RESPONSE ON THE DEPOSIT TAKERS ACT: CRISIS MANAGEMENT CONSULTATION

ANZ BANK NEW ZEALAND LIMITED

22 November 2024

INTRODUCTION

ANZ Bank New Zealand Limited (**ANZ**) thanks the Reserve Bank of New Zealand (**Reserve Bank)** for the opportunity to provide feedback to the Deposit Takers Act: Crisis Management Issues Paper (**Issues Paper**). ANZ appreciates the work spent developing the discussion points in the Issues Paper and the Reserve Bank's engagement with industry and ANZ to support it.

ANZ is aware that the New Zealand Banking Association (**NZBA**) has also provided an industry response to the Issues Paper. ANZ has contributed to and supports the relevant aspects of that response.

CONTACT DETAILS

ANZ welcomes the opportunity to discuss our submission with Reserve Bank officials. Please contact Penny Dell, Treasurer at S9(2)(a) if you would like to discuss the contents of this response.

CONFIDENTIALITY

ANZ consents to the publication of this submission, with certain aspects withheld to protect the privacy of natural persons under the Reserve Bank's publication of submissions policy, being that section marked for redaction, italicised and within square brackets (i.e. ["…"]), as identified in 'Contact Details'.

SUMMARY

ANZ wishes to make the following key points/recommendations:

a) *General comments*

- ANZ broadly supports the Reserve Bank's establishment of a more comprehensive crisis management regime under the Deposit Takers Act 2023 (**DTA**) that would more closely align New Zealand's approach to crisis management with those countries that comply with the Financial Stability Board's (**FSB**) Key Attributes (**Key Attributes**).
- We acknowledge that, as "foreign-owned banks play a major role in the New Zealand financial system", New Zealand needs local standalone resolution options. Those options should consider the full New Zealand regulatory landscape.

b) *Single comprehensive regime*

- We strongly recommend that changes to existing crisis management tools (including Open Bank Resolution (**OBR**) and bank separation under BS11 Outsourcing Policy (**BS11**)) are considered contemporaneously with the Reserve Bank's proposed additions to its crisis management toolkit, including Depositor Compensation Scheme (**DCS**), bail-in and sale of business and Group led resolution tools.
- We also recommend that, as far as is reasonably practical, crisis management standards and related obligations are documented in a single comprehensive standard from the outset.
- By identifying and considering at the same time which functionality might be required and how it might be used in a single standard (at the initial policy development stage), we believe potential conflicts between tools and unnecessary uncertainty and complexity across the regime could be significantly reduced.

c) *Better alignment with Key Attributes*

- While some provisions of Part 7 of the DTA already create a degree of inconsistency with the Key Attributes, we are concerned that certain Reserve Bank proposals would move New Zealand's crisis management regime even further away from what is considered international best practice.
- The Reserve Bank is provided with wide discretions under the DTA (when compared with other international regimes) and, without clear guidance as to how those discretions might be exercised, it will be difficult for deposit takers and other industry participants (such as investors) to gauge how differently the Reserve Bank might act when compared to other regulators from

FSB compliant regimes, and consequently what the associated risks are for New Zealand deposit takers and investors.

d) Statutory & contractual bail in

- We do not consider that a statutory bail-in power is required under the DTA. However, if the Reserve Bank determines that certain instruments should be able to be bailed-in, in ANZ's view that that decision should be informed by:
    - the low likelihood of a resolution event, given the risk tolerance for a deposit taker failing was set at 1-in-200 years when the Reserve Bank determined the incoming capital requirements for New Zealand deposit takers;
    - the availability of a Group led resolution option for the largest deposit takers. Parent entities of the Australian owned banks are already required to issue capital instruments subject to bail-in for their New Zealand subsidiary's assets; and
    - there are already suitable bail-in powers available under the DTA: contractual and structural bail-in.

DETAILED RESPONSES

1. Do you have any views on our proposed approach to implementing the crisis management framework under the DTA? Are there any factors we should, or should not, take into account when implementing the framework?

A comprehensive and harmonious framework

1.1 It will be critical that New Zealand's deposit taker crisis management strategies and tools operate clearly, simply and harmoniously throughout the crisis management stages - from business as usual operation and planning through to resolution. To achieve this, a single, comprehensive regime that is not unduly complex is required.

1.2 For these reasons, we strongly recommend that changes to existing crisis management tools (including OBR and bank separation under BS11) are considered contemporaneously with the Reserve Bank's proposed additions to its crisis management toolkit, including its approach to DCS, bail-in, sale of business and Group led resolution. We know, from previous experience, that taking a piecemeal approach to developing crisis management tools (such as OBR and bank separation under BS11) greatly increases the cost, complexity and difficulty of implementation and ongoing compliance.

1.3 A more holistic approach to resolution design, would, for example, enable far greater clarity regarding the purposes and uses for an integrated OBR/DCS resolution tool. In ANZ's response to the Reserve Bank's Non-Core Standards Consultation (para 110.2), we query the rationale for requiring the large five banks to implement an integrated OBR/DCS resolution tool, in light of the fact that liquidation and an upfront payout to depositors from the DCS seems highly unlikely. We can see that this rationale might include the Reserve Bank wanting to be able to use an integrated OBR/DCS tool to support a sale or bridge institution by transferring insured deposits to the new entity and leaving behind the "frozen" deposits. However, if an integrated OBR/DCS tool was to be used for the purpose of transfer (as opposed to payout), we would expect it to be designed differently (i.e. any insured amounts would need to split off from the account as opposed to the account at the failing entity remaining open). Being clear on the functionality required to achieve resolution will help avoid confusion and unnecessary compliance costs or rework.

1.4 For similar reasons, and as far as is reasonably practical, from the outset all crisis management requirements (including pre-positioning) should be documented in a single comprehensive standard that covers crisis preparedness, recovery and exit planning and resolvability. Instead, the current round of consultation for non-core standards under the DTA maintains existing and new resolution tools as separate standards.

1.5 If separate standards are retained, we would have broad concerns regarding:

- Efficiency impacts of deposit takers having to comply with multiple resolution standards.
- Uncertainty created as to what will happen at the time of failure in relation to which tool is used and how it might work together with other tools.
- Risk of conflict between standards, given the high degree of complexity currently involved, particularly in light of historical challenges in aligning existing resolution standards.
- Risk of additional rework and other unnecessary costs both at the time the separate standards are implemented and when a single crisis management standard is developed (as proposed in the Issues Paper).

1.6 In practical terms, we are suggesting that the Reserve Bank:

- Bring forward the timing for development of a single crisis preparedness / crisis management standard.
- To the extent required, extend the date for full Depositor Compensation Scheme (**DCS**) implementation to align with implementation of the full suite of resolution tools (refer to our proposal for an interim approach to DCS in paragraph 110.3 of our Submission on the Non-Core Standards Consultation).

1.7 On a similar note, we recommend that the Reserve Bank also brings forward the development of its Statement of Approach to Resolution (**SoAR**) and the creation of its individual deposit taker resolution plans. This would enable any remaining practical challenges to be identified and solved for early on (as opposed to during implementation, or worse, during application in a crisis), which would better support the development of Reserve Bank guidance and deposit taker implementation.

Competition and investor impacts

1.8 From an overseas investor perspective, the simplicity of New Zealand's crisis management framework will be key. If it is too complex for investors to readily understand, overseas investors might not invest (particularly where New Zealand's crisis management framework does not follow international best practice).

1.9 We disagree with the Reserve Bank's assessment that its proposals support competition because they will enable deposit takers to enter and exit the market in a timely and efficient manner without significant damage to financial system (para. 25).

1.10 From a competition perspective, the current proposals appear more likely to significantly raise costs of compliance and regulatory uncertainty, both of which increase barriers to market entry and follow-on investment.

2. Do you have any comments on our proposed approach to dealing with distressed deposit takers under the DTA? Are there any alternative approaches we should be considering?

Better alignment with Key Attributes

2.1 We agree that, notwithstanding that "foreign-owned banks play a major role in the New Zealand financial system", New Zealand needs local standalone resolution options for New Zealand owned, as well as branches and locally incorporated subsidiaries of foreign owned, deposit takers to ensure that the DTA's statutory purposes are met.

2.2 However, the number of foreign owned bank subsidiaries and branches in New Zealand still raises the practical importance of ensuring that New Zealand's crisis management framework aligns with, and leverages, international best practice. The failure of several United States' regional banks and the merger of Credit Suisse in early 2023 has shown that crisis management tools that have been developed in the aftermath of the Global Financial Crisis can be used successfully and mitigate wider market contagion.

2.3 ANZ supports the development of a crisis management regime that more closely aligns New Zealand's current regime to the Key Attributes and, consequently, to all those G20 countries which comply with the Key Attributes, in particular Australia given the ownership structure of the largest banks in New Zealand including ANZ.

2.4 The Key Attributes require the following features for an effective crisis management framework.

- Simple and clear crisis management objectives for both rule setting and regulatory decision making.
- Clear delineation between the business as usual, recovery and exit and resolution stages.
- Appropriate and transparent triggers to move between stages, with the trigger for resolution being non-viability of the deposit taker.
- Appropriate and ongoing engagement, detailed forward planning and testing between home and host resolution authorities.
- Detailed regulatory guidance that ensures stakeholders have a clear understanding of the basis on which home and country regulators would exercise their discretions.
- A crisis management group with the objective of enhancing preparedness for, and facilitating the management and resolution of, a cross-border resolution event.

2.5 While we recognise that certain sections of Part 7 of the DTA embed a degree of inconsistency with the Key Attributes (e.g. the grounds upon which a deposit taker may be resolved extend well beyond non-viability), we are concerned that the effect of the Reserve Bank's consultation proposals would be to move New Zealand's crisis management regime even further away from international best practice. To the extent permitted under the DTA, we believe it is very important that consistency with the Key Attributes is achieved. Our specific concerns are further explained in paras 2.6 to 2.12 below.

Objectives for rule setting and decision making

2.6 Section 259 of the DTA sets out Part 7's specific purposes for crisis management and resolution. In para. 52, the Reserve Bank outlines its own vision for its crisis management framework - being: effectiveness; flexibility and optionality; timeliness, preparedness and cooperation. While there are some links between s.259 and the Reserve Bank's own vision, overall, the relationship between the two appears unclear. We believe that having two sets of considerations (Reserve Bank and DTA) builds in an extra layer of uncertainty regarding how the Reserve Bank will exercise its discretion or set rules in an already complex and multilayered set of statutory purposes for crisis management.

Clear delineation between stages

2.7 The Key Attributes provide for clear delineation between crisis management stages (being business as usual, recovery and exit and resolution). This delineation is important when determining the

point at which the deposit taker enters in or out of resolution and who bears responsibility for decision making and managing the affairs of the deposit taker.

2.8 While the diagram in para. 51, Table C, separately identifies all resolution tools, the Reserve Bank states in paragraph 235 that "recovery and resolution processes are likely to overlap in practice". We are concerned that without clear segregation between stages there might be confusion over who is responsible for decision making, which might lead to delay at the point of resolution. It would be helpful for the Reserve Bank to confirm that it intends to treat "recovery and exit" and "resolution" as operationally separate.

Transparent triggers for moving between stages

2.9 Triggers for resolution under paragraph (a) of s.280 of the DTA extend well beyond non-viability, subject to the Reserve Bank being "satisfied that there is no reasonable prospect of the matters that apply under paragraph (a) being adequately dealt with to the [Reserve Bank's] satisfaction in a timely and orderly way other than through resolution."

2.10 The Key Attributes require appropriate and transparent triggers to move between stages, with the trigger for resolution being the non-viability of the deposit taker. Some FSB compliant regimes go further to require non-viability to be evidenced by an external assessment.

2.11 The Reserve Bank has been afforded unusually wide discretion under the DTA to recommend resolution. Without clear guidance as to how that discretion might be exercised, the triggers for resolution lack the necessary transparency required under the Key Attributes. It will be difficult for deposit takers and other industry participants (such as investors) to gauge how the Reserve Bank might act when compared to other regulators from FSB compliant regimes, and consequently it will be difficult for them to assess what the associated risks are when investing in New Zealand deposit takers.

2.12 Additionally:

- To reduce complexity and uncertainty, we recommend there be a hierarchy of resolution options and/or a clear indication of the Reserve Bank's preferred resolution tool for each deposit taker. As relevant, this should be resolution of the group as a whole in the first instance, followed by bail-in and transfer/ sale or insolvency (based on size / systemic importance). This would be similar to the United Kingdom and Australian models.
- It is unclear whether a direction order is intended to automatically trigger bank separation under BS11. If this is the case, further thought should be given to the resolution hierarchy having regard to Group led resolution and bank separation under BS11, and how that might work in practice under the DTA.
- We would like to also better understand the grounds on which the Reserve Bank might recommend the end of resolution under s.282.

Engagement between home and host resolution authorities

2.13 We strongly support the Reserve Bank's inclusion of Group led resolution as an appropriate resolution tool for foreign owned deposit takers. We also support the ongoing engagement between APRA and the Reserve Bank on crisis management, particularly through the 'Crisis Management Group'.

2.14 We recognise that the SoAR (described in para. 42) will include information on the Reserve Bank's approach to cooperation with Australian financial authorities, however, that document will not be made available to deposit takers until mid-2029 (a full year after the DTA comes into force). We feel this is too late (see our earlier comments in para 1.7).

2.15 The Issues Paper refers to the 2010 Memorandum of Cooperation on Trans-Tasman Bank Distress Management between APRA and the Reserve Bank. In light of more recent changes to the FSB's crisis management framework and Australia's crisis management framework and now the Reserve Bank's own proposed changes, we are keen to understand whether APRA and the Reserve Bank have plans to revisit this Memorandum, to ensure it remains fit for purpose.

2.16 It would also be helpful to understand whether APRA and the Reserve Bank plan to develop institution specific cross border cooperation agreements for each key foreign owned bank (along the lines recommended under Annex 2 of the Key Attributes).

3. Do you agree with our assessment of the costs and benefits of a potential statutory bail-in power? Are there additional costs or benefits we should consider? Do you have any view on the need for statutory bail-in powers given the structural and contractual bail-in options are already available with the powers under the DTA?

3.1 We do not consider that a statutory bail-in power is required. However, if the Reserve Bank is of the view that certain instruments should be able to be bailed-in, ANZ considers that appropriate tools that could be applied to deposit takers proportionally already exist under the DTA, contractual and structural bail-in.

