

The Treasury

Reserve Bank Act Review Phase 2 Second Consultation Information Release

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Phase 2 of the review of the Reserve Bank of New Zealand Act: CRISIS MANAGEMENT

IEAP presentation
14 December 2018



Presentation contents



What do we mean?



Key Attributes of Effective Resolution Regimes



New Zealand's legislative framework



Australia's regime



Singapore's regime



UK's regime

The Review's approach

What kind of crisis?



Operational



Internal business continuity / disaster recovery plans



Liquidity



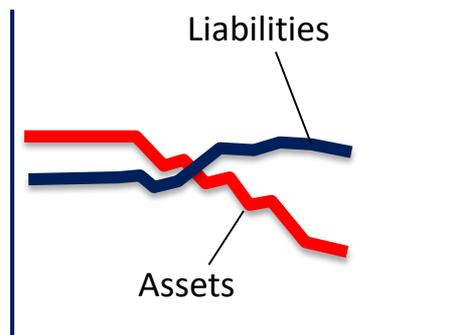
RBNZ Lender of Last Resort (LoLR)



Non-viability



Crisis management & resolution



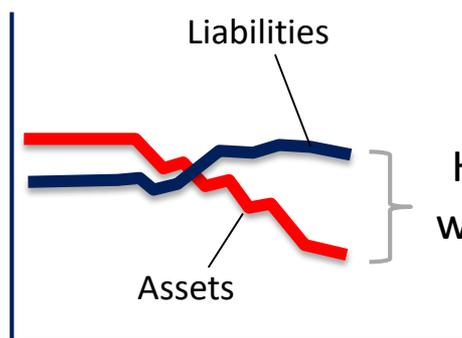
What do we mean by resolution?



“Resolution is the restructuring of a bank by a resolution authority through the use of resolution tools in order to safeguard public interests, including the continuity of the bank’s critical functions, financial stability and minimal costs to taxpayers.”



“Resolution is the process by which the Bank of England can step in to make sure that a bank that is failing does so in an orderly way.”



How to deal with the gap?

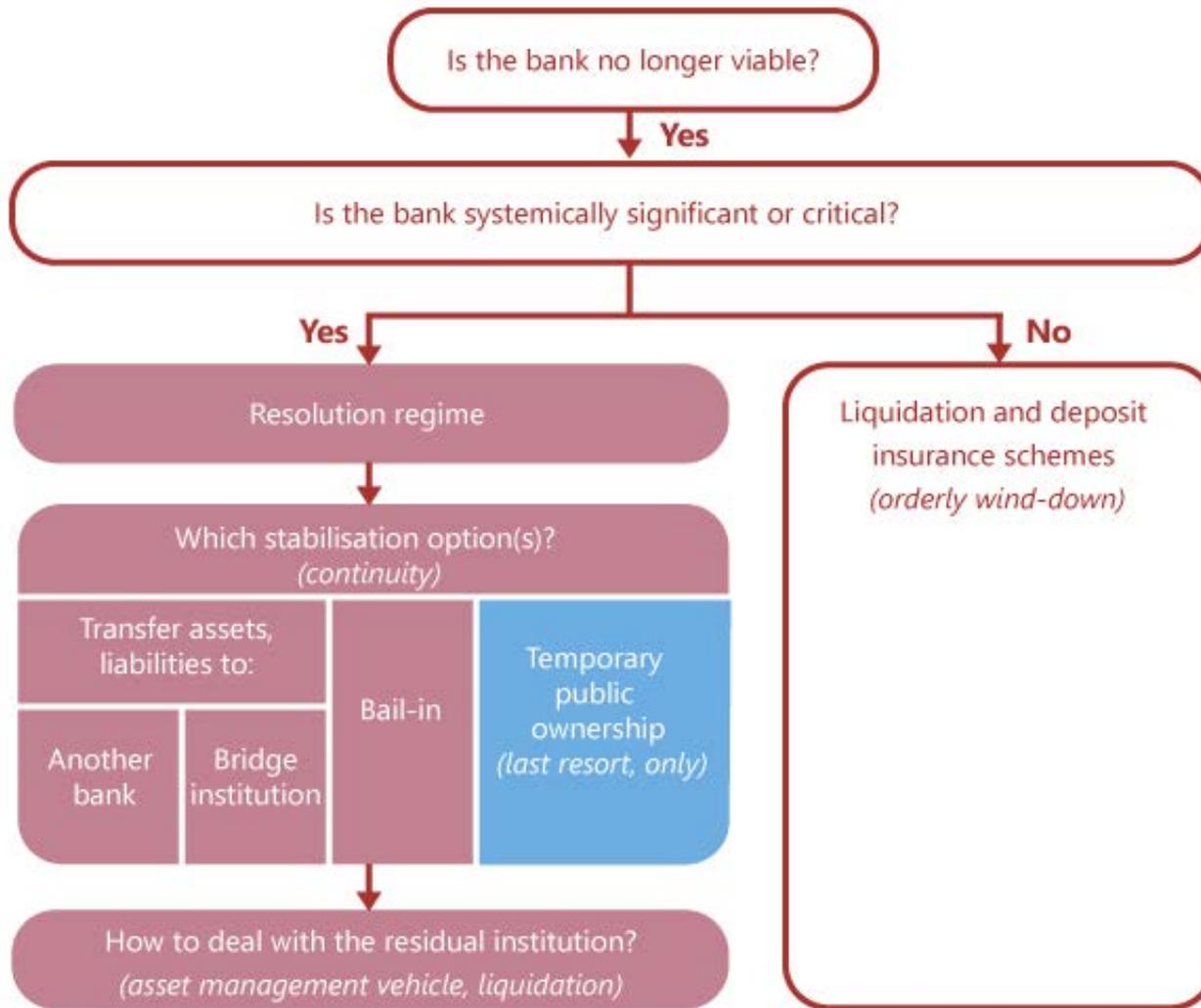
Bail-out (taxpayer-funded)

