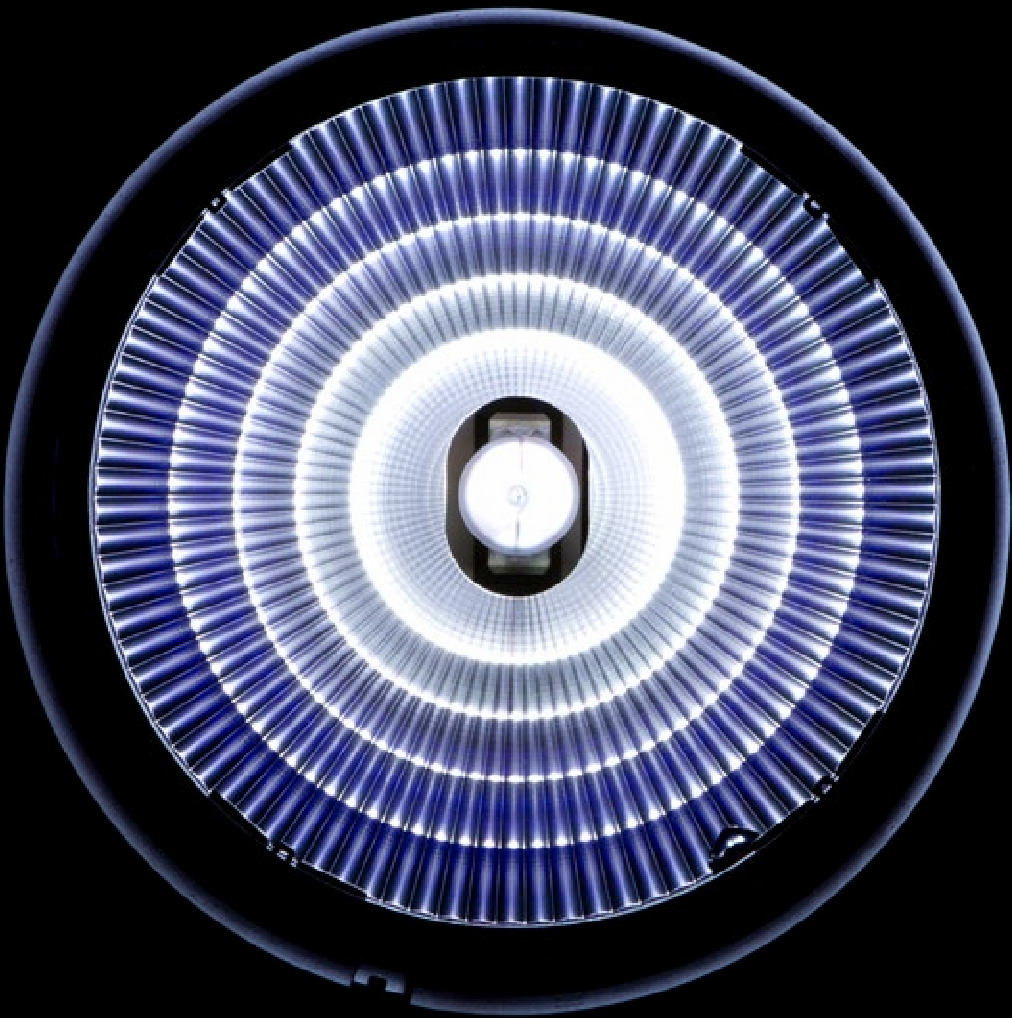


Section 95 – Review of ANZ Bank New Zealand Limited – Effectiveness of the directors' attestation and assurance framework

ANZ Bank New Zealand Limited

Context

Introduction

In response to a number of matters that received public attention from March to June 2019, the Reserve Bank of New Zealand (RBNZ) issued a formal notice to ANZ Bank New Zealand Limited (ANZ NZ or “the bank”) requesting that it engage an external party to complete two section 95 reviews.

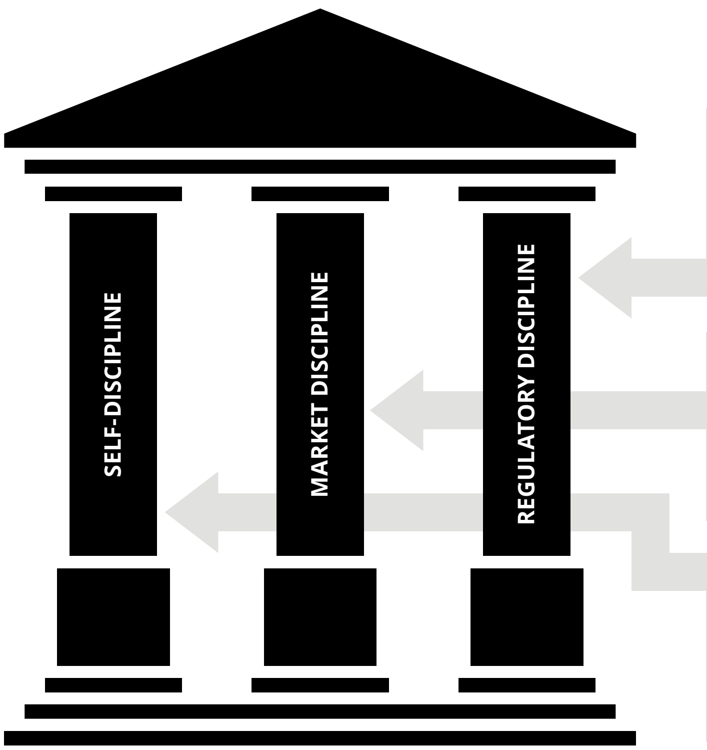
The first of these reviews was to assess the effectiveness of the directors’ attestation and assurance framework in use by ANZ NZ after 22 November 2017 (focusing on internal governance, risk management and internal controls) and to answer specific questions in relation to four case studies. The second review was to assess compliance with the RBNZ’s capital adequacy requirements from the time of accreditation.

