Reserve Bank of New Zealand and Treasury Joint Report: Cabinet Paper and Technical Decisions Related to the Deposit Takers Bill

To	Hon Grant Robertson Minister of Finance	**Date**	9 Sep 2021
Authorised by	Geoff Bascand Deputy Governor / GM Financial Stability Bryan Chapple Deputy Secretary Treasury	**Report no**	RBNZ 5853
Prepared by	David Hargreaves Manager, Policy Projects	**Security**	In-Confidence

Action Sought

Action sought	Deadline
1)Refer this paper to Hon David Parker, Associate Finance Minister, and Hon Dr David Clark, Minister of Commerce and Consumer Affairs	1)16 Sep 2021
2)Agree to the recommendations (in consultation with those Ministers	2)27 Sep 2021
3)Provide any feedback on the draft Cabinet paper	3) 20 Sep (if aiming for fast track to Cabinet)
Indicate if you would like to meet with officials	

Reserve Bank Contact for Telephone Discussion (if required)

Name	Position	Telephone
David Hargreaves	Manager, Policy Projects, RBNZ	s 9(2)(a)

Actions for the Minister's Office Staff

Return the signed report to the Reserve Bank

Refer the report to the Associate Minister of Finance, Hon David Parker, and the Minister of Commerce and Consumer Affairs, Hon Dr David Clark

Note any feedback on the quality of the report.	

Attachments – Draft Cabinet Paper

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Executive Summary

To complete the exposure draft of the Deposit Takers Act (DTA), it is necessary to take further decisions to complement the decisions taken by Cabinet in April 2021 [DEV-21-MIN-0076, DEV-21-MIN-0077, DEV-21-MIN-0078, and DEV-21-MIN-0079]. We recommend that some of these decisions are taken using the authority Cabinet delegated to you (either jointly or in consultation with the Associate Minister of Finance and the Minister of Commerce and Consumer Affairs).

These decisions relate to the following areas in the Deposit Takers Act:

- The Prudential and Supervisory framework – matters include the penalties regime, and principles guiding the use of regulatory powers.
- The Deposit Insurance Scheme – matters include the name of the scheme, triggers for payout, funding strategy, levy setting, powers necessary for payout, operating budget, and eligibility requirements.
- The Crisis Management and Resolution Framework – matters include direction powers available to the Minister of Finance in resolution where public funds are at risk, funding for resolution, and adaptions of the statutory management powers in the 1989 Act into the new resolution framework.

We also recommend that decisions on significant policy matters relating to the crisis management framework are taken by Cabinet and have provided a draft Cabinet paper for your consideration and feedback. These matters include:

- Proposals to limit legislative reforms on bail-in to contractual bail-in initially – these proposals represent a departure from Cabinet decisions in April which approved a statutory bail-in regime.
- The use of the deposit insurance fund in resolution and applicable safeguards – these proposals permit the fund to contribute to resolution (including to no creditor worse off

payments) provided the resolution protects insured depositors, and contributions are no more than what the deposit insurance scheme would have paid in a liquidation net of recoveries.

- Key features of the No Creditor Worse Off mechanism to be included in the DTA and appeal rights in resolution.
- Technical amendments aimed at mitigating impediments to resolution by constraining certain creditor rights.

If you agree to the set of recommendations here, we will finalise the Cabinet paper, and continue work with PCO to complete the exposure draft of the Deposit Takers Bill. If you would like to refer certain decisions to Cabinet rather than take them under delegation, please provide feedback and we will redraft the Cabinet paper as required.

Purpose of Report

1. The purpose of this report is to seek your agreement on progressing decisions related to a final set of policy issues for the Deposit Takers Bill. Once these decisions are taken, the Bill will be completed for an exposure draft stage, with the intention that it be introduced to Parliament in the second quarter of 2022.

Background

2. In April 2021, the Cabinet Economic Development Committee, considered four papers relating to the Deposit Takers Bill. These papers made recommendations seeking agreement to a new prudential and supervisory framework for deposit takers, the introduction of deposit insurance scheme, and reform to the crisis management and resolution framework for deposit takers. The Committee took decisions on these papers [DEV-21-MIN-0076, DEV-21-MIN-0077, DEV-21-MIN-0078, and DEV-21-MIN-0079] and these decisions were confirmed by Cabinet on 19 April 2021 [CAB-21-MIN-0128].

3. Cabinet agreed that you would have the delegated authority to take additional decisions necessary to complete the Deposit Takers Bill (either in consultation with the Associate Minister of Finance and the Minister of Commerce and Consumer Affairs, or jointly in the case of matters that affect their portfolios).

4. The Committee noted that additional Cabinet decisions may be required to finalise the Deposit Takers Bill (DEV-21-MIN-0076). On 1 July (RBNZ #5832) we recommended that the delegated authority be used to take detailed decisions (as suggested in this paper), but that Cabinet agree some of the significant policy aspects.

5. This paper contains recommendations that we propose are taken under the delegated authority agreed by Cabinet. A draft Cabinet paper is attached for your feedback which contains recommendations focused on significant policy aspects of the crisis management framework that we propose are taken by Cabinet. Subject to feedback, we will finalise the attached Cabinet paper for consideration in early October.

6. This paper was produced by the Reserve Bank, working to the joint RBNZ/Treasury Steering Committee. The following other agencies were consulted on the contents of this paper: the Ministry of Business, Innovation and Employment; the Financial Markets Authority. We also consulted the Independent Expert Advisory Panel, who provided the comments in the section below.

The Panel's Independent Advice to the Minister of Finance

7. The Panel wishes to convey that it is supportive as to the thrust of what is being proposed for the Deposit Takers legislation. It commends the Reserve Bank, Treasury and Review Team for progress made to address the many complex topics to be covered.

8. From the beginning of discussions about depositor protection, the Panel has emphasised the importance of being aware of the trans-Tasman relationship. This is particularly important, given the relative size of New Zealand's four largest deposit takers who are subsidiaries of four large Australian banks. The Panel is pleased to note that concerns it has raised earlier about no creditor worse off (NCWO) provisions in crisis resolution have been thoroughly addressed. The proposed NCWO protections

seem likely to alleviate concerns that may have been held from a trans-Tasman banking perspective.

9. The Panel recognises that depositor compensation is a new initiative for New Zealand, requiring distinct legislation. It appreciates that due to time pressure and the normal processes around the preparation of legislation, some key issues are still being worked through and some features have been deferred to secondary legislation.

10. There are three topics, however, where the Panel recommends time and resources be identified now to carry out further analysis prior to finalising the exposure draft for consultation. These topics are temporary high balances, the treatment of AML requirements and the registration of overseas beneficial ownership of Trusts (and any other relevant legal entities) that may be eligible for deposit insurance. The credibility of the legislation will be enhanced by a thorough examination of these areas to ensure as much as possible can be resolved for the implementation of the DTA. Waiting for a 5 year review risks considerable uncertainty, undermining what could otherwise be strong public, consumer and deposit taker support.

11. In regards to Ministerial directive power for bank resolution action, the Panel would like to see some further consideration of the rationale for this, but is supportive of it being subject to the same objectives as specified for the resolution authority.