Bail-in (contractual/statutory write-off or conversion of debt)

Transfer/sale (+ liquidation?)

Liquidation

The FSB approach to resolution

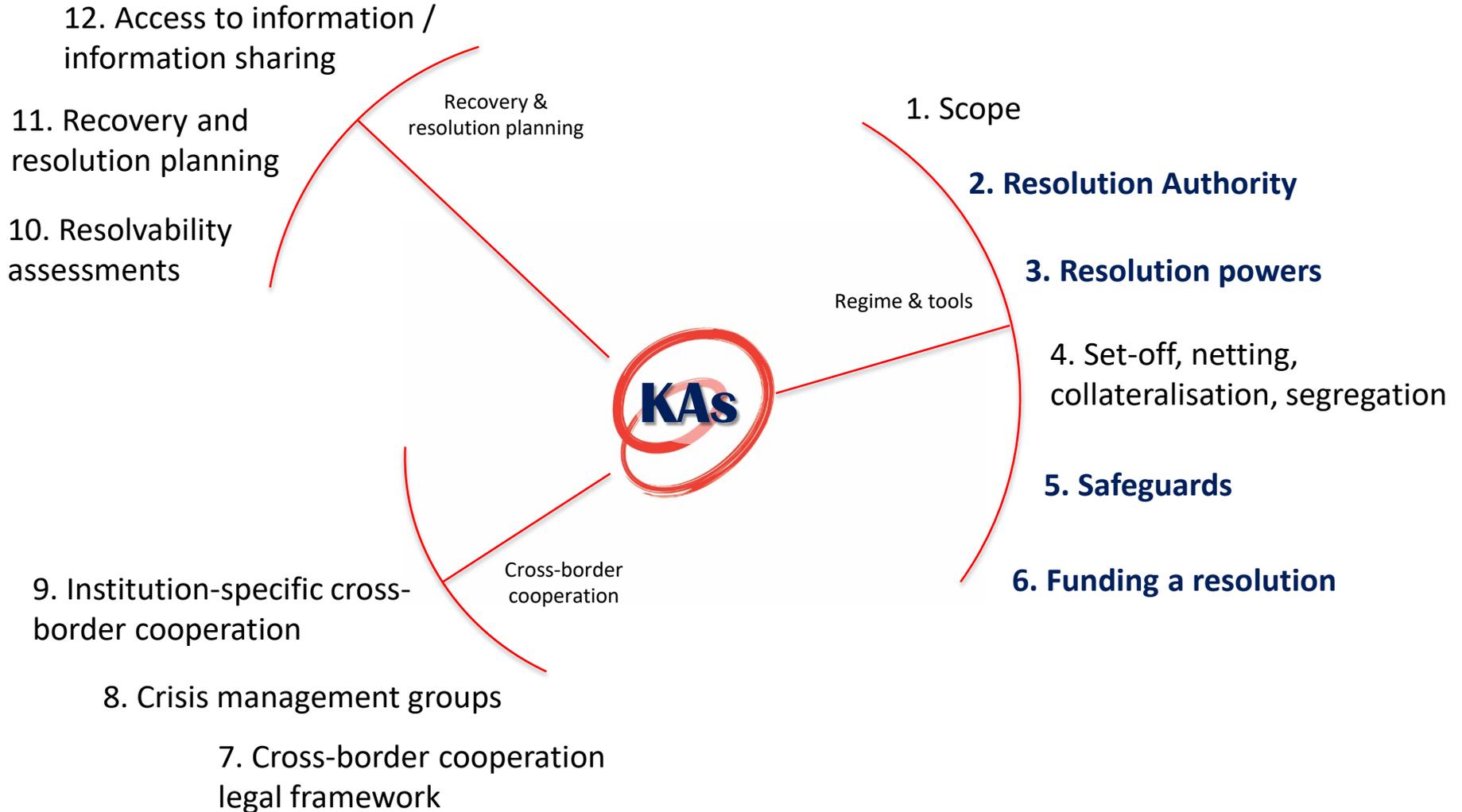


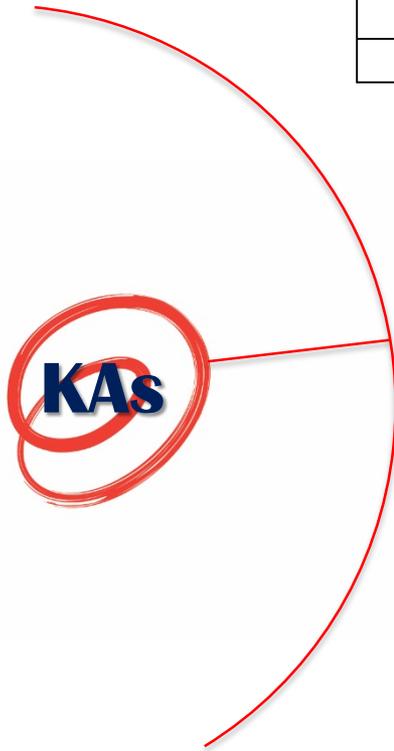
Financial Stability Board

- The G20's 2009 successor to the G7's 1999 Financial Stability Forum
- Membership: G20 + 5, International Financial Institutions, International Standard-setting Bodies
- A product of the GFC: taxpayer-funded bailouts of banks too big to fail
- Collective GFC lesson: no firm should be deemed 'too big to fail' and taxpayers should not bear the costs of resolution in the future
- International standard-setters and national authorities (including finance ministries, central banks, and regulators) took steps to reduce the probability and impact of the failure of systemically important firms.

Key Attributes of Effective Resolution Regimes (2011/2014)

- ★ Resolve financial institutions in an orderly manner...
- ★ without exposing taxpayers to losses from insolvency support...
- ★ while maintaining continuity of essential services
- November 2011: Endorsed by G20 as 'a new international standard for resolution regimes'
- Referenced by the IMF in its FSAP assessments
- Ongoing implementation monitoring and reviews





2. Resolution Authority

- A clearly designated authority with clearly defined mandate, roles, responsibilities
- Statutory objectives & functions
- Transparency, accountability, & rigorous evaluation of effectiveness of resolution measures

3. Resolution powers

- Clear non-viability triggers
- Ability to remove replace managers / directors
- Ability to appoint an administrator
- Ability to contract, purchase, sell, restructure
- Bail-in powers

5. Safeguards

- Respect for creditor hierarchy
- Flexibility to depart from *pari passu*...
- But no creditor worse off than in liquidation
- Legal safeguards

6. Funding a resolution

- There should be options other than bail-out
- Temporary use of public funds should be recoverable
- Should have deposit insurance or ex-post funds recoverable from industry



NZ's Legislative Framework

- Graduated set of interventions
- Close monitoring, recovery planning, & early intervention are critical
- Resolution: the ambulance at the bottom of the cliff



RBNZ directions:

- To consult with the RBNZ
- To continue/cease any business
- To exclude specific persons from management
- To remove/replace any directors
- To remove/replace/appoint any auditor
- To take any specified action

