Introducing deposit insurance and a new regulatory system for deposit takers

We're seeking your views on the design of the deposit insurance scheme and the regulatory system for deposit takers. Our proposals should promote financial stability and improve the safety of deposits, but may also impact the range of products on offer and their level of financial returns.

What's happening?

Deposit takers, such as banks, credit unions and building societies play a crucial role in our economy and our everyday lives. They enable us to save and invest money, borrow to buy houses and start businesses, and pay for goods and services.

When a deposit taker fails, it can create problems that affect the whole economy. To reduce the likelihood of this happening, the Reserve Bank sets and monitors rules designed to promote the safety of deposit takers (prudential regulation and supervision).

We are reviewing the framework for these regulations to make sure that New Zealand has a stable financial system that supports a productive, inclusive and sustainable economy. Following earlier rounds of public consultation, the government has decided to:

- create a single, flexible regulatory regime for banks and other deposit takers
- strengthen the tools and powers available to the Reserve Bank if a deposit taker fails
- introduce deposit insurance that will protect the first $50,000 of deposits held at a single entity, and
- introduce new duties that hold directors of deposit takers to account.

We are now seeking your views on our next set of proposals

Which products should be covered by deposit insurance?

New Zealand's deposit insurance scheme will give certain and prompt access to up to $50,000 of insured deposits if a deposit taker such as a bank fails.

We're seeking your feedback on which products should be covered by this insurance scheme. As shown below, we're proposing that insurance covers basic deposit products that are widely used by everyday depositors.

Deposit insurance will need to be paid for, and this might result in lower returns on products that are eligible for deposit insurance. If any higher risk products were to be covered, these products would likely see a larger reduction in their financial returns.

Covered (Proposed)

- Transactional accounts
- Savings accounts
- Term deposits

Not Covered (Proposed)

- Bonds and debentures
- Managed investments
- Kiwisavers funds

How should finance companies be regulated?

Only licensed deposit takers would be able to offer insured deposits. They would be subject to appropriate levels of regulation and supervision by the Reserve Bank, helping to manage any increase in risk taking resulting from the introduction of deposit insurance.

We're considering whether there should be different rules for lenders such as finance companies that borrow from the public but that do not offer insured deposits. These businesses would still be subject to rules designed to promote their safety, but the rules would be less intensive than for businesses that offer insured deposits.

This approach would allow businesses such as finance companies to offer investments to the public with higher risks and returns than deposits, providing more investment options for New Zealanders. Investors would need to be clearly informed of these risks and these products would need to be clearly distinguished from insured deposits.

How should public awareness of the insurance scheme be promoted?

It is important that the public understands which financial products are subject to deposit insurance, and the maximum level of coverage. This will contribute to public confidence in the financial system, and lift awareness of the level of risk involved in different investments. We're seeking your views on options for promoting awareness, such as:

- enhancing disclosure requirements for uninsured products offered to retail investors
- preventing uninsured products from being marketed as "deposits"
- requiring deposit takers to proactively inform depositors about insurance coverage levels, and
- running a significant public awareness campaign before deposit insurance is introduced.

