RESERVE BANK

OF NEW ZEALAND

TE PŪTEA MATUA

Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks

Summary of submissions and policy decisions

18 December 2015

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Contents

Executive Summary

E1. In 2014 the Reserve Bank announced that it would be carrying out the "Regulatory Stocktake" (the stocktake), a review of the prudential requirements applying to registered banks and licensed NBDTs.

E2. As part of the stocktake, on 21 July 2015 we published the consultation document *Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks*, and a separate "Industry Update" for NBDTs.

E3. Our primary objective in conducting the stocktake has been to enhance the efficiency, clarity and consistency of the specific prudential requirements applying to banks and NBDTs. The secondary objective of the stocktake has been to consider whether there are areas where we can further improve the quality and effectiveness of current policy development process across our prudential and macro-prudential functions. A particular focus of this objective is considering the transparency of our policy development processes and our engagement with stakeholders[1].

E4. Submissions on this consultation document and industry update closed on 16 September 2015. In total, we received 20 submissions: 11 from banks, two from industry associations, one from a rating agency and six from private individuals. Appendix A provides a detailed list of submitters.

E5. This document provides a summary of the written submissions on the consultation document, our response on the main matters raised, and our final proposals. Feedback on the NBDT Industry Update that we released at the same time as the bank consultation document is included in a separate paper.

E6. The work of the stocktake, both in the year leading up to the consultation document and subsequently, has benefited greatly from the input of a number of interested parties. We would like to thank the staff of registered banks, independent directors of some of the banks who we talked to about off-quarter disclosure, our "Expert Panel" of outside advisors, and a broad range of other users of disclosure statements, for their helpful contributions to the work.

(1) Data reporting and disclosure requirements

E7. In the consultation document we summarised banks' current public disclosure and private statistical reporting requirements under the prudential regime, and explained how they contribute to our "three pillars" approach to prudential supervision (the three pillars being self-discipline, market discipline and regulatory discipline). We noted that although the disclosure regime plays an important role in market and self-discipline, it also imposes costs, and that the judgement of whether all the costs of the regime are justified by the benefits it delivers is a complex one.

E8. The consultation document therefore set out three main strands of work that attempted to make the disclosure regime more cost-effective:

[1] The Consultation Document for banks as well as the full initial Terms of Reference for the project are available on our website at: http://www.rbnz.govt.nz/regulation_and_supervision/stocktake/5966232.html.

(1)(a) ***Off-quarter disclosure:*** Options to change or remove the current off-quarter disclosure requirement;

(1)(b) ***Detailed disclosure changes***: A number of detailed proposals to change the content of on and off-quarter disclosure statements; and

(1)(c) ***Private reporting of quantitative content:*** A proposal to streamline the Reserve Bank's preparation of published summary tables that we draw from banks' disclosure statements.

(1)(a) Off-quarter disclosure

E9. We proposed four options for the treatment of off-quarter disclosure requirements. Specifically:

Option 1	The status quo.
Option 2	Scaling back off-quarter disclosure statements for larger locally incorporated banks to capital and asset quality disclosure, and removing the requirement for branches and locally incorporated banks with retail deposits below $200 million to prepare off-quarter disclosure statements.
Option 3	Removing the requirement for banks to prepare off-quarter disclosure statements and replacing it with some kind of continuous disclosure regime.
Option 4	Removing the requirement for banks to prepare off-quarter disclosure statements altogether.

Feedback

E10. Banks mostly preferred Option 4. Among other things, they argued that current off-quarter disclosure statements are of little value for market discipline, given the limited number of people who read them, and given how out of date the information is that they contain. Banks also noted the costs to them of publishing off-quarter disclosure statements, both direct financial costs and opportunity costs, and generally felt that Options 2 and 3 would result in at most minor savings from the status quo (Option 1).

E11. On the other hand, several private submitters argued that off-quarter disclosure statements should be retained (Option 1) because of the value of transparency to the market. These included a rating agency, who also pointed to the value of off-quarter disclosure in allowing the market to benchmark and to query individual bank figures.

E12. Two private submitters argued that a further reduction in public disclosure, on top of the introduction of private prudential reporting by banks to the Reserve Bank in recent years, would increase moral hazard for the Reserve Bank. They felt that this is compounded by the Open Bank Resolution (OBR) framework, which means that depositors still bear the risk of loss and therefore should have access to information that helps them assess and monitor the soundness of banks. One of these individuals argued that an alternative option would be to scrap the disclosure statement regime altogether, and instead have the Reserve Bank publish promptly all of the private reporting it receives from banks.

Conclusions

Option 4 rejected

E13. The Reserve Bank does not propose to remove off-quarter disclosure statements altogether for all banks (Option 4). While there is no single piece of compelling evidence that off-quarter information is regularly used by market counterparties to inform their decisions in respect of particular banks, there are a number of different considerations that cumulatively suggest benefits for market discipline from most locally-incorporated banks continuing to provide off-quarter information to the market. These considerations are listed in paragraph 84 in the main paper.

E14. Furthermore, the scale of the costs involved in publishing off-quarter disclosure statements does not appear unreasonable given the potential benefits, although we are still keen to find ways to reduce those costs (as discussed below).

E15. This conclusion is not dependent on self-discipline benefits. The Reserve Bank broadly accepts banks' arguments that the marginal impact of preparing off-quarter disclosure statements on the quality of their internal governance and risk management is not material (although one private submitter argued otherwise). We would be comfortable with an off-quarter disclosure outcome that does not necessarily include the current director attestation.

Option 3 rejected

E16. In light of feedback, the Reserve Bank has also decided not to pursue the continuous disclosure option (Option 3). Among other things, the objectives of standard stock exchange continuous disclosure are somewhat different to the financial stability aims of the disclosure regime. Setting up a different form of continuous disclosure, with different triggers, would likely be burdensome for the banks and confusing for the market. The requirement for directors' signatures would add to the cost and make the disclosure less timely. This option seems unlikely to either improve market discipline, or to result in any cost savings for banks compared to the status quo.

Option 2 preferred to Option 1, but new variant proposed for further consultation (Option 2b)

E17. Although we have decided against options 3 and 4, we are still keen to find a way to reduce the cost to banks of disclosing some regular off-quarter information. Of the options consulted on, our preference is therefore for Option 2. However, we note that banks do not generally expect Option 2 to deliver much reduction in costs compared to Option 1 (except for those that will be exempted from publishing off-quarter disclosure statements). We also note some of the concerns raised about the effectiveness of off-quarter disclosure under current arrangements.

E18. As a result, we are now considering an alternative approach, "Option 2b", which would aim for broadly the same objectives as Option 2, but which would aim to be:

a) More cost-effective for banks, by drawing on data that banks already prepare, and by simplifying the sign-off process; and

b) More effective, by enabling the information to be published in a timelier manner, and ensuring that it is more comparable across banks and more easily accessible.

E19. The basic concept that we want to develop is that the Reserve Bank would publish a quarterly electronic "dashboard" of key financial information on individual banks, drawn from the statistical and prudential returns that the banks submit privately to the Reserve Bank.

E20. This aligns with work that the Reserve Bank's Statistics Unit is currently carrying out to rationalise the current range of returns that registered banks have to submit. As well as providing a more comprehensive and relevant dataset, the aim of this work is to make the collection more efficient, following the basic principle of "provide once, use many times". The dashboard concept would build on this, as key information would be provided once not only to meet various private reporting needs, but also to populate the quarterly dashboard.

Key Advantages of the Quarterly "Dashboard" – Option 2b	
More Comparable	The data would be drawn from templated, standardised returns, making it easier to compile a dashboard of figures that are readily comparable across banks.
More Timely	The streamlined delivery mechanism, using data already produced by the banks, should in principle allow greater timeliness in the disclosure of the information.
Lower Cost	The data would not be subject to the directors' signature requirement applying in the disclosure statement regime (provided banks give their consent to the Reserve Bank publishing specified data that has been submitted via prudential returns). The fact that this would be based on reports already produced by the banks would mean some reduction in costs.

E21. The dashboard is still at the early conceptual stage. Key questions include the exact content and layout of the dashboard, and how to manage the trade-off between the timeliness of disclosure and the quality of the data being disclosed. (Current deadlines of up to 15 working days for private reporting returns compare with the two month deadline for off-quarter disclosure statements.) We propose to consult with banks and users on these and other important questions in the New Year, to assess whether Option 2b is workable and if so, whether it is preferable to Option 2.

<u>Removal of off-quarter disclosure requirements for branches</u>

E22. The other key aspect of our Option 2 was the removal of the off-quarter disclosure statement requirements from all overseas bank branches and locally-incorporated banks with less than $200mn in retail deposits. In light of the feedback we have received and the planned development of the dashboard model, we have concluded that:

a) We will recommend to the Minister of Finance that an Order in Council should be made to remove the requirement for branches to publish off-quarter disclosure information, once we are confident that we have sufficient private reporting in place for supervisory purposes (the specific rationale for this decision being what we consider to be the lesser value of off-quarter disclosure in providing market discipline for branches); and

b) We will defer a decision on whether to remove off-quarter disclosure from smaller locally-incorporated banks, and on the precise cut-off point, until we have decided what form that off-quarter disclosure will take, and hence can compare how much it costs those banks against the benefits that it delivers.

(1)(b) Detailed disclosure changes

E23. We also proposed a number of possible detailed changes to the content of disclosure statements. Table 1 of the main feedback statement sets out what we proposed, the feedback we received, and our policy decisions. Implementation of these decisions is subject to further consultation and the need to have Orders in Council made. Key changes include:

- We will retain the disclosure of concentrated credit exposures for locally-incorporated banks, but remove this requirement from branches;
- Banks will no longer have to include all conditions of registration in their disclosure statement, only those that are non-standard. (Standard conditions will be readily available on the Reserve Bank's website.);
- The table reconciling residential mortgage-related amounts will still be disclosed;
- We will remove the requirement for banks to disclose the contractual maturity analysis of financial assets; and
- We will specify that a bank's disclosure statement should include the bank's credit rating that applies on the date the directors sign the disclosure statement, rather than on the reporting date.

(1)(c) Private reporting of quantitative content

E24. The Reserve Bank's Statistics Unit is aiming to develop a private reporting template that banks would be required to complete from specified figures in their disclosure statement. This would replace the current process of the Statistics Unit extracting the data from published disclosure statements and manually putting it into a spreadsheet. From the Reserve Bank's perspective, the objective would be to save significant time and resources and minimise the opportunity for errors in the data collection process.

E25. Several banks noted that this proposal would be likely to result in a small increase in costs, but that it was not possible to be more specific without more information on the content of the template. Cost estimates that a few banks did provide suggest ongoing costs of a few thousand dollars p.a. at most, following somewhat higher set-up costs.

E26. Several banks saw potential benefit for them: if they could obtain these spreadsheets, that would save them the time they currently spend entering competitor data from disclosure statements into their own internal benchmarking templates.

E27. In response, we note that the issues and ideas discussed here have helped shape our initial thinking on the "dashboard" concept described above. We will integrate further consideration of this proposal into broader public consultation on the dashboard concept.

(2) Format and structure of the Banking Supervision Handbook

E28. The consultation document described a number of problems with the Banking Supervision Handbook (the Handbook), which is the suite of documents setting out a range of different matters relating to the Reserve Bank's regulatory requirements for banks. In various places the Handbook is unclearly drafted and hard to navigate, and the distinction between binding requirements, definitions and guidance is not always clear.

E29. To deal with these problems, we consulted on a major programme of work to restructure the Handbook, with a number of key objectives. Given the scale of the work, the consultation document also set out a high-level plan for how it would be carried out, broken down into four stages and lasting until at least the end of 2016.

E30. Submitters were largely supportive of the proposed restructuring. Some suggested a few additional issues that could be dealt with in the process.

E31. We plan to implement the restructuring largely as set out in the consultation document. Some specific points raised by submitters that we will take account of in the restructuring are:

- We will aim to make it clearer which material only applies to branches, which to locally-incorporated banks, and which to all banks;
- We will cross-refer to sections of other legislation and standards rather than copying the text of them into the Handbook, unless there are good reasons to do the latter;
- We recognise the need to allow banks sufficient time for implementation as well as consultation, and will not push ahead with any stage of the project until we have completed the previous stage (the updated version of the work plan now runs until mid-2017 – see Appendix C);
- We will ensure that sufficient review processes are in place to avoid unintended consequences (and to be clear about intended ones);
- We are not attracted to the suggestion of staff from banks being directly involved in the re-drafting, but will consider setting up a small drafting review group of volunteers drawn from banks; and
- One submitter provided an alternative to the two options we consulted on for standard document layout and numbering, which we prefer to those two options, and we will start the re-drafting using this alternative (see Appendix B).

(3) Capital requirements

E32. The subject of capital requirements was originally identified as one of the stocktake work streams, but in the event the consultation document did not make material proposals in this area. Some issues have been flagged for future work, and there are also separate initiatives currently underway outside the scope of the stocktake.

(4) The Reserve Bank's policy making approach

E33. Throughout the stocktake process, bank and NBDT stakeholders have indicated a strong interest in greater transparency regarding the Bank's policy making processes, as well as enhanced engagement with industry regarding policy changes. The Bank is proposing to take a number of steps to address these issues, including:

- Continuing to conduct targeted industry workshops for more significant or complex issues, as was done as part of the stocktake;
- Finalising and publishing a new document that describes our approach to policy-making and indicative timeframes for consultations. We should note here that the core elements of this document will apply to our work across sectors, though details of the approach (e.g. frequency of engagement with industry) will vary by sector;
- Lengthening the indicative timeframe for primary consultations to a standard 6-10 week period, unless exceptional circumstances require a shorter period;

- Revising the content of the website to make it more user-friendly and focussed, building to some extent on the changes to the structure and presentation of the Banking Supervision Handbook;
- Providing a more dynamic and comprehensive "Consultations and Policy Initiatives" section on our website;
- Developing a semi-annual "Industry Update" newsletter for banks to keep them informed about our work;
- Proactively using the Banking Forum to promote coordination among regulators regarding timelines for consultations and better informing industry about the Forum's work;
- Streamlining the process for amending regulations by eliminating some of the current need for changes and making the change process more transparent; and
- Making historical consultations, summaries of submissions, the relevant policy decisions and (when produced) the Regulatory Impact Statements (RISs) easier to find and link to the relevant policy. As described in detail in Part 4, we would welcome comments from industry or any members of the public on the quality and comprehensiveness of any of these specific documents.

(5) Differentiated approaches in the banking prudential regime

E34. As part of the stocktake, the Reserve Bank reviewed the nature of the differentiation between different classes of banks under the prudential regime. The consultation document reported on the outcome of this review, and highlighted some key principles that underlie the differentiated approach.

E35. Specific proposals coming out of this analysis were that we would: reduce disclosure requirements applying to branches; consider whether the application thresholds for the outsourcing and OBR requirements should be made the same; and assess whether to extend a form of one week liquidity mismatch ratio to branches.

E36. The analysis in this part of the consultation document was generally welcomed, and some submitters said they would welcome a clearer articulation in our policy documents of the rationale for differentiation, which we will aim to provide.

E37. The feedback and policy decisions on the proposed reduction of disclosure for branches are covered in the sections of this feedback document that deals with disclosure and data reporting.

E38. On the other two specific proposals, the question of thresholds is currently being considered, and the possibility of extending liquidity requirements to branches will shortly be considered, as parts of separate strands of work. The few comments that we received on these issues as part of the stocktake feedback will be taken account of in those other projects.

(6)(a) Refinements to director and senior manager non-objection process

(6)(a)(i) Narrowing the definition of "senior manager"

E39. As part of the stocktake we identified two specific issues with the current process for assessing the suitability of banks' directors and senior managers. The first was that the definition of "senior manager" can sometimes cover persons who do not have, or are unlikely to have, significant influence over a bank's financial soundness or governance, and hence are less relevant to our responsibility for the soundness of banks.

E40. We consulted on two options to address this issue:

- Define senior manager as certain key office holders, for example, Chief Executive Officer, Chief Financial Officer, Chief Operating Officer and Chief Risk Officer, or persons with equivalent responsibilities (our initial preference); or
- Define senior officer as a person occupying a position that allows the person to exercise significant influence over the management or administration of the bank (for example, a chief executive or a chief financial officer).

E41. There was unanimous preference for narrowing the scope of the definition of senior manager, and for doing so by means of a specified list. Banks mainly agreed with the proposed list of specified posts, although noted some practical issues: for instance, not all banks employ a person specifically with the title "Chief Operating Officer", and some thought that the meaning of "equivalent responsibilities" would need to be more tightly defined.

E42. Two private submitters however felt that the Reserve Bank should have no role at all, or no active role, in the vetting of board and senior management appointments.

