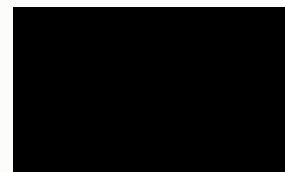




ASB Bank Limited



## ASB response to the Commerce Commission's draft report for the market study into personal banking services

### 1. Whakarāpopototanga Summary

- 1.1 ASB Bank Limited (**ASB**) welcomes the opportunity to respond to the Commerce Commission's (**Commission**)'s draft report for the market study into personal banking services (**draft report**).
- 1.2 We are committed to being a great bank and delivering on our purpose of accelerating progress for all New Zealanders. ASB provides products, service and support to over 1.5 million personal customers and our people work hard every day to retain these customers and attract new ones.
- 1.3 ASB supports many of the Commission's preliminary recommendations and we are already progressing several of these, independently of the current process. For example, we have supported lending for Māori freehold land since 2014 and we are well progressed with the development of a basic bank account product that will better support customers in vulnerable circumstances. ASB already pro rates clawbacks on broker commissions and customer cashback incentives. However, there are some draft recommendations which raise serious concerns for ASB given the risk they present to the long-term stability of the financial system in New Zealand, and in turn a direct adverse impact on individual customers.
- 1.4 The Commission's recommendations propose significant changes to the Reserve Bank of New Zealand's (**RBNZ**) prudential settings, the legal framework focused on the financial safety and stability of financial institutions and the broader financial system. These settings are currently based on the Basel framework, the global standards for banks.
- 1.5 The importance of a safe and secure financial system to consumers and New Zealand cannot be understated. Price competition, availability of new credit and new customer experiences will only occur where there is financial stability.
- 1.6 In suggesting that the RBNZ should place greater weight on competition, as opposed to stability, the Commission has placed insufficient weight on the fact that:
  - (a) the RBNZ's approach to capital requirements for New Zealand banks, including the internal ratings and standardised options, is aligned to the approach set out by the Basel Committee into Banking Supervision (**BCBS**) which is the global standard for banks;
  - (b) when analysing the impact on capital requirements of the internal ratings based (**IRB**) models versus the standardised approach, it is critical to also account for the additional capital the domestically systemically important banks (**D-SIBS**) using IRB must hold due to the 2% buffer;
  - (c) the upcoming Deposit Compensation Scheme (**DCS**) is already heavily skewed towards promoting competition. In ASB's view, the proposed risk-based levy framework is unlikely to appropriately reflect the risks of the entities paying these levies. The current levy proposals

(which place significant weight on competition) could significantly mis-price the risks associated with some riskier deposit takers, which could undermine financial stability should these riskier deposit takers see increased deposit inflows once the scheme commences. To require the RBNZ to give even more weight to competition would further exacerbate the risk to financial stability, and in turn a direct adverse impact on individual consumers (beyond the limits of the DCS); and

- (d) the RBNZ engaged extensively with industry during the design of the DCS framework and, noting our comments above, considers the current proposed composite risk adjusted levy will need to be supported by other aspects of the Deposit Takers Act (**DTA**), such as increased supervisory oversight and the design of appropriate prudential standards (particularly for capital and liquidity).

- 1.7 ASB remains committed to open banking and continues to progress the implementation of systems and processes required to support open banking in New Zealand. As we have said consistently, safety must be the first priority for customers. Therefore, combatting the rapidly rising frauds and scams remains our top priority. As part of achieving this, New Zealand needs to move beyond a sole focus on open banking and payments to prioritise the development of a strong and safe digital infrastructure. ASB looks forward to continuing to engage with the Commission and collaborating with the wider industry to build a world class digital infrastructure with safety and security at its core. This must include clarifying the requirements for open banking to be 'fully operational' and appropriately scoping, sequencing and revising implementation plans to address rapidly evolving risks.

## **PART A: Ngā whakautu ki ngā whakatau tauwhāinga ā-māketē matua** Response to key competition findings

This response, including the discussion above 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.

### **2. Introduction**

- 2.1 ASB supports many of the Commission's preliminary recommendations, several of which we are progressing independently of the current process.
- 2.2 However, ASB disagrees with a number of the Commission's conclusions and draft recommendations. In particular, we fundamentally disagree:
- (a) with any suggestion that capital requirements are 'unfairly' tilted in favour of the four larger banks, and more generally with the suggestion that the RBNZ should consider making changes to its settings that, in ASB's view, will reduce the safety and stability of the banking system for all New Zealanders in order to promote competition; and
  - (b) with the characterisation of the market as a 'two-tier' oligopoly with Kiwibank 'stuck in the middle', and that competition between ANZ, ASB, BNZ and Westpac is sporadic.
- 2.3 We will comment on some specific aspects of the draft report below, and then address each of the Commission's draft recommendations.<sup>1</sup>

### **3. Capital requirements**

#### *Use of IRB models*

- 3.1 ASB believes a stable, well capitalised banking system is fundamental to a well-functioning economy, as it provides the base from which competition, lending and the provision of other products of value to customers can occur. International experience confirms that the regulatory framework needs to include all participants who hold customer deposits, rather than focussing purely on the largest players.
- 3.2 The RBNZ approach to capital requirements for New Zealand banks, including the internal ratings and standardised options, is aligned to the approach set out by the BCBS. The BCBS approach is globally implemented and designed to enhance financial stability.
- 3.3 The use of IRB models in particular improves financial efficiencies and is a widely accepted global standard. As APRA has recently stated, "*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.*"<sup>2</sup> Put another way, IRB models are fundamentally 'a good thing' as they more accurately reflect the overall risks associated with lending, compared to standardised models.
- 3.4 Banks using IRB models do not have an overall capital or competitive advantage.<sup>3</sup> This is due to the interaction of the 2% capital buffer (which currently only applies to those banks using IRBs) which offsets the possible benefit from using IRB modelling by virtue of the 85% floor.

<sup>1</sup> The absence of a specific reference in this response to a finding in the draft report does not mean ASB necessarily agrees with that finding.

<sup>2</sup> <https://www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans>

<sup>3</sup> See for example, ASB's PIP Cross Submission at paragraphs 2.3 and 2.4.

- 3.5 'Levelling the playing field' between IRB banks and non-IRB banks was a specific consideration for the RBNZ when setting the 85% floor and the RBNZ's 2019 Capital Reforms as a whole.<sup>4</sup> The 85% floor is high by international standards and non-IRB banks are relatively better off than they would have been if the RBNZ had adopted a floor consistent with those used overseas, with Basel/APRA setting the floor at 72.5% of total risk-weighted assets (**RWA**).
- 3.6 While the *overall* effect of the floor and the buffer is neutral, because IRB models price risks more granularly there will necessarily be some loans which require less capital than the standardised model would require, but equally there will be others (for instance, low equity loans) for which IRB models will require **more** capital. The key point is that the overall position is neutral and reflects a considered decision by the RBNZ as to how to best balance the critical need for financial safety and stability in line with the RBNZ's mandate with other factors, such as competition.
- 3.7 A higher standardised floor would have a negative impact on customer pricing for a large proportion of the market. To the extent there is a concern around relative risk weights for relatively homogenous home lending products, a preferred approach would be for the RBNZ to issue a more granular version of the standardised model (consistent with APRA and the BCBS standards).