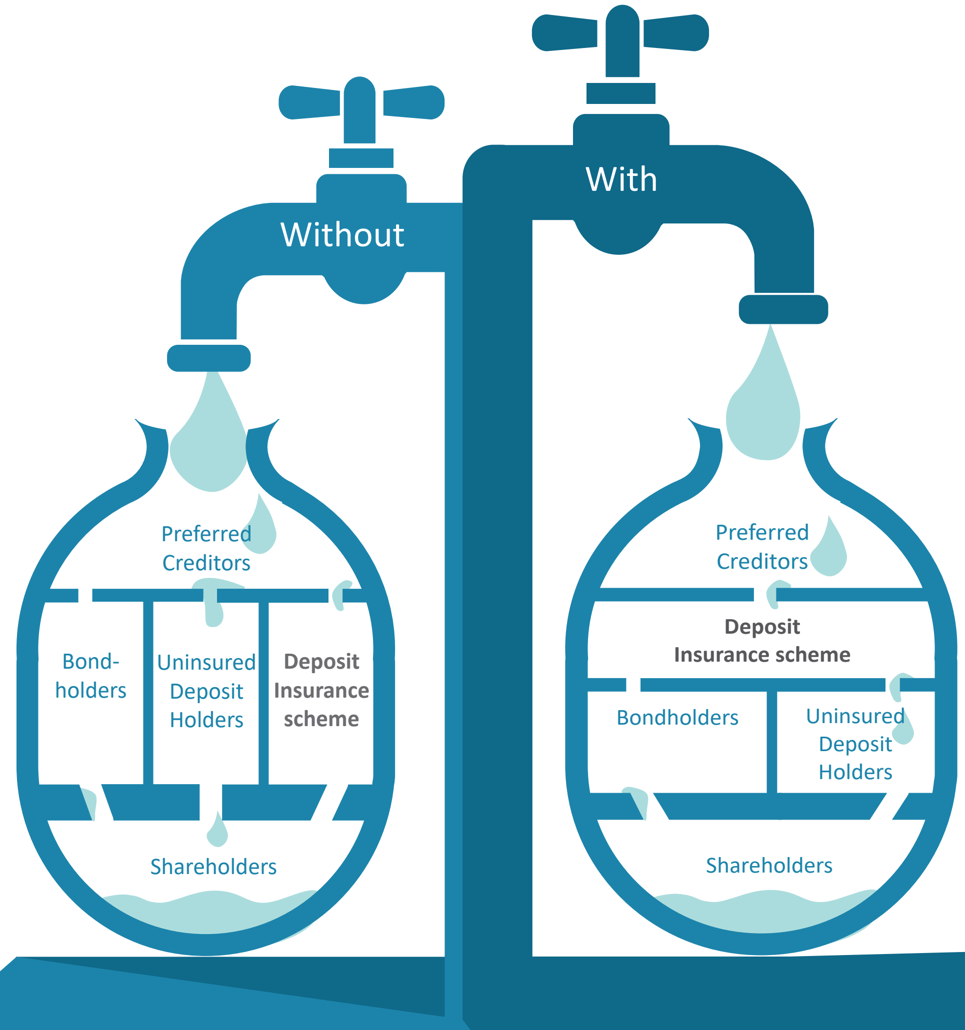
Who should bear losses first if a deposit taker fails?

The failure of a deposit taker would create financial losses that would need to be borne by someone. If losses exceed shareholder funding, losses would be borne by people who the deposit taker owes money (creditors). While the introduction of deposit insurance will mean that depositors will not face any losses on the first $50,000 of deposits, the deposit insurance scheme would bear these losses for them.

We're seeking your views on whether New Zealand should introduce a preference for insured deposits. This would mean that, if a deposit taker fails, other creditors such as uninsured depositors and institutional debt investors would bear losses before the deposit insurer (see figure to the right).

By reducing the likelihood that the insurance scheme suffers losses, a deposit preference would lower the cost to deposit takers of deposit insurance. These savings could be passed on to customers in the form of better returns on deposits. On the other hand, deposit preference would concentrate losses in a failure on depositors with over $50,000 and institutional investors, increasing the risk to these investors.

Diagram below illustrates the effect of depositor preference on how losses (represented by water) would be allocated in a failure.



We want to know what you think

Fill out this short survey to help inform the design of the regulatory framework and deposit insurance:
https://www.surveymonkey.com/r/68GC3Z8

The full consultation document covers a range of other proposals relating to the regulatory and supervisory framework for deposit takers.

For more information or to make a submission, go to treasury.govt.nz/rbnz-act-review or contact us directly at rbnzactreview@treasury.govt.nz

You can make a submission until 23 October 2020

RESERVE BANK OF NEW ZEALAND
TE PŪTEA MATUA

TE TAI ŌHANGA
THE TREASURY