Deloitte.

Reserve Bank of New Zealand

Review of the bank directors' Attestation regime

10th August 2017

Contents

Introduction

This report should be read in conjunction with the Statement of Responsibility at the back of the report, limitation and disclaimer set out in 1.3.

1.1. Report structure

This report is structured in 5 Parts, prefaced with an Executive Summary and supported by Appendices:

- **Executive Summary** details the Review objective, places the Review in context of contemporary prudential policy and supervision developments and summarises the key thematic findings and recommendations.
- **Part A** describes, in an executive summary format, the Review's key thematic findings. These thematic findings take a medium to long-term view of those matters consider important in assuring the long-term sustainability and success of the Reserve Bank's supervisory regime with its reliance on the three pillars of market discipline, self-discipline and regulatory discipline;
- **Part B** describes a best practices (maturity) model developed specifically for the Review that incorporates (7) criteria that underpin attestation 'effectiveness'. The Model was applied at the individual bank level in order to review the banks against a consistent set of criteria and as the basis to aggregate information for purposes of informing the thematic findings (Part A.);
- **Part C** details the reviews undertaken for each bank using the Model described in Part B and a combination of information gathered from the Section 93 documentation request and from the interviews carried out with bank executives and directors;
- **Part D** provides both summary and detailed information from the anonymous survey undertaken at the outset of the Review. Apart from the stand-alone insights offered by the survey, the survey also helped in the framing of several hypotheses that were later tested during the documentation review and interviews.
- **Part E** describes the detail the Review approach.
- **Appendices** comprising details of the survey results; a summary of the banks (including Bank officers and other stakeholders) engaged during the Review. The list of documents supplied by the banks is not referenced for reasons of anonymity and due to the sheer volume (circa 800).

1.2. Acknowledgment

We would like to acknowledge the assistance received from the following:

- The Reserve Bank of New Zealand (Reserve Bank) as the prudential regulator for their broad assistance in a range of logistical matters including scheduling the extensive interactions with senior people across the banks and their advisers;
- The 'participating banks' including respondents to our online survey, interviewees we spoke to and those bank personnel responsible for providing requested documentation under the direction of the Reserve Bank.

1.3. Disclaimer

This report is provided solely for the exclusive use of the Reserve Bank of New Zealand and solely for the purpose of assessing the effectiveness of the director attestation regime established by the Reserve Bank of New Zealand Act 1989, with respect to New Zealand-incorporated registered banks.

Our report is not to be used for any other purpose, recited or referred to in any document, copied or made available (in whole or in part) to any other person without our prior written express consent. We accept or assume no duty, responsibility or liability to any other party in connection with the report or this engagement, including without limitation, liability for negligence in relation to the estimates of compliance costs and any industry feedback expressed or implied in this report.

The assumptions used within this report are based on the prevailing Reserve Bank Act and regulations in force in New Zealand at the time of writing and the results / findings have been provided following all reasonable engagement with senior officers of the Bank's concerned and the representations made and information supplied by these officers in response to our requests. We provide no assurances that the information supplied is either complete or correct and accept no accountability or responsibility for the information supplied.

The procedures we have performed as part of this engagement do not constitute an assurance engagement in accordance with New Zealand Standards for Assurance Engagements, nor do they represent any form of audit under New Zealand Standards on Auditing, and consequently, no assurance conclusion or audit opinion has been provided.

1.4. Report Clearance

The contents of this report have been discussed with the Reserve Bank of New Zealand in a series of review meetings and cleared for publication in final form on 10th August, 2017.

Executive summary

2.1 Objective and context

The objective of this thematic review (Review) is to: *to assess the effectiveness of the New Zealand-incorporated registered banks' arrangements for quarterly disclosure statement attestations (Directors' attestation regime), and the processes that bank directors use to fulfil their obligations under sections 81 to 82 of the Reserve Bank of New Zealand Act 1989.*

The Review should be seen in the context of the wider set of consultations being undertaken by the Reserve Bank related to prudential policy and supervision, including in particular: the dashboard approach to quarterly disclosure, the Capital Review (upcoming)[1]. Also relevant is the recently completed IMF Financial Sector Assessment Program (FSAP) assessment[2].

The case for assessing the 'effectiveness' of the directors' attestation regime at this time also rests fundamentally on (challenging) the assumption that given its track record to date it will continue to serve New Zealand well for the foreseeable future. Our Review has throughout implicitly challenged and tested this assumption with an eye to the future, recognising the regime's positive (20 year) track record and contrasting this to the majority of alternative supervisory regimes around the world that rely extensively on comprehensive onsite inspections of banks. Our approach is accordingly precautionary, underpinned by a philosophy of 'Trust but Verify'.

While conducted at the instance of the Reserve Bank and with the support and involvement of its personnel the Review has been an independent process led by Deloitte and in that respect the conclusions and recommendations are based on what we heard from the banks and our own professional judgment in interpreting and evaluating that feedback. Our recommendations are mindful of the critical balance that needs to be struck between regulatory policies and constraints on the one hand and the ability of bank boards to take decisions considered in the best interests of their shareholders on the other and which, if impeded, brings attendant risks and costs. The inherent moral hazards have been evident at every stage of the Review, with the FSAP report (10 April10, 2017) one example of the ongoing and robust challenge needed to ensure the regime's continued effectiveness.

The Review has been conducted with substantial input from a wide cross section of New Zealand registered banks and the boards, senior managers and advisers including: chairmen, executive, non-executive and independent board members, chief executives, senior management and external auditors. We are grateful and thank them for the significant time and effort they have invested in participating in the initial online survey, the subsequent targeted interviews and compiling relevant bank documentation requested by the Reserve Bank under a Section 93 request specifically for purposes of the Review.

This report has, in the spirit of the review, been written in the style of a consultative document. The key thematic findings and any related draft recommendations are set out immediately below. The recommendations are proposed as good practice based on our view that their adoption will benefit the directors' attestation regime without increasing moral hazard and recognising the bias of other equivalent (prudential, supervisory) regimes toward other interventions and tools for which the case remains to be convincingly made in a New Zealand context.

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[1] http://www.rbnz.govt.nz/-/media/ReserveBank/Files/regulation-and-supervision/banks/publications/Banking-industry-update-newsletter-apr2017.pdf?la=en

[2] http://www.rbnz.govt.nz/news/2017/05/imf-releases-new-zealand-fsap-findings-and-recommendations

Summary assessment

Based on the key thematic findings from the interviews, our judgement of the relative maturity levels of the individual banks against a range of (effectiveness) criteria (details provided in the body of this report) and using what in substance was a 'reverse stress-test' of the regime. We are of the view that the directors' attestation regime is ***largely effective***[3]***.*** A lower assessment of 'Somewhat Effective' would in our view be unwarranted given the extent of positive evidence we have gathered and which outweighs known shortcomings. A higher assessment of 'Fully Effective' is similarly unwarranted given the extent of the unknown unknowns facing all regulatory and supervisory regimes in an uncertain world. Our final assessment is accordingly forward-looking and takes a precautionary view of the regulatory operating environment in a global context.

Our concerns are that while the regime appears to have been effective since its inception, including through periods of significant market disruption, this is no guarantee of future effectiveness and there are some areas in which its operational resilience could in future be challenged.

Three particular vectors of potential vulnerability (superordinate themes) stand out, where future risks could crystallise:

First, the reliance on high quality directors, particularly those with experience in banking, in a market generally regarded as 'thin' in New Zealand. While outside of the control of the Reserve Bank, this is an area where the Bank can help catalyse market-led enhancements in governance e.g. by providing leadership in working with the sector to both clarify and raise its expectations of boards. In this context the Bank should also review the effectiveness of its current 'no objection' approach to director appointments.

Second, (poor) culture. Culture is not currently captured explicitly in any Reserve Bank requirement or guidance, nor is it assessed and yet is ultimately at the root cause of many failures.

Third, the extent of verification as a basis for determining banks' compliance with regulations and guidelines. There is a case for more verification short of extensive on-site audits by the Reserve Bank's own staff and practical examples suggested as to how this might be achieved e.g. periodic thematic reviews across all banks focused on particular areas of concern / interest. Such reviews could also serve to surface 'best practices' for wider sharing across the sector (see workshop feedback under *Thematic Findings* below).

The thematic findings below marshal up into these three superordinate themes. The recommendations in each case are aimed at helping further enhance the overall operational resilience of the regime.

2.2 Thematic findings

We summarise below the key thematic findings from the Review along with related recommendations. As at the date of this report these findings have been shared by the Reserve Bank with the industry and a number taken up in discussion with the banks in series of (Reserve Bank led) workshops, in which Deloitte also participated. The Reserve Bank will be making its own determination, given this workshop feedback, of the relative importance and priority of these findings and its responses.

It is noteworthy that the banks participating in the workshops were unanimous in calling for similar and more regular forums in which the discuss and share views on 'best practices' across the areas and topics mentioned below as well as others that become topical in time. We are supportive of this as it speaks to the 'supervisory engagement' finding below, and can only further benefit the resilience of the attestation regime.

[3] On a graduated scale of: *Ineffective – Somewhat Effective – Largely Effective – Fully Effective.*

Area / Topic	Key Finding	Recommendation/s
Director responsibility	• Board directors appeared unanimously aware and mindful of their personal responsibilities and accountability under the attestation regime. This extended beyond a purely legal view to embrace the substance of their attestations.	• Reserve Bank continue to exercise professional regulatory leadership including benchmarking its own role in helping catalyse improvements.
Culture	• The importance of a strong positive culture was widely acknowledged simultaneously as: critical to attestation integrity and the ongoing sustainability of the attestation regime; a source of competitive advantage, and the absence of which raised the chances of negative events and even bank failure. • Culture is not currently captured in any Reserve Bank requirement or guidance, nor is it formally assessed.	• Reserve Bank require the banks to form a view on risk culture and monitor this. • Reserve Bank to form its own view on individual bank's culture and across the sector and use to inform more explicitly its own ongoing supervision of individual banks.
Attestation - Type	• There are, prima facie, varying degrees of clarity, and potential misalignment, between each bank's stated director attestation goals including type of assurance (whether 'reasonable' or 'limited') and the approaches followed (including supporting executive and management attestations) to provide that assurance.	• Reserve Bank clarify its expectation that 'reasonable assurance' applies as well as generally accepted assurance standards.
Attestation – Design and execution	• While 'end-to-end' views of the directors' attestation process are evident among the larger banks, this is not so with the smaller banks. Moreover, even with the larger banks a 'comprehensive' and holistic approach to attestation is still in its early stages of development.	• Reserve Bank set out its expectations of banks in relation to risk management (e.g. via a standard equivalent in substance to APRA's CPS 220) and in relation to directors' attestations as comprehensive and integrated risk and control system beyond process.
Board performance	• Not all boards are regularly or systematically assessing their performance. • Board performance in relation to specific 'board only' responsibilities is not consistently carried out by all banks. There was little or no evidence of any bank board evaluating specifically how well the board or individual directors fulfilled their specific responsibilities relating to quarterly attestations.	• Reserve Bank require as part of BS10 that bank boards assess their own performance on a regular basis, ideally with external facilitation and that these assessments include selected topic 'deep-dives' e.g. directors' attestations. • Reserve Bank encourage disclosure by banks of their (board) evaluation process and plans for continuous improvement.
Regulatory interpretation	• Interpretations of some regulations appear to vary quite widely between the banks. This coupled with the absence of materiality thresholds in relation to the Conditions of Registration can result in	• Reserve Bank issue guidance on matters identified (in conjunction with the banks) on which

Area / Topic	Key Finding	Recommendation/s
	disproportionate effort being expended by a bank in meeting the 'not false or misleading' requirement under the directors' attestations; and / or reducing the incidence of relatively minor (unimportant) differences.	there is a consensus that there is unnecessary lack of definitional clarity; and Materiality in relation to the Conditions of Registration.
Board composition and experience	• There was wide recognition and acceptance that the effectiveness of the attestation regime depended heavily on having appropriately skilled, competent and experienced individuals in key roles – both board and management. Opinions were divided on how to achieve and maintain this through time, mindful of the challenges faced at an industry level in attracting and retaining high calibre personnel.	Reserve Bank consider: • Being more active in assessing weaknesses on boards[4] (and senior management) and requiring them to be addressed (rather than just attempting to use moral suasion); • Setting policy requirements around how many boards an individual could sit on in addition to their bank board. • Consider periodic reassessment by banks of directors and senior management rather than the current 'set and forget' approach.
Attestation architecture	• There were views variously expressed (although pervasive) that the disclosure regime and particularly the conditions of registration have become somewhat difficult to navigate and understand potentially rendering its implementation increasingly ineffective (by design) through time.	• The Reserve Bank consider, in conjunction with the above recommendations (in particular: 2.3, 2.4 and 2.6), providing explanatory guidance as to how the component parts of the attestation regime fit together as a framework (from the regulator's perspective) and in particular how prospective regulatory developments will be catered for and factored into the framework
Data and Analytics	• Banks are increasingly realising the value of their data assets and planning to leverage these. The larger banks have plans within 5 years to make increasing use of data and analytics beyond credit (scoring / rating) to support unbiased decision making, and automate aspects of auditing e.g. controls testing.	• The Reserve Bank similarly leverage this trend, and increasing availability of cost effective tools to validate and corroborate bank attestations beyond

[4] Through a combination of bank self-assessments and the Reserve Bank's own assessments.