ANZ NZ commissioned Deloitte New Zealand (Deloitte) to complete these reviews and this report documents our findings from the first review. The second review is still underway.

Regulatory overview

The RBNZ’s approach to banking supervision relies on the three pillars of self-discipline, market discipline and regulatory discipline. The self-discipline pillar relies on the bank directors signing “attestations” confirming their bank has complied with its regulatory obligations across a range of areas. These directors’ attestations are made in “disclosure statements” – which also include various financial performance information – that all registered banks must publish twice a year.

Figure 1: Three pillars of RBNZ’s approach to banking supervision



Regulatory discipline
The mandated rules and requirements set by the RBNZ to support the safety and soundness of individual institutions and the stability of the financial system as a whole.

Market discipline
The way in which market participants influence a financial institution’s behaviour by monitoring its risk profile and financial position.

Self-discipline
The responsibility of senior management and directors for an institution’s own processes and risk management frameworks.

The New Zealand regime is different from many others in that the regulator historically has not conducted direct onsite supervision to confirm that banks are complying with its requirements. This makes the directors' attestation system and the assurance framework that underpins it particularly important. It is designed to put the onus on bank directors to make their own due inquiries and to be rigorous in reaching their beliefs before they sign off on each set of disclosure statements.

The five directors' attestations state that the directors believe, after due enquiry, that:

1. The disclosure statement contains all the information required (by the Order in Council).[1]
2. The disclosure statement is not false or misleading.
3. The registered bank has complied with all conditions of registration (CoRs) that applied during that period.
4. Credit exposures to connected persons (if any) were not contrary to the interests of the registered bank's banking group.
5. The registered bank had systems in place to adequately monitor and control material risks, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk and other business risks, and that those systems were being properly applied.

What we were asked to do

The focus of this review was, in essence, whether ANZ NZ has adequate systems in place to enable the bank's directors to sign their attestations with confidence. Further, whether any failures in those systems led directly to the matters that raised the RBNZ's concerns (the "case studies").

Specifically, ANZ NZ engaged Deloitte to:

- assess the effectiveness of ANZ NZ's arrangements to support the required directors' attestations
- consider the RBNZ's feedback letter of 22 November 2017 on the directors' attestation thematic review, including the bank's response to the "areas for improvement" identified in that letter
- review the internal governance, risk management and systems and controls ANZ NZ has in place to ensure the business and affairs of ANZ NZ can be run in a prudent manner under the direction of the ANZ NZ Board
- consider four case studies nominated by the RBNZ in light of specific questions asked by the RBNZ.

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1. Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014.

Summary assessment

Our view is that ANZ NZ's directors' attestation practices stand at a maturity rating of 3 out of 5. This is a level that we describe as "Defined & Integrated" on the scale we developed as part of a 2017 industry-wide ("thematic") review of directors' attestation practices among New Zealand banks (see Figure 2 below). ANZ NZ was also considered to be "Defined & Integrated" at that time with identified improvements.

This rating shows that the core of the bank's directors' attestation practices is functioning adequately, but is not yet fully effective and improvement is required. In particular, the bank largely has sound practices in place to support Attestations 1 and 2. These practices enable ANZ NZ to confidently attest to the bank's financial position and financial reporting risk, and to approach the majority of the RBNZ's CoRs (which are covered by Attestation 3) with confidence.

Our view is that the bank's approach to Attestations 3 and 4 is less robust than Attestations 1 and 2, but more formalised and structured than for Attestation 5 (which is the least robust, informed and structured, with some gaps in accountability and inconsistent application). The bank's improvement plan, together with our recommendations should enhance the design and effectiveness of Attestations 3 to 5.

We note that the bank's current Board and Management have a high level of awareness of the directors' attestation and assurance framework and are focused on ensuring its effectiveness. This is reflected in a range of improvements that have been made since the RBNZ issued its feedback letter in 2017 and particularly where the activity has significantly accelerated in recent months.

However, to move to a 4 or 5 on our maturity scale, ANZ NZ would need to achieve significant uplifts in terms of the robustness and sustainability of its governance, risk management and controls. It would also need to ensure that the reforms it was making to aspects of its culture in relation to the directors' attestation framework, which historically evidenced a level of complacency, are executed effectively. This cultural challenge was shown through a lack of urgency in improving practices (noting the slow start in responding to the concerns expressed by the RBNZ two years ago) and an over-reliance on trust in key individuals. It was also shown through a highly trusting working environment, which can and did, lead to insufficient challenge of information and evidence (as seen in the operational risk capital model breach issue described in Case study 1 below).

