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Reserve Bank Act Review - Deposit Takers Bill Information Release

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Office of the Minister of Finance

Chair,

Cabinet Economic Development Committee

Reserve Bank Act Review – Deposit Takers Bill: Crisis Management and Resolution (Paper 4 of 4)

Proposal

1 This paper is one of a suite of four papers on Phase 2 of the Review of the Reserve Bank of New Zealand Act 1989 (the Review). This paper presents proposals on the crisis management regime (for when licensed deposit takers become distressed or non-viable) for inclusion in a Deposit Takers Act (DTA). This paper should be read in conjunction with the Overview paper (Paper 1).

Executive Summary

2 Crisis management is a key part of the regulatory system's financial safety net, along with prudential regulation and supervision, a central bank's ability to supply liquidity to the system, and depositor protection. The proposed reforms to New Zealand's crisis management framework have been informed by the international experience and the subsequent post-global financial crisis (GFC) reforms. This approach has been well-supported in stakeholder feedback.

3 The Reserve Bank's 'power of direction' applies to both the Reserve Bank's normal supervision and enforcement function as well as its ability to intervene in a crisis management context. The proposed criteria for the use of these 'early intervention' powers focusses on non-compliance with prudential requirements and early indicators of financial distress. The proposed terms of the direction power are essentially the same as the existing power, but without the current requirement for ministerial consent and with some added clarification to help avert a deterioration in a distressed deposit taker's situation.

4 'Resolution' in the context of financial institutions is the use by authorities of powers to deal with a failing entity in an orderly manner, particularly to avoid the wider economic and social spillovers of a deposit taker failure or significant damage to the financial system itself, including by maintaining the continuity of critical financial services and preventing contagion. To be effective, a 'resolution authority' needs to have considerable powers. Access to those powers demands clarity on the conditions that must first be met.

5 In line with international guidance and emerging good practice, the criteria for placing a deposit taker into resolution will be clarified and focused on meeting a non-viability test as well as a necessity test, but in a way that enables the Reserve Bank to act in a timely manner and before a deposit taker is balance-sheet insolvent.

6 In December 2019, Cabinet agreed in principle [DEV-19-MIN-0346 refers] that, where practicable, powers that are currently available to a statutory manager would be available directly to the Reserve Bank as the resolution authority. These are significant powers, including the ability to take control of an entity in resolution, to suspend payments, and to set up a new entity and transfer parts of the business of the failed entity to that new entity or another entity. I am now seeking agreement that powers based on those in the existing act should be included in the DTA, after they are reviewed, adapted and appropriately modified under delegated authority.

7 Cabinet also agreed in principle to introduce the power to write down and convert to equity unsecured liabilities of an entity that is in resolution. This is known as statutory bail-in. Statutory bail-in is designed to help resolve large institutions by internalising losses in a manner that allows critical operations to continue and deposit accounts and other services to remain accessible without requiring taxpayer support. While the scope of bail-in is generally set broadly, insured depositors are often explicitly excluded (e.g. under the UK and European Union frameworks). However, those jurisdictions have adjusted their creditor hierarchy to provide a preferential status to insured deposits. I am not proposing to adopt such an approach here. The appropriate treatment of insured deposits within this framework is still under consideration, but they will be protected by deposit insurance in any case. The scope of statutory bail-in will also be extended to writing down share capital and cancelling shares.

8 The Reserve Bank will be able to require deposit takers to maintain minimum amounts of bail-inable instruments for the purposes of resolution planning. This approach also borrows from post-GFC international practice and will help to make bail-in an alternative to taxpayer bailouts of large institutions.

9 To support general awareness and openness of how a failed licensed deposit taker might be resolved, the Reserve Bank will be required to publish a ‘statement of approach to resolution’ setting out the expected resolution strategies for different types of deposit taker. The Minister of Finance will be consulted in the preparation of the Reserve Bank’s statement. This is in recognition of the Minister’s interest in the wider economic and social impact risks associated with deposit taker failure and the management of such failures, as well as managing any expectations that public funds will be put at risk in managing a deposit taker failure.

10 I am also proposing changes to the role of Minister of Finance in deposit taker resolutions. First, I am proposing to empower the Reserve Bank to act independently where it is able to resolve an entity by converting pre-positioned, subordinated wholesale instruments to recapitalise a distressed institution. However, I propose to maintain the existing requirement for the

Minister's agreement to be obtained before a deposit taker is put into a closed resolution, where broader powers will become available to the Reserve Bank.

11 The second change will be the ability for the Minister of Finance to direct the Reserve Bank on the management of risk to any public funds in a resolution. This direction power is intended as a residual ministerial lever only, in order to enable the Minister to manage risks to public funds and not used for day-to-day intervention in a resolution.

12 I am also taking the opportunity of this Review to address a long-standing gap in the government's financial crisis management framework by amending the Public Finance Act 1989 to authorise the Minister of Finance to approve expenditure in a financial crisis whether or not there is an appropriation in place. This authority will be similar to the existing authority to incur expenditure in a civil defence or health emergency. The authority will have several conditions attached to ensure that it does not raise expectations of taxpayer bailouts and would only be used as a last resort to maintain the stability of the financial system and the continuity of critical financial services when all other options were unlikely to succeed or not in the public interest.

13 Further work is continuing on a number of additional aspects of the crisis management framework, including a 'no creditor worse off' compensation mechanism. Delegated authority to make decisions for finalising drafting instructions for the DTA in these and related areas is being sought in Paper 1 (Overview).

Background

14 Crisis management is a key part of the regulatory system's financial safety net, along with prudential regulation and supervision, a central bank's ability to supply liquidity (i.e. lender of last resort), and depositor protection.

15 New Zealand's legislative framework for bank crisis management, being largely based on statutory management, has not been meaningfully reviewed since the late 1980s. Under this framework, the Reserve Bank developed the Open Bank Resolution (OBR) policy to manage the failure of a large bank. Since then, bank resolution regimes have been fundamentally overhauled internationally, particularly in the wake of the 2007-08 GFC. It is therefore timely to consider possible enhancements to New Zealand's framework.

16 In December 2019, the Cabinet Economic Development Committee made a number of in-principle decisions relating to the crisis management part of the Review [DEV-19-MIN-0346 refers]. These decisions included:

16.1 designating the Reserve Bank as the resolution authority for licensed deposit takers;

16.2 statutory objectives that the Reserve Bank must achieve in performing the resolution authority function;

16.3 where practicable, making available directly to the Reserve Bank existing powers that are currently available to a statutory manager;

16.4 introducing statutory bail-in powers for the Reserve Bank (i.e. the power to write down or convert to equity unsecured liabilities);

16.5 requiring resolutions to be conducted in a manner that respects the creditor hierarchy that would normally apply in a liquidation unless departure from the hierarchy is necessary to maintain the stability of the financial system; and

16.6 introducing an after-the-event compensation mechanism to compensate any creditors that a resolution leaves worse off than they would have been in a normal liquidation (the 'no creditor worse off', or NCWO, safeguard).