Area / Topic	Key Finding	Recommendation/s
		the manual processes currently deployed.
Residual Regime vulnerabilities	• Interviewees when asked ventured a range of risks that the directors' attestation regime was not well suited to identifying / dealing with including: (i) 'event risks' - because of their potential 'surprise' / 'speed of onset' e.g. cyber risk, conduct risk and (ii) Risks characterised by their secular nature ('secular risks') that might not be identified sufficiently early by either management or the regulators e.g. poor culture (see above), progressive risk appetite 'creep', complacency.	• In addition to and complementary to this Review the Reserve Bank continue to explicitly challenge on an ongoing basis, the directors' attestation regime as a prudential tool. This includes identifying and forming its own view on where residual vulnerabilities lie and whether any further mitigating measures need to be taken having regard to it full suite of regulatory tools.
Supervisory engagement	• A significant number of interviewees ventured that they would like more frequent and constructive engagement / interaction with the Reserve Bank beyond what is currently in place, to achieve greater consistency and clarity on matters open to widely varying interpretation. This in turn would assist them in benchmarking and improving their practices.	• The Reserve Bank consider the suggestions raised by the banks, as a way of further improving the attestation regime. This necessarily involves a potentially fundamental review of its own supervisory resourcing model to achieve the right (sustainable) outcomes

Part A – Major themes

We highlight in this section the major 'themes' that emerged from our review. In each case we have also provided recommendations for consideration by the Reserve Bank. We do not venture a view on the appropriate instrument this being beyond the review scope. We do however distinguish at a high level between what we refer to as regulatory 'standards' and 'guidance'. The former a compulsion instrument and the latter enunciating observed 'good practices' as these continue to evolve locally and in the international markets.

We do not see our recommendations as conflicting with or contradicting the Reserve Bank's general approach of issuing outcomes-based regulation.

For each of the key themes we have highlighted particular 'Areas of focus' (boxed) drawn from the Review terms of reference (in red), as well as from bank director reciprocal lines of enquiry shared during interviews (in green). These are not mutually exclusive to each theme, so there are some repeats.

While responding to the IMF's FSAP concerns is beyond the scope of the Review we have, where appropriate, also captioned the IMF's observations / recommendations where they relate to a key theme.

The themes are not presented in any order of priority, rather in a logical structure.

2.1 Director responsibility

Areas of focus:

- Any differences in the roles (perceived or in practice) between the independent directors versus non-independent directors in the attestation process?

- What behaviours is the regulator seeking to induce and maintain in bank disclosure processes and reporting?
- Are the regulator's own behaviours/communications/approaches well aligned to supporting and enhancing the behaviours that it seeks from institutions?
- How might the regulator differentiate its response to institutional behaviours along a continuum from: an honest mistake, with full early disclosure and correction/remediation through to the more serious / egregious?
- How might the regulator form a view of its engagement effectiveness and the extent to which any changes might in turn enhance the effectiveness of the directors' attestation regime?

The survey and interviews showed that all directors, whether independent or not, were well aware of their important responsibilities in attesting and the seriousness with which they approach their individual attestations.

This conviction arises in part from a legal perspective on their (non-delegable) responsibilities, borne out by the various opinions cited and which a number of banks appear to commission periodically. More importantly however were strongly held views that the strong emphasis on director accountability is the only effective way for banks to proactively manage risk in a forward-looking way that fits the individual circumstances of a bank, in an environment that is increasingly characterised by constant, rapid change. Directors also ventured that this approach helps mitigate against attestation becoming a 'box-ticking' exercise, while acknowledging that this ('box-ticking') risk is ever present irrespective of the type of supervisory regime.

Recent historical precedent, particularly in the wake of the finance company collapses and case law (including the Feltex and Centro cases), will undoubtedly have influenced the gravity with which directors view and carry out their responsibilities.

Views were also variously expressed that the attestation responsibility carries with it related responsibilities for the board as a whole to have in place a rigorous training program to continually reinvigorate and reenergise its focus on evolving and emerging trends, risks and issues. This extended to the personal responsibility of individual directors to remain widely read and have in place a program of self-directed continuing professional education relevant to their work on the bank board. One ex director felt that banks boards generally were not working intensively enough at new appointments and then ongoing training of the board to constantly 'lift the bar'.

Recommendation

The Reserve Bank continue to use every opportunity, to:

- Remind directors of their non-delegable responsibility, whether through policy, supervision or enforcement activities;
- Reinforce the institution-specific and system-wide connections, implications and expectations arising both directly and indirectly from this personal responsibility that each director carries;
- Challenge and test that its regulatory approaches / responses are demonstrably proportionate to the risks posed and the attitude and motivation of individual banks toward compliance.

The Reserve Bank continue to show proactive leadership both as part of existing regulatory fora[5] and through even higher levels of constructive engagement with individual banks along the lines suggested / encouraged by many of the banks interviewed (See 2.11 *Supervisor Engagement*). There is a particular and distinct role for the Reserve Bank to encourage, set expectations and facilitate opportunities for the Boards to set their own (formal) programs for renewal and continual improvement (See 2.5 *Board Performance* and 2.7 *Board Composition & Experience*).

2.2 Culture

Areas of focus:

- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.
- What processes exist when directors or management conclude there has been non-compliance with matters that are attested to.
- Examples of best practices adopted by registered banks with respect to directors' attestation arrangements, and on the extent to which banks materially diverge from best practices.

- What behaviours is the regulator seeking to induce and maintain in bank disclosure processes and reporting?
- Are the regulator's own behaviours/communications/approaches well aligned to supporting and enhancing the behaviours that it seeks from institutions?
- How might the regulator differentiate its response to institutional behaviours along a continuum from: an honest mistake, with full early disclosure and correction/remediation through to the more serious / egregious?
- How might the regulator form a view of its engagement effectiveness and the extent to which any changes might in turn enhance the effectiveness of the directors; attestation regime?

During the majority of interviews, at all levels, good culture was cited as an important, if not the most important, feature of successful enterprises and critical for effective, sustainable risk management practices. We attribute this awareness largely to the sector's experiences during and post the global financial crisis and the focus the topic continues to attract from regulators globally.

[5] Joint supervisors and initiatives such as the Government Regulatory Practice Initiative (G-Reg) Steering Group

Many directors commented on the correlation between an effective attestation process, and the bank having an open culture, one in which directors are confident that management and staff will report upwards all matters that could negatively impact on the attestations. The unavoidable reliance of management sign-offs due to the complexity (and size) of modern banks and to maintain appropriate separation of governance from management underscored the importance of forming a view on culture and regularly testing this through time.

Most directors were quick to note that they believed there was an open culture in their respective banks, and that bad news would flow upwards. Few were able to point to a systematic and regular process or methodology by which this was achieved, some citing the results from staff engagement surveys and others bespoke (risk) culture surveys. One bank cited the APRA (CPS 220) Standard as the key driver for a Group-wide initiative currently in progress.

Culture is not currently mentioned or captured in any Reserve Bank requirement or guidance, nor is it formally assessed. This stands out in contrast with the significant focus on the topic not only by other regulators but by the industry at large and the vast majority of directors we interviewed. Given the fundamental premise and basis of the New Zealand prudential regulatory regime and its reliance on strong governance in the first instance, its omission is the more conspicuous.

Recommendations

- The Reserve Bank consider introducing a requirement, similar to APRA, for the Board to: Form a view of the risk culture in the institution, and the extent to which that culture supports the ability of the institution to operate consistently within its risk appetite; identify any desirable changes to the risk culture and ensure the institution takes steps to address those changes. The regulatory instrument for this could be a general Risk Management Standard equivalent to APRA's CPS 220 – refer further below.
- While already a requirement for the Australian owned 'majors' (under CPS 220) this is an opportunity for the Reserve Bank to ensure that the smaller banks benefit from equivalent guidance while at the same time addressing the IMF's concerns regarding the need for strengthening regulatory discipline[6] and issuing enforceable supervisory standards on key risks[7]. This would also be aligned with the FMA's guidance note for directors and executives of licensed financial services providers[8].
- The Reserve Bank to form its own view of culture within each of the New Zealand banks and explicitly consider culture during its ongoing supervision and regulatory intervention strategies for individual banks and the sector at large.

2.3 Attestation - Type

Areas of focus:

- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.
- What processes exist when directors or management conclude there has been non-compliance with matters that are attested to.
- Examples of best practices adopted by registered banks with respect to directors' attestation arrangements, and on the extent to which banks materially diverge from best practices.

- It became apparent as the review progressed that, unlike financial reporting where generally accepted accounting practice and auditing standards together codify good practice and ensure consistency, there is

[6] B28 –IMF. New Zealand Financial System Stability Assessment (FSSA). April 10, 2017.
[7] B31 – FSSA.
[8] A guide to the FMA's view of conduct. February 2017.

significant variability in how regulations are interpreted and in turn the robustness and quality of the internal controls design and operation to ensure compliance. This was first signalled in high-level discussion around whether each bank's attestation was in substance delivering 'positive' (reasonable) or 'negative' (limited) assurance. Whatever the stated intent, it became evident the controls frameworks and their operation were not necessarily designed accordingly and were in some cases contradictory to the stated intent.

- As a consequence of past regulatory related 'incidents' and the implicit 'positive' form of the director attestations we note that many of the surveyed banks are now requiring that 'due enquiry' include producing evidence to demonstrate appropriate regulatory interpretation, controls design and operation. This is a positive development and underscores the dictum: 'trust but verify'.

- While it is not the responsibility of the Board to concern themselves with the minutiae of controls design and operation it is their responsibility to be explicit about the type of attestations they are making; that they are in turn expecting from management and whether the bank's internal control systems remain fit-for-purpose in fulfilling both the form and substance of their attestations.

Recommendation

The Reserve Bank clarify to the banks (for the avoidance of doubt) its expectation that:

- Directors are providing 'reasonable' assurance when attesting;
- Banks are applying good practice assurance standards in line with ISAE (NZ) 3000 in delivering their attestation recognising the particular requirements for 'reasonable' assurance

2.4 Attestation – Design and execution

Areas of focus:

- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.
- What processes exist when directors or management conclude there has been non-compliance with matters that are attested to.
- Examples of best practices adopted by registered banks with respect to directors' attestation arrangements, and on the extent to which banks materially diverge from best practices.

- Many of the banks (the majors in particular) have well developed and documented attestation processes that cover attestation 'end-to-end', from control source to directors' sign-off. In the case of the second tier banks these were less well developed and for the smaller foreign-owned subsidiaries even less so.

