtain the appropriate credit rating from rating agencies. One of the consistent reasons given to NBDTs for not obtaining an upgrade from the rating agency is that “there is no financial support from the central bank for NBDTs”.

ESAS Accounts

The Bill should also specifically provide that any licenced deposit taker has the right to an ESAS account with the Reserve Bank. This enables all deposit takers to have access to a central banks account for their own deposits and not have their funds at risk with other deposit takers in a crisis. This would also likely enable some of our suggesting above relating to liquidity and counter-cyclical support. As licensed deposit takers will already be regulated and supervised by the Reserve Bank, we believe this right would not pose any meaningful risk.

Depositor compensation scheme

The NBDTs consider the depositor compensation scheme levies as potentially one of the greatest risks to their ongoing viability under the new regime. As such, this is a matter we would like to continue to work closely on with the Reserve Bank as part of a working group.

Part 6 of the Deposit Takers Bill provides for the new Depositor Compensation Scheme. Reading the Bill in isolation, it appears that the Reserve Bank has opted for an ex-ante fund with no government backstop (clause 227(a) suggests that the sector will meet any shortfalls). This completely shifts the risk of any short-term failures away from the government and onto the sector. This is an incredible risk for NBDTs to take on and means that the collapse of a DSIB could easily lead to one or many of us becoming unviable. We note that the Cabinet Paper suggested that the intention would be to have a Government backstop while the fund was being built up – we hope that this remains the intention and believe this should be expressly provided for in the Bill.

The principles in clause 227 for setting levies do not specify that a proportionate approach will be taken. Instead, the required considerations are risk, cost of a specified event (noting this includes both depositor compensation and scheme infrastructure) and the impacts of levies on financial stability of institutions apply broadly to "classes" of deposit takers that are not defined in the Bill. As a starting point, the Bill should include the safeguard implemented in Australia and the United Kingdom, where levies may not exceed 0.5% of the entity's insured deposits in any calendar year.[9] We believe the approach we have suggested to classes of deposit takers for determining standards is probably equally applicable to Depositor compensation. The Bill should also explicitly provide that levies must be proportionate to the level of insured deposits of each individual entity and an ability for non-systemically important deposit takers to opt out of the scheme.

The Reserve Bank appears to have taken the view that risk of failure should be a primary consideration. As we have submitted previously, we strongly believe that risk-based levies are likely to be problematic and prefer a flat rate with DSIBs being required to pay a premium to reflect the systemic risk and the implicit supports likely required for them and signalled through proposed changes to the Public Finance Act. The purpose of implementing the scheme (which requires significant infrastructure as well as the direct cost of depositor compensation) is to promote the stability of New Zealand's financial system, and this purpose should be reflected in setting levies. Further, the likelihood of an insolvency event occurring is incredibly hard to measure, and will likely result in the use of proxies for risk that unfairly favour the large banks. A clear example of this was the failure of Northern Rock, which was rated Aa3 by Moody's immediately prior to its difficulties and was rated by its regulator as a "low probability" firm.[10] Financial strength measures used by central banks are designed for large and complex institutions and do not necessarily reflect the reality of financial risk. For example, empirical evidence shows that mutual deposit takers have a significantly lower rate of failure and maintain funding stability in a financial crisis better than large commercial banks, despite not being subject to the same levels of prudential regulation.[11]

We remain particularly concerned that credit ratings may be used for this purpose. It is clear that the larger, foreign-owned banks benefit from the implicit guarantee of their parent (and in some cases, their parent's government) and our own government. The proposed amendment to the Public Finance Act 1989 to allow for government bail outs (which the Cabinet Paper clearly signals will only be used for the purpose of

[9] Financial Claims Scheme (ADI) Levy Act 2008, s5(2); PRA Rulebook "Depositor Protection", cl 33.4.
[10] FSA Internal Audit Division *The supervision of Northern Rock: a lessons learned review* March 2008.
[11] Annals of Public & Co-operative Economics (Volume 91, Issue 2 pages 237-268)

maintaining financial stability, ie for a DSIB) only strengthens this position. These implicit guarantees, whether or not they would materialise in practice, will certainly not step in ahead of the depositor compensation scheme.

