Addendum 1

Operational notice pertaining to the committed liquidity facility

South African Reserve Bank

November 2015

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1. Background

1.1 During 2012, the South African Reserve Bank (Bank) approved the provision of a committed liquidity facility (CLF) in order to assist banks in meeting the requirements of the liquidity coverage ratio (LCR). Guidance Notes 5/2012 and 6/2013 were issued to inform banks about the details of acceptable collateral for the CLF. Guidance Note 8/2014 replaced Guidance Note 6/2013 and contained revised guidelines in terms of the acceptable collateral and other requirements for the CLF and other related conditions, while this Addendum to the Operational Notice (Addendum 1) provides details on the operational requirements thereof.

1.2 On 7 January 2013, the Basel Committee on Banking Supervision (the Basel Committee) published a document detailing changes to the definition of the LCR, including an expansion in the range of assets eligible as high-quality liquid assets (HQLA) and some refinements to the assumed inflow and outflow rates to better reflect actual experience in times of stress. The LCR was introduced on 1 January 2015, but the minimum requirement was set at 60 per cent and will rise in equal annual increments of 10 per cent to reach 100 per cent on 1 January 2019. Guidance Note 5/2015 replaces Guidance Note 8/2014 and contains revised guidelines in terms of the acceptable collateral and other related requirements for the CLF.

1.3 Addendum 1 clarifies the eligible collateral for CLF as well as the operational arrangements pertaining to a drawdown on the CLF by a bank. The Bank may from time to time amend Addendum 1. The Bank, however, will endeavour to give reasonable notice of any amendments, but reserves the right to introduce any amendment with immediate effect, if necessary. A legal contract will be negotiated between the Bank and any individual bank applying for the CLF and will be finalised and signed by the respective parties prior to the commencement of the year when the CLF will be required for LCR. The contract will be effective for a year.

1.4 The CLF is only available to the extent that it will cover an individual bank's shortfall for the LCR requirement, provided that such shortfall is attributable to a general shortage of HQLA in the South African financial system.

2 Application process for the provision of the committed liquidity facility

2.1 The facility is negotiated for a calendar year and is renewable on an annual basis.

2.2 Banks that apply for the CLF for the first time should apply to the Registrar of Banks before the end of July of the year preceding the year for which they require the CLF to provide sufficient time to negotiate a contract and ensure adherence to the collateral requirements. The CLF facilities for 2016 shall be granted only up to 30 November 2016, i.e. for 11 months. Thereafter the CLF will revert to a 12 month facility from 1 December to 30 November.

2.3 When a bank applies for CLF, the following process is followed. Banks should send the application letter via email to the Bank Supervision Department (BSD). The BSD will channel the letter to the Committed Liquidity Facility Implementation Committee (CLFIC). The application letter will contain the following documents:

- A document detailing the characteristics and identification of collateral to be lodged;
- Redemption sheet;
- Authorisation to enter into the CLF agreement from the Board of Directors of the particular bank; and
- CLF application motivation – detailing the reasons for entering into the CLF agreement.

2.4 Applications to make use of the CLF should be directed in writing to the Registrar of Banks, utilising the template provided in the CLF contract. Drawdown of the facility will be for a period of 31 days.

2.5 Detailed information on all collateral should be kept in the Collateral Management System as maintained by FMD or in any collateral management system approved by the Bank.

2.6 Commercial banks that intend rolling over an existing CLF the following year can apply to do so by the end of September of the preceding year for which they require the CLF.

2.7 The Bank reserves the right to adjust the amount of acceptable collateral required, the commitment fees and the drawdown fees when a facility is renewed.

3. Characteristics of the committed liquidity facility

3.1 Size of the facility

3.1.1 Each individual bank will be required to meet the level 1 HQLA requirement of the LCR on its own. The CLF is only available to banks with a LCR shortfall that can be attributed to a shortfall of HQLA in South Africa. The CLF will be capped at 40 per cent of the total amount of HQLA any particular bank is required to hold in rand.

3.1.2 For the purpose of entering into a facility agreement with the Bank during the phase-in period of the LCR (that is, for the years up to 2018), the size of the CLF will be capped at 40 per cent of the full HQLA requirement as projected for the year for which the application is made. For example, banks applying for the CLF in 2015, for implementation in 2016, should project their maximum full HQLA requirement for 2016, and the CLF would be capped at 40 per cent of this projected amount.

