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TECHNICAL NOTE

CONTINGENCY PLANNING AND CRISIS MANAGEMENT
FRAMEWORK

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Department**

This Technical Note was prepared by Michael Andrews (External Expert) in the context of the Financial Sector Assessment Program in New Zealand. It contains technical analysis and detailed information underpinning the FSAP's findings and recommendations. Further information on the FSAP can be found at

<http://www.imf.org/external/np/fsap/fssa.aspx>

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Glossary

AMI	Allied Mutual Insurance
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
AUD	Australian Dollars
CIMA	Corporations Investigation and Management Act
CoFR	Council of Financial Regulators
ESAS	Exchange Settlement Account System
FMA	Financial Markets Authority
FMI	Financial Market Infrastructure
GMRA	Global Master Repurchase Agreement
IAIS	International Association of Insurance Supervisors
IPSA	Insurance (Prudential Supervision) Act 2010
MOC	Memorandum of Cooperation on Trans-Tasman Bank Distress Management
MOU	Memorandum of Understanding
MMOU	Multi-lateral Memorandum of Understanding
NBDT	Nonbank Deposit Taker
NBDT Act	Nonbank Deposit Takers Act 2013
NZD	New Zealand Dollar
OBR	Open Bank Resolution
OMO	Open Market Operation
ORRF	Overnight Reverse Repurchase Facility
PRESS	Proportionate Risk Evaluation Surveillance System
RBA	Reserve Bank of Australia
RBNZ	Reserve Bank of New Zealand
RMBS	Residential Mortgage Backed Securities
TAF	Term Auction Facility
TTBC	Trans-Tasman Banking Council

EXECUTIVE SUMMARY

Several unique considerations apply to contingency planning and crisis management arrangements in New Zealand. These include dependence on self-discipline, market discipline and low intensity prudential supervision. There is also strong interdependence with Australia given that the four systemically important New Zealand banks are all large enough to be of material concern to their Australian parents and home supervisor. Successive New Zealand governments have elected not to introduce deposit insurance, one of the usual elements of the financial safety net.

The Reserve Bank of New Zealand (RBNZ) is the prudential supervisor, lender of last resort, and has oversight responsibility for designated payment systems. The Financial Markets Authority (FMA) is the market conduct regulator, and together with the RBNZ oversees securities settlement systems. The Treasury is the lead advisor to the government on economic, financial, and regulatory management. These three agencies, together with the Ministry of Business, Innovation and Employment (portfolio responsibility for the FMA) comprise the Council of Financial Regulators (CoFR).

The CoFR is an advisory and coordinating body. There are no standing arrangements for crisis management, but as the experience in dealing with the failure of a large insurer after the Canterbury earthquakes illustrates, incident-specific committees can be quickly formed. Work to date on financial sector crisis preparedness has focused on the large banks.

Greater clarity is required on the decision-making process for dealing with a crisis and the exercise of resolution powers. There are currently differences among key stakeholders in their interpretation of the legal framework and respective roles and responsibilities in resolution. The RBNZ should be the sole resolution authority, with clear mandates and accountabilities. In addition, the RBNZ should require an approval by the Minister of Finance only for resolutions with fiscal or systemic implications. The Treasury's lead role should focus on whether and how to provide a guarantee or public funds in support of a resolution recommended by the RBNZ, and provision of advice to the Minister in this respect.

Work has already begun to identify the necessary resources such as rosters of potential statutory managers, and personnel from government, agencies and the private sector, who could be mobilized to deal with a crisis. This work needs to be further developed. In parallel, the RBNZ should continue with documenting the procedures required for appointing a statutory manager, open bank resolution (OBR) and other resolution options. The Treasury should complete "shelf" agreements that may be required for provision of a Crown guarantee or other support in a crisis.

Trans-Tasman cooperation arrangements are well-established. The Memorandum of Cooperation on Management of trans-Tasman Bank Distress (MOC) should be expanded to include insurance and financial market infrastructures (FMIs). While there are work streams underway to address both areas, it would be preferable to broaden the existing crisis management agreement.