17 The proposals in this paper build on the above in-principle decisions. The proposals focus on 'early intervention' powers, statutory criteria for placing a licensed deposit taker 'into resolution' and exercising resolution powers, key resolution authority powers, further details on statutory bail-in, ministerial powers to manage fiscal risks, and amendments to the Public Finance Act 1989 to provide authority to incur expenditure without an appropriation in a financial crisis.

Direction powers and triggers for early intervention

18 The Reserve Bank currently has the power to direct registered banks in situations where certain statutory triggers have been met (essentially where the Reserve Bank has reasonable concerns about the soundness of the registered bank, its compliance with the regulatory regime, or broader risks to the financial system). This power can be used to effect corrective action, and to ensure compliance with prudential requirements. Cabinet has previously agreed in principle to remove the current requirement for there to be Ministerial consent to using direction powers. In addition, I am proposing further minor adjustments to these powers to make them fit coherently with the wider set of changes.

19 It is important that direction powers strike a balance between enabling the Reserve Bank to respond proactively in times of financial stress, but also ensuring that there is certainty for industry and protection from overreach. Having a clear set of statutory triggers and requiring that regulatory actions are in proportion to the risk or the harm will ensure that there are checks on the Reserve Bank's use of these powers.

20 I propose that the statutory triggers for direction powers be where the Reserve Bank has reasonable grounds to believe that:

20.1 there is a contravention, or a likely contravention, by a licensed entity of its prudential requirements or obligations (including, without limitation, if the licensed entity is insolvent or likely to become

insolvent, or is about to suspend payment or is unable to meet their obligations as they fall due); or

20.2 the business of the licensed entity is not being conducted in a "prudent manner"; or

20.3 the circumstances of the licensed entity are such as to be prejudicial to the soundness of the licensed entity or the financial system.

21 I propose that the terms of the directions will be whatever the Reserve Bank believes is necessary or desirable to remedy the situation that has given rise to the grounds for the direction ('the event'), avoid or mitigate the harm or potential harm arising out of the event, potential event, or risks to the ongoing viability of the entity. This would include any of the existing scope of directions, and new additional powers to give the Reserve Bank the ability to direct the entity to implement a recovery plan or issue additional shares.

22 I also propose that direction powers be available for use by the Reserve Bank in the context of associated persons. Although associated persons, as unlicensed entities, are out of the scope of prudential regulation, they can create wider risks and costs to society through their impact on licensed entities. Allowing the Reserve Bank to direct associated persons would enable it to manage these risks. The proposal is modelled on the test currently outlined in the Insurance (Prudential Supervision) Act 2010.

23 Entities subject to a direction will be able to seek judicial review, but not otherwise challenge the direction through the courts. Intentional non-compliance with a direction would be a criminal offence and potentially also carry a civil pecuniary penalty. Appeal rights are discussed in more detail in Paper 2, which covers the prudential framework for the DTA.

24 The Reserve Bank should also have a power to directly remove, replace or appoint directors of a licensed entity. This ability currently exists in the 1989 Act and I am proposing that it be included in the DTA.

Criteria for placing an entity into resolution and exercising resolution powers

25 I propose that there be a set of clear statutory triggers for placing a licensed entity into resolution that will enable the Reserve Bank to act proactively when licensed entities are in decline. These triggers should be based on the Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions (the 'FSB's Key Attributes') and should comprise a non-viability test and a necessity test. The non-viability test would be satisfied when one or more of the following applies to a licensed entity:

25.1 The value of the deposit taker's assets is or is likely to become less than the value of its liabilities;

25.2 The deposit taker is unable or likely to become unable to pay its debts as they fall due;

25.3 The deposit taker has persistently or seriously failed to comply with any direction, condition or other requirement that it must comply with to be a licensed deposit-taker;

25.4 The deposit taker is failing or has failed to maintain a minimum amount (or ratio) of capital as required under an applicable standard or licence condition.

26 The necessity test would be satisfied when there is no reasonable prospect (based on the Reserve Bank's opinion) of the non-viable deposit taker being remedied outside resolution to the satisfaction of the Reserve Bank.

27 Both the non-viability test and the necessity test would need to be satisfied for a resolution to be initiated.

28 Further work is being undertaken on a possible additional trigger for resolution to deal with the situation where an overseas authority has taken, or is taking, resolution action against the licensed deposit taker or a member of the licensed deposit taker's group. I propose that a decision on this will be taken under delegated authority.

Resolution authority objectives

29 In addition to the Reserve Bank's objectives in performing the resolution authority function that Cabinet agreed in principle in December 2019, I am proposing an additional resolution objective along the lines of 'protecting depositors to the extent they are covered by the deposit insurance scheme'.

30 This additional objective recognises that resolutions other than liquidation with a deposit insurance payout may offer preferable outcomes for depositors to the extent they are covered by the deposit insurance scheme. To ensure that the Reserve Bank is able to meet this objective, I am proposing that the DTA provide the Bank with a clear lever to access the funds of the deposit insurance scheme for the purposes of protecting insured depositors in resolutions (outside of liquidation and payout). This provision is discussed in Paper 3, and will be subject to safeguards that will be set out in legislation.

Empowering the Reserve Bank as the resolution authority

31 An effective resolution authority requires a full range of resolution options and supporting powers in the 'resolution toolkit' and flexibility in how it can use them. Some of these powers are significant and can involve overriding individual property rights in order to safeguard the public interest and financial stability. International good practice guidance is nevertheless clear that such powers are required, provided they are balanced by creditor safeguards, particularly the NCWO safeguard referred to above.

32 I propose that the existing process for placing a deposit taker 'under statutory management' and the appointment of a statutory manager be replaced with placing an entity 'into resolution' (provided the above statutory resolution criteria have been met).

33 Once an entity has been placed into resolution, the Reserve Bank as resolution authority would have access to the full range of resolution powers. These powers would include the ability to take full control of the entity in resolution or to appoint one or more 'resolution managers' to take control of the entity (as a statutory manager would under the 1989 Act). The resolution manager would be able to exercise resolution powers on behalf of the Reserve Bank and the Reserve Bank would be responsible for the resolution manager's performance. This approach aligns with international guidance. It also addresses industry's request that the existing model be overhauled to be more consistent with this guidance.