E43. In response, we will go ahead with our initial preference, that is, to define senior manager as one of a list of specified office holders, or persons with equivalent responsibilities. To address the detailed design questions that have been raised about this approach, we propose to consult with banks early in the new year on:

- Any additions to the proposed list of specified office holders;
- The wording of the change to banks' conditions of registration that we would need to make, to bring this proposal into effect; and
- Guidance on the meaning of "persons with equivalent responsibilities".

E44. To clarify, these changes will not affect branches: for them, we propose to retain the current approach in which the New Zealand CEO is the only senior manager subject to a suitability assessment (other than at the point of registration).

(6)(a)(ii) Ensuring ongoing suitability

E45. The second issue is that there is currently no ongoing requirement to ensure the continued suitability of directors and senior officers who have already been appointed. We also proposed two options to address this issue:

- Requiring directors to attest in disclosure statements that they have effective systems and processes in place for ensuring the ongoing suitability of directors and senior managers, and that those systems and processes are being correctly applied (our initial preference); or
- Requiring banks to notify the Reserve Bank when any director or senior manager is subject to criminal, civil or disciplinary proceedings, or has been involved in the management of a failed institution.

E46. Each of these options was favoured by two banks. Concerns with the attestation option included that it would add an extra layer of complexity and process to director sign-offs, and that it was wrong for director liability to arise from something so subjective. One bank was concerned that the notification option would have to be implemented by a condition of registration, which would be complex to draft correctly.

E47. Four banks preferred another option, in which banks would be required to have an internal policy of continuing assessment of suitability, with annual attestation to the Reserve Bank that it has been properly run.

E48. In light of the feedback, we now propose to add a condition of registration that banks must have internal processes in place to ensure the ongoing suitability of directors and senior managers, and must follow these processes. This condition would probably also be supported by guidance on how such internal processes should work, and would not require directors to make a specific attestation on compliance with those internal processes (instead compliance with these processes would be covered by the general "risk management" attestation in disclosure statements).

(6)(b) Addressing issues around breaches of conditions of registration

(6)(b)(i) Notifying Reserve Bank of breaches

E49. As a matter of practice, registered banks privately notify the Reserve Bank whenever they identify that they have breached a condition of registration. But there is no formal legal obligation for banks to report breaches to us, so we consulted on using our existing information-gathering powers under the Act to require a bank to report any actual or potential breach privately to us as soon as practicable after it occurs.

E50. Most banks that responded agreed that some formalisation of the requirement would be preferable to the status quo. However, they raised some concerns about how to define the exact nature of the reporting obligation. For instance, the requirement should relate to the time that the bank becomes aware of the breach, not the time of the breach itself. Various questions were also raised around the exact nature of "potential" breaches. One bank also requested that we align the requirement as far as possible with analogous requirements under the Financial Markets Conduct Act 2013 ("FMCA").

E51. We propose to implement this requirement by means of a notice to all banks issued under s93 of the Act. We propose to adopt wording similar to s412 of FMCA in respect of the nature of the breach and the timing of the notification.

(6)(b)(ii) "Genuinely trivial" breaches of conditions of registration

E52. We also responded to the concern expressed by several banks that the need to publicly disclose a breach in their next disclosure statement can be disproportionate if the breach is of a very minor or trivial nature. We consulted on a proposal that we would deal with this by considering how conditions of registration are drafted to reduce the risk that genuinely trivial matters could result in technical breaches.

E53. Banks were in favour of any changes that reduce the scope for genuinely trivial breaches. One noted that the financial press seems to focus particularly on breaches when reviewing banks' disclosure statements, without usually giving any analysis of the seriousness of the breach, and also sometimes comment on the Reserve Bank's failure to take any action in response to the breach.

E54. Some banks suggested an approach under which they would notify the Reserve Bank of any breach (under the arrangements discussed above), but public disclosure of the breach would then be a matter for the Reserve Bank to decide, depending on materiality. One bank suggested a number of factors that we could stipulate in guidance on what we would treat as "material". Banks generally said that they would not want to be responsible themselves for deciding whether a breach was material: this could lead to varying interpretations across banks.

E55. In response, we confirm that we will address this issue using the approach we consulted on, namely through reviewing the drafting of conditions of registration. The restructuring of the Banking Supervision Handbook will provide opportunities to do this.

E56. The reasons for this are, first, that we continue to have concerns about the practicality of a materiality threshold, and whether the threshold would be applied consistently across banks and over time, and second, that we do not want to water down the requirement to disclose breaches, as we see this as an important discipline on banks.

Introduction

1. In 2014 the Reserve Bank announced that it would be carrying out the “Regulatory Stocktake” (the stocktake), a review of the prudential requirements applying to registered banks and licensed NBDTs.

2. As part of the stocktake, on 21 July 2015 we published the consultation document *Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks*, and a separate “Industry Update” for NBDTs.

3. Our primary objective in conducting the stocktake has been to enhance the efficiency, clarity and consistency of the specific prudential requirements applying to banks and NBDTs. By reducing any unnecessary costs or restrictions arising out of the current framework, we aim to help facilitate innovation and the efficient allocation of resources in the market, while still achieving our core financial stability objectives.

4. Within the scope of this stocktake are the contents of the current banking supervision handbook (which includes conditions of registration, guidance material, and the Orders in Council that set out the prescribed frequency and contents of the disclosure statements that are published by banks), and the specific prudential requirements for NBDTs (capital, liquidity, etc.). Outside of the scope of the stocktake are the contents of Part 5 of the Reserve Bank of New Zealand Act 1989, and other parts of the Non-bank Deposit Takers Act 2013 (for example, the provisions governing licensing, supervision, and investigations/enforcement).

5. The secondary objective of the stocktake has been to consider whether there are areas where we can further improve the quality and effectiveness of current policy development processes across our prudential and macro-prudential functions. A particular focus of this objective is considering the transparency of our policy development processes and our engagement with stakeholders.

6. Submissions on this consultation document and industry update closed on 16 September 2015. In total, we received 20 submissions: 11 from banks, two from industry associations, one from a rating agency and six from private individuals. Appendix A provides a detailed list of the respondents.

7. This document provides a summary of the written submissions on the consultation document, our response on the main matters raised, and our final proposals. Feedback on the NBDT Industry Update we released at the same time as the consultation document is included in a separate paper.

8. In addition to the consultation document, the stocktake has involved a major amount of industry engagement. We have actively engaged banks through five industry workshops, have consulted extensively with other government agencies and have benefitted greatly from the feedback of our “Expert Panel” of outside advisors who have helped us to test ideas as the project has progressed. We have also engaged directly with a broad range of other users of disclosure statements. The project has also benefitted from direct input from a number of independent directors of banks, who were particularly helpful in helping us assess the costs and benefits of the off-quarter disclosure statements. We would like to express our thanks to the Expert Panel members and the independent directors who made time to discuss the issues with us throughout the process.

The structure of this feedback statement

9. This feedback statement is divided into six parts, covering the different work streams that have been considered as part of the stocktake, and reflecting the structure of the consultation document. Specifically:

- Part 1: Data reporting and disclosure requirements for banks;
- Part 2: Format and structure of the Banking Supervision Handbook;
- Part 3: Capital requirements;
- Part 4: The RBNZ's policy making approach across regimes;
- Part 5: Differentiated regulatory approaches in the banking prudential regime; and
- Part 6: Miscellaneous changes to Bank policies and regulations.

Part 1: Data reporting and disclosure requirements

Summary of proposals

10. In the consultation document, we noted that the Reserve Bank's current approach to disclosure is heavily influenced by our broader approach to regulation, which is based upon the three pillars of:

- Regulatory discipline (i.e. the requirements imposed on a regulated firm by the prudential regime);
- Self-discipline (i.e. a firm's internal risk management and governance systems); and
- Market discipline (i.e. the incentives placed on firms by the fact that investors and other market participants are monitoring their risk profile, and financial performance and position).[2]

11. The prudential regime for banks is designed in part to buttress the operation of self-discipline and market discipline aspects of this approach. One of the most important ways that it aims to do this is through disclosure requirements that:

- Encourage market discipline through the quarterly publication of disclosure statements; and
- Encourage self-discipline through the due diligence that is required before the board will sign off on the content of these disclosure statements.

12. However, we remain conscious of the importance of ensuring that the disclosure regime remains fit for purpose and operates efficiently. To this end we carried out a review of the disclosure regime between 2009 and 2011 which made a number of important changes. These changes included:

- Removing the requirement to publish quarterly Key Information Summaries (KISs) and make hard copies of them available in every bank branch;
- Removing the requirement to publish Supplemental Disclosure Statements (SDSs) containing information such as the full text of guarantee arrangements and netting agreements;

[2] *The Evolution of Prudential Supervision in New Zealand*, p.5, Reserve Bank of New Zealand: *Bulletin*, Vol. 75, No. 1, March 2012.

- Providing that the financial statements included in half year disclosure statements no longer had to be prepared on an IFRS full year basis, and could instead be prepared on an interim basis; and
- Reducing capital adequacy information in the off-quarter disclosure statement from a full update to a brief summary.

13. At the time, cost estimates from banks suggested that these changes would result in direct costs savings of between $99,000-$140,000 per year for larger banks, and $21,500 per year for smaller banks.

14. Notwithstanding these changes, whether it remains appropriate for banks to prepare off-quarter disclosure statements is an issue that has arisen again in the course of the stocktake. We have given careful consideration to whether further changes to this requirement would be appropriate. In considering this issue we have focused on the underlying question of whether the benefits of this requirement outweigh the costs, taking into account the effect of any changes on the :

    - Market disciplines applying to banks;
    - Internal disciplines applying to banks;
    - Regulatory disciplines applying to banks;
    - Costs of preparing off-quarter disclosure statements;
    - Consequences of any changes for the treatment of banks under other regulatory regimes;
    - Overall impacts on financial stability; and
    - Consistency with international standards and the approach taken in other jurisdictions.

15. In light of this analysis, in the consultation document we proposed four options for the treatment of off-quarter disclosures requirements. Specifically:

Option 1	The status quo.
Option 2	Scaling back off-quarter disclosure statements for larger locally-incorporated banks to capital and asset quality disclosure (see paragraph 93 of the consultation document for more detail), and removing the requirement for branches and locally incorporated banks with retail deposits below $200 million to prepare off-quarter disclosure statements.
Option 3	Removing the requirement for banks to prepare off-quarter disclosure statements and replacing it with some kind of continuous disclosure regime to ensure that material adverse changes are disclosed when they occur between full and half year disclosure statements being published.
Option 4	Removing the requirement for banks to prepare off-quarter disclosure statements altogether.

16. We noted that Options 2, 3 and 4 would also require banks to provide additional private reporting to the Reserve Bank for supervisory purposes (and possibly also require banks to provide additional private reporting to rating agencies and/or the IRD).

17. We did not express a preference between these options. We stressed that a key consideration in choosing whether to scale back or remove the requirement to prepare off-quarter disclosure statements is likely to be whether or not it would materially

impact on the market and internal disciplines that banks are subject to. We encouraged any submitters who support changes to the status quo to directly address this issue.

18. In addition to possible changes to the requirement to prepare off-quarter disclose statements, the consultation document referred to a number of other disclosure related issues that we were considering.

19. Firstly, we are considering a number of more minor and technical changes to the content of disclosure statements. Details of these changes are outlined below in Table 1 (along with a summary of submissions and policy decisions). Secondly, we are proposing that as part of banks' private statistical reporting they provide certain information drawn from their disclosure statements in templated form, which we consider would be a more efficient way of compiling this information for statistical purposes.

Summary of submissions and policy decisions

Options for off-quarter disclosure statements

20. This section summarises the general points that were made on the options for removing off-quarter disclosure statements, summarises the responses that were provided in answer to each of the specific questions in the consultation document, and sets out the Reserve Bank's policy conclusions.

21. Generally the banks that submitted supported the removal of off-quarter disclosure statements (Option 4) on the basis that:

- The number of people who use them is limited;
- They provide limited value to the market given that the information they contain is so out of date;
- The costs of preparing them outweigh the benefits;
- Moving to half-yearly reporting is consistent with listed company financial reporting;
- The recent increase in private reporting reduces the value of off-quarter disclosure statements to the Reserve Bank for supervisory purposes;
- The off-quarter disclosure statement does not contribute to internal governance and risk management;
- Removing the requirement will make it easier to raise funds offshore.

22. A handful of banks also noted that:

- More information on Option 2 and Option 3 would be required to fully assess these options; and
- While they find off-quarter disclosure statements useful for competitor analysis, this is not sufficient justification for retaining them.

23. One bank also suggested that if the Reserve Bank is concerned about the effect on market discipline, an alternative approach would be to remove the requirement to prepare off-quarter disclosure statements and replace it with a power for the Reserve Bank to require a bank to publish information in off-quarters when it considers that additional information should be provided to the market.

24. Other submitters argued that off-quarter disclosure could be useful. Two private submitters argued that over the last 10 years the Reserve Bank has moved away from a regime based more on market discipline and disclosure, and minimising moral

hazard through ensuring that the Reserve Bank and the market both receive the same information. They contended that this has resulted in a major gap and inconsistency in the system, and is also problematic when the Open Bank Resolution (OBR) framework means that depositors still bear the risk of loss. They also suggested that a reduction in off-quarter disclosure will compound these issues. One of these individuals argued that an alternative option would be to scrap the disclosure statement regime altogether and instead have the Reserve Bank publish promptly all of the private reporting it receives from banks, as it clearly thinks this is more timely and useful information.

25. Another private submitter argued that removing the requirement to prepare off-quarter disclosure statements would be a further move away from market discipline, and result in an additional increase in moral hazard and risk of the Crown needing to bail out a bank.

26. Several private submitters argued that off-quarter disclosure statements should be retained because of the value of transparency to the market. The rating agency noted that “scaling back could materially undermine bank accountability to large swathes of market participants.”

> ***Q1.*** To what extent does private sector analysis and other published research on the financial system make use of off-quarter disclosure statements?

27. Outside the financial institution surveys carried out by KPMG and PWC, submitters were not aware of specific published research on the financial system that made use of off-quarter disclosure statements. But it was noted that some academics made use of off-quarter disclosure statements.

> ***Q2.*** How important is the role of off-quarter disclosure statements in imposing market disciplines on banks?

28. Generally banks argued that off-quarter disclosure statements create little or no additional market discipline on banks, as there is limited evidence that they are used by investors or the market, the information they contain is out of date by the time that it is published, and it only covers a three month period. However, one branch suggested that they would be of more value for locally incorporated banks than branches (where in most respects the financial position of the overseas parent is what counts).

29. Two private submitters argued that off-quarter disclosure statements support market discipline.

> ***Q3.*** Do you consider that the requirement to prepare off-quarter disclosure statements materially improves banks’ internal governance and risk management? If so, do you consider that there may be more effective ways of achieving these benefits?

30. Banks generally argued that preparing off-quarter disclosure statements does not affect, or materially affect, banks’ internal governance and risk management. Many of them noted that monthly Board reporting is standard or commonplace, and alternative mechanisms exist for banks to monitor their compliance over time. Two banks also argued that well-prepared disclosure statements were a product of good governance rather than a cause of good governance.

31. One bank suggested that a more efficient way to achieve what self-discipline is provided by the off-quarter disclosure statement requirement would be for the CEO

and CFO of branches to attest to the accuracy of quarterly private reporting to the Reserve Bank.

32. The rating agency argued that the ability for market participants to query unadulterated quarterly data can improve internal governance and risk management. One private submitter argued that the off-quarter director attestation requirement positively influences internal disciplines.

> ***Q4.*** How much cost savings for banks would result if the requirement to prepare off-quarter disclosure statements was removed, but additional financial information was provided to the IRD?

33. Banks provided a range of responses to this question, that included both quantitative and qualitative assessments of the costs.

34. Quantitative estimates varied considerably across most classes of banks (except the Big Four) and ranged from $5,600 p.a. to several hundred thousand dollars. However, the most common cost estimates were around $100,000 p.a. or slightly over.

35. Quantitative descriptions of costs focused on the staff, management and director time saved, and the opportunity cost in terms of the amount of that time that was currently devoted to off-quarter disclosure statements.

> ***Q5.*** Do you agree with our assessment of how effective the disclosure statement regime currently is about providing information about the soundness of a bank in a crisis situation or stressed market situation?

36. Banks argued that off-quarter disclosure statements are of limited effectiveness in a crisis or stressed market situation, given that the information they provide is historical in nature.

37. One private submitter argued that more disclosure should be required in a crisis situation to enable the true financial position of a bank to be determined.

38. The rating agency and one private submitter both suggested that off-quarter disclosure statements help to identify trends and potential problems at an earlier stage, which could help to avert a crisis. The rating agency also considered that the ability of banks to produce quality and detailed disclosures, especially in a time of stress, is important (regardless of whether the disclosed information is historical in nature).

