

DRAFT FOR CONSULTATION – NOVEMBER 2023

Financial Sector Regulation Act, 2017 (Act No. 9 of 2017)

Prudential Standard CBA-02

Governance requirements for co-operative financial institutions and co-operative banks

Objective and Key Requirements of this Prudential Standard

This Standard is made in terms of sections 105 and 108 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (Financial Sector Regulation Act) read with section 46 of the Co-operative Banks Act, 2007 (Act No. 40 of 2007) (Co-operative Banks Act).

This Standard sets out the principles and requirements for governance with respect to Co-operative Financial Institutions (CFIs) and co-operative banks registered in terms of the Co-operative Banks Act.

This Standard covers matters concerning general principles of governance, fitness and propriety of directors, members of the audit committee, managing director and executive officers, code of conduct, culture, board competencies, chairperson of the board, board committees, audit committee, allocation and delegation of roles and responsibilities, duties of directors, roles and responsibilities of management, constitution of a CFI or co-operative bank, remuneration and regulatory reporting.

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1 Commencement

- 1.1 This Standard commences on 1 July 2024 (proposed).

Version Number	Commencement Date
1	1 July 2024 (proposed)

2 Legislative authority

- 2.1 This Standard is made in terms of sections 105 and 108 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (Financial Sector Regulation Act) read with section 46 of the Co-operative Banks Act, 2007 (Act No. 40 of 2007) (Co-operative Banks Act)

3 Definitions and interpretation

- 3.1 In this Standard, “the Act” means the Co-operative Banks Act and any word or expression to which a meaning has been assigned in the Act or the Financial Sector Regulation Act, bears the meaning so assigned to it, unless the context indicates otherwise.

- 3.2 For purposes of this Standard –

‘audit committee’ means the audit committee for a CFI¹ and a co-operative bank;

‘Authority’ means the Prudential Authority established in terms of section 32 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017);

‘board’ means the board of directors of the CFI or co-operative bank as appointed by members in accordance with the constitution of the CFI or co-operative bank;

‘CFI’ means a co-operative financial institution as defined in the Act;

‘competence’ includes experience, knowledge, skills, qualifications and continuous professional development;

‘control function’ means each of the following:

- (a) the risk management function;
- (b) the compliance function; and
- (c) the internal audit function, when required by the Authority;

‘co-operative bank’ means a co-operative bank as defined in the Act;

‘Co-operatives Act’ means the Co-operatives Act, 2005 (Act No. 14 of 2005);

‘executive officer’ means any employee of a CFI or co-operative bank that reports directly to the managing director;

‘management’ means the managing director and executive officers of the CFI or co-operative bank;

‘material roles and functions’ means an element which has the potential to have a significant impact on the CFI or co-operative bank or its ability to manage risks effectively; and

‘members’ means the members of the CFI or co-operative bank.

- 3.3 The ‘Objectives and key requirements of this Prudential Standard’ in the preamble of this Standard must not be used in the interpretation of any paragraph of this Standard.

¹ In some instances, CFIs refer to the audit committee as the supervisory committee. It is advised that this audit committee should not be confused with audit committees that are appointed for companies.

4 Application

- 4.1 This Standard applies to all CFIs and co-operative banks registered under the Act, irrespective of its categorisation under a specific tier, unless explicitly provided for in this Standard.
- 4.2 This Standard applies in addition to the requirements of the Co-operatives Act and the Principles of Good Governance for Co-operatives issued under the Co-operatives Act.

5 Roles and responsibilities

- 5.1 The care, diligence and skill displayed by the board and management of a CFI or co-operative bank have a significant influence on the CFI or co-operative bank's sustainability, safety and soundness as well as its ability to meet its business objectives.
- 5.2 The board of a CFI and co-operative bank is ultimately responsible for ensuring that the CFI or co-operative bank complies with the requirements and principles of good governance outlined in this Standard.
- 5.3 The board and the audit committee must, without delay, inform the Authority in writing of any matter they become aware of in the performance of their functions that has or may contravene the principles and requirements of this Standard.