In the event that individual entity risk remains a key principle for setting levies, we support the inclusion of clear guidance in the Bill on how the risk should be measured to avoid disproportionate burden falling on non-systemically important deposit takers. In accordance with international best practice, the assessment of an entity's risk should align with prudential requirements to incentivise these best practice risk mitigation activities.[12] The Bill should explicitly provide that credit ratings should not be used as a proxy for risk.

Another option could be to provide for multiple depositor compensation funds whereby we contribute to the funds for our sectors (similar to how ACC has different funds for different sectors). This might reduce the complexity of determining how our risk compares with that of the DSIBs for the purpose of setting levies and the associated risk that levies will be unsustainable for our sector.

The inclusion of the term "debenture" in the exclusions from protected deposits creates unnecessary uncertainty. The common meaning and usage of the term has changed over time and the legal definition of debenture is, in essence, a debt (which is clearly too broad in the circumstances). This term should be removed or clarified if it serves a particular purpose. If this term was included to address a concern that a deposit could simply be transferred to a new owner in order to extend coverage to it under the scheme, we note that any debt (and not just certain types of instruments) can be assigned under the Property Law Act 2007. The Bill would be better off including a general ant-avoidance provision.

The exclusion of directors of a deposit taker from being eligible for deposit compensation is unnecessary and we believe counterproductive. The exclusion of directors is unlikely to have any meaningful impact on the liability of the depositor compensation scheme. It is good governance practice to have There are potential risks that could arise from a director withdrawing their funds in a crisis. Further, this is likely to create another barrier to us funding talented individuals to join our boards, especially for those of us whose directors are volunteers. It is particularly unfair in the context of the CUBS whose membership structure requires their directors to hold deposits with them (i.e. they must be members to be elected).

Finally, an issue with the depositor compensation scheme in the Bill (and another reason for the Reserve Bank to provide us with direct access to counter-cyclical support), is that the Reserve Bank requires us to hold deposits with banks as part of our capital requirements, then provides that those mandatory deposits are not "protected deposits". While we understand the rationale that sophisticated investors should not be protected, that rationale seems very unfair when those deposits are mandatory. We are forced to hold unprotected deposits with another deposit taker, and if that deposit taker fails, the capital we hold with them is not compensated, which automatically puts us in breach of our own capital requirements. We strongly recommend that the Reserve Bank reconsider this approach and would like to work with the Reserve Bank as part of the working group to come to a solution on this matter, which might include the ability to hold our mandatory capital deposits directly with the Reserve Bank or providing that any "mandatory" deposits must be covered by the scheme 100% regardless of the $100,000 limit.

Regarding the limit on insured deposits, we were pleased to see that it has been raised to $100,000 as a result of our submissions. However, we would like to note for the record that we still believe a limit of $250,000 would be more appropriate to align us with the Australian market.

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[12] See for example the 'Guidelines on Methods of Calculating Contributions to Deposit Guarantee Schemes' published by the European Banking Authority

Crisis management and Resolution

Part 7 of the Bill is impractical for smaller deposit takers. The requirements that each licenced deposit taker must have a plan in place for the event that it enters into resolution seems unnecessary for the NBDTs. Unless the deposit taker poses a threat to financial stability, we do not see the need to commit significant time and resource to pre-planning. While the Bill makes this the responsibility of the Reserve Bank, this will undoubtably require significant resource from the deposit takers to support the development of this plan.

Part 7 also sets out a very complex statutory management regime for deposit takers. The reality is that the complexity of this approach and the resources required to undertake such a process would not be used on deposit takers of our size, whose failure would have minimal impact on financial stability and the economy. The Bill does not provide the Reserve Bank with any alternatives which means the most likely outcome for smaller deposit takers is that they will be put into liquidation. That being the case, it is also worth noting that smaller deposit takers will not have the benefit of accessing funds from the deposit compensation regime to support a resolution measure under clause 218 of the Bill. This increases the benefit of the depositor compensation scheme for DSIBs relative to smaller deposit takers and should be included in the Bill as a matter the Minister must have regard to when setting levies.

