

TE TAI ŌHANGA  
THE TREASURY

# Statement of Funding Approach (SoFA) - Consultation

# Overview

- Introduction & context
- Overview of the sections for consultation
- Conclusion & Next Steps
- Question & Answer

# Purpose of the SoFA and the current consultation

- The Deposit Takers Act establishes the Depositor Compensation Scheme (DCS).
  - levy funded with a Crown backstop.
- The SoFA is the funding strategy for the DCS and must contain:
  - likelihood of a payout event
  - estimated costs of the DCS
  - target fund size & a timeframe (if any)
  - *investment strategy*
  - *an approach to managing the Crown's financial position in connection with the DCS.*

# Sections for Consultation

# Section 3: Decision-making principles

## Objective or principle

**Public Confidence:** The DCS has the objective of contributing towards protecting and promoting the stability of New Zealand's financial system by protecting depositors and allowing the DCS fund to be used to support a resolution measure.

**Accountability:** The DCS should be fully funded by industry over time.

**Predictability:** The funding strategy should aim for levies to be predictable over time.

**Resilience:** The DCS funding strategy should have regard to the impact of failures on the Crown's balance sheet and the wider deposit-taking sector.

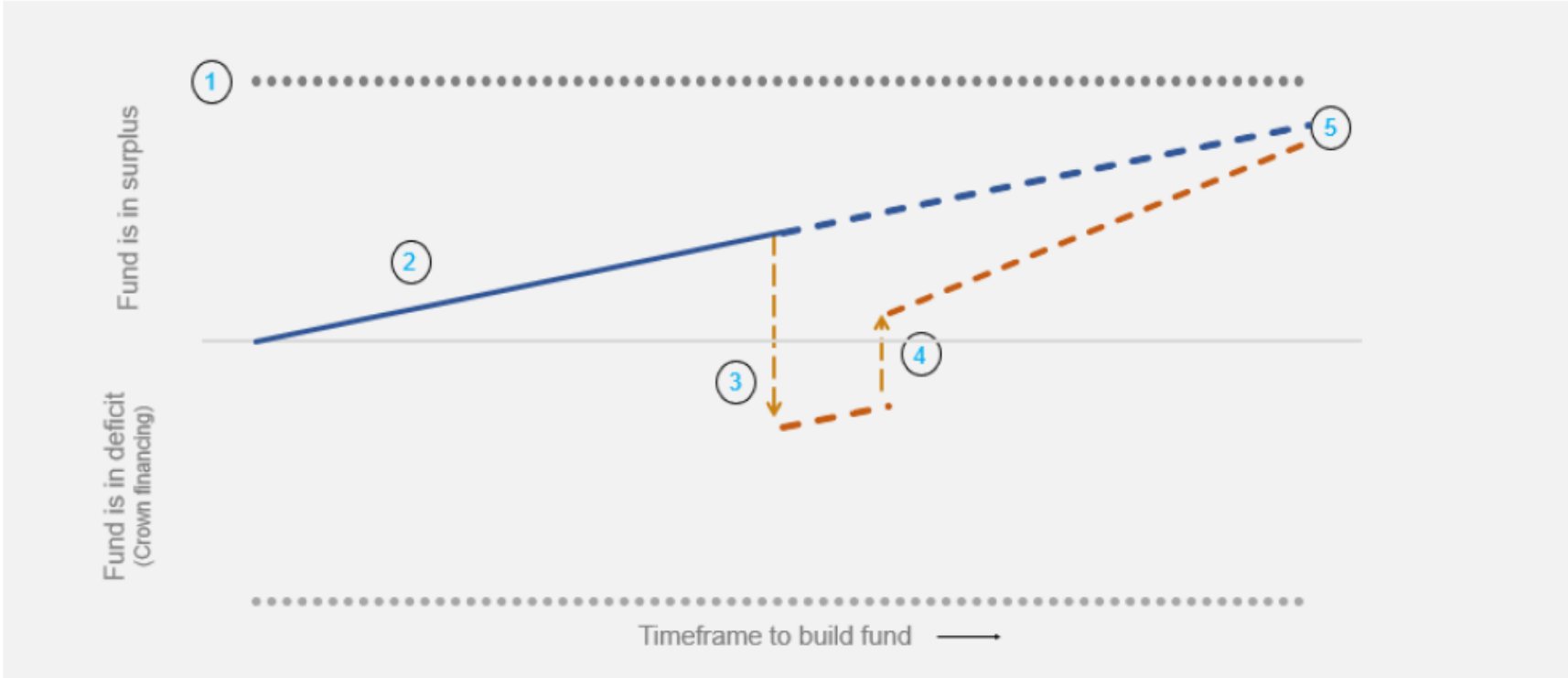
**System alignment:** The DCS funding strategy should consider the likelihood of failure, and be tailored to the nature of New Zealand's financial system and existing and forthcoming prudential regulation.

