



SOUTH AFRICAN RESERVE BANK
Prudential Authority

DRAFT FOR FORMAL CONSULTATION– OCTOBER 2020

Prudential Standard FC02

Intragroup transaction and exposure requirements for financial conglomerates

Objectives and key requirements of Prudential Standard FC02

This Standard is made in terms of section 164 read with sections 105 and 108 of the Financial Sector Regulation Act, 2017 (Act No.9 of 2017) and requires the holding company to operate within the principles and comply with the requirements relating to intragroup transactions and exposures of financial conglomerates.

It is the responsibility of the board of directors of the holding company of a financial conglomerate to ensure that the financial conglomerate meets the requirements for intragroup transactions and exposures on a continuous basis.

This Standard prescribes the Prudential Authority's requirements in terms of the management of intragroup transactions and exposures, and sets down the reporting requirements for material or significant transactions.

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1. Commencement

- 1.1 This standard commences on 1 January 2022 (proposed)

Version number	Commencement date
1	1 January 2022

2. Legislative authority

- 2.1 This Standard is made in terms of section 164 read with sections 105 and 108 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (FSR Act).

3. Application

- 3.1 This Standard applies to the holding company of a financial conglomerate as designated by the Prudential Authority in terms of section 160 (1) read with section 160(2) of the FSR Act.
- 3.2 This Standard applies in addition to the financial sector laws which are applicable to specific financial institutions within a financial conglomerate.

4. Definitions and interpretation

- 4.1 The terms used in this Standard, unless indicated otherwise, are defined in the FSR Act and the financial sector laws, and have the same meaning in this Standard.

'auditor' means a registered auditor as defined in the Auditing Profession Act, 2005 (Act No. 26 of 2005);

'board' means the board of directors of the holding company;

'holding company' means the holding company of the financial conglomerate as designated by the Prudential Authority in terms of section 160(1) read with section 160(2) of the FSR Act;

'ITEs' means intragroup transactions and exposures that can take the form of a direct or indirect claim between members of the financial conglomerate or between the holding company and members of the financial conglomerate;

'member of the financial conglomerate' means a company that has been scoped into the financial conglomerate but excludes the holding company; and

'material or significant ITEs' as defined in paragraph 7 of this Standard.

- 4.2 The 'Objectives and key requirements of Prudential Standard FC02' that is italicised in the preamble of this Standard must not be used in the interpretation of any paragraph of this Standard.

5. Roles and responsibilities

- 5.1 The board is ultimately responsible for ensuring that the financial conglomerate complies with the principles and requirements of this Standard.
- 5.2 Where a financial conglomerate's control functions are required to perform certain functions in terms of this Standard, the board must ensure that the control functions regularly review and report to the board on the financial conglomerate's compliance with this Standard.
- 5.3 If requested to do so, the board and/or the auditor of the financial conglomerate must provide assurance to the Prudential Authority that the financial conglomerate complies with the requirements of this Standard.

6. Principles and requirements for ITEs

- 6.1 ITEs are means by which financial conglomerates rationalise capital and funding to enhance cost and operational efficiencies. Material or significant ITEs must be the focus of robust risk management practices due to the potential that such transactions can lead to contagion risk within the financial conglomerate.
- 6.2 The board must ensure that there is disclosure of material or significant ITEs to the Prudential Authority in accordance with the provisions of paragraph 9 of this Standard.
- 6.3 ITEs may originate through:
 - (a) cross shareholdings;
 - (b) trading operations whereby one member of the financial conglomerate or the holding company deals with, or on behalf of, another member of the financial conglomerate or the holding company;
 - (c) central management of short-term liquidity within the financial conglomerate;
 - (d) guarantees, loans and commitments provided to, or received from, other members of the financial conglomerate or the holding company;
 - (e) the provision of management and other service arrangements (e.g. pension fund administration and management);
 - (f) exposures to major shareholders of eligible financial institutions (including loans and off-balance sheet exposures, such as commitments and guarantees);
 - (g) placement of clients' assets with other members of the financial conglomerate or the holding company;
 - (h) purchases or sales of assets with other members of the financial conglomerate;
 - (i) transfer of risk through reinsurance to members of the financial conglomerate or the holding company ;
 - (j) transactions to shift third-party-related risk exposures between members of the financial conglomerate as well as the holding company, including transactions with special-purpose vehicles or ancillary entities;
 - (k) insurance, reinsurance and retrocession operations; or

- (l) transactions that consist of several connected transactions where assets or liabilities are transferred to entities outside of the financial conglomerate, but ultimately risk exposure is brought back to the financial conglomerate.
- 6.4 The holding company of a financial conglomerate must identify material or significant intragroup transactions, and must take at least the following into account:
- (a) the specific structure of the financial conglomerate;
 - (b) the possibility of contagion effects within the financial conglomerate;
 - (c) the possibility of conflicts of interests;
 - (d) the solvency and liquidity position of the counterparty; and
 - (e) transactions among eligible financial institutions belonging to different sectors of a financial conglomerate, if not already reported to the Prudential Authority in terms of other financial sector laws.

7. Material or significant ITEs

- 7.1 Material or significant ITEs include those that would potentially have a material impact, either financial or operational, on the financial conglomerate. The Prudential Authority requires the Board to determine what it considers to be a material or significant ITE, and that this would vary according to the financial conglomerate's risk profile.
- 7.2 The materiality or significance of an ITE depends on the size, nature and complexity of the exposure to the holding company or eligible financial institutions. Where a material or significant ITE is identified, the board must understand the material drivers of this risk.
- 7.3 A financial conglomerate's governance arrangements, data capabilities, and reporting in relation to ITEs would reflect how the board makes decisions and oversees material or significant ITEs. The Prudential Authority requires data capabilities and ITE risk reporting to be relevant and appropriate for the intended purpose and to meet business specifications (i.e. fit-for-purpose) for the needs of the board and other decision makers in the financial conglomerate.

8. ITEs policy, process and procedures

- 8.1 The holding company must implement robust board-approved policies as well as risk management processes and procedures relating to ITEs, which policies, processes and procedures must:
- (a) capture all material or significant ITEs;
 - (b) include limits on acceptable levels for ITEs for the holding company and members of the financial conglomerate;
 - (c) ensure that adequate systems and controls are in place to continuously identify, measure, manage, monitor and report on material or significant ITEs of the financial conglomerate in a timely manner; and
 - (d) ensure that all material or significant ITEs outside the scope of solo and consolidated supervision, are adequately covered in the financial conglomerate's ITEs policy.

8.2 The ITEs policy must be:

- (a) reviewed, at least annually, by the board; and
- (b) subject to review by the internal audit function or the auditors of the financial conglomerate.

9. Reporting requirements

9.1 All material or significant ITEs must be reported to the Prudential Authority on a semi-annual basis.

9.2 The holding company may also be required to report ITEs to the Prudential Authority based on a threshold determined by the Prudential Authority.

9.3 The form and manner of regulatory reporting returns will be determined by the Prudential Authority and published on its website.

10. Regulatory action

10.1 If in the view of the Prudential Authority, a financial conglomerate has not complied with the principles and requirements of this Standard, the Prudential Authority may take appropriate regulatory action.