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## Executive Summary

Dosh welcomes the opportunity to submit to the Inquiry into banking competition in New Zealand. We congratulate the Government for launching this Inquiry to better understand the state of banking competition in New Zealand and to drive solutions to improve customer outcomes.

There is an opportunity for New Zealand to be a fast follower of world-best banking solutions, and to leverage the $1.8 billion fintech industry, by enabling the digital-only banking model to unlock greater competition and new customer value.

This requires the right regulation. NZ operates under banking regulations that limit competition, with high barriers to entry and a lack of capital available for start-ups. Building on the Commerce Commission's recent market study into personal banking services, this Inquiry is an opportunity to transform insights into meaningful action – including by catalysing legislative change.

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**Recommendations**

*1. Lower the barriers preventing competition in banking*

- Enable selected entities registered as financial service providers (FSPs) per the Department of Internal Affairs (DIA) framework to access the Exchange Settlement Account System (ESAS)
- Remove barriers and facilitate investment into fin tech entities driving competition in NZ
- Ensure fair access to Open Banking for all participants

*2. Address the regulatory constraints to drive competition and efficient access to lending*

- Amend initial capital requirements for bank registration to reflect the actual risk of an entity
- Enable more FSPs to use the phrase 'banking services' to describe their services where appropriate (with only registered banks to use the term 'bank' in their title)
- Remove unnecessary KYC/AML requirements – including, for example, the requirement to prove a new customer's address
- Adjust prudential capital requirements per the Commerce Commission's recommendations

We discuss each of these recommendations in turn, drawing broad alignment with the terms of reference.

Dosh's submission may be publicly disclosed and Dosh's contact person for this submission is:

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## 1. Lower barriers to entry preventing competition in banking

### Limitations of FSP access to ESAS

Currently a barrier preventing competition in banking and a direct driver of higher consumer prices, is the accessibility of the Exchange Settlement Account System (ESAS). This system gives registered banks the opportunity to place capital with the Reserve Bank earning the Official Cash Rate (OCR) in interest. This enables banks to lay off customer deposits and earn the OCR. If more financial services providers (FSPs) were able to do this, they would be able to pass the improved rate that they earn to customers, significantly improving the rate that customers earn on deposits.

This has a further benefit of reducing potential conflicts of interest that arise from Bank's providing retail customer deposit rates, while also setting rates for FSP competitors in the market. This would limit non-bank FSP's exposure to incumbent banking rates by giving them access to wholesale rates.

In essence broader access to ESAS would allow a wider range of FSPs to offer better interest rates to consumers, and would have a flattening effect on prices. This is the single, highest impact action that the Government could take to drive competition and transfer wealth from banks to customers.

**Recommendation:** Enable selected entities registered as financial service providers (FSPs) per the Department of Internal Affairs (DIA) framework to access the Exchange Settlement Account System (ESAS). Entities should meet minimum criteria to ensure the system access is preserved for qualified providers. Such criteria could include

- a minimum of two years track record of managing customer deposits for each customer segment they are sourcing deposits

- a minimum of $5m customer deposits under management

- at least one AML/KYC audit completed and available for review.

## Barriers to accessing capital for investment in fin tech

A lack of access to capital in New Zealand is an economy-wide challenge, reflecting our scale and distance from global markets. However, there is an opportunity to unlock the capital that is available in New Zealand by supporting its investment into strategic companies. This includes fin tech companies – with only $22m raised for the sector in the last calendar year.

**Recommendation:** Remove barriers and facilitate investment into fin tech entities driving competition in NZ

## Unequal access to open banking

There is early evidence that fin tech access to open banking APIs will be constrained or limited entirely. Bilateral arrangements need to be replaced by industry wide arrangements that are fair and consistent in their application. Payments NZ, in their role governing this process, need to ensure all entities face equal and fair access to open banking if the promise of improved competition is to be met.

**Recommendation:** Commerce Commision to ensure Payments NZ delivers fair access to open banking for all industry participants.

## 2. Address the regulatory constraints to drive competition and efficient access to lending

### The Reserve Bank's initial capital requirements

We support the role of the Reserve Bank in protecting the financial stability of the system. However, the current capital requirement of $30m to become a bank is out of step with other jurisdictions and is poorly rationalized. Rather than responding to risk, the current capital requirement is a blunt instrument and barrier to entry.

We recommend that the initial capital required for an entity to register as a bank is staggered in proportion to risk. This would require the Reserve Bank to undertake a risk assessment of the entity seeking bank registration. We recommend that the Reserve Bank use broadly the same parameters for this assessment as those set out in its application form for new bank registrations. These include:

- The size and nature of the business
- background and experience of the board and executive
- the extent to which credit is being relied on, and
- time in financial services market (including as a non-bank provider)

**Recommendation:** Replace the $30m initial capital requirement with a tiered requirement which is proportionate to risk

## Restrictions on the use of the word ‘banking services’

The Reserve Bank currently has stringent restrictions – with heavy penalties for non-compliance – setting out which entities can call themselves a ‘bank’, or refer to their financial services as ‘banking services’. Whilst we agree that the term ‘bank’ ought to be limited to those who have successfully applied to become a bank, we believe that all registered FSPs should be able to refer to services they provide – which are synonymous with those provided by a bank – as ‘banking services’. This would create greater customer recognition of the services offered by non-bank FSPs (NBFSPs) and even the playing field between NBFSPs and banks – increasing competition and customer choice.

**Recommendation:** Change the Reserve Bank restrictions around the use of the term ‘banking services’ to allow NBFSPs to use this description of their services.

### Unnecessary Know your customer / Anti-money laundering requirements

The Anti-Money Laundering (AML) requirements – including ‘know your customer’ (KYC) requirements are dated, impractical and restrict some groups to from accessing banking services. These include

- confirm a customer’s address before providing them with financial services. Meeting this requirement electronically is generally done by way of someone’s credit profile – excluding those customers who do not have one. This has the perverse effect of disproportionately excluding young people from accessing these services. Compliance with this requirement also increases cost which is passed on to consumers.
- Limitations to New Zealand issued identification for electronic verification mean foreign residents in New Zealand are less likely to access digital services.

**Recommendation:** Update the AML/KYC requirements to ensure equal access to digital financial services, specifically for young people and foreign residents.

### The role of prudential regulation and any impacts on risk allocation, smaller banks, and non-bank deposit takers (NBDTs)

The current prudential capital requirements (set out by the Reserve Bank’s proportionality framework) have a flow-on effect to customer prices and limit competition by creating an uneven playing field between Tier 1 and Tier 2 banks. We support the Commerce Commission's position on this as set out in their recent market study report, and recommend that this is advanced.

**Recommendation:** Advance the Commerce Commission's proposed changes for prudential regulation, as set out in the final market study report into personal banking services