3.1.3 The amount of the CLF that can be recognised for LCR purposes that can be drawn down in stress will at all times be limited to the lesser of the amount of collateral that is lodged with the Bank, after haircuts, and the size of the facility that has been granted.

3.2 Commitment fees

3.2.1 Banks electing to make use of the CLF will pay a commitment fee to the Bank, even if they do not draw funds from the CLF. In order for the fee charged by the Bank to provide an incentive for banks to reduce their liquidity risk exposure, and therefore their dependence on the CLF, a scaled commitment fee will be applied. Banks with a higher dependence on the CLF will be charged a higher weighted average commitment fee, as set out in Table 1, which will be applicable to applications received during 2015 for facilities in 2016. The commitment fee, which will be the same for all banks, will be set on an annual basis, based on market conditions prevailing when a bank applies for the facility or if the facility is renewed. The annual fees will be payable in advance by the fifth working day of January of each year.

Table 1: Commitment fee structure of the CLF for 2016

CLF as percentage of required HQLA	***Proposed fee per tranche (basis points per year)***	***Weighted average fee* (basis points per year)***
≤10 per cent	30	30
>10 ≤ 20 per cent	40	35
>20 to ≤30 per cent	50	40
>30 to ≤40 per cent (maximum = 40 per cent)	60	45

*If full tranche is used in the calculation.

3.3 Drawdown procedures

3.3.1 In the event that banks draw funds from the CLF, they will be charged an interest rate equal to the Bank’s repo rate plus 100 basis points (equal to the Bank’s normal standing facilities). Any draw-down of funds will be for a period of 31 calendar days.

3.3.2 When a bank requests for a drawdown, the following process is followed. The commercial bank will submit the request to drawdown to the Registrar of Banks. For drawdown funds to be released on a particular day, banks should submit the required drawdown form by 09:00. Banks should note that once notification is received by the Bank, there is no withdrawal of the request for funds. The drawdown form is part of the CLF contract. No additional documents will be required during the drawdown application process.

3.4 Eligible collateral

3.4.1 The collateral should be in security format with the exception of other loans and advances that remain on the bank’s balance sheet. Assets selected as collateral should provide adequate credit risk protection acceptable to the Bank, while also limiting any distorting effects on the securities market. While specific criteria may be agreed with individual banks on a case-by-case basis, acceptable collateral that will generally be considered for the CLF comprises the following:

3.4.1.1 Listed domestic debt securities with a minimum credit rating of A- on a domestic rating scale (equivalent to BBB- on an international scale) by an eligible External Credit Assessment Institution (ECAI). For foreign listed debt securities, an international scale rating of BBB- or better will be accepted as collateral.

3.4.1.2 Notes of self-securitised pools of high-quality residential mortgage loans

a) Notes of self-securitised pools of high quality residential mortgage loans, which are ring-fenced in an insolvency-remote structure or SPI, shall qualify as collateral for the CLF. Such self-securitised assets should be managed and controlled in a similar way as a normal securitisation as required by the provisions of Government Notice No. 2 published in Government Gazette No. 30628 dated 1 January 2008 (the Securitisation Exemption Notice), the SPI created has to be insolvency remote.

b) A bank will be allowed to create more than one SPI that could issue commercial paper to qualify as collateral for the CLF, provided that the criteria and conditions set by the Bank in its approval of the securitisation are complied with. The composition of the underlying portfolio of assets should be specified in the securitisation application. The collateral has to be lodged with the Bank when the application is approved. The chosen composition needs to be maintained throughout the approved period to use the CLF.

c) For the residential mortgage-backed securitisation structures only, an external credit rating will not be required if the underlying residential mortgages adhere to the following criteria set out below. The Bank, however, retains the option to require an external rating.
   (i) The residential mortgages shall comply with the definition as specified in regulation 23(6)(c) of the regulations relating to Banks (the Regulations).
   (ii) The property against which a mortgage is granted shall be located in the Republic of South Africa. At the inception of the mortgage loan, the borrower should also be domiciled in South Africa.
   (iii) Residential mortgages shall be denominated in rand.

(iv) The residential mortgages shall be governed by the laws of the republic of South Africa.

(v) The residential mortgages shall be originated during the issuer's normal course of business under the applicable lending criteria.

(vi) The residential mortgage loan repayments shall not be in arrears for more than 90 days.

(vii) Mortgages over vacant land may be included.

(viii) The capital amount outstanding shall not exceed 80 per cent of the current market value of the property. The property has to be revalued at least once a year using the methodology approved for the normal course of business of the bank for residential mortgages.