12. The Panel was comfortable with the concept of ex post levies on surviving firms, provided they are in some way proportionate to the benefit they gain as survivors. An important related point is that deposit and business transfers in a resolution need to be done in a way that doesn't confer undue competitive advantage to any particular firm. The Panel suggests consideration be given to including this in the objectives assigned to the resolution authority.

Analysis

13. The recommendations here fill out an additional level of detail behind high level policy decisions already taken. The key attribute of the recommended approaches to these issues is that they are aligned with the overall policy decisions made by Cabinet.

The framework for the regulation and supervision of deposit takers

Development of the Bill and design choices

14. Cabinet agreed that, if feasible and appropriate, certain prudential powers the Reserve Bank is able to exercise over multiple different parts of the financial sector (e.g. deposit takers and insurers) would be consolidated into the new Reserve Bank Act rather than continue to be contained in separate sectoral legislation. Some issues have arisen with this, partly relating to the desirable scope of these powers being slightly different for different sectors. We have also been advised that it is more transparent if the key powers to regulate a sector are contained in the relevant Act rather than spread across multiple Acts. For this reason, we recommend that most powers (such as information gathering and on-site inspection powers) are placed in the sectoral Acts. Some matters such as the confidentiality practices the Reserve Bank must follow in handling supervisory information (which are less sector-specific) can likely still be consolidated.

Regulatory principles

15. The DTA includes a set of principles to guide the use of regulatory powers, including matters such as the need to avoid unnecessary compliance costs. We have been advised that it is appropriate to add additional principles that ensure the list is balanced and does not impede appropriate use of regulatory powers. The additional principles are subject to drafting, but would likely be along the lines of: the desirability of sound governance of deposit takers, the desirability of effective risk management, and the value of disclosure that helps stakeholders monitor deposit takers. Similar principles are included in the Insurance Prudential Supervision Act.

Penalties

16. In April, Cabinet took a number of decisions towards forming a penalty regime for the DTA that would use civil pecuniary penalties for contraventions of requirements under the DTA, with criminal offences reserved for more severe matters (such as intentional or reckless non-compliance). Pecuniary penalties are still adjudicated by a court but have a lower burden of proof and do not result in criminal conviction.

17. We have developed a tiered approach to criminal penalties, with three tiers. Tier 3 offences (the most serious) include operating a deposit-taking business without a licence or failing to comply with a direction. Tier 1 offences are less serious (not presenting immediate risks to financial stability), and Tier 2 offences are somewhere in-between. The penalty tiers and some proposed offences are as follows:

Table 1 A 3-tier criminal penalties approach

Maximum Penalty Level	Body Corporate	Individual	Example Offences
1	Fine not exceeding $500,000	Fine not exceeding $50,000	Failure to supply information; Failure to disclose warning
2	Fine not exceeding $2,500,000	Fine not exceeding $100,000 or imprisonment for a term not exceeding 1 year (or both)	Failure to hold a current credit rating; Failure to comply with condition of license
3	Fine not exceeding $5,000,000	Fine not exceeding $500,000 or imprisonment for a term not exceeding 2 years (or both)	Failing to comply with a direction.

18. These maximum penalties are significant, but will require a court-based enforcement process and in most cases demonstration that the offence was intentional or reckless. We are still considering how to use infringement notices to address certain more straightforward, relatively minor contraventions.

19. We recommend (as in the competition and conduct regimes) pecuniary penalties for breaches of prudential requirements given effect through ‘standards’ (a secondary legislative instrument) which are scaled relative to the size of the deposit taking institution. Specifically, we propose a maximum civil penalty of the highest of either 0.1% of the assets of the deposit taker, or $5,000,000. The $5 million maximum amount for smaller entities is designed to align with the maximum criminal penalty for an institution, reflecting the potential severity of breaches of standards. However, for the largest deposit takers in New Zealand, 0.1% of assets can be $100 million-$200 million (reflecting the greater financial stability risks of breaches at a large bank). The court

would be expected to have regard to the recommendation of the Reserve Bank amongst other factors when setting a penalty.

20. Civil penalties are also available for Board directors of deposit takers who have breached duties under the DTA. Directors will have a positive and on-going duty to ensure there are adequate systems, processes, and policies in place to ensure the entity complies with its prudential obligations.

21. We recommend a maximum penalty of $1 million for breaches of the director duty. This significant maximum penalty reflects the importance of this penalty, which will be the primary means of holding directors to account. As discussed in the Cabinet paper, there will be rules limiting the extent to which deposit takers can insure or indemnify directors in respect of this penalty. Our thinking on penalties reflects the similar UK regime. However, we note the draft Australian equivalent regime initially proposed penalties equivalent to just over $1 million AUD, but more recent drafts have instead proposed disqualification rather than a direct financial penalty. This matter will be discussed with industry in the exposure draft process.

Changes to FMC Act and regulations

22. Cabinet agreed in April that consequential amendments to the Financial Market Conduct Act 2013 (FMCA) and Regulations (including disclosure requirements) be made where required as a result of Deposit Insurance proposals.

23. For any non-bank deposit takers (NBDTs) that become deposit takers, the changes in disclosure and governance requirements in the FMCA and regulations imply that these deposit takers will:

- not be required to comply with the FMCA's trust deed requirements
- not be supervised by financial market Supervisors currently licensed under the FMCA
- not be required to prepare or provide product disclosure statements for less complex debt securities (e.g. deposit products)
- only be required to prepare limited disclosure statements in relation to other, more complex, debt securities (e.g. retail bonds)

24. This approach is consistent with the creation of a single regulatory regime for deposit takers and the shift to the Reserve Bank directly supervising all deposit takers. Risks associated with the removal of FMCA governance and supervision would be managed by strengthened prudential regulation and supervision by the Reserve Bank and the introduction of FMA conduct licensing for all deposit takers, including NBDTs.

Depositor protection and deposit insurance

General

25. In the Cabinet paper seeking agreement on depositor protection arrangements, it was noted that there were a number of detailed issues that needed to be progressed before legislation could be introduced. Recommendations in respect of these issues and related matters are provided below. These matters include:

- changing the scheme name to Depositor Compensation Scheme
- triggers for activating reimbursement to eligible depositors
- the funding strategy for the scheme
- powers necessary to make reimbursement
- the operating budget for the scheme and transparency requirements
- clarifying the scope of coverage and eligibility requirements
- treatment of temporarily high balances
- managing risks to the scheme

Change the scheme name to Depositor Compensation Scheme

26. Cabinet agreed in April to establish a Deposit Insurance Scheme. The term 'insurance' may cause confusion because the activities of the scheme are not consistent with what would typically be associated with insurance. The scheme is more consistent with a compensation scheme rather than an insurance scheme since it is not intended to involve the issuance of 'contracts of insurance' nor is the Reserve Bank (or the Crown) 'carrying on insurance business in New Zealand'. There is no direct contract between depositors and the scheme, although eligible depositors will be compensated by the scheme in specified events. It is not uncommon in other jurisdictions to name similar schemes as 'compensation scheme', 'claim scheme' or 'protection scheme'.

27. We recommend using "Depositor Compensation Scheme" (DCS) in the legislation to better reflect the nature and characteristics of the scheme and to mitigate potential confusion for the public when implementing the scheme. The new name also aligns better with the accounting and tax treatment of the scheme.

