

BILLS DIGEST

RESERVE BANK OF NEW ZEALAND AMENDMENT BILL (No 3) 2007

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RESERVE BANK OF NEW ZEALAND AMENDMENT BILL (No 3) 2007

Date of introduction:	21 November 2007
Portfolio:	Finance
Select Committee:	As at 22 November, 1st reading not held

PURPOSE

The primary purpose of this Bill is to amend the Reserve Bank of New Zealand Act 1989 (the Act) in order to implement elements of the new regulatory framework for non-bank deposit takers and enhance the Reserve Bank of New Zealand's (the Bank) accountability and transparency arrangements in relation to its financial sector functions¹.

BACKGROUND**The Reserve Bank of New Zealand Act 1989****Establishment of the Reserve Bank of New Zealand**

The Reserve Bank of New Zealand Act 1989 establishes the Reserve Bank of New Zealand. Amongst its purposes, the Act must provide, “... while continuing to recognise the Crown’s right to determine economic policy, for the Reserve Bank of New Zealand, as the central bank, to be responsible for formulating and implementing monetary policy designed to promote stability of the general level of prices” (*Reserve Bank of New Zealand Act 1989, Long title*).

Dealing in foreign exchange by Bank

The Act provides that for the purposes of performing its functions and fulfilling its obligations under this Act or any other Act, the Bank may, from time to time, deal in foreign exchange with such persons, including the Crown, and on such terms and conditions as the Bank thinks fit (*Section 16*).

Power of Minister in relation to foreign exchange

The Act provides that Minister may, for the purpose of influencing the exchange rate or exchange rate trends, from time to time, by notice in writing to the Bank, direct the Bank to deal in foreign exchange within guidelines prescribed by the Minister in the notice. The Minister may from time to time, by notice in writing to the Bank, direct that all foreign exchange dealing by the Bank shall be at rates of exchange, or within a range of rates of exchange, specified by the Minister in the direction and direct the Bank to deal in foreign exchange at those rates or within that range of rates with such persons or class or classes of persons as may be specified by the Minister in the

¹ Reserve Bank of New Zealand Amendment Bill (No 3), 2007 No 174-1, Explanatory note, General policy statement, p. 1.

direction. These directions by the Minister override the policy targets and the Reserve Bank must ignore those policy targets and must comply with the directions regardless of whether or not they “would be inconsistent with the economic objective of monetary policy” (*Sections 17 - 20*).

Foreign reserves

The Act provides that the Minister shall, from time to time, in consultation with the Bank, determine the level at which, or the levels within which, foreign reserves are to be maintained for the purpose of enabling the Bank to exercise its statutory powers and the Bank must hold and maintain foreign reserves at that level or within those levels and, for that purpose the Bank may acquire and deal in foreign currency, deal in foreign currency on behalf of the Crown and appoint any person to acquire and deal in foreign currency on behalf of the Crown or the Bank (*Section 24*).

Regulation of Banks: Part 5 of the Reserve Bank of New Zealand Act 1989

Part 5 of the Reserve Bank of New Zealand Act 1989 is headed; “Registration Of Banks And Prudential Supervision Of Registered Banks” and the sections in Part 5 provide the necessary powers for the Reserve Bank to carry out these functions. Section 68, in particular, provides that the powers conferred on the Governor-General, the Minister, and the Bank by Part 5 must be exercised for the purposes of “promoting the maintenance of a sound and efficient financial system” or “avoiding significant damage to the financial system that could result from the failure of a registered bank”.

The need for the Bill

"As part of the Government's Review of Financial Products and Providers, a new regulatory framework for deposit takers was agreed in September 2007. The new framework will require all deposit takers, as defined in the Bill, to be licensed by the Bank, the directors and senior managers of deposit takers to be subject to fit and proper requirements, and deposit takers to comply with minimum prudential standards prescribed in regulations and enforced by trustees and the Bank. Deposit takers will continue to be subject to trust deed, prospectus, and investment statement requirements under the Securities Act 1978 and will continue to be supervised by trustees.

"This Bill implements part of the new regulatory framework for deposit takers--- mainly, the matters for which prudential regulations may be prescribed. The licensing and fit and proper requirements for deposit takers will be implemented in separate legislation intended to be introduced into Parliament in 2008.

"The existing law is inadequate in setting prudential standards on non-bank deposit takers and provides insufficient support to trustees as the frontline supervisor. Recent collapses of finance companies have demonstrated the need for regulation that raises prudential standards across the industry.

