



Summary of Submissions: Enforcement Principles & Criteria

May 2022

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Background

At Te Pūtea Matua, the Reserve Bank of New Zealand, we are *kaitiaki* (guardians) of New Zealand's financial ecosystem. We carry out our prudential functions with the objective of protecting and promoting the stability of New Zealand's financial system and in accordance with the purposes and objectives of the prudential legislation for different sectors.

For banks and non-bank deposit takers (**NBDTs**) the purposes include avoiding the significant damage to the financial system that could result from the failure of a regulated entity. For insurers, the purposes include promoting public confidence in the insurance sector. For financial market infrastructure (**FMIs**), we jointly regulate and supervise settlement systems with the Financial Markets Authority.

We also perform and exercise functions or powers conferred on us by the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (the **AML/CFT Act**), in accordance with the purposes of the AML/CFT Act.¹ We are the designated AML/CFT supervisor for banks, NBDTs and life insurers.

In order to achieve the purposes of our various pieces of legislation we use a range of supervisory and enforcements tools to promote compliance. Our supervisory approach uses relationship-based monitoring of an entity's compliance with prudential and reporting obligations. This monitoring ensures that we maintain familiarity with the financial condition and risk profile of each entity we regulate and that we maintain a state of preparedness to instigate corrective action should this be considered necessary.²

In most circumstances, supervisory responses are effective in achieving our purposes in a resource-efficient and timely manner. However, the effectiveness of prudential and AML/CFT supervision depends on regulated parties knowing that we will take firm action where non-compliance is identified and risks are not being properly addressed. Enforcement is therefore an integral part of our compliance toolkit. Where we identify serious non-compliance, issues will be referred to our specialist Enforcement team for formal investigation and response as appropriate.

Enforcement framework

We are developing our enforcement framework to provide guidance on our approach to using our enforcement discretion to address risks associated with our prudential mandate and our responsibilities under the AML/CFT Act.³ The enforcement framework will consist of several pieces of public guidance which should be read alongside each other to provide a comprehensive understanding of our enforcement process:

- **Principles and Criteria Guidelines** – describe the fundamental considerations for the enforcement framework that we will work through and weigh when deciding on the appropriate enforcement response.
- **Enforcement Guidelines** – describe our escalating regulatory response model and further detail on how we apply the enforcement principles and criteria when selecting the appropriate regulatory response.

¹ The Reserve Bank is one of three agencies in New Zealand tasked with supervising, monitoring and enforcing obligations under the AML/CFT Act.

² Overview of the banking oversight regime at <https://www.rbnz.govt.nz/regulation-and-supervision/banks/overview>

³ The enforcement framework will also apply to other areas that we may choose to investigate such as non-compliance with the restricted word provisions of the RBNZA and IPSA, and our central bank remit under Part 2 of the RBNZA.

- **Investigation Guidelines** – describe our approach to formal investigations and how we apply the enforcement principles and criteria throughout the lifecycle of an investigation. The Investigation Guidelines also describe our use of information gathering powers under our legislation.

Enforcement Principles and Criteria

The enforcement principles and criteria are fundamental considerations for the enforcement framework.

- The principles are a set of high-level values that guide the direction of our enforcement strategy and inform our approach to applying our enforcement discretion. Our three enforcement principles are: **risk-based, proportionate, and transparent**.
- The criteria are specific considerations which will be worked through and weighed against the available evidence when deciding on the appropriate enforcement response. They will be used by the enforcement team as a guide to analysing evidence, and will inform our consideration of a particular issue, through their inclusion in referral and enforcement decision memos. Our four enforcement criteria are: **seriousness of conduct, responsiveness, public trust and confidence, and efficacy**.

To collaborate with industry in the development of the enforcement framework, we published the Enforcement Principles and Criteria Consultation Document (the **consultation document**) in October 2021.