As noted in our previous submissions, our supervisors under the current regime have the ability to appoint a receiver. Receivership is well-understood by insolvency professionals and the legal profession and can be implemented at speed. We strongly suggest that this should be included in the Reserve Bank's resolution toolbox. There is precedent for a regulator having this power with the FMA under the FMCA. An alternative for most NBDTs, if the charge over assets was preserved in a trust deed, is to retain the power to appoint the receiver in those trust deeds on the direction of the Reserve Bank. In our view, a clear statutory power would be preferable, but this option is still worth considering. If receivership were included in the Bill we do not believe that the no creditor worse off rule would need to apply, as a receiver would be exercising conventional powers and almost by definition no creditor should be worse off.

Accountability

The Bill proposes to grant the Reserve Bank significant levels of discretion to determine the rules applying to deposit takers outside of the legislation. We believe the scope of this discretion is wider than appropriate and risks giving the regulator de facto powers that should be exercised by Ministers who are politically accountable. The Legislation Guidelines created by the Legislation Design and Advisory Committee state that:

> [l]egislation should not delegate a power to make secondary legislation in respect of matters that are more appropriate for an Act. As a general rule, matters of significant policy and principle should be included in an Act. Secondary legislation should generally deal with minor or technical matters of implementation and the operation of the Act.[13]

This wide discretion is coupled with an absence of accountability mechanisms that provide regulated entities with little comfort that they will be regulated fairly, consistently or transparently over time. While we are encouraged by the profile of and support for the NBDTs in the Reserve Bank at present, this is not guaranteed indefinitely, and we are not convinced that this will protect us against well documented phenomena such as regulatory creep and regulatory capture by the large, systemically important banks.

We believe that it is important that constraints are incorporated into the Bill. The rules created by the Reserve Bank under delegated authority will not be subject to the parliamentary process (noting that standards will be subject to the Regulation Review Committee, but do not appear to need cabinet approval) and the Bill provides no real means of challenging them. Earlier in our submission, we have suggested some areas of the Bill where guidance should be provided on how discretion should be exercised in relation to proportionality. We expect there may be other discretions that would benefit from additional guidance.

We also suggest the following mechanisms be included in the Bill to enable entities that are regulated by the Reserve Bank to be able to get some comfort that there are practical mechanisms available if they believe the Reserve Bank overreaches in its role as kaitiaki or makes decisions that have not properly considered its statutory mandate.

Strategy and Reporting

First, we suggest that the Bill requires the Reserve Bank to develop and publish a strategy on how it intends to deliver on the purposes of the Deposit Takers Act, in a manner similar to that required of the PRA under the Financial Services and Markets Act 2000 (UK).[14] The Reserve Bank would be required to:

a) determine its strategy in relation to its objectives and revise that strategy as necessary from time to time;

b) consult with the Finance and Expenditure committee on the draft strategy before finalising it;

c) complete a review of the strategy annually; and

d) publish the strategy (and any revised strategies).

We would also encourage the Finance and Expenditure Committee to hear from regulated entities as part of the reporting process.

We note that the Governor mentioned during the Hui that the Reserve Bank will go through a process of re-evaluating its risk appetite. We welcome this review and recommend that a transparent risk appetite in

[13] LDAC Legislation Guidelines at 68.
[14] Financial Services and Markets Act 2000 (UK), s 2E.

relation to its role as prudential regulator be required to be developed and published by the Bill as an additional accountability measure. In setting risk appetite, the Reserve Bank should be required to have regard to the Financial Policy Remit, proportionality and trade-offs between greater competition and diversity in the financial sector and the soundness of the institution (taken in aggregate).

Administrative Appeals Tribunal

Regulated entities need a mechanism to challenge the Reserve Banks decisions that is more accessible than applying to the courts. This is particularly so given the decision when enacting the Reserve Bank of New Zealand Act 2021 not to appoint a separate governance board to oversee prudential regulation (similar to the Financial Markets Authority – but modelled on the approach used in England). This means the Reserve Bank may not have the expertise on a governance board to review decisions of officials, nor a culture or structure to do so.

Decisions of APRA and the PRA in the United Kingdom can both be appealed at administrative appeal tribunals. The Australian AAT can consider appeals on their merits and exercise the same powers as the original decision-maker. The tribunal in the United Kingdom will consider appeals on points of law only and can direct the decision maker to reconsider if they determine an error was made. In either case, but particularly the latter, it will be crucial to ensure the Bill provides a robust legal framework as a means of holding the Reserve Bank to account.