Inter-relationship of capital rules and resolution

3.2 Capital and resolution are inter-connected and should be considered as a package. The purpose of the capital adequacy requirements is to determine the amount and form of capital that will be the first to absorb losses, both on a going concern basis and in resolution. The Reserve Bank stated in its Capital Review Regulatory Impact Assessment and Cost Benefit Analysis that the "capital review sets the risk tolerance at a level equivalent to approximately a 1-in-200 year chance of a financial crisis". The ongoing costs of resolution tools should reflect that the likelihood of resolution is, as Reserve Bank has stated, "very small"[1].

3.3 As outlined in the Issues Paper, a key recovery option for foreign owned deposit takers is a Group led resolution. This approach, which ANZ strongly supports, further increases the improbability of needing to use any DTA statutory bail-in power. The parent banks of New Zealand's domestically-systemic banks (**NZ D-SIBs**) are all subject to APRA's capital and resolution requirements. Under these requirements, the parent banks are required to issue sufficient regulatory capital instruments for their banking group, including their NZ D-SIBs, that could be bailed-in at the point of non-viability of the group.

3.4 We acknowledge the Reserve Bank's stated position that it will not be revisiting previous decisions made during the capital review on contractual bail-in features in capital instruments. However, we do not believe this aligns with the effectiveness and timeliness principles for developing the crisis management framework.

3.5 The increasing capital requirements have significantly increased capital funding costs for New Zealand deposit takers and decreased the likelihood of a resolution event. This is important context when considering bail-in, as the likely additional cost of any instrument subject to bail-in is approximately 20 basis points (relative to the same instrument with no bail-in).

Preference for contractual bail-in

3.6 A statutory bail-in power would need to respect the shareholder and creditor hierarchy and thus extend to capital instruments (refer to Key Attribute 5.1). We are not aware of any precedents globally where senior ranking instruments were subject to bail-in and capital instruments were not. Such an approach would add significant complexity to resolving a deposit taker in an orderly manner and likely generate significant claims on a resolution authority under the no shareholder or creditor worse off (**NCWO**) safeguard (refer DTA, part 7, sub-part 9 and Key Attribute 5.2). That risk of creditor claims would also place a high reliance on, as any application of statutory bail-in would, the accuracy of valuations at the point immediately before entering resolution[2].

[1] Capital Review - Regulatory Impact Assessment and Cost-Benefit Analysis 2019, page 8.
[2] We understand that the European resolution framework also has a NCWO principle. Valuations and assessment against that principle for certain European banks that have failed (e.g. Banco Popular Español) took several years to finalise.

3.7 If statutory bail-in was to apply to capital securities, as implied in the Issues Paper, it would seem that the Reserve Bank is contemplating bail-in in some form for capital securities. If so, the tool already available under the DTA, contractual bail-in, should be revisited.

3.8 Any decision on the form of bail-in should be driven by operational considerations in New Zealand, including effectiveness and the allocation of risk.

3.9 The Reserve Bank's reasons for not permitting contractual bail-in features during the Capital Review (Issues Paper – Box 4, page 47) did not consider the benefits of contractual bail-in relative to statutory bail-in, including:

- Contractual bail-in could be applied in a proportional manner across the spectrum of deposit takers reflecting that the resolution approach for certain entities will be liquidation, rather than bail-in.
- As the contractual terms would clearly set out the triggers and terms on which bail-in would occur, and investors have consented to those terms when purchasing the instrument, bail-in could be executed in a timely manner with likely less reliance on the NCWO safeguard as the valuation related risks would be transferred from the resolution authority to investors.
- As the Reserve Bank has acknowledged on page 49 of the Issues Paper, contractual bail-in can be "operationally simpler to execute".
- If conversion to equity occurs at the parent holding company entity level, bail-in could occur earlier, potentially avoiding a resolution event at the operating entity level altogether[3]. This is also consistent with maximising the effectiveness of the transfer of business powers contained in the DTA.

Trans-Tasman considerations

3.10 Although investors require a higher return on instruments that include bail-in features, the decision to remove that feature from eligible capital instruments during the capital review significantly increased ANZ's capital funding costs. This is because APRA requires a bail-in feature in instruments that contribute to their capital rules whereas Reserve Bank does not allow it. There is no capital instrument that can be issued to meet both APRA's and the Reserve Bank's requirements. If the Reserve Bank was to reconsider contractual bail-in in such a way that addresses this, the cost of bail-in to support resolution could be mitigated.

3.11 Issuing instruments subject to bail-in to our parent bank, either in the form of capital instruments or senior unsecured debt, is not currently a viable option for ANZ given APRA's restrictions on ANZ Banking Group Limited (**ANZBGL**). It is prohibitively expensive to issue capital instruments to our parent bank as ANZBGL is required to take a full deduction from their Level 1 common equity tier 1 (**CET1**) for any additional capital investment in ANZ. Non-equity exposures, including senior unsecured debt, are limited by APRA to 5% of ANZBGL's Level 1 tier 1 capital.

3.12 If the Reserve Bank's principal concern with contractual bail-in is "the Trans-Tasman structure and unlisted nature of D-SIBs" there are other potential structuring options that should be explored prior to discounting contractual bail-in altogether. For example, utilising structural subordination for issuance from an intermediary holding company (as ANZ did in September 2024), which can facilitate internal bail-in of TLAC at the operating entity level, and allow the ultimate holding company to deliver its shares so any bail-in of external investors does not impact the direct ownership of the failing New Zealand deposit taker. These structures support resolution of the group as a whole, the single point of entry resolution model and significantly simplify the issues created through statutory bail-in. Holding companies are used extensively in the United Kingdom and the United States to support resolution.

[3] Certain Credit Suisse holding company issued instruments were bailed-in despite the operating entity never entering resolution.

Senior ranking debts

3.13 Given the Reserve Bank's broad powers to trigger resolution under the DTA and the likelihood of a resolution event being significantly diminished following the Reserve Bank's capital rule changes, ANZ does not consider it necessary that any bail-in framework should extend to senior ranking instruments. With this context, if a suitable bail-in framework was introduced and the Reserve Bank's broad powers to trigger a resolution remain, we would question whether the retention of OBR and/or its integration with the DCS is even necessary.

3.14 If a senior ranking bail-in funding instrument was introduced, it would risk further diluting liquidity in New Zealand deposit takers wholesale funding instruments by generating yet another class of instrument and an increase in complexity during resolution.

Other considerations

3.15 In addition to the above comments, there are certain other matters that are important to consider with regards to the implementation of any bail-in framework.

- Credit rating agencies have well-established criteria for bail-in instruments that should be factored in from a cost mitigation perspective.
- The approach that will be taken with regards to the NCWO safeguard while there is co-existence of pari passu ranking instruments and some are subject to bail-in and others are not. This was observed in the United Kingdom's implementation of bail-in and limited the ability to bail-in the new securities. This would need to be very carefully navigated.
- The amount of equity and/or debt instruments that are subject to bail-in should have regard to the "very small" likelihood of such a feature being used.

4. Do you have any view on the potential new crisis preparedness requirements (i.e., recovery and exit planning, and resolvability)? If these requirements were imposed, do you have any initial comments on how they should be designed?

Recovery and exit planning

4.1 The Consultation states that the recovery and exit planning requirements "would mostly be principles based" (para. 223), which would reflect the approach taken under the Key Attributes (and adopted by other FSB compliance regimes).

4.2 However, the essential elements described in para 220 appear very specific (as opposed to principles-based). We are concerned that these are likely to result in tick box planning, as opposed to a holistic, less siloed approach to planning. We recommend that these requirements be reframed at a principles level.

Resolvability

4.3 Further to our points made under Question 1 above, we believe that execution and ongoing costs and risks will be significantly increased if resolution pre-positioning is spread across multiple standards.

4.4 It is unclear when the Reserve Bank intends to develop its own entity specific resolution plans (as required under s.260 of the DTA). However, we strongly recommend that the Reserve Bank commences this work early. We believe that the complexities and challenges of maintaining multiple standards, while seeking a high level of optionality, may only become truly clear once the Reserve Bank moves through that planning phase.

4.5 Further to our comments above, we believe that taking a holistic approach to identifying and prepositioning for functionality to support a range of resolution strategies is the better approach. This should be developed within a single crisis preparedness standard.

4.6 Overall, it is very important that recovery and exit and resolvability planning requirements do not create a lot of unnecessary duplication of effort and information, which would have short and long term efficiency and cost implications.

5. Are there any other issues that we should consider when operationalising the crisis management framework under the DTA?

See comments above.

Crisis Management under the Deposit Takers Act 2023

Q1. Do you have any views on our proposed approach to implementing the crisis management framework under the DTA? Are there any factors we should, or should not, take into account when implementing the framework?

ASB supports the Reserve Bank's intention to develop a new Crisis Preparedness Standard as part of the Deposit Takers Act (DTA) implementation.

ASB's specific recommendations regarding the development of the crisis management framework are outlined below.

ASB recommends that the Reserve Bank thoroughly considers the interaction between the proposed Crisis Preparedness Standard and the other DTA standards, and revise consultation timings to avoid any potential conflict or duplication of effort.

As outlined in the Issues Paper, the Crisis Preparedness Standard may include new requirements for deposit takers around pre-positioning for a crisis or resolution, which will need to be integrated with other obligations under the DTA standards. These integrations will need to be carefully thought through to avoid any potential conflict or duplication of effort. For example, for 'Group 1' deposit takers, the definitions and requirements regarding 'systemically important activities' under the crisis management framework are likely to be very similar to the concept of 'critical operations' under the Operational Resilience Standard and should be aligned as much as possible and where it makes sense to do so. Similar consideration should be given to any requirements around the scenarios used for recovery and exit planning, which are likely to be analogous to requirements for stress testing, business continuity planning etc.

Given the requirements for alignment, in order to avoid potential conflict and rework, the first round of consultation on the Crisis Preparedness Standard should be undertaken at the same time as the next stage of consultation on the Non-Core Standards in 2026. ASB consider that the Reserve Bank should from the outset, be working towards a single Crisis Management Standard that encapsulates the requirements for OBR, outsourcing and the proposed Crisis Preparedness Standard, in order to avoid duplication, inconsistences and rework.

ASB recommends that the Reserve Bank works closely with APRA when developing the Crisis Preparedness Standard.

Several new requirements proposed under the Reserve Bank's Crisis Preparedness Standard (e.g. recovery and exit planning, resolvability assessments etc.) are already in place (or are in the process of being implemented) in Australia. Given one of the Reserve Bank's intended outcomes from the Crisis Preparedness Standard is consistency with 'group level' recovery and exit plans and resolution approaches, aligning requirements as much as possible with APRA will be critical. Any unnecessary inconsistencies or novel requirements could undermine this objective and create duplication of work for deposit takers.

The Crisis Preparedness Standard will need to include appropriate transition provisions for deposit takers.

Any new requirements for deposit takers under the Crisis Preparedness Standard will need to be carefully sequenced to avoid overlapping with the significant amount of work being undertaken to implement the DTA during 2027-2028.

ASB understands from offshore that implementation of recovery and resolution planning requirements has been a very significant undertaking for both regulators and deposit takers, and ASB recommends that appropriate transition provisions be factored in at an early stage of development.

Q2. Do you have any comments on our proposed approach to dealing with distressed deposit takers under the DTA? Are there any alternative approaches we should be considering?

As mentioned above, the Reserve Bank will need to carefully consider the other DTA standards as it develops its definition and requirements regarding 'systemically important activities'. There is a risk of overlap or conflict with other similar requirements regarding 'critical functions' under the Operational Resilience Standard and potentially also 'material service providers' under the Outsourcing Standard. These requirements should be aligned as much as possible.

With regard to the Reserve Bank's 'group level' resolution tool; ASB submitted as part of our feedback on the Restricted Activities Standard, that the Reserve Bank should have the ability to make additional covered bond capacity available during a crisis should it be needed.

Q3. Do you agree with our assessment of the costs and benefits of a potential statutory bail-in power? Are there additional costs or benefits we should consider? Do you have any view on the need for statutory bail-in powers given the structural and contractual bail-in options are already available with the powers under the DTA?

ASB does not believe there is a strong case for a statutory bail-in regime in New Zealand. The main drivers for bail-in regimes offshore were to:

- Ensure that sufficient capital or loss-absorbing buffers were in place to absorb losses during resolution; and
- Support continuity of access for critical services provided by banks that are too large to resolve quickly.

The Reserve Bank has largely resolved the above concerns through its previous policy decisions as part of the capital review which will see total capital levels at or above most comparable offshore jurisdictions, along with a much heavier weighting on common equity. In addition, continuity of access for critical services has been addressed through the Reserve Bank's Open Bank Resolution (BS11) and Outsourcing (BS11) requirements.

Incorporating statutory bail-in at this point will also be a substantial undertaking at this stage of the legislative process and would only be justified if it delivers clear benefits over and above the cost and effort required to implement such an approach. We strongly submit the benefits are not clear, and

such a regime would add significant unnecessary complexity to the DTA. Some of the potential challenges include:

- defining the sequencing and processes for any write-off and conversion of liabilities;
- possible tax considerations; and
- Interaction with offshore legal regimes (for offshore funding).

Given the above, and that the Reserve Bank already has the ability under the DTA to implement a 'structural' bail-in (supported by the 'No Creditor Worse Off' provisions), it would seem hard to justify statutory bail-in powers are necessary now.

Similarly, any new additional Total Loss Absorbing Capital (TLAC) funding requirements will also re-introduce significant complexity for deposit takers and investors. Any TLAC instrument will likely need to include many of the complex contractual features that were present in the previous 'Basel 3' style hybrid capital instruments (e.g. conversion at the point of non-viability etc.), which the Reserve Bank removed as part of the capital review.

ASB believes that consideration of a bail-in regime in New Zealand would only make sense as part of any future review of the capital requirements and capital instruments for deposit takers.

Q4. Do you have any view on the potential new crisis preparedness requirements (i.e., recovery and exit planning, and resolvability)? If these requirements were imposed, do you have any initial comments on how they should be designed?

Please refer to ASB's response above under question 1 regarding the design and implementation of the crisis management framework more generally.

Q5. Are there any other aspects of crisis management we should be considering as part of our review?

ASB does not have any comments on the above question.

Deposit Takers Act – Crisis Management Issues Paper:

BNZ Response to the Reserve Bank of New Zealand issues paper questions on Crisis Management under the Deposit Takers Act.