6 Governance framework

- 6.1 An effective corporate governance framework plays a fundamental role in ensuring that a CFI or co-operative bank responsibly delivers on its obligations to its stakeholders while ensuring the ongoing viability of the business.
- 6.2 In driving the culture of the CFI or co-operative bank, the board must consider the following principles:
 - 6.2.1 create, protect and return member value;
 - 6.2.2 lay solid foundations for management and oversight;
 - 6.2.3 structuring the board to add member value;
 - 6.2.4 act ethically and responsibly;
 - 6.2.5 safeguard integrity in reporting;
 - 6.2.6 make timely and balanced disclosures;
 - 6.2.7 respect the rights of members and other stakeholders;
 - 6.2.8 recognise, identify and manage risk; and
 - 6.2.9 remunerate fairly and responsibly.
- 6.3 The board of a CFI or co-operative bank must, in discharging its governance responsibilities, ensure that the following key areas of governance are effectively managed and addressed in a governance framework:
 - 6.3.1 Co-operative values and principles
 - (a) approve and monitor organisational ethics, adherence to co-operative principles and values;
 - (b) approve and monitor operational and compliance standards and policies;

- (c) acknowledging that acting ethically and responsibly goes beyond mere compliance with legal obligations; and
- (d) reinforcing the principle of acting with honesty and integrity to create, protect and return value to members, including acting ethically towards the broader community.

6.3.2 Strategic planning

- (a) Considering, approving, and monitoring strategic business plans for the CFI or the co-operative bank;
- (b) finalising a clear set of strategic objectives designed to ensure the sustainable creation, protection and return of value for members;
- (c) obtaining collaboration and support for these strategic objectives from the members;
- (d) monitoring and reviewing implementation of the strategic objectives; and
- (e) reporting regularly to members as to the implementation, monitoring and review of the strategic objectives.

6.3.3 Oversight

- (a) Approving and overseeing management's implementation of the CFIs or co-operative bank's strategic objectives, governance and risk management frameworks as well as the corporate culture. This should also include mechanisms to determine how the performance of the board and management is monitored and evaluated; and
- (b) taking the necessary action when risks are identified.

6.3.4 Structure and composition of the board

- (a) Planning and ensuring that the CFI or co-operative banks has a board that meets the organisation's minimum requirements, is of an appropriate size, diversity and composition, and has the skills, independence and commitment to discharge its duties and responsibilities effectively; and
- (b) ensuring as a collective that the members of the board are fit and proper persons.

6.3.5 Competent management

- (a) Ensuring that the board employs management with the necessary experience, knowledge and qualifications to operate the CFI or co-operative bank;
- (b) ensuring that the management is fit and proper as contemplated in paragraph 7 below; and
- (c) appropriately overseeing the management activities.

6.3.6 Risk identification

- (a) Recognising, identifying, evaluating the risks involved in a CFIs or co-operative bank's business operations and governance.

6.3.7 Systems integrity

- (a) Ensuring that business operations are functioning properly and effectively, and under a sound system of internal controls.

6.3.8 Succession planning

- (a) Ensuring that the board has a plan of succession to replace board members or the managing director should it become necessary. The succession plan must also include measures on how the prospective successors will be trained.

6.3.9 Communication and disclosure

- (a) Approving and monitoring a system of effective communication that addresses communication among its members, board, management, other employees and stakeholders of the CFI or co-operative bank as well as the general public; and
- (b) ensuring timely, transparent and balanced disclosure of all matters concerning the CFI or co-operative bank that a reasonable person would expect to have a material effect on the value received from ongoing membership and the interests of members and other stakeholders.

6.3.10 Accountability

- (a) Being primarily accountable for the governance and performance of the CFI or co-operative bank; and
- (b) being accountable for ensuring that the CFI or co-operative bank follows the applicable laws, behaves in an ethical manner, and manages the member's funds with due care.

6.3.11 Relationship with stakeholders

- (a) Ensuring that the CFI or co-operative bank has considered and implemented processes and procedures to define clear roles to create and maintain effective relationships with stakeholders.