As well as being costly, recourse to the courts is largely meaningless when legislation provides such wide discretion – and while judicial review has been used successfully against other regulators in New Zealand, it is widely thought globally to be a largely ineffective remedy against central banks. We suggest the Bill provides for a tribunal where decisions of the Reserve Bank can be reviewed and that this potentially includes merits review of decisions on standards – rather than effectively leaving the use of the Regulations Review committee with its limited scope as the next best option. New Zealand does not have a general administrative appeals tribunal, but examples of specific ones can be found with the Customs and Social Security Appeal Tribunals.

An example of where it is desirable to have a mechanism to challenge the Reserve Bank is conditions of licence. The Bill has included both the concept of standards and conditions of licence. The former will be subject to review by the Regulatory Review Committee to ensure consistency with the Deposit Takers Act and because they will be legislative instruments there is some legal certainty on how to interpret them, the latter do not carry with them the same legal certainty and yet can have very similar consequences where there is non-compliance. It will be important to avoid regulatory creep through the overuse of conditions and the risk of criminal liability for breaches of potentially unclear conditions (because they are not subject to the same statutory test as standards). New and smaller banks may wish to challenge the Reserve Bank on whether conditions are proportionate to their size and the risk they pose to financial stability.

While decisions relating to the resolution of a deposit taker would not be subject to this appeal right because of their critical and timebound nature, review of other discretionary powers would support the fairness and legitimacy of the regulatory framework for deposit takers.

Other Matters

There are a number of other matters that we believe should be clarified or included in the Bill which we set out below:

(a) The definition of "prudential obligation" includes AML/CFT obligations. We do not think this is appropriate given the existing framework for obligations, enforcement and supervision under the AML legislation and might lead to inconsistencies.

(b) We suggest that "conduct" be included as a standard under Part 3 with the intention that it satisfy the FMA's conduct requirements as a means to streamline the regulatory burden.

(c) The director's due diligence duty needs to be very carefully considered to ensure that it does not effectively require directors to take on the role of management in respect to prudential obligations and it does not unreasonably deter talented individuals from taking on roles as directors. While NBDTs directors already have significantly wider liability than bank directors (because they are liable for all offences committed by the entity), the addition of a due diligence obligation is a significant addition.

(d) Directors' liability for making false or misleading representations to the Reserve Bank under clauses 168-170 should only include circumstances where the director knew or was reckless to the fact that the statements were false or misleading. Criminal liability is not appropriate in circumstances where the director "ought reasonably to have known".

(e) We do not understand why the Trustee Supervisor Act 2011 has been amended to include references to deposit takers if the intention is that deposit takers will no longer be required to comply with s 103 of the FMCA. We assume this is an error.

(f) We are unable to find the source of law in the Bill which exempts all deposit takers from the requirement to comply with section 103 of the FMCA.

(g) We believe this Bill should be used as an opportunity to align the change of control process in subpart 5 of part 2 of this Bill, Financial Markets (Conduct of Institutions) Bill and in the Building Societies Act / Friendly Societies and Credit Unions Act so that we do not need to involve the RBNZ, FMA and registrar in different ways at different times.

(h) We are not sure how clause 80(a)(v) is meant to work in respect of issuing standards in respect of "concentration risk". Is this intended only to refer to an individual deposit taker's concentration risk in a specific area / product, or is it intended that this will be used to address systemic concentration risk? How this is applied could be particularly concerning for NBDTs who operate only in some regions, have a common membership bond based on workplaces or focus on niche markets. Given the value to the wider system, this should not be discouraged.

(i) We do not understand why there is an ability to create standards in relation to "security interests granted over the property of the deposit taker" in clause 73 – giving security usually related to deposits where customers had a charge under trust deeds, which is being removed. This type of standard was not described in the Third Consultation Paper.

(j) It is not entirely clear who the recipient of sums paid in lieu of a penalty is meant to be – the Reserve Bank or the Crown? Clause 145 seems to suggest it is paid "to the Bank" but clause 147 suggests it is paid "into a Crown Bank Account". We would be concerned if the Reserve Bank used the power in clause 145 to use the undertaking provisions as a "revenue generating" exercise.

