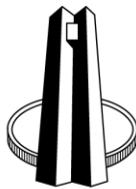


Addendum 1

Operational notice pertaining to the committed liquidity facility



South African Reserve Bank

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1. Background

- 1.1 During 2012, the South African Reserve Bank (SARB) 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, 8/2014 and 5/2015 were issued to inform banks about the details of eligible collateral for the CLF. Guidance Note 6/2016 replaces Guidance Note 5/2015 and attempts to address some areas of uncertainty identified and contains revised guidelines in terms of eligible collateral, pricing and other requirements related to the CLF for the period 1 December 2016 to 30 November 2017.
- 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.
- 1.3 Section 3.4 of this Addendum 1 to the Operational Notice provides details on the operational requirements. It specifies the eligible collateral for CLF as well as the operational arrangements pertaining to a drawdown on the CLF by a bank. The SARB may from time to time amend Addendum 1. The SARB 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 SARB and any individual bank applying for the CLF which shall be finalised and signed by the respective parties prior to the commencement of the period for which the CLF will be contracted.

1.4 The CLF is only available to banks that experience a shortfall in their LCR, provided that such shortfall is attributable to a general shortage of HQLA in the South African financial system. In return for the CLF facility, the banks are required to lodge acceptable collateral with the SARB.

2 Application process for the provision of the committed liquidity facility

2.1 The facility is negotiated for 12 months 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 (or another authority assuming the duties of the supervisory authority for banks) (the Registrar), by the end of August for a facility that commences on 1 December of the same year, in order to provide sufficient time to negotiate a contract and ensure adherence to the collateral requirements. Re-applications can be made on an annual basis and are due by 30 September. The CLF facilities shall be granted as a 12-month facility from 1 December to 30 November.

2.3 When a bank applies for the CLF, it should send an application letter to the Registrar. The application letter will contain the following documents:

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

2.4 Detailed information on all collateral lodged with the SARB under the terms of a CLF agreement shall be registered in the Collateral Management System as maintained by FMD or in any collateral management system approved by the SARB.

2.5 The SARB 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 For the purpose of entering into a facility agreement with the SARB, 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.

3.1.2 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 SARB, reduced by any applicable haircut, 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 an upfront commitment fee to the SARB, even if they do not draw funds from the CLF. For 2017, a flat commitment fee of 58 basis points is being charged. The commitment fee will be payable in advance by the fifth working day of December of each year.

3.2.2 The commitment fee is set by the SARB on an annual basis. In order to comply with the eligibility requirements for alternative liquidity approaches, (ALA) specified by the Basel Committee on Banking Supervision (BCBS),

the commitment fee is determined from a minimum value based on the difference between a three-year weighted average yield earned on assets that have been used as collateral for the CLF and a three-year weighted yield on a portfolio of government bonds and corporate bonds.

3.3 Drawdown procedures

- 3.3.1 Applications to draw on the CLF should be directed in writing to the Registrar, utilising the template provided in the CLF contract. 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 SARB, the request for funds cannot be cancelled.
- 3.3.2 In the event that banks draw funds from the CLF, they will be charged an interest rate equal to the SARB's repo rate plus 100 basis points (equal to the SARB's normal standing facilities).
- 3.3.3 Drawdown of the facility will be for a period of 31 days. Any subsequent drawdown will require a new application therefore. A request for renewal of the drawdown period (i.e. for another 31 days), should be submitted to the Registrar in writing at least two working days before the drawdown period expires.

3.4 Eligible collateral

- 3.4.1 With the exception of loans and advances that may remain on the balance sheet of a bank (refer paragraph 3.4.2.4 (b)), collateral should be in the format of securities that can be lodged with the SARB. Assets selected as collateral should provide adequate credit risk protection acceptable to the SARB.

3.4.2 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:

3.4.2.1 Listed domestic debt securities with a minimum South African national scale rating of A- issued by an eligible External Credit Assessment Institution (ECAI). For foreign listed debt securities, a global scale rating of BBB- or better will be accepted as collateral.

