



ASB Bank Limited
PO Box 35, Shortland Street
Auckland 1140, New Zealand
Telephone +64 9 377 8930
Freephone 0800 803 804
CX10087 Auckland DX Sort
asb.co.nz

ASB's cross submission on the Commerce Commission's draft report for the market study into personal banking services

This response contains confidential, commercially sensitive information which has been highlighted in green. ASB requests confidentiality for the Confidential Information and also that it be withheld from any response to an Official Information Act (**OIA**) request, on the basis that release would unreasonably prejudice the commercial interests of ASB (per 9(2)(b)(ii) of the OIA). In addition, the information has been provided voluntarily as part of the Commission's market study and therefore ought also to be withheld pursuant to section 9(2)(ba) of the OIA, on the grounds that disclosure would be likely to prejudice the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied.

1. Introduction / summary

- 1.1 ASB was pleased to participate in the Commission's recent Conference and it was good to see a high level of engagement across the industry on a range of topics. In this response we comment on some of the issues raised at the Conference and in submissions on the Commission's draft report.
- 1.2 ASB is committed to delivering on our purpose of accelerating financial, social and environmental progress for all New Zealanders. We are proud to support more than 1.5 million personal, business and rural customers, with a team of around 6000 people and network of 80 branches throughout the country.
- 1.3 ASB acknowledges that regulation is important for financial stability and ensuring good customer outcomes. However, a common theme throughout this market study from a broad range of stakeholders has been the impact the overall regulatory burden has on the scope for innovation and competition. We do not support the notion of singling out one piece of regulation or one regulator: it is the aggregation, sequencing and timeframes of all regulation that creates challenges for an industry.
- 1.4 We support the continued evolution of the Council of Financial Regulators (**CoFR**) to ensure a coordinated and appropriately sequenced regulatory agenda; and a role for the Ministry of Regulation regarding future regulation. This will help regulated entities and their regulators to deliver outcomes that best serve New Zealanders and the economy in the long term.
- 1.5 As ASB has outlined in previous submissions, we believe advance risk-based modelling strengthens the overall resilience of the banking system and supports the efficient and effective allocation of capital across the New Zealand economy. Internal Ratings Based (**IRB**) models are widely used internationally for this very reason. The Reserve Bank of New Zealand's (**RBNZ**) analysis shows the risk sensitive capital modelling facilitated by the IRB approach supports New Zealand's financial stability and is therefore ultimately better for customers.
- 1.6 ASB agrees with the RBNZ analysis that shows IRB modelling does not given an advantage to the Domestic Systemically Important Banks (**D-SIB**).

- 1.7 ASB was encouraged to see broad alignment across the industry at the Conference on a number of matters that would support the development of open data in New Zealand. We recommend there should be broad industry collaboration on a design roadmap for open data which sets timeframes and sequencing to ensure the safety and security of banking systems aren't compromised. We also recommend the scope of future deliveries are reworked to ensure functionality that will deliver the most value to New Zealand customers, fintechs and the wider economy are prioritised.
- 1.8 We believe the Government should prioritise a Consumer Data Right, remove address verification requirements and develop a centralised digital ID utilising Government data to assist the development of open data.
- 1.9 ASB would be happy to discuss any aspect of this response with the Commission if that would be helpful.

2. The New Zealand regulatory environment is overly complex

- 2.1 ASB acknowledges that regulation is important for financial stability and ensuring good customer outcomes.
- 2.2 However, there can be legitimate differences of opinion regarding the appropriate extent, sequencing and overall pace of regulation. Throughout this market study, a common theme from a broad range of stakeholders has been the impact the overall regulatory burden has on the scope for innovation and competition.
- 2.3 We do not support the notion of singling out one piece of regulation or one regulator: it is the aggregation, sequencing and timeframes of all regulation that creates challenges for an industry.
- 2.4 While acknowledging the inherent difficulties, we think there is an opportunity among policymakers and regulators to:
- (a) consider the *overall effect of regulation*— bearing in mind that banks like ASB need to also comply with a wealth of international regulation; and
 - (b) *better sequence and coordinate the timing* of the various changes, and the impact this has on consumers.

- 2.5 As discussed in further detail below, ASB would therefore support a **Recommendation** for:
- (a) evolution of the purpose, design and mandate of CoFR, to ensure regulators can deliver a coordinated and appropriately sequenced regulatory agenda, aimed at optimising the impact of regulation; and
 - (b) a role for the Ministry of Regulation regarding competing or coordinating Ministerial priorities,
- so that regulated entities can deliver efficiently to best serve New Zealanders and the economy.

New Zealand needs "right size" regulation

- 2.6 While ASB supports the appropriate use of international best practice, there has been a growing trend of New Zealand regulators adopting regulatory regimes and initiatives from overseas but then adding additional requirements, which, in our view:
- (a) may not give sufficient consideration to the relatively small size of the New Zealand economy and the firms operating within it; and

- (b) creates a higher risk of unintended consequences by adding new components compared to components that have been tested in other markets; and
 - (c) can have timeframes that necessitate tactical technology solutions rather than strategic solutions which add to the burden of legacy technology.
- 2.7 Recent examples include BS11 implementation, the overly prescriptive nature of the Credit Contracts and Consumer Finance Act (**CCCFA**) reforms introduced in 2021 and the approach to preparing for negative interest rates (compared to, for example, Australia). Other examples include the duplicative nature of the Conduct for Financial Institutions (**CoFI**) regime and the Financial Advice Provider (**FAP**) regime under the Financial Markets Conduct Act (**FMCA**). The FAP and CoFI overlaps are further exacerbated by additional Financial Markets Authority (**FMA**) licences required for managed investment schemes and Discretionary Investment Management Service providers under the FMCA.