#### *Deposit Takers Act and Depositor Compensation Scheme*

- 3.8 The RBNZ's adoption of a relatively high standardised floor is not the only example of the RBNZ having regard to competition issues. An additional example is that smaller lenders look likely to benefit from highly pro-competitive RBNZ settings relative to their risk profiles under the proposed terms of the 'composite risk-based approach' to the DCS levy.
- 3.9 The RBNZ's 11 March 2024 consultation paper on the DCS regulations (**Second DCS Consultation**) includes an indicative range for the DCS levy of between 0.05% (lowest risk deposit takers) and ~0.20% (highest risk deposit takers). In ASB's view this is a far smaller band than would otherwise be required to truly reflect the relative riskiness of many smaller deposit takers (based on their respective credit ratings). These indicative levies compare favourably to the "50-60 basis point funding cost advantage" between small banks and large banks identified by the Commission in the draft report<sup>5</sup>, and the RBNZ's own analysis of deposit rates in the Second DCS Consultation of ~15bps to ~120bps above the major banks.
- 3.10 If the imposed levy does not match the underlying risk, the levy collection over time from these organisations is likely to be low compared to their expected losses from failure, which risks leaving the scheme underfunded relative to the losses it would be expected to cover over the long term.
- 3.11 While ASB has been generally supportive of the RBNZ's proposed approach in our previous submissions, we think the current levy proposals (which place significant weight on competition) could significantly mis-price the risks associated with some riskier deposit takers, which could undermine financial stability should these riskier deposit takers see increased deposit inflows once the scheme commences. To require the RBNZ to give even more weight to competition would further exacerbate the risk to financial stability and in turn a direct adverse impact on individual consumers (beyond the limits of the DCS).
- 3.12 As a result, it will be crucial that the risk-based levy framework for the DCS is supported by other aspects of the DTA, such as increased supervisory oversight and the design of appropriate prudential standards (particularly for capital and liquidity).

<sup>4</sup> See for example, paragraph 268 of the RBNZ 'Capital Review, Consultation Paper 4: How much capital is enough? Response to Submissions': "[t]he 2019 reforms have the effect of increasing the potential for non-systemic banks to compete with the four systemic banks. This is because the 2019 reforms have fewer unintended, uneven, competitive impacts on locally incorporated banks than the current capital framework...However, on balance, the Reserve Bank views the reforms as enhancing competition between banks."

<sup>5</sup> Commerce Commission's draft report for the market study into personal banking services (**draft report**), at 5.52. The 'funding cost advantage' identified by the Commission associated with greater transaction deposits also ignores the significant costs associated with those transaction deposits, including the costs of maintaining a branch network, call centres, payment systems, applications, and complying with AML.

*Financial stability must remain paramount*

- 3.13 We have outlined above how we believe the RBNZ has more than adequately balanced competition with financial stability. By the Commission's own admission, it has not carried out a cost/benefit analysis when developing the draft recommendations.<sup>6</sup> Any suggestion the RBNZ should go even further would risk undermining the stability and security of New Zealand's financial system, which must be paramount given it is the underlying enabler of price competition, availability of new credit and customer choice.
- 3.14 Getting these settings wrong would materially increase the risk of a financial crisis. The cost of any crisis has direct costs on customers through any losses they bear. Furthermore, under the DTA the New Zealand Government (i.e. taxpayers) carries a contingent liability to underwrite losses from a deficiency in the DCS fund until any scheme payments can be recovered through levies on deposit takers.<sup>7</sup>
- 3.15 This is not a theoretical risk. The failure in March last year of Silicon Valley Bank, which was quickly followed by the collapse of Signature Bank and First Republic Bank, in the United States of America (and the subsequent failure of Swiss bank Credit Suisse, which was considered 'too big to fail'<sup>8</sup>) is a cautionary tale of the knock-on effects across the industry and economy of a bank failure (even when involving banks not classed as being 'systemically important'). The extensive finance company collapses in New Zealand between 2006-2012 are other examples of the impact smaller deposit takers can have on financial stability.

**4. Kiwibank and the nature of competition**

- 4.1 ASB disagrees with the Commission's conclusion that Kiwibank is somehow different to New Zealand's other large banks, or that its growth "*has not been fast enough for Kiwibank to be a significant competitive disruptor*".<sup>9</sup> We also believe insufficient weight has been placed on the growing challenge posed by non-traditional banks e.g. the dominance of Apple in the payments space, which is now being looked at internationally.
- 4.2 ASB has already provided extensive evidence in this study on this point – including evidence that Kiwibank is absolutely one of the key competitive constraints on ASB – but we do note that, in our view, the Commission's headline conclusion doesn't sit comfortably with some of the Commission's own findings. For example:
- (a) the draft report concludes that Kiwibank is the "*only provider that has grown consistently at or above system growth over the four-year period*";<sup>10</sup>
  - (b) the Commission includes Kiwibank as one of the five main banks which are said to focus largely on each other when setting interest rates for home loans and savings/term deposits; and
  - (c) Kiwibank is referred to as the same as the 'major banks' when it comes to descriptions of how pricing decisions are made, how interest rates move (concluding that Kiwibank and the major banks rates tend to move together), the effect of funding from deposits, and survey responses regarding consideration of main banking providers, for example.
- 4.3 Finally, while the Commission says it cannot rule out that tacit coordination is occurring in home lending, it does not reach a view that it is occurring. Indeed, many of the Commission's findings suggest it is not a factor. For instance, the Commission notes that the large banks have different strategies over time which see different banks, for example, leading prices down in the market at different times. It also notes "*there is some dynamism in the relative growth of home lending providers' portfolios over time*".<sup>11</sup> The Commission has also found that "*[e]ach of the major banks will have greater or lesser growth ambitions at any point in time, reflecting their individual*

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<sup>6</sup> Draft report, at 1.44.

<sup>7</sup> Deposit Takers Act 2023, subpart 8 – Deficiency in Fund, sections 248 to 250.

<sup>8</sup> See <https://www.thebanker.com/The-Silicon-Valley-Bank-collapse-and-Credit-Suisse-s-last-minute-lifeline-1678982054>

<sup>9</sup> Draft report, at page 73.

<sup>10</sup> Draft report, at 4.13.3.

<sup>11</sup> Draft report, at 4.13.1.

*circumstances and strategies*";<sup>12</sup> and "our analysis of headline interest rates...is consistent with these intermittent strategies of offering best in market interest rates (or not)".<sup>13</sup> The Commission also noted the "relative intensity when all the banks are competing harder".<sup>14</sup>

## 5. Open banking

- 5.1 ASB continues to progress the implementation of systems and processes required to support open banking in New Zealand. ASB recently began onboarding our first open banking partners, who reported excellent feedback on the usability of ASB's diligence process and documentation.
- 5.2 ASB remains committed to open banking. However, as we have consistently submitted, the development of open banking needs to be carefully sequenced to ensure that the safety and security of banking systems are not compromised. This is especially important with New Zealand already battling a rise in frauds and scams, which is a global issue. Getting this right goes to the core of ensuring consumers' confidence in open banking, which the Commission rightly calls out as one of the four key minimum requirements for the successful establishment of open banking.<sup>15</sup> While fraud and scams are not just a banking specific issue and need to be addressed across the economy, they are a particular issue which ASB urges the Commission to consider in relation to its recommendations regarding open banking, given open banking involves providing access to sensitive customer information to a variety of businesses including start-up companies which inherently increases cyber risks.
- 5.3 As part of achieving this, New Zealand needs to move beyond a sole focus on open banking and payments, to prioritise the development of a strong and safe digital infrastructure which prioritises mitigating frauds and scams. This starts with delivery of standardised APIs that will support implementation of confirmation of payee, building infrastructure required for a successful digital identity system and then add functionality that will deliver the most value to New Zealand consumers, fintechs and the wider New Zealand economy. A safer open banking ecosystem also requires a focus on cyber control standards.
- 5.4 New Zealand has not been the first country internationally to introduce open banking, which puts us in the useful position of being able to learn from the progress in other countries. We should capitalise on those learnings to proactively address problems seen elsewhere and ensure an optimal experience for New Zealand consumers. Rushing too quickly to implement a system may see an immediate need for changes to address verification and security issues, usability and / or low uptake. The complexities of the interactions with various bank systems is why ASB believes industry is best placed to lead these developments.
- 5.5 Important features to work through are, for example:
- (a) the involvement of Government and Police in addressing frauds and scams (which will become increasingly important in a digital payments ecosystem), similar to the models employed in Singapore and Australia;
  - (b) an appropriate framework for the participation of high risk providers (e.g. cryptocurrency businesses) or providers requesting information that is inappropriate (such as login and password details from customers); and
  - (c) the regulation of those who participate in payments. For example, Apple controls more than 80% of the payments made via cell phones in Australia, with Apple currently able to charge whatever it likes for those payments. Apple also prevents bank apps from making tap-and-go payments, unless they are routed through Apple Pay and charges banks for payments using bank cards stored in iPhones.<sup>16</sup> The focus of regulation on banks rather than all providers of a service stifles innovation and competition and leaves consumers

<sup>12</sup> Draft report, at 4.40.