> ***Q6.*** Would removing the requirement to prepare off-quarter disclosure statements (or scaling it back to disclosure of a narrower range of matters) create larger windows for New Zealand banks to raise offshore funds? If so, please explain the reasons for this.

39. Submitters were divided on this issue.

40. Three banks argued that this would increase funding windows, which are constrained by the inability to go to market when preparing the off-quarter disclosure statement.

41. One bank said it would not materially influence their ability to raise funds from offshore.

42. Another bank noted that it may assist slightly with raising funds offshore, but that they do not have a formal blackout period before the release of off-quarter disclosure

statements the way they do for full or half year, so this is less of an issue for them. However, they consider that off-quarter disclosure statements can cause confusion for offshore investors and result in questions about whether any of the information in the off-quarter disclosure statements is material.

43. The rating agency and one private submitter both argued that there was no evidence to suggest that this would affect banks' ability to raise funds from offshore.

> ***Q7.*** Are there other issues we should be considering with regards to off-quarter disclosure requirements for banks?

44. Several banks noted that it was important that the removal of off-quarter disclosure statements should not affect banks' Financial Markets Conduct Act exemptions.

45. One bank suggested that if Option 2 or Option 3 are adopted, consideration should be given to not requiring directors to attest to these disclosures.

46. One bank considered that if removing off-quarter disclosure statements is problematic, the Reserve Bank should compensate for this by having the power to direct banks to make disclosures when events occur that should be notified to the market.

47. One bank also suggested that we should be cautious about imposing a one-size-fits-all approach in order to align with international trends.

> ***Q8.*** Do you agree with the options that we have identified for the treatment of off-quarter disclosure statements? Are there other options that we should be considering?

48. One submitter suggested that Option 2 should be divided into two separate options – one on scaling back to capital and asset quality disclosure, and one on the exemption for branches and smaller banks (the threshold for this exemption should ideally be based upon total liabilities rather than retail deposits).

49. One bank argued that the option of scaling back off-quarter disclosure statements to just capital and asset quality disclosure for all banks should be considered.

50. One bank argued that a continuous disclosure option would be costly to comply with and increase fragility in the financial system.

51. One bank suggested that there could be an option where the Bank, with the collective agreement of banks, publishes an industry wide summary of the health of the sector and key financial metrics.

> ***Q9.*** Do you agree with our assessment of the costs and benefits of Option 1? To what extent can these costs and benefits be quantified? Are there other costs and benefits that we should be considering?

52. There were differing views on the costs and benefits of Option 1.

53. One bank noted that its best estimate is that the costs of preparing off-quarter disclosure statements is about $10,600. It takes staff members 8.5 days and directors time also needs to be added to this.

54. Another bank suggested that the costs associated with preparing off-quarter disclosure statements is approximately $30,000-$40,000 in staff, management and director time alone, and removal of off-quarter disclosure statements is likely to result in a cost reduction even if additional information may need to be reported privately to the IRD, the Reserve Bank and others.

55. Two banks suggested that the principal costs associated with preparing off-quarter disclosure statements are the opportunity costs in terms of staff time, which are difficult to quantify with any accuracy.

56. Two banks also suggested that the opportunity costs to the Reserve Bank should also be considered given that there is presumably duplication in assessing the contents of disclosure statements and the private reporting that the Reserve Bank receives on substantially the same matters.

57. Several banks also suggested that this option does not enhance market or investor discipline, and one bank suggested that removal of off-quarter disclosure statements should not impact on banks' Financial Markets Conduct Act exemptions as these are based upon the fact that banks are prudentially regulated.

58. One submitter suggested that the costs of this option are likely to be limited compared to the benefit of a public that is well informed about the financial position of a bank.

> ***Q10***. Do you agree with our assessment of the costs and benefits of Option 2? To what extent can these costs and benefits be quantified? Are there other costs and benefits that we should be considering? Are there ways of mitigating the costs or risks of this option?

59. Most banks suggested that subject to the detail being confirmed, the costs of this option are likely to be similar or only slightly smaller than the costs of the status quo.

60. One bank also suggested that subject to more information about the detail, the costs of preparing this scaled down off-quarter disclosure statement is likely to be around $80,000.

61. Two banks suggested that this option would result in a cost saving, but that this cost saving may be small. One bank also questioned who would benefit from just having this information disclosed given that there was limited evidence of current disclosure statements being used in the first place.

62. One submitter noted that the costs of this option potentially include later public detection of a troubled bank.

> ***Q11.*** How would banks' internal risk management and governance be influenced by this option? [Option 2]

63. Banks argued that this option would have no significant effect on internal disciplines.

64. One submitter argued that a lower reporting frequency would create more scope for discrepancies between accounting and risk management practices in banks.

Q12. Do you agree with our assessment of the costs and benefits of Option 3? To what extent can these costs and benefits be quantified? Are there other costs and benefits that we should be considering? Are there ways of mitigating the costs or risks of this option?

65. Several banks questioned whether this option is viable and disagreed that it would have the proposed benefits. They also felt that it would not create any cost savings.

66. Two banks suggested that it is difficult to determine the costs and benefits of this option until more detail is provided, but the costs could be significant.

Q13. How would banks' internal risk management and governance be influenced by this option? [Option 3]

67. Banks argued that this option would have no significant effect on internal disciplines.

68. One submitter argued that a lower reporting frequency would create more scope for discrepancies between accounting and risk management practices in banks.

69. One bank suggested that this option could make risk management processes more expensive.

Q14. Do you agree with our assessment of the costs and benefits of Option 4? To what extent can these costs and benefits be quantified? Are there other costs and benefits that we should be considering? Are there ways of mitigating the costs or risks of this option?

70. Most banks referred to their earlier description of the costs associated with the status quo here. A number of banks also suggested that the costs of this option are likely to be negligible given the limited evidence of disclosure statements being used.

71. One bank suggested that the cost saving from this option may be up to $150,000 p.a. (mostly made up of management time).

72. One bank suggested that the costs and benefits of this option are difficult to determine without more information on what information other government agencies may require in private reporting.

73. One private submitter suggested that the costs of this option are likely to be limited compared to the benefits of a public that is well informed about the financial position of a bank.

Q15. How would banks' internal risk management and governance be influenced by this option? [Option 4]

74. Banks argued that this option would have no significant effect on internal disciplines.

75. One submitter argued that a lower reporting frequency would create more scope for discrepancies between accounting and risk management practices in banks.

Q16. Of the four options presented above, which do you prefer and why? Please provide detailed reasons, and thoughts on how the costs and risks of your preferred option could be managed.

76. Opinions on which options should be preferred were divided.

77. Option 1 was supported by three private submitters as well as the rating agency who submitted.

78. Most banks supported Option 4, subject to the views of other government agencies on the consequences of this option.

79. Two banks suggested that the preferred option depended upon the consequences in terms of additional private reporting and the treatment of banks under other regulatory regimes.

Reserve Bank conclusions on off-quarter disclosure statements

Option 4 rejected

80. We do not support Option 4, the complete removal of off-quarter disclosure statements.

81. We accept that off-quarter disclosure statements no longer play a role in regulatory discipline, as the Reserve Bank now receives most of the information it needs for supervisory purposes on a private and more timely basis than the off-quarter disclosure, and could obtain any additional information as needed if off-quarter disclosure statements were no longer published.

82. In the light of feedback received from some banks, it also appears that off-quarter disclosure statements currently play a limited role in self-discipline in many cases. However, we have received some evidence to suggest that they may support the development of effective governance and risk management process in newer entrant banks. The Reserve Bank is also concerned about the risk that the removal of off-quarter disclosure statements could result in the gradual decline in some internal governance and risk management over time, at least in some cases.

83. Most importantly, we are not convinced by arguments put forward that six-monthly information on the financial situation of banks is sufficiently frequent to provide adequate market discipline. This was also the view of a number of non-bank submitters, who argued strongly for the “in principle” benefits of off-quarter disclosure statements in contributing to market discipline.

84. Given this context we consider that a number of considerations combine to suggest some benefits from most locally-incorporated banks continuing to provide off-quarter information to the market:

    a) The Reserve Bank requires registered banks to maintain and publish a credit rating, reflecting the value it attaches to credit ratings as one easily understandable indicator of bank soundness. As noted above, at least some of the rating agencies see value in banks’ off-quarter disclosure statements. Although they have the ability to require updates from the banks that they rate, public information on all banks helps them to benchmark those banks against the banking sector as a whole;

    b) New Zealand registered banks have a variety of financial reporting years: currently there are banks with year-ends at end-March, end-June, end-September and end-December. Removing off-quarter disclosure would undermine comparability, as banks would not all be publishing data covering the same six-month periods;

c) The timeliness of disclosures to the market is important, and removing the requirement to make off quarter disclosures would mean that the latest public information available to the market could be up to nine months out of date (rather than the current maximum of six months out of date);

d) Our approach to international standards is generally to adopt them with (where appropriate) amendments to reflect New Zealand conditions. There are benefits in being able to demonstrate broad compliance with the spirit of such norms where they are relevant for New Zealand. In this respect, removing the requirement to make any off-quarter disclosures would be inconsistent with Basel's Pillar 3 requirements;

e) Ordinary depositors in New Zealand are not covered by a deposit insurance scheme, and if their bank becomes insolvent and is subject to OBR they may lose part of their deposits. This is consistent with the philosophical underpinning of the regime which stresses market discipline, and the fact that it is not a "zero-failure" model. Disclosure is a key element that supports this framework, and significantly scaling it bank would be inconsistent with this approach;

f) Recent data from the Reserve Bank's own website shows approximately 100 hits (from external users) per month on the Bank's tables that give a side-by-side comparison of select data from banks' Disclosure Statements: http://www.rbnz.govt.nz/statistics/tables/g1/. The hits on the website are relatively constant throughout the year and come from a range of countries, though the majority of users are in New Zealand and Australia. At the moment, this information is relatively difficult to find on our website, which may partially drive the limited use of the data. 2009 data from some of the larger banks showed a few hundred hits per month on the disclosure statement pages of their websites. This indicates some interest in disclosure statements (although it does not show the purposes for which they are being downloaded or how important off-quarter disclosure is for those purposes).

85. However, we also accept that the current content and presentation of off-quarter disclosure statements may not support market discipline as effectively as possible, and there may be scope for improvements in this regard. Notwithstanding this, the costs of off-quarter disclosure statements do not appear to be prohibitive and as noted earlier, non-bank submitters saw benefits in the requirement to produce off-quarter disclosures.

Option 3 rejected

86. At a general conceptual level we see the appeal of a continuous disclosure regime in this context, in that it would theoretically result in real-time, or close to real-time, disclosure of relevant information. In turn, this could be expected to improve market discipline (especially if there was an audience of analysts who made use of this information).

87. However, banks did not support this option, and for a variety of reasons we do not support it either. The immediate reason for this is that we consider that the costs of implementing a fully fledged continuous disclosure regime are likely to outweigh the benefits. More specifically:

- Unless the regime was set up effectively to mirror the current NZX disclosure regime, there might be confusion in the market about the nature of the disclosure and inefficiencies for the banks in producing it by creating an additional set of disclosure obligations that they needed to comply with;

- The purpose of standard stock exchange continuous disclosure is different from that of the Reserve Bank's disclosure regime. The basis of the former is information that is likely to be material to the price of the security traded on the market. The basis of the latter is information relevant to a broader picture of financial stability. It is not clear in practice how a continuous disclosure regime might require disclosure of information relating to financial stability rather than the pricing of financial products. Arguably a form of periodic rather than continuous disclosure is more suitable for information relating to financial stability; and

- Any requirement to have directors provide the kinds of attestations they do on disclosure statements in respect of information disclosed under a continuous disclosure regime is unlikely to be workable.

Option 2 preferred to Option 1 but variant to be developed (Option 2b)

88. In light of the above considerations, the Reserve Bank believes that market discipline will continue to be best met by at least the more systemically important banks providing some form of update to the market in off-quarters (particularly given that the costs associated with doing this do not seem to be especially high).

89. The Reserve Bank notes the estimates that banks have provided on the cost of producing off-quarter disclosure statements. We do not regard these as particularly significant relative to the size of banks' business, or viewed as a cost that they might pass on to customers, when considered against the benefits they provide. Nevertheless, we acknowledge that as a point of good regulatory design requirements should aim to avoid imposing redundant or unnecessary costs where possible. In this respect, we acknowledge that not all the information in off-quarter disclosure statements necessarily supports market discipline, and it should be possible to save costs without materially affecting the benefits (more specifically, it may be an argument for changing some of the content of off-quarter disclosures, rather than abolishing the requirement to prepare these disclosures altogether).

90. For this reason, we prefer Option 2 to Option 1 (the status quo), as it would achieve the following:

    a) Save all the cost of off-quarter disclosure for overseas bank branches (the treatment of smaller locally-incorporated banks is discussed further below);

    b) Represent some cost saving for banks that are still required to publish off-quarter disclosure statements (although the feedback was that this would not be a major saving);

    c) Still provide rating agencies with the information that they regard as most important; and

    d) Broadly comply with the Basel Pillar 3 requirements for off-quarter disclosure.

91. However, we are now considering an alternative approach, which we refer to as Option 2b, which would aim for broadly the same objectives as Option 2, but which would aim to be:

a) More cost-effective for banks, by drawing on data that banks already prepare, and by simplifying the sign-off process; and

b) More effective, by enabling the information to be published in a more timely manner, and ensuring that it is more comparable across banks and more easily accessible.

92. The basic concept that we want to develop under Option 2b is that the Reserve Bank would publish a quarterly electronic "dashboard" of key information on individual banks, drawn from the statistical and prudential returns that the banks submit privately to the Reserve Bank. So neither the dashboard, nor the information submitted by banks to feed into it, would be "disclosure statements" as currently defined in the Reserve Bank of New Zealand Act 1989.

93. This aligns with work that the Reserve Bank's Statistics Unit is currently carrying out to rationalise the current range of returns that registered banks have to submit (referred to as the "Balance Sheet Redevelopment project"). As well as providing a more comprehensive and relevant dataset, the aim is to make the collection more efficient. The basic concept is "provide once, use many times". The dashboard concept fits with this in that banks would no longer publish off-quarter disclosure information that is a re-worked version of information already provided privately. Instead information that is provided privately would then be published in the dashboard.

94. The proposal could rely on a different mechanism than that used for current disclosure statements. The Reserve Bank uses s93 of the Act to require banks to submit the completed statistical and prudential returns privately. This information is protected by confidentiality provisions in the Act. The publication of a dashboard would rely on banks giving the Reserve Bank permission to publish the specific information it contains.

95. There is also a possibility of revising the provisions of s81 of the Act. Banks have told us that one of the major components of the cost of Disclosure Statements is the Director signature requirement. They have also told us this is one of the reasons that disclosure information data takes longer to produce. There is a possibility we could remove the Director signature requirement for "dashboard" information but still require banks to publicly disclose it using section 81. If we did this, we would expect to put other mechanisms in place to ensure the quality of the data.

96. One mechanism that we have suggested previously is the use of reports commissioned under s95 of the Act to assess how banks extract information from their records to complete the prudential returns submitted to the Reserve Bank. The suggestion has been that we would implement a programme of such reports on a rolling basis across different returns. We raised this previously in the general context of obtaining greater confidence in the accuracy of returns that we rely on for supervisory purposes, but this would also increase confidence in the accuracy of data included in the dashboard.

Preliminary thoughts on the Quarterly "Dashboard" – Option 2b	
Key Features	Templated, comparable, based on existing private reporting, no Director signature requirement (though still quality controlled through other means), timely, electronic
Key Advantages	More comparable, more timely and lower cost for banks
Basis for Design	Existing summary reports (current and historical) available on our website at: http://www.rbnz.govt.nz/statistics/tables/g1/

	(see Excel file for historical reports) Input from users: rating agencies, banks, other investors, financial journalists, academics, some depositors

97. We see two big practical advantages in the dashboard model. First, the data it would contain is drawn from templated standardised returns, making it easier for the Reserve Bank to put together a dashboard of figures on a readily comparable basis across banks. Secondly, this information would not be subject to the legal requirement for signature by all the bank's directors that applies in the disclosure statement regime.

98. These two changes would also potentially lead to greater timeliness in the disclosure of information, which would help meet the policy objectives of the disclosure regime better. This approach would also be consistent with the original principle underlying the disclosure regime, namely that information available to the Reserve Bank should also be available to the market.