22 November 2024

Introduction

1.1 BNZ welcomes the opportunity to provide a response to the Reserve Bank of New Zealand – Te Pūtea Matua on the issues paper questions on Crisis Management under the Deposit Takers Act.

1.2 We acknowledge the considerable work that has gone into developing the Deposit Takers Act (the Act or DTA) and the Crisis Management issues paper. We also acknowledge and commend the active engagement and consultation by the Reserve Bank of New Zealand – Te Pūtea Matua (the Reserve Bank). BNZ welcomed the opportunity to engage with the Reserve Bank in the recently held workshops on the DTA.

1.3 Set out below we provide responses to the consultation questions.

1.4 Should the Reserve Bank team have questions in relation to this response please contact Paul Hay, S9(2)(a) .

Paul Hay

Chief Regulatory and Compliance Officer, Bank of New Zealand

BNZ Response to Reserve Bank Questions

Q1	Do you have any views on our proposed approach to implementing the crisis management framework under the DTA? Are there any factors we should, or should not, take into account when implementing the framework?
	BNZ broadly agrees with the proposed approach to implementing a crisis management framework under the DTA, including the proposal for individual resolution plans for each deposit taker. BNZ supports ongoing robust discussions between RBNZ and industry regarding the policy options and tools for crisis management under the DTA. We note that while the crisis management aspects of the DTA have a slightly longer timeframe than the rest of the standards, there is still a significant amount of work to be completed and a transition timeframe to uplift pre-positioning for resolution tools may be required. BNZ believes it is important that the design and implementation of the resolution framework and tool kit is not rushed, and that comprehensive consultation and engagement is undertaken to ensure that the framework is proportionate in addressing the risk of failure of a deposit taker to financial stability, while not imposing unnecessary upfront costs and effort to pre-position. BNZ notes there will be many challenges and complexity in operationalising a range of resolution options under the proposed crisis management framework. It is critical resolution options are targeted for deposit takers as not all resolution options will be appropriate and having too many potential options can create uncertainty amongst depositors, senior creditors and capital providers. To address this, alignment between RBNZ resolution planning for each deposit taker with the deposit taker's own resolution plans will be critical. The cost of implementing the different resolution plans should also be considered under the range of resolution options that have been proposed to determine which of these would be appropriate in different circumstances. There will be significant resource required prior to a crisis event to simulate and test plans to ensure operational readiness – limiting the range of resolution tools that are applicable will therefore enable more thorough testing and preparedness. While we understand the intention to minimise cost to the taxpayer by utilising the deposit compensation scheme under the DTA, BNZ notes that if there is a significant idiosyncratic event, there will be the inevitable need for a potential temporary public sector liquidity backstop to access as a last resort. The rise in 24/7 payments, internet banking and social media can also exacerbate outflows and management of this will need to be factored into the crisis management framework under the DTA. RBNZ should also consider how the crisis framework and testing will work in conjunction with crisis related requirements in other standards such as capital adequacy and buffers via deposit takers internal capital adequacy assessment programmes (ICAAP), contingency funding plan (CFP) and also Open Bank Resolution (OBR). As a result of the introduction of the proposed crisis management resolution framework, these requirements should be reviewed for consistency and to ensure that there are no unintended consequences (such as holding additional capital buffers if new TLAC instruments are introduced). BNZ notes maintaining the confidence of international creditors that provide significant debt capital to domestic banks should be a key factor in resolution planning.

Q2	Do you have any comments on our proposed approach to dealing with distressed deposit takers under the DTA? Are there any alternative approaches we should be considering?
	The bridge institution and sale of business tools, which both involve a separate entity absorbing insured deposits and a proportion of uninsured deposits from the failing deposit taker, are complex resolution concepts and more detail on practically how these would be implemented is required. In particular, there are operational challenges that need to be worked through to implement the sale of business and bridge institution tools in a crisis event. Potential challenges that RBNZ would need to consider in regard to selling or transferring a deposit taker's business are: • Determination of which parts of the failing deposit taker should be transferred to the purchasing or bridge institution will take time to assess. • Preparation of bids, including any due diligence, by purchasers will likely take time and may impact a quick and effective resolution. • Transition of relevant assets and liabilities of the failed deposit taker to the new institution will be complicated and will need to be well managed. RBNZ has proposed the potential for the new institution to initially continue to use the failing deposit takers systems to enable access to deposits more quickly - some consideration is required regarding how this could work if only some of the deposits in that system are transferred to the new institution. • AML obligations will need to be complied with as part of the transition. The impact of the above operational challenges means that, even with pre-positioning by the failing deposit taker, it would be difficult to implement these resolution tools within a short timeframe, including over a weekend. It will also be important to consider the interplay between these resolution tools and OBR. While it is ultimately a decision for the Minister of Finance, BNZ views the government guarantee of unfrozen uninsured deposits as fundamental to OBR being successful and avoiding a potential idiosyncratic event leading to a systemic crisis. Without the government guarantee there would be a risk of a run on the bank (with depositors removing their unfrozen money) and there would be a risk that other entities would not want to continue engaging with the failing bank which could impact the ability of that failing bank to continue to remain open (for example, the failing bank may not be allowed back into the payments system without a guarantee). Given the operational considerations of the sale of business and bridge institution tools noted above, it is unlikely that OBR could be implemented and then an immediate transfer of the continuing aspects of the failing deposit taker to a new institution implemented without the need for a government guarantee in the intervening period. RBNZ also needs to consider how the bridge institution would be capitalised, including whether this could be through an equity transfer from the DCS.

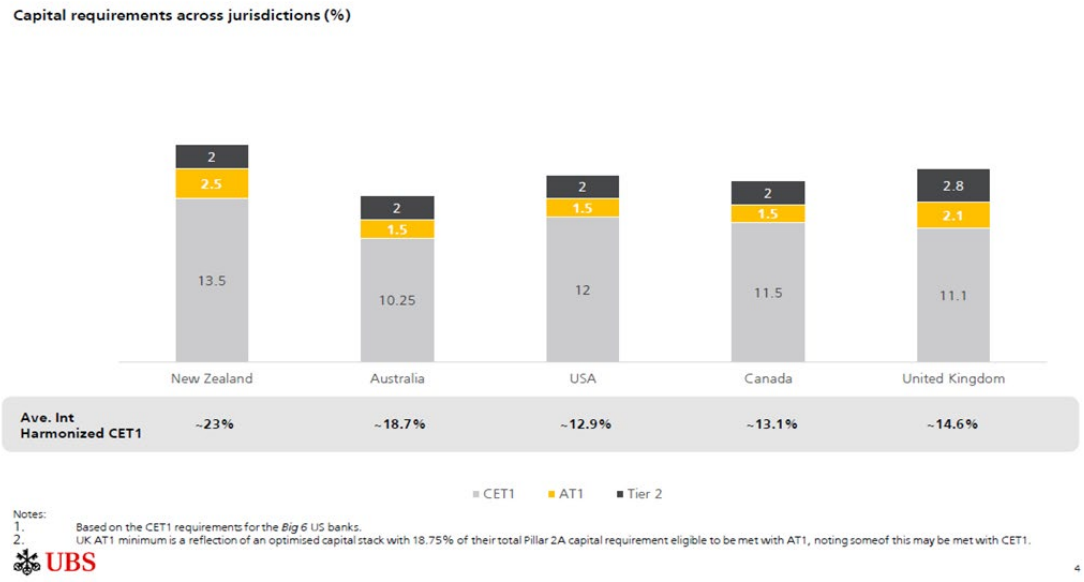
Q3	Do you agree with our assessment of the costs and benefits of a potential statutory bail-in power? Are there additional costs or benefits we should consider? Do you have any view on the need for statutory bail-in powers given the structural and contractual bail-in options are already available with the powers under the DTA?
	BNZ agrees with the relative advantages and disadvantages of a potential bail-in power highlighted by RBNZ and agrees that there are a variety of complexities associated with designing a statutory bail-in power. Including a legal basis to bail-in certain liabilities increases resilience of the industry to ensure we have a (1) transparent and (2) credible way to transfer/share losses with private sector investors as we recapitalise a failing institution. However, we need to also appreciate the uniqueness of the NZ regulatory capital framework, where at the 2028 end-state we are mandated to hold 13.5% of the highest quality CET1 capital, which is a significant requirement when compared to global peers. BNZ is not opposed to statutory bail-in as a resolution tool but believes that if it is to be implemented under the DTA the following issues need to be considered (noting that structural and contractual bail-in are already available under the DTA): • The fundamental safeguard to address is that, through the exercise of bail in powers, no creditor should be left in a worse off position than they would have been if the failing deposit taker had been wound up as result of liquidation (insolvency proceedings) or statutory management. • Major NZ banks currently have loss absorbing capacity and in the remote event that there is a need for additional recapitalisation, then the currently mandated minimum of 4.5% of AT1 and T2 subordinated capital instruments should be sufficient to evidence adequate private sector burden-sharing. • An option is to restrict the statutory bail-in power to be limited to just subordinated liabilities. This way the authorities have the flexibility to use the AT1 and T2 capital instruments readily in a bank failure – an improvement from current situation – without there being any legal challenge from investors. This has the benefit of not unduly distorting the demand and pricing of other liabilities including wholesale funding and operational liabilities. We understand that the Monetary Authority of Singapore has taken a similar approach in its resolution regime framework. • BNZ notes that there will be inevitable legal issues that need to be factored into a statutory bail in regime to ensure creditor hierarchy is protected and to avoid uncertainty to investors given the absence of write off or conversion features in both AT1 & Tier 2 instruments under the current capital regime. Consideration needs to be given to the ranking of capital instruments currently on issue vs those with bail in conditions and the impact on current investors in bank capital instruments. There are lessons to be learnt from both CS and SVB bank collapses that were noted in the FSB 2023 report on "Bank Failures Preliminary lessons learnt for resolution 10 October 2023"[1] which provides a good backdrop to the proposed crisis management framework. • RBNZ notes in the paper that most major overseas jurisdictions have adopted bail in as a resolutions tool but most (if not all) of these jurisdictions would also have convertible capital instruments in their stack which in practice should convert before the TLAC if ranking of loss absorption is upheld. Another key barrier for TLAC capital instruments in the NZ market is that conversion into ordinary shares

[1] https://www.fsb.org/uploads/P101023.pdf

is problematic operationally for NZ banks who are not currently listed.

- If RBNZ was to introduce statutory bail-in then current instruments could either be grandfathered to carry a regulatory value for a defined period but not be subject to the bail-in regime or a clear pronouncement could be made that inclusion of statutory bail-in in the resolution tool kit constitutes a regulatory event and existing instruments could be called early to avoid uncertainty and protect creditor hierarchy. Having legacy instruments in circulation adds to uncertainty and misinterpretations as to where creditors stand in the hierarchy.

RBNZ notes in the consultation paper that any future bail-in resolution tool would likely involve TLAC requirements. BNZ does not believe that the introduction of a new TLAC capital instrument on top of existing capital instruments is required. RBNZ regulated deposit takers already have the highest capital ratio requirements globally on a harmonised basis (refer to illustration below). Additional capital requirements would likely have an impact on lending decisions and would not be in proportion with the risk being addressed. Consideration would also need to be given to the impact that any TLAC requirements would have on credit rating agency considerations in assessing credit ratings of the deposit taking institution.



In summary, BNZ acknowledges statutory bail in provides RBNZ with a recapitalisation capital option (from capital and non-capital instruments) during a crisis without any legal disputes if:

- statutory bail-in ensures creditor hierarchy is respected and codified;
- logically junior-ranking capital instruments are equally part of the burden-sharing either via contractual triggers or via the same statutory powers;
- credit rating agency considerations are factored into assessing the impact on credit ratings of the deposit taking institution; and
- the future state of OBR is considered if statutory bail in is introduced.

Before any decisions are made regarding TLAC, there should also be a capital impact study undertaken to assess RBNZ's desired quantum of loss absorbing capital against the cost of issuance and the form of such an instrument, noting current domestic market constraints. The possible conversion into ordinary shares needs to be considered in the context of NZ deposit takers that are not currently listed, as well as whether there is adequate demand in the domestic market from professional investors to support TLAC.

	BNZ understands that RBNZ does not intend to revisit decisions from the 2017-19 Capital Review (which determined to remove bail-in mechanics from regulatory capital instruments) as part of this consultation. However, BNZ considers that the structure of these instruments should be reconsidered if statutory bail-in is introduced to avoid inconsistent bail-in mechanisms across the capital and funding stack and uncertainty among investors.
Q4	Do you have any view on the potential new crisis preparedness requirements (i.e., recovery and exit planning, and resolvability)? If these requirements were imposed, do you have any initial comments on how they should be designed?
	BNZ agrees with the proposal for RBNZ to prepare and maintain resolution plans for each deposit taker. Considering the most appropriate tools for each deposit taker and how this would be managed in practice in advance of a crisis event occurring will better position both RBNZ and the deposit taker to respond more quickly when required. BNZ notes that NZ banks are well capitalised and managed within existing regulatory frameworks, including cross-border regulatory oversight for Group 1, which significantly reduces the likelihood of a failure event occurring. The proposed additional crisis management tools are therefore an additional safeguard to enable a better response to a 1 in 200-year event and need to be considered from a proportionality perspective against this low risk. While BNZ understands the RBNZ's preference to have available a wide range of resolution tools to provide flexibility in a crisis event, the proposed requirements appear to require deposit takers to consider a wide range of potential (hypothetical) scenarios and continuously assess them in the context of a wide-ranging set of potential recovery tools. The proposed requirement for deposit takers to undertake recovery and exit planning during normal operations is comprehensive and may require significant resources to address properly. BNZ believes it is important to balance the need to be prepared in a crisis event with the time and effort required to preposition for a range of resolution tools. BNZ suggests that RBNZ not require a deposit taker to pre-position for resolution tools that are unlikely to be used for that deposit taker in a crisis event. In addition, RBNZ should consider whether all resolution tools that are included in a deposit taker's resolution plan need to be pre-positioned for and would provide material benefit in a crisis event. This will ensure that deposit takers can focus testing and operationalising resolution tools that are likely to be used in a real event. Some of the resolution tools, such as sale of business and bridge institution, are complex from both an operational and system perspective, especially when involving cross border regulators. These tools are also unlikely to be able to be implemented quickly (e.g. over a weekend), regardless of the pre-positioning done and therefore the benefits of pre-positioning to enable resolution to happen quickly may be less significant for these options, particularly given the potential cost and operational impact that such pre-positioning may have on the deposit taker's business as usual activity. Noting the above, it will be important that RBNZ provides clear guidance to each deposit taker regarding what pre-positioning is required and the timeframes to implement any changes. It would also be useful to understand RBNZ's thinking regarding how OBR will interact with contractual, structural and statutory bail-in tools and how this may impact pay out

	under the Deposit Compensation Scheme. Finally, BNZ suggests consolidating crisis testing requirements into a single annual test to avoid testing fatigue within organisations. Having several tests across the year (for OBR, BS11 and crisis preparedness) may limit the effectiveness of the exercises and the learnings obtained from them. BNZ suggests that RBNZ set a theme for crisis testing each year and deposit takers could focus efforts into one test covering all requirements, which will avoid testing fatigue and result in more valuable testing. This would also enable RBNZ to compare results more easily across the industry to obtain thematic findings and recommendations.
Q5	Are there any other aspects of crisis management we should be considering as part of our review?
	BNZ notes that cross border resolution planning for NZ deposit takers that are part of an overseas group is fundamental to assessing the appropriateness of resolution tools, including the impact of any structural and statutory bail in. We support RBNZ's proposal in the issues paper to focus on group level resolution in co-operation with regulators in other jurisdictions – while noting that group level resolution will not always be possible and RBNZ also needs resolution tools that can be utilised in relation to the NZ deposit taker on a standalone basis. BNZ also believes that RBNZ's resolution tools should, to the extent possible, be consistent with global resolution frameworks to avoid being an outlier and provide more confidence to overseas investors. Focusing on consistency with global resolution frameworks would also avoid uncertainty and allow NZ to capture learnings from other regimes where resolution tools have been used in practice.

