The Treasury

Phase 1 RBNZ Act Review Information Release

December 2018

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[2] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand;
[3] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials;
[4] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions;
[5] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice;
[6] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice;
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Treasury Report: Reserve Bank of New Zealand (Monetary Policy) Amendment Bill: Draft Departmental Report

Date: 3 October 2018
Report No: T2018/2587
File Number: MC-1-7-6

Action Sought

<table>
<thead>
<tr>
<th>Action Sought</th>
<th>Deadline</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minister of Finance (Hon Grant Robertson)</td>
<td>Agree recommended changes to the Bill.</td>
</tr>
<tr>
<td></td>
<td>Approve the draft Departmental Report to the Finance and Expenditure Committee.</td>
</tr>
</tbody>
</table>

Contact for Telephone Discussion (if required)

<table>
<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Telephone</th>
<th>1st Contact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Virginia McLean</td>
<td>Contractor - Macroeconomic &amp; Fiscal Policy Team</td>
<td>[7]</td>
<td>✔</td>
</tr>
<tr>
<td>Ben Gaukrodger</td>
<td>Senior Analyst - Macroeconomic &amp; Fiscal Policy</td>
<td>[1]</td>
<td></td>
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</tbody>
</table>

Actions for the Minister’s Office Staff (if required)

Return the signed report to the Treasury and pass on any feedback on the draft Departmental Report. Subject to the Minister of Finance’s decision, refer this report and attachment to the Associate Ministers of Finance (Hon Parker, Hon Jones and Hon Shaw).

Note any feedback on the quality of the report.

Enclosure: Yes Departmental Report Reserve Bank of New Zealand (Monetary Policy) Amendment Bill (Treasury:4006212v2)
Purpose of Report

1. This report seeks decisions on two proposed changes to the Bill and your approval of the attached draft *Reserve Bank of New Zealand (Monetary Policy) Amendment Bill: Departmental Report to the Finance and Expenditure Committee on submissions on the Bill* (Departmental Report).

Background

2. The Reserve Bank of New Zealand (Monetary Policy) Amendment Bill (the Bill) had its first reading on 26 July 2018 and was referred to the Finance and Expenditure Committee (the Committee). Officials presented the initial briefing to the Committee on 5 September. The Committee received 14 submissions on the Bill and heard six.

3. The Committee will report to the House on 3 December. We have commenced planning and delivering activities for implementation of transitional provisions in the Bill in anticipation of the Bill being passed in December. The Reserve Bank Board has begun the search for potential external members to the Monetary Policy Committee (MPC).

Summary of Submissions

4. Of the 11 submissions that commented on the changes to the objectives of monetary policy, a slight majority (six) supported the addition of an employment objective for monetary policy, although most of these submissions recommended changes to the wording of the employment objective. A large majority of submissions supported the MPC, with most proposing changes. Table 1 below provides a breakdown of submissions.

<table>
<thead>
<tr>
<th>14 Submissions</th>
<th>Monetary Policy Objectives</th>
<th>MPC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Submissions were from five individuals, two banks, six industry organisations and 1 think tank</td>
<td>6 Supported (4 of the 6 supported with amendments)</td>
<td>9 Supported (6 of the 9 supported with amendments)</td>
</tr>
<tr>
<td></td>
<td>5 Opposed</td>
<td>2 Opposed</td>
</tr>
<tr>
<td></td>
<td>3 Did not specify</td>
<td>3 Did not specify</td>
</tr>
</tbody>
</table>

Key issues and recommendations

5. The Departmental Report provides a detailed analysis of the issues raised in submissions, our response and recommendations. A summary of issues raised in submissions is below:

- **Inclusion of the employment objective**: four of the five submissions that opposed the employment objectives did so because they believed it undermined the price stability objective. Their preference was to dismiss the Bill.

- **Phrasing of the employment objective**: five submissions proposed changing the employment objective from “supporting maximum sustainable employment” to something else, such as “supporting full employment”, “avoiding involuntary
unemployment”, “minimising unemployment”, or “keeping the rate of unemployment as low as possible”.

- **Relationship between the price stability and employment objectives**: five submissions proposed changes to clarify the relationship between the two monetary policy objectives. Most sought changes to introduce a hierarchy between the two objectives, with price stability taking precedence.

- **Process for setting operational objectives**: five submissions proposed changes to how the operational objectives are set. Proposals included retaining the Policy Targets Agreement provisions in the Act, removing the public consultation requirement, or having an independent committee advise the Minister of Finance (the Minister) on the remit for the MPC, rather than the Bank.