<sup>13</sup> Draft report, at 4.41.

<sup>14</sup> Draft report, at 4.45.

<sup>15</sup> Draft report, at 9.83.4.

<sup>16</sup> CEOs push for more Apple scrutiny, Australian Financial Review - Wednesday, 27 Mar 2024 - Page 3.

<https://www.afr.com/companies/financial-services/westpac-and-nab-back-cba-call-for-more-scrutiny-of-apple-in-payments-20240326-p5ffck#:~:text=The%20chief%20executives%20of%20National.giant%20as%20global%20counterparts%20have.>

unprotected. As we have consistently submitted, consumer confidence requires that the activity, not the entity, is regulated.

- 5.6 ASB looks forward to continuing to engage with the Commission and collaborating with the wider industry to build a world class digital infrastructure with safety and security at its core. Progressing this digital infrastructure in New Zealand will require strong government leadership. This must include clarifying the requirements for open banking to be 'fully operational' and appropriately scoping, sequencing and revising implementation plans to address rapidly evolving risks.

## 6. Profitability

- 6.1 ASB is pleased to see the Commission has acknowledged points raised by ASB, NERA and others in respect of the Commission's Preliminary Issues Paper (**PIP**) profitability analysis.
- 6.2 An appropriate return on capital is needed to attract capital for banks, which ultimately supports the stability of the financial system. Without a reasonable return on capital the economy will not get the funding required to grow. As the Commission says in the draft report "*[i]t is important that a banking sector remains well capitalised. This maintains confidence in the banking system which supports financial stability by improving banks' ability to access funding, by improving resilience to shocks throughout the business cycle, and by reducing the probability of bank runs.*"<sup>17</sup>
- 6.3 ASB also notes the limitations of the Commission's analysis, which the Commission itself accepts, where it said that "*[a] more refined analysis may allow for more concrete conclusions to be reached on whether profitability exceeds what would be expected in a workably competitive market*".<sup>18</sup>

## 7. Innovation

- 7.1 ASB fundamentally disagrees with the suggestion that banks' under-investing in innovation is a result of a lack of competition.<sup>19</sup> As has been previously submitted, ASB is currently undertaking significant work to update and upgrade its systems. ASB has made significant investments in innovations where it has had the capacity to do so. For example, ASB has and is continuing to invest in its digital customer experiences.<sup>20</sup> ASB invested [Redacted] million on innovation initiatives in FY23.<sup>21</sup>
- 7.2 However, these efforts have been impacted by the persistent pace of regulatory change, which must be prioritised above other changes to ASB's systems. From FY18 to FY23 regulatory compliance has cost ASB over [Redacted] million.<sup>22</sup> There are only so many changes which ASB can make to its core systems at any one time, and only so many people with the necessary skills to understand the complexity in ASB's systems available to work on that change. Switching ASB's systems to new technology will improve ASB's future ability to make change, but work on core systems has been impacted by the prioritisation of regulatory change.
- 7.3 This is further illustrated by the fact that smaller banks also indicated that regulatory compliance is a key constraint to innovation.<sup>23</sup> If the lack of innovation was due to a lack of competition or complacency from larger banks (as the Commission suggests), then the smaller banks would have made significant innovations to improve their competitive position.
- 7.4 ASB supports consideration of the barriers imposed by the Anti-Money Laundering and Countering Financing of Terrorism (**AML/CFT**) regime, provided that the financial crime risk associated with some fintech providers (e.g. cryptocurrency businesses) is appropriately

<sup>17</sup> Draft report, at 6.6.

<sup>18</sup> Draft report, at 6.61.

<sup>19</sup> Draft report, at 9.16.

<sup>20</sup> ASB's Preliminary Issues Paper Response (**PIP Response**), see examples from paragraph 25.6, such as ASB ID, digital financial wellbeing tools, digital messaging, fraud protection, how to guides and other innovative tools.

<sup>21</sup> See PIP response at 29.9.

<sup>22</sup> See PIP Response at 29.6.

<sup>23</sup> See Heartland's PIP submission at 11(d) and TSB/Co-Op/Kiwibank/SBS joint PIP submission at page 3.

managed, alongside frauds and scams, and it does not result in New Zealand falling out of step with its international commitments to combatting money laundering and terrorist financing.<sup>24</sup>

- 7.5 ASB notes the comments in the draft report regarding access to bank accounts for fintechs. We can only assume that is directed at other banks as ASB has banking relationships with a number of different fintechs.

## 8. Customer switching

- 8.1 ASB queries the Commission's conclusions that customers 'seldom' shop around for a good deal. As ASB has previously submitted, many customers have banking relationships with multiple providers which means they can (and do) 'shop around' without showing up as formally switching. In fact, [Redacted]% of ASB's customers also bank with a competitor today and presumably switch between offerings of different providers. Maintaining multiple accounts further ensures customers can switch between providers without risk and with confidence. Further, ASB's share of new home loan business which originates via a mortgage broker (as opposed to directly from customers), is now comfortably over [Redacted]%.
- 8.2 Further, the results of the survey commissioned by the Commission and undertaken by Verian<sup>25</sup> also do not appear to sit comfortably with the Commission's conclusions on this point.
- (a) 17% of customers had either switched, or internally switched one or more product by renegotiating a better offer, in the last three years. This is a significant proportion. Further, 23% of people considered switching but did not go through with it, which may well indicate that having shopped around they were happy with the competitiveness of their current provider's offering. Combined, ASB understands this indicates that nearly two out of every five customers responding to the survey either switched or considered switching at least one or more product in the last three years.<sup>26</sup>
- (b) In addition, 28% of customers in the survey said they would consider the smaller banks for their main banking provider. This is a significant proportion, and well above the combined share currently accounted for by these smaller banks, indicating significant room to grow share.
- (c) In terms of those who did switch, 62% reported it to be easy or very easy.
- 8.3 The Commission indicated that none of the major banks actively recommend the Payments NZ switching service. However, as ASB has previously advised the Commission, ASB's "Bank Switch" process is integrated in ASB's Customer Relationship Management system, which ASB's frontline teams use when engaging with customers. ASB's switching service is also mentioned on its website.
- 8.4 Notwithstanding ASB questioning the need for further discrete switching initiatives, to the extent there is residual friction we are supportive of any measures to support customers (for example, by prorating any clawbacks on cashback payments and broker commissions, which ASB already does). Therefore, customers are not unfairly penalised if they choose to switch.

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<sup>24</sup> For example, the FATF Recommendations, reporting requirements under the Foreign Account Tax Compliant Act (**FATCA**) and the common reporting standard required by the Global Account Tax Compliant Act (**GATCA**).