This document outlines the feedback received from our consultation and the key themes emerging from the consultation process. After considering submissions, we intend to incorporate some of the feedback into the final version of our Enforcement Principles and Criteria Guidelines (**P&C Guidelines**). Other elements of the feedback will be incorporated into other parts of our published enforcement framework, such as the Enforcement Guidelines and the Investigation Guidelines. We expect to publish the Enforcement Guidelines in Q2 2022, with the Investigation Guidelines to follow in Q3. We do not intend to consult on the development of other parts of the enforcement framework as they are largely operational guidelines detailing how we apply the principles and criteria and our other commitments in practice.

Consultation process

The consultation process on the enforcement principles and criteria opened on 13 October 2021, and closed on 24 November 2021. We received 12 submissions on the consultation paper, comprising:

- 11 substantive submissions from Banks, NBDTs, Insurance, and FMIs; and
- One brief statement of support from NBDT trustees.

Non-confidential submissions have been uploaded to the Reserve Bank website.

This document provides a summary of the submissions received in response to our consultation, as well as a brief response to those submissions. Here, we focus on the common themes and views raised in the submissions. This document is not intended to be an exhaustive summary and response to all points raised. We direct readers to the consultation document and published substantive submissions for a full understanding of our responses.

We intend to finalise and publish the final P&C Guidelines in Q2 2022, with further guidance to follow in due course.

Our responses to feedback received

Submissions on choice and application of individual principles

Submitters generally responded positively to the proposed enforcement principles and the way that they were described in the consultation document.

- **Transparency** – Submitters supported the transparency principle as it promotes consumer confidence in market monitoring and positively influences the behaviour of financial institutions. Six submitters made specific suggestions relating to either *transparency of process* or *transparency of outcome* as delineated in the consultation document.
 - *Transparency of process* – Two submitters suggested that *transparency of process* should explicitly record how the Reserve Bank will engage with entities transparently throughout the lifecycle of any enforcement activity. Specifically, that the Reserve Bank’s commitment to open and transparent communication should be consistent across its supervision and enforcement functions.
 - *Transparency of outcome* - Several submitters commented on the considerations behind when the Reserve Bank will publish an enforcement outcome and what will be published. Specifically, submitters were keen that the Reserve Bank recognises that publication is part of, not separate to, an enforcement response that serves as a deterrence for future misconduct, both for the entity itself and the wider market. Additionally, submitters noted that publication should not be automatic, and may not be appropriate if it is not in the public interest to do so and the threshold included in the consultation document of ‘exceptional circumstances’ for non-publication is a high bar.
- **Proportionality** – Submitters were generally supportive of the proportionality principle. Two submitters made specific suggestions on how the proportionality principle could be improved:
 - One submitter suggested that the Reserve Bank clarifies its statement that the enforcement response will be ‘calibrated to the individual entity’ by expressly acknowledging the relevance of the size and nature of the entity in the enforcement response. However, another submitter noted that entity size and influence in the industry should not become a defining factor in the Reserve Bank’s enforcement strategy, causing the enforcement function to overly focus on key industry participants rather than the industry as a whole.
 - One submitter recommended that the proportionality principle be expanded to include ‘fairness’. In their view, regulators should be seen as consistent and fair in their treatment of regulated entities, to promote and maintain open, collaborative relationships with the sector.
- **Risk-based** – None of the submitters made explicit comments on the risk-based principle.

Our response

We note that the principles are intended to provide a lens through which the criteria (specific considerations) are applied and so are deliberately drafted at a high-level to guide and inform decision making. However, we have considered submitters' responses and make the following comments:

- **Transparency** – Given the high-level nature of the principles and criteria, in our view, it would be inappropriate to make commitments in the final P&C Guidelines relating to how we will engage with entities in specific circumstances. However, we will keep these comments under consideration as we continue to develop the enforcement framework, in particular, the Investigation and Enforcement Guidelines. We respond to other specific comments below:
 - Regarding consistency between the Enforcement and Supervision functions under *transparency of process*, we believe it is appropriate to draw out how our Relationship Charter applies in respect of Enforcement matters.
 - Regarding the publication of enforcement action under *transparency of outcome*, in our view, the consultation document is sufficiently clear that publication will not be automatic. However, we will review the language used to make sure that we are being clear about the factors that may weigh against publication. The *transparency of process* principle (and, more broadly, our adherence to the Relationship Charter) should ensure that regulated entities are not surprised by a public statement of the initiation of formal action against them.
 - Finally, we agree that publication may form part of an enforcement response and will acknowledge this in the final P&C Guidelines.
- **Proportionality** – Noting the high-level nature of the principles, in our view it would be inappropriate to make commitments in the P&C Guidelines relating to how we will specifically calibrate our enforcement response to a particular entity or industry. However, we will keep this point under review as we further develop the Investigation and Enforcement Guidelines. Regarding expanding the proportionality principle to include 'fairness', in our view 'fairness' does not need to be explicitly included in the proportionality principle as it is already captured under the 'public trust and confidence' criterion.

Submissions for other principles

Four submitters suggested additional enforcement principles, including:

- **Priority/focus areas:** Two submitters suggested that it would benefit financial markets for the Reserve Bank to be more specific about its particular priority or focus areas for compliance and enforcement, so that regulated entities may respond more effectively.
- **Forward looking:** One submitter recommended that the Reserve Bank includes a 'forward-looking' principle that seeks to proactively identify prudential risks and take action to prevent harm.
- **Impact of non-compliance:** One submitter suggested elevating the 'impact of non-compliance' factor to a principle.

- **Sound legal basis for acting:** Two submitters commented that the most important principle when considering whether enforcement action is appropriate should be whether there is a sound legal basis for acting.

Our response

We have considered the four suggested additional principles above and in our view, they are already sufficiently dealt with elsewhere in the descriptions of the principles and criteria or are outside the scope of the enforcement function.

- **Priority/focus areas:** As part of our commitment to being a proactive regulator, we will continue to engage with industry and relevant stakeholders openly and constructively to promote a sound and efficient financial ecosystem. As part of this, and as the enforcement function develops, we will look to publish enforcement-specific priority or focus areas, similar to the approach taken by our peer regulators.
- **Forward looking:** Proactive identification of prudential risks forms part of the Reserve Bank's broader financial stability objective to ensure the ongoing financial wellbeing of New Zealand. In particular, our supervisory approach and thematic reviews ensures that we are attuned to future entity-specific and sector-wide risks as they develop. 'Forward-looking' is covered in elements of the principles and criteria such as the risk-based principle and the deterrence impact of any enforcement response. As such, in our view, 'forward looking' does not need to be a separate principle. Because of this, in our view, forward looking is sufficiently captured in the principles and criteria and wider Reserve Bank approach to meeting the financial stability objective.
- **Impact of non-compliance:** In our view, this is adequately dealt with under the 'seriousness of conduct' criterion and does not need to be elevated to a principle. Additionally, the proportionality and risk-based principles include assessments of the non-compliance against the desired outcomes of the legislation when determining enforcement resourcing and response.
- **Sound legal basis for acting:** The existence of a sound legal basis for acting is fundamental to the Reserve Bank's work. Determining whether there is a legal basis for enforcement action is a part of the proper process that we follow when deciding whether to investigate and what the appropriate enforcement response will be. Additionally, we point to the 'strength of evidence' factor under the 'efficacy' criterion which specifically acknowledges that the Reserve Bank will undertake an assessment based on the Solicitor-General's Prosecution Guidelines' (S-GPG) Evidential Test for both civil and criminal actions.

Other comments on principles

Several submitters provided general comments on the principles, these included:

- The principles and criteria should align with any matters which the Court must have regard to under the governing statutes.
- Regard needs to be had for unique regulatory areas (such as the FMI regime) where the application of the principles and criteria may not be immediately apparent.
- It will be important to ensure that any changes over time that are made to principles and criteria are considered in light of the wider regulatory environment and multiple regulatory bodies that entities engage with.

Our response

We agree with the points raised above and will look to:

- i. Include reference to the matters that a Court must consider under applicable legislation in the P&C Guidelines and the Enforcement Guidelines.
- ii. Adjust the wording in the P&C Guidelines to make it clear that our enforcement strategy will need to be adapted for the different regulatory areas, such as FMI and AML/CFT.
- iii. Include acknowledgements that we will keep the enforcement framework documents updated in light of changing practices of the Reserve Bank and the changing legislative landscape.