Triggers for activating reimbursement to eligible depositors

28. Cabinet agreed in April that the scheme funds may be released by the Reserve Bank for purpose of protecting insured depositors in resolution. Cabinet also agreed that the scheme will provide reimbursement when eligible depositors become entitled to compensation.

29. Further clarification is required on when eligible depositors will be formally entitled to compensation. Triggers should be consistent with the statutory objectives of the scheme to protect depositors, and its statutory function to promptly provide compensation to eligible holders in a liquidation or other events in which depositors would not have prompt access to protected deposits. We recommend that the legal entitlement of the scheme to compensate eligible depositors will be triggered:

    - when a licensed deposit taker is placed into liquidation on the application (or with the consent) of the Reserve Bank; or
    - if the Reserve Bank is satisfied that
        i. the licensed deposit taker is non-viable according to the statutory tests under the resolution framework, and

ii. eligible depositors would not otherwise have access to protected deposit amounts within a reasonable timeframe in light of the Bank's purposes and functions under the scheme.

30. Trigger (a) covers liquidations only initiated by the Reserve Bank. If liquidation is initiated by other persons, it will not trigger reimbursement under the scheme unless the Reserve Bank consents to the liquidation.[1] Trigger (b) deals with the scenario when payout happens without a liquidation. It allows the Reserve Bank to commence a reimbursement process when a deposit taker is non-viable and eligible depositors would not have access to protected amounts within a reasonable period of time. This is especially relevant if an entity has been placed in resolution, but the resolution authority (the Reserve Bank) finds there is no practical way for the resolution to promptly restore depositors' access to insured deposits.

Funding strategy for the scheme

31. The intention is for the compensation scheme fund to be built up from levies. Cabinet agreed in April that if the balance of the scheme fund is not sufficient to meet the scheme's payment obligation, the Crown will provide the required funding to satisfy the scheme's payment obligation. Any delays or uncertainties associated with the scheme's ability to meet its payment obligations would undermine the credibility of the Scheme and the ability of the Reserve Bank to carry out its functions. Cabinet agreed that shortfalls in funding can be recovered through future levies.

32. We recommend including a provision in the DTA to allow a permanent legislative authority (for the Minister) to spend public money in this way, without further authority. This is consistent with the policy intention of the scheme to promptly meet its reimbursement obligations.[2]

33. Cabinet agreed in April that shortfalls in funding can be recovered through future levies. We recommend that the Minister may determine whether all or part of the funding provided to the scheme by the Crown be repayable, and the terms and conditions that apply to any repayment obligation. This is to build in flexibility for a future Minister to effectively subsidise the scheme, due to a concern that recovering extensive past losses via levies could have adverse economic effects.

34. We do not recommend that the Crown is able to charge an ex-ante fee for its obligation to provide funds to the scheme. The fund mitigates Crown funds being needed in the first place, and any funds provided can be structured in a way so that the scheme is charged for the use of Crown funds (e.g. interest) in the interim. An ex-ante fee would potentially lead to the scheme paying twice for funds it receives via the backstop. We note that provisions in the Earthquake Commission Act 1993 allowing the Crown to charge a fee for funding obligations have been removed for similar reasons.

35. The Statement of Funding Approach will underpin the target fund and levy setting. It can be modified and adjusted over time.

[1] This implies that if the Reserve Bank considers that placing the deposit taker into resolution could better address its financial stability and other statutory objectives, the Reserve Bank can place the deposit taker into resolution rather than payout, even if another person initiates liquidation proceedings.

[2] In April Cabinet agreed to a separate PFA amendment that would give the Minister the ability to spend without appropriation where necessary in a financial crisis. This is also likely to be progressed in the exposure draft, but is distinct from this authority, which is solely to support the Deposit Insurance Scheme.

Powers necessary for payout

36. Cabinet agreed in April the statutory purpose for the scheme is to promptly reimburse eligible depositors in a specified event. The payout framework has been designed to provide a high degree of confidence that the Reserve Bank will have sufficient powers to be able to fulfil this function under a range of payout approaches.

37. Cheques have been phased out in New Zealand, so are no longer available as a mechanism for making a payout. This leaves electronic funds transfer to another bank account as the most likely mechanism for making a payout. As a result, we recommend that, to the extent it is necessary for the Reserve Bank to fulfil its role as manager and administrator of the scheme, the Reserve Bank have the power to open accounts with another deposit taker on behalf of insured depositors.

38. This power (which already exists in Australia) would ensure that payments can be made to depositors who have not previously nominated an account with another deposit taker to receive a payment, or who are unable to quickly open up another account with an alternative deposit taker for that purpose. It is important to note that while this power would provide the ability to open an account on behalf of insured depositors, it would not extend to requiring surviving deposit takers to accept these new accounts. Arrangements would have to be negotiated with surviving deposit takers for them to take these accounts, and the allocation of new accounts to surviving deposit takers would have to be managed carefully to ensure it did not provide any surviving deposit takers with an unfair competitive advantage.

39. To enable deposit takers to share personal information of depositors with the Reserve Bank for the purpose of facilitating reimbursement to eligible depositors under the scheme, our engagement with the Office of the Privacy Commissioner (OPC) shows that privacy issues could be dealt with by either:

    - A provision in the DTA to override the Privacy Act 2020 for the limited purpose of allowing the DIS to obtain information relevant to depositors' entitlement to compensation without seeking their consent first; or

    - By requiring all deposit takers to amend their existing terms and conditions with eligible depositors so they have consented to this sharing of information.

40. We recommend testing these two options with industry during the DTA exposure draft public consultation, and will engage further with the OPC on this issue.

41. Establishing new accounts on behalf of depositors for the purposes of making reimbursement under the scheme also has implications under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT Act). We are discussing this issue with the Ministry of Justice, including the option of providing a deposit taker that accepts new accounts for payout purposes with an exemption from certain requirements of the AML/CFT Act (e.g. customer due diligence (CDD) requirements). This exemption could be subject to conditions (e.g. a requirement to comply with CDD requirements within a certain time after receiving the new accounts), but may not be, if it is sufficient to simply rely on the previous due diligence carried out by the failed deposit taker. We will continue working with the Ministry of Justice on this issue. Although it will be necessary to resolve this issue before the scheme becomes operational, this will not affect the progress of the draft Bill, because the exemption would be established via regulations made under the AML/CFT Act.

The operating budget for the scheme and transparency requirements

42. Cabinet has agreed that the scheme will be fully funded by levies on member institutions, including the scheme's operational costs. With the exception of a payout event and the initial stage of establishing the scheme and its operational infrastructure, the ongoing operational expenditure is expected to be small relative to the fund.

43. The RBNZ Act 2021 provides the provision that the Minister and the Reserve Bank may enter into a funding agreement that specifies the amounts that may be paid or applied in meeting the expenditure incurred by the Reserve Bank in each financial year in performing or exercising its functions or powers under the RBNZ Act or any other legislation. The Reserve Bank and the Treasury have agreed that the operational cost of the scheme should be included in the 5 year funding agreement, and the Reserve Bank should be reimbursed from the scheme fund for its operational expenditure related to the Reserve Bank's statutory function of performing and exercising the function of the scheme.

44. We recommend that the scheme fund can be applied by the Bank for the purpose of covering actual and reasonable scheme operating costs.

45. We recommend that the operational cost of the scheme will be included in the funding agreement between the Minister of Finance and the Reserve Bank.