<sup>25</sup> See Verian – Personal Banking Survey – Report – February 2024 available at: [https://comcom.govt.nz/data/assets/pdf\\_file/0030/347376/Verian-Personal-Banking-Survey-Report-February-2024.pdf](https://comcom.govt.nz/data/assets/pdf_file/0030/347376/Verian-Personal-Banking-Survey-Report-February-2024.pdf)

<sup>26</sup> ASB understands that the 1.8% of survey responders that were "effective switchers", renegotiating a better deal with their current provider, are included in both the 17% and 23% figures. ASB understands that when this double counting is excluded, the cumulative percentage of survey responders that either switched or considered switching would amount to 38.2%.



**PART B: Ngā whakautu ki ngā tūhinga hukihuki** Response to draft recommendations

We turn now to each of the Commission's specific recommendations.

**Improve the capital position of smaller providers and Kiwibank**

1. **Recommendation 1: The Reserve Bank should review its prudential capital settings to ensure they are competitively neutral and smaller players are better able to compete.**

*The prudential capital settings are already competitively neutral*

- 1.1 As noted above, ASB believes the prudential capital settings are already competitively neutral. This finding is supported within the Commission's draft report where the Commission says "[t]he 85% floor and 2% D-SIB buffer led to major and other banks having similar total capital requirements".<sup>27</sup> ASB disagrees with any analysis of risk weights that does not consider the amount of capital required to be held against those risk weights.

*Financial stability should be the primary consideration of prudential capital settings*

- 1.2 Quite apart from the fact the settings are already competitively neutral, ASB strongly believes that financial stability must be the primary consideration of the RBNZ's prudential capital framework, whereby the level of capital held, regardless of an institution's size, matches the level of risk being taken. Any attempts to artificially distort this direct link between risk taken and the level of capital held could lead to excessive risk taking relative to an institution's financial soundness, such as that which resulted in New Zealand finance company collapses between 2006 and 2012, with significant bailout costs being borne by the New Zealand Government (i.e. taxpayer).<sup>28</sup>
- 1.3 It is not enough for New Zealand's capital regime to only focus on ensuring the stability and security of larger market participants. The New Zealand finance company collapses post the global financial crisis are a local example of financial failures associated with light regulation of smaller participants. International examples, which have had significant knock-on effects, include:
- (a) the US Savings and Loan Crisis of the 1980s;
  - (b) the 2023 failure of Silicon Valley Bank, Signature Bank and First Republic Bank; and
  - (c) the UK secondary banking crisis during the 1970s.

*Benefits of the IRB framework*

- 1.4 In relation to residential mortgages, ASB believes that advanced risk-based modelling (the IRB approach) plays a critical role in risk assessment across the ~\$350bn residential mortgage lending sector in New Zealand. This 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. As noted earlier, IRB models are widely used internationally for this very reason.
- 1.5 In developing the IRB framework, the BCBS aimed to achieve two key objectives:<sup>29</sup>
- (a) *"Additional risk sensitivity, in that a capital requirement based on internal ratings can prove to be more sensitive to the drivers of credit risk and economic loss in a bank's portfolio."*
  - (b) *"Incentive compatibility, in that an appropriately structured IRB approach can provide a framework which encourages banks to continue to improve their internal risk management practices."*

<sup>27</sup> Draft report, at 7.40.

<sup>28</sup> See further concerns as recently outlined by Martien Lubberink in <https://www.interest.co.nz/banking/127100/new-zealand-commerce-commissions-plea-lower-bank-capital-bolster-bank-competition-%E2%80%93>

<sup>29</sup> Basel Committee on Banking Supervision, Consultative Document "The Internal Ratings-Based Approach", 1 January 2001. Available at <https://www.bis.org/publ/bcbsca05.pdf>.

- 1.6 APRA's recent publication 'Demystifying credit risk capital requirements for housing loans'<sup>30</sup> notes the following advantages of IRB risk weights tending to be on average lower than standardised weights:
- (a) to encourage investment by banks in advanced modelling capabilities and associated technology, data and specialist skills. Such investment is significant and ongoing but provides substantial risk management benefits, such as:
    - (i) improving a bank's ability to identify the risk profile of its lending and other business activities;
    - (ii) facilitating risk-based and evidence-based decision-making and portfolio management;
    - (iii) ensuring risk is properly priced;
    - (iv) supporting financial innovation and the bank's ability to respond to market changes and changes in risk profile; and
  - (b) to enable banks to more accurately allocate capital for risk.
- 1.7 Table 7.1 of the draft report purports to compare the bank capital for a \$1 million home loan using the standardised vs the IRB approach. The analysis is simplistic as:
- (a) the risk sensitivity of the IRB approach means that in some cases the standardised method will result in lower capital for home loans. For ASB, portfolio IRB risk weights are higher than standardised risk weights for home lending with loan to value ratios between 70% and 100%. For example, for a \$500,000 owner occupied loan with LVR of 85%, ASB's IRB risk weights would be \$[Redacted] compared with standardised risk weights of \$250,000; and
  - (b) the IRB method requires additional capital for the undrawn proportion of revolving loans and for defaulted loans.
- 1.8 At a practical level, the effect of the 2% D-SIB buffer and 85% floor eliminates the difference between D-SIB RWA under the standardised floor and non D-SIB standardised RWAs. Any intervention to increase the output floor or otherwise increase the level of capital required to be held by D-SIBs (both of which are already high by international standards) for the purposes of in theory "levelling the playing field" would result in further inefficiencies in the allocation of capital, with consumers ultimately being worse off through greater capital costs being passed through in higher prices.
- 1.9 Alternatively, the RBNZ could consider adopting a more risk sensitive version of standardised home lending. Appendix 1 demonstrates APRA and Basel III risk weights by LVR bands in comparison to RBNZ standardised and ASB IRB models.
2. **Recommendation 2: Kiwibank's owner should consider what is necessary to make it a disruptive competitor, including how to provide it with access to more capital.**
- 2.1 As set out in Part A above, Kiwibank is already a strong industry player, competing effectively with the other large banks in mortgage and deposit products. Indeed, Kiwibank has seen significant

<sup>30</sup> Available at: [www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans](http://www.apra.gov.au/demystifying-credit-risk-capital-requirements-for-housing-loans).

growth in recent years, with the Commission recording that Kiwibank is the only provider that has grown consistently at or above system growth over the four-year period considered.<sup>31</sup>

### Accelerate progress on open banking

#### 3. **Recommendation 3: The Government should set clear deadlines and work with industry to ensure open banking is fully operational by June 2026.**

- 3.1 ASB is committed to progressing open banking in New Zealand for the benefit of consumers.
- 3.2 ASB remains committed to delivering API v2.1 throughout 2024. ASB will continue to engage with the API Centre, Payments NZ, the Commission and with third party providers in a way which is open and transparent and which, importantly, puts safety and security first.
- 3.3 While ASB is supportive of open banking in New Zealand, we know from research that customers have a low understanding of the benefits of open banking and valid concerns around privacy and security of their data.<sup>32</sup> The potential benefits of open banking, from a consumer perspective, need to be clearly called out by the Commission. Making sure customers are well protected from cyber risks, scams and fraud, and can therefore trust open banking from a safety and security perspective, will be essential to the success of open banking and the development of a digital payments ecosystem. Customers need to trust the process to opt-in (as recognised by the Commission in the draft report).<sup>33</sup> A Government led trust framework and clarity about how this will operate at a practical level, will be essential.