FINANCIAL SERVICES FEDERATION

22 November 2024

Reserve Bank of New Zealand – Te Pūtea Matua
Wellington dta@rbnz.govt.nz

Dear Madam/Sir,

Re: Crisis Management under the Deposit Takers Act

The Financial Services Federation ("FSF") is grateful to the Reserve Bank of New Zealand ("RBNZ") for the opportunity to respond on behalf of our members to the consultation on the Crisis Management under the Deposit Takers Act ("the Consultation").

By way of background, the FSF is the industry body representing the responsible and ethical finance, leasing, and credit-related insurance providers of New Zealand. We have over 90 members and affiliates providing these products to more than 1.7 million New Zealand consumers and businesses. Our affiliate members include internationally recognised legal and consulting partners. A list of our members is attached as Appendix A. Data relating to the extent to which FSF members (excluding Affiliate members) contribute to New Zealand consumers, society, and business is attached as Appendix B.

Introductory Comments

We appreciate the opportunity to provide feedback on the proposed crisis management framework under the Deposit Takers Act (DTA)and we recognize the importance of a robust and transparent crisis management system to ensure financial stability and protect depositors and the importance of the RBNZ's role within this. However, we have specific concerns and suggestions regarding the implementation of this framework, particularly in relation to the unique challenges faced by smaller deposit takers.

Proposed Approach to Implementing the Crisis Management Framework

We support the overall objective of the crisis management framework to enhance financial stability and protect depositors. However, we urge the RBNZ to consider the proportionality of the requirements imposed on smaller deposit takers. The compliance burden and costs associated with extensive crisis management preparations could disproportionately impact smaller institutions, potentially affecting their viability at a time when there has been an excessive amount of different compliance costs implemented at once (CoFI, DCS etc).

Dealing with Distressed Deposit Takers

The proposed resolution tools, including Open Bank Resolution (OBR), sale of business, bridge institutions, and orderly wind-down, are comprehensive. However, we recommend that the RBNZ provide clear guidelines and support for smaller deposit takers to navigate these processes. Alongside this the RBNZ needs to work individually with deposit takers to

set clear expectations and take an educative approach. Additionally, the potential role of bail-in mechanisms should be carefully evaluated to ensure that they do not unduly burden smaller institutions and their stakeholders for the reasons mentioned above.

Statutory Bail-In Powers
While we understand the rationale behind statutory bail-in powers, we have concerns about their application to smaller deposit takers. The complexity and potential legal challenges associated with bail-in mechanisms could be particularly onerous for smaller institutions. We suggest that the RBNZ consider alternative approaches or exemptions for smaller deposit takers to mitigate these challenges. We welcome further consultation on this point.

Crisis Preparedness Requirements
We acknowledge the importance of recovery and exit planning, as well as resolvability requirements. However, we request that the RBNZ tailor these requirements to reflect the size and complexity of smaller deposit takers. Simplified and proportionate requirements would help ensure that smaller institutions can effectively prepare for potential crises without facing undue burdens. More emphasis neds to be placed on the proportionality requirement to ensure that the RBNZ maintains a diversity of different deposit takers.

Coordination and Support
Effective crisis management requires coordination with various stakeholders, including regulators, other financial institutions, and service providers. While we have been happy with the level of communication thus far, we encourage the RBNZ to establish clear communication channels and provide ongoing support to smaller deposit takers to enhance their crisis preparedness and response capabilities.

Please do not hesitate to reach out if you wish for us to speak further on any of the points made in this submission.

Yours sincerely,

S9(2)(a)

Katie Rawlinson
Legal and Policy Manager
Financial Services Federation

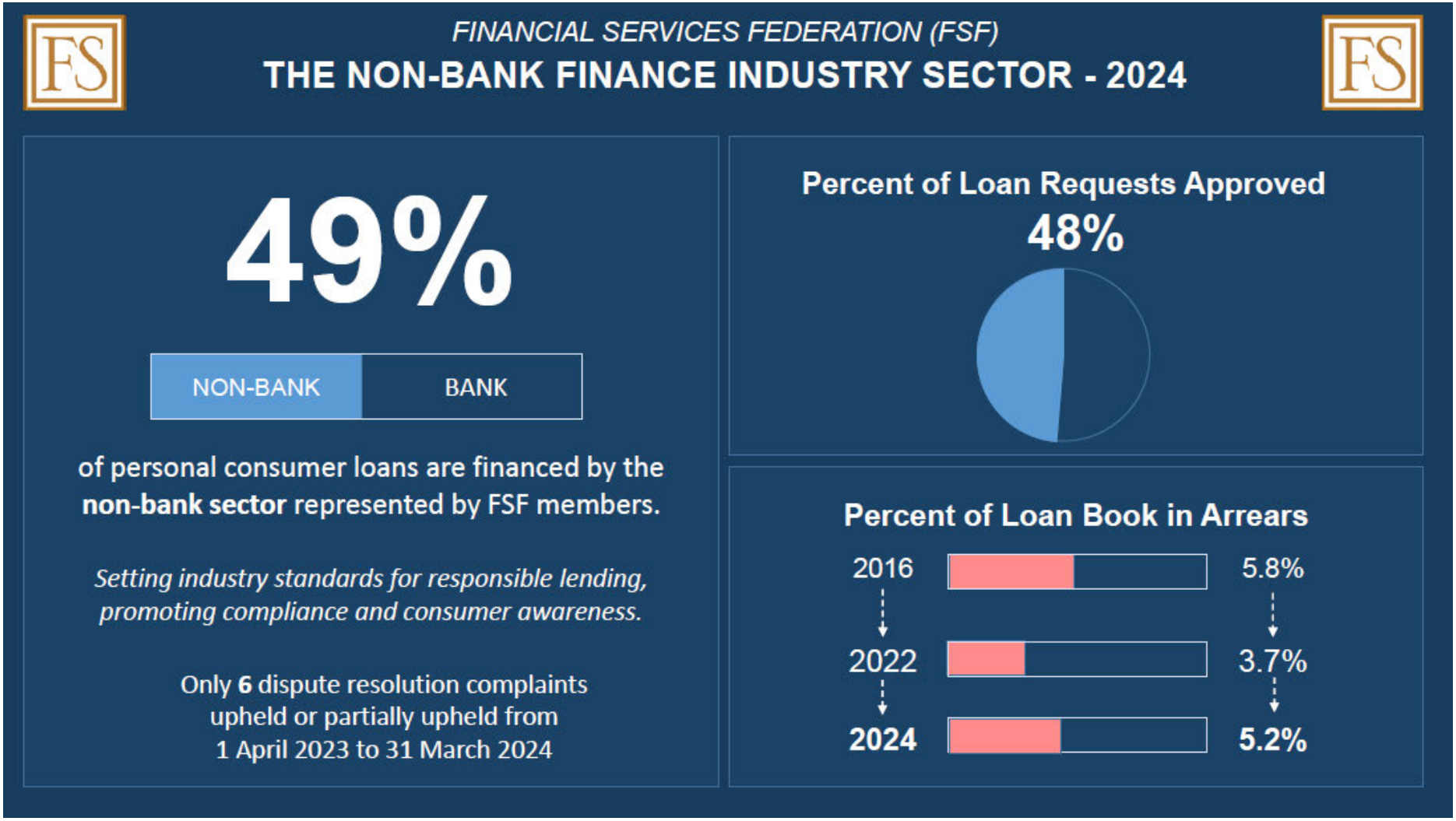
Appendix A

FINANCIAL SERVICES FEDERATION

FSF Membership List as at September 2024

Non-Bank Deposit Takers, Specialist Housing/Property Lenders, Credit-related Insurance Providers	Vehicle Lenders Finance Companies/ Leasing Providers	Finance Companies/ Diversified Lenders	Finance Companies/ Diversified Lenders contd, Insurance Premium Funders	Insurance Premium Funders contd/ Social Impact Lenders / Affiliate Members	Affiliate Members contd
Non-Bank Deposit Takers Finance Direct Limited ➢ Lending Crowd General Finance (BB) Gold Band Finance (B+) ➢ Loan Co Mutual Credit Finance (B) Credit Unions/Building Societies First Credit Union (BB) Nelson Building Society (BB+) Police and Families Credit Union (BB+) Specialist Housing/Property Lenders Basecorp Finance Limited First Mortgage Managers Ltd. Liberty Financial Limited Pepper NZ Limited Resimac NZ Limited Credit-related Insurance Providers Protecta Insurance Provident Insurance Corporation Ltd	Auto Finance Direct Limited BMW Financial Services ➢ Mini ➢ Alphera Financial Services Community Financial Services Go Car Finance Ltd Honda Financial Services Kubota New Zealand Ltd Mercedes-Benz Financial Motor Trade Finance Nissan Financial Services NZ Ltd ➢ Mitsubishi Motors Financial Services ➢ Skyline Car Finance Onyx Finance Limited Scania Finance NZ Limited Toyota Finance NZ ➢ Mazda Finance Yamaha Motor Finance Leasing Providers Custom Fleet Euro Rate Leasing Limited Fleet Partners NZ Ltd ORIX New Zealand SG Fleet	Finance Companies & Diversified Lenders AfterPay Avanti Finance ➢ Branded Financial Basalt Group Blackbird Finance Caterpillar Financial Services NZ Ltd Centracorp Finance 2000 DebtManagers Finance Now ➢ The Warehouse Financial Services ➢ SBS Insurance Future Finance Geneva Finance Harmoney Humm Group Instant Finance ➢ Fair City ➢ My Finance John Deere Financial Latitude Financial Lifestyle Money NZ Ltd	Limelight Group Mainland Finance Limited Metro Finance Nectar NZ Limited NZ Finance Ltd Personal Loan Corporation Pioneer Finance Prospa NZ Ltd Speirs Finance Group (L &F) ➢ Speirs Finance ➢ Speirs Corporate & Leasing ➢ Yoogo Fleet Turners Automotive Group ➢ Autosure ➢ East Coast Credit ➢ Oxford Finance UDC Finance Limited Yes Finance Limited Zip Co NZ Finance Limited Insurance Premium Funders Arteva Funding NZ Ltd Elantis Premium Funding NZ Ltd Financial Synergy Limited	Hunter Premium Funding IQumulate Premium Funding Rothbury Instalment Services Social Impact Lenders Money Sweetspot Ltd Affiliate Members Alfa Financial Software American Express AML Solutions Limited Buddle Findlay Chapman Tripp Credisense Ltd Deloitte EY FinTech NZ Finzsoft Happy Prime Limited IDCARE Ltd KPMG Loansmart Ltd Match me Money Ltd	Motor Trade Association Odessa Technology Inc. One Partner Limited PWC Sense Partners Simpson Western Summer Lawyers Credit Reporting, Debt Collection Agencies, Centrix Credit Corp ➢ Baycorp ➢ Collection House Debtworks (NZ) Limited Equifax Gravity Credit Management Limited Illion Quadrant Group (NZ) Ltd Recoveries Corp NZ Ltd Total 98 members

Appendix B


FINANCIAL SERVICES FEDERATION (FSF)
THE NON-BANK FINANCE INDUSTRY SECTOR - 2024
49%
NON-BANK
BANK
of personal consumer loans are financed by the non-bank sector represented by FSF members.
Setting industry standards for responsible lending, promoting compliance and consumer awareness.
Only 6 dispute resolution complaints upheld or partially upheld from 1 April 2023 to 31 March 2024
Percent of Loan Requests Approved
48%
Percent of Loan Book in Arrears
2016
5.8%
2022
3.7%
2024
5.2%

KEY FACTS: THE NON-BANK FINANCE INDUSTRY SECTOR

FSF Members (as at 31 Mar 2024)

Number of Members	97
Number of Employees	3,353
Applications Processed	1,102,266
Loan Requests Approved	527,382
Percent of Loan Book in Arrears	5.2%
Loan Disputes Upheld	6

Bank Sector (as at 31 Mar 2024)

Value of Mortgage Loans	$352B
Value of Consumer Loans	$7.7B
Value of Business Loans	$125B

Non-Bank Sector Share (as at 31 Mar 2024)

% of Total Mortgage Loans	0.3%
% of Total Consumer Loans	48.5%
% of Total Business Loans	8.7%

Insurance Credit Related (as at 31 Mar 2024)

Number of Employees	250
Number of Policies	300,209
Gross Claims (annual)	$22.1M

Consumer Loans (as at 31 Mar 2024)

Total Value of Loans	$8.2B
Number of Customers	1,537,502
Number of Loans	1,735,718
Average Loan Size	$4,746
Total Value of Loans:	
Mortgage	$979M
Vehicle Loan	$4,036M
Unsecured	$2,129M
Other Security	$361M
Lease Finance	$733M
Average Value of Loan:	
Mortgage	$134,675
Vehicle Loan	$13,337
Unsecured	$1,588
Other Security	$4,245

Business Loans (as at 31 Mar 2024)

Total Value of Loans	$11.9B
Number of Customers	131,161
Number of Loans	202,921
Average Loan Size	$58,894
Total Value of Loans:	
Mortgage	$4,092M
Vehicle Loan	$2,989M
Unsecured	$262M
Other Security	$2,846M
Lease Finance	$1,763M
Average Value of Loan:	
Mortgage	$766,527
Vehicle Loan	$37,362
Unsecured	$48,107
Other Security	$54,724
Lease Finance	$29,308

Submission in response to: Crisis Management under the Deposit Takers Act 2023

Introduction

I enclose our response to the Reserve Bank of New Zealand's (RBNZ) request for submissions in regard to Crisis Management under the Deposit Takers Act 2023 (DTA).