- Internal Audit (where these functions exist) appear to provide some confidence based on general internal audit work performed across relevant areas and view of the control environment, however internal audits of the 'end-to-end' attestation process are not generally undertaken. There was evidence that some audits had been extended to others areas of the attestation process and related control environment with the chance discovery (and then more systematic identification) of shortcomings in regulatory interpretation, controls design and operation. In some cases a significant overhaul of the attestation systems is underway and remains a 'work-in-progress'.

- Even the well documented 'end-to-end' processes (sighted) however failed to capture a more 'comprehensive' view of directors' attestations beyond simply process e.g. the linkages with risk appetite, the Bank's ICAAP. In the cases of the smaller banks (groups 2 and 3); this risks directors, particularly those without banking backgrounds, missing important questions when challenging the attestations and underlying processes.

Recommendation

- The Reserve Bank consider issuing a standard equivalent to APRA's Prudential Standard CPS 220 (Risk Management). The reasons for this (apart from serving as a platform to raise and set expectations in relation to 'culture' (2.2 above) are as follows:

  - To raise the bar for the non-Australian owned banks and present a level-playing field;
  - To bring together in a single standard, its expectations for integrated[9] risk management essential for the effective design and operation of any attestation regime within individual banks and systemically; and
  - To serve as a 'bridge' between the already well developed financial reporting control environment and the less well developed risk control environment, thereby preventing any further development of what is already seen as a somewhat bifurcated (financial reporting vs. risk) attestation regime. In this respect the potential evolution of non-financial reporting controls can be seen as analogous to that that accompanied the Sarbanes-Oxley regime for financial reporting controls – with its explicit requirement for certifying officers (in this case executive management) to attest that:

  o They are responsible for establishing and maintaining 'disclosure controls and procedures'……..for the issuer and have:
    - Designed such disclosure controls and procedures or caused such disclosure controls and procedures to be designed under (their) supervision, to ensure that material information is made known to them, particularly during the period in which the report is being prepared;
    - Designed internal control……………or caused such internal control to be designed under their supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements……;
    - Evaluated the effectiveness of the disclosure controls and procedures, as of the end of the period…………and have presented in their report their conclusions about the effectiveness of the ………controls and procedures based upon their evaluation.

2.5 Board performance

Areas of focus:

- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.
- Any specific role the Chair undertakes in respect of the process, which will potentially require an understanding of the nature of the Chair's relationship with the CEO.
- Any differences in the roles (perceived or in practice) between the independent directors versus non-independent directors in the attestation process;
- The roles of board sub-committees and management committees in the attestation process.
- Examples of directors challenging (and potentially changing) the conclusions reached by management in respect of compliance with matters that are attested to.
- Examples of best practices adopted by registered banks with respect to directors' attestation arrangements, and on the extent to which banks materially diverge from best practices.

[9] Including: scope, roles and responsibilities (Board and management), risk appetite statement, risk management strategy, a business plan, policies and procedures, designated (risk management) function, Internal Capital Adequacy Assessment Process (ICAAP), a management information system (MIS); and a review process to ensure that the risk management framework is effective in identifying, measuring, evaluating, monitoring, reporting, and controlling or mitigating material risks.

- The board of directors is a cornerstone of our prudential regulatory regime. An effective board through its individual and collective (non-delegable) responsibility ensures that the bank complies, on an ongoing basis, with both the letter and spirit of banking regulations.

- Its performance in fulfilling this role significantly influences the culture of the bank and in turn the bank's overall effectiveness in meeting its regulatory obligations. This includes avoiding any complacency and identifying the need for new skills and perspectives in order to respond dynamically to changes in the business environment. Regular and rigorous self-evaluations help a board to assess its performance and identify and address potential gaps in the boardroom.

- Not all of the boards reviewed undertake (independent) board self-assessments as a matter of good practice. In addition, there was little or no evidence of any bank board evaluating specifically how well the board or individual directors fulfilled their specific responsibilities relating to quarterly attestations. However, for those boards that do undertake some form of self-assessment, the documentation provided afforded useful insights into matters considered as being of particular importance to the effectiveness of the directors' attestation regime as a whole, including:

    - Performance of the Chair;
    - Autonomy of the Board
    - Handling of dissent and challenge;
    - Relations with the CEO and management; amongst others

- The quality of the self-assessment tool/s and the manner of their administration affect the quality of the outcome and their value for purposes of assessing effectiveness in the context of the attestation regime. There is high variability in the quality of the sighted self-assessments and scope (apart from encouraging their more regular use) to encourage the inclusion of content that tests the board's effectiveness beyond the routine board protocols and in matters of particular relevance in the context of directors' attestations (and of interest to the Reserve Bank).

Recommendations

- The Reserve Bank consider requiring, as part of BS10, that Boards regularly assess their performance including specifically on matters related to the discharge of their statutory obligations. This can extend to providing self-evaluation topics of particular relevance to the attestation process e.g. culture (of challenge within the Board), the extent and intensity of board training programs and the extent of continuing professional education of individual directors etc.

- The Reserve Bank encourage, in line with best practice, bank board's disclosure of their evaluation process. Research shows that stakeholders value detailed disclosure of the board evaluation process: Disclosures about how the board evaluates itself, identifies areas for improvement and addresses them, and examples of any significant changes in the board's processes or practice that have resulted, provide a window into how robust the board's process is for introducing change. There is no expectation that details of board or individual director evaluations are disclosed; rather, the *process* by which the board approaches the task of continually improving itself.

2.6 Regulatory Interpretation

Areas of focus:

- How directors "benchmark" (or "interpret") each matter that they are attesting to, in the absence of published standards.
- Whether the benchmarking by the directors aligns with the Reserve Bank's understanding on what the directors are attesting to.

Directors found it easier both to attest to and benchmark certain matters compared to others. These appeared to distil to two groups:

a) Those matters where inconsistent interpretations appear to be widest; and
b) Those matters related to materiality

a) <u>Inconsistent interpretation</u>

- A number of areas were cited by interviewees where (presumed) regulatory intent is consistency and precision in measurement and yet either the metric definitions or the basis for their calculation is unclear, leading to a diversity in industry practices. Wide differences in interpretation and application can potentially undermine the integrity of the attestation regime (refer also *Attestation – design and execution* – above). Examples cited include: Mismatch ratios (liquidity); Concentration risk.

- In addition there were a number of areas cited where the outcomes based nature of the regulation can (and does) lead to significantly different interpretations and approaches and where a more prescriptive approach in policy making appeared to be supported. Examples include: Outsourcing policy; Open bank resolution.

b) <u>Materiality</u>

- In a similar vein to regulatory interpretation (above) Financial disclosures have generally accepted accounting principles that apply while the Conditions of Registration have no provisions for materiality. Bringing both the financial and non-financial disclosures together (as two legs) in a single Disclosure Statement with materiality (principles) absent from the one leg (the conditions of registration) creates problems including:
    - Disproportionate effort being expended by a bank in reducing the incidence of relatively minor (unimportant) differences;
    - Conflicting messages e.g. 'not false or misleading' (a relative perspective) compared with the absolute precision which has been shown to apply to some Conditions of Registration breaches;

<u>Recommendations</u>

The Reserve Bank consider issuing guidance on:

- Those matters identified (in conjunction with the banks) on which there is a consensus that there is unnecessary lack of definitional clarity; and

- Materiality in relation to the Conditions of Registration. This guidance should as far as practicable draw on the same principles that underpin the application of materiality to Financial Statement Reporting to ensure from an end user perspective consistency and alignment between both financial statement materiality and materiality as it relates to the conditions of registration in particular as it relates to risk estimates used in financial reporting.

2.7 Board – composition & experience

Areas of focus:

- How directors "benchmark" (or "interpret") each matter that they are attesting to, in the absence of published standards.
- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.
- Specific role the Chair undertakes in respect of the process, which will potentially require an understanding of the nature of the Chair's relationship with the CEO.
- Any differences in the roles (perceived or in practice) between the independent directors versus non-independent directors in the attestation process;

Banking is becoming so complex that its risks cannot be monitored only by bank supervisors and bank regulation cannot try to respond to every single financial innovation. The safety and soundness of banking requires the upfront involvement of shareholders and their representatives on the bank boards. As Alan Greenspan once said, "We need to adopt policies that promote private counterparty supervision as the first line of defence for a safe and sound banking system."[10]

A recurrent theme, whether in relation to directors, management or staff was recognition that the effectiveness of the attestation regime depended heavily on having appropriately skilled, competent and experienced individuals in key roles.

Apart from meeting the regulatory requirements contained in BS10 it was emphasised by a number interviewed that the board must include directors who have the ability to understand the organisational complexities and the risks inherent in the bank's businesses. The predominant view was there should be at least one director (and preferably more) with a detailed knowledge of banking and 'long-term memory' (through the cycle) of the industry. Absent this detailed knowledge strong views were expressed that key issues, risks and developments might be inadvertently missed or passed over. At the same time views were expressed that, without detracting from the importance of good banking experience / knowledge, diversity of skills, experience and background were also very important.

We were provided with one example of a bank's Board Skills Matrix, which was used actively in assessing the current adequacy and future skills required during board succession. In our experience across industries, such forward-looking succession planning is good practice but is not widely practised.

The same interviewees ventured various suggestions on how these challenges could be addressed, including:

- The Reserve Bank being more active in assessing weaknesses on boards and requiring them to be addressed (rather than just attempting to use moral suasion);
- Setting policy requirements around how many boards an individual could sit on in addition to their bank board, so as to avoid directors spreading themselves thinly and not dedicating enough time to properly discharge their banking governance responsibilities;
- Requiring that directors and senior managers go through periodic reassessment by the Reserve Bank;
- As a precursor the above, requiring that formal internal assessments of talent and performance be undertaken and that self-managed 'continuing professional education' (CPE) regime/s be put in place, tracking advancing good practices across the industry;
- Boards being required to put in place formal board training programs, involving 'hard-nosed', bank-oriented workshops against an 'approved' list of topics.

[10] Guidance for the Directors of Banks. Global Corporate Governance Forum (2003).

Recommendations

The above recommendations from industry have merit and are worth pursuing.

In order to avoid the possibility of increasing moral hazard in pursuing any of these options though, we would recommend that the Reserve Bank require banks in the first instance, as a matter of good practice, to:

- Compile a (senior) Management Responsibilities Map – equivalent to the approach used by the FCA[11]. This should include identification of all key responsibilities / responsible in relation to the directors' attestations. This could extend to include specific board roles (Chair, Managing Director, Committee Chair), but with the caveat that this should in no way compromise or be seen to compromise the governance principle of collective responsibility i.e. by implying that different directors may have different levels of duty of care or skill.
- Complement the Responsibilities Map with details of the optimal skills and experience required for the discharge of each of the identified responsibilities;
- Require that boards put in place formal programs for their own renewal, including an appointments strategy and ongoing training program;
- Continuing Professional Education for directors is increasingly accepted as good practice. The Reserve Bank might consider setting an expectation of a certain number of formal CPE hours each year for bank directors, split between bank-specific and other topics.[12]
- Require that boards conduct regular formal assessments of actual skills and experience, and individual as well as collective performance. To avoid assessment fatigue an alternating cycle of evaluating the 'whole of board' and board leadership in year 1, followed by individual director evaluations in year 2, seems to work in practice.

- We generally support the Reserve Bank's 'no objection' approach and do not recommend moving to a formal 'approval' process, which could create a moral hazard for the Reserve Bank, by removing the full responsibility for bank board appointments from a Registered Bank and transferring it at least in part (and perception) to the regulator. We nonetheless also recommend that Bank self-review the effectiveness of its current 'no objection' approach to director appointments (see following bullet).

- It should, however, be expected that over time the acceptable 'fit and proper' benchmark for director skills and competence will rise. The Reserve Bank's current approach to the 'fit and proper person' test for a new director (or designated senior bank officer) is to confirm 'no objection' when he/she is first nominated, but not to monitor or re-assess whether the director continues to satisfy the test ('set and forget'). The Reserve Bank may wish to consider periodic re-validation at, say, intervals of no longer than three-years.