3.4.2.2 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 Special Purpose Institution (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 SARB 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 SARB 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 may not be required if the underlying residential mortgages adhere to the following criteria:

- (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 not 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 excluded from the calculation of eligible collateral immediately.
- d) The SARB retains the option to require an external rating prior to approving the CLF and collateral.

- e) In conjunction with the CLF application banks will have to apply to the Registrar 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.
- f) A minimum haircut of 5 per cent will be assigned to the notes serving as collateral.

3.4.2.3 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 SARB will in exceptional cases consider the acceptance thereof as collateral. An external credit rating will be required and based on the rating, a minimum haircut as specified in paragraph 3.5 will be applied.

3.4.2.4 Loans other than mortgages

- a) The SARB will accept other loans and advances, for example, vehicle and asset finance, as an eligible form of collateral for the CLF. The assets could 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 SARB. Banks with approval to use the internal ratings-based approach for credit risk will be allowed to rate the proposed structure internally, the SARB, however, retains the option to require an external rating. Banks on the standardised approach for

credit risk will be required to have their asset pools externally rated by an eligible ECAI. A minimum haircut as specified in paragraph 3.5 will be assigned 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 SARB 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 excluded from the collateral pool. In the event of drawdown, the SARB will provide a loan against the collateral, at an agreed haircut.

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

- a) it shall be unencumbered;
- b) securitised asset pools shall be audited on an annual basis; and
- c) collateral shall have an outstanding maturity of more than one year.

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

3.4.4 The Board of Directors of a bank shall ensure that the collateral requirements are met upon application for the CLF and throughout the contract period. The application pack for the CLF shall include a signed letter from the bank's independent auditors confirming that the collateral requirements have been met.

3.5 Haircuts on collateral

3.5.1 Minimum haircuts on collateral as set out in Table 1 will apply. These haircuts may be changed at the discretion of the SARB prior to the commencement of a new CLF contract period.

Table 1: Proposed minimum haircuts on securitised CLF collateral

Global scale rating	National scale rating	Residual maturity	Residential and commercial mortgages securitisation	Other securitisation
AAA to AA-	n/a.			
		> 1 yr ≤ 5 yrs	10%	10%
		> 5 yrs	12%	15%
A+ to BBB-	AAA (zaf) to A- (zaf)			
		> 1 yr ≤ 5 yrs	12%	15%
		> 5 yrs	17%	24%

4 Disclosure requirements

4.1 The look-through approach will be applied for assets transferred into an SPI, that is, for the calculation of minimum required capital relating to credit risk, the amount of capital that banks would be required to maintain shall be equal to the capital that would have been required if the assets had not been transferred to the SPI. Banks should report the assets that have been transferred to the SPI for CLF purposes in their original asset classes (e.g. residential mortgage advances) on the form BA200. The bank may not derecognise the assets and from a monthly regulatory reporting perspective, nothing changes.

4.2 For CLF monitoring purposes, banks will be required to complete the BA200 forms on a quarterly basis, based on the underlying assets in the SPI. This form shall be signed off by the respective bank's internal auditors.

- 4.3 The aforesaid internal audit sign-off shall be based on the controls-based audit in order to verify the accuracy and completeness of the reporting of assets maintained in the SPI and that reasonable control measures are in place for the SPI, that is, the transfer of assets in and out of the SPI and the risk management controls in place for the SPI are commensurate with those that are in place in the relevant business unit.
- 4.4 In its annual financial report, a bank shall disclose that a CLF has been secured from the SARB. The SARB will reflect in its Annual Report the total value of the CLF approved on aggregate.

5 Legal implications and considerations

- 5.1 The information contained in this Addendum represents the SARB's general conditions for the CLF. The SARB will enter into bilateral contractual agreements with individual banks that apply for the CLF, which could stipulate more specific collateral requirements.

6 Termination of the availability of the CLF

- 6.1 In an event that the SARB can no longer justify the use of the CLF as an ALA option, based on a market-wide shortage of HQLA, the availability of the CLF will be terminated. However, a three-year notice for such termination will be given to facilitate the orderly phase-out of the CLF as an ALA option and to allow banks time to rebalance their HQLA portfolios.

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