South African Reserve Bank

From the Office of
the Registrar of Banks

G9/2012

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

Guidance Note 9/2012 issued in terms of section 6(5) of the Banks Act, 1990

Capital framework for South Africa based on the Basel III framework

Executive summary

The Office of the Registrar of Banks (this Office) hereby informs all relevant persons of matters related to the prescribed minimum required capital ratios and the application of various components of the said capital requirements such as the systemic risk capital requirement (Pillar 2A), the domestic systemically important bank (D-SIB) capital requirement, the countercyclical buffer range and the capital conservation buffer range. This guidance note also details the phase-in requirements for the prescribed minimum required capital ratios.

This guidance note ensures that banks have adequate time to prepare for the implementation of the prescribed Basel III minimum required capital ratios on 1 January 2013. It should be noted that the revised capital framework will be issued as a directive in terms of section 6(6) of the Banks Act, 1990, after 1 January 2013, once the proposed amended Regulations relating to Banks have been implemented.

1. Introduction

1.1. In view of the implementation of the Basel III framework on 1 January 2013, the current South African capital framework as set out in the current Regulations relating to Banks will be replaced by an amended capital framework as set out in the proposed amended Regulations relating to Banks (proposed amended Regulations), which will be implemented with effect from 1 January 2013.

1.2. In order to prevent any potential ambiguity, Annexure A of this guidance note stipulates the various capital tiers, together with various related elements specified in the proposed amended Regulations and in the Basel III framework, including the systemic risk capital requirement (Pillar 2A), the bank-specific individual capital requirement (ICR, also known as Pillar 2B), and the phasing in of the related minimum requirements.

1.3. The phase-in arrangements for the minimum requirements have been set out in Annexure B of this guidance note to indicate more clearly when and to what extent the requirements become effective.

1.4. The domestic systemically important bank (D-SIB) capital requirement will be finalised and communicated to all banks conducting business in South Africa well in advance of the implementation date of 1 January 2016. The requirement will be specific to each bank or banking group based on criteria related to systemic importance. This minimum requirement will be phased in over a three-year period on a straight-line basis, from 2016 to 2019.

2. Minimum capital requirements

2.1 Regulation 38(8)(e)(ii) of the proposed amended Regulations prescribes that the capital requirement for systemic risk (that is Pillar 2A) will be specified by the Registrar of Banks. The Pillar 2A requirement may therefore also be revised from time to time.

2.2 The Pillar 2A capital requirement will be set at 1,5 per cent of risk-weighted exposures for all banks at a total capital level with effect from 1 January 2013, whereafter it will be increased to 2,0 per cent. In order to ensure that factors related to systemic risk are not double counted, the Pillar 2A capital requirement will be adjusted during the phase-in period of the higher loss absorbency (HLA) requirement for D-SIBs, which will come into effect from 1 January 2016, resulting in an appropriate reduction in some components of the Pillar 2A requirement over time.

2.3 In order to assist banks in appropriately managing their capital plans, this Office hereby notifies banks that the combined total capital-adequacy requirement in respect of the Pillar 2A and the HLA requirement for D-SIBs will not exceed 3,5 per cent of a bank's risk-weighted exposure.

2.4 Furthermore, excluding both bank-specific ICR and the countercyclical buffer requirement, the highest minimum total capital-adequacy requirement to be met by any bank or banking group conducting business within South Africa receiving the highest possible HLA requirement for a D-SIB will be 14 per cent at the end of the phase-in period on 1 January 2019.

2.5 This Office will specify the HLA requirement for each individual bank or banking group identified as a D-SIB in terms of regulation 38(8)(e)(vi) of the proposed amended Regulations. The HLA requirement will accordingly vary between banks identified as D-SIBs. This Office has decided to apply a 'bucketing approach' when assigning the relevant HLA requirement for D-SIBs. Banks and banking groups identified as D-SIBs will be advised in writing by this Office during 2013 of this fact and of the individual HLA requirements assigned to them. The HLA requirement for a D-SIB is regarded as an extension of the capital conservation buffer, and the consequences applicable to breaching the capital-adequacy requirement at the capital conservation buffer level will also apply to breaching the combined total of the capital conservation buffer and the HLA requirement for a D-SIB. The first 50 per cent of the specified D-SIB capital requirement, up to a maximum of 1 per cent of a bank's risk-weighted exposures, must be fully met by common equity Tier 1 capital and reserve funds, and any requirement exceeding the aforementioned requirement may be met by a combination of additional Tier 1 and Tier 2 capital and reserve funds.

