

Memorandum of Cooperation on Trans-Tasman Bank Distress Management

Purpose of the Memorandum of Cooperation

The purpose of this Memorandum of Cooperation (henceforth Memorandum) is to assist the participants in achieving a coordinated response to financial distress in any bank or banking group that has significant operations in Australia and New Zealand (referred to as a "trans-Tasman bank") in a manner that avoids, where practicable, instability in the financial systems of Australia and New Zealand and promotes an effective resolution of the bank's financial distress. The Memorandum does not pre-commit to, or rule out, any particular resolution option. However, the participants recognise the importance of the continuation of critical shared services and functions and other outsourcing arrangements between members of a trans-Tasman bank and agree that those arrangements must continue uninterrupted in a trans-Tasman banking crisis.

The Memorandum sets out principles to which the participants will have regard in the decisions they take, and in the advice they will provide to the Australian and New Zealand Governments, when faced with financial distress in a trans-Tasman bank. As such, other than the section "Outsourcing arrangements", it is not intended to bind the Australian or New Zealand Governments in any way. Rather, the Memorandum provides a broad framework to promote and facilitate a coordinated response by the participants to a trans-Tasman banking crisis, and to allocate responsibility for particular elements of the response.

The Memorandum is not governed by international law and, other than the section "Outsourcing arrangements", does not create legal relations between the participants to the Memorandum.

Participants to the Memorandum of Cooperation

The participants in the Memorandum are:

- The member agencies of the Australian Council of Financial Regulators (the Council):
 - Australian Commonwealth Treasury (Australian Treasury)
 - Australian Prudential Regulation Authority (APRA)
 - Reserve Bank of Australia (RBA)
 - Australian Securities and Investments Commission (ASIC)
- The agencies in New Zealand responsible for responding to financial system distress:
 - New Zealand Treasury
 - Reserve Bank of New Zealand (RBNZ)

In this Memorandum, unless otherwise indicated, reference to the "participants" is a reference to the Australian and New Zealand participants.

Responsibilities of the participants to the Memorandum of Cooperation

Australia

In Australia, the Council provides the forum for facilitating coordination among the members in order to ensure prompt and effective identification of, and responses to, developments that pose a threat to the stability of the financial system. It is also the forum within which the Australian response to the distress of a trans-Tasman bank will be coordinated. Further detail on the processes by which the four Australian agencies will deal with distress in the Australian financial system are contained in a memorandum of understanding between the Council agencies, signed in September 2008.

The responsibilities of each member for dealing with stress in the financial system are as follows:

- **Australian Treasury.** The Australian Treasury provides advice to the Government on policy and possible reforms that promote a sound financial system, including on financial distress management arrangements. The Australian Treasury has responsibility for advising the Government on matters relating to the exercise of the Treasurer's powers, and on the broader economic and fiscal implications of developments that pose a threat to the stability of the financial system. In the case of a trans-Tasman bank distress situation, the Australian Treasury has lead responsibility for advising the Australian Government on any responses to the parent bank and its foreign operations that involve the exercise of powers or provision of assistance by the Australian Government.
- **APRA.** APRA is responsible for the prudential supervision of authorised deposit-taking institutions, life and general insurance companies, friendly societies and certain superannuation funds. In performing its functions to protect the interest of depositors, policyholders and fund members, APRA is required to balance the objectives of financial safety and efficiency, competition, contestability and competitive neutrality and, in balancing these objectives, is to promote financial system stability in Australia. APRA has failure management and enforcement powers to deal with a distressed institution and is responsible for administering the Financial Claims Scheme (FCS).

In the case of a trans-Tasman bank distress situation, APRA has lead responsibility for assessing the financial condition of the parent bank and its operations outside Australia and New Zealand, for exercising supervisory powers in respect of the parent bank and for assessing possible options for responding to the distress of the parent bank and its operations outside Australia and New Zealand.