We believe that better coordination and alignment is needed to develop a sustainable pipeline of regulatory change

- 2.8 ASB's primary focus is on best serving our customers and the New Zealand economy. While we are generally supportive of the purpose of much of the regulatory change proposed, the volume, pace and sequencing of initiatives makes it difficult to operationally comply and limits capacity to pursue strategic and innovation objectives. This creates less optimal outcomes than could otherwise be achieved for our customers and increases operational risk.
- 2.9 Every day ASB processes over [Redacted] million card transactions and over [Redacted] transfers and payments transactions. Every week ASB opens many thousands of new term deposits, savings accounts and transaction accounts. The systems underpinning these transactions must remain operational and resilient 24/7 for our customers and the day-to-day functioning of the wider economy.
- 2.10 Therefore, only so much change can be implemented at once, regardless of how much capital we have to invest. As we have said before, funding is not constraining us, rather change saturation and the availability of skilled resource is what constrains us. Customers can also be impacted significantly by regulatory change, for example the CCCFA changes in 2021 resulted in poorer outcomes for consumers overall.

The role of CoFR

- 2.11 CoFR was established in 2011 and is currently made up of government agencies and regulators: the RBNZ, the FMA, the Commission, the Ministry of Business, Innovation & Employment (**MBIE**) and the Treasury (together the **CoFR Members**). It is chaired by the RBNZ and the FMA. The statutory function of CoFR is to 'facilitate co-operation and co-ordination between members of the council to support effective and responsive regulation in the financial system in New Zealand'.
- 2.12 The current relationship between CoFR Members is governed by a Memorandum of Understanding (**MoU**).¹ Clauses 1.2 and 2.1 of the MoU provide that the purpose of establishing CoFR is to "facilitate consistent cooperation and mutual assistance" between the CoFR Members, by "the exchange[s] of information, ideas and expertise". CoFR Members meet quarterly to "discuss regulatory issues, risks and priorities for financial markets". Meetings are usually attended by the CEOs of each of the CoFR Members.
- 2.13 The current MoU appears to constrain the statutory functions of CoFR by limiting the mechanisms through which co-operation and co-ordination between the CoFR Members is meant to be achieved to the exchange of information, ideas and expertise. The MoU's focus on information sharing could now be regarded as inconsistent with the wider statutory purpose. CoFR's accountability for discharging its statutory function could be made clearer, and explored further.

¹ Available at <https://www.cofr.govt.nz/key-documents/memorandum-of-understanding.html>.

CoFR forums

- 2.14 CoFR Members may share information with each other or “within CoFR forums” that are “joint interest matters”, as set out in clause 4.1 of the MoU. “Joint interest matters” are matters that are of joint interest between the CoFR Members and/or CoFR forums, that “relates to the regulation of New Zealand’s financial system”. The MoU does not define “CoFR forum”, however CoFR’s current sub-committees are:
- (a) The **Banking Forum**, which is governed by a Terms of Reference (**ToR**) dated April 2014.² The purpose of this forum is to “coordinate the work of several government agencies that regulate banks”.³ Its ToR states that it “aims to contribute to the efficiency and coordination of banking sector regulation”. This forum meets quarterly.
 - (b) The **Insurance Forum**, which was established in October 2021 and is governed by a ToR.⁴ The purpose of this Forum is to “contribute to the efficiency and coordination of insurance sector regulation” through quarterly meetings.⁵
 - (c) The **Monitoring and Coordination Forum**, which was established in June 2022 and is governed by a ToR dated August 2023.⁶ This ToR is reviewed annually as part of the first meeting of this Forum of each calendar year. The Forum members are the RBNZ, the FMA, and the Commission. The purpose of this Forum is to “improve the sharing of information, including best practice” and “the understanding of operational activity in areas of shared regulatory remits”.⁷ This is not a decision-making body, but may make recommendations to the members that are consistent with its purpose.

Improving effectiveness of CoFR in aligning and coordinating regulators

- 2.15 According to the MBIE website, CoFR was last assessed as Fit for Purpose in 2017.⁸ We believe a refreshed assessment would be helpful. A collective view on longer-term strategic priorities of the financial system should be a critical part of a new mandate. We believe there is an opportunity to better engage at that strategic level than currently occurs. This requires the New Zealand Banking Association (**NZBA**), other industry bodies and regulated entities to work differently with CoFR.
- 2.16 A key example of this are the concurrent streams of work on open data, CDR, digital cash, digital ID, real-time payments, fraud and scams prevention and mitigation initiatives. None of this work is happening (or should happen) in isolation, yet that is what is occurring. Alignment on future state, clear sequencing and clarity on prioritisation is crucial to ensure benefits for New Zealanders are realised by ensuring an appropriate balance so that regulated entities can prioritise resource to innovation.
- 2.17 CoFR is further challenged by CoFR members reporting to different Ministers, who are (naturally) pursuing and promoting their own portfolio agendas. This can result in CoFR members running major consultations or implementing significant regulatory change at the same time, with limited ability to respond to concerns raised by industry regarding the timing and sequencing of reforms, if implementation is codified into statute.
- 2.18 Other points of note would include the following:
- (a) The CoFR Regulatory Charter acknowledges the twin peaks model on which New Zealand’s financial regulation is based and describes how the CoFR Members work together. It appears to be quite outdated, with references to a review of the Financial

² Available at <https://www.cofr.govt.nz/files/banking-forum-terms-of-reference.pdf>.