6.4 In addition to the responsibilities outlined in paragraph 6.3, the board must ensure that:

6.4.1 an effective board approved and documented governance framework is developed and implemented by the CFI or co-operative bank;

6.4.2 the governance framework:

- (a) is proportionate to the nature, size, complexity and risk profile of the business of the CFI or co-operative bank;
- (b) includes effective systems of corporate governance, risk management and internal controls; and
- (c) is reviewed regularly, but at least annually;

6.4.3 the governance framework is supported by a board approved risk management framework;

6.4.4 the board's roles and responsibilities are clearly specified and includes:

- (a) establishing and overseeing the control function and material risk decisions; and
- (b) ensuring the independence and adequate resourcing of the control functions;

6.4.5 there is compliance with all supervisory and regulatory requirements;

6.4.6 there are appropriate processes in place that support strong communication between management, the board and board committees, and the encouragement of employee participation, including whistleblowing;

- 6.4.7 the CFI or the co-operative bank has comprehensive internal processes to assist the board and management to monitor and assess the adequacy and effectiveness of the financial institution's risk-management policies, procedures, systems, and controls; and
- 6.4.8 members of the board, directors and management declare all conflicts of interest.
- 6.5 For Tier 3 CFIs or co-operative banks, the internal processes referred to in sub-paragraph 6.4.7 above must be structured in accordance with the three lines of defence governance model, comprising the:
 - 6.5.1 first-line of defence – management and internal controls;
 - 6.5.2 second-line of defence – risk management and compliance; and
 - 6.5.3 third-line of defence – internal audit.

7 Fitness and propriety of directors, members of the audit committee, managing director and executive officers

- 7.1 Members of the board, members of the audit committee and management of a CFI or a co-operative bank must be fit and proper taking into account the requirements prescribed under 7.4 below.
- 7.2 The CFI or co-operative bank must have processes in place to assess the fitness and propriety of new directors, members of the audit committee and management as well as review the fitness and propriety of existing persons at least on an annual basis.
- 7.3 When assessing and reviewing the fitness and propriety the CFI or co-operative bank must have regard to its code of conduct as outlined in paragraph 8 below.
- 7.4 In addition, when assessing and reviewing the fitness and propriety the CFI or co-operative bank must have regard to:
 - 7.4.1 the competence and soundness of judgement of the person for the fulfilment of the responsibilities of the particular office and nature, size, complexity and risk profile of CFIs or co-operative banks;
 - 7.4.2 the diligence with which the person concerned is likely to fulfil those responsibilities;
 - 7.4.3 previous conduct and activities of the person in business or financial matters; and
 - 7.4.4 any evidence that the person -
 - (a) has been convicted (and that conviction has not been expunged) of a financial crime as defined in section 1 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) or any offence involving dishonesty;
 - (b) has been convicted of an offence committed after the Constitution of the Republic of South Africa, 1993 (Act No. 200 of 1993), took effect, and sentenced to imprisonment without the option of a fine;
 - (c) has contravened the provisions of any law designed for protecting members of the public against financial loss due to the dishonesty or incompetence of, or malpractices by, persons engaged in the provision of banking, insurance, investment or other financial services; or the management of juristic persons, or against financial loss due to activities relating to insolvency;
 - (d) is a former director or manager of a CFI or co-operative bank or any other bank and that the person's actions contributed to the inability of that CFI or co-operative bank or other bank to pay its debts;

- (e) had taken part in any business practices that, in the opinion of the CFI or co-operative bank, were deceitful, prejudicial, or otherwise improper (whether unlawful or not) or which otherwise brought discredit to that person's methods of conducting business; or
- (f) had taken part in or been associated with any such other business practices as would or had otherwise conducted himself or herself in such a way as to, cast doubt on his or her competence and soundness of judgement.

7.5 *Prudential Standard CBA-01 – Registration and operational requirements for CFIs and co-operative banks* deals with the approval requirements from the Authority for the appointment of members of the board, members of the audit committee and management.

7.6 The fitness and propriety of new directors must be assessed before taking up their roles or being nominated as a candidate for election as a director.