As part of our review, we have interacted with all of the current directors and many members of the Executive and Management. Based on our work and throughout all of these interactions we do not see that complacency is presently an issue in relation to the directors' attestation and assurance framework.

Our review notes a range of other weaknesses in the bank's approach, especially around Attestation 5, and provides related recommendations for improvements or notes initiatives the bank has underway.

In addition, a number of in-use but unapproved credit models were identified in mid-November 2019 during the section 95 review of the bank's capital adequacy requirements (which was ongoing at the time of this report). This matter has been communicated by us and ANZ NZ to the RBNZ, and is in addition to ANZ NZ's self-reported operational risk capital breach.

We believe the root causes of these exceptions (which occurred approximately 10 years ago) are likely to be similar to the ones behind the operational risk capital breach. These causes were historic assumptions about whether the bank's models were approved, a culture of acceptance and lack of challenge, and an absence of adequate checks and balances.

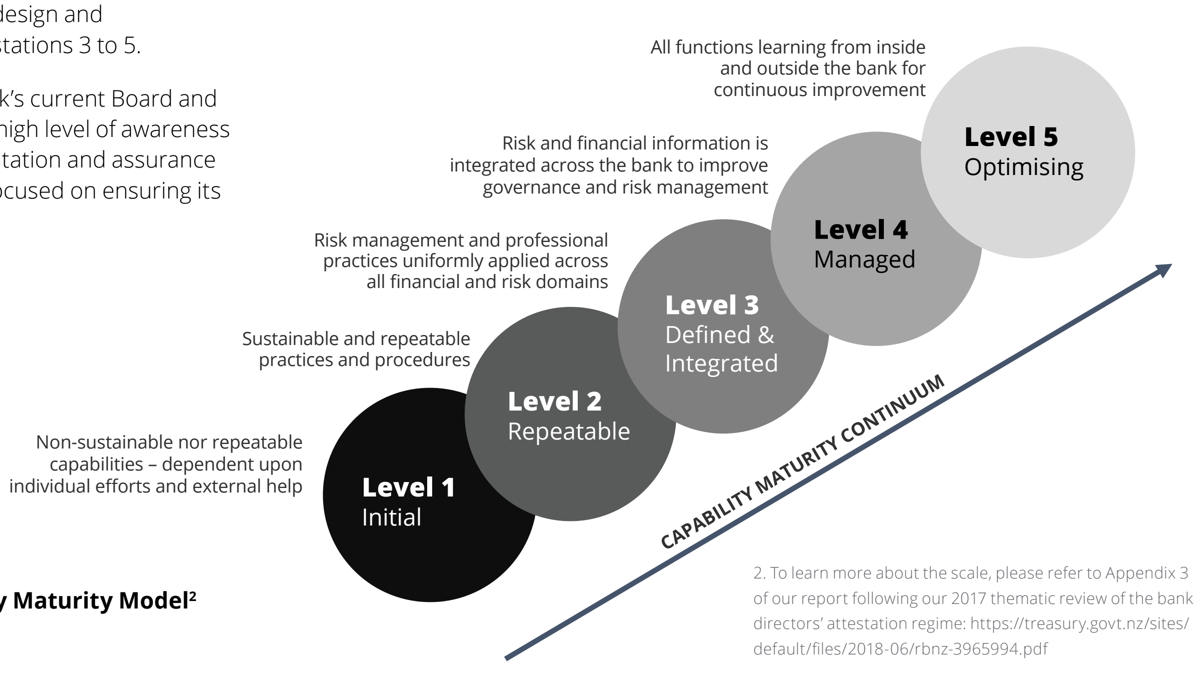

Figure 2: Capability Maturity Model[2]

2. To learn more about the scale, please refer to Appendix 3 of our report following our 2017 thematic review of the bank directors' attestation regime: https://treasury.govt.nz/sites/default/files/2018-06/rbnz-3965994.pdf

Key findings

The systems and processes ANZ NZ has in place to support the directors' attestations required by the RBNZ are complex and highly interrelated. These key findings highlight a range of issues that were evident during our review period, while also noting the significant number of improvement initiatives that the bank has underway. Notwithstanding these issues, including the Operational Risk Capital Model decommissioning and the un-approved credit models the underlying attestation framework still supports a rating of 3 out of 5.

Recent progress

Elements of the bank's arrangements for supporting its directors' attestations have improved since 2017, but there is significant work to do.

We believe the bank has positive intent regarding the work being done to enhance the controls that the attestation framework fundamentally relies upon. This is appropriate and valuable, and we note that the bank's focus on the improvement programme has increased since the appointment of the new Chairman and, more recently, the Acting CEO.

The improvements made to date are modest relative to the bank's planned initiatives. A full programme of work will be necessary to lift the framework to a point where each attestation is fundamentally backed by hard evidence, and for the bank to be considered closer to Level 4 on our maturity scale.

Governance

The Board is overly reliant on the high quality of individuals within the bank when processes, governance and controls are inconsistent.

Throughout our interviews it was clear there was a strong understanding of the critical nature of the directors' attestation process and its outcomes. In particular, the bank's Board members are active in participating in the attestation process through review and engagement with the Executive in relation to the attestation material and associated evidence. The Board gains comfort for its attestations through awareness of the significant number of management and control processes presented by the Executive to support attestation requirements, particularly, but not exclusively, as they relate to Attestations 1 and 2.