Submissions on choice and application of individual criteria

In general, submitters were supportive of the proposed enforcement criteria. Several submitters approved of the consistency between our criteria and those of the Financial Markets Authority (FMA) and the Commerce Commission. Several submitters made specific recommendations on individual criteria and factors:

- **Responsiveness** – One submitter noted that an entity’s responsiveness should be a strong factor in determining how, and to what extent, the Reserve Bank exercises its enforcement discretion. Another submitter noted that the ‘entity’s compliance history’ should be considered in light of general trends in compliance and take into account positive changes that the entity may have made. For example, where there are significant historic issues that are of concern, but an entity has responded appropriately and is now demonstrating improved behaviour, the compliance history should not be a significant factor. Additionally, an ‘entity’s compliance history’ should only be relevant *after* the initial matter has been determined.⁴
- **Public trust and confidence** – Submitters requested that the Reserve Bank describes what would be specifically involved in weighing up the benefits of public action against any immediate risk to financial stability. Specifically, they requested that the Reserve Bank provides further guidance on balancing ‘deterrence’ and the ‘seriousness of the conduct’ on one hand, and ‘maintaining public confidence’ in the financial system on the other hand. Another submitter recommended that ‘deterrence’ should be balanced with encouraging compliance and avoiding overly punitive impacts on a particular entity.
- **Efficacy** – Submitters recommended that the guidelines reference the need for coordination and planning between regulators and between the Reserve Bank’s Enforcement and Supervision functions. Additionally, submitters recommended that the ‘efficacy’ criterion explicitly recognise that ‘other regulatory bodies’ could include those outside New Zealand, particularly in the FMI space.

Our response

We thank submitters for their suggestions, and respond to them below:

- **Responsiveness** – In our view, an entity’s responsiveness to the breach is sufficiently covered by the ‘cooperation with the Reserve Bank in reaction to the breach’ factor. We

⁴ We interpret this comment to mean that an entities compliance history is not a factor in determining whether a breach has occurred. Rather it should be considered when deciding on the appropriate enforcement response after the Reserve Bank has satisfied itself that there is an actionable breach.

also believe that the general trends in compliance and any positive changes that the regulated entity may have made are appropriately captured in the 'responsiveness' and 'public trust and confidence' criteria. However, in the P&C Guidelines we will look to more clearly capture the overarching concept that the criteria and factors will be applied in a way that weighs up the positive conduct of the entity as well as the conduct that contributed to the breach.

- **Public trust and confidence** – In our view the requested level of specificity does not fit with the purpose of the P&C Guidelines. The individual principles and criteria are not intended to be read in isolation, rather they are part of the broader enforcement framework which will be captured in the P&C Guidelines and the Investigation and Enforcement Guidelines documents. The enforcement framework must be applied and operated within our legislative mandates and as part of our broader purpose, vision, and values as described in the Statement of Intent. However, in the final P&C Guidelines, we will look to give this point more prominence.
- **Efficacy** – We agree that international bodies should be referenced in the discussion of 'other regulatory bodies' as part of the 'efficacy' criterion. We will also look to elaborate on our approach to cooperating with peer regulators, in the Investigation and Enforcement Guidelines.

Submissions for other criteria

Several submitters suggested additional considerations that could be included in criteria or factors, these include:

- **Constructive and open communication:** One submitter recommended that we describe how we will ensure that the parties engage constructively, while focusing on the intent of the regulation, industry interpretations, and communicating openly without reliance on legal privilege.
- **Clarity of application:** One submitter recommended that we outline how we will approach enforcement in a manner that clarifies and reflects the regulatory context, as well as how we will seek the appropriate outcome in the most efficient and practical manner.
- **Crown Prosecution Guidelines:** One submitter noted that any decision to prosecute must satisfy the evidential and public interest test in the S-GPG. It was suggested that the public interest test has not been sufficiently canvassed in the consultation paper, and needs greater prominence.
- **Self-reporting:** One submitter recommended that self-identification of issues and escalation to the Reserve Bank should be taken into account when considering the enforcement approach. In particular, they noted that entities that undertake robust assurance and compliance testing, which identifies compliance weaknesses and potential breaches, should have this positive risk culture factored into enforcement action.