99. The dashboard is still at the early conceptual stage. Further work is needed on the workability and design of this proposal, and we propose to consult banks and potential users of the dashboard on these issues in the new year. This consultation will need to develop Option 2b in detail and seek views on how its costs and benefits compare with those of Option 2. Key questions that we think need to be addressed to develop the dashboard concept include:

- What particular data should be included in the dashboard and how should it be presented?;
- How should the trade-off be struck between the timeliness of disclosure and the quality of the data being disclosed? (i.e. how much time should banks be given to prepare this information before it is published);
- How would the dashboard interrelate will full and half-year disclosure statements? (e.g. if there was an inconsistency between information disclosed in the dashboard and in disclosure statements how would this be reconciled?); and
- What potential liability risks are raised by this option?

100. We will also need to address the specific disclosure around new capital issuance and breaches of conditions of registration, which we would still want to see disclosed more frequently than six-monthly, but which do not lend themselves to the "dashboard" presentation.

101. We note that these four questions are heavily interrelated. For example, how significant the data quality and liability issues may be depends upon what information is in the dashboard and how long banks have to prepare it.

102. However, we believe that if these issues are addressed it may be possible for the dashboard to be a more efficient approach for the market, the Reserve Bank, and industry. In particular:

- For the market (and depositors especially) it may result in more accessible and focused information; and

- For banks there may be cost savings as a result of not having to prepare off-quarter disclosure statements, even if the cost of preparing some statistical reporting increases as a result of that reporting being used in the dashboard.

103. If the dashboard concept proves workable, its implementation will require completion of the Balance Sheet Redevelopment project being carried out by our Statistics Unit. The reasons for this are that until this project is completed:

    - We may not have all of the necessary data reporting in place to enable the dashboard to be implemented; and

    - We may not have complete assurance that there is no information in off-quarter disclosure statements that could be useful for supervisory purposes.

104. The Balance Sheet Redevelopment project is due to be completed by December 2016.

105. If the dashboard concept does not prove workable, then we will carry out further work to refine the original proposals under Option 2, retaining off-quarter disclosure statements but seeing how far unnecessary content can be removed.

106. Separately from the preceding discussion, there is also a question around whether smaller locally incorporated banks (e.g. those with retail deposits under $200 million), and branches of overseas banks should still be required to prepare off-quarter disclosure statements.

107. In respect of small locally incorporated banks, the issue is whether the benefits of this requirement outweigh the costs. We do not consider that it is possible to answer this question until we have explored the dashboard approach in more detail. Accordingly, we do not propose any changes to the requirement on these banks to prepare off-quarter disclosure statements at this point.

108. In respect of branches, there is a more fundamental question about whether the requirement to prepare off-quarter disclosure statements makes much contribution to market discipline, given that branch specific data is of much more limited value for market discipline purposes. In particular, the soundness of a branch cannot be separated from the soundness of its parent, and market discipline in this context is likely to be better served by the market looking at data on the parent bank.

109. We consider that this distinguishes branches from locally incorporated banks and changes the cost/benefit analysis in the cases of branches. In conjunction with the fact that most branches are relatively small banks, we consider that the cost/benefit analysis here justifies remove the requirement for branches to prepare off-quarter disclosure statements. However, we need to be sure that all of the private reporting we need from branches is in place before removing the requirement to require branches to prepare off-quarter disclosure statements.

110. In summary then:

    - We propose to consult with industry in the New Year to develop the dashboard approach, with the aim of designing an Option 2b that would allow cost savings while simultaneously improving the effectiveness of off-quarter disclosure in terms of market discipline. If Option 2b proves workable and is the preferred option following consultation, we anticipate that it could be implemented once the Balance Sheet Redevelopment is in place at the end of 2016. Otherwise we will implement Option 2, subject to further refinement of its details; and

- Regardless of the choice between Option 2 and Option 2b, we propose to remove the requirement for branches to prepare off-quarter disclosure statements once we are confident that all of the necessary private reporting we need for supervisory purposes in place. This may require completion of the Balance Sheet Redevelopment, but we will also consult further on the timing of this change in the New Year.

Other detailed changes to disclosure statements

111. The consultation document discussed a range of possible technical amendments to the content of disclosure statements, and asked the following question:

> ***Q17.*** Do you have any comments on the proposed changes to the content of disclosure statements? Are there any other matters we should consider adding to, or removing from, disclosure statements?

112. A number of banks supported the proposed technical changes as a whole.

113. Some individual banks made comments on some of the specific proposals. The following table summarises the proposals we made, the feedback we received, and what we plan to do next in each case. Every proposed change in disclosure requirements that is noted below can only be made by Order in Council on the advice of the Minister of Finance in accordance with a recommendation made by the Reserve Bank, and will also require further consultation with banks, the FMA, and other interested parties.

Table 1: detailed changes to disclosure requirements		
What we proposed	**Feedback**	**What we propose now**
We proposed some reduction in public disclosure of concentrated credit exposures, in view of possible regular private reporting to the Reserve Bank on large exposures. We also noted that a branch's large exposures are disclosed in relation to the whole overseas banking group's capital, so are particularly uninformative	One bank agreed specifically that these disclosures may not be informative. But two users of disclosure statements noted these among their "top 10" most useful disclosures.	We propose not to change this requirement for locally-incorporated banks, at least until decisions have been made on the possible private reporting. We propose to remove the requirement from branch disclosure statements. This includes "dual-registered branches" (those with an associated locally-incorporated bank), since the relevant information on the group's NZ large exposures is provided in the local bank's DS.
We could consider changing the approach to disclosure of Conditions of Registration so that conditions that apply to all banks do not need to be disclosed.	One bank suggested that it was clearer to include all conditions in the disclosure statements unless standardised conditions are available elsewhere in an easily understandable format for readers (e.g. in a single publication on the Reserve Bank website) that the disclosure statements can cross reference to. However, the redrafting of the handbook might address this issue. If so, disclosure statements would only need to repeat the special conditions applicable to individual banks. Another bank suggested that banks could disclose their conditions separately on their website.	We propose to change disclosure requirements so that a bank will only need to disclose those of its conditions that are non-standard, and will only need to report changes in its conditions of registration that are non-standard. In the revised Handbook structure, there will be a stand-alone document that will set out the standard set of conditions applying to each bank of a given type.
We could review how informative the disclosure of credit risk mitigation is, and consider ways to improve it if necessary.	One bank agreed that the disclosure of credit risk mitigation could be reviewed, especially given that some information on credit risk mitigation is already required by NZ IFRS 7.	We note that we will be aiming to clarify the treatment of credit risk mitigation in the Handbook documents BS2A and BS2B, as part of the handbook restructuring (see Part 2 below). We plan to review the disclosure of credit risk mitigation in due course, but given the need to take account of the work on BS2A and BS2B, as well as to compare our requirements with those of NZ IFRS 7 and Basel Pillar 3, any changes may take some time to work through.

Table 1: detailed changes to disclosure requirements		
What we proposed	**Feedback**	**What we propose now**
We could review how useful supplementary information on asset quality is for the New Zealand financial reporting groups of branches, and whether it could be cut (as opposed to asset quality for the overseas banking group as a whole – which is required anyway).	In one bank's view, it is preferable to maintain disclosures at the New Zealand financial reporting group level, as this provides a complete picture of a bank's operations in New Zealand.	We will consider further whether the asset quality information that branches must disclose in any case under NZ IFRS (both full year and in other periods) would remain adequate if we drop this, before deciding whether to remove the supplementary disclosure requirement.
We added a table reconciling residential mortgage-related amounts into disclosure statements because of the diversity of figures that banks publish relating to residential mortgage lending. We could review how useful this disclosure has been.	One bank noted that this table is useful, given the diversity of figures some banks publish relating to residential mortgages, and that journalists and analysts make use of these disclosures.	We have reviewed examples of what these tables show, and agree that in some banks' disclosure statements this requirement helps readers to understand how different housing lending figures relate to one another. We propose to retain it.
We suggested that in the required disclosure of risk management policies, references to the Foundation IRB approach could be cut if the approach itself is cut, and more reliance could be placed on new expanded NZ IFRS 7 disclosure.	One bank commented more generally on the overlap between our disclosure requirements and NZ IFRS, and suggested removing disclosure requirements that are already covered by NZ IFRS.	The comment is more general than the specific proposal. We note that we carried out a similar exercise as part of our major Disclosure Review over 2009-2011, but also note that NZ IFRS requirements have expanded somewhat since then. We agree that it will be worthwhile to repeat the exercise, but that may be a significant piece of work so the timing will depend on resources. We propose to remove the references to the Foundation IRB approach.
	One bank suggested we remove the requirement for locally-incorporated banks to disclose their internal figure for capital held against "other material risks", under the Basel Pillar 2 framework. They felt that it was not useful and was difficult to interpret, as every bank calculates the number differently in line with their own ICAAP ("internal capital adequacy assessment process").	Pending further work on our approach to setting expectations for banks' ICAAPs, we do not agree with removing this disclosure. At present, we view this disclosure as part of the limited incentives in place to encourage banks to identify capital for other material risks.

Table 1: detailed changes to disclosure requirements		
What we proposed	**Feedback**	**What we propose now**
We suggested that IRB banks' disclosure of capital requirements for credit risk could be based on a standard set of PD (probability of default) ranges, rather than using their own PD ranges as at present. This would both improve comparability, and align with the recent Basel Pillar 3 revisions	The only specific feedback on this noted that different PD ranges will be appropriate to each bank.	We do not propose to make this change in the short term. We note on the one hand that this change might require a bank that uses different PD buckets in its IRB models to have to change those models to meet the disclosure requirements. But we also note that we are developing a private reporting template for capital adequacy, for which standard PD ranges might be desirable. International disclosure standards are also moving in the direction of greater use of standard templates. So we may revive this proposal later in light of other developments.
A reconciliation of regulatory capital versus accounting capital could be added (this is a Basel III requirement).	One bank thinks that regulatory capital can be reconciled to accounting capital from the current disclosures, without the need for adding a specific reconciliation. Another bank supports publication of a reconciliation of capital on a Basel 3 harmonised view, similar to that done by Australian banks, as this will assist peer bank comparisons and improve the quality of investor analysis.	After reviewing how banks disclose the components of their regulatory capital, we take the view that, at least for some larger banks, some additional explanation would help users understand how regulatory capital relates to figures in the financial statements. However, the latest revisions to the Basel Pillar 3 disclosure framework include a reconciliation between capital ratios and financial statements across the whole risk-weight calculation, not just the capital base. We do not propose to make any changes in this area in the short term, but will consider in due course whether a more comprehensive reconciliation should be added, as part of deciding whether to switch to the more templated approach required under the new Pillar 3.

Table 1: detailed changes to disclosure requirements		
What we proposed	**Feedback**	**What we propose now**
We could consider whether additional dedicated disclosure is needed for a bank's covered bond issuance.	One bank felt that no additional disclosures on covered bonds are necessary. But another bank suggested we could require twice-yearly disclosure of: the percentage issued compared to the regulatory limit, the number of issues made, and the value of encumbered assets.	A review of current disclosures shows that bank disclosure statements contain a fair amount of information on covered bonds, but often scattered throughout the notes to the accounts. We will consider whether it would be worthwhile to require banks to summarise key information under one heading, and/or to require a link to be added to the public register of covered bonds.
	One bank felt that we should consider an alternative presentation for the risk notes – specifically currency, interest rate, liquidity and sensitivity notes. While recognising they are required under IFRS, they noted that the complexity for banks makes their length and readability challenging both for preparers and readers.	We feel that this is a reasonable point, although addressing it would not be a trivial matter. It might for instance help to require these notes to be more clearly broken up into separate sections, but there would be a question of how that would interact with IFRS. We will review this issue as resources permit.
	One bank requested that the contractual maturity analysis for financial assets be removed from disclosure statements. They noted that banks do not use this information in their liquidity risk management, that neither NZ IFRS nor APRA require this disclosure, and that the information contained is likely to be misleading to an uninformed reader.	We note that a maturity analysis of <u>liabilities</u> is required by NZ IFRS, but that the equivalent for assets is only required for our disclosure purposes. We accept the points made, and propose to remove this requirement in the near term.
Dual-registered branches have a complex directors' sign-off requirement, covering management of risks in entities that are in the branch's financial reporting group but not in the locally-incorporated bank's group. This could be simplified or cut.	One of the dual-registered branches supports this change.	A review of what is actually presented in the full-year directors' attestations of dual-registered branches confirms that they are unlikely ever to be informative for the reader. We will try to find a better solution to the problem that this approach was meant to address, namely that the normal attestation for a stand-alone branch is not suitable for a dual-registered branch.

Table 1: detailed changes to disclosure requirements		
What we proposed	**Feedback**	**What we propose now**
We could tidy up disclosure of the overseas banking group's P&L and balance sheet.	No specific comments.	We note that branches are currently interpreting the requirements in differing ways, because they are not clear. We will recommend clarifications to these requirements as soon as possible.
We could review the nature of what must be covered in the auditor's report/review opinion (full year and half year): (1) detail could be cut from what the Orders specify, to allow more reliance on audit standards; and (2) the current multi-part opinion on the different disclosure components is complex and potentially could be simplified.	No specific comments.	We propose to go ahead with rationalisation in this area. This will require engagement with the audit profession, and may be quite a significant piece of work.
The word "examine" to refer to auditors' limited scope reviews is not the right technical term, and should be corrected.	No specific comments.	We will address this issue as part of the previous point, in consultation with auditors.
We could clarify disclosure of Credit Valuation Adjustments.	No specific comments.	A necessary prior step is to clarify the capital requirements for counterparty credit risk, and how the CVA fits within them. We aim to achieve that as part of the restructuring of the Handbook, and will then address the associated disclosure.
We can clarify whether the disclosed credit rating is meant to be as at signing date or as at balance date.	No specific comments.	We will recommend clarifying this. We believe the appropriate requirement is for banks to disclose the current rating that applies <u>on the date that directors sign the DS</u>. We believe this is consistent with directors having to attest that the DS is not false or misleading as at the date on which they sign it.
We could tidy up the wording of the requirement for a branch's DS to be easy to find on the bank's NZ website.	No specific comments.	We will recommend going ahead with this: we view it as a minor but helpful change that should not be a big burden for banks.

<u>Private reporting of quantitative content of disclosure statements</u>

114. We also consulted on the private reporting of the quantitative content of disclosure statements. Related to the Balance Sheet Redevelopment project referred to above, the Bank is currently looking to develop a private reporting template for the quantitative component of disclosure statements. More specifically, our aim would be to require each bank to enter specified figures from its disclosure statement into an excel template, similar to those currently used for other types of private reporting. The intended benefits would be significant savings in time and resources for the Reserve Bank, and minimising the opportunity for errors in the data collection process.

Summary of submissions and policy decisions

> ***Q18.*** What would be the costs associated with the supplemental private reporting of the quantitative components of disclosure statements?

115. Several banks noted that this proposal would be likely to result in a small increase in costs, but that it was not possible to provide an estimate of the costs without more information on the specific quantitative matters that would need to be taken from disclosure statements and reported in template form.

116. One bank suggested that the proposal could result in initial one-off costs or around $5000, and ongoing costs of around $1000 p.a., Another bank estimated costs of around $2500 p.a., another bank costs of around $2000-$5000 p.a., and another bank suggested costs of around $20,000 (based on 1-2 people working on it 4-8 hours per month).

117. One bank expressed concern that any template might be geared to the circumstances of the larger banks.

118. Several banks and one private submitter supported the idea that this type of template reporting should be made available to the public, as it would be useful for disclosure statement users.[3]

Reserve Bank response

119. The issues and ideas discussed here have helped shape our initial thinking on the “dashboard” discussed under Part 1. We propose to work with industry to more fully explore the potential details of this option. We will likely go ahead with the proposal to ask banks to enter the specified figures into excel templates, but will consult further as we determine the precise figures that will be required. We will integrate this consultation into broader public consultation on the dashboard concept described above.

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[3] At the final industry workshop for banks, one of the participants suggested scaling back off-quarter reporting to just quantitative information, and having the Bank publish this information for industry as a whole. This would save the banks the time that they currently spend entering competitor data (from Disclosure Statements) into their own internal benchmarking templates. Several of the banks agreed that this could be seen as a “quid-pro-quo” for the banks having to enter this information themselves.

Part 2: Format and structure of the Banking Supervision Handbook

Summary of proposals

120. The Banking Supervision Handbook (the Handbook) is the title given to a collection of documents that sets out a range of different matters relating to the Reserve Bank's regulatory requirements for banks.

121. We explained in the consultation document how the Handbook has grown "organically" over time, and how this has led to a number of problems that have been identified by Handbook users and also by the Reserve Bank. For instance, it is not always clear what the legal status is of any given part of the Handbook text, the organisation of subsections and headings within some documents makes them hard to navigate, and the drafting is unclear in places.