Remove, replace, appoint any directors

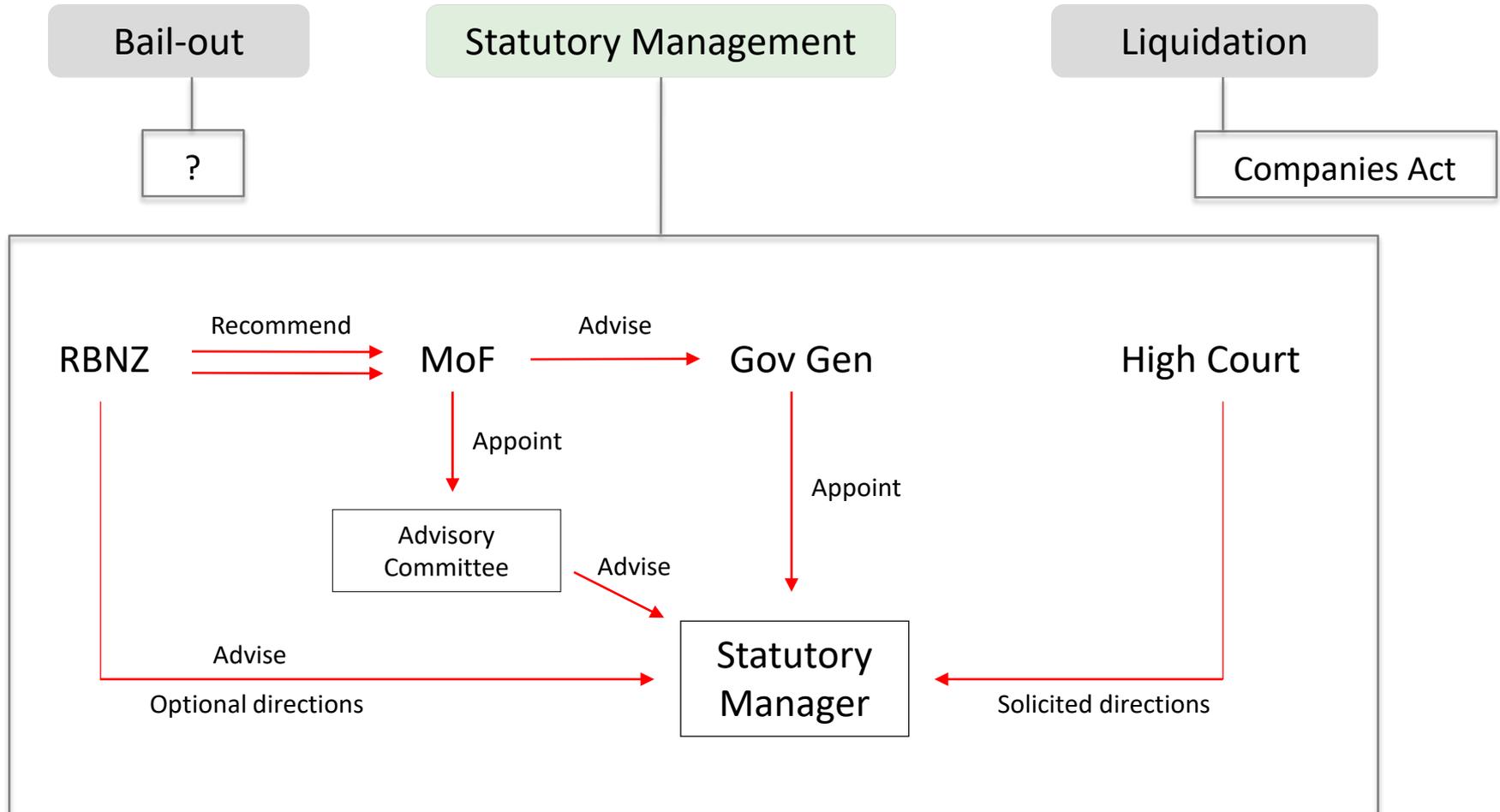
RBNZ powers

Subject to MoF consent



NZ's Legislative Framework

Failure Management





NZ's Legislative Framework

Statutory Management

'Have regard to' considerations

- (a) Maintaining public confidence in operation & soundness of financial system
- (b) Avoiding significant damage to the financial system
- subordinate to (a) and (b):
- (c) Resolving problems asap
- subordinate to (a), (b), and (c):
- (d) Preserving the position of creditors / ranking of claims
- (e) Advice of the RBNZ