(k) It is not clear to us how clauses 91(1) and (2)(b) operate together. Clause 91(a) seems to suggest a director can only be indemnified in respect of costs associated with a claim made under clause 88 if judgment is given in favor of the director or the proceedings are discontinued (and if expressly permitted by the constitution). However, clause 91(2)(b) goes on to say that a director can also be indemnified in respect of costs incurred by the director in defending or settling any claim or proceeding relating to any "such" liability (which we expect relates to liability for a breach of clause 88). If our reading is correct, then clause 91(2)(b) renders clause 91(1) largely redundant. Can the RBNZ clarify how these sections are intended to operate together? Finally, we question what value there is in requiring all deposit takers to, effectively, amend their rules and constitutions to permit an indemnity to be given. We suggest that if a right to grant an indemnity already exists in the Constitution or Rules, say, for the purposes of section 162 of the Companies Act (or equivalent) that should be sufficient.

(l) In addition, we note that there are many similarities between clauses 90-92 of the Exposure Draft and section 162 of the Companies Act, albeit structured quite differently. Can the RBNZ confirm whether the intention is for clause 90-92 to operate similarly to the Companies Act position or whether the intention is for the prohibition and exceptions to operate quite differently and if so, what the policy reasons for this are?

Deposit Takers Bill - Summary of Suggestions

Introduction

2. The Bill needs to have an explicit purpose of fostering a more inclusive, diverse and innovative financial sector.

3. The Reserve Bank should create working groups including NBDTs to refine the Exposure Draft of the Bill.

Transitional Uncertainty

4. Many of the NBDT's trust deeds provide for a charge over our assets in favour of depositors; the Bill needs to deal with mitigating the risk to depositors of the loss of that charge (or preserving it).

5. NBDTs below a certain size should be exempt from the requirement to have a credit rating – this should not be a matter for RBNZ discretion (given it is currently a regulatory exemption).

6. Macro-prudential policy should only apply to lenders over a certain size, and not all registered deposit takers.

7. The RBNZ's role in imposing lending standards should be limited to macro prudential standards and indirectly through capital adequacy rules.

8. All NBDTs should be automatically transitioned to the new regime based on meeting existing standards.

9. The RBNZ should work collaboratively with the Trustees and NBDTs (as the supervised entities) to enable the lowest impact transition possible.

10. There should be a statutory obligation on the Reserve Bank to make regulatory decisions as soon as reasonably possible (i.e. no derogation from the current time frames with trustees).

Purpose

11. The focus on financial stability needs to be weighed against other societal benefits, such as competition, innovation and financial inclusion. This should be reflected in the Bill. Additional purposes could include, for example, promoting financial inclusion, competition, the co-operative economy, innovation and increasing domestic capability.

12. The sub purpose in clause 3(2)(a) should be amended to read "*to promote the safety and soundness of each deposit taker having regard to their systemic importance and consequence of failure on the whole financial system*".

13. An additional principle should be included in clause 4, being the need to give effect to the Financial Policy Remit.

Proportionality

14. The FMA and the Reserve Bank (along with the rest of Council of Financial Regulators) should work together to articulate the details of how regulatory proportionality will operate in practice and that this detail should be translated into the Bill.

15. Proportionality should be expressly referenced in:

(a) part 2 relating to criteria for applying for a licence, imposing conditions of licence (including the application of standards) and the process for assessing whether a director or senior manager is fit and proper;

(b) part 3 relating to whether the Reserve Bank will exempt a deposit taker from the requirement to get a credit rating, when creating classes of deposit takers for the purposes of issuing standards, and when issuing standards;

(c) part 4 relating to the Reserve Bank's approach to supervision of deposit takers;

(d) part 6 relating to the levies imposed on deposit takers; and

(e) part 7 relating to the use of resolution tools.

Standards and Conditions

16. The Bill should set out principles that the Reserve Bank must have regard to when making decisions relating to the establishment of classes, conditions of licence and standards, including that standards should be proportionate to the risk the entity poses to New Zealand's financial stability.

17. The Bill should provide for certain classes of deposit takers in the legislation itself as a starting point, based on factors such as market share of deposits, corporate form, a class for DSIBs, a class for deposit takers with cross-border operations and even classes based on sources of funding.