If there are any aspects of our submission that you would like further comment upon, please do not hesitate to contact me by email at S9(2)(a) or by phone at S9(2)(a)

Yours,

Mark Obren
Director
Technology Development Group Limited

in conjunction with:
Alex Ross
Sasquatch Limited

Q1 Do you have any views on our proposed approach to implementing the crisis management framework under the DTA? Are there any factors we should, or should not, take into account when implementing the framework?

There seems to be a central theme throughout the proposed approach to minimise the impact of future financial crises on the public purse. It is noted that the RBNZ seeks "to support the effective and efficient management of public financial resources by avoiding or minimising, and otherwise managing, the need to rely on public money to deal with a licensed deposit taker that is in financial distress or other difficulties." (RBNZ, 2024, p.16).

While in isolation this may sound like a worthwhile objective, the statement is devoid of context.

In particular, it is made without regard to the least overall cost to society in general, and in disregard to all risk management and prudential theory that he who can wear the risk at the lowest cost should the one that wears that risk. It is difficult to assert that the Government is the entity in New Zealand least able to carry the cost of risk.

Further, the RBNZ states that under the proposed approach "... the Bank must take into account the following principles...: the desirability of ensuring that the risks referred to in section 3(2)(d) are managed" (RBNZ, 2024, p.17), but to what end? It is worth noting that there is no need to manage risks to minimise the overall costs of the risks to society. Indeed, one can manage them with any outcome in mind.

This lack of specificity of purpose reinforces the impression that the central premise of the proposed approach is for Government to shift the financial and political cost of financial failures onto others, regardless as to whether this induces an improved or worsened outcome for society at large, the creditors involved or the institution that is involved itself.

That is not to say that bail-outs are a preferred option either, as there are also costs to the rest of society if we have bail-outs rather than bail-ins. In bail-outs we are simply transferring costs from depositors, who knowingly took a risk to deposit funds with these firms, to those who elected not to deposit or are unable to deposit with these institutions. Is this merely another form of corporate welfare, creating moral hazard where depositors need not undertake any diligence in ensuring the resilience of the deposit takers, and can accept higher interest returns from riskier institutions without regard to any attached risk?

We can recognise that both bail-ins and bail-outs incur costs to society. One difference between these options is who bears those costs. Another factor that could be explored more fully is the difference in the magnitude of the costs between these two options.

The RBNZ states that "the main purpose of the DTA is to promote the prosperity and well-being of New Zealanders and contribute to a sustainable and productive economy by protecting and promoting the stability of the financial system" (RBNZ, 2024, p.16). Yet, one does not "promote the prosperity and well-being" of society by ensuring the survival of inefficient firms or by protecting the firms and their management from consequences of their own risk-taking; and that is the usual outcome from creating conditions of moral hazard.

If this policy truly seeks "to allocate costs to deposit takers, their investors or industry more broadly, rather than relying on public money from the government, thereby reducing the risk of moral hazard and improving market efficiency (RBNZ, 2024, p.12), then it may have merely moved the costs of moral hazard around rather than address the central issue that has generated it in the first place.

As usual, the devil is in the detail, and while this policy discussion is commendable for attempting to address a complex issue, at the same time it has brought attention to other areas that can cause new sources of moral hazard and inefficiencies.

Thus, while the openness of the RBNZ's attempts at this approach should be lauded, it is suggested that the core issue that has generated the need for such an approach has not been acknowledged.

That unacknowledged issue is market failure.

Maybe it is time to consider letting a truly free market operate, at least as a counter-factual analysis of an alternative to the bail-in and bail-out approaches, and compare the real costs and benefits to society of the proposed policy.

Q2 Do you have any comments on our proposed approach to dealing with distressed deposit takers under the DTA? Are there any alternative approaches we should be considering?

The preparation for future potential crises is likely to have, at best, mixed results. An institutional crisis is most likely to occur during times of discontinuous change, rather than during times of normality. One cannot predict the nature of such a discontinuity, only that one will inevitably occur.

The problem for planners is that as the nature of a discontinuity cannot be foreseen, any preplanned response or contingency is likely to be ineffective at best. Firms require flexibility and an alignment of incentives to be able to recognise signals of such change from the market and to navigate this change in sufficient time to avert potential disaster. The RBNZ, through creating an expectation of intervention, could inadvertently reduce the capability of individual firm's ability to navigate such circumstances, by encouraging delay or misguided responses that exacerbate the situation.

Thus, the proposed preparation for crises may have unintended negative consequences and will certainly bear a cost no matter how effective they prove to be.

So, it is suggested that while the proposed early detection and diagnosis may well be effective in normal times, such as when a firm fails primarily due to its own mismanagement of an ordinary situation, one can be certain that such information gathering will fail to pick up on signals of discontinuous change. That can lead to an artificial aura of confidence that may delay effective responses to unforeseen change until it is too late to take effective action to counter a building discontinuity.

Further, one needs to take care in regard to the responses (i.e. tools) developed to meet detected anomalies or evolving circumstances that demand attention. In general principle, the range of tools used to address a failure should seek to reduce the systemic risk to the financial system rather than merely transfer or defer risks. For example, forcing the merger of a 'bad' bank with a 'good' bank can not only reduce competition within the banking sector, but also enhance the risk of further failure due to the larger share of the market structure being held by an incumbent with a weakened quality of its balance sheet compared with the balance sheet quality of the originally 'good' institution. All that has really been achieved in this example is a transfer of risks and a temporary disguising of underlying issues while nothing has really been fixed at all. The Credit Suisse situation cited by RBNZ (2004, p. 28) is an example of such a transfer and deferral of risk, and arguably an obfuscation of the resulting overall risk profile.

The nature of the planned responses to a potential crisis can also frame the understanding of a developing situation, and prevent other potentially less harmful or more effective responses from being considered. This can be a consequence of the case where the RBNZ (RBNZ 2024, p.23) focuses on restoration as a core objective of the proposed policy. When restoration is the only allowable policy option, a moral hazard situation is inevitable that will lead to future increased appetite for risk by deposit-takers and depositors alike.

An alternative approach can be to allow some of these cases to fail, i.e. to conduct a disorderly exit from the market, thereby ensuring an attention by all parties to the risks that they are embarking upon and thus provide an incentive upon all to align future risk with reward.

Despite the suggestion that the situation where a "deposit taker may make a strategic decision to cease its regulated activities in response to distress" is an "extreme scenario" (RBNZ 20024, p.22), participant entry and exit from markets are normal features of any healthy market.

In fact, one feature of discontinuous change periods is a proliferation of entrants into a market, and measures that prop up incumbents against entrants can do much to slow or stall structural change within an industry, thereby delaying advantages to society at large for the benefit of a minority, and possibly even create a National Competitive Disadvantage (Porter, 1990) vis-à-vis other societies that can impact many industry segments.

So, depending upon the nature of the conditions that generate a crisis, a planned response may in fact cause widespread harm and incur a cost that can take quite some time to overcome.

However, what if one cannot allow an institution to fail, on account of the scale of the impact on others? There is a tacit admission that there are institutions within New Zealand whose failure would cause a risk to the entire system, with the acknowledgment that "Keeping the failed deposit taker open for business may also help mitigate any loss of confidence in the financial system" RBNZ (2004, p.41).

Risk management principles suggest that such an institution should not be allowed to exist in the first place – it is a risk that is too big to be borne. Considering this type of situation using this lens, any institution that is 'too big to fail' should be 'too big to tolerate'. In such circumstances, it is better practice to adopt early measures to break up such an institution whose potential failure would constitute a systemic risk to the entire system, before such a risk is realised.

It is a little late in the day to realise a risk to the entire system before one chooses to do something about it.

In such a situation, is a bail-in a fair or effective approach? Presumably any institution that is 'too big to fail' has market power, and has likely distorted the market in its favour, thereby creating conditions where many feel obliged to use its services. Is it reasonable that if such people who are caught by the exercise of market power, at a cost to themselves through a lack of competitive offerings and likely resulting corporate underperformance, and are then required to pay further for the outcomes of the risks taken on by the management of such an institution?

It is a difficult policy question to answer fairly and in a manner that is economically efficient.

Yet, despite these issues, the DTA decision is proposed to be made by criteria set by the RBNZ and public sector, carried by decision solely of the RBNZ and public sector, and implemented despite the interests of any other. This is the consequence of the statement that "the decision to place a deposit taker via Order in Council into resolution sits with the Governor-General on the advice of the Minister of Finance in accordance with the Reserve Bank's recommendation" RBNZ (2024, p. 24).

There is no mention anywhere of the views of the deposit-taker or the depositors being taken into account.

Presumably, one is to rely on the foresight, competence and good intentions of the public sector to avoid any abuse of such a situation. However, events over the past few decades have led many across society to become sceptical in regard to the public sector being always able to exhibit these characteristics.

The DTA is a policy proposal that risks creating the conditions for events that run absolutely contrary to the original stated intentions, namely "to promote the prosperity and well-being of New Zealanders and contribute to a sustainable and productive economy" (RBNZ, 20024, p.16). There is a real risk of making things worse for society over the long term rather than better.

But what is wrong with people sorting out their own affairs under true market conditions?

It appears that laizzez-faire has not even been explicitly considered as a viable policy possibility, and could prove a useful counter-factual for policy formation.

Q3. Do you agree with our assessment of the costs and benefits of a potential statutory bail-in power? Are there additional costs or benefits we should consider? Do you have any view on the need for statutory bail-in powers given the structural and contractual bail-in options are already available with the powers under the DTA?

In comparing statutory versus contractual or structural bail-ins, we agree that the statutory approach is simpler conceptually and imposes lower direct costs to society than the other two approaches.

We do agree that contractual measures may be simpler to administer in many cases, but administrative convenience is rarely a good reason to select one policy over another. Indeed, the ever decreasing cost of information processing is such that the real operational cost of any policy is likely to become increasingly less significant over time compared to the inherent economic costs derived from the various bail-in options.

A statutory bail-in does carry its own risks inherently, with such a RBNZ intervention overriding the property rights of the institution's shareholders and negating the situational awareness of its management – both circumstances that are not conducive of superior outcomes.

There can also be the appearance of favouritism in dealings with third parties, and of political interference in predetermining a course of action – no matter what decision is made.

In any case, one has to ask whether the action is likely to produce the desired outcome of "reducing the risk of moral hazard and improving market efficiency" (RBNZ 2024, p.12) Does bail-in really address the issue at hand? One can argue that bail-in does not reduce systemic risk but that it merely shifts it around, while creating a moral hazard that acts to heighten the risk further over time. This is a result at odds with the stated desired outcome of the policy.

There is a school of thought that the financial industry's systemic risks have been rising since at least the financial crisis of 1987, and the failure of successive administrations to pay the political and economic capital to face and deal with the situation has led to increasingly severe effects from each successive crisis. On this basis, we can predict that sooner or later there will be a crisis from which there cannot be a transfer of risks that ameliorate the systemic risk and that the system will inevitably collapse.

Thus, it can be said that bail-ins can do nothing to reduce this long term effect. Instead they merely allow further delays in facing decisions that must inevitably be made. That outcome is hardly desirable, and thus it can be argued that bail-ins is a policy that would be better to not be implemented at all.

The counter factual position is to have no bail-in facility at all, and the development of an understanding within the financial sector that the costs will be left to be borne by those who created them. In the long term, this course of action will reduce moral hazard and the overall cost to society, albeit at a political cost for those who will have to forego a 'white knight' role during a future crisis in favour of communicating and supporting a 'laissez-faire' approach – an uncommon and presumably uncomfortable position for the current political generation.

We would suggest that the current and proposed bail-in powers are unnecessary and indeed counter-productive, in that they induce more speculative and risky behaviour, thereby creating the very conditions for which they are designed to manage, and that it would be better in the long term to abolish these powers altogether.

Further to the central question of the optimal bail-in policy, let's consider some other points:

a. Deposit Insurance

The purpose of Deposit Insurance is to make whole depositors' losses incurred when a bank fails or defaults on its obligations to depositors who are, to all intents and purposes, merely unsecured creditors. However, if a bail-in policy was in place, then the conditions for triggering a Depositor Insurance claim will never arise, as the bail-in will presumably pre-empt those conditions by converting the depositors' debt into a form of equity.

Thus, if a bail-in provision is enabled, there is no justification at all for a Depositor Insurance, and in particular a compulsory scheme, where costs are being incurred by all Depositors for no return on investment, as there is no risk to ameliorate.

So, if bail-ins are formulated as policy, then all compulsory depositor insurance should be scrapped.

There is no need to have two separate policies aimed at solving the same problem, especially as there is a real cost to society attached to each.

b. Bail-in or Bail-out?

"A bail-in resolution tool would enhace *(sic.)* optionality for us to deal with a failed deposit taker in a way that meets the relevant DTA purposes...recapitalise the deposit taker without use of public funds." (RBNZ, 20204, p.41).

In other words, a bail-in would transfer the costs of failure from Government to others; while presumably asking those others to take it on good faith that such transfer is on the basis of the minimal cost to society rather than one of political convenience.

This is in contrast to bail-outs, where the costs of intervention are paid by the Government. A bail-in "provides an alternative to taxpayer-funded bail-outs, helping to avoid or minimise the need to rely on public money (while acknowledging that the use of public money would depend on the circumstances at hand)." (RBNZ, 2004, p.41)

This raises the real issue as to when a bail-out strategy should be chosen, and when a bail-in strategy should be chosen. Presumably, there should be some transparent measure for strategy selection to avoid the appearances of the strategy being chosen either on the basis of choosing favourites, or on the basis of political pressure.