³ Available at: <https://www.cofr.govt.nz/about-us/our-sub-committees.html>.

⁴ Available at <https://www.cofr.govt.nz/files/insurance-forum-terms-of-reference.pdf>.

⁵ Available at: <https://www.cofr.govt.nz/about-us/our-sub-committees.html>.

⁶ Available at <https://www.cofr.govt.nz/files/monitoring-and-coordination-forum-terms-of-reference.pdf>.

⁷ CoFR “Monitoring and Coordination Forum (MCF) – Terms of reference” at page 1. Available at: <https://www.cofr.govt.nz/files/monitoring-and-coordination-forum-terms-of-reference.pdf>.

⁸ Available at: <https://www.mbie.govt.nz/cross-government-functions/regulatory-stewardship/regulatory-systems/financial-markets-regulatory-system>.

Advisers Act 2008 and the IMF Financial Sector Assessment Programme to be conducted in 2016 (both on page 8 of the Charter). It is unclear the extent to which the Charter remains relevant or operative, but it does not appear to have been replaced.

- (b) There are only three CoFR forums, of which only two are targeted at particular sectors (banks and insurers) within the wider financial services industry.
- (c) The CoFR banking and insurance forums are only attended by industry bodies such as the New Zealand Banking Association (**NZBA**), Financial Services Council (**FSC**) and the Insurance Council of New Zealand (**ICNZ**). Given the large number of members these Associations represent they are often constrained in their ability to provide meaningful feedback or input if there are differing views amongst their memberships. NZBA represents 17 banks of varying sizes, business models and risk profiles.⁹ The FSC has over 100 members, which includes life and health insurers, investment managers, KiwiSaver providers, among others.¹⁰
- (d) The Commission's market study has highlighted the need for all affected stakeholder groups to have a seat at the table to feed into needs and cost/benefit analysis and impact assessments of proposed new regulation or regulatory reform. For example, consumer groups and fintechs are not represented at present, and we believe they should be where appropriate.
- (e) A key output from CoFR is the quarterly regulatory initiatives calendar. While this is a useful document for tracking upcoming regulatory consultations or reforms, it does not extend beyond 8-9 months into the future. This does not provide enough certainty for banks to adequately anticipate and plan the resourcing and funding required to consult on proposals thoroughly or implement changes safely. It also does not consider what the trade-offs may be for banks and ultimately customers. It needs to take into account significant global regulation (e.g. our commitments to the Financial Action Task Force in respect to the Anti-Money Laundering and Countering Financing of Terrorism Act (**AML/CFT**) and implementation of ISO 20022) that all banks must execute.

International examples

- 2.19 As part of assessing the scope for improvements to be made, it is useful to look at overseas jurisdictions, which we summarise below.

Australia

- 2.20 The New Zealand CoFR mirrors the Australian Council of Financial Regulators, which is comprised of the Australian Prudential Regulation Authority (**APRA**), the Australian Securities and Investments Commission (**ASIC**), the Reserve Bank of Australia (**RBA**), and Treasury. The Australian version was established in 1998 in response to a recommendation by the Financial Systems Inquiry in its 1997 report for a collaborative, non-statutory structure. Its Charter allows for the exchange of information and views on financial regulation, and coordination between members where members' responsibilities overlap.
- 2.21 However, in response to inefficiencies in coordinating regulation, on 11 March 2024 the Albanese Government announced plans to introduce a financial sector regulatory initiatives grid to ensure regulation is carried out in a more coordinated way. The "regulatory grid" is intended to help financial services businesses engage with the Government and regulators more effectively and allow regulators to avoid duplication, build shared strategic priorities, and focus on how to best implement reforms. In turn, it will allow regulated entities to allocate their resources more efficiently when implementing regulation, reducing compliance burden and costs.
- 2.22 It is to be modelled on the grid in place in the United Kingdom and will be a rolling, 24-month forward looking programme of regulatory initiatives that affect the financial sector. It will be

⁹ See <https://www.nzba.org.nz/about-us/members/>.

¹⁰ See <https://www.fsc.org.nz/who-we-are-fsc>

established and administered by the Australian Treasury and include proposed legislation, rule, and regulation and standard making, consultation processes, and data collection processes.

- 2.23 Australian Banking Association CEO Anna Bligh said providing a clearer picture of the future regulatory landscape would allow the Government to implement policy initiatives while at the same time reducing the compliance burden on industry:¹¹

With almost 1200 pages of new laws and regulations placed on the banking sector in the past four years, any initiatives that will allow banks to better plan and coordinate future regulation is welcome [...] Better coordination of regulation will provide more certainty for banks and ensure the sector continues to deliver for customers and the economy [...] Being able to better navigate regulatory reform will allow banks to reduce compliance costs and invest more in areas such as innovation and new technology.