2.8 Attestation architecture

<u>Areas of focus:</u>

- How directors "benchmark" (or "interpret") each matter that they are attesting to, in the absence of published standards.
- Whether the benchmarking by the directors aligns with the Reserve Bank's understanding on what the directors are attesting to.
- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.

[11] http://www.bankofengland.co.uk/pra/Documents/authorisations/smr/prasmrinternal.pdf
[12] For comparison, the Institute of Directors in New Zealand requires 'Chartered Directors' to complete a rolling 60 hours of CPE over a three-year period (i.e. 20 hours per year on average).

A number of interviewees reflected that the disclosure regime and particularly the conditions of registration have become somewhat difficult to navigate and understand. This is somewhat inevitable given the passage of time since the regime was first introduced and the significant amount of regulatory change in the interim, including significant changes globally to prudential capital rules, liquidity rules and the introduction of macro prudential tools.

Two characteristics of the current regime were called out in particular: the expanding list of conditions of registration which have become simply that - a list, added to each time a new condition is imposed; the often highly technical and in some cases complex nature of the guidance – the prudential capital rules being a case in point. Both do not make it easy for directors to gain a deeper appreciation of the substance of the conditions and their complementary nature. This can in turn undermine their ability to challenge management beyond a seriatim approach to each condition.

This is more than simply a presentation and expression challenge. Better articulation extends to explaining how the component parts of the regime fit together as a complementary whole

Recommendation

- The Reserve Bank consider, in conjunction with the above recommendations (in particular: 2.3, 2.4 and 2.6), providing explanatory guidance as to how the component parts of the attestation regime fit together as a framework (from the regulator's perspective) and in particular how prospective regulatory developments will be catered for and factored into the framework e.g. the current consultation on *Serviceability Restrictions as a Potential Macro prudential Tool in New Zealand*[13]. A potential framework could be that embodied in CPS220 (See 2.4 *Attestation – Design and execution*).

2.9 Data and analytics

Areas of focus:

- How directors "benchmark" (or "interpret") each matter that they are attesting to, in the absence of published standards.
- Whether the benchmarking by the directors aligns with the Reserve Bank's understanding on what the directors are attesting to.
- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.

A common theme through virtually all interviews was a recognition by interviewees (directors and management) of the need for demonstrable evidence to support their assertions - the 'Trust but verify' axiom. This aligns with the 'due enquiry' onus on directors (and in turn management) when attesting and consequent increasing trend noted through the Review toward a 'reasonable assurance' approach premised on good evidence. A number of banks, large and small cited that this approach was no different from how they approached acquisition due diligence and prospectus issuance.

While quality evidence was recognised as essential in supporting attestations there were varying views on how well the banks felt they were identifying, capturing, recording, communication and archiving this evidence. Sub-themes that emerged in this regard included:

[13] http://www.rbnz.govt.nz/-/media/ReserveBank/Files/Publications/Policy-development/Banks/DTI/Consultation-paper-DTIs-June-2017.pdf

- Banks (mainly the larger ones) maintaining electronic risk and compliance applications to capture, store and report (controls) evidence. These appeared to be operational risk data bases bringing together controls and incident data;
- An acknowledgement that data quality and data management generally needed to further continued improvement. This was a key focus particularly for the larger banks and driven in the first instance by the advent of IFRS9 as well as commercial imperatives (customer intelligence);
- References to the increasing flow of bank proprietary data directly to the Reserve Bank, particularly in relation to the 'dashboard initiative'.
- Banks' plans (mainly the larger ones) within 5 years to make increasing use of data and analytics beyond credit (scoring / rating) to support unbiased decision making, and automate aspects of auditing e.g. controls testing.

Recommendation

The Reserve Bank make increasing use of data analytics to corroborate bank attestations. While this is done at present (largely a manual process we understand), there are increasing opportunities to do so using advanced tools. This should extend to linking bank supplied proprietary data (e.g. via the 'dashboard initiative' or other online information / data requests) with attestations, and communicating to the banks that this is occurring - as part of ensuring attestation regime alignment and integrity across information and communication channels.

Such an approach could also serve as a 'half-way-house' solution, avoiding expensive on-site examinations and opening up fresh opportunities for efficient and effective supervision through electronic tools.

2.10 Residual Regime vulnerabilities

Areas of focus:

- How directors obtain the necessary level of comfort they need to be able to attest that a bank's conditions of registration are being met, and that the bank has adequate risk management processes in place.
- Examples of directors challenging (and potentially changing) the conclusions reached by management in respect of compliance with matters that are attested to.

Interviewees were asked if and where they thought that the current attestation regime had vulnerabilities that might be exposed in time and which in hindsight could and should have been avoided. Our line of enquiry here was to probe the operational resilience of the regime with a forward-looking view.

In order to better countenance the possibility of regime failure a mental 'reverse stress test' was framed where interviewees were asked to countenance that the regime had 'failed' and to share their thoughts on where and why the failures might have occurred.

The responses included a range of 'event risks' that the regime was not considered well suited to either detecting, either because of their potential 'surprise' / 'speed of onset', or dealing with when immediately presenting. These risks, all of which could result in significant reputation damage for the target, with potential contagion effects, included e.g. cyber risk, conduct risk.

There was another category of risks characterised by their secular nature ('secular risks') that might not be identified sufficiently early by either management or the regulators e.g. progressive risk appetite 'creep', complacency.

Recommendation

The Reserve Bank itself explicitly challenge the directors' attestation regime as a prudential tool to identify and form its own view on where residual vulnerabilities lie and whether any further mitigating measures need to be taken having regard to it full suite of regulatory tools.

2.11 Supervisory engagement

Areas of focus:

- How might the regulator form a view of its engagement effectiveness and the extent to which any changes might in turn enhance the effectiveness of the directors; attestation regime?

Related IMF findings:

B29. The overall framework for prudential regulation is well-developed, though there is scope to extend the powers of the RBNZ and develop enforcement practices.

………Supervisory engagement, particularly with large institutions, needs to move towards communicating supervisory expectations and requiring action.

B31. Initiating on-site programs to test the foundation of the three-pillar approach and directors' attestations.

……..The onsite activity, which could be undertaken by the staff of RBNZ or by external experts, should be targeted to areas of high risk, to issues identified through off-site analysis, or to determine how banks and insurers are managing new risks and products. It is also important to test the accuracy of the regulatory reports.

B30. While RBNZ staff are highly competent, insufficient resources are an impediment to enhancing the effectiveness of the three pillar approach, even if the low-intensity approach is retained.

The competence and professionalism of staff is recognized by market participants, but the RBNZ operates under specific resource constraints and numbers are insufficient. Strengthening the regulatory discipline pillar will require increased resources, including technical capacity to develop prudential requirements and guidelines, deepen the analysis that supports the supervisory ratings, and to develop a supervision policy that reflects a balance between risk and efficiency costs of supervision………

A significant number of interviewees at various times ventured that they would like more frequent and constructive engagement and interaction with the Reserve Bank beyond what is currently in place, including:

- Opportunities to discuss 'best practices', particularly in relation to the risk related matters in the attestation and to benchmark themselves accordingly. This is particularly the case with the smaller banks that are not able to leverage off the experiences of a parent operating across jurisdictions and in larger markets;
- Some banks indicated that they would not be averse to thematic (cross-sector) 'deep-dives' being undertaken at the instance of the Reserve Bank by their external auditors, similar to those undertaken by APRA. The benefits were again seen as an opportunity to benchmark themselves;
- In a number of instances banks ventured that in areas where regulatory definition and / or measurement have proven to vary widely across the sector, that workshops convened by the Reserve Bank e.g. between CROs, could assist in developing a greater shared understanding of what was intended by the regulations and how to achieve it. This is not in lieu of the initial regulatory consultation process but a recognition that

once 'in use' practical issues can and do emerge and this would be a practical way of dealing with such matters. Examples of these issues were cited by the Banks (See *2.6 Regulatory Interpretation* – above).

Recommendation.

We are in principle supportive of the above suggestions, including the Reserve Bank sharing identified examples of Attestation Best Practice and we do not believe that they need create any moral hazard for the Reserve Bank if undertaken:

- Within a well thought through framework of protocols which are in turn an integral part of the broader attestation framework (See *2.8 Attestation Architecture* – above);
- With an engagement style and culture that recognises the many shared interests of boards and the Reserve Bank – in particular: trust, openness, and avoidance of surprises. We see this engagement style as being well articulated in both intent and execution in the G30 Report: *A New Paradigm. Financial Institution Boards and Supervisors.*

Heightened engagement as suggested above clearly has ramifications for the Reserve Bank's own resources (as do many of the other recommendations above) including:

- The Reserve Bank having sufficient staff with the appropriate skills to be able to engage effectively, particularly in areas that require deep technical expertise (e.g. credit and market risk measurement and models);
- Supervisory staff who are able to adjust their style to suit the compliance risk[14] posed by individual banks and the behaviours the Reserve Bank is seeking to induce and maintain in the interests of a robust and sustainable attestation regime (Refer also *2.1 Director Responsibility* – above).

[14] Refer also the Braithwaite 'triangle' - commonly used approach (Ayres and Braithwaite, 1992).

Part B – Best practices

3.1 Criteria applied

Our assessment was carried out using (7) criteria that in combination underpin attestation 'effectiveness' and a combination of primary information and data gathering tools (anonymous survey, bank supplied documentation and interviews with bank directors and senior executives.

Our summary assessment in the Executive Summary is based on these criteria, applied at an individual bank level (in Part C), and the key themes (in Part A) that emerged from the interviews with the 11 banks.

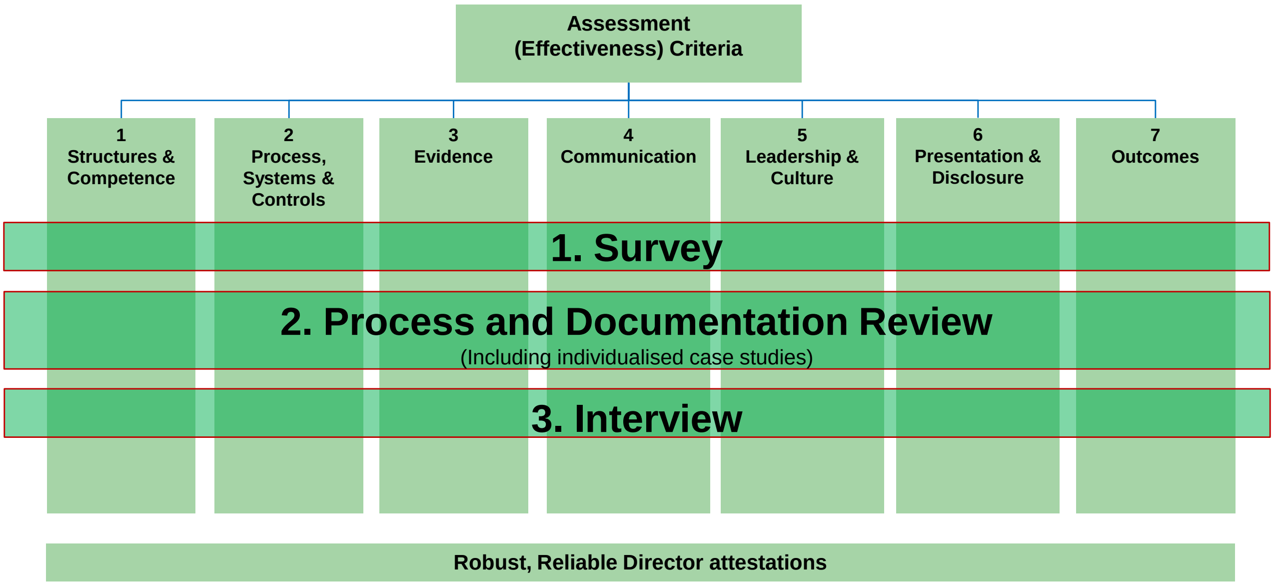


Figure 1: Effectiveness Criteria and Assessment Tools

For each criteria we detailed a series of 'best practice' features (considered relevant to the New Zealand directors' attestation regime and our Review mandate) drawing on recognised principles and practices from a range of authoritative sources including: Basel Committee on Banking Supervision, Generally Accepted (Professional) Standards – covering financial reporting, audit and control, among others.