Our response

We have considered the submissions on additional criteria and, in our view, many of the recommendations can be addressed by clarifying or elaborating on the current criteria or including further detail in the other enforcement framework guidance such as the Enforcement and Investigation Guidelines. Specifically:

- **Constructive and open communication** – In our view, our approach to communications (in the context of the P&C Guidelines) is sufficiently captured in the transparency principle. Although we will look to further address how enforcement related communications are conducted in accordance with the Relationship Charter, as described above.
- **Clarity of application** – The purpose of developing an enforcement framework is to clearly outline how we approach enforcement in a manner that reflects the regulatory context. We also aim to detail how we will seek appropriate outcomes in accordance with our purpose, vision, and values as described in our Statement of Intent. We will look to give this point more prominence in the P&C Guidelines and other enforcement framework guidance.
- **Crown prosecution guidelines** – The ‘strength of evidence’ factor under the ‘efficacy’ criterion includes a specific reference to the Evidential Test under the S-GPG. We will look to include reference to the Public Interest Test under the ‘public trust and confidence’ criterion to give further clarity. We may also provide further guidance on the application of the S-GPG in other enforcement framework guidance.
- **Self-reporting** - In our view, the impact of self-reporting on the ultimate enforcement decision is already incorporated in the proportionality principle and the ‘responsiveness’ criterion. However, we will look to draw out these themes more explicitly in the final P&C Guidelines.

Other comments on criteria

Several submitters provided general comments on the criteria, including that we should make explicit references to ‘potential’, ‘possible’ or ‘alleged’ non-compliance/breaches, and include wording that reflects the fact that only the courts determine whether an activity has broken the law or not. Additionally, submitters recommended that we explicitly refer to the principles and criteria when exercising our enforcement powers or discretion.⁵

Our response

We acknowledge that only the courts can determine whether an activity has broken the law or not and will look to add words to reflect this in the final version of the P&C Guidelines and the Enforcement Guidelines.

In our view, our approach to public statements and communications in the context of the principles and criteria is covered by the transparency principle.

Suggestions for additional guidance

Eight submitters made specific recommendations for further enforcement guidance that the Reserve Bank could produce. These suggestions included guidance on:

- **Application of natural justice principles** – Submitters requested further guidance on the application of natural justice during the investigation, litigation, and decision-making processes. Specifically, guidance on the rights of investigated parties during an investigation, including: the right to be heard, the opportunity to explain their conduct and to put forward their version of events, the right to legal representation, and the application of legal privileges.

⁵ We took this to mean that we should use the Principles and Criteria to guide public statement and communications on enforcement outcomes.

- **Relationship between Enforcement and Supervision** – Submitters requested an explanation and examples of any practical differences that can be expected for enforcement activities under the new enforcement-led framework compared to the old supervision-led process.
- **Relationship with peer regulators** – Submitters noted their strong support for collaboration between regulators, where enforcement falls within the remit of more than one regulator. However, further guidance was requested on our approach to such collaboration.
- **The enforcement process** – Submitters requested further guidance on elements of the enforcement and investigation process, including: guidance on the statutory tools and regulatory responses (powers and ability to sanction) in the Reserve Bank's tool-kit, and guidance on what supporting documents will be considered when deciding on an enforcement action, for instance, the Relationship Charter, Statement of Intent, and any other published policies.
- **Sector specific application** – Submitters requested additional guidance on how the principles and criteria apply to sectors governed by specific legislation. In particular, guidance was sought on how we consider the scope, purpose, and principles of the relevant regulatory regime and the general behaviour and maturity of a particular regulated population.
- **Lessons from enforcement activities** – Submitters suggested that we should share supervisory insights gathered from their monitoring and provide specific examples of good and poor practices in the industry. This would allow discretion on which enforcement actions to publicise, while giving the industry the chance to find and fix things and learn from others.