122. The consultation document set out how we propose to reorganise the Handbook in a number of ways to address these problems. Among the specific proposals were the following:

- A single document will provide all the material needed by applicants for registration, and will be designed so that banks will not need to refer to it once they have been registered;
- The documents setting out capital adequacy requirements and other related documents will be broken up into a number of smaller "modules";
- A standard organising principle will be applied to each document, to make it clear what the status of the material in the document is, and to facilitate navigation within the document;
- Material that provides guidance will be clearly, separately marked as such, and existing "guidelines" issued by the Reserve Bank under s78(3) of the Act will be re-presented as guidance clarifying how a bank can meet a particular condition of registration; and
- Documents that are cross-referred to in other documents will in future be referred to as "the version applying in the registered bank's conditions of registration", rather than being the version at a specific date. This will remove the need to replace whole documents and associated conditions of registration just to update date references.

123. We also noted in the consultation document that the proposed reorganisation would represent a substantial exercise, and included the outline of a four-stage project running from September 2015 to end-2016.

Summary of submissions and policy decisions

> ***Q19.*** Have you found any other problems with the current format and structure of the Handbook that are not covered by this list?

124. Submitters were largely supportive of the proposed restructuring of the Handbook. Some suggested a few additional issues that could be dealt with in the process. These issues and our responses are summarised in the following table:

Feedback	Reserve Bank response
It could be made clearer what only applies to branches, and what only to NZ-incorporated banks (and both).	This is a worthwhile objective, and we will factor it into the restructuring as far as we can.

Feedback	Reserve Bank response
Illustrative tables are useful: we could use them more.	This is also a worthwhile objective that we will factor into the restructuring as far as we can.
We should just cross-refer to other legislation and standards, rather than copying text across.	This is a useful general principle for managing the length and readability of handbook material, although we believe there may be times when it is helpful to have the full text of the other material referred to, to help understand any discussion or guidance on the material.
The glossary was welcomed, and one submitter noted that we should define as many terms as possible, eg “credit event”, to provide greater certainty.	We agree with defining as many terms as possible, although some terms (such as “credit event”) may not be susceptible of a hard and fast definition. More use of guidance may be helpful in such cases.
It would be useful to be able to find the rationale for policies (and updates) more easily: could we have an extra column in the handbook index with links to the consultation documents and feedback leading to the final policy?	We agree that this would be a desirable change, and will aim to back-load previous consultations and feedback statements going back five years. (This may take some time to achieve.) This is discussed in further detail under Part 4: The Reserve Bank’s policy making approach.

Q20. What do you see as the costs or risks arising from this proposed restructuring? Do you have any alternative suggestions for making it easier for new applicants to know what is expected of them, and for registered banks to be clear about the continuing requirements applying to them?

125. A number of submitters noted the risks of unintended consequences, although it was acknowledged that we have reasonable plans to mitigate those. One bank suggested we get an independent legal review to check whether requirements have changed unintentionally in the re-drafting. Banks will need time to update their internal compliance registers, and there needs to be clarity all the way through the process about which document applies to which bank.

126. There was some support for retaining a separate document with a list of the standard conditions of registration applying to different classes of bank. (And it was noted that the current list in BS1 includes liquidity conditions for branches, which we have never imposed, so they should be removed from the list.)

Reserve Bank response

127. The Reserve Bank is aware of the risks of unintended consequences, and will ensure that sufficient review processes are in place to ensure that any actual changes in requirements are clearly flagged in the consultation process. The timetable is not driven by any policy imperatives, and we recognise the need to allow banks sufficient time for implementation as well as for consultation.

128. We agree with the proposal to keep a separate document within the new handbook that sets out the standard conditions of registration. This aligns with removing standard conditions of registration from banks’ disclosure statements, as noted above.

Q21. Do you have any comments on the proposed restructuring of the documents in the capital adequacy framework?

129. The proposed modular approach was generally accepted. There were some alternative suggestions given on how to group the material outside the core definitions for calculating ratios, i.e. the notification and approval requirements, and the crisis management material. One suggestion was to split the material into "inputs" (capital calculations) and "outputs" (capital monitoring and management).

130. BS2B was noted as the main area of obscurity: submitters have given us some specific examples to work on. It was noted that removing FIRB will help, but will need to be done carefully, as it not always clear which sections only relate to FIRB. Having a clear map of Handbook changes will help.

131. Some banks have suggested that some of their staff could be seconded to the Reserve Bank on a rotating basis to help with the re-working of the Handbook, or that a small working group of employees from some of the banks could be set up to review drafts as they are developed.

Reserve Bank response

132. The Reserve Bank will take the alternative suggestions for the grouping of the capital modules into account as it works through the current material. We fully recognise that it is not clear which sections only relate to FIRB, and the importance of keeping a clear and comprehensive map of the changes to the Handbook. We do not think it is appropriate for bank staff to be directly involved in the re-drafting work, but will consider setting up a small drafting review group.

Q22. Do you have any other suggestions for how a standard handbook document should be structured? Of the proposed numbering structures in Sample 1 and Sample 2, which do you prefer? Can you suggest any alternative numbering approaches that you believe would work better? Do you have any other suggestions for renaming the Handbook itself and replacing the BS numbering convention?

133. There was general support for our approach here as well, with some suggestions on the detail. On the layout / numbering style, there was strong preference for our Sample 2, although one bank proposed a third option. It was suggested that we should use diagrams, tables and flowcharts as much as possible to help provide clarity and simplicity. The suggestion for labelling guidance is welcomed, although there was a question whether we would "grey out" a whole document if it is all guidance (which some documents will be).

Reserve Bank response

134. We think the alternative numbering style suggested has some advantages over both of the options that we proposed (a sample is included at Appendix B). We propose to start the re-drafting work on sections of BS2A and BS2B using this style, although remain open to improvements as we go along, in light of experience with the work and feedback from users.

135. We will make a final decision on whether any guidance-only documents should be entirely greyed out, as we work our way through the handbook. This will depend on various factors, including how many documents this will apply to, whether there is a different way to clearly label a whole document as guidance, whether it would be

confusing not to have guidance all labelled in the same way, and whether there may be an overall better alternative way of identifying guidance.

> ***Q23.*** Do you have any concerns about the proposal to remove from the Handbook guidelines issued under s78(3) of the Act? Do you have any other suggestion for how the Reserve Bank could most effectively require improvements by banks in more subjective areas such as risk management?

136. A number of banks support our proposals in this area. One noted that there needed to be a balance in the handbook between simplicity and sufficient detail, and that there was always going to be some need for banks to discuss interpretation of particular definitions with the RB.

137. One bank was not happy with our proposals (specifically, to convert current guidelines issued under s78(3) of the Act into short high-level conditions of registration with supporting guidance on how we expect the conditions to be met). This bank regards this as outside the scope of the Handbook restructuring, as it means actual changes in requirements, and would need careful consideration to ensure ongoing compliance. We should consult separately on the wording of any such new conditions.

Reserve Bank response

138. We accept that this is likely to mean some change in effect at the margin (the aim is to make this guidance more effective). We will carry out full consultation on the form of the conditions of registration in question and on the associated guidance, to ensure that banks understand the objectives of the conditions, and that they can realistically comply with them. We do not agree that this is outside the scope of the stocktake. It does not aim to change the fundamental building blocks of the regime, but is a necessary step to clarifying the intent of expectations that are currently expressed as guidelines issued under s78(3) of the Act.

> ***Q24.*** Can you see any drawbacks with this proposed approach to handling different versions of a given document?

139. The majority of banks supported these proposals as set out in the consultation document. One bank suggested that we should not need to cross-refer between different handbook documents to define terms so much in future, if we make full use of the new Glossary as the repository for defined terms.

140. Two banks questioned why we need to refer to specific versions of our policy documents in banks' conditions of registration, when general legislation does not do this. They noted that if we dropped this practice, and if we always ensured that policy changes applied to all affected banks at the same time, then we would not have to update banks' conditions whenever we introduced a new policy. One of them also noted that these updates would not then need to be disclosed as a change in CoRs in each bank's disclosure statement.

Reserve Bank response

141. This alternative approach suggested for updating policy requirements would on its own be more efficient than the current approach, but we believe that it would only be achievable within a legislative framework completely different from the one currently provided by the Reserve Bank of New Zealand Act 1989 (the Act). The requirements set out in our policy documents are only given legal effect by being referred to in a

condition of registration. Such requirements are in effect incorporated by reference into the associated condition, and a change in the requirements therefore amounts to a variation in conditions of registration, which is governed by s74 of the Act. General legislation comes into force by different mechanisms.

> ***Q25.*** Are there any ways in which you think the current layout of the disclosure Orders in Council, as presented on the Reserve Bank's website, could be improved?

142. There was only one suggestion on the layout, which was that it would be useful to have the disclosure requirements for each quarter grouped together. It was noted that the better use of definitions and the glossary should also have benefits for the Orders in Council. There was a suggestion that online navigation could be added to our working copies of the OICs (such as "click-through" from the contents page).

Reserve Bank response

143. We note that each of the Schedules to the disclosure Orders in Council is headed up by a title clearly indicating whether it applies to the full year, half year or off-quarter disclosure (or a combination of those). But we will consider whether some re-grouping would improve clarity. We agree that online navigation could be added in our working copies, and will look at the feasibility of this when we are upgrading the website presentation of the handbook.

> ***Q26.*** Could you please give us any comments on the proposed grouping of the work in the different stages of the migration plan, and on their respective timings?

144. The migration plan was broadly welcomed. The importance of no overlaps between the consultation stages was emphasised, so that if one stage falls behind schedule, the later stages should also be delayed. One (small) bank noted it would be helpful not to have consultation periods during the months just after quarter-ends (eg April), given competing demands on limited staff time.

145. One bank suggested including a transition period to give banks time to move across from their current compliance frameworks. It will be important for us to maintain a detailed change register.

Reserve Bank response

146. We intend the stages of the migration to be interdependent. If one stage is delayed the following stages will be postponed correspondingly, and if banks need additional transition periods between stages, we can incorporate those as well. The attached Appendix C sets out a revised version of the migration plan, with timings updated to reflect the fact that we have not yet started substantive drafting work on Stage 1, and also to build in some longer consultation periods, in line with the changes in our policy-making approach. The plan now extends to mid-2017, but will remain dependent on resource constraints and other work priorities.

Part 3: Capital requirements

Summary of proposals

147. Although the substance of the Reserve Bank's capital requirements is outside the scope of the regulatory stocktake, the Reserve Bank noted in the consultation document that it is keen to clarify these requirements in order to improve accessibility.

The structure of the Banking Supervision Handbook, including its capital adequacy components, was dealt with in Part 2 of the consultation paper, with the responses and policy decisions as noted above.

148. Apart from this, under this heading the consultation document mainly referred to separate initiatives outside the stocktake, and so had no specific consultation questions.

Summary of submissions and policy decisions

149. A few responses from banks noted the proposed future work to review the current 1% limit on banking groups' insurance business, and expressed their interest in being involved in the work when it gets under way. There are no policy decisions as such under this heading.

150. The follow-up work on these issues is noted in Appendix D: Stocktake Register of Issues Addressed (marked as "follow-on initiatives"). Going forward, we will transfer these follow on initiatives to the "Future Policy Work" table on the Consultations and Policy Initiatives section of our website.

Part 4: The Reserve Bank's policy making approach

Summary of proposals

151. In the initial industry consultation, a number of our stakeholders indicated an interest in greater transparency regarding the Reserve Bank's policy making processes, as well as enhanced engagement with industry regarding new policies or policy changes.

152. The Reserve Bank is proposing to take a number of steps to address these issues, including:

- Publishing a new document that describes our approach to policy-making and indicative timeframes for consultations (the outline for a possible draft of this document is included in Appendix E of this paper);
- Revising the content of the website to make it more user-friendly (this will build to some extent on the changes to the structure and presentation of the Banking Supervision Handbook);
- Providing a more dynamic "Consultations and Policy Initiatives" section on our website by updating it on an at least quarterly basis to include current initiatives of the various departments within the Reserve Bank working on matters relating to bank regulation and supervision;
- Developing an "Industry Update" newsletter for banks (based on the current "Insurance Industry Update") to keep them informed about our work;
- Exploring ways of more proactively using the Banking Forum[4] to promote coordination among regulators regarding timelines for consultations; and

[4] The Banking Forum is a subcommittee of the Council of Financial Regulators (CoFR), which is a venue for government departments and agencies with responsibility for, or an interest in, the financial sector. The members of CoFR are the Reserve Bank, Treasury, Ministry of Business, Innovation and Employment, and Financial Markets

- Streamlining the process for amending regulations by eliminating some of the current need for changes (for example as a result of cross referencing between documents), and making the change process more transparent by providing a "change register" that shows amendments to prudential requirements that have been made over time.

153. In the consultation document, we outlined a number of policy making objectives and the related proposals that had been discussed at the industry workshops. The objectives were the following:

    1. Improve Forward Planning: Provide clearer information to industry and better coordinate within the Reserve Bank and with other regulators regarding timelines and consultations including:

        - Clearer information via the Reserve Bank's website
        - Creation of an industry newsletter
        - Enhanced coordination with other regulators
        - Better use of existing supervisory communication channels

    2. More clearly communicate basic principles of our policy making approach, including timeframes for consultations; and

    3. Streamline process for amending regulations.

> ***Q27***. Do you agree that these are the correct proposals to consider? If not, why not?
>
> ***Q28.*** If possible, please quantify the benefit of the specific options presented above. Which of the specific proposals do you see as the most effective?
>
> ***Q29.*** Are there other options we should consider to solve the problem (either as we have identified it in the document, or as you identify it)?

154. Below is a detailed summary of the submissions we received and the policy decisions we are proposing.

Authority. These four organisations are also permanent members of the Banking Forum. The Inland Revenue Department and Ministry of Justice are associate members of the Banking Forum.

Objective 1: Forward Planning

Feedback	Reserve Bank response
Banks were generally appreciative of the changes proposed and the changes that have already been made to the Reserve Bank website. The "Consultations and Policy Initiatives" page of the "Banks" section of the website now includes the projects of a number of different Reserve Bank departments (Statistics and Macro-financial Department) and has been updated more regularly in recent months. In terms of the website, one bank suggested a "rethink of the website to be more user-friendly." In terms of the frequency of updates, it noted that "as soon as practicable" would be preferable to "at least quarterly" updates. They also noted that it would be useful to have our communications strategy posted on our website and that more plain English and improved navigation would make the website more effective. Finally, this bank noted that Reserve Bank has a role in educating consumers: "With significant attention around issues like the Auckland housing situation and OBR, we consider there is room for a greater educational focus in Reserve Bank communications."	We appreciate the positive feedback and will continue to make enhancements to the Reserve Bank Website, focusing on the needs of target users, particularly, navigability and plain English drafting. We will continue with our efforts to keep the website as dynamic as possible, seeking to make updates "as soon as practicable" though only committing to "at least quarterly." We will also continue providing the date of the last update of our "Consultations and Policy Initiatives" page. We have noted the comments regarding our educational focus and will take these into consideration when developing content for the distinct users of our website.
A number of bank submitters were supportive of the creation of an industry newsletter. One bank suggested including the minutes of the Banking Forum meetings in this newsletter.	We will aim to publish an industry newsletter for banks twice a year, timed to complement our Financial Stability Report. The FSR is currently published in May and November so our target months for publishing the newsletter would likely be February and August. We will aim to publish the initial newsletter in August of 2016. We will model the initial newsletter on the one we currently publish for the insurance industry but will modify the structure over time, integrating user feedback.

Feedback	Reserve Bank response
One submitter noted that it "has observed, and commends recent improvements in the Reserve Bank's policy making approach." They also applauded the efforts of the Banking Forum but noted there was still scope for further collaboration. They would like to see a combined "radar" of upcoming consultation and implementation across the Banking Forum members and suggested a calendar format may be the most useful way to present this. Individual banks also indicated support for some sort of calendar approach. One bank mentioned a desire to see greater coordination with APRA in regard to timeframes on consultations, to the extent possible. A number of banks noted the importance of coordination among regulators around consultations, but also around implementation of new initiatives, recognising the stress that regulatory changes put on front-line teams. A number of banks noted the challenges created by the recently overlapping LVR change implementation, stocktake consultation, balance sheet collection project, BS5/AML consultation and the outsourcing consultation.	We will also continue with our efforts to improve coordination internally within the Reserve Bank and also externally via the Banking Forum. As Chair of the Banking Forum, the Reserve Bank would welcome input from NZBA or from industry more broadly regarding specific issues they think need to be addressed at the quarterly meetings of the Forum. We have invited NZBA to attend the Q1 and Q3 meetings of the Banking Forum for 2016. We believe NZBA's participation will help the Forum to more effectively meet its objectives.