Assessment ('Effectiveness) Criteria	Best Practice Features
1. Structures & Competence	• Clear roles and responsibilities that separate governance and management. The roles and responsibilities of each party, including board (incl. committees), management (incl. committees), staff, and other parties (e.g. advisers) are clearly defined in the context of and as they relate to the directors' attestations. Clear roles and responsibilities make the differing interests transparent and foster effective decision-making. • The framework should also cover how the board will be accountable for future-focused decisions, such as maintaining and enhancing the capability of the bank in all areas

Assessment ('Effectiveness) Criteria	Best Practice Features
	covered by the directors' attestations including the attestation framework and processes itself. • Clear line of authority and responsibility; effective 'span of control' and direct communication lines. Independent assurance 'hard-wired'; appropriate (risk-proportionate) investments in capacity and capability (systems, processes and people). • Getting the best from Audit and Risk Committees – including regular interaction between committees (board and management committees) and between committees and management as well as between audit committees and their external auditors (to highlight issues and bring a different perspective).
2. Process, Systems & Controls	• A good attestation process (and supporting processes e.g. risk management etc.) is: Complete (end-to-end), relevant, effective, efficient, valid, usable, used, managed and measured. • Ensure good process, information, systems, and controls - Directors are fully and individually accountable for the attestations they make. Therefore, they need relevant, accurate, and up-to-date information to make good decisions. The board also has a responsibility to form their own view on the design and effectiveness of the bank's internal systems and controls, particularly as they relate to the directors' attestations. These systems and controls are critical to providing assurance that the bank is compliant and in line with regulatory expectations. The board has a role to review them regularly to ensure that they remain fit for purpose.
3. Evidence	Quality of the attestation evidence i.e. its *relevance, reliability, accuracy / integrity, completeness, timeliness, adaptability:* • *Relevance* – The relevance of the evidence refers to the relationship to the (management) assertions made and the resulting (directors') attestations and to the objectives of the underlying controls being tested. • *Reliability* – Depends on the nature and source of the evidence and the circumstances under which it is obtained. E.g. Evidence obtained from a knowledgeable source independent of the bank is more reliable than evidence obtained only from internal bank sources; Reliability of information generated internally is increased when the bank's control over that information are effective. • *Accuracy and Integrity* – Bank's ability to generate accurate and reliable risk (and financial) data to meet normal and stress/crisis reporting requirements. Data aggregation should be largely automated so as to minimise the probability of errors. • *Completeness* – Bank's ability to capture and aggregate all material risk (and financial) data across the banking group. Data should be available by business line, legal entity, asset type, industry, region and other groupings, as relevant for the risk in question, that permit identifying and reporting risk exposures, concentrations and emerging risks. • *Timeliness* – Bank's ability to generate aggregate and up-to-date risk (and financial) data in a timely manner while also meeting the principles relating to accuracy and integrity, completeness and adaptability. The precise timing will depend upon the nature and potential volatility of the risk being measured as well as its criticality to the overall risk profile of the bank. The precise timing will also depend on the bank-specific frequency requirements for risk management reporting, under both normal and stress/crisis situations, set based on the characteristics and overall risk profile of the bank. • *Adaptability* – Bank's ability to generate aggregate risk (and financial) data to meet a broad range of on-demand, ad hoc risk management reporting requests, including requests during stress/crisis situations, requests due to changing internal needs and requests to meet supervisory queries.

Assessment ('Effectiveness) Criteria	Best Practice Features
4. Communication & Reporting	• Involving the Right people – For governance (and) management to be effective, it is critical that the right people are involved. The level of trust between people – between directors, management, and stakeholders – affects the effectiveness of the governance arrangements and resulting attestations. • Having the right mix of people and skills on the board should help it to be more effective. An effective board will have members who bring multiple perspectives, who debate issues robustly, constructively challenge and who then speak with unity of voice and message about the decisions made. • Appropriate induction and training – investment in and development of directors is vital including new directors receiving a formal induction into the bank and in relation to the attestation regime, its objectives and processes etc. • Effective relationships built on mutual trust and respect - Strong relationships between directors and management are essential. These relationships should be based on mutual respect and trust. However, they should not become 'cosy'. • All attestation related communications are effective – i.e. they are: complete, concise, considerate (of end-users and their objectives), concrete (supported by evidence – see above), clear and correct. Communications lines are clear and direct.
5. Leadership & Culture	• Clear strategic purpose (for governance generally and attestations in particular) and a clear direction for how to achieve that purpose based on an understanding of regulator expectations and the wider regulatory context that the bank operates in. Clarity of vision and objectives (as they relate to directors' attestations). • Strong united leadership at Board and executive levels in particular (right 'tone at the top'); strong employee engagement and positive, open culture. • Lead by setting a constructive tone. The leadership role is to set a suitable tone from the top that shapes the culture and demonstrates the desired values and ethics of the organisation. • Powerful questioning. The Board's questioning of management needs to be constructive and testing. Effective Boards use their combined experience and skills to query information, to probe, and to challenge so they can make informed decisions. Boards need to keep asking questions until they understand what they are being asked to rely on. Sometimes decisions need to be deferred until further information is supplied. • Directors and executive management are aware of and alert to organisational biases (cognitive, emotional and deeply embedded belief systems) and their impact on decision-making. They consciously use a range of de-biasing approaches based upon the type and frequency of the decisions that are being de-biased e.g. analytical tools (credit scoring models).
6. Presentation & Disclosure	Quality of attestation related reporting and disclosure: • *Accuracy* - Risk management and financial reports accurately and precisely convey aggregated risk and financial data. Reports are reconciled and validated. Financial reporting – High quality financial reporting in compliance with generally accepted accounting practice (GAAP). • *Comprehensiveness* - Risk and financial reports should cover all significant attestation related matters. The depth and scope of the reports is consistent with the size and complexity of the bank's operations and risk profile, as well as the bank's specific attestation requirements (incl. conditions of registration). All components that should be included in the disclosure statement are so included, and are properly organised, described and disclosed. • *Clarity and usefulness* – Attestation related risk and financial reports communicate information in a clear and concise manner directly relevant to the directors' attestations. Reports are easy to understand yet comprehensive enough to facilitate informed decision-making by management and the directors.

Assessment ('Effectiveness) Criteria	Best Practice Features
	• Internal verification processes and assurance reviews are in place for attestation related reports, whether internally generated or from third parties. • *Frequency* – The frequency of management and board reports reflects the needs of management and directors in meeting their respective attestation related reporting obligations. • *Distribution* – attestation related reports are distributed to the relevant parties while ensuring confidentiality is maintained.
7. Outcomes (future-focused)	• The objectives and purpose of the attestation regime are well understood • The results are not seen as discrete outputs from a single attestation but rather as results collectively, through time and viewed through the lens of the ultimate stakeholders and beneficiaries. • The results anticipate / discount future needs and respond to these mindful of those needs. • Directors' proactively adapt their governance approach, structures and processes to support changing needs generally mindful of the specific requirements in relation to their director attestations; These are adapted for the specific situations and needs of the bank; one size does not fit all. • From governance to stewardship – future-focused boards are focused not only on the current regulatory context but also evolving trends and expectations and able to relate these back to the present and in so doing 'set a higher bar' for regulatory compliance that transcends the boundaries of their own bank. • Emerging trends and risks are understood, tracked and their implications (effectively) discounted into current attestations

3.2 Maturity framework

Using information gathered through the online survey, individual bank interviews and bank-supplied documentation we have assessed each of the (11) banks against a maturity model developed for the attestation regime[15] and covering the 7 domains outlined above which are also the criteria by which we have assessed the 'effectiveness' of the regime both at the level of individual banks and also in aggregate at a 'system' level.

Five (5) levels of capability apply to each of the (7) domains:

L1 – Initial
L2 – Repeatable
L3 – Defined & Integrated
L4 – Managed
L5 - Optimising

[15] Drawing on good practices in Maturity Models from a variety of sources – see Bibliography

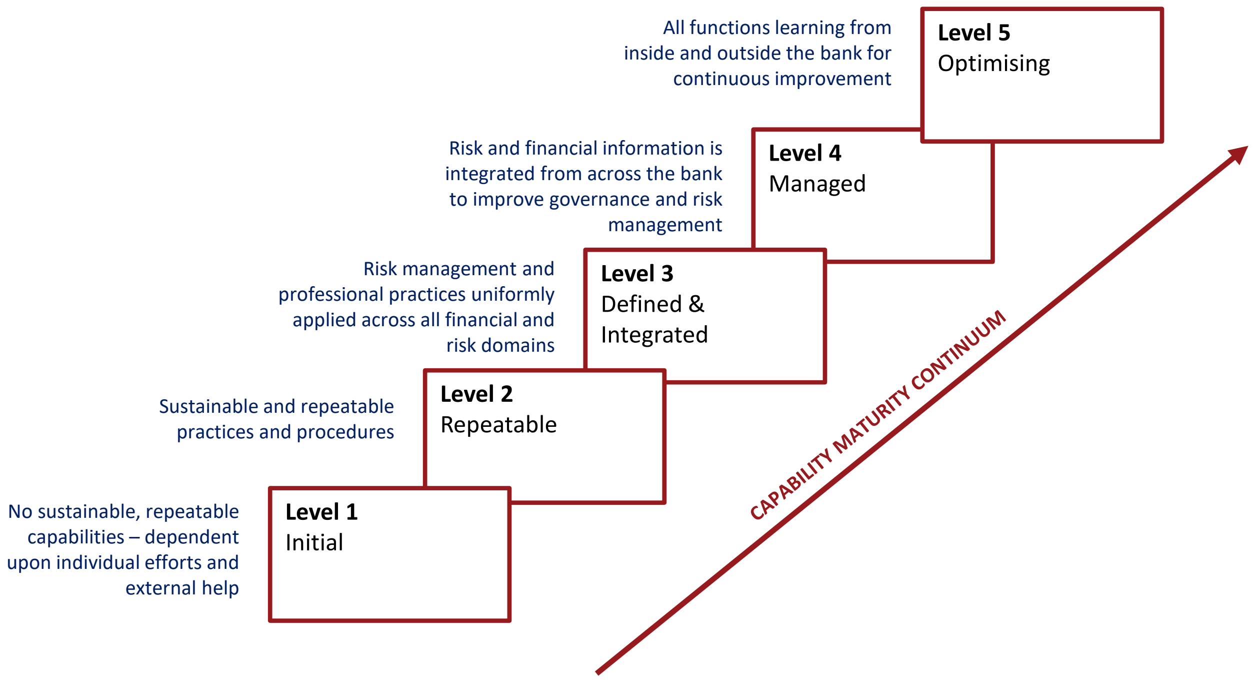


Figure 2: Capability Maturity Model

For each of the 5 levels of maturity we detail the evidence we would expect to see to support performance at that level for the criteria concerned.