18. The Bill should require the Reserve Bank to tailor standards to separate classes unless there are good reasons not to do so. The Bill could then enable the Reserve Bank to create additional classes based on characteristics that may change over time such as dollar value of deposits or assets, customer niches, complexity of business and financial products offered.

19. Minimum capital requirements should be introduced for new licenced deposit takers. All existing NBDTs should be "grand-fathered". However, those below the threshold, should be given the option to opt out of either:

    (a) being fully licenced and be subject to a simplified regime, or

    (b) at least of the depositor compensation scheme on the basis they make it very clear their deposits are not subject to the scheme.

Supervision

20. Guidelines to entrench proportionality should also be included around the intensity of supervision, particularly information gathering powers under clause 95 and onsite inspection powers under clause 110.

Benefits of being prudentially regulated

21. The Bill should follow the Australian approach, which allows all authorised deposit takers to call themselves banks unless APRA determines otherwise.

22. The Reserve Bank should be required to:

    (a) provide liquidity support itself (through liquidity facilities with appropriate modifications to acceptable collateral and by holding deposits); or

    (b) reclassify our deposits with banks so NBDTs can earn retail rates; or

(c) if it will not provide standby liquidity enable registered deposit takers to raise insured funds without paying the insurance premium.

23. The Bill should specifically provide that any licenced deposit taker has the right to an ESAS account with the Reserve Bank.

Depositor compensation scheme

24. The Bill should include the safeguard implemented in Australia and the United Kingdom, where levies may not exceed 0.5% of the entity's insured deposits in any calendar year.

25. The Bill should explicitly provide an ability for non-systemically important deposit takers to opt out of the deposit compensation scheme.

26. The Bill should explicitly provide that credit ratings should not be used as a proxy for risk.

27. The Bill should include systemic risk as a factor to be taken into account.

28. The Bill should include a general anti-avoidance provision against deposit splitting when an entity is under stress, rather than, for example, excluding debentures (which are not clearly defined) when term deposits have exactly the same characteristics (ie can be assigned).

29. The exclusion of directors of a deposit taker from being eligible for deposit compensation should be removed.

30. Mandatory deposits held for liquidity requirements should be protected deposits.

Crisis management and Resolution

31. NBDTs should be excluded from needing a resolution plan because of the simplicity of their business.

32. The ability to appoint a receiver to NBDTs should be included in the Reserve Bank's resolution toolbox. No creditor worse off should not apply to receivership.

Accountability

33. The Reserve Banks discretion to determine rules applying to deposit takers is wider than appropriate and should be limited to operational matters.

34. The Bill should require the Reserve Bank to develop and publish a strategy on how it intends to deliver on the purposes of the Deposit Takers Act and particularly proportionality.

35. The Bill should require a transparent risk appetite in relation to the Reserve Bank's role as prudential regulator to be developed and published as an additional accountability measure.

36. The Bill should provide for a tribunal where decisions of the Reserve Bank can be reviewed and that this potentially includes merits review of decisions on standards and conditions.

Other Matters

37. The definition of "prudential obligation" should not include AML/CFT obligations.

38. "Conduct" should be included as a standard under Part 3 with the intention that it satisfy the FMA's conduct requirements as a means to streamline the regulatory burden.

39. Directors' liability for making false or misleading representations to the Reserve Bank under clauses 168-170 should only include circumstances where the director knew or was reckless to the fact that the statements were false or misleading.

40. The Trustee Supervisor Act 2011 should not be amended to include references to deposit takers if the intention is that deposit takers will no longer be required to comply with s 103 of the FMCA.

41. This Bill should be used as an opportunity to align the change of control process in subpart 5 of part 2 of this Bill, Financial Markets (Conduct of Institutions) Bill and in the Building Societies Act / Friendly Societies and Credit Unions Act so that we do no need to involve the RBNZ, FMA and Registrar in different ways at different times.

42. Clause 80(a)(v) relating to concentration risk needs to be proportionate to take account of specialised lending and regional NBDTs.

43. There should not be an ability to create standards in relation to "security interests granted over the property of the deposit taker" in clause 73 (without clearer guidance on why it is needed).

44. Sums paid in lieu of fines as part of undertakings should be paid to the Crown not Reserve Bank.

45. Clauses 91(1) and (2)(b) should be reviewed as clause 91(1) appears redundant.