**Equity:** The DCS funding strategy adopts an equitable approach to funding over the long-term.

**Efficiency:** The DCS funding strategy adopts an efficient approach to funding over the long-term.

# Sections 4-5: Conceptual approaches to the funding strategy

Figure 1: Illustrative path for the DCS fund under a target fund approach, with or without the failure of a deposit taker



# Sections 6 – 8: Estimating costs to the DCS and proposals for a potential target fund size

- Given limited risk information, we have developed severe but plausible failure scenarios to guide calibration of a potential target fund size:

**Table 4: Funding requirements for the DCS in severe but plausible failure scenarios**

Failure scenario	Funding required for upfront payout to depositors (\$ billion)	Losses after recoveries are made or following use of resolution tools (\$ billion)
Resolution of one of the largest five banks	Not estimated, given the low expected likelihood that liquidation would be used over resolution	0-3.3 The upper end is the estimated maximum contribution the DCS would make to a resolution of a deposit taker
Liquidation of one medium-sized bank	1.3-3.4	0-0.3
Widespread liquidations in the non-bank deposit taker sector	0.8-0.9	0.1-0.4

We are seeking feedback on a target fund size in the range of **0.5 to 1.1 per cent of protected deposits**

# Sections 9 & 10 – Timeframes and Consultation Options

Principles	Option A (0.5% fund over 20 years)	Option B (0.8% fund over 15 years)	Option C (1.1% fund over 10 years)
Resilience	+ Reduces impact on Crown balance sheet in short to medium term compared to status quo	++ After 15 years prevents the Crown bearing medium term costs of a failure	+++ Provides a buffer against the failure of 1 of the big 5 banks after 10 years
System alignment	+ Levies would fund a significant portion of the estimated cost of failure scenarios	+ Levies broadly match the estimated cost of failure scenarios	+ Levies would provide a small buffer over and above the estimated cost of failure scenarios
Equity	+++ Costs spread over more potential beneficiaries relative to other options	++ More front loaded than A	+ Costs would be concentrated in the first 10 years of the DCS
Efficiency	+ More scope to calibrate levies over time based on actual events	- Levies would likely exceed estimated failure costs in the 15 year build up	-- Greater risk of levies exceeding expected costs over time

## Key:

+ better than status quo

- worse than status quo



# Conclusion & Next Steps

# Conclusion & Next Steps

## *Linkages with the RBNZ consultation*

- The SoFA will inform the policy work of the RBNZ in setting specific levies for the DCS fund.

## *Next Steps*

- Consultation 2 will take place early next year, including:
  - the investment strategy
  - operating costs of the DCS.
  - an approach to managing the Crown's financial position in connection with the DCS.

A submissions template is available online and submissions can be received via email or post.

Deadline: 25 September 2023.

Contact:

[sofaconsultation@treasury.govt.nz](mailto:sofaconsultation@treasury.govt.nz)

Questions?