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
1. Structures & Competence	• There is no formal governance structure or policies in place to direct and support the Directors' attestations. • Skills and competencies do not match attestation needs and are not formally assessed against a robust (needs) framework either at the Board level or across management. Training programs not defined	• A formal governance structure is in place to support director attestations; however, individual roles and responsibilities for managing the associated risks and regulatory obligations are not explicitly assigned to senior business leaders / managers. • There is limited evidence of risk and compliance focussed discussions and challenge taking place at senior management team meetings and at the Board. • Some specialised technical skills and credentials; Skills and competencies are assessed for /	• A formal governance structure is in place to support director attestations including clear assignment of individual responsibilities for managing the associated risks and regulatory obligations at all levels. • There is good evidence of risk focussed discussions and challenge taking place within the board and across management including in the respective committees. • Appropriate skills and credentials in place. Skills and competencies are	• Director attestations and 'attestation risk' are framed distinctly within the governance structure and drive governance, risk and compliance strategies and initiatives down within the bank • There are mechanisms in place for encouraging appropriate business unit involvement in Board attestation related discussions and debate and reciprocal sharing of Board insights (e.g. via 'deep-dives'). • All resources have appropriate skills and credentials. SMEs are identified and used. Skills and	• The scope of director attestations and governance structure extends beyond the bank providing stewardship and oversight / foresight of system level risks in support of sector-good outcomes. • Board / management interaction and challenge on attestations occurs systematically through and between board and management committees. • All resources have appropriate skills and credentials, with robust succession planning in place. Skills and competencies are

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
		within functional roles as part of performance appraisals (incl. self-evaluation). Training and development are ad hoc.	assessed at least annually for / within functional roles and at an aggregate (portfolio) level. Training requirements documented and executed	competencies are assessed as composites / clusters and directly related to performance in managing 'attestation risk'. Training is systematic, targeted and bank-wide.	dynamically assessed in the context of performance using both technical and non-technical components, including behavioural insights. Training is individualised (need-based), self-directed (professional development), future-focused and ongoing.

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
2. Process, Systems & Controls	• Attestation methodology and processes are not defined or in place. • High reliance on manual systems and spreadsheets; critical information not readily available	• Uniform attestation methodology and processes are defined and in place but may not be documented. • Partially effective systems are in place; low reliance on data and information generated from systems • Basic risk management frameworks and disclosure policies and procedures in place that have been approved by the Board. • Application of the risk management policies and procedures are varied across business units.	• There is an attestation framework in place, including policy and procedures uniformly applied across all business units (form). • Stable systems in place; information generated is reliable and relied upon. • Risk management frameworks and disclosure policies and procedures are applied consistently and uniformly across the bank.	• The attestation framework includes a chronology of all past attestations, issues raised, judgments exercised and lessons learned (institutional memory) to guide future improvement. • System integrity is high; automated reports are in use and reliable; key data is monitored continuously. • Risk management frameworks and disclosure policies and procedures cater explicitly for the needs and requirements of directors' attestations, are well integrated and applied uniformly across the bank.	• The attestation framework captures the substance of director attestations (is well codified) with explicit examples of good / leading practices to encourage continued improvement. • Extensive use of systems, data mining and analytics; continuous audit and monitoring processes in place driving value • There is continuous monitoring and updating of risk management frameworks and the attestation methodology for necessary changes and emerging leading practices.

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
3. **Evidence** (includes all relevant information and data supporting attestation)	• Attestation relies significantly or exclusively on management representations unsupported by any hard evidence. • There are no governance arrangements in place covering information or data.	• Attestation is accompanied by some hard evidence. Evidence is patchy / partial, subject to availability and selectively provided. • Evidence and data managed informally.	• Attestation is underpinned by a policy requirement for supporting evidence although process and systems limit full application. • Evidence / data are managed in accordance with formal policies and procedures	• Attestation is supported by comprehensive evidence. Systems and processes are designed and operated to provide the required evidence in line with best practice principles. • Evidence / data viewed and managed as a strategic asset	• Attestation is supported by comprehensive evidence (sourced internally and externally), viewed through and corroborated by multiple lenses using advanced tools and analytics. • Formal 'data governance' arrangements are in place and augment / complement the work of management (data architecture and IT infrastructure supporting data aggregation capabilities and risk reporting practices under a wide range of conditions).

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
4. **Communication & Reporting**	• Attestation communication and reporting done on an ad hoc basis; no validation of results or focus on quality. • Board / CE dialogue • Board management dialogue	• Attestation communication and reporting processes are defined and in place but may not be documented.	• Attestation communication and reporting processes are defined, in place, and documented; effective use of reporting structures and formats aligned with attestation objectives. • Communication and reports largely based on 'spot' information and hindsight views.	• Attestation communication and reporting highly effective; quality and timeliness metrics comprehensively defined and monitored. • Communication and reports have a forward view focused on extrapolating existing trends.	• Attestation communication and reporting highly effective; high level of quality demonstrated in timely reports at all levels. • Communication and reports are forward-looking and actively canvass emerging trends and risks under various (stress) scenarios.

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
5. Leadership & Culture (See also '7. Outcomes' – below**)**	• There is no clear link between the bank's organisational values and behaviours and governance, risk and compliance practices. • There is a covert approach to breach disclosure. • There is no or limited evidence that the board, management or staff are encouraged to improve their governance, risk management or compliance performance. • Largely confrontational and or 'Defensive' posture with the regulator.	• Well informed governance, risk and compliance practices are implied through the bank's organisational values and behaviours. • Breach disclosures are selective / partial and delayed. • There is some evidence of conscious initiatives by the board, management or staff to improve their governance, risk management and compliance performance • Largely guarded engagement with the regulator (infrequent).	• The bank's organisational values and behaviours explicitly and clearly support its governance, risk and compliance practices. • Proactive breach disclosure is encouraged, internally and to the regulator. • There is good evidence of initiatives by the board, management or staff to improve their governance, risk management and compliance performance. • Largely formal engagement with the regulator (frequent).	• The bank's organisational values and behaviours are partially integrated into all its governance, risk and compliance practices. The right behaviours are actively encouraged, supported and incentivised. • There is an open and transparent approach to breach disclosure from discovery. • There is consistent evidence of ongoing initiatives by the board, management or staff to improve their governance, risk management and compliance performance. • Largely open engagement with the regulator (frequent).	• The bank's organisational values and behaviours are fully integrated into all its governance, risk and compliance practices. The right behaviours are consistently and proactively encouraged, supported and incentivised. • Breach disclosure is open, transparent and continuous as breaches are detected • Innovative governance, risk and compliance ideas and techniques are piloted on an ongoing basis and shared with strategic partners. • Highly constructive, engaged and mutually respectful (ongoing) dialogue with the regulator.

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
6. Presentation & Disclosure (post Board approvals)	• The attestation disclosures are largely procedural and minimalist (following regulatory prescribed format/s only). • Financial (disclosure) and non-financial components are distinctly separate in presentation. • Processes to publish the disclosures are largely 'manual' with little additional integrity validation post board approval	• The attestation disclosures involve succinct supplementary information to facilitate better understanding of the substance of the attestations e.g. circumstances and drivers behind CoR breaches, materiality / relativity Etc. • Attempts are made to better link financial (disclosure) and non-financial components in presentation. • Processes to publish the disclosures are largely 'manual' but additional steps are taken to validate	• The attestation disclosures are well integrated between financial and non-financial information. There is a clear and logical framework to assist the reader link, navigate and understand the related attestation components. • Processes to publish the disclosures involve some automation including integrity validation.	• The attestation disclosures are largely procedural and minimalist (following regulatory prescribed format/s only). • Financial (disclosure) and non-financial components are distinctly separate in presentation. • Processes to publish the disclosures are largely 'automated'	• The Board provides additional disclosures about how it evaluates itself in relation to its governance performance, including its attestations, identifies areas for improvement and addresses them to provide stakeholders with a window into how robust the board's process is for introducing change. • Processes to publish the disclosures are highly automated with additional automated checks to validate data

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
		integrity until the point of disclosure.			integrity until publishing.

Criteria	L1 Initial	L2 Repeatable	L3 Defined & Integrated	L4 Managed	L5 Optimising
7. Outcomes (future-focused)	• There is no or limited evidence of learning from 'risk events' including past attestation related incidents. • Majority of breaches that have occurred are regulator detected.	• There is some evidence of learning from negative 'risk events' that have affected the bank.	• There is good evidence of learning from negative and positive risk events that have affected the bank as well as the experiences of other banks.	• There is very good evidence of learning from risk events, both positive and negative, that directly or indirectly affect the bank.	• There is a systematic approach to learning from past risk events, which are also shared openly across the bank and with strategic partners. • The majority of breaches are self-detected / disclosed by the bank.

Part C – Individual banks

Our assessment for each of the (11[16]) banks is covered in a separate companion report to this (main report).

We followed a 'sifting' process, calling out key observations (direct quotations) made by interviewees, corroborating this, where applicable (and possible) with the documentation supplied[17] by the bank concerned, and then summarising the main features and evidence to support our assessment.

By its nature this cannot be a precise process and while we have endeavoured to map with some precision the evidence gathered to the 'effectiveness' criteria applied, there will inevitably be gaps and differences of judgement and opinion given the idiosyncrasies of each bank situation (summarised in introductory 'high-level context' observations for each of the banks).

The intention is that this information assist the Reserve Bank in the following ways:

1. As basis for individualised feedback to the banks concerned;
2. For use selectively and at an aggregate level to further inform the Reserve Bank's supervisory strategic for individual banks and the sector as a whole;
3. For further hypothesis testing on the basis of Survey feedback and the Reserve Bank's own views and information available on individual banks. In this regard we have not attempted to undertake any hypothesis testing, mindful of the pitfalls in inferring on the basis of the Review information only e.g. the relationship between small vs large banks and attestation maturity; and.
4. As basis for determining how best to advance individual and collective bank (sector) governance capabilities up the maturity continuum[18] using a combination of appropriate positive incentives, sanctions and regulatory *'surprise'*[19]

[16] For logistical reasons only 11 of the 15 surveyed banks (See Part D.) were involved in the interviews.
[17] Under the Section 93 request.
[18] As represented in the stylised maturity model used in this report, recognising the evolutionary nature of best practice and therefore non-static nature of the model.
[19] Consistent with techniques associated with monetary policy: https://www.wsj.com/articles/why-the-fed-should-surprise-us-more-1498233889, while mindful of unintended consequences.

Part D – Survey

This section provides both summary and detailed information from the anonymous survey undertaken at the outset of the Review.

The survey was undertaken during April 2017. Participation rates were high at 89.1% in aggregate. The highlights and key insights are summarised below with further detail in the appendices.

Insights drawn from the survey responses were used to inform discussions with banks during the interview stage of the Review and have been cross-referenced where appropriate to the Key Theme findings in Part A, above).

5.1 Survey participation

Bank Group	Responses	Total Population	% Response Rate by Group
1. ANZ, ASB, BNZ, Kiwibank, Rabobank, WNZL	44	50	88%
2. Co-operative Bank; Heartland Bank; SBS, TSB	29	32	91%
3. Bank of Baroda, Bank of China, Bank of India, CCB, ICBC	25	28	89%
Total	**98**	**110**	**89.1%**

5.2 Survey insights

1. Overall, the survey responses indicate support for the directors' attestation regime, with a high proportion of directors largely agreeing with positive statements. For example, all respondents largely agreed that they fully understand that what they were attesting to is what is required and expected by the Reserve Bank, and 99% responded that they have not signed an attestation collectively while having their own reservations. Refer also:
    - Part A – *2.1 Director Responsibility*
    - Appendix 1 – *Detailed Survey Responses*

2. While the responses were generally very positive, it is evident that Group 2 respondents consistently responded less favourably compared to the other groups, especially in the 'Evaluation' and 'Opinion' survey questions (The differences were statistically significant).
3. The questions with the highest proportion of 'disagreement' (or responses of "Partially disagree" or lower) and added comments, are listed below:
    - *E15: Our Board relies significantly on its subcommittees for detailed evaluation of the attestation information, results and process.*
    - *E16: Our Board relies significantly on the external auditor in respect of the financial statement disclosure aspects of the directors' attestations.*
    - *E17: Our Board relies significantly on any "non-objections" or "approvals" issued by the Reserve Bank of New Zealand.*
    - *E18: As part of our Board evaluation process, we formally evaluate our Board's performance in respect of the attestations we make.*

- *O1: Our Board arrives at its collective view of the final form and content of each attestation based upon the formal consent of each Board member rather than consensus.*

- Refer also:
  - Paragraphs 4-7 below for further explanation.