This positive intent needs to be matched with a more explicit and well-articulated understanding of the interrelated nature of the five attestations. The requirement for the degree of formality and rigour seen in Attestations 1 and 2 needs to be matched in the bank's approach to Attestations 3, 4 and 5.

This formality relates to structure, documentation and clear definitions of the roles, responsibilities and accountabilities of all those involved in the preparation of attestation materials. These issues remained in place at the time of our review, leaving the Board effectively trusting in the intent, capability, judgement and vigilance of a number of individuals who play key roles in the attestation process – from the front line to the executive levels – in the organisation.

The Board should set the standard for the directors' attestation programme, and embed accountability across the programme.

We determined that the Board was clear it ultimately owned the attestation framework. We also observed that operational accountability for the framework was split between the Chief Financial Officer (CFO), who is responsible for Attestations 1 to 4 and presents to the Board Audit Committee (BAC), and the Chief Risk Officer (CRO), who is responsible for Attestation 5 and presents to the Board Risk Committee (BRC). The attestation sign-off by the Board is supported by a confirmation letter signed by the Chief Executive Officer (CEO) and CFO that covers off Attestations 1 through to 5, which is supported by Management representation letters for Attestations 1 and 2 and an attestation statement from the CRO in relation to Attestation 5.

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Throughout our interviews it was clear there was a strong understanding of the critical nature of the directors' attestation process and its outcomes.

The framework is designed and executed to a standard defined by the CFO and CRO as the accountable executives, with input and challenge from the Board in relation to content. The Board is primarily a recipient of the outputs from the framework, with relatively recent activity designed to uplift its understanding and awareness of the framework's components. The Board's reliance appears justified in the case of Attestations 1 and 2, but needs to be supported by a deeper involvement in the design of the collective framework and, in particular, greater clarity in how Attestation 5 is addressed. This will in turn require a greater level of structure and rigour from the risk function.

Given the directors' attestation and assurance framework in its entirety incorporates an integrated and holistic view of the governance of the bank, we believe the Board should play a more significant leadership role in its ongoing development. Specifically, the Board should define the standard of evidence it requires to support its attestations, with the accountable executives building a framework that enables them to meet that standard.

In our view, while necessary, the current improvement programme is overly tactical and should be further developed based on a clear understanding of the future maturity level the Board believes appropriate, and the depth of evidence required by the Board to enable it to attest with confidence. The programme should also include workstreams that capture the organisational changes that will deliver broader results, such as governance and culture initiatives.

Culture

There was no evidence the bank has a culture of supporting non-compliance or deception, but there has been a level of complacency in relation to the execution of some aspects of the directors' attestation framework.

In recent years, ANZ NZ has recognised the value of taking a systematic approach to understanding the organisation's culture. Formal programmes have been in place since 2016 to assess culture, and more recently, the bank's Internal Audit function has created a team for assessing the company's culture as part of its audit activities.

In response to the November 2018 RBNZ and Financial Markets Authority (FMA) Bank Conduct & Culture Review and Report, ANZ NZ has introduced a significant programme of cultural uplift, which is, in our view, well directed. As a component of this broader programme, ANZ NZ has introduced mechanisms such as the Speak Up Champions initiative and I.AM framework[3] to enhance the ability of staff to be heard and accountable.

These are positive initiatives that supplement ANZ's whistleblower programme. Consistent with better practice, ANZ NZ has a range of options to enable people to raise concerns anonymously. The framework of communication options (including telephone, email and a web portal), external contact and portal management, and internal review and management of contacts, is designed to ensure whistleblower communication is taken seriously and is robustly and independently managed, and that the whistleblower is protected.

To protect the integrity of the whistleblower framework, the absence or presence of whistleblowers in relation to any aspect of our work remains confidential. As part of our work, we reviewed the ANZ NZ whistleblower policies and framework and found them to be sound.

Throughout our review of the directors' attestation framework, we have found no evidence to suggest that the bank's culture is characterised by any intention to wilfully non-comply, deceive or mislead as it relates to the directors' attestation practices. On the contrary, through our interviews with all directors, and our interactions with a wide range of senior managers and other personnel, we found the bank to be candid and transparent in all dealings with us. As a specific example, we found its response in the Trans-Tasman Facilities case study (Case study 4 below), showed the bank acting in the spirit of the RBNZ's subsequently released Relationship Charter.

Even so, we do believe that as evidenced through our review (in particular the operational risk case study and the more recently identified credit risk model issue) there has been a level of complacency or "cultural ease" when it comes to proactively identifying and dealing with shortcomings relating to matters underpinning elements of the directors' attestation framework. In these examples, inherent reliance was placed on people's knowledge and beliefs, as shown through the limited amount of evidence that was required when staff should have challenged supporting material for attestations. Our view is also based on the bank's reliance on a negative assurance approach ("nothing has come to my attention") in areas of its attestation processes.

3. I.AM simplifies the approach to operational risk and promotes the concept of "Identify, Act, Monitor".

This lack of challenge is evident in the response to improvement opportunities, such as the RBNZ directors' attestation–related letter of 2017 and the section 95 Review of Westpac New Zealand's compliance with BS2B. The RBNZ letter and Westpac review could have provided the impetus to robustly review the accuracy of data and the effectiveness of controls around ANZ NZ models.