7.7 Individuals who are holding, or who are proposing to hold the office of a director on the board, management of a CFI or co-operative bank, must submit information in the form and manner and at intervals determined by the Authority.

7.8 The information determined by the Authority must be completed and submitted to the Authority when:

- 7.8.1 a new director, managing director or executive officer has been appointed;
- 7.8.2 a director, managing director or executive officer has changed his or her address; or
- 7.8.3 a director, managing director or executive officer has vacated his or her office; and
- 7.8.4 circumstances arise where the Authority may request such information.

8 Code of conduct

8.1 A CFI or co-operative bank must develop and implement a code of conduct that applies to the members of the board, management and members of the audit committee:

8.2 The code of conduct must require the persons mentioned in paragraph 8.1 above to:

- 8.2.1 act in accordance with the highest standards of honesty and ethical conduct;
- 8.2.2 protect and safeguard the assets and resources of the co-operative bank against loss, theft, misuse and misapplication;
- 8.2.3 ensure effective communication with and provision of accurate information relating to financial and operational matters to the members;
- 8.2.4 ensure full, accurate, sensible, timely and meaningful disclosures in reports submitted to the Authority and other regulatory authorities;
- 8.2.5 treat information obtained in the performance of his or her functions with the necessary confidentiality; and
- 8.2.6 ensure compliance with all applicable legislation and report any non-compliance or unlawful behaviour to the relevant regulatory authorities.

9 Culture

- 9.1 CFIs and co-operative banks must have in place a demonstrated co-operative culture that is core to the business model and which supports appropriate outcomes including ethical behaviour, promotion of member interest as well as sound and prudent management.
- 9.2 The board is responsible for overseeing and ensuring compliance with the appropriate co-operative culture within the CFI or co-operative bank and must set the tone at the top.

10 Board competencies

- 10.1 The board must have the necessary expertise, qualifications, knowledge and skill to be able to exercise competent and independent judgement when considering all matters relating to the operation and governance of the CFI or co-operative bank.
- 10.2 To enable directors to understand their roles and responsibilities as well as enhance their knowledge and skills, the CFI or co-operative bank must implement new director orientation, training and awareness programs.
- 10.3 The programs referred to in paragraph 10.2, above must inform directors about new and on-going business developments, the changing risk profile of the financial institutions as well as regulatory and supervisory requirements and changes.
- 10.4 The board must assess its effectiveness at least on an annual basis. The annual review must include the following areas:
 - 10.4.1 the profile of qualifications, knowledge, skill, experience, and involvement required of directors;
 - 10.4.2 the quality and effectiveness of the board's performance;
 - 10.4.3 the processes utilised for setting agendas and priorities;
 - 10.4.4 the quality and timeliness of materials provided for meetings;
 - 10.4.5 the conducting of meetings: whether adequate time is given to directors to scrutinise and discuss issues that are relevant to the board's role and responsibilities; and
 - 10.4.6 the robustness of discussions and level of scrutiny applied by the board.

11 Chairperson of the board

- 11.1 The principal role of the chairperson² is to manage and provide leadership to the board of the CFI or the co-operative bank.
- 11.2 The chairperson must:
 - 11.2.1 ensure that adequate time is allocated for discussion of board matters, especially discussions of a strategic or policy nature;
 - 11.2.2 engage with key stakeholders, where the intervention or engagement at the level of the board is needed in addition or instead of management engagement
 - 11.2.3 promote a culture of openness and debate among directors and management,

² Adapted from the King Committee Practice Note 22/09/27– The role of the Chair and Lead Independent. Available at: https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/562ED5CF-02E8-4957-97C8-D3F0C66A7245/King_IV_Practice_Note_on_Role_of_Chair_and_LID.pdf

- 11.2.4 take the lead in the allocation of board members to committees including the appointment of the respective chairs;
- 11.2.5 ensure clarity of mandate and effectiveness of such committees;
- 11.2.6 encourage congeniality, team-work and collaboration among governing body members without inhibiting candid debate and creative tension;
- 11.2.7 oversee conflicts of interest, including policy, declarations, recusal are addressed appropriately;
- 11.2.8 ensure that board members contribute fully to the effective and objective discharge of the board's role and duties;
- 11.2.9 take the lead in ensuring the evaluations of the board, its members, chair and committees and in addressing non-performance by members of the board and if necessary, the removal of unsuitable board members from the board;
- 11.2.10 mentor new or less experienced governing body members to develop skill and enhance confidence; and
- 11.2.11 ensure that new governing body members are appropriately made aware of their responsibilities through an induction programme.