46. To ensure transparency, the DTA should aim to require the Reserve Bank to provide assurance to Ministers, deposit takers, and the wider public that levies and assets are being managed and used appropriately. We recommend that the Reserve Bank be required to publish the financial position of the fund annually.

The scope of coverage and eligibility requirements

47. Cabinet agreed in April that protected deposits will be defined in legislation. We recommend that protected deposits under the Scheme will include debt securities repayable in New Zealand dollars, governed by New Zealand law. Debentures, commercial papers, bonds and capital notes are excluded from protected deposits. The scope of the product boundary for protected deposits may be adjusted through regulations made on the advice of the Minister of Finance by Order in Council.

48. Cabinet agreed in April that regulations to deal with how eligibility applies to other types of ownership structures (e.g. trusts) may be made by Order in Council. However, the potential for trustees to be eligible investors under the scheme adds to the complexity of the pay-out process and raises the question of whether trusts should be excluded entirely from the DIS. We are aware that all overseas depositor protection schemes cover trusts and trusts are widely used in New Zealand.

49. We recommend confirming in the legislation that trustees of New Zealand law governed trusts are eligible investors under the scheme.

50. Cabinet agreed in April to exclude deposits held by financial institutions, large non-financial corporates, related parties of scheme members, and government bodies from the coverage by the scheme. The main purpose is to avoid the scheme weakening the incentive for these more sophisticated depositors to monitor the risk-taking of their deposit takers. To further clarify the exclusions, we recommend the following persons will not be eligible investors under the scheme for deposits held in their own right:

- large corporations and unincorporated bodies with the threshold for “large” to be based on the meaning of this term in the Financial Markets Conduct Act 2013 (i.e., $5 million annual turnover or net assets for last two years)

- licenced deposit takers, licenced insurers, operators of Financial Market Infrastructures

- in relation to a failed licenced deposit taker, the associated persons and directors of that deposit taker

- government agencies based on the meaning of this term in the FMCA, but school boards and tertiary education institutions (within the meaning of section 7 of the Crown Entities Act 2004) are eligible investors under the scheme

51. We recommend that persons excluded from eligibility for the scheme may be adjusted through regulations made on the advice of the Minister of Finance by Order in Council.

52. Regulations developed under the DTA will provide more detailed rules for the treatment of investors for complex ownership structures of eligible products, for example, the eligibility of clients of associated persons of deposit takers holding deposits on behalf of customers (e.g. for bank-issued PIE funds).

Treatment of temporarily high balances

53. Protection for temporarily high balances (THB) mitigates hardship for depositors who, at the time of a deposit taker failure, have balances that were only expected to remain at the deposit taker for a short period of time (for example, monies for the purchase or sale of a house, or a lump sum payment from Kiwisaver after retirement). Without being covered by the scheme with an adjusted limit for dealing with THB, those people may suffer unexpected losses. Around 40% of OECD, EU, and BRIC (Brazil, Russia, India and China) jurisdictions with depositor compensation schemes have THB protection.

54. However, extending the scheme’s protection to cover THB could potentially impose significant costs on the scheme by adding more complexity of eligibility rules and significant time for processing entitlement applications when compensation does occur. As a result, the levy burden on industry would also increase to cover the additional liability associated with this protection, and this additional liability would introduce additional complexity in setting levies. Establishing the rules and systems for temporary high balance protection could put additional pressure on the current implementation timeline.

55. Considering both the benefits and the challenges of extending the scheme to cover THB when introducing the scheme in the planned timeframe, there are two options to progress the policy decision. One is to consider extending the scheme to cover THB in the post-implementation review of the DTA. This is preferred by the Reserve Bank as it provides the option of introducing this protection in the future while maintaining the priority of implementing the scheme within the timeframes envisaged. An alternative option we also provide below is to include a provision in the DTA allowing regulations to be developed to enable the scheme to cover THB. While such regulations would not need to be in place by late 2023, this provision could create a public expectation that THB will be covered, and that such regulations would be in place when the scheme is introduced. Given the pressures on the current

implementation timeframe, there would be risks in completing the regulations by the time the scheme is in place.

Managing risk to the scheme associated with transitional firms

56. Cabinet agreed in April that membership of the scheme will be compulsory for all licenced deposit takers. You have agreed that finance companies should be included in the regulatory perimeter and should be able to offer insured deposit insurance products, with the Reserve Bank managing moral hazard by imposing sufficiently robust regulatory requirements and risk-based pricing for deposit insurance (T2020/3517 and T2021/783 refers).

57. Alongside risk-based pricing for deposit insurance levies, we consider the existing prudential and supervisory tools available to the Reserve Bank are sufficient to manage moral hazard risk associated with finance companies, and potentially other higher risk deposit-takers during the transition period until prudential requirements under the DTA are fully developed and implemented. These tools include prudential guidance, limiting the growth of deposits, and more stringent capital and/or liquidity requirements. We are satisfied that the current legislation provides a sufficient legal basis for employing those additional tools. The Reserve Bank will closely monitor the behaviour and risk of the NBDT sector during the transitional period and employ appropriate tools as needed. This may imply significantly tighter regulation of some firms (for example, the Reserve Bank is likely to be less tolerant of rapid growth in a finance company when its deposits are or will shortly be insured).

Miscellaneous

58. We recommend that the Reserve Bank as manager of the scheme has the power to recover for the scheme any amount paid from the scheme fund in excess or error from the persons who received those funds.

Crisis management and resolution

Direction power for the Minister of Finance

59. Cabinet agreed in April that the Minister of Finance should have the ability to direct the Reserve Bank on the management of risks to public funds in a resolution, as a backstop if other factors (such as contractural rights available to the Minister, and the Reserve Bank's own concern to limit risks to public funds) had not proved sufficient, but left the statutory test and other details of this power for finalisation under delegated authority.

60. One issue that arises is whether actions by the Minister in the resolution regime should also consider the statutory purposes of the resolution regime that guide the Reserve Bank's use of resolution powers. There is a risk of inconsistency if the statutory purposes of the Minister are different to those of the Reserve Bank or undefined. For this reason, the draft Cabinet paper asks Cabinet to clarify that these purposes also apply to the Minister. This clarifies that the primary purposes of resolution powers relate to avoiding damage to the financial system and related matters, while also having regard to other factors including protecting public funds.

61. We propose that the direction power is available to the Minister where (and only where) there is a material risk to public funds as a result of other resolution actions. This (coupled with the need to consider the wider purposes of the resolution regime) is how

we recommend formulating the “statutory test” which Cabinet agreed would need to be met for the direction power to be used [DEV-21-MIN-0079 decision 58].

62. We are still to formulate process requirements for the use of the direction power. These will be designed to make it clear that this power is a “residual lever” rather than something that will be used for day to day management of an entity in resolution. We will provide further advice on this and other issues that arise in drafting.

63. This proposal has been discussed in some detail between Treasury and the Reserve Bank. The Reserve Bank would on balance prefer a regime where key resolution decisions require explicit consent from the Minister rather than a residual direction power, which is different to that agreed in April. In this regard, the Reserve Bank notes that where public funds are put at risk in a resolution, the most effective lever to manage the associated risk will generally be the contractual provisions that are used in the provision of any public support. However, the Reserve Bank considers that the alignment of the purposes applying to resolution actions by the Minister and Reserve Bank mitigate to some degree the risks associated with the proposed direction power.

