



South African Reserve Bank

Prudential Authority

Ref.: 15/8//2

G4/2020

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

Guidance Note issued in terms of section 6(5) of the Banks Act 94 of 1990

Recommendations on the distribution of dividends on ordinary shares and payment of cash bonuses to executive officers and material risk takers, in light of the negative economic impact of the Coronavirus Disease (Covid-19) pandemic and the temporary regulatory capital relief provided by the Prudential Authority.

Executive Summary

The negative impact of the spread of Covid-19 on the global economy has resulted in the Prudential Authority (PA) recently providing substantive temporary regulatory relief to banks, branches of foreign institutions and controlling companies (hereinafter collectively referred to as 'banks').

In light of the critical role played by banks to continue to provide the necessary required funding, for example, to households and businesses amid the Covid-19 pandemic, it is essential that banks conserve their capital resources, among others, to retain their capacity to support the real economy in an environment of heightened uncertainty caused by Covid-19 whilst continuously complying with the prescribed prudential requirements and ensuring the long-term safety and soundness of the bank.

In addition to supporting the real economy, capital resources must also be available to absorb losses that may result from an economic downturn.

As such, capital conservation must take priority over any distribution of dividends on ordinary shares and the payment of cash bonuses to executive officers and material risk takers.

This Guidance Note outlines the expectations of the PA with regard to banks' distributions of dividends on ordinary shares and the payment of cash bonuses to executive officers and material risk takers during this period of uncertainty.

1. Introduction

- 1.1 The PA is pursuing a range of regulatory and supervisory relief measures to promote the safety and soundness of regulated financial institutions and, together with the South African Reserve Bank, is undertaking measures to mitigate the risks to financial stability caused by Covid-19.
- 1.2 The substantial reduction in current and expected economic growth is expected to result in significant declines in banks' profits or headline earnings, resulting in substantially reduced returns on equity for regulated financial institutions.
- 1.3 As stated hereinbefore, banks play a critical and unique role in supporting the wider economy, particularly during a period of economic disruption, such as the disruption caused by Covid-19.
- 1.4 Regulation 39(1) of the Regulations relating to Banks (the Regulations) imposes a duty on the board of directors of a bank to ensure that an adequate and effective process of corporate governance, which is consistent with the nature, complexity and risk inherent in the bank's on-balance sheet and off-balance sheet activities and that responds to changes in the bank's environment and conditions, is established and maintained.
- 1.5 Furthermore, regulation 39(16) of the Regulations imposes a duty on the board of directors of a bank to ensure that-
 - 1.5.1 the bank's compensation or remuneration policies, processes, practices and procedures are duly aligned with the board approved tolerance for risk or risk appetite, and in particular the board of directors shall ensure that compensation in the bank is duly adjusted for all relevant and material types of risk;
 - 1.5.2 the bank's policies, processes, practices and procedures protect and promote the long-term safety and soundness of the bank.
- 1.6 Regulation 38(4) of the Regulations states that when the Authority is of the opinion that a bank's policies, processes and procedures relating to compensation or remuneration are inadequate, the Authority, among other things, may require the said bank-
 - 1.6.1 to maintain additional capital, calculated in such a manner and subject to such conditions as may be specified in writing by the Authority; or
 - 1.6.2 to duly align the bank's compensation or remuneration policies, processes or procedures with the bank's relevant exposure to risk.

2. Guidance

- 2.1 The PA considers it critical that banks continue to fulfil the fundamental role of providing the required funding, among others, to households and businesses amid Covid-19. For this purpose, it is essential that banks appropriately conserve

capital to retain their capacity to support the real economy in an environment of heightened uncertainty caused by Covid-19.

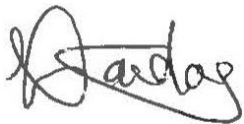
- 2.2 As such, the PA is of the view that capital resources must continue to be available to support the real economy and to absorb losses in the immediate and medium to long term, and as such, the PA expects that no distribution of dividends on ordinary shares and no payment of cash bonuses to executive officers and material risk takers, should take place in 2020. The PA further expects the board of directors of a bank to take appropriate action in respect of any distributions on dividends that may have already been declared by the bank and in respect of the accrual, vesting and payment of variable remuneration, in a manner that is aligned to the principles enumerated in this guidance note and in accordance with the relevant legal requirements, as applicable.
- 2.3 The PA will continuously review this guidance in light of new information on the duration and extent of the Covid-19 stress event, and remains confident that the respective boards of directors of banks are duly taking into consideration, among others, the current and anticipated capital levels of their banks, the impact of Covid-19 and the economic downturn on the safety and soundness of the respective institutions, as well as the increased risk exposures to the said institutions, within the short, medium and long-term.

3. Further action

- 3.1 Banks that are uncertain about the intended application of this guidance note should contact their respective frontline analysts for further guidance.
- 3.2 The PA will continue to engage with the banking industry and all other relevant stakeholders during this time and will issue further guidance or implement any additional measures as and when necessary.

4. Acknowledgement of receipt

- 4.1 Kindly ensure that a copy of this guidance note is made available to 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 the PA at the earliest convenience of the aforementioned signatories.



Kuben Naidoo
Deputy Governor and CEO: Prudential Authority

Date: 6 April 2020

Encl. 1

The previous guidance note issued was Guidance Note 3/2020, dated 26 March 2020.