4. The negative responses for questions E15-E17 are pleasing as they support appropriate practices for boards (i.e. the boards do not rely significantly on any "non-objections" or "approvals" from the Reserve Bank). However, reviewing the comments for those questions suggested that some respondents, particularly from Group 2, interpreted the questions as total reliance on external parties, with the Board having no due diligence procedures, and this should be further questioned during the interview process. For E15 and E17, the proportion of 'Largely Agree or higher' responses were significantly higher for Group 3 compared to Groups 1 and 2. One possible hypothesis is that Tier 3 banks are more reliant on subcommittees and Reserve Bank guidance, given their relatively less mature governance and prior experience in the New Zealand regulatory environment.

5. The question on formal evaluation of the Board's performance in respect of attestations (E18) also had a high proportion of 'Not Applicable' responses (14% total, 23% for Group 1, 7% for Group 2, and 68% for Group 3). The comments for E18 indicate that performance regarding attestations is not usually included as a specific component of the formal Board evaluation. The comments also suggest that the large proportion of "Not Applicable" responses, particularly among Group 3, is mostly due to the short tenure of some directors. Many respondents have not been on the board long enough to participate in the formal evaluation process.

6. A relatively high proportion of Group 2 (14%) and Group 3 (12%) disagreed with the statement that the Board arrives at its collective view based on the formal consent of each Board member rather than consensus (O1), while none of Group 1 directors disagreed with this statement. Upon review of the comments, it appears that at least one of the Group 2 or 3 banks currently reach a consensus view as opposed to an individual position. The comments, however, indicate that there is a lot of discussion and debate that occur prior to each director giving their formal consent.

7. Aside from E18, the other question with a high proportion of 'Not Applicable' responses is:
   - *O2: My attest conclusions and opinions on occasion differ from those of my Board colleagues and are resolved through convincing discussion and evidence.*

   Upon review of the comments for O2, it appears that the directors have ticked 'Not Applicable' to mean that situations where their own conclusions and opinions differed from their Board colleagues have not occurred. This in itself may point to an undesirable situation in which group bias might at times be present.

8. Only 1% of directors disagreed with the statement "*I have never had cause to withhold my support for any final attestation by our Board"*. One director commented that this situation occurred only once in his 9-year tenure, while another director commented that he/she has withheld support in the past until certain matters were clarified to his/ her satisfaction.

9. A test for statistical significance[20] of the spread of responses for each of the (3) groups / sets of questions (Comprehension, Evaluation, Opinion) was undertaken, using the following comparisons:
   a) Comprehension to Evaluation

[20] *The **chi-square goodness of fit** test is used to compare the observed distribution to an expected distribution, in a situation where we have two or more categories in a discrete data. In other words, it compares multiple observed proportions to expected probabilities. In the above analysis, one of the group's results was used as the benchmark to test another*

b) Comprehension to Opinion, and
c) Evaluation to Opinion

from "Analysis" tab in data sheet

		Combined					
S. Disagre	L. Disagre	P. Disagre	P. Agree	L. Agree	S. Agree		
0	0	2	10	103	272	387	Comp
6	19	15	154	546	993	1733	Eval
1	6	5	18	73	171	274	Opin
						2394	
7	25	22	182	722	1436	2394	
0.00%	0.00%	0.52%	2.58%	26.61%	70.28%	100.00%	Comp
0.35%	1.10%	0.87%	8.89%	31.51%	57.30%	100.00%	Eval
0.36%	2.19%	1.82%	6.57%	26.64%	62.41%	100.00%	Opin
0.29%	1.04%	0.92%	7.60%	30.16%	59.98%	100.00%	

For the first two comparisons the Chi-Square test result p-value was extremely small, suggesting there was a statistically significant difference in the spread of answers to each question group.

In the third comparison, the response spreads were found to be equivalent with no statistically significant difference.

In summary, the Comprehension group of questions seem different in some way in terms of response spreads to the other two groups. This could be an artefact of the survey design and as such would need addressing should the survey be run again, or, there could be a clear disconnect in directors interpretations between the groups of questions and as such this would be a valuable finding.

5.3 Analysis of comments

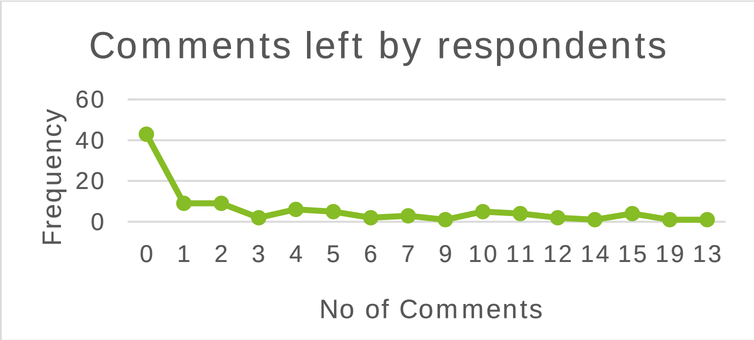
This section examines the distribution of comments left by respondents to understand:

- The number of respondents who commented, versus those who were silent; and
- Of those who commented, what are their characteristics?

Unless stated to the contrary, this analysis includes responses from “other comments” at the end of the survey, but excludes comments with a simple “no comments” answer.

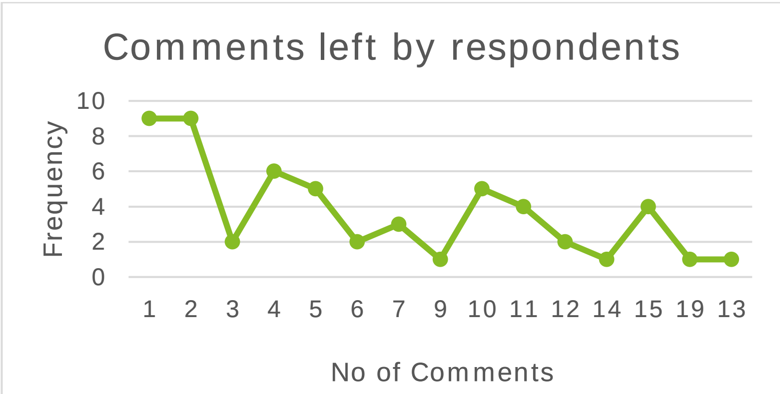
Respondents who commented

The distribution of comments is displayed below:



56% of respondents (55) have left at least one comment on the survey; in other words, 44% of respondents (43) have not left any comment.

Below shows the frequency of comments with zeroes removed:



Detailed analysis of comments by Bank Group / Tier and Respondent type showed the following:

<u>By Tier</u>

- Tier 1 respondents had the highest involvement with comments (most people left at least one comment), while Tier 2 has the lowest.
- In terms of average number of comments left by respondents (not accounting for silent respondents), Tier 2 commenters have provided the most comments; this is followed by Tier 1. Tier 3 commenters left the fewest comments.

<u>By Role</u>

- The Board has the highest proportion of commenters, although they also left the fewest comments on average. On the other hand, independent directors and non-executive directors left the most comments.

- Considerably fewer executive directors left a comment when compared with the other roles (noting that executive directors had the smallest sample at 12, which may exaggerate the differences expressed in percentage.)

Part E – Review approach

6.1 Overview

The Review approach with its emphasis on the 'effectiveness' of the disclosure regime, is underpinned by a 'best practice' framework for purposes of ensuring completeness and integrity of process, evidence gained, and practicable utility of results. The 'best practices' were sourced having particular regard to the Review terms of reference and included:

- International regulatory guidance from authoritative bodies, including the Reserve Bank;
- Special reports commissioned by, or at the instance of governments and / or regulatory authorities (the most relevant being those published as a consequence of, and in the wake of the global financial crisis);
- Professional standards – particularly in relation to assurance (e.g. ISAE NZ 3000)

6.2 Methodology

A combination of the three (3) primary methods was used to source the required information from each of the 'in scope' banks:

1. *Survey* – At the commencement of the Review an anonymised online survey was administered in two simultaneous tranches as follows:

    a. *Tranche 1*: To the Chairs and board members of all (15) locally incorporated New Zealand banks irrespective of whether the banks were subsequently involved in the interviews (see next); and

    b. *Tranche 2*: To the Chairs and board members of those (11) New Zealand banks selected for interview.

    The purpose of the survey was threefold:

    i. To set context for the review;
    ii. To allow directors to thoughtfully 'self-reflect' on, and respond to some key questions; and
    iii. To test a range of hypotheses using the survey responses (and in combination with subsequent interview feedback and bank documentation review).

2. *Documentation review* – A targeted selection of documents was requested from (11) banks under a Reserve Bank Section 93 request. The documents covered a range of topics directly related to the bank attestations (with attestations viewed as an 'end-to-end' process):

    a. Relevant Policies; Frameworks; Systems
    b. Committee Charters; Terms of Reference; Self and independent assessments
    c. Committee minutes (Board and management)
    d. Reports (Internal and external)

    The documentation review (circa 800 individual documents) was done in advance of the interviews with the respective banks and along with the general survey findings helped define the focus of the interviews. While bank specific case studies were originally intended to serve this purpose experience showed that the bank specific documentation was better suited to this purpose.

3. *Interview* – In excess of 70 interviews (each lasting an hour) were conducted with the following from each bank:

a. Chair
b. An independent director
c. A non-executive director
d. An ex-bank director (in selected instances)
e. Chief Executive
f. Chief Risk Officer
g. Chief Financial Officer
h. External auditor (signing partner)
i. Internal auditor (as applicable)

The interviews made use of insights and material gained from both the survey and documentation relevant to the bank. The interviews served as the primary means of articulating the key thematic findings, then corroborated / supported with reference back to a combination of survey responses and themes emerging from the documentation reviews.

Appendix 1: Detailed survey responses

The table on the following page summarises the detailed survey responses.

Detailed survey responses[21]