#### *Review of AML obligations*

- 3.4 The draft report notes that the due diligence requirements under the AML/CFT Act create impediments to switching, because of the customer identification and verification processes.<sup>34</sup> It goes on to state that the Ministry of Justice is undertaking a review of the AML/CFT Act and proposes to reduce address verification requirements by switching to a risk-based approach.<sup>35</sup> ASB considers removal of address verification obligations from the AML/CFT regime is an important initial step. Removal of unnecessary barriers for onboarding will:
- (a) **promote financial inclusion** – mean more customers can successfully be onboarded digitally, without having to produce document verification, thereby increasing ease of competition for new accounts. Address verification often presents huge obstacles for some of our most vulnerable communities (such as the homeless, recent migrants, etc.) to access banking services. This is despite address verification providing little to no value in mitigating AML/CFT or sanctions risks;
  - (b) **improve productivity** - easier AML/Know Your Customer (**KYC**) processes across industry will result in fewer branch visits and contact centre calls for onboarding, allowing banks and other AML reporting entities to focus on assisting those who need help the most (i.e., those with complex needs or in vulnerable circumstances). Allowing cross-reliance on AML checks conducted by reporting entities will be more efficient for customers and industry;
  - (c) **enable digital identity** – in turn this would enable development of a digital identity service, requiring fewer sources for verifying customer identities only (rather than addresses). This in turn would assist with the development of confirmation of payee functionality. A simple and secure digital identity verification system is a foundational need for developing a trusted open banking and digital payments ecosystem; and
  - (d) **facilitate deposit insurance payouts** – simpler AML/KYC and digital identity capability would also ensure a smoother process for any required payouts under the DCS/DTA. A

<sup>31</sup> Draft report, at 4.13.3.

<sup>32</sup> For example, in a consumer survey conducted by ASB regarding enabling the digital economy, the key concerns identified by customers included what companies would do with their data and also privacy/safety concerns. Additionally, in response to the question: how interested would you be in using an app-based subscription service that enables people to manage their own finances including holding accounts from multiple banks: 36% were not interested, 29% were interested and 12% were unsure.

<sup>33</sup> Draft report, at 9.83.4.

<sup>34</sup> Draft report, at 8.77.

<sup>35</sup> Draft report, at 8.79.

reduced AML/KYC burden could also support competition once the DCS is in effect if customers looked to spread deposits across multiple deposit takers to benefit from increased insurance.

*Open banking needs to be rescoped in light of emerging risks/opportunities*

- 3.5 ASB's view is that for New Zealand to truly be a productive, inclusive and innovative nation, we need a strong and safe digital ecosystem. That is much broader than open banking and payments, it's an infrastructure that enables safe exchange of rich data, coupled with identity verification, real time fraud detection and a safe and efficient, modern, adaptable payments system. To realise this, New Zealand must prioritise the introduction of confirmation of payee and a digital identity regime.
- 3.6 All stakeholders should be engaged to redevelop a roadmap for delivery of digital infrastructure modernisation which factors in and prioritises the following.
- (a) **Mitigating financial crime:** As ASB has said consistently, combatting the rising number of frauds and scams remains our top priority. By way of example, 38% of crime in the United Kingdom is now fraud and scams.<sup>36</sup> The increasing sophistication of scammers requires New Zealand government agencies and the private sector to work together to protect New Zealanders' assets and data. The draft report refers to the need for increased preventative action around scams and fraud.<sup>37</sup> Developing the confirmation of payee functionality by the end of 2024 must therefore be the first priority. This needs to be factored into the scope of v2.3 as it will require alignment with standardised API functionality. A safer open banking ecosystem also requires a focus on cyber control standards.
- (b) **Building a strong foundation for a safe and secure digital infrastructure:** Work with relevant government departments to:
- (i) reduce some of the burdens associated with AML/KYC onboarding obligations, as noted above; and
- (ii) collaborate as an industry to leverage the work already underway by various private sector parties and the Department of Internal Affairs, including the trust framework the API Centre proposes to develop through its partnering project. Opportunity exists also to leverage work done by banks on Connect ID in Australia. ASB is of the view that while the Government must lead the trust framework and establish how this will operate at a practical level, Payments NZ could lead the work on a fit-for-purpose digital ID scheme which is also likely to require standardised APIs, but in turn this requires strong Government support.
- (c) **Agreeing a delivery roadmap for digital infrastructure modernisation that best serves the needs of New Zealanders:** Simultaneously with (b) above, collaborate with Payments NZ, the Commission, the Government and the wider industry to develop a roadmap for delivery of open banking and a digital payments infrastructure which is safe, secure and has the trust and confidence of New Zealanders. We consider the scope of open banking and its implementation plan should be reviewed given that it was initially designed in 2017 and that much has changed, including the significant increase in cyber events, frauds and scams and to ensure the above key priorities are appropriately baked in.
- 3.7 The Commission has expressed concerns that *"[i]f done sequentially, open banking will take much longer to be implemented and there is a risk that the various components do not fit well together. For example, if the digital identity framework is developed without close links to how it could be used in open banking, it may need to be adapted later on, causing further delays and cost."*<sup>38</sup> ASB disagrees, delivery of v2.1 is well underway, so now is the right time (together with confirmation of payee) to design the required APIs to support a digital identify framework. ASB

<sup>36</sup> See for example <https://www.thenationalnews.com/world/uk-news/2024/03/11/world-leaders-at-london-summit-agree-on-unity-to-fight-fraud/>.

<sup>37</sup> Draft report, Attachment D, at D36.

<sup>38</sup> Draft report, at 10.23.

considers that this work will deliver more value to New Zealanders than some of the functionality currently in scope for v2.3.

#### *Open Banking partnering pilot*

- 3.8 ASB has recently commenced a pilot to onboard third parties using carefully designed commercial agreements and due diligence processes. The pilot has been very well received so far with positive feedback on the usability of ASB's diligence process and documentation.

#### *New API standard functionality*

- 3.9 ASB notes that the Commission has recommended that the “*APIs that are designed and implemented should...include payment initiation, confirmation of payee, account information, product information, and ‘other actions’ initiation such as opening and closing accounts*”.<sup>39</sup> Product information and opening and closing accounts functionality is not in scope of the open banking minimum implementation plan and therefore would need to be fully scoped and designed before committing to a set delivery timeframe. This work should not be at the expense of securing New Zealand's digital infrastructure against cybercrime, and therefore needs to be appropriately sequenced.
- 3.10 ASB is keen to discuss its views further with the Commission and collaborate with the wider industry to build a world class digital infrastructure with safety and security at its heart, and which will ensure New Zealand remains competitive in an increasingly digital global economy, enabling New Zealanders to benefit from greater innovation and competition.

#### 4. **Recommendation 4: The Government should reduce the barriers imposed by the AML/CFT regime on banks working with fintechs.**

- 4.1 ASB is committed to protecting New Zealanders from the impacts of financial crime and works hard to adhere to its AML/CFT obligations. ASB does, however, support a move towards a more risk-based approach which does not unfairly or unnecessarily deny access to financial services to some of our most vulnerable communities. ASB is involved in a number of initiatives to support financial inclusion and Māori access to banking services and capital, and has supported the Ministry of Justice, via participation in an industry advisory group, in its recent review of the AML/CFT regime.
- 4.2 On the subject of fintech onboarding specifically, ASB banks, supports and partners with a number of fintech customers. ASB's processes do not, as a default, class fintechs as being outside of ASB's risk tolerance, nor does ASB actively de-risk or de-bank fintech customers. Fintech AML risk is assessed using the same criteria as other customers. A fintech's risk profile will depend on a number of objective factors such as their suppliers and third parties, types of services, and degree of inter-reliance of controls.
- 4.3 While some fintechs may experience difficulties in obtaining banking services, particularly if their business relies on or participates in cryptocurrencies, ASB considers that if such fintechs were to become regulated, this could be beneficial for establishing relationships with banks, as they could be eligible for simplified due diligence as a regulated financial entity.
- 4.4 ASB acknowledges there are ways to improve the AML/CFT regime, improving the experience for the customer and ease of access to banking services, without scaling back the necessary customer verification controls that are required to detect and prevent financial crime and would be happy to engage further with relevant stakeholders to progress this.

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<sup>39</sup> Draft report, at 10.27.1.