Powers

- Automatic moratorium on claims / liquidation / voluntary administration
- SM can waive any aspect of the moratorium
- Powers of management, board, shareholders (AGM)
- Set up new company to acquire a branch of a foreign bank
- Agree a compromise with any creditor
- Sell/transfer any part of a bank (subject to consent requirements)
- Apply for liquidation



NZ's Legislative Framework

What the IMF said (2017 FSAP)

Observations

- **Short-comings** vis-a-vis the FSB *Key Attributes*
- NZ has been a pioneer in addressing too-big-to-fail with bank creditor recapitalisation. What evolved into OBR is conceptually elegant, but **practical and legal issues** need to be addressed
- No **standing arrangements** for crisis coordination and management among agencies
- No **resolution planning** for smaller banks, insurers, or NBDTs
- No **tailored** crisis management regime for **NBDTs**
- Merits of **deposit insurance** should be reconsidered
- Questions the **role of the Minister** in early intervention
- Legislative framework **shortcomings** plus **lack of consensus** on key issues (incl. decision-making, roles, and responsibilities)
- Act is **ambiguous** regarding the exercise of resolution powers
- No specific **objectives** for the use of statutory management
- No **safeguards** to creditors respecting the hierarchy of claims



NZ's Legislative Framework

What the IMF said (2017 FSAP)

Recommendations

Provide greater clarity and certainty in resolution:

- Remove **role of the MoF** in early intervention
- Resolution **objectives** (incl. protection of depositors and the public interest)
- **Accountability** reporting against resolution objectives
- Clarify that the RBNZ is the **sole resolution authority**
- **Ministerial consent** for resolutions with fiscal or systemic implications only
- Clarify the **Treasury's role**
- Provide express **bail-in** powers



NZ's Legislative Framework

Where the framework could potentially be improved

Reducing the Minister's role in early intervention

Clarifying the RBNZ as the resolution authority

Clarifying resolution objectives, responsibilities, and accountabilities in legislation

Clarifying resolution objectives outside of legislation (if any)

Clarifying bail-in and bail-out powers other resolution mechanisms such as stays

Enabling resolution options outside liquidation that don't rely on taxpayer support

Clarifying the role of the Minister, the Reserve Bank, and other agencies when taxpayer funds are at risk

Providing legislative clarity on creditor safeguards



NZ's Framework: Trans-Tasman dimension

Statutory obligations

- RBNZ to support Australian authorities
- RBNZ to avoid any action likely to have a detrimental effect on Australia
- RBNZ to consult with Australian authorities
- Statutory manager to notify and obtain RBNZ consent before taking such action (if reasonably practical)

MoC on trans-Tasman bank distress management

- Non-binding
- Principles of cooperation guiding responses to a financially distressed trans-Tasman bank
- Anticipates **Multiple-Point-of-Entry** resolution.
- TTBC discussions have focused on **Single-Point-of Entry** resolution.

? How does the cross-border parent-sub relationship affect the design of resolution financing options?

FSB: 'Keeping the pressure up'

Growing consensus around strategy...

- Two-pronged focus: **reducing the probability** of failure and **reducing the impact** of failure
- All FSB jurisdictions have completed substantive reviews of their resolution regime since the GFC
- Increasing consensus around the potential value of pre-positioning: use of TLAC and resolution planning

...but progress on resolution is a journey

- Several jurisdictions have designed their regimes to fully implement the KA's (e.g. UK/EU, Canada, Hong Kong, the Netherlands, Switzerland). These have primarily been G-SIB home jurisdictions
- More variation in how differing stakeholder considerations are balanced beyond those jurisdictions, most notably:
 - Capital markets certainty and bail-in (e.g. Australia, Singapore)
 - Ministerial influence on resolution (e.g. Singapore)



The Australian regime

Institutional arrangements

- APRA acts as resolution authority, prudential supervisor
- Deposit insurance scheme (FCS) is a paybox administered by APRA
- RBA provides LOLR
- Powers are primarily found in industry legislation (e.g. Banking Act 1959)
- No explicit resolution objectives
- Minister of Finance involved where public funds are at risk