34 In December 2019, Cabinet agreed in principle that, where practicable, powers that are currently available to the statutory manager would be available directly to the Reserve Bank as the resolution authority. These are significant powers, including the ability to take control of an entity in resolution, to suspend payments, and to set up a new entity and transfer parts of the business of the failed entity to that new entity or another entity. I am seeking agreement that powers based on those in the existing act and other existing supporting provisions should be included in the DTA, after they are reviewed, adapted and appropriately modified under delegated authority. This includes a moratorium provision based on the existing act (but with further decisions still to be made around matters such as duration and process).

35 In addition, I propose that the powers available in respect of a deposit taker that is in resolution would also be available in respect of an 'associated person' that has been put into resolution. I also propose that the Reserve Bank be able to immediately place into resolution a new company that has been established to hold some of the business of a deposit taker that is in resolution.

Additional powers and supporting provisions

36 Resolution powers require clarity on the status of transactions that are in progress at the point of an entity being placed into resolution. Provisions that clarify the status of these transactions and the point in a transaction where it creates a debt will reduce uncertainty and make it easier to apply resolution powers appropriately. In addition, a temporary stay on early termination rights for certain financial contracts will be critical for an effective resolution regime. Further work is required on the design of these tools. I therefore propose that decisions on these topics are taken under delegated authority.

Statutory bail-in

37 The GFC demonstrated the need for resolution authorities to have tools to resolve failing banks quickly, without destabilising the financial system or exposing taxpayers to loss. The international bailouts of large institutions during the GFC were costly for governments and taxpayers.

38 The solution envisaged at the global level was to internalise losses through 'bail-in'. Bail-in is the main tool underpinning the FSB Key Attributes and reforms in many other jurisdictions. By credibly shifting the cost of a crisis

from taxpayers to investors and creditors, the new framework also aimed to reduce moral hazard and restore the level playing field for larger and smaller banks by eliminating the implicit subsidies enjoyed by the former.

39 The Reserve Bank's OBR policy relies on existing powers to set aside a portion of a failing entity's liabilities for loss-allocation in a subsequent liquidation once surviving parts of the firm are transferred to a new entity. The statutory bail-in power would give the Reserve Bank the ability to directly write down or convert certain types of unsecured liabilities into equity and to write down share capital and cancel shares. Alongside the implementation of deposit insurance (discussed in Paper 3), these new powers should help to further ensure that the costs of a crisis fall to investors and creditors rather than taxpayers.

40 As noted in the background section, Cabinet has already agreed in principle that the Reserve Bank should have the power to write down or convert to equity unsecured liabilities (statutory bail-in). This paper now turns to the liabilities that should be eligible for statutory bail-in in New Zealand and a number of other features of bail-in.

Liabilities eligible for statutory bail-in

41 Not all unsecured liabilities lend themselves to being bailed in. As such, recommendation 38 lists the proposed exclusions from the scope of statutory bail-in. International practice (particularly the UK and EU) has tended to also exclude insured deposits from the scope of statutory bail-in. However, this exclusion is generally accompanied by a preferential claim for insured depositors. I am not proposing that we adopt such a preferential claim in New Zealand.

42 Insured depositors will need to have confidence that they will get prompt access to their deposits in a resolution irrespective of how that resolution is conducted. In resolutions other than liquidations, this can either be achieved by exempting them from bail-in, or by making it clear that the deposit insurance fund will operate (under the Reserve Bank's direction) to ensure access to deposits that would otherwise have been bailed in. I will take further advice from officials and finalise how depositors are protected outside of liquidation and pay-out under delegated authority. This will involve decisions on the eligibility of insured deposits for bail-in and other matters (such as the rules relating to use of the deposit insurance fund and the operation of the NCWO provisions).

43 With respect to fixed-term debt, statutory bail-in would only apply to such instruments issued after the date that the DTA or any relevant regulations enter into force. Prospective application enables investors to assess and price the risk of bail-in into their decision-making at the time of making their investment. This approach was supported by the banking sector.

44 There are likely to be disclosure implications for bail-inable liabilities under the financial markets conduct regime. These implications will need to be worked

through with the Ministry of Business, Innovation and Employment and the Financial Markets Authority.

45 While the scope of bail-in is relatively broad, further operational refinement and pre-positioning that ties in with the Reserve Bank's resolution planning would be required to support an 'open resolution' (where the entity is resolved and remains fully open with full access to services in its existing form) because:

45.1 the availability of certain otherwise eligible liabilities (short-term debt and uninsured deposits) cannot be relied upon for planning purposes; and

45.2 some bail-inable liabilities will need to be subordinated to other liabilities that otherwise rank equally in the creditor hierarchy.

46 I propose that the Reserve Bank would have the power to direct deposit takers to maintain minimum amounts of certain bail-inable liabilities. The nature of those minimum liabilities would be defined in prudential standards, including requirements for them to be contractually subordinated to other liabilities.

Writing down share capital and cancelling shares

47 Cabinet's December 2019 decision on bail-in was phrased in terms of writing down or converting to equity unsecured liabilities. In a liquidation, equity and associated instruments would be the first to absorb losses. If, in the event of a resolution for which bail-in is to be used, there remained any shares with value, it would be important that those shares can be written down prior to bailing in eligible liabilities, to mirror the creditor hierarchy in liquidation. For the avoidance of doubt, it is therefore proposed that the bail-in power includes the power to write down share capital or to cancel shares.

The legislative instrument for defining the scope of bail-in

48 In December 2019 Cabinet also agreed in-principle that legislation would provide for the Governor-General, by Order in Council, to make regulations specifying types or categories of unsecured liabilities that would be excluded from bail-in [DEV-19-MIN-0346]. Following further work and consultation with the Legislation Design and Advisory Committee, I propose that the scope of bail-in be specified in primary legislation.

49 However, recognising that financial instruments can evolve over time, I propose that the DTA also provides the ability to make regulations that specify additional unsecured liabilities as ineligible for bail-in.

Contractual recognition of New Zealand bail-in powers

50 Bail-inable debt instruments will need to include contractual terms under which the holder of the instrument recognises and agrees that the instrument is subject to New Zealand law on bail-in (and the subordination of that instrument, as applicable) and agrees to be bound by the terms of a bail-in

under those statutory powers. This is in line with international good practice and to minimise the risk of legal challenge to a bail-in (e.g. in a foreign jurisdiction).

51 I propose that the specific wording for contractual recognition be set in standards so that the wording can be modified as required from time to time in line with international developments.

Potential tax implications of bail-in

52 A bail-in could lead to a significant amount of debt forgiveness income for the entity in resolution and therefore a potentially significant tax liability. While it is consistent with our tax system to recognise taxable income as arising in these circumstances, it is also important that a tax liability does not imperil the viability of a bail-in, particularly if a bail-in were considered necessary to maintain critical financial services and to protect financial stability.