It would be useful if the RBNZ could be more explicit in the criteria for each policy choice.

c. Other Jurisdictions

Just because some other jurisdictions do certain things does not mean that New Zealand has to ape them. Policy for New Zealand would be more effective if it is formulated based on sound principles that are applicable to the New Zealand situation, rather than merely copying others as supposed 'best practice' or copying policies that are formulated for quite different economic circumstances or is based upon theory that does not apply to economies of the nature and scale of New Zealand.

It is important to note that most economic theory has been created within economies of different scale, sophistication, dependencies and exposure to international pressures than the New Zealand economy. Much of this theory does not translate well to different contexts, and thus practice that makes sense in usually larger economies is better to be rigorously tested in the New Zealand context to ensure its validity before such practice is adopted within New Zealand.

d. Mission Creep

It is noted “the bail-in tool is that it could provide a pre-positioned option for us to both stabilise and recapitalise a deposit taker in resolution” (RBNZ, 2004, p.41). Why should it be the RBNZ that manages or arranges the recapitalisation of an institution? That is normally the role of their board of directors and shareholders, or in case of failure an Official Assignee.

Further, a “bail-in could be designed to ... create a new ownership structure... Alternatively, the deposit taker could be sold to a third party” (RBNZ, 2024, p.41). A new ownership structure would prevent the existing management and shareholders gaining direct benefit from the bail-in, which would restrict their capture of the benefits of a bail-in – thus reducing moral hazard to some extent. However, in this case who becomes the new owner? There is the real possibility that there will be an appearance of the RBNZ allowing a favoured party to assume ownership rights, and at what price? This raises the risk of at least the spectre of corrupt practice in the future, or of political interference steering outcomes for political advantage.

It is also noted that “We could potentially achieve similar outcomes under a so-called “structural bail-in”.” (RBNZ, 2024, p.42). But who chooses the conditions of the structure? There is no transparency to this model, which provides the opportunity and thus the suspicion of outcomes being structured for the benefit of favoured parties or of political interference.

These three cases can represent mission creep into areas of capitalisation, ownership and structure, where the central bank usurps some of the responsibilities inherent in private sector governance and management. These skills are not normally seen as central bank competencies.

Such usurpation could instead foster greater risk-taking behaviour by these institutions, secure in the knowledge that favourable outcomes will be captured by the management and shareholders, while adverse outcomes will have the RBNZ rescuing the institution from the impact of its own choices. There is a moral hazard risk inherent with deploying the bail-in tools in this manner.

e. Derivatives

The RBNZ stated that “it would be very complex to convert senior-ranking claims into shares in practice, noting these claims could include uninsured deposits, derivative liabilities, and liabilities owed to suppliers, payments systems and other counterparties” (RBNZ, 2024, p.42)

Beyond the complexities in such a system that almost ensures that there is no real chance of an equitable outcome for individual depositors, one has to consider the role of derivatives in this situation.

The global derivative market has grown to such an extent that the ordinary financial economy has been dwarfed in comparison. There are some estimates that the global derivative market is now

some 4 Quadrillion US dollars in size, compared to a 2023 global GDP of US$105.44T (World Bank, 2024) - i.e. derivatives are some forty times the size of GDP.

While one can suggest that the large international banks are the main participants in the derivative market and that this has less bearing on the New Zealand situation, it should be recognised that Australian financial institutions are very active in the global financial space, and thus there is a derived risk for their local subsidiaries.

It would be better to ring fence derivatives from any bail-in proposition to reduce the moral hazard inherent in the derivative space, and to isolate New Zealand exposure to a market that would be beyond the capacity of any institution in New Zealand, including the RBNZ or the New Zealand Government, to contain without decimating the local currency and financial system.

f. TLAC

The RBNZ is proposing forcing institutions to set aside funds to meet future failures. Specifically, it is stated that "Total loss-absorbing capacity (TLAC) ... require relevant deposit takers to hold additional financial resources beyond going-concern capital, in a form that can be used to allow recapitalisation in the event of resolution" (RBNZ, 2024, p. 42).

It is a basic principle upon which the insurance industry is founded that the accumulation of diverse risk into a single fund reduces the overall cost of risk. Even if a TLAC was feasible, which is presumably not in a world where banks hold significant amounts of derivative contracts, this is a proposal to shift the cost of risk from a central source, such as publicly funded bail-in option, to multiple funds held and managed by each institution separately. There will be an inevitable increase of cost to society in this option versus the alternative of publicly funded bail-ins, thanks to the unwinding of increasing returns resulting from the diversification of risk through its centralisation.

There may well be political advantage to the TLAC, in that the costs will be hidden from political accountability from the public, but this political advantage would come at the cost of real economic disadvantage from the raised cost of capital to society in general.

It is suggested that "TLAC would be held by either professional investors or (if applicable) a parent entity who should arguably be relatively well placed to take on and understand this risk" (RBNZ, 2024, p.43). It is also acknowledged that "TLAC also comes with its own challenges...Lessons from the failure of Credit Suisse highlight that the potential challenges that can arise where TLAC investors are not fully aware of their exposure to bail-in, and where TLAC is issued across multiple jurisdictions"" (RBNZ, 2024, p. 43).

One can conclude however that the past forty years of financial experience suggests otherwise, and the noted example of Credit Suisse is merely a recent example of failure, or indeed incapacity, within the financial sector to recognise the risks inherent within the system at any particular time. Indeed, the creation of formalised TLAC may well entrench financial interests and reduce flexibility, thus working directly against the development of effective counter-measures for actual risks. Meanwhile, there has been increasing concentration of risks during this multi-decadal period through the concentration of the financial sector into ever larger firms, which has raised the cost to society of each failure.

Indeed, one can suggest that it is the hubris of policy makers and industry insiders that has led to a complicated obfuscation of the problems from increasing financial risk, and has deflected the capacity of society to deal with the underlying issues. It is quite possible that TLAC is likely to end up being recognised as merely another of these deflections.

Thus, it is noted that the RBNZ is undecided regarding TLAC and is “still considering whether or not to introduce TLAC requirements...future TLAC requirements would be in addition to existing minimum capital and buffer ratio requirements, not instead of these existing requirements” (RBNZ, 2024, p.43).

The recommendation is to not proceed with TLAC. It is unlikely that any local implementation will have a meaningful impact in a future crisis, as the facility is likely to be overwhelmed by the scale of the issue, while the costs of such a policy will undoubtedly be fully borne within the New Zealand society. It is hard to see where the economic benefits in practice of such a policy would outweigh the costs. Any fleeting political benefits by portraying one as ‘doing something’ will be surely paid for by significant and ongoing economic costs.

Q4. Do you have any view on the potential new crisis preparedness requirements (i.e., recovery and exit planning, and resolvability)? If these requirements were imposed, do you have any initial comments on how they should be designed?

The crisis preparedness measures rely on having a sound understanding of the risks involved. This is likely to be problematic.

In regard to the identified areas of risk (RBNZ, 2024, p. 58-59):

- Valuations may work well in a period of equilibrium (i.e. normality), but during a financial crisis valuations rapidly become unreliable or at least outdated.
- Funding may be stated as being available and sufficient in a time of stress, but with contagion being a real possibility during a crisis, reality could prove quite different.
- Operational continuity is a lofty goal, but once confidence is broken it may prove hard to restore; with the same dynamic applying to continuity of financial contracts.
- Restructuring, communications, management and governance are all aspects that are most likely to be better decided ad-hoc based on the circumstances at the time.
- The concern regarding Access to Financial Market Infrastructures may become a moot point over the next few years, with the RBNZ's Open Banking initiative potentially negating the effects of any institution being denied access to other systems.

Thus, there is a strong likelihood that the real risks will not be recognised or at least adequately scoped and scaled, and thus the planned measures are likely to prove insufficient or even counter-productive.

There is a point at which regulators, no matter how talented and well intentioned, cannot withstand market pressures and it is better to let radical change develop in order to wash away the malinvestments that led to the situation in the first place. The alternative is to weaken society in general in a forlorn bid trying to prevent a change that is beyond the power of society to resist.

Having said all of that, if one was to proceed with crisis preparedness requirements, then one has to be realistic. The RBNZ approach is that "the Crisis Preparedness standard could require that deposit takers (1) are able to achieve various outcomes to support orderly resolution; (2) have specific capabilities and arrangements in place to do so; and (3) suitably oversee, document, test and assess their compliance with these requirements, as well as their overall resolvability (RBNZ 2024, p. 59). This approach is easy to state and probably impossible to implement in practice during a crisis that carries systemic risk to the monetary system. Beforehand, one can pretend to meet these goals, and until tested, such an approach can help project an aura of false confidence, but when a real crisis emerges one can be assured that assurances of meeting such requirements will prove as robust as those of Financial Soundness indicators in cases of recent major bank failures, such as Silicon Valley Bank – i.e. not at all.

Radical change will occur. We can be sure of that. History also teaches that it will come from a quadrant that had previously been considered unimportant or sound. History is littered with figures who thought that they had foreseen all eventualities, only to be proven mistaken. It is purely hubris to think that the next crisis will be any different.

Resolution of a crisis requires flexibility and creative thinking. These are not the hallmarks of any government or central bank, but are the hallmarks of a free market. If one really wants to resolve the next crisis at the minimal economic cost, the optimal solution is to free the market and let the market self-correct on its own, and better to adopt such measures before the crisis develops than afterwards. That is the counter-factual that the RBNZ can consider when developing any approach in this field.

Q5 Are there any other aspects of crisis management we should be considering as part of our review?

One has to consider who is best placed to meet the cost of any action, and who is in the best place to make decisions in regard to localised circumstances. These are likely to be different players in the system.

Crisis Management is a serious topic, and the first priority is to not make the situation worse through misguided approaches, no matter how well intended.

Pre-positioning resources and planning responses is highly likely to go awry. Strategic planning has been well recognised within the Strategy field to have severe limitations, largely due to imperfect information, limited decision-making capability and an inherent bias of those acting prior to a crisis based upon previous crises, thereby creating a frame blindness to the actual nature of any threat.

Crises happen, and there can be good long-run results if long periods of malinvestment are readjusted so that society can make better use of resources. The result may be painful for many involved, but the costs of decisions should fall on the decision-makers, as should the benefits.

Corporate welfare, in the sense that the Government or central banks make institutions or management partially or wholly immune to the consequences of their decision-making, induces moral hazards that can induce enormous costs upon society at large. The very fact that bail-in provisions are being considered as being necessary at all is indicative that we are nearing the end of an economic cycle, where such moral hazards have induced large amounts of malinvestment, and that it is intuitively recognised that the pressures of adjustment will cause substantial pain throughout society.

However, sometimes we should just allow change to occur, as it is the least painful course of action in the long term. We suggest that we are experiencing one of these times, and thus recommend that bail-ins should be abandoned in New Zealand as a suboptimal policy for New Zealand society in the long term.

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New Zealand Banking Association
Te Rangapū Pēke

Submission

to the

The Reserve Bank of New Zealand - Te Pūtea Matua

on the

Crisis Management under the Deposit Takers Act 2023 Issues Paper

22 November 2024

NEW ZEALAND BANKING ASSOCIATION – TE RANGAPŪ PĒKE
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About NZBA

1. The New Zealand Banking Association – Te Rangapū Pēke (**NZBA**) is the voice of the banking industry. We work with our member banks on non-competitive issues to tell the industry's story and develop and promote policy outcomes that deliver for New Zealanders.

2. The following eighteen registered banks in New Zealand are members of NZBA:
   - ANZ Bank New Zealand Limited
   - ASB Bank Limited
   - Bank of China (NZ) Limited
   - Bank of New Zealand
   - China Construction Bank (New Zealand) Limited
   - Citibank N.A.
   - The Co-operative Bank Limited
   - Heartland Bank Limited
   - The Hongkong and Shanghai Banking Corporation Limited
   - Industrial and Commercial Bank of China (New Zealand) Limited
   - JPMorgan Chase Bank N.A.
   - KB Kookmin Bank Auckland Branch
   - Kiwibank Limited
   - MUFG Bank Ltd
   - Rabobank New Zealand Limited
   - SBS Bank
   - TSB Bank Limited
   - Westpac New Zealand Limited

Introduction

3. NZBA welcomes the opportunity to provide feedback to the Reserve Bank of New Zealand - Te Pūtea Matua (**Reserve Bank**) on its issues paper "Crisis Management under the Deposit Takers Act 2023" (**Consultation**). NZBA commends the work that has gone into developing this document and the technical analysis supporting it.

Contact details

4. If you would like to discuss any aspect of this submission, please contact:

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- *Q1 Do you have any views on our proposed approach to implementing the crisis management framework under the DTA? Are there any factors we should, or should not, take into account when implementing the framework?*

NZBA supports general proposed approach to crisis management, but coordination, consistency and clarity are key

General support for approach

5. NZBA is generally supportive of the Reserve Bank's proposed approach to implementing a new crisis management framework.

6. We agree with the move to reflect international best practice and modernise approaches (particularly consistency with the FSB's Key Attributes (**Key Attributes**) and their compliant regimes such as Australia, the United Kingdom and Hong Kong)) – noting however our responses to question 3 in relation to contractual and statutory bail-in in the New Zealand context.

7. We also support further engagement on crisis management with members of the Council of Financial Regulators and (in relation to Group 1 deposit takers) Australian financial authorities.

Coordination, consistency and clarity are key

Implementation of Crisis Preparedness Standard

8. As noted in the Reserve Bank's concurrent Non-core Standards Consultation it is proposed that the OBR Pre-positioning Standard will be implemented in 2028, whilst the Crisis Preparedness Standard is proposed to be implemented in 2028 or 2029, and subject to a legislative backstop of July 2029.

9. We submit that the Reserve Bank should consider at an early stage how these Standards will interact, and provide guidance on this. In particular it would be helpful for industry to have an understanding of the extent to which the requirements included in the OBR Pre-positioning Standard will be moved into the Crisis Preparedness Standard, and whether, as a consequence, aspects of the OBR Pre-positioning Standard will be effectively superseded by the Crisis Preparedness Standard.

10. Given the significant work that deposit takers will need to undertake to comply with both standards we strongly encourage the Reserve Bank to avoid overlapping, conflicting or superseding requirements, particular given the gap between implementing these standards could be at most a year. This is especially so if it would otherwise result in deposit takers having to adopt a two stage approach, whereby deposit takers are required to significantly amend or build systems for an initial/temporary OBR Pre-positioning Standard to only then have to rebuild them for a Crisis Management Standard.

11. Considering these matters at an early stage should allow the Reserve Bank to avoid any potential delays in the implementation dates described above, while minimising unnecessary cost.