## Ensure the regulatory environment better supports competition

5. **Recommendation 5: The Reserve Bank should use its new decision-making framework under the DT Act to explicitly and transparently consider competitive effects.**
- 5.1 ASB's purpose is to accelerate the progress of all New Zealanders. ASB therefore supports legislative changes that aim to create a trusted and consistent regulatory framework for banks and other deposit taking institutions, promote financial stability, and support the economy.
- 5.2 The DTA broadened the remit of prudential regulation as it integrated the previously separate regimes (under the RBNZ Act 1989 and the Non-Bank Deposit Takers Act 2019 (**NBDT Act**)) to create a single coherent framework for the regulation of all financial institutions (including NBDTs) which take deposits from the public and lend to individuals, households and businesses.<sup>40</sup> The DTA includes a wide range of purposes and principles, both for the overall application of the DTA and for the DCS levies specifically. These include 'avoiding or mitigating risks to the financial system' (purpose) and maintaining competition within the deposit-taking sector (principle).
- 5.3 ASB does not agree with the Commission's comments that the RBNZ has not appropriately considered competition impacts of the DTA and DCS schemes. Throughout the development of the DTA, the RBNZ has engaged collaboratively with industry on the proposals and has considered competitive effects of the DCS and DCS levies. In the Second DCS Consultation, the RBNZ explains the potential impacts of their proposals on competition several times, including as part of setting the levies. The RBNZ stated "*Their [larger banks] ability to pass on levy costs may also be reduced by the increased competition in the industry as a result of the rate compression by small deposit takers*" (emphasis added).<sup>41</sup>
- 5.4 ASB believes the proposed approach for the DCS levy is heavily pro-competition and that smaller lenders look likely to benefit from these levy settings relative to their riskiness once the scheme commences. ASB considers that the current levy proposals could significantly mis-price the risks associated with some smaller deposit takers, which could undermine financial stability should these riskier deposit takers see increased deposit inflows once the scheme commences. To require the RBNZ to give even more weight to competition would further exacerbate the risk to financial stability and in turn a direct adverse impact on individual consumers (beyond the limits of the DCS).
- 5.5 We consider that financial stability (in particular, seeking to avoid the issues encountered during the global financial crisis with government guarantees, and other financial crises, and the potential for a direct adverse impact on individual customers) should be the RBNZ's primary consideration, as to do otherwise would be inconsistent with international best practice. This focus on financial stability will also be crucial as the RBNZ develops the prudential standards under the DTA for all deposit takers.
6. **Recommendation 6: The Reserve Bank should explicitly and transparently articulate how it is applying the purposes and principles of the DT Act to its Deposit Compensation Scheme levy advice.**
- 6.1 ASB supports the introduction of the DCS. While capitalisation of New Zealand banks is on track to be amongst the highest in the world, depositors nevertheless want to have confidence that there is a safety net if they ever find themselves with deposits held by an institution in financial distress.
- 6.2 ASB has no objection to the RBNZ being explicit and transparent in terms of how it applies the purposes and principles of the DTA Act to its DCS levy advice.
- Risk-based versus flat-rate levies*
- 6.3 It will, however, be important that financial stability is not threatened by significant inflows of funds to deposit takers with less robust capital and liquidity management practices. Mitigating the

<sup>40</sup> See <https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/publications/speeches/2023/kerry-beaumont-speech-another-seismic-shift-in-nz-banking-regulatory-reform.pdf> at page 8.

<sup>41</sup> [https://consultations.rbnz.govt.nz/dta-and-dcs/dcs-regulations/user\\_uploads/dcs-regulations-consultation-paper.pdf](https://consultations.rbnz.govt.nz/dta-and-dcs/dcs-regulations/user_uploads/dcs-regulations-consultation-paper.pdf) at page 16.

potential moral hazard risks associated with the DCS is critical, and this is best addressed by using appropriately differentiated risk-based levies, rather than a flat-rate levy.

- 6.4 Without appropriately differentiated risk-based levies in place, riskier deposit takers may seek to exploit the market distortion created when depositors can seek the highest deposit rate without regard to the risk profile of the deposit taker, knowing that their funds are protected by the DCS.
- 6.5 The Treasury and the RBNZ have stated that the purpose of risk-based levies is to avoid the unfair outcome of deposit takers that pose lower levels of risks to the DCS subsidising higher risk deposit takers in funding the DCS.<sup>42</sup>

*Current proposed 'composite risk-based approach' supports competition*

- 6.6 ASB considers that the RBNZ's current proposed levy framework is already too heavily skewed towards competition. As the Commission has recognised, "[t]he incoming DCS could reduce some challenges that smaller providers face for attracting retail deposits."<sup>43</sup> Once the DCS commences, smaller deposit takers are likely to be able to offer insured deposits at higher interest rates than larger deposit takers. The RBNZ has stated in the Second DCS Consultation that "[t]he DCS levy is expected to narrow but not close" the interest rates offered by different classes of deposit taker.
- 6.7 The Second DCS Consultation includes an indicative range for the DCS levy under the proposed 'composite risk-based approach' of between 0.05% (lowest risk deposit takers) and ~0.20% (highest risk deposit takers). In ASB's view this is a far smaller band than a band which truly reflected the relative riskiness of many smaller deposit takers (based on their respective credit ratings). These indicative levies are based on the median proposed in the Treasury's July 2023 Statement of Funding Approach consultation paper and are small relative to the "50-60 basis point funding cost advantage" between small banks and large banks identified by the Commission in the draft report<sup>44</sup>, as well as the RBNZ's own analysis of deposit rates contained in the Second DCS Consultation paper (~15bps to ~120bps above the major banks).
- 6.8 If the imposed levy does not match the underlying risk, the levy collection over time from these organisations is likely to be low compared to their expected losses from failure. The current levy proposals (which place significant weight on competition) could significantly mis-price the risks associated with some riskier deposit takers. To require the RBNZ to give even more weight to competition would further exacerbate the risks to financial stability and in turn a direct adverse impact on individual consumers (beyond the limits of the DCS).

*Potential mis-pricing risk of the current proposal*

- 6.9 While ASB has been supportive of the RBNZ's proposed approach in our previous submissions, we do consider that the current levy proposals could significantly mis-price the risks associated with some smaller deposit takers, which could undermine financial stability should these riskier deposit takers see increased deposit inflows once the scheme commences.
- 6.10 ASB notes the Commission's concerns that despite a similar scheme in place in Australia there appears to be an enduring perception that the major banks are safer.<sup>45</sup> It is not surprising that well-funded banks with long standing reputations and higher levels of capital are well trusted. However, the DCS scheme will ensure that smaller banks and NBDTs can publicise the insured nature of their deposits, which will inevitably have an impact on consumer perceptions of safety and trust.
- 6.11 While ASB agrees that the failure of a D-SIB could cause systemic issues for the New Zealand economy, ASB does not agree that the higher impact of a less likely scenario outweighs the higher likelihood of a smaller bank or NBDT collapsing. Between 2006 to 2012, over 50 New

<sup>42</sup> Reserve Bank of New Zealand and Treasury Joint Report: Draft Cabinet Paper and Further Policy Decisions Related to the Deposit Takers Bill – 2 June 2022, at 154. Available at: <https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/proactive-releases/5-reserve-bank-of-new-zealand-and-treasury-joint-report-technical-decisions-related-to-the-deposit-t.pdf>

<sup>43</sup> Draft report, at 5.54.

<sup>44</sup> Draft report, at 5.52. The 'funding cost advantage' identified by the Commission associated with greater transaction deposits also ignores the significant costs associated with those transaction deposits, including the costs of maintaining a branch network, call centres, payment systems, applications, and complying with AML.

<sup>45</sup> For example, at 5.18 of the Draft report.