53 Inland Revenue has acknowledged that recognition of any tax liability that could not immediately be offset through tax losses might undermine the effectiveness of a bail-in. However, any potential solution to this issue would need to balance the integrity of the tax system and the objectives of the bail-in and would likely require a targeted amendment of tax legislation.

54 I will be consulting the Minister for Revenue on whether any changes to tax legislation should be made to resolve this issue, and I am seeking delegated authority (in Paper 1 – Overview) for both Ministers to make decisions on this matter.

Minister of Finance roles and powers in a resolution

55 A Minister of Finance has key responsibilities on behalf of the government when a deposit taker fails. These include:

55.1 understanding and managing the economic and social impact risks associated with the failure and its management;

55.2 the wider international (especially trans-Tasman) relationship if the failure was one of New Zealand's foreign-owned banks;

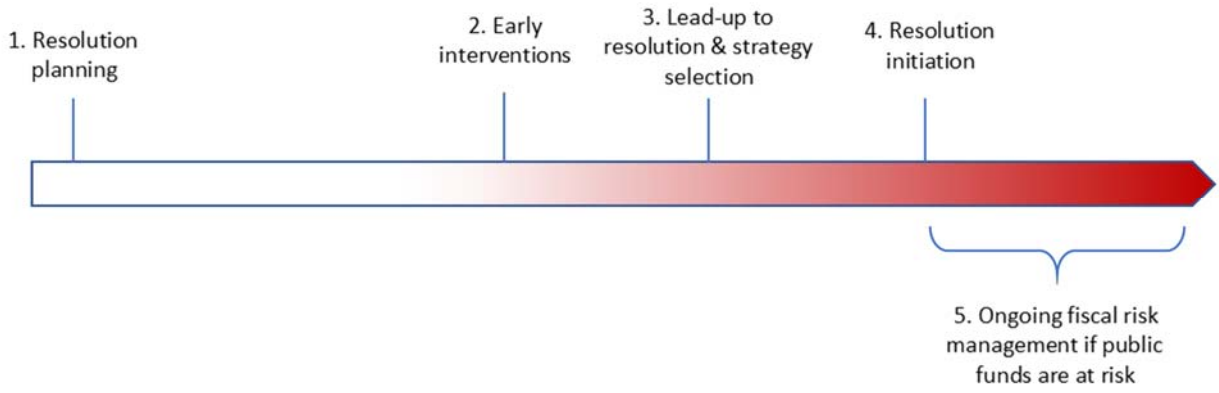
55.3 managing expectations that public funds will be put at risk to manage a deposit taker failure; and

55.4 managing fiscal risk to the government.

56 The crisis management framework needs to strike a balance between an appropriate level of operational independence of the Reserve Bank with appropriate opportunities and levers for the Minister of Finance to manage the government's interest in crisis management.

57 Figure 1 below shows five key points of ministerial interest in crisis management.

Figure 1: Key points of ministerial interest in crisis management



Planning and engagement prior to resolution

58 At point 1 – during normal times – the Reserve Bank will be required to develop resolution plans for deposit takers (advance planning being critical to smooth and orderly resolutions). Resolution plans should set expectations as to how a deposit taker would be resolved in the event of triggering the conditions for resolution.

59 I propose that, alongside the development of these resolution plans, the Reserve Bank will be required to consult the Minister of Finance in the preparation of a general 'statement of approach to resolution'. The statement of approach would be published and should include:

59.1 the expected resolution strategies for different types of deposit taker;

59.2 the approach to collaborating with other agencies (e.g. the Treasury) in resolution planning;

59.3 how the Reserve Bank will inform and engage with the Minister of Finance and other agencies on the use of crisis management and resolution powers (including the use of early intervention powers and on consultation prior to an entity being put into resolution – points 2 and 3 in Figure 1).

60 Consultation with the Minister of Finance on the statement of approach to resolution is intended to provide an opportunity for the Minister to ensure he or she is comfortable with the Reserve Bank's approach to resolution planning and preferred resolution strategies, especially on the costs and benefits of different resolution strategies and – importantly – to manage expectations of reliance on public funds.

Placing a deposit taker into resolution

61 Placing a deposit taker into resolution (point 4 in Figure 1) unlocks the ability of the Reserve Bank to exercise significant powers. Reasonable cases can

be made for the decision to be made by an independent regulator or, alternatively, by the Minister of Finance.

62 Appendix 1 sets out two approaches that the Review has considered. I propose the following approach:

62.1 An open resolution based on bailing in prepositioned, subordinated wholesale instruments or a suitable funding instrument from a parent entity (i.e. bail-in is limited to any minimum and subordinated bail-inable resources that have been required as part of resolution planning) would be able to be executed by the Reserve Bank without formal involvement of the Minister of Finance. Such resolutions aim for a rapid recapitalisation using the internal resources of the failed entity resulting in uninterrupted operations including continued access to accounts and critical financial services.

62.2 In all other cases, formal ministerial agreement would be required. These include resolutions where:

- losses are envisaged to be imposed on a broader set of creditors that are not prepositioned for it as part of minimum requirements supporting an open resolution;
- the deposit taker would be wound down after transferring deposits and matching assets to another entity; or
- the deposit taker may be closed and a deposit insurance payout made.

63 Further work is needed on the options for the 'legal instruments' that the DTA would require to give effect to resolution. I propose that a decision on the legal instruments be made under delegated authority.

Managing fiscal risk to public funds

64 Point 5 in Figure 1 refers to the management of fiscal risk to the government if a resolution were to put public funds at risk – e.g., through a government guarantee or an equity injection. Only the Minister of Finance, as authorised by Parliament, has the ability to commit or put at risk public funds in a resolution. An important question is whether the Minister should have statutory powers to direct the management of risk to any public funds that have been committed.

65 The Reserve Bank will have a resolution objective to protect public funds. Nevertheless, there is inherent uncertainty in crises. For this reason, the crisis management framework should provide sufficient levers for the Minister of Finance to demonstrate an ability to prudently manage fiscal risks facing the government in line with the principles of responsible fiscal management set out in the Public Finance Act 1989.

66 There may be some scope to include risk management clauses in the terms and conditions of an instrument that provides public funds, but the efficacy of

such clauses may not provide sufficient surety. A residual ministerial lever to manage fiscal risk may be necessary if, after a resolution's initiation, the Minister of Finance weights the need to protect public funds differently than the Reserve Bank does in balancing its multiple resolution objectives (of which protecting public funds is just one).

67 It is proposed that the DTA provides the Minister with the ability to direct the Reserve Bank on the management of risks to public funds in a resolution. In other words, the Minister would be able to direct the Reserve Bank to take an action in the course of a resolution provided that it is for the purpose of managing risks to public funds.