Framework design

The bank should recognise that all attestations are interrelated, rather than approaching them as separate items.

The five individual attestations are intended to be considered as an interrelated and collective articulation of the strength of a bank's governance. ANZ NZ has a structured framework that considers predominantly financial attestations together (Attestations 1 and 2), the individual CoRs (Attestations 3 and 4), and the risk attestation (Attestation 5) separately. This approach is operationally convenient, but because the systems are inexorably linked, it fails to acknowledge that the weaknesses present in Attestations 3 to 5 have an impact on the strength of the framework as a whole.

Considering the attestations in silos could reduce the Board's opportunity to test the strength of systems and processes more broadly, and may limit the ability to identify weaknesses that would question its unqualified attestation.

This has already been seen in the example of the operational risk capital breach and some unapproved credit risk models. In these cases, a failure of a framework element that sits in Attestation 5 is specifically attested to in CoR 1B within Attestation 3, and any resulting material variances relating to regulatory capital requirements (including the methodology used) will be reflected within the disclosure statements and are therefore captured in Attestations 1 and 2.

We note that this is not necessarily unique to ANZ NZ and reflects the evolution of directors' attestation frameworks more generally across the sector.

Inconsistencies in architecture and content across the financial and risk attestations limit the effectiveness of the framework overall.

Attestations 1 and 2 largely (but not entirely) relate to financial matters. The bank's financial control framework, which underpins the preparation of the financial statements, is mature, well understood and executed by competent and senior personnel. Not surprisingly the framework that supports the bank's process to obtain director sign-off for Attestations 1 and 2 is similarly more mature than for the remaining attestations.

However, Attestations 3, 4 and 5 do not enjoy the more comprehensive structure and formality that underpins Attestations 1 and 2. Although we were able to identify a significant amount of relevant control work across the bank that either directly or indirectly supported these attestations, this work was not explicitly structured and managed in a way that ensures complete coverage and articulation of any of these attestations, nor do they provide a robust foundation to support Attestations 1 and 2.

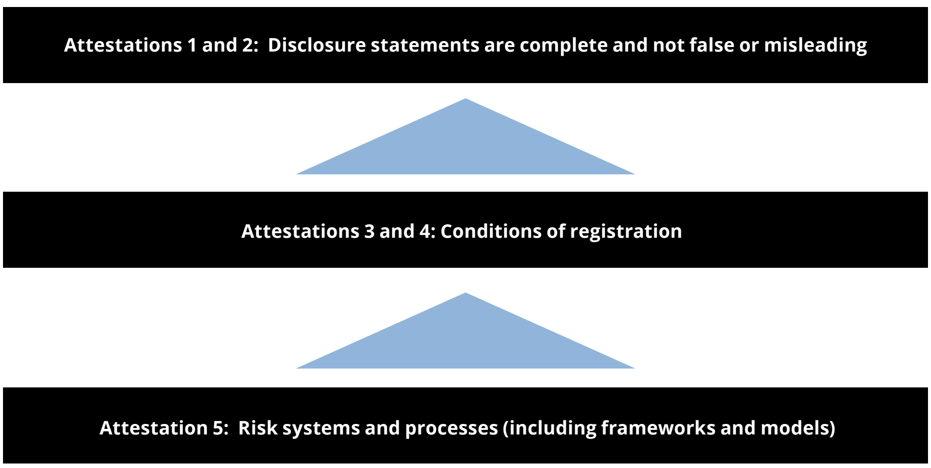
Figure 3 illustrates the attestation relationships.

Assurance over Attestation 5 needs to become genuinely positive.

Negative assurance substantially persisted for Attestation 5 at the time of our review, even though the final attestation sign-off was presented as "positive assurance".[4]

This design logic weakness (for Attestation 5 and potentially all of its dependent attestations) is being resolved through the bank's Attestation 5 enhancements. However, the issue cannot be comprehensively resolved until the bank's relevant compliance plans[5] (that is, for Attestations 3 and 4) have been completed and proven to be effective from both a design and operational perspective. This is due to the fact that compliance with Attestations 3 and 4 has a direct and indirect link to the assessment of material risk management, which in turn impacts on the sign-off on Attestation 5.

Figure 3: The relationship between Attestations 1 to 5



4. "Positive assurance" is a statement asserting to what the accountable or responsible person believes regarding the content asserted. For example, "I believe to the best of my ability there is no material mis-statement in…" is a form of positive assurance. A "negative assurance" refers to a statement about what the accountable person or responsible person does not know. For example, "I am not aware of any instances of…" is an example of a negative assurance statement.

5. A compliance plan comprises a set of defined procedures that collectively specify and establish compliance expectations, requirements and the specific activities and required supporting evidence to meet the required legislative obligations.

Assurance

The assurance framework is not integrated, and assurance activities appear to have had limited effectiveness in relation to the directors' attestation framework.

A number of assurance activities based on the "three lines of defence" model take place across the attestation framework to effectively manage current and emerging risks. Within each of these lines of defence, separate actions are undertaken to assess if the framework is robust and delivering the outcomes that are required.