2.6 This Office will continue to assess the bank-specific ICR as part of its supervisory review and evaluation processes. These supervisory assessments may attribute ICRs in order to address specific risks identified by this Office in terms of the provisions of regulation 38(8)(e)(iii) read with regulation 38(4) of the proposed amended Regulations. Any ICR may also be based on the levels of economic capital a bank holds to cover risks not regarded as Pillar 1 risks, as observed in the Internal Capital Adequacy Assessment Process (ICAAP) of a bank. This Office will continue to utilise this supervisory tool to increase or decrease the level of ICR; however, factors that form part of the D-SIB capital framework will no longer form part of the ICR framework.

2.7 Commencing 1 January 2016, if a bank's capital-adequacy ratios fall below the levels set out in Annexure A (South African minima including the countercyclical buffer, the conservation buffer and the HLA requirement for D-SIBs), in the absence of other remedial actions acceptable to the Registrar to improve the bank's capital-adequacy ratios, capital conservation ratios will be imposed that will limit discretionary payments such as dividend distributions. These limits will be increased as a bank's capital levels approach the specified minimum requirements. Once imposed, capital conservation measures will remain in place until such time as minimum required capital-adequacy ratios have been restored. If a bank wants to make payments in excess of distribution limits, sufficient capital will have to be raised to fully compensate for the excess distribution. A bank will be required to discuss this alternative with this Office as part of the bank's ICAAP.

2.8 Banks should maintain an additional discretionary capital buffer above the specified minimum requirements, as envisaged in regulation 38(8)(e)(vii) of the proposed amended Regulations, to ensure that the execution of internal business objectives or the occurrence of adverse external environmental factors do not prevent banks from operating above the relevant minima. This Office will continue to monitor and assess the adequacy of this internal buffer against a bank's strategy, risk profile and levels of capital.

2.9 As is standard practise in most international jurisdictions and in accordance with Banks Act Circular 5/2011, and to ensure that no confusion exists in the market, banks are advised to continue to refrain from disclosing to the public their ICR (Pillar 2B) or any HLA requirement for D-SIBs as these are bank-specific requirements and are therefore not directly comparable across banks. This Office will issue further guidance regarding the disclosure of capital-related matters at a later stage.

2.10 Finally, banks are advised to take note of the fact that guidance will be provided on specific aspects of the new capital framework, should it become necessary, after the Basel Committee on Banking Supervision has finalised the consultative processes which are currently still under way.

3. Acknowledgement of receipt

3.1 Two additional copies of this guidance note are enclosed for the use of your institution's independent auditors. The attached acknowledgement of receipt, completed and signed by both the chief executive officer of your institution and the auditors, should be returned to this Office by no later than 12 November 2012.

René van Wyk
Registrar of Banks

The previous guidance note issued was Guidance Note 8/2012, dated 15 August 2012.

Encl. 2

Annexure A: Capital Framework for South Africa based on the Basel III framework, after phase-in period

Capital tiers	Reference in the proposed amended Regulations	CET 1 Capital Requirement	Tier 1 Capital Requirement	Total Capital Requirement	Effective date
BCBS Basel III minima		4,5%	6,0%	8,0%	Phased in from 1 January 2013
South African minima	**Reg 38(8)(b) & Reg 38(8)(e)(i)**	**4,5%**	**6,0%**	**8,0%**	**Phased in from 1 January 2013**
Systemic risk add-on[1] (Total Pillar 2A range 0,5% to 2,0%)	Reg 38(8)(e)(ii)	$A_1 \geq 50\%$ of P2A	$A_2 \geq 75\%$ of P2A	P2A (≤2.0%)	Phased in from 1 January 2013 to 31 December 2015, thereafter adjusted to cater for D-SIB requirements
South African base minima	**Reg 38(9)(a)(i) to (iii)**	**$4,5\% + A_1$**	**$6,0\% + A_2$**	**8,0% + P2A**	**Phased in from 1 January 2013**
Bank-specific ICR add-on (Pillar 2B)[2]	Reg 38(8)(e)(iii) & Reg 38(4)	B_1 = 50% of ICR	B_2 = 75% of ICR	ICR	Fully effective from 1 January 2013
South African minima (prudential minima)		**$4,5\% + A_1 + B_1$**	**$6,0\% + A_2 + B_2$**	**8,0% + P2A + ICR**	**Phased in from 1 January 2013**
Domestic Systemically-Important Bank capital add-on[1] (0% to 2.5%)	Reg 38(8)(e)(vi)	C_1 = min(1% or 50% of DSIB)	C_2 = min(1,5% or 75% of DSIB)	DSIB (max of 2,5%)	Phased in from 1 January 2016
Conservation buffer range (0% to 2.5%)	Reg 38(8)(e)(iv) & Reg 38(8)(f)	D_1 = 100% of CB	D_2 = 100% of CB	CB (≤2.5%)	Phased in from 1 January 2016
Countercyclical buffer range[3] (0% to 2.5%)	Reg 38(8)(e)(v) & Reg 38(8)(g)	E_1 = 100% of CCB	E_2 = 100% of CCB	CCB	Phased in from 1 January 2016
SA minima including countercyclical buffer, conservation buffer and D-SIB requirements[4]		**$7,0\% + B_1 + E_1 + \min(2,0\% \text{ or } (A_1 + C_1))$**	**$8,5\% + B_2 + E_2 + \min(2,5\% \text{ or } (A_2 + C_2))$**	**10,5% + ICR + CCB + min(3,5% or (P2A + DSIB))**	