64. Treasury considers that while specific contractual provisions between the Crown and the entity in resolution will generally support the management of fiscal risks associated with the use of public funds, there may be instances where such provisions prove limiting and do not afford the government an appropriate degree of flexibility. For this reason, Treasury supports a crisis management regime within the DTA that provides the Minister of Finance with an effective lever to fulfil their obligations under the Public Finance Act to prudently manage fiscal risks – albeit a residual lever with the safeguards and process requirements described above.

No Creditor Worse Off (NCWO)

65. As part of the resolution framework, the DTA will establish a mechanism to compensate creditors if a resolution of a deposit taker has left some creditors worse off when compared to an ordinary liquidation (the ‘no creditor worse off’ principle). The attached Cabinet paper seeks Cabinet decisions on key aspects of the NCWO framework and authorises you to take further detailed decisions on the NCWO mechanism under delegation. We will provide you with further recommendations on these aspects once Cabinet decisions have been taken.

Funding for resolution

66. To the extent that other resources available to absorb the losses in a resolution (e.g. shareholders, subordinated creditors, the deposit insurance scheme) have been exhausted, additional funding may be required to support the preferred resolution strategy.

67. For the resolution of many deposit takers, resolution funding will not be required. Financial stability will be preserved through the orderly wind down of a failed deposit taker and prompt reimbursement to depositors through deposit insurance.

68. However, for systemically important deposit takers, winding down may have broader economic and financial stability consequences, and it is the role of the resolution authority to implement resolutions that minimise these impacts. Depending on the circumstances in which the resolution plans are being executed, the Minister may elect to provide additional support measures to improve public confidence, or take alternative actions in the event a deposit taker is under stress (e.g. through a re-

capitalisation using public funds). In these instances, where there is unwillingness to impose losses on certain creditors, resolution funding may be required to achieve the desired resolution strategy.

69. As a general principle, the institutions that pose risks to financial stability, and directly benefit from financial stability, should be made to internalise the costs of the risks they pose. The existing regulatory framework ensures that these institutions already internalise some of these costs through requirements such as capital ratios, and outsourcing requirements. It may be appropriate for industry to bear some of the cost of resolutions, in cases where imposing remaining losses on creditors is expected to materially weaken financial stability. However, the Crown may elect to take resolution measures for other objectives such as social and economic concerns. Furthermore, financial stability benefits a broad range of society not just financial institutions.

70. The Financial Stability Board sets out three possible forms of resolution funding (besides simple public funding) – deposit insurance funds, pre-funded resolution funds, and temporary access to public funds supported by ex-post recovery mechanisms. New Zealand's deposit insurance scheme may contribute to resolution but any contributions it can make may not be sufficient to fund a resolution due to safeguards around the use of the scheme funds. Pre-funded resolution funds can have similar benefits to a deposit insurance fund and avoid having to impose levies on an already weak industry after a crisis. However, unlike deposit insurance funds (where the use is linked to the objectives of the scheme), the use of this fund can be more discretionary, making it harder to justify to industry. The size of the required resolution fund is hard to quantify, and assessing the opportunity costs of the earmarked resources will always be difficult. We do not support a pre-funded resolution fund for these reasons, coupled with the difficulty of imposing another levy on industry (alongside deposit insurance levies and potential supervision levies that may be applied in the future).

71. An ex-post recovery mechanism could be included in the legislation. This would preposition a levy making power to recover all or some of the public funds deployed as part of a resolution from deposit takers. Prepositioned resolution funding mechanisms transfer the contingent liability of resolution from Government to industry. This approach would mean that the levy power is prepositioned in advance, setting industry's expectation that the obligation to pay for a resolution may arise in the future, and enabling cost recovery without requiring new legislation to be passed. The legislation would not require that the levy power is used, or that all costs incurred in a resolution are recovered. While the details of the levy could be left to regulations, the legislation would need to contain relevant information on the levy including the purpose of the levy, persons to be charged, and factors relating to its calculation.

72. A pre-positioned levy (even if only raised ex-post) raises a number of potential concerns, including:

- Moral hazard and distortionary impacts: the existence of a resolution funding mechanism could increase moral hazard as creditors may expect to benefit from the funding made available. If a resolution levy is imposed, firms not requiring assistance are likely to bear a disproportionate amount of the costs as resolved entities may no longer be in existence because they have been wound up or acquired.

- Could undermine the resolution framework: a prepositioning resolution funding may incentivise overly frequent bail-out that would undermine the resolution framework. While this risk can be mitigated by placing conditions on the use of the levy-making power, these are subjective judgements.

- Lack of consultation and inconsistency across the sector: there has been limited consultation on funding for resolution. The option of establishing an industry resolution fund (alongside a DIS fund) was briefly canvassed in the second consultation and did not received support from submitters. Importantly, similar arguments for an ex-post resolution levy could also be applied to insurers and financial market infrastructures. Any work on levies to recoup public funds used should consider the merits of introducing a levy across the financial sector, rather than being limited to deposit takers.

73. In light of these concerns the Reserve Bank recommends further work on resolution funding is undertaken at a later date, likely as part of the post-implementation review of the DTA. This would enable a full public consultation on resolution funding, including on the option of an ex-ante resolution levy. In addition, the option of not progressing the levy would avoid worsening the already challenging timetable and resourcing for drafting the DTA. The Treasury sees merit in a prepositioned levy but appreciates the concerns set out above.

Carry over of existing statutory management provisions

74. Cabinet has previously:

- Agreed in principle that, where practicable, existing resolution powers currently available to a statutory manager be available to the Reserve Bank as resolution authority [DEV-19-MIN-0346 refers];

- Agreed 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 licenced deposit takers under delegated authority [Cab min reference to add]; and

- Noted that the significant resolution powers referred to include having the power to assume full powers of management of a deposit taker in resolution, sell or transfer all or part of the business of a deposit taker in resolution, and having the power to suspend payments of the deposit taker in resolution [Cab min reference to add].

i. Important statutory management provisions we recommend be carried across into the resolution regime

75. The more significant statutory management provisions that we currently recommend be carried across into the new resolution regime (with appropriate modifications) are:

- Section 122(1), which sets out the scope of the moratorium;

- Section 122(3), which provides the power to waive the moratorium;

- Section 127, which provides the power to suspend payment of debts and the fulfilment of obligations;

- Section 131, which provides the power to pay creditors in whole or in part; and

- Section 132, which provides the power to sell all of part of a distressed institutions business, or transfer all or part of that business to a bridging institution.

76. We discuss these provisions in more detail below.

ii. Sections 122(1) and 122(3)

77. Section 122(1) sets out the scope of the moratorium that applies to creditors' claims in statutory management. In summary, it states that no person shall (while the moratorium applies):

- commence or continue any action or other proceedings against that registered bank; and

- enforce debts against a registered bank (including by enforcing security interests over assets of the registered bank, or by taking steps to place the registered bank into liquidation or voluntary administration).

78. However, the moratorium only applies to obligations entered into before the statutory management has commenced, and the statutory manager may waive the application of the moratorium in whole or in part. The moratorium also does not affect the existence of any security interest or prevent proceedings to identify whether a right or liability exists (although such proceedings require leave of the statutory manager or court).