The first line of defence includes the business unit Operational Risk. First line risk teams own and manage the risks and are responsible for implementing and executing control reviews and assurance activities, and conducting risk assessments. Second Line Operational Risk and Compliance oversees the management of risks, including supporting the first line in escalating and resolving incidents and events. The third line of defence includes Internal Audit, which undertakes independent risk-based assurance reviews.

For the Board to gain maximum comfort from these assurance activities, it needs to understand the degree to which these lines of defence capture all of the critical elements of risk across the framework – that is, to provide an integrated view of assurance.

The responsibility for ensuring that a robust and integrated framework of assurance is in place typically rests with the second line of defence – with the exception of the financial statement risks, which are the responsibility of the Finance function. Our view is that the bank's assurance mechanisms as they relate to the directors' attestation framework and associated infrastructure (across all three lines of defence) are not integrated. In particular, the purpose and scope of assurance activities are not well defined, understood and complementary across the first and second lines. This subsequently limits the ability for the third line (Internal Audit) to execute its required independent assurance role.

A top-down, strategic and integrated approach to assurance will enable the Board to be confident that all critical controls across the director's attestation framework are adequately supported by assurance activities.

Our review indicated that assurance activities undertaken across the three lines of defence were limited in their effectiveness, often due to the lack of examination and testing of existing processes to ensure they were effectively designed to achieve the outcome required. In addition, while it is positive that Internal Audit increased its effort across the CoRs from FY18, this work appears to have had limited impact in identifying control weaknesses during the review period. Their limited impact may be due to the lack of compliance plans specifying the required obligations and therefore providing the foundation on which to base their testing, and an earlier focus on monitoring of review controls rather than on obligations testing. Regardless, Internal Audit needs to increase its ability to challenge the business to identify core underlying control weaknesses.

The operational risk capital case study again supports this observation. Annual CoR audits, the 2018 BS2B audit conducted by Internal Audit, and other assurance activities collectively failed to identify this longstanding breach. This indicates the bank's combined assurance activities, as they relate to the directors' attestation process, were limited in their effectiveness during the period of our review.

Our view of the case study matters

As stated above, the RBNZ asked us to review four case studies regarding matters that received public attention in early 2019. These are the:

- Case study 1: Operational risk capital breach
- Case study 2: Inaccurate management attestation of the former CEO's expenses
- Case study 3: Transaction relating to the St Heliers property
- Case study 4: Breach relating to treatment of commitments.

Our view is that three of the four case studies do not represent systemic failures in ANZ NZ's directors' attestation and assurance framework. The exception is the critical failures that led to the first case study (that is, the operational risk capital breach).

We believe the influence of the lack of challenge and a historically complacent approach, (particularly in the risk function), the absence of a comprehensive compliance plan, diffused accountability and inadequate assurance processes, all contributed to the operational risk capital breach not being identified for more than five years. These factors may also be behind further unapproved models being found in our second review.

However, we note that the work being conducted by the bank to address the relevant issues should dramatically improve its control environment over time.

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Case studies

Case study 1: Operational risk capital breach

This case study focuses on the bank's use of an unapproved operational risk capital model, and its management and the communication about the model status with the RBNZ. We believe the breach covered in this case study and the additional issues identified during the section 95 reviews in relation to the credit risk models indicate a weakness in the control framework in the risk environment that was not identified as part of the directors' attestation framework reporting.

Background

On 8 April 2019, ANZ NZ notified the RBNZ that it had breached the conditions of its banking registration by using an unapproved method for calculating the amount of capital it needed to hold to cover its operating risks. The bank reported it had used the unapproved approach – which rested on the final capital outcome of a model that had been decommissioned in 2014, and scaled up in line with the bank's growth – from 2014 to 2018 in the belief this method of calculating capital had been approved by the RBNZ.

While the bank has since addressed the issue and reported the breach, it was a serious error that highlights inadequacies in the framework of checks and balances that underpin the bank's directors' attestation framework. Specifically, we found that the original issue was caused by a failure to follow expected confirmation procedures and a lack of clarity around roles within the bank's risk teams. The issue was exacerbated by a culture of staff failing to question the status quo and trusting in verbal assurances, and other weaknesses around on-boarding, a lack of compliance plans and ineffective assurance.

We also believe that the facts relating to this operational risk capital breach indicate that there is a reluctance to "challenge" by the functions relevant to elements of the directors' attestation framework. The bank must ensure that it addresses this issue through its developing cultural programmes, to enable the risk framework to reach the required level of maturity.

Case study 2: Inaccurate management attestation of the former CEO's expenses

This case study relates to the reporting of the former CEO's expenses. We believe the non-identification of this incident arises from the CEO's inaccurate reporting of some of those expenses rather than a systemic issue regarding the directors' attestation framework. We also note that once aware of the issue, the ANZ NZ Chairman and Board responded promptly and in line with the requirements of the RBNZ.

Background

In March 2019, ANZ NZ became aware that its CEO at the time may have stated that a range of personal expenses were business expenses, which were subsequently incurred by the bank. The ANZ Group Integrity (GI) unit investigated the issue and determined that this had been the case in relation to some transport and storage expenses.

We note the former CEO has steadfastly asserted he was entitled to claim these expenses under his employment package as an expatriate, based on what he has said was a verbal agreement with the former ANZ Group CEO.