"The objectives for the regulation of deposit takers are to promote a sound and efficient financial system and avoid the significant damage that may occur to the financial system if a deposit taker fails"².

² Ibid.

MAIN PROVISIONS

New purpose section for the Act

The Bill provides that the purpose of the Act is to provide for the Reserve Bank of New Zealand (the Bank), as the central bank, to be responsible for:

- formulating and implementing monetary policy designed to promote stability in the general level of prices, while recognising the Crown's right to determine economic policy; and
- promoting the maintenance of a sound and efficient financial system; and
- carrying out other functions, and exercising powers, specified in the Act (*Part 1, Clause 5, inserting substituted Section 1A into the Act*).

Foreign exchange role

The Bill provides (as is currently provided in the Act) that the Bank may deal in foreign exchange with any person it thinks fit, including the Crown and in addition (and this is new) provides, that the Bank may deal in foreign exchange on behalf of any person, including the Crown (*Part 1, Clause 6, inserting substituted Section 16 into the Act*).

Ministerial direction

The Bill provides that the Minister may direct the Bank to have regard to a government policy that relates to the Bank's functions under Parts 5 to 5C (which relate to the registration of banks and prudential supervision of registered banks) and new Part 5D inserted by this Bill - see below) (which relates to deposit takers) (*Part 1, Clause 10, inserting New Section 68B into the Act*).

Deposit takers

The Bill provides that a deposit taker is a person who offers debt securities to the public in New Zealand and carries on the business of borrowing and lending money, or providing financial services, or both. This includes: building societies as defined in section 2(1) of the Building Societies Act 1965; credit unions as defined in section 2(1) of the Friendly Societies and Credit Unions Act 1982; and a person or class of persons that is declared by regulations to be a deposit taker. It is made clear that the term does not include: an issuer of a collective investment scheme; a registered bank; a local authority; or a person or class of persons that is declared by regulations not to be a deposit taker. An additional person or class of people may be declared to be deposit takers by regulation made by the Governor-General on the advice of the Minister in accordance with the Bank's recommendation (*New Section 157C*). The Bill makes detailed provision in relation to deposit takers including the power for the Bank to exempt persons or classes of persons from compliance with any of the requirements of New Part 5D or regulations made under it (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157A -157H*).

Credit ratings

The Bill provides that a deposit taker must have a current rating of its creditworthiness from a rating agency approved by the Bank (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157I -157K*).

Governance and risk management

The Bill provides that regulations may be made imposing governance requirements, and systems, policies, and standards for managing risk on deposit takers (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157L - 157O*).

Capital

The Bill provides for the making of regulations prescribing amounts and forms of capital and also provides for the making of regulations providing that that trustees must ensure that trust deeds include a capital ratio, calculated in accordance with a prescribed framework, that the deposit taker must maintain (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157P - 157T*).

Exposure and liquidity

The Bill also provides for regulations to be made placing restrictions on exposures of deposit takers to related parties and in relation to liquidity. (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157U - 157ZA*).

Trust deeds

The Bill provides that a trustee may, in certain circumstances, amend a trust deed, without the consent of the deposit taker. The bank is given certain powers over trustees. For example, trustees may be required to report on a deposit taker's compliance and also disclose other information to the Bank (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157ZB - 157ZG*).

Enforcement powers

The Bill provides enforcement powers for the Bank (*Part 1, Clause 11, inserting New Part 5D into the Act, New Sections 157ZH - 157ZL*). New Section 157ZO relates to the application of the Official Information Act.

Offences

The Bill provides for offences (*Part 1, Clause 11, inserting New Part 5D into the Act, New Section 157ZP*).

Breach of credit rating requirement

The Bill provides that the offence of breaching New Section 157I (which relates to the requirement to have a current credit rating) is punishable, in the case of an individual, by imprisonment for a term not exceeding 18 months or a fine not exceeding \$200,000, or both, and in the case of a body corporate, by a fine not exceeding \$2,000,000. The offence of breaching any of the other sections referred to in new section 157ZP is punishable, in the case of an individual, by imprisonment for a term not exceeding 12 months or a fine not exceeding \$100,000, or both, and in the case of a body corporate, by a fine not exceeding \$1,000,000 (*Part 1, Clause 11, inserting New Part 5D into the Act, New sections 157ZT(1) and (2) and 157ZQ*).

Reporting and accounting documents

The Bill makes detailed requirements in relation to reporting and accounting documents (*Part 2, Clause 12, amending Part 6 of the Act, Clauses 13 - 21*).