Zealand finance companies either went into liquidation or receivership, or froze payments.<sup>46</sup> The 2011 parliamentary inquiry stated that these failures put at risk approximately \$6 billion of investors' deposits, it was estimated that between 150,000 and 200,000 deposit holders were affected, and the losses as at 2011 were estimated at over \$3 billion.<sup>47</sup> This devastated many investors and had far reaching consequences for families. For example, some customers lost their entire life savings. One consumer stated "*we are in our 80s and face living below the poverty existence level for the rest of our natural lives*", describing it as a "*crippling loss*".<sup>48</sup> Additionally, this had not just financial impacts, but also had far reaching impacts on the health of those who invested and lost money.<sup>49</sup> In that same time period, while some banks withdrew from the New Zealand market, no New Zealand banks failed.

6.12 In this context, it will be crucial that the risk-based levy framework for the DCS is supported by other aspects of the DTA, such as increased supervisory oversight and the design of appropriate prudential standards (particularly for capital and liquidity).

7. **Recommendation 7: the Reserve Bank should consider broadening access to ESAS accounts.**

7.1 ASB is not opposed to the broadening of access to ESAS accounts, provided it is for the purpose for which ESAS was established. That is, it should be used to facilitate Real-Time Gross Settlement and efficient operation of Exchange Settlement accounts for properly certified participants, rather than a source of funding. Safety and security of the system must remain the primary consideration for the RBNZ.

8. **Recommendation 8: the Government should amend the DT Act to allow the Reserve Bank to promote competition, rather than maintain competition.**

8.1 As set out in Part A and ASB's responses to recommendations 5 and 6 above, financial stability must remain the overarching priority of the RBNZ, above all other considerations.

8.2 The RBNZ has to date had regard to the impact of its decisions on competition (such as in considering the DCS and DCS levies, as set out above), which ASB considers could significantly mis-price the risks associated with some smaller deposit takers, which could undermine financial stability should these riskier deposit takers see increased deposit inflows once the DCS scheme commences.

8.3 To amend the DTA to instead require the RBNZ to 'promote' competition would further risk diluting the RBNZ's primary focus on financial stability which is ultimately for the benefit of consumers. The RBNZ is best placed to weigh the impact of its decisions given its primary mandate.

9. **Recommendation 9: the Government and policy makers should seek competitive neutrality across banks and other providers in their decision-making wherever possible.**

9.1 As a matter of general principle, ASB supports the Government having regard to the impact of its decisions on competition. Naturally, the Government must make a risk-based assessment, and to date the outcome of that assessment is often to refer to a 'registered bank'.

9.2 ASB has no objection to the Government continuing to refine these risk-based assessments. If competitive neutrality can be achieved without incurring offsetting detriments (e.g. in terms of safety and security of funds), then we would expect the Government to seek to achieve it.

9.3 In aiming for competitive neutrality, the Commission should ensure that all market participants are designated / regulated as part of its proposals to designate the interbank payments network. This must include dominant technology providers such as Apple (see for example 5.5(c) above),

<sup>46</sup> <https://www.fma.govt.nz/about-us/enforcement/cases/finance-company-collapses/>

<sup>47</sup> [https://www.parliament.nz/resource/en-nz/49DBSCH\\_SCR5335\\_1/0d9cfef1280ab5ba97f9569c8f965bfd7374305f](https://www.parliament.nz/resource/en-nz/49DBSCH_SCR5335_1/0d9cfef1280ab5ba97f9569c8f965bfd7374305f) at page 7.

<sup>48</sup> <https://www.nzherald.co.nz/nz/the-5-billion-failure/2EY3NDOBOU2KYDAROWWLJQPShI/> see underneath the section titled "Out of Pocket and Angry: what investors lost and learned".

<sup>49</sup> [https://www.parliament.nz/resource/en-nz/49DBSCH\\_SCR5335\\_1/0d9cfef1280ab5ba97f9569c8f965bfd7374305f](https://www.parliament.nz/resource/en-nz/49DBSCH_SCR5335_1/0d9cfef1280ab5ba97f9569c8f965bfd7374305f) at page 7.



fintechs and others. Consumer confidence requires that payments activity, rather than payments entities, is regulated.

10. **Recommendation 10: the CCCF Act should be competitively neutral with respect to home loan refinancing to make it easier for consumers to switch providers.**

- 10.1 ASB supports a broad review of the CCCFA and agrees that reform is needed to strike the right regulatory balance.

*Reforming the affordability assessment regime - refinancing*

- 10.2 As a responsible lender, it is in ASB's and its customers best interests that their loan is affordable. This has always been a consideration for ASB's lending.

- 10.3 ASB is broadly supportive of changes to the current regulations to ensure that applications to refinance home loans do not result in consumers having to undergo detailed affordability assessments, regardless of whether they remain with their existing home loan provider or switch to a new lender. Those changes must be effected in a way which ensures consumer interests remain paramount.

*Reforming the affordability assessment regime – 'safe harbour' benchmark*

- 10.4 The Commission's secondary recommendation on changing the affordability assessment regime involves providing lenders a 'safe harbour' benchmark. No detail is provided in the draft report, but the Commission says the benchmark will reduce lenders' regulatory burden and promote competition by reducing the cost and risk to lenders associated with an affordability assessment under the current regime.

- 10.5 ASB supports increasing competition by reducing the cost and risk of conducting affordability assessments. A 'safe harbour' benchmark could make conducting affordability assessments easier for some lenders. ASB considers more detail needs to be provided in respect to this recommendation in order to provide feedback.

*Reforming the penalty regime*

- 10.6 ASB supports the Commission's recommendation to reform the CCCFA penalty regime.
- 10.7 ASB supports the recommendation to review the penalty regime as it applies to directors and senior managers. ASB agrees that the regime may disincentivise the assumption of directorships and senior management roles.

## **Empower customers**

11. **Recommendation 11: Industry should create an enhanced switching service with appropriate Government oversight.**

- 11.1 The draft report refers to the costs to consumers associated with opening a new account and moving financial activities to it, which the Commission says arise regardless of whether a customer is 'multi-banked' or not. ASB disputes these costs are a disincentive, especially given the fact there are no financial costs as accounts and payments are free and noting the very high proportion of customers who are multi-banked and who presumably switched between offerings of the different providers. Maintaining multiple accounts further ensures customers can switch between providers free of charge, without risk and with confidence (further issues identified in the draft report).
- 11.2 As previously shared, ASB participates in the account switching arrangement established by Payments New Zealand, "Easy Switch" and follows the timeframe of five business days to complete the switching process. As the Commission's survey found, 62% of customers who have actually switched provider in the last three years reported it to be easy or very easy.