Preparation of consolidated Crisis Management Standard

12. NZBA considers that the Reserve Bank should progress work on a consolidated Crisis Management Standard discussed under "Enhanced crisis preparedness" in the table below paragraph 12 of the Consultation (which should be scheduled for implementation after the mid-2028 target for the non-core standards).

13. We consider that the Crisis Management Standard should be developed as a single Standard that, as overarching principles:

    13.1. brings the current requirements together in order to reduce duplication and potential for inconsistency between the relevant Standards; and

    13.2. otherwise carries forward the substantive position with the OBR Pre-positioning Standard, Outsourcing Standard and Crisis Preparedness Standard (as well as the Operational Resilience Standard as discussed in paragraph 17). This should be used to streamline unnecessary costs involved in complying with three separate standards (OBR Pre-positioning Standard, Outsourcing Standard and Crisis Preparedness Standard), rather than creating new or substantially altered requirements.

14. To be clear, NZBA does not advocate a delay in starting work on drafting the OBR Pre-positioning Standard (or other Standards that are to be consolidated into the Crisis Management Standard) in order to have these finalised in line with the current proposed timeline (i.e. by January 2027). Rather, we submit that the Reserve Bank should bring forward the start of the work on the proposed Crisis Management Standard so that it runs in tandem with the work on the other Standards.

Coordination with regard to OBR pre-positioning and outsourcing

15. As discussed in more detail in our submissions on the OBR Pre-positioning Standard and Outsourcing Standard, as part of NZBA's submission on the consultation on non-core standards (**Non-core Standards Consultation**), NZBA considers that it is not desirable to maintain separate OBR pre-positioning, Outsourcing and Crisis Preparedness Standards in the longer term. With this in mind, any changes to OBR pre-positioning made now should be done as part of a planned shift towards a single Crisis Management Standard.

16. The Reserve Bank's work on crisis management should inform developments in OBR pre-positioning and outsourcing, and any changes to existing resolution strategies (including the extent to which they impact on outsourcing) should, wherever possible, only be made where they will be consistent with the Reserve Bank's final crisis management framework, in order to avoid unnecessary and potentially highly costly rework.

Additional comments on scope and interaction of Standards

17. We also note that footnote 255 (at paragraph 888) of the Non-Core Standards Consultation Paper outlines that the Reserve Bank will need to consider how "systematically important activities" might intersect with "critical operations" in the context of the Crisis Preparedness Standard. We would welcome the Reserve Bank providing further information on this intersection in the crisis management and crisis preparedness context, particularly given the significant changes to the deposit taking sector scheduled to occur in 2027 - 2028.

18. Additionally, we request that the Reserve Bank clarifies the scope of the Crisis Preparedness Standard. We understand that the Reserve Bank is still considering the extent to which branches of overseas banks will be included, although it is conscious of the limited role that branches generally have in the New Zealand financial system. However the Consultation includes examples of critical functions (Box 2: Systemically important activities, page 26) which include activities that could be offered by branches. We ask that the Reserve Bank provide this clarification as soon as practical to ensure the relevant entities are able to prepare accordingly.

- *Q2 Do you have any comments on our proposed approach to dealing with distressed deposit takers under the DTA? Are there any alternative approaches we should be considering?*

More clarity on the approach to dealing with distressed deposit takers will be required in advance of resolution

Clear Reserve Bank guidance on approach to resolution

19. Under the DTA, the Reserve Bank has a very wide discretion to recommend a deposit takers be placed in resolution and the Consultation proposes that the Reserve Bank would also have very wide discretion to apply a large number of relatively complex resolution tools, once a deposit taker enters resolution. The Consultation does not include any information explaining how that discretion might be applied, including which tools might be more or less relevant for each group of deposit takers or the grounds on which the Reserve Bank might choose one tool over another (nor does the Consultation suggest that this type of guidance will be produced).

20. NZBA is concerned that the Reserve Bank's proposed approach to resolution might have adverse impacts, including:

    20.1. for some deposit takers, the efficiency and complexity impacts of having to comply with multiple regimes. This includes:

        (a) compliance across multiple standards covering similar matters and potentially overlapping requirements (as discussed above); and

        (b) requirements for deposit takers that are part of international banking groups to maintain preparations for group-led resolution (driven by the rules of the home authority, which are generally closely aligned with the Key Attributes) alongside substantially different requirements under the DTA;

    20.2. creation of unnecessary uncertainty as to which tool might be used in resolution, among deposit takers, depositors, investors and other stakeholders. Simplicity and a high-level of certainty regarding New Zealand's crisis management framework is key to attract investment to New Zealand. As a related point, the Reserve Bank should not be requiring deposit takers to pre-position for a resolution tool that will not be used for that individual deposit taker in reality; and

    20.3. increasing the risk of conflict between new and updated crisis management related standards, given the complexity and high degree of optionality

involved, already evidenced in the historical challenges in aligning existing resolution standards.

21. NZBA strongly recommends developing (and setting out in clear guidance) a standardised approach to crisis preparedness and resolvability, repackaging continuing resolution tools with new resolution tools into a single well-aligned and harmonious resolution framework.

22. To reduce complexity and uncertainty, we recommend there be a hierarchy of resolution options, and/or a clear indication of whether the Reserve Bank's preferred resolution tool for each deposit taker is bail-in, transfer/ sale or insolvency (based on size / systemic importance) (i.e. similar to the model in the United Kingdom).

23. To the extent permitted under the DTA, we request that the Reserve Bank more closely align its crisis management framework to the Key Attributes, which provide for a crisis management framework that has:

    23.1. simple and clear crisis management objectives for both rule setting and regulatory decision making;

    23.2. clear delineation between business as usual, recovery and exit and resolution stages;

    23.3. appropriate and transparent triggers to move between stages, with the trigger for resolution being non-viability of the deposit taker;

    23.4. appropriate and ongoing engagement, detailed forward planning and testing between home and host resolution authorities; and

    23.5. detailed regulatory guidance that ensures stakeholders have a clear understanding of the basis on which home and country regulators would exercise their discretions.

Clear delineation between recovery and exit, and resolution

24. The Key Attributes provide for clear delineation between crisis management stages (being business as usual, recovery and exit and resolution). This delineation is important when determining the point at which the deposit taker enters in or out of resolution and who bears responsibility for decision making and managing the affairs of the deposit taker both before and after.

25. While the diagram in paragraph 51, Table C separately identifies all resolution tools, the Reserve Bank states elsewhere that "recovery and resolution processes are likely to overlap in practice" (para. 235).

26. It would be helpful for the Reserve Bank to confirm that it intends to treat recovery and exit and resolution as operationally separate.

Clarity on triggers for moving between stages

27. The DTA grants the Reserve Bank significant powers over a deposit taker once it enters resolution. Triggers for resolution under section 280(1)(a) of the DTA extend beyond non-viability to include circumstances where the deposit taker has:

27.1. contravened, may have contravened, or is likely to contravene a requirement under an applicable standard, or a condition of its licence, to maintain a minimum amount (or ratio) of capital;

27.2. contravened a direction given under subpart 3;

27.3. persistently or seriously contravened any other 'prudential obligation' (extended to include AML/CFT requirements),

provided that the Reserve Bank "is satisfied that there is no reasonable prospect of the matters that apply under paragraph (a) being adequately dealt with to [its] satisfaction in a timely and orderly way other than through resolution."

28. This means that, in a number of respects, the Reserve Bank has a far greater discretion under the DTA to trigger resolution than would be found in regimes aligned to the Key Attributes (where non-viability is a pre-condition for resolution, and in some cases must be evidenced by a third-party non-viability assessment).

29. Given the Reserve Bank's wide discretionary powers, it seems essential that the Reserve Bank provides guidance regarding how it intends to exercise its discretion, particularly in circumstances where a deposit taker remains viable.

30. On a similar note, it should be made expressly clear that a direction order is not intended to automatically trigger BS11 bank separation. If such a trigger was intended, further would be needed around the resolution hierarchy having regard to BS11 bank separation and Group led resolution, and how that might work in practice under the DTA.

31. Finally, we would like to better understand the grounds on which the Reserve Bank might recommend the end of resolution under section 282.

32. Without clear guidance, we are concerned that the Reserve Bank's broad resolution powers, combined with low threshold triggers for resolution, will create significant uncertainty and a lack of market transparency for when resolution might be triggered.

Advance engagement between home and host resolution authorities

33. NZBA strongly supports the Reserve Bank's inclusion of Group led resolution as an appropriate resolution tool for foreign owned deposit takers. We also support the ongoing engagement between APRA and the Reserve Bank on crisis management (where appropriate and proportionate depending on the type and nature of deposit taker), particularly through the Crisis Management Group.

34. The Consultation refers to the 2010 Memorandum of Cooperation on Trans-Tasman Bank Distress Management between APRA and the Reserve Bank. In light of more recent changes to the FSB's crisis management framework and Australia's crisis management framework and now the Reserve Bank's own proposed changes, we are keen to understand whether APRA and the Reserve Bank have plans to revisit this Memorandum, to ensure it remains fit for purpose.

35. It would also be helpful to understand whether APRA and the Reserve Bank plan to develop institution specific cross border cooperation agreements for each key foreign owned bank (along the lines recommended under Annex 2 of the Key Attributes).

36. We recognise that the Statement of Approach to Resolution will include information on the Reserve Bank's approach to cooperation with Australian financial authorities. However, that document will not be made available to deposit takers until mid-2029 (a full year after the DTA is expected to come into force).

Additional work required for use of bridge institution tool

37. In principle we support the potential usage of a bridge institution (as has been used in a number of international examples). However, we consider that significant additional work will be required by the Reserve Bank, as well as dedicated resourcing, in order to effectively use a bridge institution tool (consistent with the Consultation's comments at paragraphs 123 and 124). In particular, we agree that further analysis would be required on how this may be adequately capitalised, noting that any framework should not be imposed on industry at a time of likely market stress.

- *Q3 Do you agree with our assessment of the costs and benefits of a potential statutory bail-in power? Are there additional costs or benefits we should consider? Do you have any view on the need for statutory bail-in powers given the structural and contractual bail-in options are already available with the powers under the DTA?*

Any new bail-in regime needs to be carefully considered, and it is not clear that such a regime is required given New Zealand's capital requirements

New bail-in regime unnecessary in the New Zealand context

38. It is not clear that introduction of statutory bail-in (by amendment to the DTA) has any strong drivers.

39. The decisions made by the Reserve Bank during the Capital Review (resulting in banks needing to fully meet the new capital requirements in 2028) will result in New Zealand banks being extremely well capitalised by international standards.

40. Structural bail-in options are already available under the DTA (without creation of a specific Standard), and the Reserve Bank's other powers will provide for a workable resolution regime without the need to develop an additional statutory bail-in regime.

41. Further, as discussed below, we consider that any decision to expand bail-in would inevitably need to include Additional Tier 1 (**AT1**) and Tier 2 instruments. However:

    41.1. Introducing a statutory bail-in regime at this point in the overall prudential supervision review will add additional complexity to both the DTA and the features of capital instruments. This would be in contrast to one of the objectives of the Capital Review, to reduce this complexity.

    41.2. Making AT1 and Tier 2 subject to bail-in would also introduce unnecessary complexity for investor relations and the treatment of legacy (existing) AT1 and Tier 2 (as acknowledged in footnote 64 at paragraph 200 of the Consultation). The confusion this would create in the market and with investors is likely to result in unnecessary increased compliance costs (inconsistent with the principles that the Reserve Bank must take into account, as described in paragraph 48 of the Consultation). It is vital that any statutory changes do not create uncertainty for international investors

looking to invest in New Zealand deposit takers, otherwise funding costs for the market generally will be increased and potential supply may reduce.

Bail-in cannot be adequately considered without revisiting decisions from the Capital Review

42. NZBA understands that the Reserve Bank does not intend to revisit decisions from the 2017-19 Capital Review (which determined to remove contractual bail-in mechanics from regulatory capital instruments) as part of this Consultation.

43. If the Reserve Bank does consider it necessary to introduce new bail-in requirements, we consider that the structure of regulatory capital instruments (and the Capital Review generally) must be revisited.

44. Introducing statutory bail-in and not applying it to regulatory capital instruments (as per the outcomes of the Capital Review) would effectively require a new form of 'bail-in-able' senior instrument (as discussed in paragraph 162 of the Consultation). If the Reserve Bank were to let this happen, we consider that it would have a number of undesirable consequences.

45. Such an approach would not respect the "capital stack", as it would leave existing AT1/Tier 2 instruments outstanding while using new 'bail-in-able' senior instruments to absorb losses. Notwithstanding the 'no creditor worse off' safeguard, we consider that New Zealand would be an unjustified outlier in this respect, and, accordingly, such a decision could adversely affect deposit takers' ability to issue such instruments in the financial markets.

46. Further, as a practical matter, the creation of such a 'bail-in-able' senior instrument would be redundant or inappropriate and would create unnecessary issuance costs:

    46.1. In relation to Group 1 deposit takers, international standard 'total loss absorbing capital' (**TLAC**) requirements could be met just by making New Zealand AT1 and Tier 2 instruments bail-in-able given existing ratio requirements (set by the Reserve Bank to provide that the likelihood of a deposit taker resolution is approximately 1-in-200 years), rather than creating a whole new tier of instrument that reintroduces the complexity that the Capital Review sought to remove. This could efficiently be achieved by re-introducing contractual bail-in on such AT1 and Tier 2 instruments.

    46.2. In relation to Group 2 deposit takers, we note that internationally TLAC is typically reserved for very large banks. The TLAC standard was developed by the FSB to apply to globally systemically important banks (G-SIBs) – banks many times the size of New Zealand's participants. Adopting a proportionate approach, consistent with the original development of TLAC, there is no clear need or driver to impose such bail-in on Group 2 deposit takers.

47. Moreover, given the introduction of the DCS to protect depositors, effectively only uninsured senior liabilities would remain available for statutory or contractual bail-in.

If bail-in is further considered, extensive engagement should be undertaken and the Capital Review decisions must be revisited

48. If the Reserve Bank does intend to continue exploring statutory or contractual bail-in options, then a wider, robust, cost/benefit analysis would be needed. This is especially

so given the current high capital requirements mean that the increased benefit would be marginal, and there would be real costs involved.