United Kingdom

- 2.24 The UK launched the Financial Services Regulatory Initiatives Forum in 2020. Its members include the Bank of England (**BoE**), Competition and Markets Authority, Financial Conduct Authority (**FCA**), Financial Reporting Council, HM Treasury (**HMT**) (Observer member), Information Commissioner's Office, Payment Systems Regulator, the Prudential Regulation Authority (**PRA**) and the Pensions Regulator. The FCA and BoE/PRA co-chair the Forum.
- 2.25 The first bi-annual Regulatory Initiatives Grid was published in April 2020. The Grid outlines the regulatory pipeline for the following 24 month period. The Grid was intended to give clarity to the financial services industry and other stakeholders to understand and plan for initiatives that may have a significant operational impact on them.

Portugal

- 2.26 The Portuguese National Council of Financial Supervisors (**CNSF**) was created in 2000. It is made up of the three financial supervisory authorities: the Insurance and Pension Funds Supervisory Authority, the Bank of Portugal, and the Securities Market Commission.
- 2.27 It was designed for coordination and exchange of information between the various supervisory authorities, and is also entrusted promoting supervisory rules and practices, and preparing draft regulations on cross-sectoral issues. Shortly after the implementation of the CNSF, the International Monetary Fund recognised that the CNSF framework was working well, noting that "From the conversations held with the three regulators, the assessor concludes that the CNSF has in fact proven useful in coordinating actions and eliminating possible sources of regulatory arbitrage."¹²
- 2.28 The 'skills' webpage of the CNSF website provides that, in addition to coordinating actions and exchanging information between the supervisory authorities, the CNSF formulates regulatory proposals on matters relating to more than one supervisory authority.¹³ It also issues opinions and formulates recommendations within the scope of the members' respective competencies. The CNSF performs consultative functions for the Bank of Portugal (the national macroprudential authority) for matters relating to the identification, monitoring, and assessment of the risks to the stability of the financial system, and assessments of macroprudential policy proposals to mitigate or reduce systemic risks to the financial system. These matters – particularly the formulation of regulatory proposals for cross-sectoral issues, and the reporting to a national macroprudential authority – are not functions that are seen in the CoFR MoU or Charter.
- 2.29 Unlike CoFR, CNSF produces its own annual activity report to the Assembly of the Republic (the Portuguese Parliament), and the member of the Government responsible for finance, by 31 March

¹¹ Available at: <https://www.ausbanking.org.au/banks-welcome-federal-governments-commitment-to-a-regulatory-roadmap/>.

¹² International Monetary Fund "Detailed Assessment of Observance of IOSCO Objectives and Principles of Securities Regulation" (January 30 2007), at page 12. Available at: <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Portugal-Financial-Sector-Assessment-Program-Detailed-Assessment-of-Observance-of-IOSCO-20339>

¹³ See <https://www.cnsf.com.pt/competencias>

each year. CNSF also produces a summary of the legislative initiatives involving its members each year (similar in concept to the quarterly regulatory initiatives published by CoFR) and releases public consultations on these matters.

“Right-sized” solutions for the New Zealand market

Regulatory coordination and alignment

- 2.30 ASB believes the Commission should **Recommend** improvements to the design and purpose of CoFR, to ensure regulators can deliver a coordinated and appropriately sequenced regulatory agenda, aimed at optimising the execution of regulatory objectives.
- 2.31 This can be achieved by adopting all of the following.
- (a) **Update the CoFR Charter** to give effect to its statutory function and objectives as outlined in the RBNZ Act. The Charter should include descriptions of each CoFR Member’s roles and responsibilities and how they fit under the twin peaks model. This could be useful to identify areas of overlap between CoFR Members / statutory frameworks (i.e. where our regulatory system differs from a strict twin peaks model). Such differences could be analysed to look for inefficiencies, duplication or a blurring of the lines of each Member’s remit under the twin peaks model.
 - (b) **Amend CoFR MoU and Forum ToR to broaden the means by which the CoFR Members can engage with each other and market participants.** A key objective would be CoFR Member alignment on:
 - (i) setting 2-5 year strategic plans for delivering regulatory change. These strategic plans should have explicit regard to optimising efficiency and impacts for New Zealanders without unduly inhibiting regulated entities’ capacity to innovate; and
 - (ii) enabling greater engagement and collaboration with regulated entities and other stakeholder groups to assist regulators to avoid duplication, build shared strategic priorities, and focus on how to best implement reforms,

which should create more certainty for regulated entities to allocate their resources more efficiently, reducing compliance burden and costs, and facilitating innovation to better serve customers.
 - (c) **Establish CoFR Impact Assessments and Post implementation reviews:** CoFR should adopt impact assessments at the design phase of proposed reforms, which would involve collecting relevant data directly from market participants and industry bodies, to develop cost-benefit analysis and ensure the timing of delivery is considered against the 2-5 year strategic plan and in light of regulatory reforms already underway.
 - (d) **Establish broader CoFR industry forums:** investment, KiwiSaver and fintech forums should be established to ensure the views and strategic goals of interest groups are appropriately considered.
 - (e) **Broaden representation at CoFR Industry Forums:** CoFR needs to hear directly from a broad section of big and small banks, NBDTs and fintechs, which will all be impacted by regulation and will all have important viewpoints.
- 2.32 We also believe the oversight and governance of CoFR could be improved to ensure it better meets its objectives. This will be even more important should its MoU be expanded to coordination on efficient regulatory change.

