



**RESERVE
BANK**
OF NEW ZEALAND



THE TREASURY
Kaitiaki Take Kōwhiri

The Open Bank Resolution (OBR) scheme – proposed communications strategy

Date	16 December 2010	Report number	4632
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Action Sought

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<p>Minister of Finance (Hon Bill English)</p> <p>Note that officials intend to proceed with a technical consultation on the implementation of OBR;</p> <p>Note that we suggest you do not proactively make any statements about OBR at this stage; but if you are approached talking points are provided for you in this report;</p> <p>Note that officials will provide you with a briefing ahead of any engagement with Australian Ministers; and</p> <p>Note that more extensive communications will be required following any decision to proceed with stage 2 of the OBR implementation process.</p>	N/A

Contacts

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Minister of Finance's Office Actions

Provide a copy of this report to the Office's media team.

Introduction

1. The recent Cabinet paper on the OBR policy indicated that Reserve Bank and Treasury officials would jointly develop a public communications strategy to be followed during the implementation of the policy. This report sets out the proposed strategy, identifies the key communications milestones for your information and provides you with talking points to use if you are approached about the OBR policy.

Proposed strategy

2. It was beneficial to consider the merits of the proposals on deposit insurance and resolution strategies as a package. But, we consider that there is a good case for maintaining a degree of separation between the two issues from a communications perspective. We would suggest that any statement that you make reiterating the Retail Deposit Guarantee Scheme (DGS) extension will end on 31 December 2011 and no permanent arrangement, such as Deposit Insurance, will follow does not explicitly refer to the on-going process to implement the Reserve Bank's OBR policy. This is primarily due to the communication complexity surrounding the impact on depositors (under the previous Crown guarantee versus OBR) and taxpayers.
3. We do not consider that the timing of the deposit insurance statement will have a significant bearing on the OBR implementation timetable. However, it would be helpful if the Minister could inform officials once any decision has been taken on the likely timing of any statement, so that the OBR consultation process can be phased appropriately. Officials will be available to provide any support required by the Minister in developing the content of that announcement. An announcement confirming the DGS extension will end on 31 December 2011 and no permanent arrangement will follow could be made early in new year in order to provide market participants with certainty about future arrangements well in advance of the expiry of the scheme. If you consider it helpful to do so, you may wish to refer, in a general sense, to on-going policy work with regards to strengthening the financial system's resilience to future crises.
4. In establishing the appropriate level of communication on the OBR, we have had regard to two key factors. First, the OBR is a long standing policy of the Reserve Bank, and does not therefore represent a new development. Second, the nature of the forthcoming work is a technical exercise designed to identify the appropriate approach for moving to full implementation of the policy, and the associated costs. No final decisions are being taken on implementation at this stage. On the basis of these points, we do not consider that it is appropriate to adopt a high-profile communications strategy at this stage of the process. We do not expect any significant market or credit rating reaction to the consultation given that OBR is a long-standing policy, many other countries are developing similar resolution mechanisms, and even if OBR was fully pre-positioned for it would still just represent one tool in the government's toolkit for responding to bank distress, and not necessarily the preferred or default option.

5. Under this strategy, the Reserve Bank will conduct an open and transparent consultation process with the banks to identify the appropriate approach to pre-positioning. This will involve the usual publication processes for consultation documents: for example, publication of the document on the Reserve Bank's website and responding to any queries that may arise. We do not propose that formal statements are provided by the government at this time. If you are approached about the OBR policy this report provides you with some suggested high-level talking points to use.
6. The next section sets out briefly the proposed approach to the consultation and identifies how this will lead to full implementation and the anticipated timetable. This is followed by a summary of the key communications milestones as the implementation proceeds.