Objective 2: Communication of Basic Principles

Feedback	Reserve Bank response
The submissions were generally quite supportive of the proposed new "Statement of Policy Making Approach" (Appendix F of the consultation document). One bank noted that the most effective and promising of the proposals would be adhering to the basic principles of policy making. This bank	We will take these comments into consideration as we finalise the draft Statement of Approach to policy making. We will likely maintain much of the current language, as the commitments are subject to a number of constraints, which are outlined in the document.

Feedback	Reserve Bank response
also noted that the language from the Statement of Approach to Policy-Making relies heavily on terminology such as “whenever possible”, “whenever available” and “subject to available resources”. They noted that these qualifiers water down the value of the commitments and cited the “last minute changes to capital rules without notice under BS2 in response to the LVR rule” and the additional attestations required under BS16, despite the statement from the RB that “the existing process is working well.” They also suggested we outline what we consider to be the difference between policy and “policy making”. Finally, this bank also felt it would be valuable to have a clear avenue for challenging policy development that hasn’t followed the principles. They suggested that this could take the form of a forum for regular reporting on the RB’s compliance with these principles, and suggested identifying (up-front) criteria that would justify a departure from the stated principles.	In terms of the avenues for challenging policy development, the Reserve Bank always welcomes feedback either directly from banks or via industry bodies (e.g. the NZBA).
A number of submitters commented on the effectiveness of recent industry workshops at early stages in the consultation process (e.g. stocktake and LVR changes).	We appreciate the positive feedback on our recent workshops and will continue seeking to conduct workshops wherever appropriate.
A numbers of banks indicated that a 4-week consultation would only be appropriate under extraordinary circumstances. These submitters asked that 6 weeks be the minimum period for consultation and that the standard consultation timeframe should be 8-12 weeks depending on the significance.	We will modify the document to state that “our aim is to consult over a 6 to 10 week period depending on the significance of the proposal.” We will not, however, change the caveat that there may be rare cases where circumstances mean we adopt a shorter consultation period. In these cases, we will seek to be clear about why a longer consultation period is not possible. We will also modify the document to indicate that the 6 to 10 week period is for the “primary” consultation. The Reserve Bank often conducts multiple rounds of consultation. We would not expect to provide a minimum of 6 weeks for second or third round consultations. These are instances in which we would expect to adopt a shorter

Feedback	Reserve Bank response
	period. Again, if we adapt shorter periods, we will seek to be clear about our rationales for doing so.
One bank also suggested that submissions should be available online, in addition to the Reserve Bank publishing the summary of submissions. This bank noted that this is the standard practice for public consultations run by other government departments (e.g. the Ministry of Business, Innovation and Employment).	Our current approach is based on our understanding that respondents prefer to keep their submissions confidential. Prior feedback indicated that banks, in particular, were reticent to share cost information and the Reserve Bank is concerned that the publication of submissions would impact the quality and detail of the submission feedback. On the other hand we also recognise the importance of transparency in the policy-making process, so we will return to this issue and consult on a revised approach under which the default position would be that all submissions are published on our website (although submitters could ask to have any confidential information in submissions redacted). We will add this issue our register of "Future Policy Work."
One bank also suggested that the Reserve Bank establish a process for undertaking a thorough cost-benefit analysis conducted by an independent party, such as Treasury. Another bank noted that requiring robust Regulatory Impact Statements (RISs), not implementing change unless the benefits outweigh the costs, and having a formal process for post implementation reviews would have the most material impact. One bank asked for a requirement that the Reserve Bank publish a summary of submissions and responses (including rationales) to viewpoints not accepted. One bank suggested good regulatory practice should require the Reserve Bank to conduct a RIS on any specific (bespoke) CoRs it imposes. This bank also commented that RISs should be conducted "for each major regulatory change rather than in general" and should also assess how the probability of financial stability crisis events has	As stated in our outline draft statement of policy making approach, the Reserve Bank seeks to follow the "Best Practice Regulation" model developed by the New Zealand Treasury wherever possible. We carry out regulatory impact analyses on all of our regulatory policies, except those of a minor or technical nature. We currently aim to publish summaries of submissions that take into account responses to viewpoints not accepted. We would welcome specific feedback from industry in cases where they feel this is insufficient. We do not publish regulatory impact analyses on institution-specific Conditions of Registration, but do seek to explain the justification for these privately to affected institutions. On the issue of Regulatory Impact Statements, we will make historical Regulatory Impact Statements (RISs) and consultations easier to find on our website. We believe some of the issues raised by banks relate to the difficulties in finding historic RISs and linking them to current

Feedback	Reserve Bank response
been reduced.	policies. We will aim to create a simple “Register of Closed Consultations,” going back 5 years, that provides the Name of the Consultation, relevant Discussion Document, Summary of Submissions and Policy Decisions and (if when available) the full Regulatory Impact Statement (RIS). Especially for new entrants into the sector, we recognise that this information may currently be difficult to find, and connect with the relevant policy, as our website is currently organised. We will link this to the sections of our website that describe each of the policies (see Handbook section above). We will begin doing this on the “banks” section of our website and will adopt this in other sectors in a later stage.

Objective 3: Streamlining of the process for amending regulations

<u>Proposal and feedback</u>

155. As noted above, in the consultation document we proposed streamlining the process for amending regulations by eliminating some of the current need for changes (for example as a result of cross referencing between documents), and making the change process more transparent by providing a "change register" that shows amendments to prudential requirements that have been made over time.

156. Two banks commented that, of all of the proposed policy making changes, these would have the most benefit.

157. One bank also noted that it would be useful for the website to retain copies of more than the previous version of handbook document (e.g. in a separate archive).

<u>Reserve Bank response</u>

158. We will move forward with the proposed actions, including:

- Bundling minor changes and seeking to publish them (or at least signal them) on a quarterly basis;
- Making tracked changes versions of documents more readily available; and
- Revising our drafting of documents to minimise the need for updates if reference documents are updated.

Collectively, our aim with these changes will be to minimise the number of minor or technical updates to documents and to increase the overall clarity and efficiency of our approach.

Part 5: Differentiated regulatory approaches in the banking prudential regime

Summary of proposals

159. As part of the stocktake work, the Reserve Bank reviewed the nature of the differentiation between different classes of banks under the prudential regime. The consultation document reported on the outcome of this review, and highlighted some key principles that underlie the differentiated approach.

160. Specific proposals coming out of this analysis were that we would:

- Reduce disclosure requirements applying to branches, both in line with the options for changes to the disclosure regime discussed above, and in some areas of more specific detail;
- Consider whether the application thresholds for the outsourcing and OBR requirements should be made the same (as part of the separate review of our outsourcing policy for banks that is currently under way); and
- Assess whether to extend a form of one week liquidity mismatch ratio to branches (as part of planned work to consider whether the Reserve Bank should modify its liquidity policy in light of the new Basel III requirements).

Summary of submissions and policy decisions

> ***Q30***. Do you have any comments on this analysis of the points of differentiation in the Reserve Bank's regulations for banks? Are there other action points that you think the analysis points to?

161. The analysis in this part of the consultation document was generally welcomed. A number of banks said that their starting point was that there should be a level playing field, but they recognised that some differentiation of approach had its place in achieving good policy outcomes. There is a fine balance to be achieved, and it is worth regularly reviewing whether the points of difference remain appropriate. Some submitters said they would welcome a clearer articulation in our policy documents of the rationale for differentiation.

162. There were no objections to the proposal to extend liquidity requirements to branches, and a few votes in favour, although one branch noted there needed to be further consultation on this as well as cost-benefit analysis of going further than the Basel III liquidity framework. One bank felt that it should only apply to branches which take senior-ranking funding from New Zealand parties (including from depositors).

163. One (large) bank did not agree with removing off-quarter disclosure statements for branches and smaller local banks: they believe that any market- or self-discipline rationale for keeping it for the bigger banks applies equally to them. The rating agency that submitted also believe that all banks (including branches) should report a baseline of information, so that the market has an understanding of where risk is being taken on across the New Zealand banking sector as a whole.

Reserve Bank response

164. We note that the project to consider whether we should replace our current minimum liquidity ratios with the Basel III requirements will include a full consultation process and regulatory impact assessment, and that the possibility of extending the one week mismatch ratio to branches will be included within that. The costs and benefits of going beyond the Basel III minimum standards will be assessed on their own merits. We will also consider the case for excluding branches that do not take senior-ranking funding from New Zealand parties.

165. The decisions on whether to remove off-quarter disclosure statements from branches and smaller local banks is discussed further in the disclosure section (above). We note that risk taken on by a branch is less important to the New Zealand banking sector than it may be to the home country banking sector.

Part 6: Miscellaneous changes to Bank policies and regulations

Part 6 (miscellaneous) – (1) Refinements to director and senior manager non-objection process

Summary of proposals

166. As part of the stocktake we identified a number of issues with the current process for assessing the suitability of banks' directors and senior managers. Specifically:

- The definition of senior manager can sometimes cover persons who do not have, or are unlikely to have, significant influence over a bank's financial soundness (e.g. a bank's Head of Change Management or a bank CEO's Chief of Staff);

- There is a lack of any requirement to ensure the ongoing suitability of directors or senior managers after they have been appointed; and

- The existing framework may raise a number of broader risks or inefficiencies. For example:

  - It may raise moral hazard issues by creating a perception that appointments were being approved by the Reserve Bank (a particular concern here is that stressing that the process provides a form of negative assurance may be insufficient to change this perception); and

  - It may create unnecessary duplication and inefficiency by not being more integrated with the internal processes used by banks to assess suitability.

167. As noted in the consultation document, we do not propose at this stage to make any changes as a result of the last of these points (i.e. that the existing framework may raise a number of broader risks or inefficiencies), although we may give further consideration to this in the longer term. One particular issue we would like to consider is the consistency of approaches across the different prudential regimes (eg banks, NBDTs and insurance). As it currently stands, each regime has a different approach to this issue and greater consistency, or at least clarity around the reasons for the different approaches, would be beneficial. Fundamental changes to any of the models would require changes to the Reserve Bank's legislation, however, which is outside the scope of the stocktake and was therefore not part of this consultation.

168. However, in the consultation document we did canvass a number of options for potential changes to the definition of senior manager. In addition to the status quo, these options were:

- Defining senior manager as certain key office holders. For example, the Chief Executive Officer, the Chief Financial Officer, the Chief Operating Officer and the Chief Risk Officer, or persons with equivalent responsibilities (our initial preference); or

- Defining senior officer as a person occupying a position that allows the person to exercise significant influence over the management or administration of the bank (for example, a chief executive or a chief financial officer).

169. We also canvassed a number of options around providing for some kind of ongoing requirement to ensure the continued suitability of directors and senior officers who have already been appointed. In addition to the status quo, these options were:

- Requiring directors to attest in disclosure statements that they have effective systems and processes in place for ensuring the ongoing suitability of directors and senior managers, and that those systems and processes are being correctly applied (our initial preference); and

- Requiring banks to notify the Reserve Bank when any director or senior manager is subject to criminal, civil or disciplinary proceedings, or has been involved in the management of a failed institution.

Summary of submissions and policy decisions

> ***Q31.*** Do you agree with the problems we have identified with the suitability assessment process of a bank's directors and senior managers? Are there other issues with this process that we should be considering?

170. There was general agreement with the issues we had raised. One branch asked whether this analysis and the proposals made were intended to include branches: they would prefer to keep the status quo.

171. Two banks noted the variety of legislation under which suitability checks apply,[5] and suggested there was a strong case for consistency of approach, and ideally for suitability approval under one regime to provide approval under others. (Although they recognised this was beyond the scope of the stocktake.) They also expressed a preference for relying first on the checks that a bank has carried out (as with our insurance regime).

172. Two private submitters submitted alternative views. One private submitter thinks the Reserve Bank should have no involvement in vetting of board and senior management appointments. Another private submitter suggested that rather than active Reserve Bank involvement, there should simply be automatic disqualification for an offence involving dishonesty within the last 10 years, and a requirement for relevant individuals to post their CV on the registered bank's website.

> ***Q32.*** Do you agree with our preferred option for changes to the definition of senior manager? If not, which option do you prefer?

173. There was unanimous preference for narrowing the scope of the definition of senior manager, and doing so via a specified list (our preferred option).

174. The status quo was viewed as burdensome and hard to justify. It was thought that Option 3 (using a "significant influence over the management of the bank" test) would to be too subjective, create uncertainty and lead to different outcomes in similar cases across banks.

175. Banks mainly agreed with the list of posts under Option 2 (CEO, CRO, CFO, and COO or their equivalents). Two banks noted that they did not currently have a "COO" at the moment, but have the responsibilities grouped in different ways: one of them previously had a COO but also a separate CIO who did not report to the COO. One of these suggested that only CEO, CRO and CFO should be captured, and noted that the PSD engagement plan involves meeting each of them. There was also a request that we tighten the drafting of "or equivalent", to avoid uncertainty.

176. One bank was concerned that just using job titles would risk this approach being subverted, and suggested linking the roles to key areas of concern (e.g. using the "prudent business" matters in s78 of the Act).

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[5] See for example, the Reserve Bank of New Zealand Act 1989, the Insurance (Prudential Supervision Act 2010, the Financial Markets Conduct Act 2013, the Anti-Money Laundering and Countering the Financing of Terrorism Act 2009, and the Financial Service Providers (Registration and Disputes Resolution) Act 2008.

177. One bank also noted that other Acts use an approach like Option 3 (a “significant influence” test), so it would help if we could confirm that any of the individuals we capture under Option 2 will also be caught under the definitions in those Acts.

> ***Q33.*** Do you agree that there should be an ongoing assessment of directors and senior managers’ suitability? If so, do you agree with our preferred option for how this should work, or would other options be more appropriate?

178. Most banks accepted the desirability of formalising ongoing assessment in some way. Two banks preferred adding a specific attestation on this matter to the regular attestation in disclosure statements. Two banks preferred requiring banks to notify the Reserve Bank when there is a problem with a director or senior manager, while four banks suggested alternative approaches involving different types of notifications to the Reserve Bank.

179. Drawbacks noted with the attestation option were that it would add an extra layer of process and complexity (contrary to the stocktake’s objectives), that it would be essentially circular (directors signing off on themselves), that it would be wrong for director liability to arise from publicly signing off a matter that is so subjective, and that public disclosure of this attestation would not contribute to the financial stability objectives of the disclosure regime.

180. A few banks favoured the idea of something like our current insurance regime: requiring banks to have an internal policy of continuing assessment of directors and senior managers, with annual attestation to the Reserve Bank that it has been properly run.

181. One bank was against any change, arguing that the case was not made that this would ever make a difference in practice, and that it was not justified in terms of the overall financial stability objective.

182. Another bank did not like the attestation option, but still preferred it to a requirement to notify the Reserve Bank in certain circumstances, as they noted that the requirement for a bank to notify the RB of a problem arising with a director or senior manager would have to be imposed by a condition of registration. This would be complex.

183. Finally, one submitter recommend that the Reserve Bank recognises Chartered Membership of the Institute of Directors: members have to attest annually to being of good character (defined according to a number of specific matters) and achieving professional standards, including completing continuing professional development.

Analysis and conclusions

184. For locally incorporated banks we propose to adopt the approach of defining senior manager as one of a list of specified office holders or persons with equivalent responsibilities. For branches, we propose to retain the current approach where the New Zealand CEO is the only senior manager subject to a suitability assessment.

185. We note that this was our preferred option in the consultation document, and there was strong support for this approach from submitters. We consider that this approach will better focus suitability assessments on those key office holders who are most likely to influence a bank’s soundness (both from a financial and a governance perspective).

186. There are two main design issues associated with this option. The first is which office holders should be covered by the definition. Our starting point on this issue is that the

CEO, CFO, CRO, and COO should be the named office holders. However, we will give further consideration as to whether a very limited number of additional office holders, such as the Head of Internal Audit, should be added to this list.

187. The second issue is to specify what we mean by these office holders "or persons with equivalent responsibilities". Our preferred approach to this issue is to provide guidance on the meaning of "persons with equivalent responsibilities". At this stage, we anticipate that this guidance would list the key roles of the listed office holders (CEO, CFO, etc) and make it clear that anyone else carrying on one or more of these roles would be a "person with equivalent responsibilities". We propose to consult with banks early in the new year on:

- Any additions to the proposed list of office holders;
- The specific drafting of the change to the condition of registration; and
- The content of guidance on the meaning of "persons with equivalent responsibilities".

188. In respect of the ongoing assessment of directors' and senior managers' suitability after their appointment, we do not support the option of having certain trigger points that require banks to report to us on suitability issues, as we are concerned that these trigger points may not cover all of the circumstances where suitability issues may arise (or alternatively, may be cast so broadly that they create unnecessary or redundant reporting requirements). However, we do note the additional cost associated with the attestation approach.