In the absence of support for deposit insurance, consideration should be given to establishing through legislative amendment a limited depositor preference to provide legal certainty for the *de minimis* deposit exemption from haircutting in OBR. A suitable *de minimis* amount could provide some of the benefits of deposit insurance, including mitigating against runs, and permitting purchase and assumption-type resolutions. It would also add to the credibility of OBR as an alternative to bailouts by mitigating potential pressure to protect depositors, as happened through the extension of the Crown Retail Deposit Guarantee Scheme to finance companies.

The RBNZ has well designed standing liquidity facilities. During the global financial crisis, the RBNZ revised conditions for standing facilities and introduced three new facilities. These remain in the RBNZ tool-kit and could be reintroduced on short notice if required.

The RBNZ has a wide range of remedial supervisory powers with respect to banks, insurance companies and nonbank deposit takers. However, for banks, the consent of the Minister of Finance is required for the issuance of directions. The RBNZ Act 1989 should be aligned with the Insurance (Prudential Supervision) Act 2010 (IPSA) and the Nonbank Deposit Takers Act 2013 by removing this role of the Minister in taking remedial supervisory action. The same principle should be reflected in the implementation of the oversight regime for FMIs.

Revision to the RBNZ Act to establish objectives for resolution should introduce requirements to consider the interests of depositors and the broader public interest. The RBNZ Act and IPSA should be revised to require post-reporting by the RBNZ on performance against resolution objectives to enhance accountability. The RBNZ Act should be revised to have the same power as in IPSA to apply for the appointment of a liquidator. A special resolution regime paralleling that in IPSA should be introduced for nonbank deposit takers.

The credibility of OBR would be enhanced by a legislative foundation for its key elements rather than relying on policy which is subject to change. Establishment of a depositor preference to an appropriate limit, and specific powers to bail-in (haircut) depositor and other creditor claims, would eliminate potential ambiguity around the requirement for a statutory manager to “have regard to” the priority of creditor claims.

A legal mechanism is required to temporarily exempt information that might impair effective resolution from the continuous disclosure requirements for listed companies. In addition, the RBNZ should pursue the possibility of including in the MOC specific provisions for the Australian authorities to ensure continued provision of services to the New Zealand subsidiary by the parent bank or other group member.

Table 1. New Zealand: Main Recommendations

Recommendation	Timing	Authorities
Strengthen domestic crisis management arrangements: <ul style="list-style-type: none"> • Reach ex ante agreement on roles, responsibilities and decision-making processes. • Preposition logistics and communications plans. • Complete initial work on plans to mobilize resources in a crisis. • Complete procedural guidance for appointment of a statutory manager, implementation of OBR and other resolution tool-kit options. • Test domestic preparations in simulation exercises. 	MT	CoFR
Revise the trans-Tasman MOC to specifically include insurance and FMIs.	MT	CoFR
Reconsider the merits of deposit insurance, or in the continued absence of policy support, introduce a limited depositor preference to provide legal certainty for the <i>de minimis</i> exemption contemplated in OBR.	MT	Treasury/RBNZ
Revise the RBNZ Act in line with IPSA and the NBDT Act to remove the role of the Minister in issuing directions.	MT	RBNZ/Treasury
Revise the RBNZ Act to provide greater clarity and certainty in resolution: <ul style="list-style-type: none"> • Insert objectives in resolution including protection of depositors and the public interest. • Require accountability reporting against the resolution objectives in both the RBNZ Act and IPSA, and NBDT Act when revised as recommended above. • Clarify that the RBNZ is the sole resolution authority. • Insert an express requirement for Ministerial consent for resolutions with fiscal or systemic implications only. • Clarify Treasury's role as a provider of advice to the Minister on the RBNZ recommendations regarding resolution. • Provide express bail-in powers to the statutory manager. 	MT	RBNZ/Treasury
Ex ante agreement on reporting requirements and decision-making procedures for OBR and other resolution options with fiscal or systemic implications.	MT	CoFR
Provide a legal foundation to exempt from continuous disclosure requirements information on resolution if such disclosure would be harmful to effective resolution.	ST	CoFR