#	Question	Topic	Not Applicable				Partially disagree or lower				Partially Agree				Largely Agree or higher			
			Total	Group 1	Group 2	Group 3	Total	Group 1	Group 2	Group 3	Total	Group 1	Group 2	Group 3	Total	Group 1	Group 2	Group 3
C1	I fully understand and am able to clearly articulate what I am attesting to and the basis / criteria on which I arrived at my conclusions and opinions.	Comprehension	0%	0%	0%	0%	0%	0%	0%	0%	2%	2%	3%	0%	98%	98%	97%	100%
C2	I fully understand that what I am attesting to is what is required and expected by the Reserve Bank.	Comprehension	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	100%	100%	100%	100%
C3	My primary focus in our attestations is always on their regulatory substance (intent) as well as their legal form.	Comprehension	0%	0%	0%	0%	1%	2%	0%	0%	4%	5%	3%	4%	95%	93%	97%	96%
C4	Our Chair sets out clear expectations for our Board in order to ensure a robust and defensible attestation process and outcome.	Comprehension	5%	7%	3%	4%	1%	2%	0%	0%	4%	2%	7%	4%	90%	89%	90%	92%
	Comprehension Summary		**1%**	**2%**	**1%**	**1%**	**1%**	**1%**	**0%**	**0%**	**3%**	**2%**	**3%**	**2%**	**96%**	**95%**	**96%**	**97%**
			Total	**Group 1**	**Group 2**	**Group 3**	**Total**	**Group 1**	**Group 2**	**Group 3**	**Total**	**Group 1**	**Group 2**	**Group 3**	**Total**	**Group 1**	**Group 2**	**Group 3**
E1	My attest conclusions and opinions balance demonstrable evidence with judgement, with emphasis on the former.	Evaluation	0%	0%	0%	0%	1%	0%	0%	4%	4%	5%	3%	4%	95%	95%	97%	92%
E2	I am not aware of any instance when I've signed an attestation collectively with other Board members, while having my own reservations.	Evaluation	0%	0%	0%	0%	1%	0%	0%	4%	0%	0%	0%	0%	99%	100%	100%	96%
E3	I systematically evaluate and form a conclusion and opinion on each component within the overall attestation.	Evaluation	0%	0%	0%	0%	0%	0%	0%	0%	5%	0%	14%	4%	95%	100%	86%	96%
E4	I form my own (independent) attest conclusions and opinions before our Board forms its collective view.	Evaluation	0%	0%	0%	0%	0%	0%	0%	0%	4%	7%	3%	0%	96%	93%	97%	100%
E5	I am always presented with sufficient hard demonstrable evidence to support my attest conclusions and opinions.	Evaluation	1%	2%	0%	0%	0%	0%	0%	0%	3%	0%	3%	8%	96%	98%	97%	92%
E6	I fully understand the Board's policy, processes and procedures supporting the directors' attestation.	Evaluation	0%	0%	0%	0%	1%	0%	3%	0%	1%	2%	0%	0%	98%	98%	97%	100%
E7	I fully understand and rely on management's evaluation and processes and procedures that support the directors' attestation.	Evaluation	0%	0%	0%	0%	1%	0%	3%	0%	8%	7%	17%	0%	91%	93%	79%	100%
E8	Our Board is able to reference explicit criteria and standards (including materiality considerations where appropriate) as part of our attestation processes and methods.	Evaluation	0%	0%	0%	0%	1%	0%	3%	0%	3%	2%	3%	4%	96%	98%	93%	96%
E9	I make few assumptions in forming my attest conclusions and opinions as I always have enough hard evidence.	Evaluation	1%	2%	0%	0%	1%	0%	0%	4%	8%	9%	10%	4%	90%	89%	90%	92%
E10	There is always enough time allowed for rigorous discussion and challenge within our Board in relation to our regulatory attestations.	Evaluation	0%	0%	0%	0%	0%	0%	0%	0%	8%	5%	14%	8%	92%	95%	86%	92%
E11	Our Board is receptive to diverse opinion, rigorous challenge and alternative points of view in relation to the attestation process and outcomes.	Evaluation	0%	0%	0%	0%	1%	2%	0%	0%	3%	5%	3%	0%	96%	93%	97%	100%
E12	Our Board devotes sufficient time and mental energy on assessing the underlying assumptions that form the foundation for director attestations.	Evaluation	1%	2%	0%	0%	0%	0%	0%	0%	9%	5%	17%	8%	90%	93%	83%	92%
E13	Our Bank's risk and compliance frameworks and controls are completely 'fit for purpose' in supporting my attest conclusions and opinions.	Evaluation	0%	0%	0%	0%	0%	0%	0%	0%	5%	0%	10%	8%	95%	100%	90%	92%
E14	I am made aware of any evidence that comes to light prior to and/or subsequent to our Board's attestations that could call the integrity of our attestations and processes into question.	Evaluation	6%	5%	7%	8%	0%	0%	0%	0%	2%	0%	3%	4%	92%	95%	90%	88%
E15	Our Board relies significantly on its subcommittees for detailed evaluation of the attestation information, results and process.	Evaluation	1%	2%	0%	0%	4%	2%	10%	0%	13%	11%	21%	8%	82%	84%	69%	92%
E16	Our Board relies significantly on the external auditor in respect of the financial statement disclosure aspects of the directors' attestations.	Evaluation	2%	5%	0%	0%	9%	9%	14%	4%	33%	25%	45%	32%	56%	61%	41%	64%
E17	Our Board relies significantly on any "non-objections" or "approvals" issued by the Reserve Bank of New Zealand.	Evaluation	5%	5%	7%	4%	11%	16%	10%	4%	18%	18%	24%	12%	65%	61%	59%	80%
E18	As part of our Board evaluation process, we formally evaluate our Board's performance in respect of the attestations we make.	Evaluation	14%	23%	7%	68%	9%	5%	14%	12%	29%	30%	38%	16%	48%	43%	41%	4%
	Evaluation Summary		**2%**	**3%**	**1%**	**1%**	**2%**	**2%**	**3%**	**2%**	**9%**	**7%**	**13%**	**7%**	**87%**	**88%**	**83%**	**90%**
			Total	**Group 1**	**Group 2**	**Group 3**	**Total**	**Group 1**	**Group 2**	**Group 3**	**Total**	**Group 1**	**Group 2**	**Group 3**	**Total**	**Group 1**	**Group 2**	**Group 3**
O1	Our Board arrives at its collective view of the final form and content of each attestation based upon the formal consent of each Board member rather than consensus.	Opinion	1%	2%	0%	0%	7%	0%	14%	12%	6%	9%	3%	4%	86%	89%	83%	84%
O2	My attest conclusions and opinions on occasion differ from those of my Board colleagues and are resolved through convincing discussion and evidence.	Opinion	18%	20%	21%	12%	4%	5%	7%	0%	12%	14%	14%	8%	65%	61%	59%	80%
O3	I have never had cause to withhold my support for any final attestation by our Board.	Opinion	1%	2%	0%	0%	1%	0%	3%	0%	0%	0%	0%	0%	98%	98%	97%	100%
	Opinion Summary		**7%**	**8%**	**7%**	**4%**	**4%**	**2%**	**8%**	**4%**	**6%**	**8%**	**6%**	**4%**	**83%**	**83%**	**79%**	**88%**

[21] For each survey question, responses of either "Not Applicable" or "Partially disagree or lower" that represent 5-10% of total or bank Group responses are highlighted in yellow, while responses of either "Not Applicable" or "Partially disagree or lower" that represent more than 10% of total or bank Group responses are highlighted in red.

Appendix 2: Examples of survey comments

The following are examples of comments provided by the survey respondents:

- “Clear understanding of financial ratios and new LVR requirements, but other areas such as Open Bank Resolution, I find the reason for the attestation harder to understand.” [sic]

- “I generally agree with this statement *(“I systematically evaluate and form a conclusion and opinion on each component within the overall attestation”),* but am conscious that the size and frequency of a Disclosure Document fails to excite me. I am however confident and do my own checks, that it is the result a compilation of processes and monitoring and that it provides an accurate picture. I do tend to focus on what is not there, to ensure that full disclosure is made.”

- “Too often, unfortunately, I have to reach a conclusion on the basis of information provided by our auditors since there never seems enough time to go through the Disclosure Statement line by line.”

- “Too often, the Disclosure Statement reaches the board close to the deadline for submission to the Reserve Bank, leaving directors in the invidious position of having to agree to the substance of the Statement or run the risk of not submitting it to the Reserve Bank before the deadline.”

- “I had understood that the Reserve Bank required each individual director to sign the Disclosure Statements, as used to be the case. This clearly required each member of the board to signify their agreement with the attestations. Now that all directors are not required to individually sign the statements, the attestation process has tended to become a bit "looser". (Comment on survey question, “*Our Board arrives on its collective view based on formal consent of each Board member than consensus*”)

- “The number of points requiring attestation rises every year and the board function gets more and more complex. There is a danger that issues may fall through the cracks because of the shear [sic] number of requirements. I would strongly urge the Reserve Bank to review and simplify their requirements.”

- “I feel that the Reserve Bank has made the Directors roles and attestation process more difficult and believe that the Reserve Bank is an effective "Shadow Director" by virtue of its prescriptive approval of detailed matters and non-objections. The Reserve Bank is prescribing actions, models, technology that drive business and risk outcomes which drives conflict with Director Responsibilities.”

- “From a governance perspective, I would prefer the Reserve Bank to use more of the approvals side of the process rather than non-objections. Approvals provide more certainty.”

- “We have such a detailed process, and the culture of the board is strong, so we don't spend a lot of time specifically calling the attestation regime out. It is discussed in the context more of regulatory compliance and our registration as being critical- the licence to operate.”
- “We are extremely responsive to regulator requests, but communication can be inconsistent from the regulator. I think the regulator is trying to find the right balance between disclosure and detailed oversight in our regime. Clarity on this would assist board governance immeasurably. I think that the FMA (to date) has struck a better balance on regulatory openness.” (Comment on survey question *“Our Bank’s risk and compliance frameworks and controls are completely ‘fit for purpose’ in supporting my attest conclusions and opinions”*).

- “Providing detailed guidelines after completion of this process, will be more useful in improving the attestation process further.”

- “Perhaps the RB should document a Best Practice Attestation Regime. We would happily pick this up and seek to implement. A good example is Q26 [O1] (“*Our Board arrives on its collective view based on formal consent of each Board member than consensus”*) where we currently reach a consensus as opposed to an individual position.”

Appendix 3: Stakeholders engaged

The following Banks, bank officers and other stakeholders were interviewed:

Bank	Officer (Name)	Position
ANZ	• John Judge • Mark Verbiest • Nigel Williams • Norman Geary • David Hisco • Stewart Taylor • Bruce McIntyre • Graeme Edwards • Shahvez /David	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
ASB	• Gavin Walker • Jane Freeman • Vittoria Short • Jon Hartley • Barbara Chapman • Jon Raby • Kevin McDonald • Philip Taylor • Carl Ferguson / Chris de Wit	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
BNZ	• Douglas McKay • Prudence Flacks • Philip Chronican • Any Pearce • Anthony Healy • Adrienne Duarte • Peter Whitelaw • Brent Penrose • Rebecca Lee	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
WNZL	• Janice Dawson • Jonathan Mason • Peter King • Peter Wilson • David McLean • Jason Clifton • Carolyn Kidd • Jonathan Freeman • Amol Patwardhan	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
Kiwibank	• - • - • - • Alison Gerry • Paul Brock • Gary Crawford • Malcolm Bruce • Chris Barber	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor

Bank	Officer (Name)	Position
	• Christine Young	• Internal Auditor
Rabobank	• Sir Henry can der Heyden • William Gurry • Peter Knoblanche • John Palmer • Daryl Johnson • Carl Grant • Justine Lane • Chris Barber • Bill Stimson	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
Coop Bank	• Steven Fyfe • Gareth Fleming • Gareth Fleming • Jeremy Valentine • Graeme Edwards	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
SBS Bank	• John Ward • Mike Skilling • Shaun Drylie • Mark McLean • Peter Taylor	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
Heartland Bank	• Geoffrey Ricketts • Bruce Irvine • Richard Wilks • Jeffrey Greenslade • David Mackrell • Richard Lorraway • Jamie Munro	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
Bank of China	• Chris Tremain • Ruth Richardson • Shanjun Hu • -David Wang • Lily Liu • Jian Cai • Graeme Bennett	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor
Bank of Baroda	• Wenceslaus Anthony • Claudio Oberto • Vipan Mahajan • -Prahlad Gupta • Sujatha Murugan • Janakiraman Sarangapani • Jason Stachurski	• Chair • Independent director • Non-executive director • Ex-bank director • Chief Executive • Chief Financial Officer • Chief Risk Officer • External Auditor • Internal Auditor

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The Bank of England's approach to operational resilience – speech given by Charlotte Gerken *Operational Risk Europe 2017 Conference. London*	Bank of England	June 2017

Statement of Responsibility

This engagement was performed in accordance with the terms contained in our Consulting Service Order dated 28 February 2017. Where Deloitte has provided advice or recommendations in relation to either thematic or individual entity-related findings, we are not responsible for whether, or the manner in which, suggested improvements, recommendations, or opportunities are implemented. The management of Reserve Bank of New Zealand, or their nominees, will need to consider carefully the full implications of each of these suggested improvements, recommendations, or opportunities, including any adverse effects and any financing requirements, and make such decisions, as they consider appropriate.

The work performed did not constitute an assurance engagement in accordance with the New Zealand Institute of Chartered Accountants.

The matters detailed in our report are only those which came to our attention during the course of performing our procedures and did not necessarily constitute a comprehensive statement of all the weaknesses or issues that exist or actions that might be taken. Accordingly, management should not rely on our report to identify all weaknesses and issues or actions that might be taken. The report should be read in the context of the scope of our work.

This report should not be relied upon as a substitute for actions that Reserve Bank of New Zealand should take to assure itself of the integrity of the existing attest regime in place in New Zealand.

This report and all deliverables have been prepared solely for the use of Reserve Bank of New Zealand, and should not be quoted in whole or in part without our prior written consent. No responsibility to any third party is accepted as the report has not been prepared, and is not intended, for any other purpose.