Approach to consultation and implementation

7. The objective of the next stage of the implementation process is to identify the appropriate approach for pre-positioning to ensure that all banks are capable of carrying out an OBR within the timescales required. As all banks have bespoke operating systems, the Reserve Bank intends to define the desired outcomes of the pre-positioning, with individual institutions tasked with identifying the most efficient solution given their existing systems. In this regard, the Reserve Bank intends to take a flexible, outcomes-focused approach.
8. These outcomes will relate to the bank's capacity to:
 - determine creditor positions at the time of statutory management;
 - freeze part of each transaction account balance;
 - provide access to the unfrozen balance through the payments system on the next business day; and
 - periodically release frozen funds to transaction accounts.
9. Given the technical nature of this exercise, the Reserve Bank intends to allow a relatively long consultation period of up to 6 months.
10. Upon completion of this exercise, each bank should have identified a means of ensuring its operating system is pre-positioned to carry out an OBR should the need arise. In the interest of minimising implementation costs, the Reserve Bank also intends to ask banks to identify the most efficient timing for making the necessary system upgrades. It is intended that this process will be flexible to align with each institutions existing proposed system upgrade cycle. As a result, the full implementation for all banks may take a number of years.

Key milestones

11. As outlined above, we advise that the decision on deposit insurance is announced separately from any statements regarding the implementation of the OBR process. The remainder of this section sets out the key milestones in the OBR process, and identifies the anticipated timings.

- Initial RBNZ engagement with banks: The Governor and Deputy Governor met with the Chief Executives of major New Zealand banks during the week commencing 6 December 2010. The intention to consult on the implementation of OBR was highlighted during these discussions. One bank raised a concern regarding the practical challenges involved in pre-positioning for OBR, however, other banks expressed a willingness to work cooperatively towards the implementation, and there were no significant objections regarding the principle of the policy.
- RBNZ consultation with banks (stage 1): The Reserve Bank anticipates publishing the consultation document by the end of February 2011. This will be treated as a business-as-usual technical consultation on an existing Reserve Bank policy. As a result, whilst the consultation will be conducted in public, with the document placed on the Bank's website, the Bank will not be actively seeking to promote the consultation in the media.
- Trans-Tasman engagement: [Withheld under s6(b)(i)]

The Deputy Governor of the Reserve Bank has recently held discussions with the Chairman of APRA, in which he provided an update on our proposed approach to consultation.

- Cabinet paper and possible Ministerial statement: During the stage 1 consultation process, officials will be undertaking the supporting work identified in the November 2010 Cabinet paper. This includes reviews of the legal framework, further analysis on possible market implications and the design and implementation of associated government guarantees. The conclusions of this work, and the assessment of the costs identified during the stage 1 consultation, will be presented in a second Cabinet paper in the second half of 2011.

At this time, we consider that there may be merit in a Ministerial statement outlining the government's role in exercising the policy and its support for appropriate resolution mechanisms is likely to be beneficial. The statement could be broad and focus on the desirability of resolution mechanisms that do not need recourse to the taxpayer, or be more specific to OBR. The precise timing and content of this statement will be considered further at the time, having regard to wider government objectives and sensitivities.

- RBNZ engagement with banks (stage 2): The Reserve Bank will then undertake a bi-lateral process with each bank covered by the scheme to ensure full implementation of the necessary pre-positioning. This will include all necessary testing.
- Additional public statements: Once the decision has been taken to proceed with stage 2 of the implementation process, we consider that there may be a case for adopting a

more active communications strategy to ensure that there is a wider understanding of the policy. This may include speeches by senior officials and/or the publication of more technical articles (e.g. through the Reserve Bank *bulletin*).

Talking points

12. We suggest that you do not proactively make any statement about the OBR policy at this stage. If you are approached about the OBR policy, you may like to use the following talking points:

- You are aware the Reserve Bank is undertaking a technical consultation with banks about OBR.
- Our banks have weathered the global financial crisis well. However, a lesson from the crisis is that governments do need to have resolution mechanisms for banks that can keep them running, if need be, but in a way that does not unduly burden the taxpayer.
- Other countries are also looking at developing better resolution mechanisms for banks, and international organisations, such as the Financial Stability Board, are recommending countries explore mechanisms such as the OBR.

Recommendations

13. It is recommended that you:

- **Note** that officials intend to proceed with a technical consultation on the implementation of OBR;
- **Note** that we suggest you do not proactively make any statements about OBR at this stage; but if you are approached talking points are provided for you in this report;
- **Note** that officials will provide you with a briefing ahead of any engagement with Australian Ministers; and
- **Note** that more extensive communications will be required following any decision to proceed with stage 2 of the OBR implementation process.



Toby Fiennes
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Please sign the enclosed original and contact Alison McKessar at the Reserve Bank on 417 3607 to arrange collection.

Noted:

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Hon Bill English
Minister of Finance