Ministerial coordination and decision making powers over CoFR

- 2.33 CoFR Member's delivery timeframes are often dictated by government agency or ministerial priorities, or where regulatory delivery timeframes are enshrined in law. A key example is MBIE which currently answers to 14 Ministers and two parliamentary undersecretaries. Multiple Ministers will inevitably create competing priorities and potential conflicts, and also increases the risk of duplication and a lack of unified direction.
- 2.34 Like CoFR Members, Ministers and government agencies need to have regard to the aggregate legislative and regulatory landscape and its sequencing, particularly where there are significant reform programmes from multiple agencies which will impact a sector within a condensed timeframe.

- 2.35 **Recommendation:** The newly established Ministry for Regulation should play a role in reviewing and considering the future government agency, Ministerial and other regulatory initiatives in the financial services sector.
- 2.36 New oversight of, and governance over, CoFR's performance against its Charter, MoU and Forum Terms of Reference should be established by either:
- (a) Treasury or the Minister of Finance having oversight of CoFR's performance. This mirrors the current plans for the financial regulation "grid" being introduced in Australia; or
 - (b) broadening the remit and scope of the Ministry for Regulation to enable the Minister for Regulation to have decision-making powers and approval over a rolling 2-5-year strategic CoFR plan. This should be in consultation with relevant government agencies and Ministers, such as the Minister for Commerce or Consumer Affairs. Approval of the plan should be required before legislation is passed giving effect to new reforms, to ensure implementation deadlines under legislation have been appropriately prioritised and sequenced. Where government agencies or CoFR members cannot align, we consider that the Minister for Regulation or (by delegation) Minister for Commerce or Consumer Affairs should have the ability to decide the regulatory change agenda for financial services, having regard to appropriate pace and sequencing of change and giving regulated entities space to deliver on their strategic and innovation objectives that will help them best serve the long term interests of New Zealanders.

3. Prudential regulation

Benefits of IRB models for risk management

- 3.1 As ASB has outlined in previous submissions, advanced risk-based modelling strengthens the overall resilience of the banking system and supports the efficient and effective allocation of capital across the New Zealand economy by better matching capital to risk. Internal ratings based (IRB) models are widely used internationally for this very reason, including in Australia, the European Union, United Kingdom, Canada and Singapore (among other jurisdictions). We set out below some comments from APRA in Australia and the RBNZ on this point.
- 3.2 APRA: "Risk-weights under the IRB approach are tailored to the risks of an individual bank and are more precise than standardised risk-weights (that is, sensitive to a wider range of borrower and portfolio risk characteristics). Therefore, the IRB approach leads to more accurate risk measurement, which enables a better alignment of capital to risk".¹⁴
- 3.3 RBNZ: "An aim of the IRB approach is to improve banks' understanding and management of the credit risk in their loan portfolios by encouraging granular modelling of risks. The supporting

¹⁴ Available at: [https://www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans#:~:text=Risk%2Dweights%20under%20the%20IRB,borrower%20and%20portfolio%20risk%20characteristics\).](https://www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans#:~:text=Risk%2Dweights%20under%20the%20IRB,borrower%20and%20portfolio%20risk%20characteristics).)

process and governance requirements for IRB accreditation help to reinforce improved risk management.”¹⁵

- 3.4 RBNZ: “Suggested changes to the risk-weighting framework in the [Commerce Commission’s] draft report would lead to very marginal benefits to competition, relative to other cost factors that smaller banks face compared to their larger peers (e.g. operating expenses). Changes to the IRB approach could result in unintended consequences such as undermining efficiency, risk management in the industry, and put us out of step with international regulatory approaches.”¹⁶
- 3.5 ASB agrees with RBNZ’s analysis which shows that IRB modelling does not give an advantage to the D-SIBs. The modelling contained in Annex 1 to ASB’s cross submission on the Commerce Commission’s Preliminary Issues paper came to the same conclusion. The RBNZ cost benefit modelling undertaken as part of the 2019 Capital Review demonstrated the importance of financial stability to New Zealand’s economy. The risk sensitive capital modelling facilitated by the IRB approach supports New Zealand’s financial stability and is therefore ultimately better for consumers.

Further Information on ASB’s IRB model for Home Lending

- 3.6 In response to the Commission’s request, we have provided further information on ASB’s IRB model for home lending below, which we trust will assist the Commission to understand the benefits of, and restrictions on, IRB modelling.
- 3.7 The RBNZ approved IRB capital models for home lending have been designed to create stable levels of capital requirements through economic and house pricing cycles. The RBNZ has specified the types of model input parameters that can be used, which are aimed at reducing cyclicity in models where capital would rise in bad times and fall in good. The two key elements of the IRB risk weight calculation for home lending are the probability of default (**PD**) and loss given default (**LGD**). Banks base the PD model on attributes that are collected at origination. At ASB these include:

[Redacted]

- 3.8 The LGD is based on the RBNZ’s requirements, as set out in the following table:

Table 1: Minimum LGD for residential mortgage loans

LVR	LGD <i>Non property- investment residential mortgage loan</i>	LGD <i>Property- investment residential mortgage loan</i>
90% and over	38.00%	40.00%
80-89%	33.25%	35.50%
70-79%	28.50%	31.00%
60-69%	19.00%	21.50%
Under 60%	10.00%	12.50%

- 3.9 As Table 1 shows, this is driven by the LVR of the loan. Crucially, the value for the purposes of this calculation is based on the value when the loan is originated, rather than current estimates. The combination of using LGD based on origination LVR and the approach to PD modelling

¹⁵ RBNZ, Submission on personal banking services market study: draft report, at page 6.