189. Given this context, our proposed approach is to add a requirement for banks to have internal processes in place to ensure the ongoing suitability of directors and senior managers, and that these processes be complied with. This would be implemented by a new condition of registration, with background material added to BS14 (at least initially). No separate attestation around the effectiveness of these processes would be required under this approach (instead it would be covered as part of more general attestations relating to compliance with conditions of registration, and risk management systems). This approach may also be buttressed by our providing high level guidance on our expectations around how these internal processes should work.

190. We see this model as a more cost effective means of achieving the intended outcomes, and propose to consult with banks on its specific design in the new year.

Part 6 (miscellaneous) – (2) Issues around breaches of conditions

Summary of proposals

191. The stocktake also identified two specific issues with the current arrangement for disclosing and reporting breaches.

192. Firstly, while the Reserve Bank is privately notified of any breaches that might occur, there is no formal legal obligation for banks to report breaches to us under existing legislation. In response to this issue, we consulted on an approach whereby we use our existing information gathering powers under the Reserve Bank of New Zealand Act 1989 to require a bank to report any actual or potential breach privately to the Reserve Bank as soon as practicable after it occurs.

193. Secondly, some banks have suggested that the need to disclose breaches in disclosure statements can be disproportionate where these breaches are of a very minor or trivial nature. We consulted on the approach of considering how conditions of

registration are drafted in future to reduce the risk that genuinely trivial matters could result in technical breaches. We also noted in the consultation document that we were not proposing some form of materiality threshold for when breaches had to be disclosed.

Summary of submissions and policy decisions

> ***Q34.*** Do you agree with the potential problems we have identified around the disclosure and reporting of breaches of conditions of registration?

194. Of eight banks that gave a view, seven agreed with the issues identified (the desirability of formalising breach reporting, and the need to improve the problem of breaches arising from trivial matters).

195. One bank does not see the need to formalise reporting of breaches. They suggest that this is better managed via our supervisory relationship with banks, by the Reserve Bank making it clear that we expect notification, and that we are more likely to take a hard line in response to a breach that has not been promptly notified to us. They asked what the evidence was of a problem to be addressed, and wondered what the RIS will look like for this change.

> ***Q35.*** Do you agree with our proposal to create a standing obligation to disclose any actual or potential breaches privately to the Reserve Bank as soon as they occur? What are the potential costs and benefits of this option?

196. Most banks agreed with the proposal in principle, but many of them raised concerns about getting the requirement exactly right.

197. First, they argued that we need to be clear what we mean by a “potential” breach. Banks are happy if this covers the case where a breach has not yet occurred but inevitably will. If it goes wider than that, the requirement becomes more subjective, which is problematic for a formal reporting requirement with penalties attached. A few banks suggested that a “potential” breach could refer to an issue which may or not be a breach but should be notified to the Reserve Bank, so that we can have a discussion with the bank on whether it is or not. One bank suggest reporting should be required only for “actual material breaches of a factual nature that have not been rectified within 10 working days of their occurrence”.

198. Second, on timing, a requirement to report “as soon as the breach occurs” is viewed as difficult to apply in practice. One bank noted for instance that they have different controls for different conditions, with internal reporting at either weekly, monthly or quarterly periods. Another bank’s suggested wording could be one way to deal with most of the issues raised: “as soon as practicable after the bank becomes aware of it”. Another bank noted that there is a particular practical issue for branches (when a breach can be at the whole bank level): their suggested wording is “as soon as NZ branch management becomes aware”.

199. Another bank asked further questions: should we require reporting within X number of days, to give the bank time to investigate the (potential breach) and obtain all the information required by the section 93 notice? Would we require the bank to notify its board before the Reserve Bank? They also requested that we align as far as possible with analogous requirements on reporting to the FMA, under the Financial Markets Conduct Act 2013, and that if we put this in place, director attestation on Conditions of

Registration compliance could be cut from the off-quarter disclosure statements (if that is kept).

> ***Q36.*** Do you agree that it would be better to ensure that the drafting of conditions of registration minimises the scope for genuinely trivial matters to result in breaches, rather than providing some form of exception to the requirement that all breaches must be disclosed?

200. Banks were mostly in favour of changing the drafting of some conditions of registration to reduce the scope for breaches arising from genuinely trivial issues.

201. Another bank noted that the financial press seem to focus particularly on reporting of breaches when they look at disclosure statements, without usually giving any analysis of the seriousness of the breach, and that they also then comment on the Reserve Bank's failure to take any action against a bank that has breached a condition of registration.

202. Most banks were not keen on a materiality cut-off for disclosure, if it meant that the decision on whether a breach was "genuinely trivial" was left up to them. They noted that this would lead to different interpretations across banks, and could open up avoidance opportunities. One bank went so far as to say that they preferred the status quo to this option: they pointed to the resources they currently expend on deciding whether matters are material enough to need disclosing under an NZX listing.

203. A few banks came up with suggested refinements on the materiality cut-off idea that worked better for them, all along broadly the same lines. The basic idea is that banks would have to report all breaches to the Reserve Bank, and it would then be up to the Reserve Bank to determine which have to be disclosed.

204. Refinements on this approach included the suggestion that the Reserve Bank publish guidance on what our tests are for whether a breach is material. They noted that possible measures of materiality are:

- Number of customers affected;
- Whether material to the bank's financial position or balance sheet;
- Whether the bank had acted contrary to the policy intent behind the specific requirement; and
- Whether the breach posed a risk to customers, shareholders, the bank itself or the wider banking system.

205. Another refinement was suggested to mitigate the increased moral hazard that this option would create for the Reserve Bank. Under this suggestion, banks would notify the Reserve Bank of all breaches, but they would give the Reserve Bank notice of their intention not to disclose certain breaches on materiality grounds: we would then have the right to override their view (ie make them publish), rather than having the up-front responsibility for the decision.

206. Coming from a rather different angle, one bank argue that the imposition of a specific condition on an individual bank should be subject to an appropriate RIS to ensure the Reserve Bank does not impose conditions where they are not needed. They also argue that where a condition is subject to interpretation, we should always take the most liberal interpretation until there has been formal clarification.

Analysis and conclusions

207. There was general support from submitters the principle of setting up a formal standing obligation for banks to privately report breaches to the Reserve Bank. We intend to adopt this proposal by issuing a notice to all banks under section 93 of the Reserve Bank of New Zealand Act 1989.

208. Submitters' comments on this proposal focused on the specific design of this proposal. Our starting point on this issue is that the wording of the obligation should largely align with the comparable reporting obligations in the Financial Markets Conduct Act 2013. The relevant reporting obligation in the Financial Markets Conduct Act 2013 is in section 412, and is worded as follows:

> "**Section 412 Licensee must report certain matters**
>
> ……
>
> (2) Subsection (3) applies if a licensee believes that:
>
> a. the licensee or an authorised body has contravened, may have contravened, or is likely to contravene a market services licensee obligation in a material respect; or
>
> b. a material change of circumstances has occurred, may have occurred, or is likely to occur in relation to the licence;
>
> ….
>
> (3) The licensee must, as soon as practicable after the licensee forms the belief referred to in subsection (2), send a report containing details of the belief, the licensee's grounds for the belief, and all other prescribed information—
>
> a. to the FMA;
>
> ….."

209. This formulation raises a number of issues for consideration. Specifically:

- What does "may have contravened" or "is likely to contravene" mean in the context of the prudential regime for banks?;
- How workable is the requirement to report matters "as soon as practicable"?; and
- Is the requirement to report "a material change in circumstances" necessary in the context of the prudential regime for banks?

210. We do not see the first two of these points as particularly problematic as they align with an obligation under the Financial Markets Conduct Act 2013 that many banks are, or will be, subject to.

211. In addition, the requirement to report would apply when a bank believes it "may have contravened" or "is likely to contravene" a condition of registration. When this reporting obligation would be triggered is ultimately a legal question that would be determined on the basis of particular facts. For this reason we cannot provide a definitive description of how the obligation would be interpreted in all cases. However, we would expect that test would normally be met when the possibility that a breach has occurred, or will occur, is brought to the attention of a bank's senior management, and they accept the

accuracy of that information (we also consider that banks could use this threshold as a reasonable rule of thumb around how we would normally interpret the obligation).

212. Likewise, when the requirement to report matters “as soon as practicable” is met is ultimately a legal question that would be decided on its particular facts. Again, this means we cannot provide a definitive description of how this obligation would be interpreted in all cases. However, we would anticipate that this test would usually be met if the Reserve Bank is notified immediately after senior management are provided with this information, and accept its accuracy (again, we consider that banks could use this as a reasonable rule of thumb about how we would normally interpret the obligation).

213. On the third of these points, we do not consider that requiring the reporting of “material changes in circumstances” is necessary in this context given the regular dialogue we have with banks, and the breadth of information they provide us with for supervisory purposes.

214. With this one exception, we propose to formulate the obligation to privately report breaches to the Reserve Bank in the same manner as the obligation in section 412 of the Financial Markets Conduct Act. However, we do anticipate an ongoing dialogue with banks on how this reporting obligation should be interpreted in more marginal cases.

215. On the issue around avoiding the need to disclose genuinely trivial breaches of conditions of registration, we continue to have concerns about the idea of some form of materiality threshold for when breaches must be disclosed, even if the determination of whether something is material is left to the Reserve Bank.

216. There are two main reasons for this. Firstly, we are concerned about the practicality of a materiality threshold, and whether this would be applied consistently across banks and over time. While this issue could be addressed to an extent by the Reserve Bank being responsible for determining whether this threshold was met, we consider that this approach would still be problematic as it would consume supervisory resources that we consider could be more effectively used elsewhere. Secondly, we have a more general concern with watering down the requirement to disclose breaches, as we see this as an important discipline on banks.

217. As a result, we propose to address this issue through reviewing the drafting of conditions of registration in order to minimise the risk that genuinely trivial matters could result in breaches. This review will be given effect through the restructuring of the Banking Supervision Handbook described above Part 2.

Part 6 (miscellaneous) – (3) AML requirements

218. The stocktake has highlighted again that some of the material in the Banking Supervision Handbook (specifically BS5) that refers to Anti-Money Laundering requirements is out of date. We have consulted banks on the contents of BS5 separately, and anticipate publishing the revised BS5 and our responses to submissions received on that consultation shortly.

Conclusion

219. In the Terms of Reference for the stocktake, we identified the following target outcomes for the project:

- Cut or simplify requirements where this can be done without compromising financial stability objectives
- Change requirements to make them more efficient (ie delivering similar benefits at lower cost)
- Present requirements in a different way to improve their user-friendliness and/or clarify their scope and nature
- Make improvements, where any are identified, in the Reserve Bank's processes for developing these prudential regulation requirements.

220. We believe that the changes proposed in this document, once finalised and implemented, will achieve these target outcomes and the overall objectives of the project. While there is still significant work to be done, the changes we are proposing will help us establish new structures that will make our prudential regulations, and our process for introducing or changing regulations, clearer, more consistent and more efficient going forward. We appreciate the industry and broader public engagement in the stocktake, and look forward to continuing this engagement as we implement the conclusions of the project.

Appendix A: List of Respondents

Below is a list of respondents to the Reserve Bank of New Zealand consultation document *Regulatory Stocktake of the Prudential Requirements Applying to Registered Banks* dated 21 July 2015.

ANZ Bank New Zealand Limited
ASB Bank Limited
Bank of New Zealand
David Middleton
David Tripe
Deutsche Bank AG - New Zealand
Don Brash
Donn Anderson
Heartland Bank
Institute of Directors
Kiwibank Limited
Martien Lubberink
Michael Reddell
New Zealand Bankers' Association
SBS Bank (Southland Building Society)
Standard & Poor's Ratings Services
The Co-operative Bank
The Hongkong and Shanghai Banking Corporation Limited
TSB Bank Limited
Westpac New Zealand Limited

Appendix B: New Handbook standard formatting / layout

In the consultation document we used an extract from Subpart 4C of Handbook document BS2B to illustrate the existing layout and two possible alternative options. This appendix uses the same extract to show a new option that was provided in the consultation feedback, which we propose to use, at least as a starting point, for redrafting the handbook. Paragraphs are numbered from (1) under each heading, and would be referred to by both heading and number, e.g. “paragraph 2(2)”, or “paragraph 2.2.1(3)”.

…

2 Rating system design

(1) The term “rating system” means all of the methods, processes, controls, and data collection and systems that support the assessment of credit risk, the assignment of internal credit-risk ratings, and the quantification of associated default and loss estimates.

(2) If multiple rating methodologies or systems are used within an exposure class, the rationale for assigning an obligor to a rating methodology or system must be documented and must be applied in a manner that best reflects the risk-level of the obligor.[6] Each of the systems used for IRB purposes must comply with the minimum requirements.

2.1 Rating dimensions

2.1.1 Corporate, sovereign, and bank IRB exposure classes

(1) A qualifying IRB rating system must have two separate and distinct dimensions:

(a) the risk of obligor default (the “obligor rating”); and

(b) transaction-specific factors (the “facility rating”).

2.1.1.1 The risk of obligor default (obligor rating grades)

(1) Separate exposures to a given obligor must be assigned to the same obligor rating grade, irrespective of any differences in the characteristics of the specific transactions.

(2) There are two exceptions to this general rule:

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[6] Banks must not allocate borrowers inappropriately to rating systems with the aim of minimising regulatory capital requirements (i.e. cherry-picking by choice of rating system).

(a) in order to take into account country transfer risk, different obligor grades may be assigned according to whether a facility is denominated in local or foreign currency.

(b) a facility's associated guarantees may be reflected by an adjustment to the obligor grade.

In the case of either exception, separate exposures to a given obligor may be assigned different obligor grades.

(3) Credit policy must articulate the levels of risk implied by each obligor grade. The grades must be such that perceived and measured risk increase as credit quality declines from one grade to the next. In articulating the risk of each grade the policy must describe both the probability-of-default risk typical for obligors assigned that grade and the criteria used to distinguish that level of credit risk.

2.1.1.2 Transaction-specific factors (facility ratings)

(1) Facility ratings must reflect LGD transaction-specific factors such as collateral, seniority, product type, etc.

(2) If the FIRB approach is used, this requirement can be fulfilled by having a rating system with a facility dimension that reflects both obligor and transaction-specific factors. For example, a facility rating that reflects EL by incorporating both obligor strength (PD) and loss severity (LGD) considerations would qualify. Likewise a rating system that exclusively reflects LGD would qualify. Where a rating dimension reflects EL and does not separately quantify LGD, the supervisory estimates of LGD must be used.

(3) If the AIRB approach is used, facility ratings must reflect only LGD and must take account of factors that influence LGD including, but not limited to, the type of collateral, product, industry and purpose. Obligor characteristics may be included as LGD rating criteria only to the extent they are predictive of LGD.

(4) If the supervisory slotting criteria are used for the SL sub-class, the two dimensional requirement does not apply. Given the interdependence between obligor and transaction characteristics in SL, registered banks may use a single rating dimension that reflects EL by incorporating both obligor strength (PD) and loss severity (LGD) considerations.

2.1.2 Rating dimensions for the retail IRB exposure class

(1) Rating systems for retail exposures must account for both obligor and transaction risk, and must capture all relevant obligor and transaction characteristics. Each exposure that meets the IRB definition of a retail exposure (see 4.7) must be assigned to a particular pool. This rating process must: provide for a meaningful differentiation of risk; group together sufficiently homogenous exposures; and allow for accurate and consistent estimation of PD, LGD and EAD at pool level.

(2) PD, LGD, and EAD must be estimated for each pool. Different pools may share the same PD, LGD and EAD estimates.

(3) At a minimum, the following risk drivers must be taken into account when exposures are assigned to a pool.

(a) Obligor-risk characteristics. Indicators of a borrower’s risk characteristics might include, for example, a measure of the borrower’s debt servicing burden and demographic information regarding factors such as age or occupation.

(b) Transaction-risk characteristics, including product and/or collateral types. Cross-collateral provisions must be explicitly addressed where present. Indicators of transaction risk characteristics might include, for example, loan to value measures, seasoning, guarantees, and seniority.

2.2 Rating structure

2.2.1 Corporate, sovereign, and bank IRB exposure classes

(1) Specific rating definitions, processes and criteria must be used to assign exposures to grades within a rating system. The rating definitions and criteria must result in a meaningful differentiation of risk. All relevant and material information must be considered when borrower and facility ratings are assigned.[7] That information must be up to date. Where only limited information is available, assignments of exposures to borrower and facility grades or pools must be made on a conservative basis.