- **The design of the MPC**: six submissions recommended changes to elements of the MPC’s design. Proposals included defining the scope of the MPC’s role in more detail, having a majority of external members on the MPC and changing the appointment process (with recommendations to both strengthen and weaken the Minister’s role in appointments).

- **Monitoring and oversight for monetary policy decisions**: three submissions recommended changes to how decisions by the MPC are reviewed. Proposals included having an independent 5-yearly assessment of monetary policy performance, and making changes to enhance the Board’s effectiveness.

6. Most of the submissions were on issues that had been thoroughly considered by the Independent Expert Advisory Panel, Regulatory Impact Statements, or in the case of wider issues, will be picked up in phase 2 of the Review of the Reserve Bank of New Zealand Act 1989 (the Act). Consequently, we have recommended no changes to the Bill on most issues.

**The Departmental Report includes two recommendations for change**

7. The attached Departmental Report contains two recommendations to change the Bill. One change relates to a proposal to require public consultation on the charter when it is under review, and the other change relates to the date for the main commencement.

8. The Reserve Bank provided input into the preparation of the attached Departmental Report and agrees with its contents, except for the recommendation to require public consultation on the charter. This issue is discussed below.

9. Both recommended changes are detailed and do not raise new policy issues, and for this reason we do not consider that they require a Cabinet decision. In addition to the two recommended changes to the Bill, we understand that PCO may recommend minor drafting or technical changes, for example to improve clarity.

**Proposal to include consultation on the charter**

10. The Bill requires that the Minister and the MPC must consider whether the charter should be replaced when a new remit for the MPC is to be issued. The Bank is required to seek the views of the public before giving advice on a new remit (although advice and public consultation is only required when an existing remit is set to expire, not when an existing remit is replaced before expiry via Order in Council). However, there are no consultation requirements relating to the charter. Apart from the first charter, the charter is agreed between the Minister and MPC. The charter will include requirements to promote transparency and accountability in connection with the performance of the MPC’s functions and decision-making procedures.

11. One submission (Westpac) proposed requiring public consultation on key matters covered in the charter (for example MPC decision-making and vote attribution).
Westpac’s argument for this change was that some matters reserved for determination in the charter constitute significant policy decisions, and consultation will add public legitimacy to the process for making such policy decisions.

**Comment**

12. The Treasury supports changing the Bill to require the Bank to undertake public consultation on the charter. The Treasury’s view is that such a change would help to ensure transparency and accountability arrangements evolve over time in a way that meets public expectations of a major public institution. This in turn would help the MPC build and maintain legitimacy in the eyes of the public. It would signal that there is a legitimate public interest in the issues, and that there is value to be gained from seeking public views in a review of the charter. It would also provide an opportunity for new ideas to be canvassed that otherwise might not be raised through an internal review process and it would increase the transparency of the charter review process.

13. To give effect to the proposal from Westpac, the Treasury recommends requiring the Bank to seek the views of the public on broad matters of public policy that will be determined in the charter rather than on the text of the charter itself (e.g. whether the views of individual MPC members should be attributed in the meeting record, or whether the MPC should vote on decisions by default or by exception). The Treasury recommends that such consultation would only be required in instances when the Bank also has to consult the public before giving advice on the remit (therefore, it would not be required if the Minister and the MPC agree to amend the charter at a different point in the cycle, as the Bill allows). Consistent with the provisions in the Bill for the first remit, the consultation requirement would not apply to the first charter.

14. The Treasury considers that this approach provides a practical means of taking the views of the public into account on a regular basis, without interfering in any negotiation between the Minister and the MPC on the precise wording of the charter. Consultation would have some resourcing implications. However, the Treasury expects that these will be relatively minor, given that consultation on the charter would be undertaken when the Bank will already be seeking the views of the public on its remit advice.

15. The Bank considers that legislating consultation on the charter is unnecessary, would make the Bill overly prescriptive and thereby limit flexibility for processes to evolve, and is conceptually confused. Given that the charter is an agreement between the Minister and the MPC, the Minister is able to seek the views of the Treasury and others before reaching an agreement, as is current practice with the Policy Targets Agreement. That the charter is an agreement with the Minister (rather than being set by the Minister or by the MPC in isolation) reflects the balance between the public’s legitimate interest in the areas of policy it addresses and that it also contains matters that are primarily operational in nature (decision-making procedures, in particular, being a largely internal matter).