[1] The aggregate requirement for Pillar 2A and D-SIB will not exceed 2,0 per cent for CET1, 2,5 per cent for Tier 1 and 3,5 per cent in respect of the total capital-adequacy ratio.

[2] The current bank-specific ICR (or Pillar 2B) for each bank or banking group will remain unchanged during 2013, unless this Office has specific reasons to adjust the ICR and pertinently informs the relevant bank in writing of such changes.

[3] In line with the BCBS's paper released in December 2010, entitled "Basel III: Global Regulatory Framework for more Resilient Banks and Banking Systems", revised June 2011, under paragraph 137, the countercyclical buffer is likely to be imposed on an infrequent basis in order to serve its intended purpose.

[4] As specified in regulation 38(9)(a) of the proposed amended Regulations, as from 1 January 2015 the South African minima ratios, including the HLA requirement for D-SIBs, the capital conservation buffer and the countercyclical buffer, shall not be lower than 6,5 per cent for CET1, 8 per cent for Tier 1 and 10 per cent in respect of the total capital-adequacy ratio.

Annexure B: Phase-in Arrangements for the minimum requirements

Shading indicates transition periods - all dates are as of 1 January

	Basel III	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Common Equity Tier 1 requirements (CET1)											
Minimum CET1 Ratio (per Basel III)	4,5%	3,5%	4,0%	4,5%	4,5%	4,5%	4,5%	4,5%			
Pillar 2A for CET1		1,0%	1,5%	2,0%	1,75%	1,50%	1,0%	0,50%			
Minimum CET1 plus Pillar 2A		4,5%	5,5%	6,5%	6,25%	6,0%	5,5%	5,0%			
Phasing in of D-SIB requirements at CET1 level [1]					25%	50%	75%	100%			
Capital Conservation buffer [2]	2,5%				0,625%	1,25%	1,875%	2,5%			
Countercyclical buffer (maximum per cent, if imposed) [2]	2,5%				0,625%	1,25%	1,875%	2,5%			
Tier 1 requirements (T1)											
Minimum Tier 1 Ratio (per Basel III)	6,0%	4,5%	5,5%	6,0%	6,0%	6,0%	6,0%	6,0%			
Pillar 2A for T1		1,5%	1,5%	2,0%	1,5%	1,25%	1,0%	0,75%			
Minimum T1 plus Pillar 2A		6,0%	7,0%	8,0%	7,5%	7,25%	7,0%	6,75%			
Phasing in of D-SIB requirements at Tier 1 level [1]					25%	50%	75%	100%			
Total capital requirements											
Minimum Total Capital Ratio (per Basel III)	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%			
Pillar 2A for Total Capital (maximum 2.0%)		1,5%	2,0%	2,0%	1,75%	1,50%	1,25%	1,0%			
Minimum Total Capital plus Pillar 2A		9,5%	10,0%	10,0%	9,75%	9,5%	9,25%	9,0%			
Phasing in of specified D-SIB charge at Total Capital level [1]					25%	50%	75%	100%			
Capital instruments that no longer qualify as additional Tier 1 or Tier 2 capital	Phased out over 10-year horizon beginning 2013										

[1] The aggregate requirement for Pillar 2A and D-SIB will not exceed 2,0 per cent for CET1, 2,5 per cent for Tier 1 and 3,5 per cent in respect of the total capital-adequacy ratio

[2] The capital conservation buffer together with the countercyclical buffer will be applied at CET1 level and will also be required to be met at both a Tier 1 and Total capital level.