- **RBA.** The RBA has primary responsibility for the maintenance of overall financial system stability, including stability of the payments system, and for providing liquidity support to the financial system or to individual financial institutions where appropriate. In the case of a trans-Tasman bank distress situation, the RBA has responsibility for assessing the impact of the distress and the possible response options on the Australian financial system, and for providing liquidity to the parent bank in Australia where appropriate.
- **ASIC.** ASIC is responsible for monitoring, regulating and enforcing corporations and financial services laws, and for promoting market integrity and consumer protection across the financial services sector and the payments system.

In the case of a trans-Tasman bank distress situation, ASIC has lead responsibility for assessing and advising on the Corporations Act-related regulatory implications of any resolution option in respect of the parent bank.

New Zealand

In New Zealand, the New Zealand Treasury and RBNZ have principal responsibility for promoting the stability of the New Zealand financial system and coordinating the New Zealand response to the distress of a trans-Tasman bank. Under the Reserve Bank of New Zealand Act 1989, statutory powers are conferred on the RBNZ and the Minister of Finance to manage a bank distress or failure situation. As any decisions are likely to have financial implications for the Crown, the RBNZ will consult with Treasury on recommendations to be brought to the Minister, given Treasury's role as the Government's primary economic and financial advisor.

The responsibilities of the respective agencies are:

- **New Zealand Treasury.** The New Zealand Treasury is the Government's primary economic and financial advisor. The New Zealand Treasury has responsibility for providing economic and strategic advice to the Government on the impact of financial distress arrangements on fiscal management, and broader government objectives such as economic growth and international connections. The New Zealand Treasury also has a central agency role in providing advice on institutional design and whole-of-government policy coherence. In the case of a trans-Tasman bank distress situation, the New Zealand Treasury has responsibility for providing advice about the provision of assistance by the New Zealand Government.
- **RBNZ.** The RBNZ is responsible for promoting the maintenance of a sound and efficient financial system. Its functions include the registration and supervision of banks, overseeing the payments system, providing liquidity to the banking system, and monitoring the stability of the financial system and its capacity to absorb shocks from various sources. In order to avoid damage to the financial system arising from bank failures, the RBNZ is able to draw on emergency powers including to act as lender of last resort, give directions to a bank, and to declare a bank subject to statutory management.

Principles for responding to the financial distress of a trans-Tasman bank

In recognition of the need for a coordinated approach to managing distress in a trans-Tasman bank, and in the situation where an open resolution is contemplated, the participants to this Memorandum have decided on the following principles to guide any response to such distress:

- a. Consistent with the legislation in both countries¹, the participants in responding to bank distress or failure situations, will, to the extent reasonably practicable, avoid any actions that are likely to have a detrimental effect on the stability of the other country's financial system. This includes maintaining international confidence in each other's financial systems. Both countries will seek to coordinate their responses to these ends.

¹ In Australia, the Australian Prudential Regulatory Authority Act 1998 and the Banking Act 1959 contain provisions that oblige APRA, to the extent reasonably practicable, to avoid any actions that are likely to have a detrimental effect on the stability of the New Zealand financial system. In New Zealand, the Reserve Bank of New Zealand Act 1989 contains provisions that oblige the RBNZ, to the extent reasonably practicable, to avoid any actions that are likely to have a detrimental effect on the stability of the Australian financial system. This includes any action that prevents, interferes with or otherwise disrupts an outsourcing arrangement.