68 Providing the Reserve Bank's statutory objectives are clear and pitched towards the desired outcomes, then in the normal course of a resolution the Reserve Bank should be able to carry out its functions to meet those objectives and without political interference. Ministerial involvement risks blurring accountability for decisions that can have far-reaching impacts. The intention would be that the Minister's direction power is a residual lever only, to enable the Minister to manage risks to public funds if necessary. It should not be used for day-to-day intervention in a resolution.

69 Procedures for issuing a direction should be consistent for directions issued under other legislation such as the Crown Entities Act (e.g. tabling the direction in the House) subject to any commercial confidentiality requirements. The DTA will need to make appropriate provision for prioritising a direction over the Reserve Bank's other statutory resolution objectives if there were to be a conflict.

70 For the purposes of this direction power, 'risk to public funds' is proposed to cover the Crown's financial interest in making commitments such as government guarantees, loans, indemnities, share purchases and underwriting, and equity injections. It would exclude the Reserve Bank's use of its own funds or use of the deposit insurance scheme funds or the government fiscal backstop for the deposit insurance scheme (conditions for which would be governed under separate provisions).

Authority to incur expenditure without an appropriation in a financial crisis

71 The Review's terms of reference include consideration of the current limitations of the Public Finance Act 1989 with regard to the authority to use public funds in a timely manner in a financial crisis.

72 The use of public funds in resolving a failed financial institution carries significant risks, particularly in terms of moral hazard and raising expectations that the government will bail out failed financial institutions. Nevertheless, having the ability to deploy a public funds solution has a place in a comprehensive financial crisis management and resolution framework – as a last resort option in limited circumstances.

73 These circumstances would generally be when other options – including those developed in this Review – are not able to ensure an orderly resolution that

avoids damage to the wider financial system, whether it be by avoiding contagion or ensuring the continuation of financial services critical to the wider economy. These circumstances would generally not include bailing out a small deposit taker, where closure supported by deposit insurance should provide a credible alternative to government bailouts.

74 A potentially critical gap in New Zealand's current legislative framework is the ability of the government to use public funds in a financial crisis where:

74.1 funding needs to be provided quickly to protect financial system stability, avoid further damage to the financial system, and maintain critical financial services; and

74.2 the funds required exceed Imprest Supply or an existing available appropriation and there is no appropriation or timely prospect of obtaining an appropriation or additional Imprest Supply from Parliament.

75 This gap applies not just in relation to deposit takers, but also in relation to insurers and other critical parts of the financial system such as financial market infrastructure. The Review has considered how to address this gap in relation to all of these types of financial entities – as long as they are regulated by the Reserve Bank.

76 A key enabler for governments to respond to emergencies quickly and effectively is authority to incur expenditure to meet the needs of the emergency without an existing appropriation. Section 25 of the Public Finance Act 1989 provides for unappropriated expenditure when either a state of emergency is declared under the Civil Defence Emergency Management Act 2002 or a situation occurs that affects the public health or safety of New Zealand or any part of New Zealand that the government declares to be an emergency. Neither of these scenarios would typically support unappropriated expenditure in support of a failing financial institution.

77 Imprest Supply could be used to provide financial support to an entity, but it is not possible to know in advance the size of a financial failure or how much contingency will exist in Imprest Supply at the time it is needed. Imprest Supply cannot therefore be relied upon in a financial crisis, particularly if the failing entity were a large one or if multiple entities required support.

78 Parliament can be asked to pass specific spending authority through an Appropriation Act or additional Imprest Supply. However, a government cannot always rely on the availability of Parliament to do so in the time required. Resolution of a financial entity must be able to be executed in a timely manner and, at least initially, often out of the public eye; speed is usually of the essence if damage to the wider financial system and economy is to be avoided.

79 I propose inserting a new section in the Public Finance Act 1989 similar to existing section 25 but focussed on and tailored to the requirements of a

financial crisis (whether in banking or insurance, such as the post-Canterbury earthquake AMI Insurance crisis in 2011).

80 A standing authority to spend without an appropriation in a financial crisis should be available only in extraordinary circumstances. It is therefore important that the circumstances in which this power can be exercised are limited and are only where it is impracticable to use other options to resolve the situation.

81 Tight statutory conditions on the use of the authority can also help guard against the risk of creating an expectation of government bailouts. I therefore propose that a provision for the Minister of Finance to approve expenditure in a financial crisis without an appropriation should apply only to financial entities regulated by the Reserve Bank and can only be exercised where the following conditions are met:

81.1 The Reserve Bank has advised the Minister of Finance that the financial entity is insolvent or would soon be insolvent or otherwise considered to be failing financially.

81.2 The Minister is satisfied that the expenditure is:

81.2.1 necessary or desirable in the public interest; and

81.2.2 necessary or desirable to maintain the stability of the financial system and the continuity of critical financial services.

81.3 The Minister is satisfied that all other options consistent with the public interest to resolve the entity without using public funds had either been exhausted, were unlikely to succeed on their own, or were not in the public interest under the circumstances.

81.4 The Minister is satisfied that adequate arrangements will be in place to prudently manage fiscal risks to the government arising from the expenditure.

82 Making this amendment as part of the Review's other proposed crisis management reforms – particularly the introduction of the bail-in power and statutory requirements on the Reserve Bank to minimise the need to apply public funds to resolve a failed deposit taker – may help to further mitigate any adverse public perceptions of the proposed authority.

83 The proposed amendment would be intended to enable financial support packages to be approved only for deposit takers, insurers, and payments systems when financial stability was at risk or that provide financial services critical to the functioning of the wider economy, and only as a last resort.

Further work

84 Further work on the crisis management framework continues in a number of areas. The key areas of further work are listed in Appendix 2. I will be seeking (in Paper 1 – Overview) delegated authority to make further policy

decisions required to finalise drafting instructions for the DTA in these and related areas in consultation with the Associate Ministers of Finance and with the Ministers of Commerce and Consumer Affairs and of Revenue where matters affect their portfolios.

Next steps

85 Following Cabinet decisions on the recommendations in the package of papers of which this paper forms a part and any further decisions taken under delegated authority, the Reserve Bank will prepare drafting instructions for the Parliamentary Counsel Office (PCO). This will enable drafting of a bill and public consultation on an exposure draft, with introduction into the House anticipated late 2021.

Financial Implications

86 A number of recommendations in this paper will require an increase in the Reserve Bank's operational expenditure with respect to its duties as the resolution authority such as undertaking resolution planning. To some extent these costs have been anticipated in the 2020-25 Funding Agreement between me and the Governor of the Reserve Bank signed in June 2020. Further details are provided in Paper 1 (Overview).

Legislative Implications

87 The recommendations in this paper will be given effect by the Deposit Takers and Depositor Protection Bill, which has a category 4 priority on the 2021 Legislation Programme (to be referred to select committee in 2021). An amendment to the Public Finance Act 1989 will also be required. There could also be consequential amendments to other legislation as a result of decisions taken under delegated authority.