49. Furthermore, given the concerns and comments discussed in this submission, and consistent with the suggestion at paragraph 202 of the Consultation and the fact that the current Consultation is preliminary by design, extensive and constructive engagement would be required with industry at a detailed level to work through the proposals and discuss all relevant issues. For instance (and without limitation):

    49.1. Clarification would be required as to whether the Reserve Bank intends to use bail-in in resolution only or whether it also might be applied in advance of resolution (the latter approach being used in Australia, and consistent with a contractual bail-in approach as discussed above);

    49.2. For overseas owned deposit takers, if Group-led resolution is the first tool used (including loss absorbing at Group level), clarity would be required as to whether bail-in of instruments from the New Zealand subsidiary would be used only if a Group-led resolution failed;

    49.3. Consideration would need to be given to features that might make bail-in instruments attractive to investors (both in New Zealand and overseas);

    49.4. Consideration should be given as to the degree to which costs of issuing bail-in might be mitigated by having regard to credit agencies' considerations; and

    49.5. Would OBR functionality (beyond customer account access) still be required if a robust bail-in framework was put in place? As a deposit taker can be placed in resolution while still solvent (e.g. at the point a (possibly high) minimum capital ratio is, or may potentially be, breached) then a tool freezing, and presumably in the future bailing-in, senior preferred creditors seems unwarranted.

- *Q4 Do you have any view on the potential new crisis preparedness requirements (i.e., recovery and exit planning, and resolvability)? If these requirements were imposed, do you have any initial comments on how they should be designed?*

Requirements to Prepare for Potential Distress and a Crisis Preparedness Standard

The Reserve Bank needs to be clear in communicating its expectations for recovery and exit planning by deposit takers

50. The proposed requirements for deposit takers to undertake recovery and exit planning during normal operations are extensive and will require significant resource. They include a requirement on deposit takers to consider an extremely wide range of potential (hypothetical) scenarios and continuously assess them in the context of a wide ranging set of potential recovery or resolution tools.

51. To support compliance and a consistent standard across industry, we ask that the Reserve Bank provide a set of crisis management scenario(s) for deposit takers to complete. It would avoid the risk of multiple crisis tests needing to be run across multiple scenarios, which could result in testing fatigue. Additionally, this would allow

the Reserve Bank to have a consistent standard and view across industry, enabling the Reserve Bank to have a better informed holistic view of crisis preparedness across the industry.

52. Given this task the Reserve Bank should be clear in communicating its expectations for recovery and exit planning by deposit takers during normal operations, and should be seeking to actively engage with industry at the earliest convenience to gauge deposit taker capability to carry out this planning.

It is important to ensure consistency with international approaches to recovery and exit planning

53. We note the Reserve Bank's objective is to ensure that recovery and exit planning across banking groups is consistent, including the expectation that deposit takers who belong to overseas deposit-taking groups develop their local recovery and exit plan in a consistent and coordinated manner with their overseas deposit taking group.

54. In order to best enable this, we submit that (where appropriate and proportionate) the Reserve Bank should seek to align any resolvability assessments and recovery and exit planning requirements with international requirements (particularly having regard to APRA requirements in relation to the Group 1 deposit takers). This would better enable deposit takers, which are members of overseas deposit-taking groups, to ensure their group and local recovery and exit plans are consistent, therefore enabling consistent resolution approaches in a group-wide recovery scenario.

55. The Consultation states that the recovery and exit planning requirements "would mostly be principles based" (paragraph 223), which would reflect the approach taken under Key Attributes (and adopted by other FSB compliant regimes).

56. However, the essential elements described in paragraph 220 appear very specific (as opposed to principles-based). We are concerned that these are likely to result in tick box planning, as opposed to a holistic, less siloed approach to planning. Ideally, these would be reframed at a principles level.

57. We also seek clarification as to whether branches of overseas banks will need to comply with the recovery and exit planning requirements, as we currently understand that these requirements may apply to all deposit takers. We note in this regard that in Australia, APRA's equivalent standard (CPS 190: Recovery and Exit Planning) specifically excludes branches (unless otherwise determined by APRA). This is consistent with the approach taken in other international jurisdictions (for example, the UK, US and the EU) where branches are not required to provide stand-alone recovery plans.

58. We submit that requiring branches to have recovery and exit plans is unlikely to be meaningful, given that branches do not have stand-alone New Zealand capital requirements and their liquidity is often managed centrally at a parent level.

Deposit takers need more clarity on timing

59. As discussed in our response to question 1, we submit that the Reserve Bank should closely consider, at an early stage, on how the OBR Pre-positioning standard (to be implemented in 2028) is proposed to interact with the Crisis Preparedness Standard (to be implemented no more than a year later in practice). Such early consideration will be vital to ensure there are no delays in implementation, while avoiding unnecessary compliance cost.

Resolvability

60. NZBA considers that execution risks will be significantly increased if resolution pre-positioning is spread across multiple standards.

61. The timing for the Reserve Bank's preparation of orderly resolution plans required by section 260 of the DTA are referred to in the Consultation, but the timeline remains uncertain. NZBA strongly recommends that the Reserve Bank commences this work early. The complexities and challenges of maintaining multiple standards, while seeking a high level of optionality, may only become truly clear once the Reserve Bank moves through that planning phase.

62. Further to our comments above, we believe that taking a holistic approach to identifying and prepositioning for capabilities and activities to support a range of resolution strategies is the better approach. This could be developed within a single Crisis Management Standard.

63. It will also be important to ensure that recovery and exit and resolvability planning requirements do not create a lot of unnecessary duplication of effort and information, which would have efficiency and cost implications.

Other Comments

- *Q5 Are there any other issues that we should consider when operationalising the crisis management framework under the DTA?*

64. The Consultation discusses developing the 'Sale of Business' tool (paragraph 110 onwards). If the Reserve Bank intends for deposit takers to pre-position this in their recovery and exit planning, then ultimately this would require industry-level solutions regarding customer transition and "on-boarding" matters such as AML and privacy.

65. Additionally, we would like to see the Reserve Bank consider setting up a centralised forum for deposit takers to allow fast and direct communication during a crisis event. The intention is that this would not interfere with the ability of the failing/failed entity and resolution authority to work through the crisis issues themselves. But a central communications forum would allow the rest of the industry to collaborate and respond in a more efficient and faster manner in relation to consequential issues affecting them during a crisis, qualities which are beneficial to effective crisis management.

Q#	Question	Response (Y/N)	Draft Response
1	Do you have any views on our proposed approach to implementing the crisis management framework under the DTA? Are there any factors we should, or should not, take into account when implementing the framework?	Y	Westpac in principle supports the policy direction to implementing the crisis management framework under the DTA as it reflects international best practice to crisis management. However, Westpac submits that, to the extent possible, it would be helpful for the RBNZ to consider how the OBR Pre-positioning, Outsourcing, DCS and Operational Resilience standards would work together to complement the Crisis Preparedness Standard moving forward. This is particularly important given the policy on crisis management is not as advanced as the other standards. This then supports a holistic approach to crisis management and would also prevent potential conflict and reduce complexity across the standards which in turn supports the DTA principle of the need to avoid unnecessary compliance costs. In addition, we would welcome further guidance in relation to footnote 255 of the Non-Core Standards Consultation Paper (i.e. reference to the concept of systemically important activities and critical operations) in the context of the Crisis Preparedness Standard. Given the large volume of transition occurring over the 2027 to 2028 timeframe, Westpac notes that further guidance from the RBNZ on the practical difference between systemically important activities and critical operations would support deposit takers' implementation and consistent application across the industry.
2	Do you have any comments on our proposed approach to dealing with distressed deposit takers under the DTA? Are there any alternative approaches we should be considering?	Y	The Crisis Management Issues Paper outlines the high-level process and expectations of deposit takers to ensure they are prepared for a crisis, however, Westpac considers that more clarity on the approach to dealing with distressed deposit takers is required in advance of resolution. In addition, we think it is important that any decisions on the policy direction do not overlap or conflict with existing requirements but instead look to replace or uplift them where required so that deposit takers are able to streamline the process(es).

Q#	Question	Response (Y/N)	Draft Response
			Westpac would welcome further information on the RBNZ's responsibilities as NZ's resolution authority (in both business-as-usual and in the event of a crisis) and the RBNZ's approach to enhancing its preparedness as the resolution authority. Westpac submits that it is important to delineate between the deposit takers' and the RBNZ's responsibilities and would support these being well defined to support economies of cost, for example, assessing the trade-off between all deposit takers setting up some resolution capability versus this being managed centrally by the RBNZ. This in turn supports the efficiency principle by ensuring there is no duplication of effort between deposit takers and the RBNZ where it is appropriate.
3	Do you agree with our assessment of the costs and benefits of a potential statutory bail-in power? Are there additional costs or benefits we should consider? Do you have any view on the need for statutory bail-in powers given the structural and contractual bail-in options are already available with the powers under the DTA?	Y	Westpac submits that the existing resolution regime available under the Deposit Takers Act (**DTA**) is sufficient. In this context, the NZ banks are already highly capitalised by international standards and will be especially so once the 2019 Capital Review initiative is completed in 2028. Hence Westpac does not see a clear need for additional new statutory bail-in powers due to the combination of globally leading NZ bank capital levels alongside the structural and contractual bail-in options already available i.e. The existing RBNZ's powers under the DTA provide for a workable future resolution regime, especially in the context of a 1 in 200-year event capital framework. In addition, in a post-Credit Suisse operating environment, Westpac submits that introducing a new class of bail-in instrument within a unique NZ framework where AT1 and Tier 2 capital instruments are not subject to bail-in, would lead to considerable capital hierarchy issues for both domestic and offshore investors. This consideration is especially topical given the RBNZ 2019 Capital Review decisions in relation to removing bail-in features from AT1 and Tier 2 capital instruments.

Q#	Question	Response (Y/N)	Draft Response
			However, should the RBNZ wish to explore the introduction of additional bail-in powers further, Westpac's view is that the below considerations and solutions could be key topics for further discussion and analysis: 1. **If introducing further bail-in powers, a statutory regime would be preferable** because it can mitigate several issues associated with the structural and contractual bail-in approaches (as set out in the Crisis Management Issues Paper). 2. **Westpac's suggested solution is that any additional new bail-in powers could be limited to new AT1 and Tier 2 capital instruments** for the following reasons: a) Making future new AT1 and Tier 2 capital instruments subject to these bail-in powers would result in a sizeable 4.50%+ of RWAs becoming bail-in-able over time. That 4.50%+ amount, combined with NZ's globally leading 13.5%+ levels of CET1 by 2028, will result in a significant level of bail-in across the capital stack which will compare strongly relative to other offshore jurisdictions, especially when measured on a globally harmonised basis. b) Making AT1 and Tier 2 capital instruments subject to bail-in would also be very well understood by investors globally i.e. it is very typical to see such terms & conditions included across other offshore jurisdictions and therefore it should not disrupt ongoing access to such markets. 3. **Creditor hierarchy considerations:** Utilising the above solution and limiting any new bail-in powers to future AT1 and Tier 2 capital instruments would avoid the considerable complexity associated

Q#	Question	Response (Y/N)	Draft Response
			with creating an entirely new form of NZ bank bail-in security (e.g. Tier 3 or Non-Preferred Senior securities) *co-existing alongside non-bail-in AT1 and Tier 2 capital instruments*. Notwithstanding the DTA's 'no creditor worse off' (**NCWO**) provision, this AT1 and Tier 2-centric solution would avoid the considerable capital hierarchy concerns that investors will have in a post-Credit Suisse operating environment i.e. Given current NZ AT1 and Tier 2 capital instruments uniquely do not have specific bail-in features, the future bail-in of a new class of e.g. Tier 3 or Non-Preferred Senior securities could essentially result in such instruments potentially absorbing losses in a crisis scenario ahead of the non-bail-in AT1 and Tier 2 holders. As such, we believe there is material uncertainty as to whether there would be the necessary international or domestic investor demand for that entirely new class of bail-in instruments. Westpac is not currently aware of any other jurisdiction globally where non-bail-in junior instruments co-exist alongside more senior bail-in-able securities and the 2023 failure of Credit Suisse has materially intensified global investor focus on capital hierarchy issues of this nature. 4. **Prospective bail-in application:** Westpac submits that any additional new bail-in powers should only apply to capital instruments issued after the new bail-in regime comes into effect and hence not apply to existing capital instruments on issue. This would provide grandfathering certainty to investors, thereby ensuring that the instrument's structural features remain consistent with those at the point of their investment. Given the considerations above, Westpac would welcome further engagement to discuss the operational challenges and potential solutions around this topic.

Q#	Question	Response (Y/N)	Draft Response
4	Do you have any view on the potential new crisis preparedness requirements (i.e., recovery and exit planning, and resolvability)? If these requirements were imposed, do you have any initial comments on how they should be designed?	Y	The current BS11 (Outsourcing) and BS17 (OBR) policies outline the requirements that need to be undertaken by a bank to get to a point of separation or invoking OBR. However, the current policies do not consider the broader impacts on the operations of the bank when executing BS11 and / or BS17. Examples of such impacts include (but not limited to): • **Contact centres:** once the bank reopens, contact centres will likely experience a high volume of calls and therefore need to be prepared for those, from a technology as well as staffing perspective. • **Legal team impacts:** higher volume of activities required to work through contracts and / or respond to legal actions taken against the bank. • **Branch impacts:** more customers will potentially visit our branches resulting in higher volume so deposit takers will need to prepare their branches (including staff) for this situation. • **Technology systems:** we expect these will experience a higher utilisation and as a result incidents may occur. • **Security threats:** we expect these to be higher than usual so deposit takers will need to be prepared for such attacks and threats. Westpac submits that the RBNZ should consider these broader bank impacts when developing the crisis management framework and Crisis Preparedness Standard as it would provide clarity to deposit takers on what is expected of them to ensure they are prepared for a crisis as well as ensure consistency in application across the industry. We note that such considerations could be in the form of guidance rather than requirements given the principles-based approach to the standards.
5	Are there any other issues that we should consider when operationalising the crisis management framework under the DTA?	Y	Westpac welcomes further guidance on which aspects of the crisis management framework would apply to branches given a branch is part of an overseas legal entity and any recovery measures are likely to be undertaken by the overseas bank. In addition, the Crisis Management

Q#	Question	Response (Y/N)	Draft Response
			Issues Paper notes that for branches, the RBNZ would look to rely on the resolution actions initiated by the home resolution authority. Westpac submits that any crisis management related requirements for branches should be proportionate to the size and operation of branches in NZ given the restricted scope of activities that branches can undertake once the Branch Standard comes into effect.