- b. A closely co-ordinated, co-operative approach involving the participants is likely to lead to a more cost-effective financial crisis resolution and a more effective means of maintaining financial system stability in both countries than one in which the respective participants pursue separate agendas. The participants will therefore seek to cooperate closely, ~~where practicable~~, in respect of all stages of resolving a crisis situation, including problem identification; information sharing; systemic impact analysis; assessment of response options; implementation of resolution; public communication; and exit strategy.
- c. The exact nature of any response pursued by the respective Governments will depend on the specifics of the particular situation. However, resolution policies in relation to outsourcing arrangements between members of a trans-Tasman bank should be agreed upon in advance by the participants, including the establishment of a crisis management group (CMG) for each trans-Tasman bank to oversee the development of bank-specific resolution plans covering the means by which the continuity of critical shared services and functions and other outsourced services can be best assured in a trans-Tasman banking crisis. The resolution plans should provide for the continuation of the supply of critical shared services and functions and other outsourced services between members of a trans-Tasman bank for a reasonable period to allow for transition-out following any separation of those members.
- d. For systemically important banks, the participants will explore options for an open resolution of the parent and subsidiary banks that are most likely to be conducive to maintaining stability and international confidence in the financial systems of both countries, and will advise their respective Governments accordingly.
- e. Private sector solutions are preferred over public support, but government support may be required in some cases, particularly where a trans-Tasman bank is severely undercapitalised or insolvent, or is under acute stress due to a fall in market confidence, and there appears to be no prospect of private capital support in the required timeframe. Public sector support may involve government guarantees, recapitalisation or liquidity support, or a combination of these.
- f. Any solution to a bank distress situation that involves government support will be designed, to the extent practicable, to: keep costs to the minimum; protect taxpayer interests; maintain market disciplines; and minimise moral hazard.
- g. In a situation where an Australian parent bank is able to provide financial support, including recapitalisation, to its New Zealand subsidiary, and where the parent bank is satisfied that providing such support is in its commercial interests, the Australian participants will encourage this support, provided that it does not compromise the financial soundness of the parent bank.
- h. In a situation where the parent bank is not able to provide financial support to its New Zealand subsidiary without compromising the parent bank's financial soundness, the Australian participants will take the lead in reviewing options for the parent bank and its foreign operations (except New Zealand). The New Zealand participants will take the lead in reviewing options for the New Zealand subsidiary.
- i. Each country remains responsible for the manner in which creditor claims are resolved in its jurisdiction, consistent with the objective of maintaining stability and confidence in both countries' financial systems.

- j. Any public support arrangements will need to be accompanied by measures that enable the Australian and New Zealand Governments to exercise an appropriate degree of control over the respective banks to which they have provided support and over the exit arrangements. Any solution involving a coordinated approach needs to be acceptable to both countries' Governments.
- k. The Australian Government is responsible for public announcements of public sector support for the parent and the New Zealand Government is responsible for public announcements of public sector support for the New Zealand subsidiary. The timing of any statements by public sector agencies will need to be coordinated where appropriate, given the pressure that announcements in one country could have on the other. The participants consider that "statements of confidence" in a trans-Tasman bank by public sector agencies in either country risk being seen as tantamount to the provision of financial support, with the potential for spill-overs to the other country.
- l. Any solution to a bank distress situation needs to take account of the impact that it has on any contractual arrangements (including outsourcing arrangements) that the distressed bank has with any related trans-Tasman bank and the importance of the continuation of services that are provided under those arrangements. The participants are to take a closely co-ordinated and co-operative approach to such matters.

Coordination of response to trans-Tasman bank distress

In accordance with the above principles, the participants to this Memorandum will cooperate to promote a coordinated response to the distress of a trans-Tasman bank. A contact list of officials in the Australian and New Zealand agencies that are responsible for financial crisis management has been developed in order to facilitate timely communication and coordination on these issues. This coordination will include the following measures:

- a. **Information sharing and early warning alerts.** The participants will keep each other apprised of any developments or expected developments that may have material impact on either country's financial system. APRA and the RBNZ will maintain systems that enable them to detect emerging stress in a trans-Tasman bank and will alert each other if they become aware of any such stress.
- b. **Diagnosis of bank distress.** In a situation where a trans-Tasman bank is in distress or likely to become distressed, the participants will coordinate the process of investigating and assessing the bank's condition. Where practicable, analysis of solvency and liquidity, and other matters relevant to an assessment of the bank's condition, will be conducted on the basis of similar analytical frameworks by APRA, RBA and RBNZ. The agencies will exchange information in a timely manner to facilitate a coordinated assessment of the trans-Tasman bank's group position.
- c. **Diagnosis of systemic impact.** The two central banks, in liaison with the other participants, will provide each other with their assessment of the potential impact on the stability of their respective countries' financial systems that could result from distress of a trans-Tasman bank. The participants will exchange such information in a timely manner.
- d. **Holding actions.** Where a trans-Tasman bank is in financial distress or likely to become distressed, the participants will coordinate any holding actions taken to restrict further deterioration. In particular, APRA and the RBNZ will coordinate the nature of any supervisory actions they may intend to take to restrict further deterioration, with a view to

minimising adverse impact on either country's financial systems and promoting an effective response to the situation.

- e. **Assessment of response options.** The participants will coordinate the assessment of possible response options, including their assessment of the potential systemic impact of such options. The Australian participants will have lead responsibility for assessing possible responses to address the parent bank's distress (and its operations outside of Australia and New Zealand), including assessing the systemic impact of those responses. The New Zealand participants will have lead responsibility for assessing possible responses to address the New Zealand subsidiary's and/or branch's distress, including assessing the systemic impact of those responses. The participants will cooperate to promote an effective group-wide response to the situation, with a view to avoiding or minimising instability in either country's financial system.
- f. **Liquidity support.** If central bank liquidity support is required as part of the response to a trans-Tasman bank distress situation, the RBA and RBNZ will coordinate the provision of liquidity support. Both countries' central banks will cooperate to ensure that their respective banking systems can also obtain liquidity in the other country's currency, should that be necessary. The RBA has responsibility for any liquidity support provided to the parent bank, and the RBNZ has responsibility for any liquidity support provided to the New Zealand subsidiary.
- g. **Government guarantee.** If the Australian and New Zealand Governments agree that a government guarantee is required as part of the response to a trans-Tasman bank distress situation, the Australian Treasury and New Zealand Treasury will coordinate the provision of the guarantee. The Australian Treasury has responsibility for the design and implementation of a guarantee of specified financial obligations of the parent bank (including of its foreign branches), and the New Zealand Treasury has responsibility for the design and implementation of a guarantee of specified obligations of the New Zealand subsidiary. The terms and conditions applicable to the guarantees will be coordinated, with a view to maintaining an effective resolution and coordinated exit from the guarantee.
- h. **Capital support.** If the Australian and/or New Zealand Governments provide or facilitate capital support as part of a response to a trans-Tasman bank distress situation, the participants will coordinate the recapitalisation process. Coordination will include consideration of the level of recapitalisation required of the parent bank and New Zealand subsidiary respectively, the nature of capital provided, and the terms and conditions attaching to the provision of capital. The Australian participants will have responsibility for the design and implementation of capital support for the parent bank and the New Zealand participants will have responsibility for the design and implementation of capital support for the New Zealand subsidiary.
- i. **Government control over a trans-Tasman bank.** Where a decision has been made by the Australian and/or New Zealand Governments to provide capital or other forms of financial support to a trans-Tasman bank, the participants will advise the respective Governments to establish and maintain an appropriate degree of control over the banking group in order to ensure that risks associated with such support are prudently managed and that the respective Governments have control over the process of exiting from the support arrangements. The Government that has provided the capital or other form of financial support will generally have the responsibility for ensuring that it has a satisfactory level of control over the entity or entities to which it has provided the support.