79. The moratorium also has a number of other exceptions (for example, to protect netting agreements).

80. Section 122(3) provides that a statutory manager may waive the application of the moratorium to any creditor or class of creditors in respect of the whole or any part of any claim of, or security interest held by, that creditor or class of creditors.

81. In properly modified form, these are essential provisions for the resolution regime. In particular, they avoid liabilities and security interests being enforced against a deposit taker in resolution, providing time for it to potentially be restructured in some manner. However, unless waived in whole or in part by the statutory manager, the moratorium remains in place for the duration of the statutory management. The potentially indefinite duration of the moratorium has been a longstanding concern of industry.

82. To address this issue, we recommend that:

- The moratorium be time limited to an initial period of 12 months; and

- Each time the moratorium is due to expire, the Reserve Bank may extend it (in whole or in part) for up to another 12 months, subject to the Reserve Bank being satisfied that this is necessary or desirable for the achievement of certain resolution objectives, namely:

- To ensure that the resolution of any licensed deposit taker is orderly; and

- To avoid significant damage to the financial system that could result from the failure of a licenced deposit taker.

83. In order to lift or extend the moratorium in this manner, the Reserve Bank would also be required to issue a notice that must be published on the Reserve Bank's website and in the Gazette.

84. We note that this approach to the duration of the moratorium is new, and may have implications for other parts of the resolution regime. As a result, we propose to test it further as part of the process of publishing an exposure draft of the Bill.

iii. Sections 127 and 131

85. Section 127 provides the statutory manager with the power to:

- Suspend in whole or in part the repayment of any deposit, or the payment of any debt, or the discharge of any obligation, to any person; and

- Cancel the obligation to provide funding to any person.

86. This power applies solely to debts and obligations established before the commencement of statutory management, and is subject to some small exceptions.

87. Section 131 provides the statutory manager with the power to:

- Pay, in whole or in part, any creditor or class of creditors of the registered bank;

- Make any compromise or arrangement with any creditor, or person claiming to be a creditor, of the registered bank; and

- Compromise all calls, debts and claims subsisting, or supposed to subsist, between the registered bank and any other person, and all questions relating to the assets of the registered bank, and give a complete or partial discharge.

88. In appropriately modified form, these are essential provisions for the resolution regime. In particular, when supported by the moratorium they are essential powers for restructuring the affairs of a distressed deposit taker, and implementing resolution options (including the partial freezing of creditors' claims in Open Bank Resolution).

iv. Section 132

89. Section 132 provides the statutory manager with the power to sell or otherwise dispose of the whole or any part of the business undertaking (including liabilities) of an institution in statutory management on such terms and conditions as they think fit.

90. This power includes the ability to establish a bridging institution to hold all or part of the business of the institution in statutory management, and the ability to sell or otherwise dispose of the bridging institution on such terms and conditions as the statutory manager sees fit.

91. In appropriately modified form, this is also an essential provision for the resolution regime. In particular, in conjunction with the other statutory management powers noted above it is an essential power for restructuring the affairs of a distressed institution. It also provides the power to effect a de facto bail-in of creditors, e.g. by shifting a failed institution's good assets, and a proportion of its liabilities, to a bridging institution (leaving the "bailed in" proportion of the institution's liabilities in a rump entity holding no, or only poor quality, assets).

v. Carrying across other statutory management provisions into the new resolution regime

92. We recommend that other existing statutory management provisions also be carried across into the new resolution regime (subject to appropriate updates and modifications consistent with other aspects of the new resolution framework). This includes important provisions that, for example, vest management of the distressed institution in the statutory manager, and give the statutory manager the powers of the board and the powers of shareholders in an annual general meeting.

93. We note that as the drafting of the new resolution regime continues to progress, there may be a need for further decisions on some of the specifics around how the existing statutory management provisions are carried across to the new framework. If so, we will seek your decisions on these matters in a separate briefing.

94. Internationally, management of small deposit takers that fail sometimes involves the use of liquidation (and deposit insurance payout) rather than the use of full resolution powers. We are still considering the feasibility of liquidation and payout in the New Zealand context, as well as the suitability of the resolution regime for smaller, non-systemic licensed deposit takers. We may subsequently seek further approvals to adapt the resolution regime to make it more suitable for resolutions of this nature.

Other matters

i. Use of Order in Council to place a deposit taker into resolution

95. We have considered a variety of options for the appropriate instrument for placing a deposit taker into resolution. These include a notice made by the Reserve Bank, a notice made by the Minister of Finance, or an Order in Council. We recommend that a deposit taker be placed into resolution by an Order in Council made on the advice of the Minister given in accordance with a recommendation of the Reserve Bank.

96. We consider that an Order in Council is the most appropriate instrument because:

- It ensures a role for the Minister of Finance in making the decision (which we think is important at the initial stage of deciding what high level approach should be taken when dealing with a distressed deposit taker);
- Using a legislative instrument like an Order in Council is more proportionate than using an administrative instrument like a notice, given the extremely significant legal implications of resolution for a deposit taker, its shareholders, and its creditors); and
- It aligns with existing New Zealand precedents (specifically, the statutory management regimes for insurers and financial market infrastructures, and for

other entities under the Corporations (Investigation and Management) Act 1989).

97. We are conscious of the concern that making Orders in Council can be more complicated and time consuming than making alternative instruments like notices. However, in the large majority of cases the Reserve Bank will have forewarning that a deposit taker is in difficulties, so these issues can be managed. In very rare cases where there is no forewarning that a deposit taker is in difficulties, it is also still possible to have Orders in Council made very rapidly, even if this requires some ordinary parts of the process to be truncated. As a result, we do not feel that these issues outweigh the arguments in favour of using Orders in Council here.

ii. Powers to obtain documents and information

98. To help facilitate the effective conduct of resolutions we recommend that the new resolution regime include a provision modelled on section 182 of the Insurance (Prudential Supervision) Act 2010. This provision provides the statutory manager of an insurer all of the powers a liquidator would have in a liquidation to access documents and information, and require certain parties to provide oral evidence.

99. We believe this is preferable to carrying over the equivalent provision in the Reserve Bank of New Zealand Act 1989 (section 150), which is not fully consistent with the powers applying in an ordinary liquidation (for example, it does not include the power to require certain parties to provide oral evidence).

100. We note that this power is intended primarily to allow for further investigation into the status of a distressed deposit taker, if that status cannot be determined by the deposit taker's existing records.

Content in Cabinet Paper

101. In addition to decisions taken under delegated authority, we propose certain decisions are taken by Cabinet. The decisions are to significant policy aspects relating to the crisis management framework and include:

- Resolution objectives
- Proposals to limit legislative reforms on bail-in to contractual bail-in and the use of resolution powers - these proposals represent a departure from Cabinet decisions in April which approved a statutory bail-in regime
- The use of the deposit insurance fund in resolution and applicable safeguards. Proposals build on existing Cabinet decisions and include:
    a. that the fund may contribute to resolutions provided that the resolution protects insured depositors, and contributions will at all times not exceed what the scheme would have paid in a liquidation and payout net of recoveries; and
    b. that contributions permitted by the fund to resolution include contributions to No Creditor Worse Off payments, subject to compliance with the safeguards described above

- Key features of the No Creditor Worse Off mechanism to be included in the DTA and appeal rights in resolution.