Core tools

- Initial focus on management driven solution: resolution plans assisted by use of directions
- APRA can require transfer of assets or liabilities to a private sector purchaser, bridge bank or asset management company
- APRA has the ability to take control through 'statutory management' (unlike NZ this is not a Ministerial process)



The Australian regime

2018 reforms have enhanced APRA's toolkit

- Recently proposed increase in capital via TLAC, with APRA having ability to convert or write-down instruments
- Broadening of stays, direction, transfer powers and statutory management

Despite reforms, Australia's resolution regime retain some elements that **diverge from international best practice**

- Australia have elected not to create a statutory 'bail-in' power – preference for contractual instruments given concern about broader impact on funding markets
- Market perception remains that the largest banks are subject to an implicit guarantee
- Resolution and FCS are both funded on an ex post basis. FSB/IMF scepticism about this approach





Singapore's regime

Institutional arrangements

- MAS operates as prudential regulator, resolution authority and LOLR
- Deposit insurance scheme (SDIC) is a paybox administered by MAS
- MAS is close to government – Deputy Prime Minister is Chair
- Powers are primarily found in a specific resolution section of the Monetary Authority of Singapore Act 1970

Core tools

- MAS has a very broad set of tools: transfer of business or shares to a private sector purchaser, bridge bank or asset management company, compulsory restructuring
- Statutory bail-in power. Doesn't include senior debt.
- MAS has the ability to take control, either directly or through a statutory manager
- Approval of 'Minister-in-Charge' of MAS is required to implement resolution. Minister of Finance also involved where public funds are at risk



Singapore's regime

2017 reforms have largely followed the FSB KA's

- Creation of a statutory bail-in mechanism
- Greater protection of creditors (NCWO) and stays on termination rights
- Enhanced resolution funding (resolution fund can provide loans and temporary support)

Singapore has invested strongly in its framework, but FSB have raised **concerns about the role of the Minister** in resolution

- Strong overall framework, with focus on safeguards
- IMF have recommended review of the role of the Minister, with a view to enhancing operational independence
- Exclusion of senior debt from bail-in diverges from KA's
- More clarity recommended around funding arrangements. These are being developed in regulations





The UK regime

- Regime is governed by Banking Act 2009 as amended to implement 2014 European Bank Recovery and Resolution Directive
- Closely aligns with FSB KAs
- Bank of England (BOE) is the resolution authority
- Regime aims to ensure financial institutions can be wound up in an orderly manner that protects financial stability (the **statutory objective** of the BOE) and best meets the public interest (the **resolution objectives** of the BOE) – reflects the KAs
- BOE implements the resolution regime and has operational responsibility over resolution actions, in close consultation with all of the UK's Financial Authorities (PRA, FCA, and HMT).
 - BOE has operational responsibility for resolution
 - HMT has responsibility for decisions relating to the use of public funds
 - Resolution regime seeks to avoid the use of public funds



The UK regime

- Resolution toolkit is broad, supporting case-by-case flexibility:
 - Modified insolvency and administration procedures for smaller firms
 - Stabilisation powers for larger firms where insolvency isn't appropriate:
 - Transfer of business to a private sector purchaser
 - Transfer of business to a temporary bridge bank (owned by BOE)
 - Bail-in
 - Temporary public ownership (HMT tool) ONLY where shown to be strictly necessary to protect financial stability
 - BOE has strong powers to require firms to address and remove barriers to resolvability in BAU
- Chosen resolution action/s must advance the **resolution objectives**

The Review's approach

Overarching questions

1. What would an effective, credible, and feasible crisis management and resolution regime for New Zealand look like?
2. How does the existing legislative framework and policy approach measure up?
3. Where would the existing legislation need reform?
4. What's the impact of the trans-Tasman dimension?

The Review's approach

Specific topic areas

- Resolution authority designation
- Resolution objectives
- Roles and responsibilities (Resolution Authority, Minister of Finance, Treasury, other agencies)
- Resolution tools and powers
- Crisis management governance and decision-making
- Transparency and accountability
- Recovery, early intervention, and resolution planning powers
- Creditor safeguards
- Continuous disclosure intervention
- The trans-Tasman dimension

The Review's approach

Key considerations

- Objectives of effective crisis management and resolution
- New Zealand's current legislative framework and New Zealand-specific considerations
- International best practice
- IMF FSAP recommendations, and
- The approach taken in other jurisdictions and lessons learned