



South African Reserve Bank
From the Office of
the Registrar of Banks

C6/2010

2010-12-14

To: All banks, branches of foreign institutions, controlling companies, and auditors of banks or controlling companies

Circular 6/2010 issued in terms of section 6(4) of Banks Act, 1990

Interpretation and application of criteria relating to exposures secured by residential mortgage bonds

Executive summary

It has come to the attention of this Office that there appears to be uncertainty among banks with regard to the interpretation and application of the criteria relating to exposures secured by residential mortgage bonds, as outlined in regulation 23(8)(c), read with regulations 23(6)(b) and 23(6)(c) of the Regulations relating to Banks. This uncertainty has resulted in inconsistency in capital calculations and reporting of exposures secured by residential mortgage bonds in the BA returns.

The purpose of this Banks Act Circular is to provide clarity on the interpretation and application of the criteria relating to exposures secured by residential mortgage bonds, as outlined in regulation 23(8)(c), read with regulations 23(6)(b) and 23(6)(c) of the Regulations relating to Banks.

1. Introduction

1.1 It has come to the attention of this Office that banks have interpreted the provisions of regulation 23(8)(c), read with regulations 23(6)(b) and regulation 23(6)(c) of the Regulations relating to Banks (the Regulations) in respect of exposures secured by residential mortgage bonds differently. These differences in interpretation have resulted in inconsistent reporting by banks with regard to regulation 23(8)(c), read with regulations 23(6)(b) and 23(6)(c) of the Regulations.

1.2 For example, some banks have interpreted 'individual' to mean a natural person only, while other banks have extended the interpretation to include other legal persons where individuals are requested to sign surety in favour of the relevant bank.

- 1.3 Furthermore, some banks have interpreted 'loan' to refer to the on-balance sheet portion only, whilst other banks have extended the interpretation of 'loan' to include off-balance sheet exposures secured by residential mortgage bonds.
- 1.4 The above treatment also impacts the interpretation of 'the capital amount outstanding' referred to in regulation 23(6)(c).
- 1.5 The purpose of this Banks Act Circular is to provide clarity regarding the application and interpretation of regulation 23(8)(c), read with regulations 23(6)(b) and 23(6)(c) of the Regulations.