¹⁶ RBNZ, Submission on personal banking services market study: draft report, at page 5.

creates very stable capital through the cycle – for instance, it avoids large reductions in capital requirements in periods of high house price inflation.

Comparison of capital for defaulted loans IRB vs standardised

3.10 Another relevant factor is that IRB banks have to provide significantly more capital for defaulted home loans than standardised banks, which does lift capital requirements during tougher economic times. The conservatism around mortgage defaults under the IRB can be seen through ASB’s March 2024 data, which reveals that:

- (a) if ASB was operating a standardised basis then the standardised model would have meant that [Redacted] of ASB’s loans would have been assessed as defaulted, requiring ASB to hold [Redacted] Risk Weighted Assets for capital purposes;
- (b) but in practice, the IRB model assessed that [Redacted] of exposure should be considered as defaulted, requiring ASB to hold [Redacted] Risk Weighted Assets for capital purposes.

3.11 Differences like this mean that if New Zealand was to have a significant downturn then IRB banks will have higher risk weights than the 85% minimum vs the standardised method.

Improvements to Risk Sensitivity of Standardised Home Lending Model

3.12 ASB has previously submitted that the risk weights for home lending under IRB are more risk sensitive than those for the standardised model. See, for example, the table provided with ASB’s submission on the draft report, replicated below for ease of reference.

Table 2: APRA and Basel III risk weights for performing loans by LVR bands in comparison to RBNZ standardised and ASB IRB models

Owner Occupied:							
Current LVR Band	a. 0% to 50%	b. 50.01% to 60%	c. 60.01% to 70%	c. 70.01% to 80%	d. 80.01% to 90%	e. 90.01% to 100%	f. > 100%
IRB risk weight	[Redacted]						
RBNZ STND Risk weight	35%	35%	35%	35%	50%	75%	100%
Basel 3 STND Risk weight	20%	25%	30%	30%	40%	50%	70%
APRA STND Risk weight	20%	25%	30%	35%	50%	70%	85%
Investor:							
Current LVR Band	a. 0% to 50%	b. 50.01% to 60%	c. 60.01% to 70%	c. 70.01% to 80%	d. 80.01% to 90%	e. 90.01% to 100%	f. > 100%
IRB risk weight	[Redacted]						
RBNZ STND Risk weight	40%	40%	40%	40%	70%	90%	100%
Basel 3 STND Risk weight	30%	35%	45%	45%	60%	75%	105%
APRA STND Risk weight	25%	30%	40%	45%	65%	85%	105%

3.13 As APRA states in its “Demystifying credit risk capital requirements for housing loans”, under the standardised approach, capital requirements for housing lending are based on a common set of risk-weights prescribed by APRA.¹⁷ Standardised risk-weights are generally calibrated at a conservative level because they are less precise, apply to a wide range of banks, and aim to

¹⁷ Available at: [https://www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans#:~:text=Risk%2Dweights%20under%20the%20IRB,borrower%20and%20portfolio%20risk%20characteristics\).](https://www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans#:~:text=Risk%2Dweights%20under%20the%20IRB,borrower%20and%20portfolio%20risk%20characteristics).)

ensure that standardised banks are adequately capitalised on an overall basis. While risk-weights are generally more conservative, there is a lower burden on standardised banks in terms of other supervisory requirements, including the management of internal risk models and data reporting.

- 3.14 The APRA implementation of the Basel III standardised risk weights is more risk sensitive than the standardised risk weights currently adopted by the RBNZ. For example, the RBNZ requires the same capital for a 50% LVR loan as for an 80% LVR loan, while APRA requires 42% lower capital. It should be noted that the APRA implementation is slightly more conservative than the base Basel III standard.

- 3.15 Given that IRB models are internationally regarded as best practice in terms of matching capital to risk, to the extent the Commission has any residual concern regarding the standardised vs IRB dynamic, ASB would support a **Recommendation** that the RBNZ consider whether a more risk sensitive implementation of the standardised method is appropriate for New Zealand.

Effect of the Deposit Compensation Scheme (DCS)

- 3.16 Credit ratings and market pricing of different financial institutions highlights that, unsurprisingly, some are riskier than others. However, as ASB has previously submitted, the fact the DCS proposals do not in our view properly reflect the *market's* view as to the relative riskiness of various firms, they are already heavily skewed towards promoting competition.¹⁸ In our view, this is evidence of the RBNZ taking into account competition factors.
- 3.17 As to the implications of this approach, [Redacted]. This suggests that the DCS could have a significant impact on encouraging consumers to engage with different providers, which may well include providers which consumers have seen as 'riskier' previously.