Our response

We appreciate the need for further clarity throughout the investigation and enforcement process and on how the enforcement process fits within the general supervisory relationship. We will be publishing further enforcement framework guidance in due course such as the Enforcement and Investigation Guidelines which will address some of these points. Specifically:

- **Application of natural justice principles** – The Enforcement and Investigation Guidelines will cover applicable natural justice principles.
- **Relationship between Enforcement and Supervision** – The Enforcement page on our website will describe at a high level the relationship between our Enforcement and Supervision functions. Additionally, the Enforcement Guidelines will provide further explanation on how and when a matter is progressed from a supervisory response to an enforcement response. The Investigation Guidelines will also deal with expected supervision-led and enforcement-led engagements with entities during the course of an investigation.
- **Relationship with peer regulators** – Our Investigation and Enforcement Guidelines will look to address at a high-level our ability to refer things to other regulators if we believe they are better suited to their regulatory remit.
- **The enforcement process** – The Enforcement and Investigation Guidelines will describe our escalating regulatory response toolkit, our approach to entity communication during an investigation, and a description of how the enforcement framework interacts with other published policies such as the Relationship Charter.

- **Sector specific application** – As discussed above, the principles and criteria are high-level so that they can be applied to the full suite of regulatory areas for which we are responsible. The final P&C Guidelines will look to clarify how the principles and criteria work together with the rest of the enforcement framework and the relevant legislation.
- **Lessons from enforcement activities** – We support the need for transparent communication of insights gained from our activities, as the enforcement function matures, we will look to provide further insight into our enforcement outcomes.

Additional comments

One submitter noted that instances of non-compliance can occur within complex businesses with complex legislative frameworks. In their view, an absence of incidents of non-compliance may be more likely to indicate a *weak* risk and compliance framework than a strong one. They submit that this be recognised within our enforcement strategy. We agree with this comment and will look to incorporate this concept into our Enforcement Guidelines.

Several submitters recommended the principles and criteria be closely monitored once implemented, re-assessed, and updated for effectiveness over time. This would ensure delivery of intended improvements in compliance standards, and assess changes and innovations in both industry and the Reserve Bank environments. One submitter commented that supervision of cyber and technology risk is a dynamic, developing area. They noted that it is unclear how tolerances and thresholds in this area will be set. As mentioned above, the guidelines that make up the enforcement framework are living documents and will include a commitment to review them regularly and amend them in light of changes in the regulatory environment.

One submitter suggested that the strategic priorities should link directly to the principles, criteria, and factors, and that the final P&C Guidelines should show how these factors would enable our Reserve Bank's strategic priorities to be achieved. Another submitter noted that we should elaborate on the intent of the compliance goals by showing how they link back to our Statement of Intent. We agree and will look to contextualise how the enforcement framework and the principles and criteria align with the Reserve Bank's strategic priorities as expressed through the Tane Mahuta narrative in the Statement of Intent.

Several submitters recommended that we hold forums and seminars to allow for engagement and constructive discussion on the enforcement function and provide an opportunity for industry to raise questions and fully understand the approach that will be taken. We appreciate industry's desire for engagement, once we have finalised the principles and criteria and issued further enforcement guidance we will consider how best to engage with industry to promote a clear understanding of our enforcement framework.

Next steps

Thank you to everyone who submitted on this guidance. The full list of substantive submissions can be viewed on our website. The table below sets out the timeline we are pursuing with respect to the remainder of the enforcement framework. We will be engaging with our regulated entities throughout this process and we welcome your views at any point. Please provide any further comments using the email address Enforcement.Consultation@rbnz.govt.nz.

Quarter	
Q2 2022	<ul style="list-style-type: none">• Publish P&C Guidelines along with this consultation response document• Publish the Enforcement Guidelines
Q3 2022	<ul style="list-style-type: none">• Publish the Investigation Guidelines