- Constraints on the ability of creditors to enforce rights against deposit takers in resolution[3]

102. A draft Cabinet paper is attached containing recommendations that we propose are taken by Cabinet. Subject to feedback, we will finalise the attached Cabinet paper for consideration in early October.

Next Steps

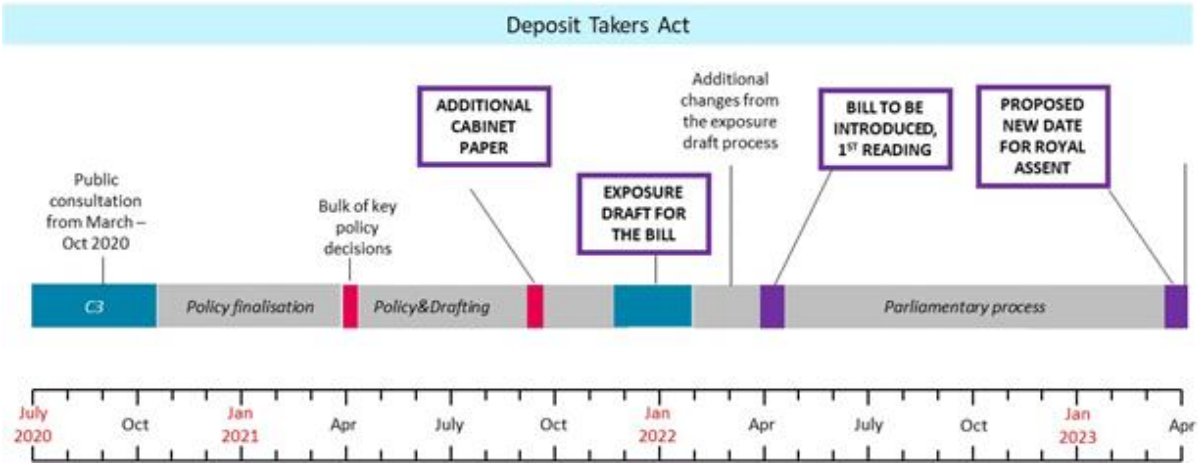
103. Once we have received your agreement to these changes, we will finalise the attached draft Cabinet paper. After Cabinet, we will provide some further advice (as noted above) and work with the Parliamentary Counsel Office to prepare the Deposit Takers Bill for the exposure draft stage. The following table sets out two sets of proposed dates for the Cabinet process (given the October recess). The faster track should lead to an exposure draft being available a week or two earlier but requires a ministerial consultation period of less than 10 days. We note there is a RBNZ meeting with you scheduled for 16 Sep so have suggested starting Ministerial consultation shortly after that. We would also be happy to brief interested ministers.

Milestone	**Faster track**	**Alternative track**
Ministerial consultation	16 Sep	20 Sep
Comments/changes back to Reserve Bank	20 Sep	4 Oct
Submission to Cabinet Office	23 Sep	14 Oct
At Dev	29 Sep	20 Oct
Cabinet consideration	4 Oct	26 Oct
Exposure draft	Late 2021	Late 2021
First reading	Late Q2 2022	Late Q2 2022

104. The exposure draft of the DTA will incorporate the decisions being taken now as well as those taken in April, including certain consequential amendments to other legislation (such as the PFA authority for spending in a financial crisis which Cabinet agreed in April).

[3] We note that this includes a proposed stay on the exercise of close out rights under derivatives contracts. This will supersede existing provisions in the Reserve Bank of New Zealand Act 1989 which a number of other Acts cross refer to (including the Companies Act 1993, Corporations (Investigation and Management) Act 1993, and Personal Property Securities Act 1999). To avoid making any substantive changes to these other Acts, we propose that these superseded provisions be shifted from the Reserve Bank of New Zealand Act 1989 into another Act (possibly the Corporations (Investigation and Management) Act 1993), and the relevant cross references in other affected legislation be updated accordingly.

105. As noted in July (RBNZ #5832 refers) the exposure draft process is expected to be followed by a 12 month period for passage of the DTA through the house, with a target of implementing deposit insurance by late 2023.



Recommendations

106. It is recommended that you:

a) **note** that Cabinet has previously agreed to proposals for the framework for regulating and supervising deposit takers, and the introduction of a deposit insurance scheme, for inclusion in a Deposit Takers Act [DEV-21-MIN-0076, DEV-21-MIN-0077, DEV-21-MIN-0078, and DEV-21-MIN-0079]

Noted

b) **note** that Cabinet has delegated you (either jointly or in consultation with the Associate Minister of Finance and the Minister of Commerce and Consumer Affairs) the authority to further clarify and develop other policy matters relating to previous Cabinet decisions on the Deposit Takers Act

Noted

c) **note** that further Cabinet decisions will be required on significant policy aspects relating to the crisis management framework in order to progress the drafting of an exposure draft of the Deposit Takers Bill and a draft Cabinet paper is attached for your consideration and feedback

Noted

d) **note** that the draft Cabinet paper contains proposals to initially limit legislative reforms on bail-in to contractual bail-in which represents a departure from Cabinet decisions in April also approving a statutory bail-in regime

Noted

e) **note** that the draft Cabinet paper contains proposals that permit the deposit insurance fund to contribute to resolution (including to no creditor worse off payments) provided the resolution protects insured depositors, and contributions can be no more than what the deposit insurance scheme would have paid in a liquidation net of recoveries.

Noted

The prudential and supervisory framework

f) **agree** that it is appropriate that information gathering powers and on-site inspection powers are included in relevant section of the Deposit Takers Act, rather than consolidated into the Reserve Bank of New Zealand Act 2021.

Agree/disagree

g) **agree** to include decision making principles to guide the use of regulatory powers, subject to drafting, but likely to be along the lines of: the desirability of sound governance of deposit takers, the desirability of effective risk management, and the value of disclosure that helps stakeholders monitor deposit takers, in addition those already approved by Cabinet.

Agree/disagree

h) **agree** to the approach to penalties outlined below, with the following specifics

   i. a 3-tiered approach to criminal penalties for breaches of the DTA as shown in Table 1 above;

   ii. provides for pecuniary penalties for breaches of standards which scale relative to the size of the deposit taker;

   iii. provides for civil penalties for directors who have breached duties under the DTA;

   iv. provides for a maximum civil penalty of $1 million for breaches of director duties.

Agree/disagree

The Deposit Insurance Scheme

i) **agree** to change the name of the Deposit Insurance Scheme to 'the Depositor Compensation Scheme'

Agree/disagree

j) **agree** that the trigger in the DTA for the Scheme to compensate eligible depositors will be along the following lines:

- when a licenced deposit taker is placed into liquidation on the application (or with the consent) of the Reserve Bank; or
- if the Reserve Bank is satisfied that:
  i. the licenced deposit taker is non-viable according to the statutory tests under the resolution framework, and
  ii. eligible depositors would not otherwise have access to protected deposit amounts within a reasonable timeframe in light of the Bank's purposes and functions under the scheme.