16. The Bank considers that a consultation requirement does not fit with the agreement mechanism for the charter. In concept at least, an agreement follows a negotiation, in this case between the Minister and the members of the MPC acting collectively, and is an iterative process. It is not clear at which point consultation makes sense. For example, should the Bill specify consultation to take place prior to any negotiation, once the MPC had presented the Minister with an initial offer, or once the Minister had responded to that proposal? Nor is it clear yet whether or why only one of the parties to the agreement is required to take into account the views of the public. The Bank is not satisfied these and other such details have been considered sufficiently, and so in addition to considering this change to the Bill unnecessary is concerned that a process would be prescribed in legislation that limited the flexibility of the MPC and the Minister to optimise the charter agreement process going forward.
17. There are arguments for and against changing the Bill, and we seek your decision on this issue.

Proposal to set a precise date for main commencement

18. The second recommendation for change was not raised in submissions and comes from officials. The change concerns the date of the main commencement.

19. In the Bill, the main commencement is three months after Royal assent. This means the precise date of main commencement will not be known until the Bill is passed and receives Royal assent.

20. We had intended that the first decision made and announced by the MPC would be on 8 May 2019. This date was targeted to give sufficient time to properly induct new MPC members before they make a decision. It would also coincide with a Monetary Policy Statement, which would allow the MPC to discuss its approach and decision in depth. However, if the Bill was to receive Royal assent before 28 December 2018, the MPC would be responsible for the OCR decision on 27 March 2019.

21. We recommend that the Bill is amended so that the date for main commencement does not fall before 1 April 2019. This could be achieved by having the commencement date set by Order in Council.

Next Steps

22. We are continuing to refine the Departmental Report. The Committee requires the final Report by 11am Monday 15 October for circulation to Committee members in advance of the presentation of the Report on 17 October. We request decisions on the changes proposed, and any other comments on the Departmental Report, by Wednesday 10 October. This is to allow us sufficient time to make changes to the Report before submitting it to the Committee.

23. For your information, the indicative timeline is outlined in the Table 2 below. The timeline has recently changed because the Committee set aside two days (19 and 26 September) instead of the original one day to hear submissions.

Table 2: Indicative timeline for the Committee’s consideration of the Bill

<table>
<thead>
<tr>
<th>1-12 October 2018</th>
<th>17 October 2018</th>
<th>24 October 2018</th>
<th>31 October 2018</th>
<th>7 November 2018</th>
<th>12-23 November 2018</th>
<th>3 December 2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-sitting weeks</td>
<td>House sitting</td>
<td>House sitting</td>
<td>House sitting</td>
<td>House sitting</td>
<td>Non-sitting weeks</td>
<td>House sitting</td>
</tr>
<tr>
<td>Departmental Report presented</td>
<td>Revision-tracked version</td>
<td>Draft commentary / Deliberation</td>
<td>Report to House due</td>
<td></td>
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24. The Committee has not sought any advice or made any recommendations to change the Bill. If the Committee seeks further changes to the Bill at the meeting on 17 October, our ability to incorporate changes during the select committee process will depend on their significance. Given the limited time available, it may not be possible to have Cabinet consider any significant policy changes before the Committee reports to the House on 3 December. If the Committee does seek changes, we will report to you on those changes and recommend how to address them.
Recommended Action

We recommend that you:

a **note** that on 17 October we are presenting the attached *Reserve Bank of New Zealand (Monetary Policy) Amendment Bill: Departmental Report to the Finance and Expenditure Committee on submissions on the Bill*;

b **note** that because most of the submissions were on issues that had been thoroughly considered during the phase 1 Review, there are no substantive recommendations for change;

c **note** that the Treasury and the Reserve Bank have different views on whether the Bill should be amended to require public consultation on the charter;

d **agree** that the Bill should:

EITHER:

- be changed to require public consultation on the charter in parallel with consultation on the remit [Treasury recommended];
  
  **Agree/disagree**

OR

- not be changed to require public consultation on the charter [Reserve Bank recommended];
  
  **Agree/disagree**

e **agree** that the Bill is changed so that there is a mechanism to set a precise date for the main commencement, so as to avoid the commencement date occurring before or close to the OCR decision on 27 March 2019;

  **Agree/Disagree**

f **approve** the attached draft Departmental Report, subject to your feedback and minor editorial changes from our final proof read;

  **Approve/Not approved**

g **refer** to the Associate Ministers of Finance (Hon Parker, Hon Jones and Hon Shaw).

  **Refer/not referred**

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Ben Gaukrodger  
**Senior Analyst, Macroeconomic and Fiscal Policy**

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Hon Grant Robertson  
**Minister of Finance**