The GI investigation however found that the former CEO did not take steps to confirm the arrangements when the new ANZ Group CEO started, took actions that reduced the likelihood of the personal expenses being detected, and did not report the benefit associated with the expenses via the bank's Key Management Personnel Disclosure Booklet system during the eight and a half years he was CEO. These actions and to a lesser degree some, now addressed, weaknesses in expense controls within the CEO office, led to this issue going undetected for a number of years.

ANZ was concerned that the former CEO's actions could be in breach of ANZ NZ's policies. This contributed to his departure as CEO in June 2019. We note that the former CEO declined our offer to be interviewed in person for this review, but did provide written responses to our questions.

Case study 3: Transaction relating to the St Heliers property

This case study relates to the purchase of a house in Auckland by the bank for the use of the former CEO and its later sale to his wife. Our conclusion is that these transactions were completed at arm's length, in a manner that was appropriate based on the situation and available information, and do not indicate systemic weaknesses in the directors' attestation framework. The valuations that were conducted subsequent to the sale of the house do not change this perspective as they were conducted in hindsight and considered information that was not available at the time of the sale price being determined.

Background

The former CEO was announced as CEO of the then ANZ National Bank in late 2010 and agreed to move with his family to New Zealand to take up the role. After being unable to find suitable rental accommodation, the bank agreed to buy a house in St Heliers in Auckland for $7.55 million. As part of his remuneration package, he was given an allowance that he used to rent the house from the bank.

In 2015, the bank decided to sell the house to reduce its non-core assets. During the course of 2016, discussions commenced with the former CEO to transfer him from an expatriate to localised status. In 2017, the bank sold the house to his wife for $6.9 million (including GST). This amount was the mid-point of two independent valuations received by the bank less $100,000 for sale process related expenses.

Given the seniority of the former CEO, it was appropriate that the bank elevated both the purchase and sale transactions to Board level. The initial purchase of the house was not a related-party transaction at the time of the purchase by the bank. The house was held by Arawata Assets Limited (AAL), which held all of the bank's real property and was a logical entity to hold the asset.

The sale of the house to the former CEO's wife was overseen by the previous ANZ NZ Board Chairman. It was completed at arm's length and based on independent market valuations, as sought by the previous Chairman. The AAL Board approved the house sale based on the information and work undertaken by the previous Chairman.

We also found the purchase and sale of the house fell outside any directly relevant bank policies (no specific policies existed or applied to the situation), so none were breached. Overall, we do not believe the incident highlights any systemic faults in the effectiveness of the directors' attestation framework.

There has been media commentary about the price at which the former CEO's wife bought the property and some of the expenses that were covered by the bank while his family was renting it. Our review found that the 2010 purchase of the house and its sale in 2017 were conducted at arm's length and the sale price was based on independent valuations, and the controls established to manage maintenance of the property were adhered to.

Subsequent valuations (in 2019) reported in the media do not invalidate the process undertaken at the time of sale. The retrospective nature of the valuation provided by Simplicity means it is not possible to compare it with the earlier valuations as it considered information that was not available at the time. The valuation quoted by Simplicity places reliance on an Auckland City Council rating valuation of $10.75 million. The Auckland City Council valuation was effective from July 2017; however, the valuation was not available until November 2017, while the sale and purchase agreement of the house was executed on 31 March 2017.

For clarity, the scope of our review did not include a determination of an appropriate value for the house at the time of sale.

Case study 4: Breach relating to treatment of commitments

As a major bank with an Australian parent, ANZ NZ provides Trans-Tasman Facilities (TTFs) to large corporate and institutional customers. This case study relates to ANZ NZ's treatment of these facilities and we find it does not point to systemic weaknesses in the bank's directors' attestation processes.

Background

When opening a new TTF in 2017, ANZ NZ revisited the treatment it had followed since 2008. When doing so, the bank could not find documentation confirming that the RBNZ had approved its capital treatment of TTFs. After discovering this issue, the bank's CFO and CRO approached the RBNZ to confirm its comfort with the current treatment.

The RBNZ said it did not regard the bank's treatment of the facilities as compliant with the terms of the BS2B Capital Adequacy Framework in its prudential rulebook. This led the bank to report the breach in its 30 September 2018 disclosure statement and to approve a new more conservative treatment of TTFs. The RBNZ did not take enforcement action against the bank, in part because it had been proactive in raising the issue.

As the RBNZ has acknowledged, the treatment of such non-routine facilities for regulatory capital purposes is complex. Further, the bank's proactive, open and collaborative response does appear consistent with the spirit of the RBNZ's subsequently released Relationship Charter.

Our recommendations

Our report provides recommendations for improving ANZ NZ's directors' attestation and assurance framework. These are summarised at a high level below.