Agree/disagree

k) **note** that Cabinet agreed that if the balance of the deposit insurance scheme fund is not sufficient to meet the scheme's payment obligations, the Crown will provide the required funding to the scheme to satisfy the scheme's payment obligations

Noted

l) **agree** that to give effect to Cabinet's agreement noted at recommendation above, the DTA provide a permanent legislative authority (for the Minister of Finance) to spend public money without further authority when providing funding to the Scheme

Agree/disagree

m) **agree** that the Minister of Finance may determine whether all or part of the funding provided to the Scheme by the Crown be repaid, and the terms and conditions

(including conditions in regard to the level and timing of any interest payment) that apply to any repayment obligation

Agree/disagree

n) **agree** that, to the extent that it is necessary or desirable for the Reserve Bank to fulfil its function as manager and administrator of the Scheme, the DTA is to include provisions to allow the Reserve Bank to establish new deposit accounts with another deposit taker on behalf of eligible depositors

Agree/disagree

o) **agree** that the exposure draft will provide two options to test with industry and the Office of Privacy Commissioner about how to deal with privacy issues related to sharing personal information for the purposes of facilitating reimbursement to eligible depositors under the scheme:

    i. statutory override of the Privacy Act 2020 for the limited purpose of allowing the DIS to obtain personal information relevant to depositors' entitlements to compensation without seeking their consent first

    ii. requiring all deposit takers to amend deposit takers' existing product terms and conditions with eligible depositors

Agree/disagree

p) **agree** that the scheme fund can be applied by the Reserve Bank for the purpose of covering actual and reasonable scheme operating costs

Agree/disagree

q) **agree** that scheme operating cost will be included in the funding agreement between the Minister and the Reserve Bank

Agree/disagree

r) **agree** the Reserve Bank should publish the financial position of the scheme fund annually

Agree/disagree

s) **agree** that protected deposits under the Scheme will include debt securities repayable in New Zealand dollars governed by New Zealand law

Agree/disagree

t) **agree** that debt securities commonly referred to as debentures, commercial papers, bonds and capital notes will not be protected deposits

Agree/disagree

u) **agree** that the scope of the product boundary for protected deposits (including the list of excluded products) may be adjusted through regulations made on the advice of the Minister of Finance by Order in Council

Agree/disagree

v) **agree** that trustees of New Zealand law governed trusts are eligible investors under the scheme

Agree/disagree

w) **agree** the following persons will not be eligible investors under the scheme for deposits held in their own right:

- large corporations and unincorporated bodies with the threshold for "large" to be based on the meaning of this term in the Financial Markets Conduct Act 2013 (i.e., $5 million annual turnover or net assets for last two years)
- licenced deposit takers, licenced insurers, operators of FMIs
- in relation to a failed licenced deposit taker, the associated persons and directors of that deposit taker
- government agencies based on the meaning of this term in the Financial Markets Conduct Act 2013, but school boards and tertiary education institutions (within the meaning of section 7 of the Crown Entities Act 2004) are eligible investors under the Scheme

Agree/disagree

x) **agree** that persons excluded from eligibility for the scheme may be adjusted through regulations made on the advice of the Minister of Finance by Order in Council

Agree/disagree

y) **agree** that whether DIS should extend the coverage to Temporary High Balances of eligible depositors will be considered in a post-implementation review of the DTA **(Reserve Bank preferred)**

Agree/disagree

OR

agree that the DTA includes a provision for regulations to be made on the advice of the Minister of Finance by Order in Council to provide additional cover for certain temporary high balances

Agree/disagree

z) **note** the moral hazard risk of the non-bank deposit takers (NBDTs) sector being included in the scheme can be managed using the existing prudential and supervisory tools until prudential requirements under the DTA are fully developed

Noted

aa) **agree** that the DTA includes a provision to allow the Reserve Bank as manager of the scheme to recover for the scheme any amount paid from the scheme fund in excess or error from the persons who received those funds

Agree/disagree

The crisis management and resolution framework

bb) **note** that Cabinet agreed [DEV-21-MIN-0079 decisions 55-59] the Minister would have the ability to direct the Reserve Bank on the management of public funds in resolution, with an appropriate statutory test

Noted

cc) **agree** that the Minister of Finance will be restricted from using the direction power except where there is a material risk to public funds as a result of any other resolution action

Agree/disagree

dd) **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), 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)

Agree/disagree

ee) **note** that the attached Cabinet paper proposes that the statutory purposes of the resolution regime will also apply to the Minister when making decisions under that part of the Act, forming part of the statutory test for the use of this power

Noted

ff) **note** that further recommendations will be provided for you to take further detailed decisions once Cabinet decisions have been taken on the No Creditor Worse Off (NCWO) mechanism

Noted

gg) **agree** that further work on resolution funding is undertaken at a later date, likely as part of the post-implementation review of the DTA **(Reserve Bank preferred)**

Agree/disagree

OR

hh) **agree** that the DTA includes a provision for regulations to be made on the advice of the Minister of Finance by Order in Council providing for levies to be paid by deposit takers after a resolution to recover all or some of the public funds deployed as part of a resolution

Agree/disagree

ii) **agree** that the following statutory management provisions in the Reserve Bank of New Zealand Act 1989 be carried across into the new resolution regime (with appropriate modifications):

- Section 122(1), which sets out the scope of the moratorium;
- Section 122(3), which provides the power to waive the moratorium;
- Section 127, which provides the power to suspend payment of debts and the fulfilment of obligations;
- Section 131, which provides the power to pay creditors in whole or in part;
- Section 132, which provides the power to sell all of part of a distressed institution's business, or transfer all or part of that business to a bridging institution.

Agree/disagree

jj) **agree** that:

- The moratorium established by carrying across section 122(1) into the new resolution regime be time limited to an initial period of 12 months; and
- Each time the moratorium is due to expire, that the Reserve Bank may extend it (in whole or in part) for up to another 12 month period, subject to the Reserve Bank being satisfied that this is necessary or desirable for the achievement of resolution objectives (e.g., to ensure that the resolution of the licenced deposit taker is orderly).

Agree/disagree

kk) **note** that the proposed approach to the moratorium set out in recommendation gg is designed to address a concern raised by industry, but may have impacts on other aspects of the resolution regime, so will be subject to further testing as part of the exposure draft process

Noted

ll) **agree** that the statutory management provisions not referred to in recommendation ii also be carried across into the new resolution regime (subject to appropriate updates and modifications consistent with other aspects of the new resolution framework)

Agree/disagree

mm) **note** that as the drafting of the new resolution regime continues to progress, there may be a need for further decisions on precisely how other aspects of the existing statutory management provisions are carried across to the new resolution regime (and that Cabinet has previously agreed to that you may make such decisions under delegation)

Noted

nn) **note** that when consulting on the Exposure Draft, the Reserve Bank will seek comments on the suitability of the resolution regime for smaller, non-systemic licensed deposit takers (e.g., credit unions) and may subsequently seek further approvals from Cabinet or under delegated authority

Noted

oo) **agree** that licenced deposit takers be placed into resolution via an Order in Council made on the advice of the Minister of Finance given in accordance with a recommendation of the Reserve Bank

Agree/disagree

pp) **agree** that the Reserve Bank have all of the powers a liquidator would have in a liquidation to access documents and information, and require certain parties to provide oral evidence

Agree/disagree

Hon Grant Robertson
Minister of Finance

Geoff Bascand
Deputy Governor/GM Financial Stability
Reserve Bank of New Zealand

09/09/2021

Bryan Chapple
Deputy Secretary
The Treasury