



South African Reserve Bank

From the Office of  
the Registrar of Banks

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

**Guidance Note 6/2013 issued in terms of section 6(5) of the Banks Act, 1990**

**Provision of a committed liquidity facility by the South African Reserve Bank**

### **Executive summary**

The South African Reserve Bank (SARB) has approved the provision of a committed liquidity facility (CLF) available to banks to assist banks to meet the liquidity coverage ratio (LCR). This facility was first announced in Guidance Note 5/2012. This guidance note replaces Guidance Note 5/2012 and contains revised guidelines in terms of the acceptable collateral for the CLF, as well as further detail on the operational requirements thereof.

## **1. Introduction**

- 1.1 On 7 January 2013 the Basel Committee on Banking Supervision (the Basel Committee) published a document detailing changes to the definition of the LCR,<sup>1</sup> 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 will be introduced on 1 January 2015, but the minimum requirement will be set at 60 per cent and rise in equal annual increments of 10 per cent to reach 100 per cent on 1 January 2019.
- 1.2 Although the revisions published by the Basel Committee in January 2013 reduce the immediate shortfall by South African banks in meeting the LCR requirements, the shortfall against a 100-per-cent requirement continues to exist, estimated to be about R140 billion.
- 1.3 During 2012 the SARB approved the provision of a CLF in order to assist banks in meeting the requirements of the LCR. Guidance Note 5/2012 was issued containing details regarding acceptable collateral for the CLF. This guidance note replaces Guidance Note 5/2012 and contains updated specifications on the acceptable collateral for the CLF, as well as details on the operational requirements thereof.

<sup>1</sup> Basel Committee on Banking Supervision, "Basel III: The Liquidity Coverage Ratio and Liquidity Risk Monitoring Tools" (issued January 2013).

## 2. Characteristics of the committed liquidity facility

### 2.1 Size of the facility

2.1.1 Each individual bank will be required to meet the level 1 requirement of the LCR on its own. As a substitute for level 2 assets, the CLF may be utilised. The CLF is only available to banks with a LCR shortfall. The CLF will be capped at 40 per cent of the total amount of HQLA any particular bank is required to hold in rand and based on the estimated requirement as from 2019. This Office will review this cap annually and reserves the right to reduce it if the supply of HQLA in the market increases.

2.1.2 For the purpose of entering into a facility agreement with the SARB during the phase-in period of the LCR (that is, for the years 2013 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 2013, for implementation in 2014, should project their maximum full HQLA requirement for 2014, and the CLF would be capped at 40 per cent of this projected amount.

### 2.2 Collateral

2.2.1 Assets selected as collateral should provide adequate credit risk protection for the SARB, while also limiting any distorting effects on the securities market.

2.2.2 Acceptable collateral that will be considered for the CLF comprises the following:

2.2.2.1 Listed 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).

2.2.2.2 Equities that are listed on the JSE's main exchange and included in the Top 40 Index.

2.2.2.3 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), 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 Notice) the SPI created has to be insolvency remote. The commercial paper created in this manner would be given an International Securities Identification Number (ISIN) and would be recorded in the collateral management system of the SARB as available for the CLF only. Once a bank needs to draw down on the CLF, a repurchase transaction between the SARB and the relevant bank would be entered into. This transaction will give effect to the true sale condition as required by the Securitisation Notice since the SARB will then become the owner of the commercial paper.

- 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 structure are complied with. The composition of the underlying portfolio of assets should be specified in the securitisation application and 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. The SARB, however, retains the option to require a 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 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 shall have to be on the bank's balance sheet for at least one year.
  - x. On a quarterly basis, the collateral pool has to be reassessed to ensure compliance with all requirements. If a loan does not comply with all requirements, it has to be replaced with immediate effect.
  - xi. The securitisation structure should service at least two different stratified risk positions or tranches reflecting different degrees of credit risk, where the junior tranche has to consist of at least 5 per cent of the total securitisation structure.
- d) In order to ensure that concentration in the portfolio is within acceptable limits and also to cater for bank-specific conditions, concentration limits (amount and percentage based) will be determined by the SARB once a bank applies to use the CLF.
- e) In the event of drawdown, the SARB will agree to invest in the senior tranche of the securitisation structure and will provide liquidity equal to the face value of the notes (no haircut will be applied).

- f) To ensure all requirements are in place before the event of drawdown, a bank applying for the use of the CLF should also apply for the approval of the securitisation structure as done under its normal course of business. The securitisation structure shall comply with the provisions of the Securitisation Notice A pre-sale report produced by the rating agency (if externally rated) or by the bank itself (if internally rated) shall form part of the application.