- 11.3 That said, to the extent some consumers are unclear as to the ease with which they can switch, then ASB agrees further promotion of Easy Switch could be of benefit.
- 11.4 ASB notes the Commission's comparison to the UK's Current Account Switch Service (**CASS**). However, this scheme has some limitations compared to the existing Easy Switch process. For example, customers still need to provide two forms of re-identification and proof of address to comply with money-laundering regulations. The whole CASS process takes seven working days compared to Easy Switch which takes five working days to complete.
- 11.5 ASB agrees that drivers of operational complexity for the current Easy Switch process include the dependency on third party initiators (companies that hold direct debit mandates) to provide the required information in a timely manner. 95% of the switching requests that ASB processes are completed on time, 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.
- 11.6 ASB is actively encouraging an interoperable digital identity scheme for New Zealand which, if supported by amendments to AML legislation, could significantly improve onboarding processes at a new bank and further streamline the workings of the Easy Switch process.
- 11.7 ASB firmly believes that providers are best placed to oversee any developments of the Easy Switch process and promotion of that service, as changes need to be practical and achievable based on the specific complexities of the banking systems already in place.
12. **Recommendation 12: Home loan providers should present offers in a readily comparable manner.**
- 12.1 ASB agrees that customers need to be able to understand the offers that have been presented to them and assess which best suits their needs.
- 12.2 ASB is concerned that a requirement for standardisation of offers across the industry might be detrimental to consumers by hampering providers' ability to innovate and offer dynamic products to consumers, or rapidly respond to changing market conditions. Formulaic disclosure requirements may not accommodate innovative new offers and may therefore stifle competition.
- 12.3 Further, a required standardised framework would add to the already heavy compliance burden on providers, with potentially limited benefit. Technical changes will inevitably be required to deliver and maintain this solution, which will divert resource away from other areas that may be of greater value to customers.
- 12.4 Finally, to the extent this is motivated by a concern in relation to cash clawbacks etc, then the Commission's recommendation to ensure these are pro-rated should address that.
- 12.5 In short, ASB is happy to engage on this point further, but it believes this recommendation is one which, while theoretically appealing, is not needed and which carries with it quite considerable direct and indirect costs.
13. **Recommendation 13: Mortgage lenders should pro-rate all clawbacks for broker commissions and cash incentives.**
- 13.1 As noted above and as previously submitted, ASB already pro-rates clawbacks on broker commissions and cash incentives over the relevant period. ASB has no objection to a requirement that all banks do so.
14. **Recommendation 14: the Financial Markets Authority should produce guidance and monitor mortgage advisors' compliance with their duties under the Financial Markets Conduct Act.**
- 14.1 ASB agrees with the Commission that mortgage brokers have an important role to play to provide guidance and advice for consumers, help them find the right mortgage to suit their needs and facilitate appropriate disclosure. They have extensive knowledge of the market and can help

consumers understand the differences between the various types of loans and the terms and conditions attached to each one.

- 14.2 As set out elsewhere in this submission, the focus of regulation is to protect consumers from harm. The potential for consumer harm does not differ depending on who provides the service to the consumer, and with that in mind ASB generally considers that, to the extent regulation is required, it should focus on all entities providing that customer service.
15. **Recommendation 15: industry and Government should prioritise work to reduce the barriers to lending on Māori freehold land.**
- 15.1 ASB recognises the barriers many Māori have faced in relation to accessing personal banking services and is committed to addressing these. ASB's Te Waka Whaihua provides dedicated support to Māori customers and engages with them to understand their concerns and priorities. Additionally, ASB has a multitude of activities which fit within its Te Ao Māori strategy, which is to accelerate the prosperity of tangata whenua, and is actively looking for ways to promote these. For additional information regarding these, please see ASB's previous submissions.<sup>50</sup>
- 15.2 ASB has recently developed a framework for lending on Māori freehold land for residential purposes where there is a maximum of six owners or trustees on the title.<sup>51</sup> As emphasised by Anthony Ririnui, Kaihautū, Te Waka Whaihua "[w]e are focused on how we can accelerate Te Ōhanga Māori (the Māori Economy) and build a sustainable Aotearoa with solutions that will make a difference for whānau and the generations to come" and "[w]e're proud to be supporting Māori housing solutions. It has been rewarding to see whānau realise their long-held dreams of returning to their ancestral whenua in new, affordable homes."<sup>52</sup> ASB has also been able to establish base line data on its total mortgages on Māori Freehold Land so it can track the opportunities to grow this book in accordance with this new framework.
- 15.3 ASB received positive recognition from Adrian Orr, the Governor of the RBNZ, in relation to this framework. Adrian Orr stated in a letter received by ASB on 19 January 2024:
- "Your proactive approach to understanding and responding to the unique financial needs of Māori is commendable and sets a noteworthy standard for the financial industry. We are encouraged by your dedication to address the challenges Māori experience in accessing capital. Your efforts showcase a commitment to fostering economic empowerment and financial inclusion and pave the way for more collaborative and inclusive initiatives that contribute to creating a more accessible and equitable financial landscape"* (emphasis added).
- 15.4 ASB notes that the Māori Land Court has recently issued a practice note in connection with lending against Māori freehold land.<sup>53</sup> This provides further clarification to the banking industry on lending against Māori freehold land.
- 15.5 ASB is committed to accelerating Māori access to capital alongside the specific initiatives relating to lending against Māori freehold land. For example, ASB announced in November 2023 that we are targeting a portion of our new \$500 million Accelerated Housing Fund for affordable and social housing specifically towards Māori housing.<sup>54</sup>
- 15.6 ASB remains committed to reducing the barriers faced by Māori in accessing personal banking services, including in relation to lending on Māori freehold land and is supportive of exploring further ways to address these barriers as an industry.
16. **Recommendation 16: Industry and Government should prioritise ensuring widespread availability of basic bank accounts.**
- 16.1 ASB already offers access to free transaction accounts to consumers.<sup>55</sup> However, ASB is conscious of the barriers some consumers face in accessing bank accounts. ASB is currently

<sup>50</sup> For example, PIP response pages 15-16.

<sup>51</sup> See <https://www.asb.co.nz/documents/media-centre/media-releases/asbs-maori-land-lending-helps-whanau.html>.

<sup>52</sup> See <https://www.asb.co.nz/documents/media-centre/media-releases/asbs-maori-land-lending-helps-whanau.html>.

<sup>53</sup> See <https://www.maorilandcourt.govt.nz/assets/Documents/Practice-notes/Banking-Practice-Note.pdf>.

<sup>54</sup> See <https://www.teaonews.co.nz/2023/11/04/asb-ring-fences-portion-of-innovative-affordable-housing-fund-for-maori-housing/>.

<sup>55</sup> See <https://www.asb.co.nz/bank-accounts/simplified-banking.html>.

exploring using technology to simplify the sign up process<sup>56</sup> and is already developing a specific basic account product.

- 16.2 Additionally, ASB is aware that some consumer groups may find it more difficult to navigate the financial system and has built internal capabilities to address this. These capabilities include our Community Council,<sup>57</sup> Vulnerability & Accessibility team,<sup>58</sup> membership on NZBA's Vulnerability Working Group,<sup>59</sup> and the Financial Assistance team's toolkit for proactively supporting and preventing vulnerable customers from spiralling into further debt. ASB has also recently created a 'Customers in Vulnerable Circumstances Standard' which helps ASB to meet its obligations under the incoming Conduct of Financial Institutions legislation (which will form part of ASB's Fair Conduct Programme).
- 16.3 Accordingly, we are already working to ensure vulnerable customers' needs are met and will continue to do so in the future. This includes progressing the development of a basic bank account product, alongside a host of other initiatives aimed at providing greater access to bank accounts and assisting vulnerable customers more generally to navigate the financial system.

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<sup>56</sup> For additional detail, see ASB's PIP response at 27.3.

<sup>57</sup> For additional detail, see ASB's PIP response at 15.2 to 15.3.

<sup>58</sup> For additional detail, see ASB's PIP response at 15.3(h).

<sup>59</sup> For additional detail, see ASB's PIP response at 15.4 to 15.6.

**Appendix 1: APRA and Basel III risk weights for performing loans by LVR bands in comparison to RBNZ standardised and ASB IRB models**

<b>Owner Occupied:</b>							
<b>Current LVR Band</b>	<b>a. 0% to 50%</b>	<b>b. 50.01% to 60%</b>	<b>c. 60.01% to 70%</b>	<b>c. 70.01% to 80%</b>	<b>d. 80.01% to 90%</b>	<b>e. 90.01% to 100%</b>	<b>f. &gt; 100%</b>
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%

<b>Investor:</b>							
<b>Current LVR Band</b>	<b>a. 0% to 50%</b>	<b>b. 50.01% to 60%</b>	<b>c. 60.01% to 70%</b>	<b>c. 70.01% to 80%</b>	<b>d. 80.01% to 90%</b>	<b>e. 90.01% to 100%</b>	<b>f. &gt; 100%</b>
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%

The table illustrates that the RBNZ implementation of the standardised risk weight model is less risk sensitive than those used in other jurisdictions.