88 The Deposit Takers and Depositor Protection Act will bind the Crown.

Impact Analysis

89 See Cabinet Paper 1: Overview for the Quality Assurance Panel's (comprising representatives from the Reserve Bank of New Zealand, the Treasury and the Regulatory Impact Analysis Team at the Treasury) assessment of the attached Regulatory Impact Statement against the Quality Assurance criteria. The Panel considers that the Regulatory Impact Statement for the reforms in this Cabinet paper **meets** the Quality Assurance criteria.

Human Rights

90 My officials will be working with the Ministry of Justice to ensure that any concerns relating to the Bill of Rights Act are addressed.

Consultation

91 The following agencies were consulted on the contents of this paper: the Ministry of Business, Innovation and Employment, the Financial Markets

Authority, PCO, Inland Revenue, and the Ministry of Justice. The Department of Prime Minister and Cabinet has been informed.

92 Three rounds of public consultation have taken place as part of Phase 2 of the Review. The first round closed in January 2019 and received 67 submissions. A second round of consultation closed in August 2019 and received 45 submissions. The third consultation closed in October 2020 (following a six-month extension to the original deadline for submissions due to COVID-19). This consultation received 45 written submissions on the detailed design aspects of a new prudential regime for deposit takers and the introduction of deposit insurance.

Views of the Independent Expert Advisory Panel

93 The joint Treasury-Reserve Bank Review team has been supported throughout Phase 2 by an Independent Expert Advisory Panel (the Panel) chaired by Suzanne Snively. The Panel's views are provided in Paper 1.

Communications

94 I recommend that Cabinet decisions, the package of Cabinet papers and related material will be publicly released on the Treasury and Reserve Bank websites shortly after decisions are made.

95 In addition I plan to announce some of the key decisions shortly after the Cabinet meeting, and the timeframe for the implementation of deposit insurance.

Proactive Release

96 I intend to proactively release supporting material and advice (such as policy advice reports, Panel papers and presentations) relating to these recommendations.

Recommendations

The Minister of Finance recommends that the Committee:

1 agree to confirm Cabinet's previous in-principle decision [DEV-19-MIN-0346] that legislation will designate the Reserve Bank as the resolution authority for regulated deposit takers.

2 note Cabinet's previous in-principle decision [DEV-19-MIN-0346] that statutory functions for the Reserve Bank as resolution authority will include the following:

2.1 to prepare and maintain a plan to resolve deposit takers in the event of a possible failure;

2.2 to test the effectiveness of each plan at regular intervals;

2.3 to coordinate with other authorities, both in New Zealand and overseas, as necessary to be prepared for the possible failure of a deposit taker;

2.4 in the event of the failure of a deposit taker, to exercise the powers under the Deposit Takers Act consistently with the objectives under that Act.

3 agree that the Reserve Bank as resolution authority will have statutory duties that capture items 2.1 to 2.4 in the preceding recommendation.

4 agree that the Reserve Bank will have the following statutory objectives in performing the resolution function:

4.1 enable all deposit takers to be resolved in an orderly manner;

4.2 avoid significant damage to financial system in the event of the failure of a deposit taker, including by maintaining the continuity of systemically important financial functions and preventing contagion;

4.3 (along the lines of) protect depositors to the extent they are covered by the deposit insurance scheme;

4.4 to the extent not inconsistent with the objectives in recommendations 4.1 to 4.3 above:

4.4.1 minimise the cost of resolution and avoid unnecessary destruction of value and interference with property rights,

4.4.2 protect public funds, including by minimising the need to apply public funds to resolve the failure of a deposit taker.

5 note that the objective in recommendation 4.3 is additional to the objectives agreed in principle by Cabinet in December 2019 [DEV-19-MIN-0346], and will be finalised under delegated authority.

Direction powers and triggers for early intervention

6 agree that the Reserve Bank would have a power to direct a licensed deposit taker, the policy intent being that the power can be used where it has reasonable grounds to believe that:

6.1 there is a contravention, or a likely contravention, by a licensed deposit taker of its prudential requirements or obligations (including, without limitation, if the licensed entity is insolvent or likely to become insolvent, or is about to suspend payment or is unable to meet their obligations as they fall due); or

6.2 the business of the licensed deposit taker is not being conducted in a “prudent manner”; or

6.3 the circumstances of the licensed deposit taker are such as to be prejudicial to the soundness of the licensed deposit taker or the financial system.

7 agree that the terms of the direction would be whatever the Reserve Bank believes is necessary or desirable to remedy the situation that has given rise to the grounds for the direction (the 'event'), avoid or mitigate the harm or potential harm arising out of the event, potential event, or risks to the ongoing viability of the entity.

8 agree that the scope of the direction power would include all of the powers currently contained within section 113A of the current Reserve Bank Act as well as process requirements in section 113 of that Act, and the following additional new powers, to give the Reserve Bank the ability to direct a licensed deposit taker to:

8.1 implement its recovery plan or;

8.2 issue additional shares.

9 agree that non-compliance by any person (including the licensed deposit taker itself, directors and senior management) with a direction would be a criminal offence, and potentially subject to other penalties determined under delegated authority.

10 agree that the Reserve Bank should be able to issue directions to an associated person where it has reasonable grounds to believe that this is necessary or desirable in order to manage the difficulties faced by a licensed deposit taker, because the affairs of the associated person and the licensed deposit taker are so closely connected, or are impacting on the solvency of the licensed deposit taker.

11 agree that the full scope of direction powers should be available to the Reserve Bank in the context of associated persons, provided that the triggers for directions to that associated person set out in recommendation 10 have been met.

12 agree that the Reserve Bank should have the power to remove, replace, or appoint directors of a licensed entity, where any of the triggers for intervention set out in recommendation 6 are satisfied, and the Reserve Bank believes it is necessary or desirable to remove, replace or appoint directors of the entity.

13 agree that, consistent with Cabinet in principle decision to remove Ministerial consent [CAB-19-MIN-0675], Ministerial consent would no longer be required where the Reserve Bank removes, replaces or appoints directors of a licensed entity.

Triggers for placing a deposit taker into resolution and exercising resolution powers

14 agree that the criteria to place a licensed deposit taker into resolution require the Reserve Bank to be satisfied on reasonable grounds that both a non-viability test and a necessity test have been met.

15 agree that the policy intent is for non-viability to occur when one or more of the following applies to the licensed deposit taker:

15.1 the value of the deposit taker's assets is or is likely to become less than the value of its liabilities;

15.2 the deposit taker is unable or likely to become unable to pay its debts as they fall due;

15.3 the deposit taker has persistently or seriously failed to comply with any direction, condition or other requirement that it must comply with to be a licensed deposit-taker;

15.4 the deposit taker is failing or has failed to maintain a minimum amount (or ratio) of capital as required under an applicable standard or licence condition.