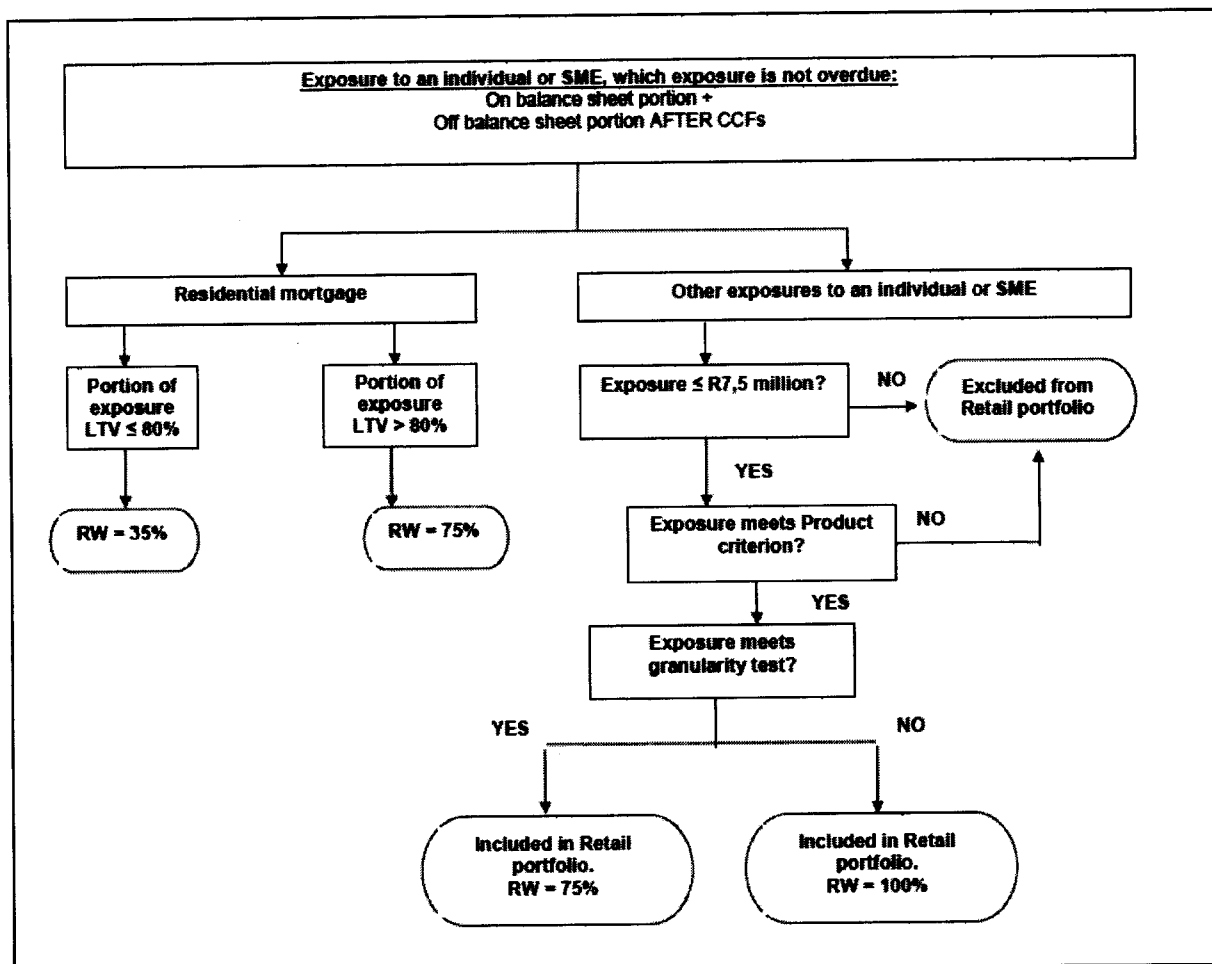
2. Regulation references

- 2.1 Regulation 23(6)(b)(ii) of the Regulations specifically excludes residential mortgage loans, as specified in regulation 23(6)(c) of the Regulations from the category of retail exposures to which a risk weight of 75 per cent is applied.
- 2.2 Furthermore, Regulation 23(6)(c) respectively refers to a loan to 'an individual' which is fully secured by a mortgage bond and to 'the capital amount outstanding'.

3. Interpretation and application of criteria relating to exposures secured by residential mortgage bonds

- 3.1 For the purpose of regulation 23(8)(c), read with regulations 23(6)(b) and 23(6)(c) of the Regulations, exposure shall be the sum of the on-balance sheet exposure and the off-balance sheet exposure after the application of relevant credit conversion factors.
- 3.2 Regulation 23(6)(c) refers to a residential mortgage loan to 'an individual'. This reference to 'an individual' is to be interpreted as including a legal person such as a trust or close corporation, where such exposure is for example supported by the personal surety of the beneficial owner of the residential property mortgaged.
- 3.3 This Office's application and interpretation of regulation 23(8)(c) read with regulations 23(6)(b) and 23(6)(c) of the Regulations will result in the following proposed amendments to the Regulations:
 - 3.3.1 For the purpose of compliance with regulations 23(8)(c), read with regulations 23(6)(b) and 23(6)(c) of the Regulations, 'mortgage loans' should be read as 'mortgage exposures'.
 - 3.3.2 The wording of regulation 23(6)(c) therefore should be read as: 'In the case of **an exposure** fully secured by a mortgage bond on an occupied urban residential dwelling or occupied individual sectional title dwelling, when the exposure is not overdue for more than 90 days and to the extent that the **exposure** does not exceed 80 per cent of the said current market value of the mortgaged property ...'. The same applies for purposes of compliance with regulation 23(8)(c) of the Regulations.

- 3.4 The impact of the above interpretations on the classification of retail-exposures can be summarised as follows:



- 3.5 These interpretations are to be implemented with immediate effect.

4. Acknowledgement of receipt

- 4.1 Two additional copies of this Banks Act circular are enclosed for the use of your institution's independent auditors. The attached acknowledgement of receipt, duly completed and signed by both the chief executive officer of the institution and the said auditors, should be returned to this Office at the earliest convenience of the aforementioned signatories.

E M Kruger
Registrar of Banks

The previous circular issued was Banks Act Circular 5/2010, dated 14 December 2010.