4. **Relevance of Kiwibank as a competitive constraint / strength of competition**

- 4.1 As ASB has previously emphasised, Kiwibank is one of the key competitive constraints on ASB. Kiwibank is already a strong industry player and has seen significant growth in recent years. ASB thinks about Kiwibank in the same way it thinks about all of the other large banks:
- (a) ASB tracks all relevant aspects of its offering in exactly the same way it does with the other large banks, e.g. the rates it offers to customers, its customer engagement, its promotional activity and its product development; and
 - (b) there are also a raft of other internal ASB metrics which draw no distinction between Kiwibank, ANZ, BNZ and Westpac.
- 4.2 For example, we include a confidential extract of an ASB pricing committee paper below, previously provided to the Commission as part of its RFIs last year. This extract show [Redacted].

Figure 1: Confidential Pricing Committee extract

[Redacted]

- 4.3 Other evidence on the record also shows the relevance of Kiwibank. In its draft report the Commission said "Main bank' relationships (held predominantly by the four major banks) are beneficial because these customers often default to their existing service provider when adding or renewing services. Once a customer is committed to the same provider for several services, they are significantly more likely to stay with that provider".¹⁹ March 2024 survey data reveals that more customers consider Kiwibank to be their main bank than they do BNZ (11% vs 10.4%).²⁰ As the Commission is aware, Kiwibank has outperformed the market in home loans over the past five

¹⁸ See, for example, ASB's response to the Commerce Commission's draft report for the market study into personal banking services, at paragraphs 3.8 to 3.12.

¹⁹ Commerce Commission's Personal banking services market study draft report, at page 31.

²⁰ Based on Retail Market Monitor rolling 6-month survey data recording main bank relationships, produced by Camorra, as at March 2024.

years, and given the continued increase in customers considering them to be their main bank, this is likely to continue.

- 4.4 ASB also continues to disagree that competition is “sporadic”. We compete daily to ensure that our overall offering is competitive. Like all industries it may be that at a particular moment in time a particular bank may be more or less focussed on market share vs margin, or vice versa. ASB’s loss of home loan market share when it took the view that pricing was unsustainably low is a recent example. As this simple example shows, the approach of banks at a moment in time is not at all predictable, which means that no bank can sit back and assume it will retain or win its fair share of customers without competing hard to do so.

5. Open Data

Alignment at the conference

- 5.1 There is strong support for open data across sectors. While there was naturally some disagreement as to some of the detail, including among different stakeholder groups, ASB was encouraged to see broad alignment across the industry at the Conference on a number of matters that would support the development of open data in New Zealand, including the following, which we think could form the basis of some useful recommendations.

Recommendations

- (a) There should be broad industry collaboration to:
- (i) design a roadmap for open data, which factors in current and planned regulatory change, and sets timeframes and sequencing to ensure that the safety and security of banking systems are not compromised, and which sees change developed at a pace that can be absorbed by the financial services industry, Government and consumers; and
 - (ii) rework the scope of future deliveries (e.g. API v2.3) to ensure prioritisation of functionality that will deliver the most value to New Zealand customers, fintechs and the wider New Zealand economy. In ASB’s view, this should include ensuring real-time fraud mitigations such as confirmation of payee and digital identity, and the inclusion of Kiwibank on the same timeframes as the other banks.
- (b) The Government should:
- (i) prioritise a Consumer Data Right, remove address verification obligations from the AML/CFT Act, and develop a centralised digital ID utilising Government data, all of which would significantly assist the development of the digital economy, open data (as well as switching more generally) and assist to address rising fraud and scam risks; and
 - (ii) support cyber control standards, which will need Government and Police involvement and an appropriate framework for the participation of high-risk providers (e.g., cryptocurrency businesses) or providers requesting information that is inappropriate (e.g., log in and password details from customers).

- 5.2 As ASB has previously emphasised, the purpose of regulation is to prevent harm. It is therefore important that any regulation of payments applies equally to all providers that participate in payments (e.g., Apple), rather than focusing on only certain entities. The focus of regulation on banks rather than all providers of a service stifles innovation and competition and leaves consumers of insufficiently regulated providers unprotected, undermining consumer trust.

Kiwibank's involvement

- 5.3 ASB notes the comment at the Conference that Government agencies such as NZ Transport Agency Waka Kotahi and the IRD have said they will continue to use POLi until Kiwibank is part of open data.²¹ Given other comments from Revolut that support from government agencies materially enhances consumer uptake of open data, and that Kiwibank has over 1 million New Zealand customers (and more customers who consider it to be their 'main bank' than BNZ), any recommendation which excludes Kiwibank from the same deliverables as the other large banks would impede the overall delivery of open data to the detriment of New Zealand consumers.
- 5.4 While ASB acknowledges and understands the points made by Kiwibank that complying with the open data requirements has implications for other initiatives, the same is true for all banks, and in ASB's view, from an overall "NZ Inc" perspective, the higher national adoption of open data via government use and promotion should outweigh any such concerns at the individual bank level.