16 agree that the policy intent is for the necessity condition to be met when there is no reasonable prospect of the difficulties of the non-viable licensed deposit taker being remedied outside resolution to the satisfaction of the Reserve Bank.

17 note that further work is being done on a possible additional resolution trigger that deals with the situation where an overseas authority has taken, or is taking, resolution action against the licensed deposit taker or a member of the licensed deposit taker's group and that a decision on this trigger will be taken under delegated authority.

18 agree that the Reserve Bank may put an associated person into resolution and exercise resolution powers on that associated person.

19 note that the triggers for placing an associated person into resolution will be determined under delegated authority.

Empowering the Reserve Bank as resolution authority

20 note that Cabinet has agreed in principle that, where practicable, existing resolution powers currently available to a statutory manager be available directly to the Reserve Bank as resolution authority [DEV-19-MIN-0346].

21 agree that the DTA will include other significant powers and technical provisions for the resolution of licensed deposit takers based on the statutory management provisions in the Reserve Bank Act 1989 as reviewed, adapted and appropriately modified for the resolution of licensed deposit takers under delegated authority.

22 note the significant resolution powers referred to in the above recommendation include the Reserve Bank (or resolution manager appointed by the Reserve Bank) having the power to assume full powers of management of the deposit taker in resolution, sell or transfer all or part of the business of the deposit taker in resolution, and having the power to suspend payments of the deposit taker in resolution.

23 agree that the Reserve Bank will have the power to appoint directly one or more persons (acting jointly or individually) as resolution manager of an entity that is in resolution.

24 agree that the resolution manager may be a Reserve Bank official or another person determined by the Reserve Bank.

25 agree that the Reserve Bank would be responsible for the performance of the resolution manager and that person would be:

25.1 subject to oversight by the Reserve Bank;

25.2 subject to and required to comply with instructions and directions by the Reserve Bank;

25.3 accountable to the Reserve Bank; and

25.4 subject to removal and replacement by the Reserve Bank.

26 agree that a resolution manager will be able to take actions to give effect to any of the Reserve Bank powers in respect of a deposit taker in resolution, but only as the Reserve Bank's delegate and in accordance with direction by the Reserve Bank.

27 agree that powers currently vested in a statutory manager under section 127 of the Reserve Bank Act 1989 to suspend payments or to cancel an obligation to provide funding be carried over to the DTA and vested with the Reserve Bank directly in respect of an entity that is in resolution, and the existing exclusions from that power be updated to include payments and transfers to central counterparties and designated settlement systems.

28 agree that, subject to further work on technical supporting provisions, the power to transfer or sell assets, liabilities, legal rights, and obligations including deposit liabilities and ownership in shares (including the power of assignment and novation) of an entity in resolution be vested directly with the Reserve Bank.

29 agree that section 142 of the Reserve Bank Act 1989 dealing with applications by a statutory manager to the High Court for directions be carried over into the DTA in respect of a deposit taker that is in resolution, with necessary or desirable updates to reflect that the Reserve Bank will be the resolution authority.

30 agree that the Reserve Bank may incorporate a new entity to receive assets and liabilities of a failed deposit taker.

31 agree that a new entity referred to in recommendation 30 may itself be placed into resolution as part of the resolution of the failed deposit taker's affairs.

32 agree the powers available in respect of a deposit taker that is in resolution also be available in respect of an associated person that is in resolution.

33 agree that the DTA will include a moratorium based on section 122 of the Reserve Bank Act 1989, with further decisions on the nature of the moratorium (such as duration and process) to be made under delegated authority.

34 agree the DTA will clarify the legal status of payment instructions on a licensed deposit taker's entry into resolution, with further decisions on how to achieve this to be made under delegated authority.

35 note that a legal stay on early termination rights for certain financial contracts is considered internationally to be an essential element of a bank resolution regime but that further technical design work is required, and decisions will either be made under delegated authority or subject to a further report to Cabinet.

Statutory bail-in

36 agree to confirm Cabinet's previous in principle decision [DEV-19-MIN-0346] that the Reserve Bank have a statutory bail-in power to write down or convert to equity certain unsecured liabilities of an entity that is in resolution.

37 agree that the statutory bail-in power includes the power to write down share capital and to cancel shares.

38 agree that the following liabilities be excluded from the scope of statutory bail-in:

38.1 secured liabilities, including those related to covered bonds;

38.2 client assets held by a deposit taker in trust or in a custodial capacity;

38.3 liabilities owed to an employee or former employee of the deposit take arising out of the employment relationship;

38.4 tax liabilities owed by the deposit taker to Inland Revenue;

38.5 employer contributions to retirement savings schemes (e.g., KiwiSaver) owed by the deposit taker;

38.6 liabilities owed by the deposit taker to its creditors arising from the provision to the deposit taker of goods or services (other than financial services) that are critical to the deposit taker's operations;

38.7 liabilities owed by the deposit taker to the DTA deposit insurance scheme (e.g. unpaid levies);

38.8 liabilities owed by the deposit taker under derivatives (but this exclusion does not apply to unsecured net amounts owed by a deposit taker to a counterparty after the application of New Zealand's netting legislation);

38.9 other liabilities that are substantially similar in character to those listed in 38.1 to 38.8 above.

39 note that the above exclusions are expected to leave the following unsecured liabilities as eligible for statutory bail-in:

39.1 subordinated capital and debt instruments;

39.2 any structurally subordinated debt issued to a holding company or a parent;

39.3 other unsecured debt (such as wholesale debt and uninsured deposits) that is not excluded under recommendation 38 above.

40 note that further work on the eligibility of insured deposits for statutory bail-in is required and a decision will be made under delegated authority, noting that they will in any case be protected by the insurance scheme.

41 agree that eligibility of liabilities for statutory bail-in will be set out in the DTA and that the Governor-General may make Regulations by Order in Council on the advice of the Minister of Finance that specify additional unsecured liabilities as ineligible for statutory bail-in.

42 agree that eligibility of debt instruments for statutory bail-in would only apply to instruments issued or renewed (including through updated terms and conditions) from or after the date that the eligibility provisions of the DTA enters into force.

43 note that eligibility of deposit accounts for statutory bail-in would only apply once statutory bail-in is appropriately recognised in the terms and conditions for those accounts.

44 agree that the Reserve Bank will have a power to require licensed deposit takers to maintain minimum amounts of specified, subordinated bail-inable instruments for the purposes of resolution planning.

45 agree that the terms and conditions for liabilities that are to be included in minimum requirements of bail-inable liabilities will be set out by the Reserve Bank in prudential standards.