(2) An obligor grade is defined as an assessment of obligor risk, based on a specified and distinct set of rating criteria, from which estimates of PD are derived. A grade definition must include a description of the degree of credit risk typical for obligors assigned to that grade and details of the criteria used to identify that level of credit risk.[8]

(3) A registered bank must have a meaningful distribution of exposures across grades on both its borrower-rating and, where relevant, facility-rating scales. To meet the objective of having a meaningful distribution of exposures across obligor grades with no excessive concentrations, there must be a minimum of seven obligor grades for non-defaulted obligors and one grade for those that have defaulted.[9]

(4) Where a loan portfolio is concentrated in a particular market segment and range of credit risk there must be enough grades within that range of credit risk to avoid undue concentrations of obligors in particular grades. Significant concentrations within a single grade or grades must be justifiable on the grounds of convincing empirical

[7] An external rating can be the primary factor determining an internal rating assignment. However, the bank must ensure that it considers other relevant information.

[8] “+” or “-” modifiers to alpha or numeric grades may only qualify as distinct grades if the registered bank employing the modifiers: has developed complete rating descriptions and criteria for their assignment; and separately quantifies PD estimates for the modified grades.

[9] This is subject to the exception for banks using the supervisory slotting approach for any SL sub-class.

evidence that the grade or grades cover reasonably narrow PD bands and that the credit risk posed by each obligor in a grade falls within that band.

(5) Registered banks using the supervisory slotting criteria for the SL exposure classes must have at least four grades for non-defaulted obligors, and one for defaulted obligors.

(6) Where the AIRB approach is used there must be a sufficient number of facility grades to ensure that no single grade contains facilities with widely varying LGDs. The criteria used to define facility grades must be grounded in empirical evidence.

2.2.2 Retail IRB exposure class

(1) For each pool of retail exposures identified, quantitative measures of loss characteristics (PD, LGD, and EAD) must be calculated. There must be a sufficient number of exposures in each pool to ensure meaningful quantification and validation of loss characteristics at the pool level.

(2) No single pool may include an undue concentration of the total retail exposure.

2.3 Rating criteria

(1) Rating-grade descriptions and criteria must enable obligors or facilities that pose similar risk to be consistently assigned to the same rating grade.[10]

etc …

[10] This consistency should exist across lines of business, departments and geographic locations within a bank.

Appendix C: Map and Indicative Timeline for Handbook Migration

Stage	Handbook documents involved	Destination of current material in new structure	Indicative timing
Stage 1 – capital	BS1 (statement of principles) BS2A (capital adequacy standardised) BS2B (capital adequacy modelling) BS6 (guidance on market risk) BS8 (connected exposures) BS12 (Internal Capital Adequacy Assessment Process - ICAAP) BS16 (processes for capital issuance and repayment) BS19 (LVR restrictions)	• BS2A and BS2B are carved up into the new modular approach for capital requirements. • FIRB and QRRE (unused sections of BS2B) will be removed at this stage. • BS16 and parts of BS1 are moved into the new "capital processes" document. (The sections of BS1 are Section H on breaches of capital ratios, and Section O(VII) on the loss absorbency of capital). • BS6 would become a separate guidance document within the capital module (subject to consultation on whether it still serves any useful purpose). • BS12 would also become a separate document within the capital module. (The current review of banks' ICAAPs may lead to changes in the content of this policy, but that will be independent of this restructuring). • The new documents would be set up in the proposed new format and layout, seeking further detailed feedback on how well that works. (But BS1, BS8 and BS19 would not be re-formatted at this stage; some BS1 text would be cut). • NB, overall Handbook layout and presentation (eg on the website) may be a bit piecemeal after Stage 1 – there will be some new documents in the new format, but others will be unchanged. • The new Glossary is set up at this stage, to be added to at each subsequent stage.	Jan 2016 – Apr 2016: develop text. May 2016: finalise formatting in line with proposed new style, and issue drafts for consultation for 10 week period. Aug 2016: update bank CoRs to put new documents in place. Minor updates will also be needed to the disclosure Orders in Council, to amend the existing cross-references to BS2A and BS2B, to come into force on the first quarterly balance date after BS2A and BS2B are replaced.
Stage 2 – pulling requirements out of BS1	BS1 (statement of principles) BS9 (acquisition of significant influence)	• New document #1 will summarise and briefly explain several standard requirements imposed by CoR (the branch size cap, the limit on insurance business, etc). It will also add requirements that are stated in BS1 but are not currently imposed by CoR (e.g. dual-registered branches cannot take retail deposits). Consultation will focus on these newly formalised requirements. • Related parts of Section C of BS1 ("bank registration") will be cut and replaced by cross-references where necessary.	May – July 2016: develop text. Aug 2016: issue drafts for consultation. We propose a 10 week consultation period, given that changes are potentially ones of substance rather than layout.

Stage	Handbook documents involved	Destination of current material in new structure	Indicative timing
		• New document #2 will set out credit rating-related matters in one place (Section J and Appendices 2 and 3 of BS1 will be cut). • We will expand BS9 to deal with the case where the would-be acquirer is a natural person rather than a corporate (using cross-reference to BS10, approval of individuals). Section M of BS1, which also covers this, will be deleted (any material that needs to be kept will be moved into BS9). • Consult on new document #3 to deal with the requirement for a bank to seek RBNZ approval before establishing an overseas branch, subsidiary or representative office: a standard CoR will be added, backed up by guidance on the factors that we may take into account before giving approval. (This will replace Section N of BS1).	Finalise and impose via banks' CoRs: either do this for end-Dec 2016, or hold the Stage 2 CoR changes until the documents in Stage 3 are ready. The latter also has benefits in terms of a single batch of changes to the website.
Stage 3 – registration requirements and s75 obligation	BS1 (statement of principles) BS3 (registration – material to be provided by applicant) "Bank registration information document" BS5 (AML guidelines) BS9 (acquisition of significant influence) BS10 (director and senior manager suitability) BS11 (outsourcing) BS14 (corporate governance)	• At this stage, the rest of BS1 is removed. • We will put together the new one-stop registration document, taken mainly from the current Section C of BS1, the Bank Registration Information document, and BS3. This will cross-refer to other documents for registration requirements that link to continuing post-registration requirements. It will also include the current AML questionnaire from BS3. • BS5 will be reformatted and possibly re-located, so that cross-references to it from the new registration document can be finalised at this stage. • A new single document will cover director/senior manager suitability (to remove duplication between BS3 and BS10). • We will put together a new document setting out our general approach to supervision (this will replace Section D of BS1, but also draw on other material). • A new document will set out the Principles required by s75 of the Act (unless these are covered in the previous document). This would include a high-level statement of our principles for granting registration (rather than a point-by-point consideration of the matters we must consider, which would be in the registration document); and a statement of how we use conditions of registration. (This will replace Sections E and F of BS1.) • BS9 is updated to refer to the new director/senior manager document. • BS14 is updated as needed, where it deals with the CoR imposing the director / senior manager non-objection requirement, and also take the current material from BS11 on the CoR that requires the business and	Aug – Oct 2016: develop text. Consult for 6 weeks from start of Nov 2016. BS11 and BS14 need CoR updates at this stage, to take effect at (say) end-March 2017, but these would be fairly minor. If Stage 2 CoR changes are held over to Stage 3, they would be implemented at the same time. Website updates would be at the same time as CoR updates.

Stage	Handbook documents involved	Destination of current material in new structure	Indicative timing
		affairs of the bank, the CEO's contract and so on to be the board's responsibility. • The material noted above is cut from BS11. • Full reformatting of BS11 and BS14 is left for Stage 4.	
Stage 4 – the rest	BS4 (audit requirements) BS7 & BS7A (explanation of disclosure regime) BS8 (connected exposures) BS11 (outsourcing) BS13 & BS13A (liquidity policy) BS14 (corporate governance) BS15, BS17, BS18, BS19 (all of these appear to need minor updates at most, or re-branding)	• This should be a relatively mechanical stage. There are no major structural issues with these documents – they mostly need only re-formatting and re-labelling. • BS4 is pure guidance for auditors, who will be consulted to see if anyone still needs it. • The substance of BS7 is now replaced by the incorporation-by-reference page on the RBNZ website, so can be removed. • BS11 and BS13/13A are, or may be, subject to separate policy reviews, so the timing of changes may be affected by co-ordinating with those. • Completion of this stage allows the new web layout and Handbook navigation to be finalised.	Nov 2016 – Jan 2017: develop text. 6 week consultation during Feb - Mar 2017. Apr - Jun 2017, finalise these documents and also complete the whole website update and deal with any snagging from previous stages. Update CoRs to implement the final set of new documents from end-Jun 2017.

Appendix D: Stocktake Register of Issues Addressed

Category	Issues to be Addressed	Status as of 1.12.2015
1. Data and Disclosure for banks	A: Consider removing requirement for parent company (solo) financial statements	Done
	B: Review the role of off-quarter Disclosure Statements	In process
	C: Improve use of technology in the Disclosure Statement regime	In process
	D: Review disclosure requirements more generally	In process
	E. Fix other minor issues previously identified (eg. IFRS 9, minor Basel III related clarifications and other potential simplifications)	In process
2. Format & structure of the Banking Supervision Handbook	A. Restructure Handbook, particularly BS1, making the distinction between binding requirements, guidance and guidelines clearer	In process
	B. Improve Handbook navigation	In process
	C. Improve consistency of presentation across the Handbook	In process
	D. Create glossary for Handbook, improving consistency with external definitions	In process
	E. Review AML matters covered in the Handbook	In process
	F. Reduce need to make such frequent Handbook and CoR updates for minor/technical matters	In process
3. Capital requirements for banks	A. Reorganize structure of capital documents	In process
	B. Improve layout of credit risk section of BS2B of the Banking Supervision Handbook	In process
	C. Consider removal of any unutilized provisions in BS2A/BS2B	In process
	D. Fix other minor issues previously identified (e.g. inconsistent wording and definitions, outdated references)	In process
	E. Review 1% Limit on insurance business	Follow-on initiative
	F. Review approach to internal models	Follow-on initiative
	G. Review purpose of ICAAPs (overlap with parallel initiative)	Follow-on initiative
4. Policy-making approach across regimes	A. Improve "Forward-Planning": Provide clearer information to industry and coordinate better within RBNZ and with other regulators regarding timelines for consultations	In process
	B. Establish target time frames to allow sufficient time for consultation (early stage) and implementation	In process
	C. Make greater use of post-implementation reviews	In process
	D. Streamline process for making changes to regulations	In process
5. Differentiated regulatory approach	A: Improve consistency across prudential regimes	In process
	B. Clarify key points of differentiation (ie size cut-offs for various policies) within the bank's regulatory approach.	In process
6. Miscellaneous changes to bank policies and regulations	A: Ensure the clarity of netting rules under connected exposure policies	Handbook and Follow-on Initiative
	B: Improve the clarity of the local incorporation and dual registration policies	Handbook and Follow-on Initiative
	C: Improve director/ manager non-objection policies	In process
	D: Improve tools for handling minor/ technical CoR breaches	In process

Appendix E: Re-print of Original Appendix F from Consultation Document

Note: As discussed in the main body of this paper, we are proposing to make a series of changes to this document, including lengthening the standard consultation period from 4-8 weeks to 6-10 weeks. For now, we have left this document unchanged and are including it for reference purposes only. We will integrate the changes discussed as we develop the document from its outline/draft into its final form. We expect to finalise this document as part of "Stage 2" of the Handbook Migration, as we reconfigure our existing BS1- Statement of Principles.

Outline Draft Statement of the Reserve Bank's Policy Making Approach

Overall approach and framework

- The Reserve Bank's approach to policy making is firmly anchored in its governing legislation (the Reserve Bank of New Zealand Act 1989) and seeks to follow the "Best Practice Regulation" model developed by the New Zealand Treasury wherever possible;[11]
- The Reserve Bank carries out regulatory impact analyses on all of its regulatory policies.[12] This analysis generally takes the form of a Regulatory Impact Statement (RIS), which includes stakeholder consultation and is published on the Reserve Bank website;
- Policy papers and potential policy consultations, and all RISs, are discussed by an internal Reserve Bank committee, which is chaired by the Deputy-Governor, Financial Stability and attended by all governors. Analysis, policy options and subsequent feedback from stakeholders are reviewed by the committee. Decisions are ultimately made by the Governor; and
- We also monitor and report on our work in the accountability documents we publish: our Statement of Intent, our Annual Report, and our semi-annual Financial Stability Report.

Approach to Regulatory Impact Assessment

- Assessments of regulatory impact generally cover the following: status quo and problem definition, objectives, options and impact analysis, consultation, implementation, monitoring, evaluation and review;
- Problem definitions are generally based on market failure arguments and/or bringing New Zealand standards into line with international practice where it is in New Zealand's interest to do so;
- Not every potential market failure warrants a regulatory solution. Regulatory costs can be significant and there is always a risk of regulatory failure. An analysis of policy options is undertaken against the status quo and/or the absence of regulation. Regulatory action is only proposed if a regulatory solution would improve on the market outcome;
- Some policy initiatives are also driven by efforts to increase the efficiency of existing regulatory regime;

[11] http://www.treasury.govt.nz/regulation/bpr
[12] Except those that are of a minor or technical nature.

- Problem definitions are supported by analysis of underlying data (whenever available) and other information, including international norms and best practices;
- Objectives may be linked to the Reserve Bank's legislative mandate as per the Reserve Bank Act with more specific objectives targeted at addressing the relevant policy objective;
- In its internal decision-making process, the Reserve Bank uses internal cost benefit frameworks to guide its analysis. Whenever possible, we quantify and seek to monetize costs and benefits; and
- We also seek to reduce and minimize costs on affected parties if possible. This may include the use of exemptions or policy thresholds, and appropriately chosen timelines.

Approach to Consultation, Implementation and Post- Implementation Review

- Industry and broader public consultation provide crucial input for the Bank's analysis. Our aim is to consult over a <u>four to eight week period</u> depending on the significance of the proposal. There may be rare cases where circumstances mean we adopt a shorter consultation period. In these cases, the Bank will seek to be clear about why a longer period is not possible;
- Unless a proposal is of a minor and technical nature, or only affects a small number of entities and is a matter of limited public interest, we will release a consultation paper inviting stakeholder feedback, followed by a policy decision paper summarizing the feedback;
- In some cases, for more significant or complex initiatives, the Bank may also hold targeted workshops with industry to elaborate or solicit more detailed feedback on specific matters. If there is a need for further discussion or consultation on an issue, we adapt our time-frames and process accordingly;
- In all of its consultations, the Bank seeks to be transparent about its assumptions and its goals, stating clearly which options may or may not be feasible and why;
- The Bank welcomes full and frank feedback from its stakeholders and gives proper consideration to alternative viewpoints;
- Each consultation should address transitional arrangements and implementation timeframes. Industry will be consulted on potential implementation timeframes and the reasons behind them. Time requirements will vary significantly depending on the nature of the policy. Wherever possible, the Bank seeks to implement policy changes in reasonable time-frames;
- The Bank is committed to reviewing its existing policies to keep them up to date and, where appropriate, in line with international regulatory developments, and to address any issues that may arise; and
- The Bank is committed to reviewing its existing policies on a regular basis, subject to available resources. In some cases, the Bank's governing legislation contains its own timelines for review.

Approach to Communication/Engagement with Industry

- To the extent possible, the Reserve Bank provides information about its upcoming consultations and policy initiatives via a dedicated section of its website;
- In some cases, the Bank is unable to signal some aspects of its workplan because doing so might create market distortions. In other cases, issues emerge suddenly and cannot be communicated with much advance notice. The Bank's policy-related work plans must remain somewhat dynamic in nature, responding to changes in the market or in international standards. The website is updated on an

as-needed basis and at least quarterly for Banks and insurers. The NBDT section of the website is updated on an as-needed basis;

- The Bank currently produces a regular newsletter for the insurance sector, to keep industry up to date on its planned consultations and work program. The Bank is considering expanding this to include a newsletter for banks;
- Consultations are posted on the Bank's website and distributed to subscriber mailing lists;
- In some cases, depending on the nature of the consultation, the Reserve Bank's communications department also makes more public announcements or press releases in order to solicit broader public input;
- Where appropriate, supervisors also discuss policy issues as a standing agenda item in their supervisory meetings with the regulated entities. Feedback from these meetings is relayed back to the policy-making departments at the Bank; and
- The Bank also has regular engagement with representatives of industry bodies in the various sectors it regulates.

Collaboration with Other Regulators and Government Agencies

- The Bank collaborates and consults with other regulators and government agencies in its policy-making work through the following mechanisms:

    - Quarterly meetings with the Financial Markets Authority
    - Membership of Council of Financial Regulators (CoFR)
    - Chairing the Banking Forum, a sub-committee of CoFR
    - Regular engagement with the Australian Prudential Regulatory Authority (APRA)
    - Membership of the Trans-Tasman Banking Council; and
- The Bank is also a member of a number of other international bodies and engages regularly with the international banking community in order to keep abreast of changing international standards and best practices.