12 Board committees

- 12.1 The board should put in place appropriate board committees commensurate with the nature, size, complexity and risk profile of the CFI or co-operative bank.
- 12.2 Board committees support the board in the execution of specific oversight functions within the financial institution.
- 12.3 Committee members must address relevant issues and make recommendations to the board.
- 12.4 At a minimum, a Tier 1 CFI or co-operative bank must constitute a governance committee and credit committee (only if the CFI or co-operative bank provide loans).
- 12.5 Board committees must have documented terms of reference, inclusive of the frequency of meetings which must be approved by the board.
- 12.6 Board committees should function independently from each other and be provided with sufficient authority, resources and assigned responsibilities in supporting the board.
- 12.7 Each committee is required to maintain adequate records of its activities and to report to the board on a regular basis.
- 12.8 The board may put in place additional committees as it deems appropriate to facilitate the efficient governance of the CFI or co-operative bank.
- 12.9 Depending on the nature, size, complexity and risk profile of the CFI or co-operative bank the Authority may require the relevant CFI or co-operative bank to establish additional board committees.

13 Audit committee

- 13.1 The audit committee is elected by the general members of the CFI or the co-operative bank at the annual general meeting.

- 13.2 The members of the audit committee are not members of the board and are accountable to the members.
- 13.3 The audit committee plays a critical role in ensuring that the requirements of corporate governance are adhered to by the CFI or co-operative bank.
- 13.4 The role of the audit committee is to have independent oversight of the operations of the CFI or co-operative bank to ensure that the interests and assets of the members are protected and safeguarded.
- 13.5 In fulfilling its responsibilities the audit committee must:
 - 13.5.1 regularly review the systems for risk management and internal controls and provide an independent assurance to the members and the board that the systems are effective;
 - 13.5.2 must provide an independent assurance to the members and the Authority, if requested, that the CFI or co-operative bank complies with the requirements of this Standard;
 - 13.5.3 must report to the members of the CFI or the co-operative bank, the board and the Authority any matters identified during the performance of its responsibilities that are contrary to this Standard or may negatively affect the maintenance of a sound risk management framework;
 - 13.5.4 review the audited Annual Financial Statements (AFS) prior to dissemination and ensure that any adjustments are effected prior to being tabled at the annual general meeting for approval; and
 - 13.5.5 have an internal process followed to address all the issues raised by the external assurance providers.

14 Allocation and delegation of roles and responsibilities

- 14.1 As the governing body of the financial institution all powers and responsibilities reside with the board.
- 14.2 The board may delegate some of the activities or functions associated with its roles and responsibilities to board committees or members of management, or in certain cases, to external parties.
- 14.3 The prior approval of the Authority is required when a CFI or co-operative bank makes a decision to outsource material roles and functions to external parties as such decision will introduce material risks to the prudent management of the financial institution.
- 14.4 The allocation of roles and responsibilities between the board and management is one of the most critical governance decisions made by the board. The board must retain all strategic and policy decisions and only delegate day-to-day management decisions and functions.
- 14.5 Delegation does not abrogate the accountability of the board for decisions made under delegation. Any action committed or omitted under a delegation is deemed to have been committed or omitted by the board.

14.6 Effective delegation requires a strong and disciplined governance model. The board of a CFI or a co-operative bank must develop an appropriate system of delegation in which:

14.6.1 delegations are appropriately and clearly mandated and documented;

14.6.2 there are adequate checks and balances;

14.6.3 there is provision for the monitoring and reporting on delegations;

14.6.4 there is no undue concentration of powers; and

14.6.5 withdrawal of delegations are specifically addressed.