- **Address the immediate structural weaknesses within the directors' attestation programme**: ANZ NZ is in the process of adopting tactical initiatives to improve the overall effectiveness of the directors' attestation regime. We observed key weaknesses that compromise the robustness of processes supporting Attestation 5 and, to a certain degree, Attestations 3 and 4. These gaps remain unaddressed at the time of our review, with various improvement initiatives either considered or underway. We believe that ANZ NZ needs to expedite and prioritise these initiatives, with particular focus on:
  - defining the expectations of Attestation 5
  - finalising and implementing compliance plans over ANZ NZ's CoR requirements.
- **Establish a strategic programme of improvement that is led by the Board**: A large number of directors' attestation–related improvement initiatives are underway and some had been completed prior to the date of our review. However, a significant number remain a "work-in-progress", including those related to Attestation 5, which the RBNZ noted in its November 2017 letter. Further, the improvement programme should have streams that deal explicitly with accountability for all elements of the directors' attestation framework.

  At present, the actions being undertaken represent a strong tactical response to the issues that have been identified. The uplift in the directors' attestation and assurance framework needs to be led and driven by the Board, with appropriate executive support, to ensure the bank obtains "outcomes" that are owned by the directors.

  For example, the Board should consider articulating its future target state as either Level 4 "Managed" or Level 5 "Optimising" on the scale[6] we provided in our 2017 review, and set out what it means for the bank to successfully achieve its desired level of maturity. This is necessarily work for the Board and should align with and drive its expectations and the requirements of future director training.
- **Enhance and complete the accountability matrix**: Develop a comprehensive responsible, accountable, consulted and informed (RACI) matrix for all Board, Executive and staff members involved in the directors' attestation programme. Ensure appropriate resources and support for all staff with these accountabilities, such that they are able to execute against the expectations effectively. This should include ensuring staff have the capabilities required to complete the roles expected of them.
- **Establish a programme to address the identified cultural issues**: Enhance the bank's existing cultural uplift programmes (I.AM and Speak Up) to ensure they address the cultural weaknesses identified in this review. This programme should be led by the Board and Executive, with behavioural expectations clearly articulated and structured to achieve change in a realistic timeframe.
- **Strengthen assurance and develop an integrated assurance plan**: The bank should strengthen the effectiveness of its assurance work. It should also develop an integrated risk-based assurance plan that ensures risks are progressively addressed by relevant assurance providers in a logical timeframe, based on a strong understanding of the holistic risk profile of the directors' attestation programme. The bank should also ensure all participants in the assurance framework are engaged in building the assurance plan; committed to and measured in their execution of the plan; and resourced and funded to enable them to succeed in executing the plan. It should also ensure the plan is sponsored by an appropriate Executive and the Board.

6. To learn more about the scale, please refer to Appendix 3 of our report following our 2017 thematic review of the bank directors' attestation regime: https://treasury.govt.nz/sites/default/files/2018-06/rbnz-3965994.pdf

Conclusion

As New Zealand's largest bank, ANZ NZ is ideally positioned to chart a future path for its directors' attestation framework that sets a more sustainable standard for itself and the sector at large. It has already made a substantial start through the initiatives it has commenced.

This review identifies further opportunities for improvement that are consistent with the expectation that ANZ NZ should be a leader in this area. We believe that if the bank completes the improvements it has planned or underway, and accepts and acts on the recommendations provided in this report, it can progressively move from Level 3 ("Defined & Integrated") to Level 4 ("Managed") on the scale described in our 2017 review.[7]

With an appropriate level of strategic focus and intent, and the desire to stay ahead of increasing regulatory and public expectations regarding best practice, it could move to Level 5 ("Optimising").

As New Zealand's largest bank, ANZ NZ is ideally positioned to chart a future path for its directors' attestation framework that sets a more sustainable standard for itself and the sector at large. It has already made a substantial start through the initiatives it has commenced.

7. To learn more about the scale, please refer to Appendix 3 of our report following our 2017 thematic review of the bank directors' attestation regime: https://treasury.govt.nz/sites/default/files/2018-06/rbnz-3965994.pdf

Disclaimers

Scope limitations

The work we have undertaken does not constitute a forensic investigation or assessment to identify, search for or quantify breaches or wrongdoing, nor does it express a conclusion about whether such actions are proper or legal. The review is not designed to examine all actual or potential breaches or issues the review is aware of or becomes aware of.

This report does not make any legal determination or conclusion as to the accuracy and reliability of the information covered by the directors' attestations, including making any assessment as to whether the directors' attestations are complete, compliant, false or misleading.

This report does not consider other controls or assurance processes that have no direct bearing on the directors' attestation process. Nor does it undertake any deep-dive assessments of specific management processes and systems (other than where they are central to the attestation arrangements and case studies). For avoidance of doubt, the review excludes any examination or audit of the personal expenses or financial interests of the Board and the Executive.

We provide no assurances that the information supplied is either complete or correct and accept no accountability or responsibility for the information supplied. The assumptions used within this report are based on the R*eserve Bank of New Zealand Act 1989* and regulations in force in New Zealand at the time of writing and the results/findings have been provided following all reasonable engagement with senior officers of ANZ NZ concerned and the representations made and information supplied by these officers in response to our requests.

Professional standards

As a member of the New Zealand Institute of Chartered Accountants, all work performed by Deloitte is subject to the Accounting Professional and Ethical Standards, which include requirements in the areas of ethics, independence, documenting the terms of the engagement, and quality control.

The procedures that we have performed do not constitute an assurance engagement in accordance with New Zealand Standards for Assurance Engagements, nor do they represent any form of audit under New Zealand Standards on Auditing, and consequently, no assurance conclusion or audit opinion has been provided.

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