- j. **Public communications.** Any public communications associated with the response to a trans-Tasman bank distress situation will be coordinated between the participants. Public communication of measures involving government-funded or facilitated support will be made by the Australian Government in respect of the parent bank and by the New Zealand Government in respect of the New Zealand subsidiary. Communications on supervisory measures will generally be made by APRA in respect of the parent bank and by the RBNZ in respect of the New Zealand subsidiary. Communications on liquidity support will generally be made by the RBA in respect of the parent bank and by the RBNZ in respect of the New Zealand subsidiary.
- k. **Exit from government support or ownership.** To assist in the orderly and effective exit from any government ownership or support of a trans-Tasman banking group, it will generally be appropriate to terminate government guarantee arrangements in respect of financial obligations of the parent bank and New Zealand subsidiary in a coordinated way. Similarly, the sale of government shares or other forms of capital in the parent bank and New Zealand subsidiary will generally be coordinated.

Testing of trans-Tasman crisis management coordination

The participants will take initiatives to test the adequacy of trans-Tasman financial crisis management coordination. This Memorandum will be reviewed from time to time having regard to the lessons learned from such testing.

Outsourcing arrangements

The participants acknowledge that the on-going provision of shared services and functions and other outsourced services to a trans-Tasman bank may be of critical importance to the on-going viability and operation of that trans-Tasman bank, and, in turn, to the stability of the financial system in that trans-Tasman bank's country. To that end, and without limiting the principles for responding to the financial distress of a trans-Tasman bank described above, the participants agree to the following specific measures:

- a. Where a trans-Tasman bank is in financial distress, or likely to become distressed (referred to as a "distressed institution"), the participants will closely coordinate the nature of any supervisory actions any of them may intend to take in respect of any critical shared service or function or other outsourcing arrangements between the distressed institution and any related trans-Tasman bank, where such action may have an adverse impact on the on-going provision of services under those outsourcing arrangements.
- b. Without limiting the above, a participant will not:
- take any action or step or give any direction that prevents, interferes with or otherwise disrupts (referred to as "preventative action") the provision of such services by the distressed institution to the related trans-Tasman bank, or which would cause, or would be reasonably likely to cause, a material breach of the arrangements in respect of such services;
 - take any preventative action in respect of any decision by a trans-Tasman bank to terminate an outsourcing arrangement with a distressed institution or in respect of any transition or disengagement services to be provided by the distressed institution;
or

- take any preventative action in respect of transition, disengagement or on-going, services provided under any outsourcing arrangement by the distressed institution to the trans-Tasman bank that was, but no longer is, a related trans-Tasman bank as a consequence of the exercise of any supervisory powers by any participant.

This measure shall apply for so long as is reasonably required for the trans-Tasman bank to transition to an alternative supplier or no longer require a supplier to provide such services.

- c. The participants will comply with these measures to the extent reasonably practicable, and will only deviate from them where they are required to do so in order meet an [express](#) statutory obligation, and then only after reasonable consultation with the other participants. The participants acknowledge that a failure by another participant or a government to provide financial or other support (whether of nature contemplated under the section “Coordination of response to trans-Tasman bank distress” or otherwise) to the distressed institution, or to take any other supervisory action in respect of the distressed institution or any related trans-Tasman bank, will not be grounds for deviating from these measures.
- d. The participants acknowledge that trans-Tasman banks have a legitimate expectation that the participants will comply with these measures in accordance with their terms and that trans-Tasman banks consider the on-going provision of shared services and functions and other outsourced services to a trans-Tasman bank is important to the stability of the financial system in that trans-Tasman bank’s country.

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MEMORANDUM OF COOPERATION ON TRANS-TASMAN BANK DISTRESS MANAGEMENT

SIGNATURE PAGE

NEW ZEALAND

Alan Bollard
Governor
Reserve Bank of New Zealand

John Whitehead
Secretary
The New Zealand Treasury

MEMORANDUM OF COOPERATION ON TRANS-TASMAN BANK DISTRESS MANAGEMENT

SIGNATURE PAGE

AUSTRALIA

Glenn Stevens
Governor
Reserve Bank of New Zealand

John Laker
Chairman
Australian Prudential Regulation Authority

Tony D'Aloisio
Chairman
Australian Securities and Investments
Commission

Ken Henry
Secretary
The Australian Treasury