#### 2.2.2.4 Commercial mortgages

- a) In view of (i) the inherently higher credit risk attached to commercial mortgages, (ii) the complexity of defining 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 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.

#### 2.2.2.5 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. Banks will have a choice of keeping the assets on balance sheet in a ring-fenced pool until the CLF is accessed, or transferring them to an SPI. The ring-fenced asset pool must at all times exceed the amount approved under the CLF. 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.
- 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 based on the underlying assets. 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 SARB will provide a loan against the collateral, at an agreed haircut.

In the event of drawdown of a ring-fenced asset pool transferred to an SPI, the SARB will invest in the senior tranche of the 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.



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

- i it has to be unencumbered;
- ii. securitised asset pools have to be audited on an annual basis; and
- iii. collateral shall have an outstanding maturity of more than one year.

2.2.4 The haircuts applied to externally rated acceptable collateral for the CLF, will be the same as prescribed in the credit risk standardised approach as contained in regulation 23(9)(b)(xi) of the Regulations. These haircuts will be based on the domestic credit rating of the particular securities, bonds or self-securitised loans.

2.2.5 The collateral requirements set out in this Guidance Note 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.

## 2.3 Capital and reporting requirements for self-securitisation schemes

The look-through approach should be applied for the securitised assets, 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 inherent credit risk had the assets not been securitised. For reporting purposes banks should remove the relevant assets that form part of the self-securitisation scheme from the form BA 200. To determine the required amount of capital in respect of the securitisation structure, the form BA500 should be completed. For monitoring purposes, banks will be required to complete the form BA 200 on a quarterly basis based on the underlying assets in the SPI. The form BA 501 shall be completed on an annual basis for the SPI.

## 2.4 Pricing

2.4.1 Banks electing to make use of the CLF will pay a commitment fee to the SARB, even if they do not draw funds from it. In order for the fee charged by the SARB 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 the table below, which applies from 2013. The commitment fee will be set on an annual basis when the facility is renewed.

CLF as percentage of required HQLA	Proposed fee per tranche (basis points per year)	Weighted average fee* (basis points per year)
<10%	15	15
10-20%	25	20
20-30%	35	25
30-40% (to a maximum of 40%)	45	30

\* If full tranche is used in the calculation.

In the event that banks draw funds from the CLF, they will pay a drawdown rate equal to the SARB's repo rate plus 100 basis points (equal to the SARB's normal standing facilities). Any drawdown of funds will be for a 31 calendar-day period.

## 2.5 Operational arrangements

2.5.1 A complete list of the operational arrangements will be contained in the Operational Notice of the Financial Markets Department of the SARB, which will be available on the SARB's website. The high-level requirements at this stage are the following:

- i. Cash reserves utilised for square-off operations in SAMOS cannot be used to comply with the LCR.
- ii. The board of directors of a bank has to ensure that the collateral requirements have been met.
- iii. The facility is negotiated for a calendar year and is renewed on an annual basis.
- iv. Banks that apply for the CLF for the first time should apply before the end of August of the year proceeding the year for which they require the CLF to provide sufficient time to negotiate a contract and ensure adherence to the collateral requirements.
- v. Banks that intend rolling over an existing CLF the following year can apply to do so by the end of October of the preceding year for which they require the CLF.
- vi. The SARB reserves the right to adjust the amount of acceptable collateral required, the commitment fees and the drawdown rate when a facility is renewed.
- vii. The CLF is only available to the extent that it will cover an individual bank's shortfall in HQLA to meet the LCR requirement provided that such shortfall can be attributed to a general shortage of HQLA in the South African financial system.
- viii. Reporting on the CLF and the qualifying collateral should be done in terms of banks' monthly BA returns.
- ix. Applications to make use of the CLF should be directed to the Registrar of Banks.
- x. Applications to make use of the CLF have to be approved by each bank's board of directors.
- xi. Accounting standards require the SARB and banks to disclose the availability of the CLF. More details regarding specific disclosure requirements are described in the Operational Notice of the Financial Markets Department of the SARB.

Should you have any questions in the above regard, please contact Dr Nicola Brink, Head: Resolution Planning, at 012 313 3614, or Mr Wessel Mostert, Risk Manager: Asset and Liability Management, at 012 313 4652.

### 3. Acknowledgement of receipt

- 3.1 Two additional copies of this guidance note are enclosed for use by 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.



René van Wyk  
**Registrar of Banks**

The previous guidance note issued was Guidance Note 5/2013, dated 24 July 2013.