15 Duties of directors

15.1 A director of a CFI or a co-operative bank in effecting their duties and responsibilities must act honestly, diligently, reasonably, in good faith and must exercise due care.

15.2 Directors must:

15.2.1 comply with the fit and proper requirements of the CFI or the co-operative bank as well as the requirements of the Act and this Standard;

15.2.2 act in the best interests of the CFI or co-operative bank and members; and

15.2.3 exercise independent judgment and objectivity in decision making, taking into account the interests of the members and the CFI or co-operative bank as well as and the applicable regulatory requirements.

15.3 A director of the CFI or co-operative bank must have the commitment necessary to fulfil his/her role, as demonstrated by, for example, a sufficient allocation of time to the affairs of the CFI or co-operative bank.

15.4 A director of the CFI or co-operative bank must act without favour, providing constructive and robust challenge of proposals and decisions and asking for information when the director considers it necessary.

16 Roles and responsibilities of management

16.1 A manager of a CFI or co-operative bank must:

16.1.1 act honestly, prudently, responsibly and with due care when performing his/her duties;

16.1.2 comply with the fit and proper requirements of the CFI and co-operative bank and any applicable Standards; and

16.1.3 be suitably qualified with the necessary skills and knowledge to effectively deliver on his/her duties and responsibilities.

16.2 Subject to appropriate delegation from the board, management is responsible for and must:

16.2.1 carry out the day-to-day operations of the financial institution effectively and in accordance with the CFI's or co-operative bank's board-approved culture, business objectives and strategies for achieving those objectives in line with the CFI's or co-operative bank's long-term interests and feasibility;

16.2.2 promote fair treatment of members;

- 16.2.3 provide the board with adequate and timely information to enable the board to carry out its duties and functions, including the monitoring and review of the performance and risk exposures of the CFI or co-operative bank, and the performance of management;
- 16.2.4 maintain adequate and orderly records of the CFI or co-operative bank;
- 16.2.5 promote strong risk management and internal controls, through their personal conduct, through the implementation of transparent policies, and by communicating to all employees their responsibilities in these areas; and
- 16.2.6 not interfere with and support the activities that control functions carry out in the rightful exercise of their responsibilities, including that of providing an independent view of governance, risk, compliance and control related matters.

16.3 In addition, management must have oversight of the following:

- 16.3.1 signs of growth i.e. membership of the CFI or co-operative bank and asset growth;
- 16.3.2 delivery of the business of the CFI or co-operative bank in a safe environment;
- 16.3.3 human resources management including but not limited to the maintenance of appropriate staff records and recruitment of suitably qualified staff, job descriptions, implementing appropriate organisational structures and staff training programs;
- 16.3.4 record keeping, including but not limited to membership records in line with appropriate Know Your Customer (KYC) principles;
- 16.3.5 management information systems, whether manual or end-user computing, including access controls and backups; and
- 16.3.6 internal controls including appropriate segregation of duties.

17 Constitution of a CFI or co-operative bank

- 17.1 The constitution of a CFI or co-operative bank is a key governance document. The requirements for the constitution of a co-operative bank and CFI are provided for in the Act and *Prudential Standard CBA01 – Registration and operational requirements for CFIs and co-operative banks*.

18 Remuneration

- 18.1 CFIs and co-operative banks must ensure that remuneration of staff of the CFI or co-operative bank is dealt with responsibly and is aligned with the sustainability of the institution.
- 18.2 Remuneration that is paid to both the staff of the CFI or co-operative bank must be considered in light of the co-operative principles as well as financial position of the CFI or co-operative bank.
- 18.3 Remuneration and other benefits of directors, including the managing director must be tabled at the annual general meeting.

19 Regulatory reporting

- 19.1 The form, manner and period for regulatory reporting on this Standard will be determined by the Authority and published on its website.
- 19.2 The Authority may specify with the relevant CFI or co-operate bank, other areas of reporting when it becomes necessary based on the nature, size, complexity and risk profile of the CFI or co-operative bank.

20 Short title

- 20.1 This Standard shall be called 'Prudential Standard CBA-02 – Governance requirements for CFIs and co-operative banks.'