6. **Switching***Multi-banking and the switching service*

- 6.1 Multi-banking, and a lack of bundling in New Zealand, allows customers to choose the best products available at any one time. As there are no costs to continuing to hold a transaction account at ASB, customers will not generally close an account when they want to begin using a different provider. This makes it easier for customers to move between suppliers in the market and thus facilitates competition. The Commission has recognised as much in numerous merger decisions.
- 6.2 But even putting that to one side, if a customer does want to 'switch' in the traditional sense, the evidence is that it is easy and efficient to do so.

The switching service 'Easy Switch'

- 6.3 According to Consumer NZ's submission on the draft report, citing its latest survey, of the customers that had switched in the previous 12 months, 87% found it easy, and only 7% found it difficult.²² This, and other comments made at the conference, suggests that issues with New Zealand's current process is very much an issue of customer perception, rather than issues with the workings of the service itself.
- 6.4 For example, 95% of the switching requests that ASB processes are completed within five working days, while the delays in 5% of cases are invariably due to payment cancellations and the migration of automatic payments and dependencies on third party initiators. The five working day timeframe in the New Zealand process is in contrast to the seven working day timeframe under the UK's Current Account Switch Service (which also requires customers to provide two forms of re-identification and proof of address to comply with money-laundering regulations).
- 6.5 Removal of address verification requirements, revisions to reliance provisions under the AML/CFT regime and development of a centralised digital ID would further assist consumers to switch providers.
- 6.6 Given the underlying switching service in New Zealand is very good, we think that any recommendations can be very targeted. We encourage the Commission not to dispense with a well-established process that works, given that doing so would add unnecessary cost and complexity (particularly in favour of a system that has its own downsides).

²¹ Consumer NZ Submission on the Personal Banking Services Market Study – Draft Report, at page 11.

²² Consumer NZ Submission, at page 9. In fact, it appears that the survey found 64% said it was "very easy", with 23 saying it was "easy", <https://www.consumer.org.nz/articles/is-switching-banks-easy>

In terms of potential **Recommendations**:

- (a) ASB acknowledges more could be done to improve customer visibility of how well the Easy Switch process works, and so supports a recommendation which would see an increased promotion of the service to customers; and
- (b) ASB supports any recommendation requiring banks / Payments NZ to report on objectively measurable KPIs in relation to their processing of switch requests.

7. Profitability

7.1 The New Zealand economy and the performance of New Zealand banks are closely linked. Strong, stable, well-funded banks are critical to supporting economic growth.

7.2 To attract capital for banks, an appropriate return on capital is needed. This ultimately supports the stability of the financial system. Shareholders have many choices about where and to which parts of their business they decide to deploy capital – without a reasonable return on capital the economy will not get the funding required to grow. This is important: banks have built up a capital base sufficient to increase total bank lending by \$268 billion since December 2008.²³

7.3 It is therefore important that a banking sector remains well-capitalised as this maintains confidence in the banking system which supports financial stability.

Comments on the Commission's profitability analysis contained in Attachment C of the draft report

7.4 In light of continued discussion regarding profitability, ASB makes the following comments on the Commission's analysis in Attachment C of the draft report.

7.5 We don't agree with the Commission's view (Paragraph C98) that it has seen no evidence that the risk borne by Australian shareholders of New Zealand's major banks is larger than that borne by any other investor in a bank operating in New Zealand. The Australian parent banks take on reputational and contagion risks from owning sizable New Zealand subsidiaries that are unique amongst owners of New Zealand-domiciled banks.

7.6 As Table C2 and Paragraph C94 of the Commission's draft report state: "The Australian-owned banks also generally have the highest credit ratings of the banks operating in New Zealand (as shown in Table C2) and the strength of the Australian parent companies appear to partly drive this difference."²⁴ We concur with Table C2's identification of the superior credit ratings of the Australian-owned banks and note our experience is indeed that these credit ratings are driven by the strength of the parents.

7.7 According to the Treasury credit rating agencies indicate that, in the absence of the 'uplift' from the Australian parents, the Australian-owned New Zealand banks would have a credit rating of two to three notches lower (i.e. A instead of AA-) without the expectation that the parent banks will provide financial support to their New Zealand subsidiaries.

7.8 In practical terms this means that ASB is able to borrow money offshore to grow the economy, at cheaper rates than if CBA's support did not exist. This has positive impacts for New Zealanders and the economy more generally.

7.9 The financial backing by the Australian parents of their New Zealand subsidiaries increases their financial exposure beyond their own stand-alone exposures. The Treasury itself alludes to the parent banks requiring a higher return on their New Zealand banking investments to compensate for the higher risks being taken from investing in New Zealand.²⁵

²³ RBNZ statistics on bank long-run total loans and assets. Available at: <https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/statistics/series/l-s/s10/hs10-long-run.xlsx>.

²⁴ Commerce Commission's Personal banking services market study draft report, at C94.

²⁵ See <https://www.treasury.govt.nz/sites/default/files/2023-07/b23-tax-4791084.pdf>.

- 7.10 Finally, in regard to the dividend franking issue, we do not think it is relevant that New Zealand subsidiaries only make up 20% of Australian parent profits (as set out by the Commission in paragraph C103). The Australian shareholders need to earn a return that justifies the risk they take on in owning the New Zealand subsidiaries. Shareholders have real choices about where and when they deploy capital and the marginal returns on capital across various opportunities is a key component of this.

We trust this response is helpful. As noted earlier, ASB would be happy to discuss any aspect of this response with the Commission if that would be of assistance.