(ix) The residential mortgages should have been on the bank's balance sheet for at least one year prior to being transferred to the SPI.

(x) On a quarterly basis, the collateral pool has to be reassessed to ensure compliance with all the relevant specified requirements. If a loan does not comply with all the relevant specified requirements, it has to be replaced immediately.

d) In conjunction with the CLF application banks will have to apply to the Registrar of Banks for the transfer of assets to the SPI, in terms of Section 54 of the Banks Act. The SPI will have to comply with the provisions of the Securitisation Notice to every extent possible. A pre-sale report produced by the rating agency (if externally rated) or by the bank itself (if internally rated) should form part of the application.

3.4.1.3 Commercial mortgages

a) In view of (i) the inherently higher credit risk attached to commercial mortgages, (ii) the complexity associated with the specification of credit risk criteria for commercial mortgages, and (iii) the fact that most banks have more than adequate collateral for the CLF even if commercial mortgages are excluded, the Bank is in principle not in favour of accepting commercial mortgages as collateral for the CLF. However, should a particular bank have an exceptional need to offer commercial mortgages as collateral, these will be considered on a case-by-case basis. An external credit rating will be required and haircuts will be applied based on this rating, as agreed on with the particular bank.

3.4.1.4 Loans other than mortgages

a) The Bank will accept other loans and advances, for example, vehicle and asset finance, as an eligible form of collateral for the CLF. The assets should also be transferred to a SPI, with commercial paper created with ISIN numbers and a five character stock code to serve as the collateral for the Bank. Banks with approval to use the internal ratings-based approach for credit risk will be allowed to rate the proposed structure internally. Banks on the standardised approach for credit risk will be required to have their asset pools externally rated by an eligible ECAI. The Bank, however, retains the option to require an external rating and to assign haircuts to the notes serving as collateral.

b) For a ring-fenced on-balance sheet asset pool (that is, no notes with ISIN numbers are issued against the loans), the Bank will provide minimum asset quality criteria. On a quarterly basis, the asset pool should be reassessed to ensure compliance with the requirements. If a loan does not comply with all requirements, the loan has to be replaced. In the event of drawdown, the Bank will provide a loan against the collateral, at an agreed haircut.

c) In the event of drawdown of a ring-fenced asset pool transferred to an SPI, the Bank will invest in the senior tranche of a securitisation structure, and will provide a liquidity amount less than the face value of the notes, that is, a haircut will be applied. Such haircuts will be agreed bilaterally with banks, based on the type, liquidity and credit quality of the underlying assets.

3.4.1.5 In general, all collateral for the CLF should have the following additional characteristics:

a) it has to be unencumbered;

b) securitised asset pools have to be audited on an annual basis; and

c) collateral shall have an outstanding maturity of more than one year.

3.4.2 The collateral requirements set out in this Addendum represent general guidelines on the Bank's preferences. The Bank may enter into bilateral contractual agreements with banks that apply for the CLF that could stipulate more specific collateral requirements.

3.4.3 The Board of Directors of a bank has to ensure that the collateral requirements have been met. The application pack for the CLF should include a signed letter from the bank's independent auditors confirming that the collateral requirements would be met.

3.5 Market-value adjustments (haircuts)

3.5.1 Market-value adjustments as set out in Table 2 will apply. These haircuts may be changed at any time at the discretion of the Bank when facilities are renewed.

Table 2: Market-value adjustments (haircuts)

International rating scale	National rating scale	Residual maturity	Sovereigns (percentage points)	Other issuers (percentage points)
AAA to AA-	n/a.	< 1yr	0,5	1
		> 1 yr < 5 yrs	2	4
		> 5 yrs	4	8
A+ to BBB-	AAA (zaf) to A- (zaf)	< 1yr	1	2
		> 1 yr < 5 yrs	3	6
		> 5 yrs	6	12

4 Disclosure requirements

4.1 Reporting on the CLF and the qualifying collateral should be done in terms of banks' BA200 and BA300 returns.

4.2 For annual financial reporting, the commercial banks should disclose that a CLF has been secured from the Bank. The Bank will reflect in its Annual Report the total CLF approved.

5 Legal implications and considerations

5.1 The collateral requirements represent general guidelines on the Bank's preferences. The Bank will enter into bilateral contractual agreements with banks that apply for the CLF which could stipulate more specific collateral requirements.

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