46 agree that requirements for contractual recognition of statutory bail-in and subordination requirements for bail-inable instruments will be set out by the Reserve Bank in prudential standards.

47 agree that consequential amendments to the Financial Markets Conduct Act 2013 and Regulations, including disclosure requirements, be developed (under delegated authority or subsequently) where required as a consequence of the introduction of statutory bail-in.

48 note that a targeted amendment of tax legislation may be required to address the timing of potential tax liabilities in the event that statutory bail-in powers were used.

Statement of approach to resolution

49 agree that the Reserve Bank be required to publish a statement of approach to resolution.

50 agree that the Reserve Bank's statement of approach to resolution be required to include matters along the following lines:

50.1 the expected resolution strategy or strategies for different types of licensed deposit taker;

50.2 the approach to collaborating with other agencies (e.g. the Treasury) in resolution planning;

50.3 how the Reserve Bank will engage with the Minister of Finance and other agencies on the use of early intervention powers (such as directions and removing/appointing directors) and resolution powers prior to an entity being put into resolution.

51 agree that the Reserve Bank be required to consult the Minister of Finance in preparing the statement of approach to resolution and have regard to the Minister of Finance's views before finalising the statement.

Placing a deposit taker into resolution

52 agree that the Reserve Bank be able to place a licensed deposit taker into resolution without authorisation from the Minister of Finance where:

52.1 the deposit taker is to be resolved in an open state; and

52.2 the use of statutory bail-in is limited to specified subordinated bail-inable instruments that have been prepositioned for statutory bail-in in line with requirements under prudential standards issued by the Reserve Bank.

53 agree that, in all other cases, authorisation from the Minister of Finance, on the recommendation of the Reserve Bank, will be required to place a deposit taker into resolution.

54 note that the legal instruments that the DTA would require to be transmitted at the point of placing a deposit taker into resolution will be determined under delegated authority.

Managing fiscal risk to public funds

55 agree that the Minister of Finance will have the ability to direct the Reserve Bank on the management of risks to public funds in a resolution.

56 agree that the Minister of Finance's direction power is intended as a residual lever only in order to enable the Minister to manage risks to public funds and not used for day-to-day intervention in a resolution.

57 agree that, for the purposes of the Minister of Finance's direction power, 'risk to public funds' covers the Crown's financial liabilities or commitments in respect of the entity in resolution (such as government guarantees, loans, indemnities, share purchases and underwriting, and equity injections) but excludes the Reserve Bank's use of its own funds or use of the deposit insurance scheme funds or the government fiscal backstop for the deposit insurance scheme (the use of which would be governed under separate provisions).

58 agree that the Minister of Finance will have a statutory test for exercising the powers that the Minister will have under the DTA resolution regime.

59 note that further work is being undertaken on the statutory test, the process to be followed in exercising the Minister of Finance's direction power, and on the Reserve Bank's accountability for its statutory objectives where it considers a ministerial direction to be in conflict with its objectives, and that decisions on these matters will be taken under delegated authority.

No creditor worse off

60 agree to confirm Cabinet's previous in principle decision [DEV-19-MIN-0346] that resolutions be required to be conducted in a manner that respects the creditor hierarchy that would normally apply in a liquidation unless departure from the hierarchy is necessary to maintain the stability of the financial system, including maintaining critical financial functions.

61 agree to confirm Cabinet's previous in principle decision [DEV-19-MIN-0346] that an after-the-event compensation mechanism be established to compensate creditors if a resolution left some creditors worse off than they would have been in an ordinary liquidation (the 'no creditor worse off' principle) deposit takers.

62 note that decisions on the 'no creditor worse off' compensation mechanism will be taken under delegated authority.

Public Finance Act 1989 amendment to provide authority to incur expenditure without an appropriation in a financial crisis

63 agree to amend the Public Finance Act 1989 to provide authority (similar to the existing section 25 of the Public Finance Act), whether or not there is an appropriation in place, for the Minister of Finance to approve expenses or capital expenditure to be incurred in respect of a financial entity regulated by the Reserve Bank where conditions along the following lines have been met:

63.1 the Reserve Bank has advised the Minister of Finance that the financial entity is insolvent or would soon be insolvent or otherwise considered to be failing financially;

63.2 the Minister is satisfied that the expenditure is:

63.2.1 necessary or desirable in the public interest, and

63.2.2 necessary or desirable to maintain the stability of the financial system and the continuity of critical financial services.

63.3 the Minister is satisfied that all other options consistent with the public interest to resolve the entity without using public funds had either been exhausted, were unlikely to succeed on their own, or were not in the public interest under the circumstances; and

63.4 the Minister is satisfied that adequate arrangements will be in place to prudently manage fiscal risks to the government arising from the expenditure.

Authorised for lodgement

Hon Grant Robertson

Minister of Finance

Appendix 1: Options considered for placing a deposit taker into resolution

The Review considered two options for placing a deposit taker 'into resolution'. The first approach is that Parliament empowers the Reserve Bank as resolution authority to take the decision. This approach recognises that assessing a deposit taker's situation against the statutory criteria for resolution requires a substantial degree of technical expertise or expert judgement of complex issues.

There are judgements to be made, but these are judgements that an independent regulator, rather than a Minister, may be best placed to make. It also helps to avoid risks of politicising the decision (particularly the risk of Ministers being pressured to opt for taxpayer bailouts instead), recognising that it is not always helpful to have Ministers involved. Providing that the Minister had been consulted on, and is comfortable with the resolution strategy and that wider economic, social, and international impacts have been appropriately considered and addressed, the final decision could be taken by the Reserve Bank acting in accordance with its statutory objectives.

The second approach is that the decision be taken by the Minister of Finance – on the recommendation of the Reserve Bank. This approach recognises that, in some cases at least, the potential impacts of the approach to resolution could be seen as warranting the explicit endorsement of the government of the day and the additional 'legitimacy' that a formal government approval imparts. The risks are that politicising the decision could result in sub-optimal approaches to resolving the failed entity.

International practice varies. The UK and Australia, for example, fully empower their resolution authorities to put an entity into resolution but with close consultation with their respective Treasuries. Canada, on the other hand, requires an order of the 'Governor in Council'.

Appendix 2: Key areas of further work

- Further provisions relating to the powers of the Reserve Bank (e.g. powers of a liquidator under the Companies Act 1993)
- Moratoria on creditor enforcement claims
- Stays on early termination rights contained in certain financial contracts
- Legal safeguards (eg, protections for directors and entities, temporary suspension of disclosure requirements)
- Tax implications of statutory bail-in
- Creditor safeguards (the ‘no creditor worse off’ mechanism)
- Resolution funding
- Reporting and accountability requirements
- Whether deposit takers should continue to be within the scope of statutory management under the Corporations (Investigation and Management) Act 1989