

—
P O Box 427 Pretoria 0001 South Africa
370 Helen Joseph Street Pretoria 0002
+27 12 313 3911 / 0861 12 7272
www.resbank.co.za



SOUTH AFRICAN RESERVE BANK
Prudential Authority

Ref.: 15/8/1/3

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

Proposed directive issued in terms of section 6(6) of the Banks Act, 1990 (Act No. 94 of 1990)

Minimum regulatory requirements relating to the deposits covered by the Corporation for Deposit Insurance and banks' fund liquidity contributions.

Executive summary

On 24 March 2023, the Minister of Finance published a commencement schedule for the Financial Sector Laws Amendment Act 23, 2021 which amends the Financial Sector Regulation Act 9, 2017 (FSR Act), setting out the implementation dates for the resolution and some deposit insurance provisions in the FSR Act. The notice established the Corporation for Deposit Insurance (the Corporation) as a legal entity effective 24 March 2023. The Corporation is expected to become fully operational from 1 April 2024, subject to the promulgation of its secondary legislation.

In this regard, the Prudential Authority (PA) aims to inform all banks, branches of foreign institutions and controlling companies (hereinafter collectively referred to as 'banks'), eligible institutions, and auditors of banks or controlling companies of the minimum regulatory requirements relating to the deposits covered by the Corporation and banks' fund liquidity contributions to the Corporation from 1 April 2024.

Regulation 23 of the Regulations relating to Banks (Regulations) specifies the minimum requirements that banks must comply with for the measurement of their respective exposures to credit risk. Banks will be exposed to credit risk through their fund liquidity contribution to the Corporation. This funding is an interest-bearing loan facility from banks to the Corporation. The Regulations specify the relevant risk estimates and the risk weights that apply to banks that have adopted the internal rating based (IRB) approaches and the standardised (STA) approach, respectively, for the calculation of the minimum required regulatory capital and reserve funds relating to credit risk.

Regulations 26(12) and 26(14) of the Regulations specify the minimum regulatory requirements relating to the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR), respectively.

Accordingly, the purpose of this proposed directive is to direct banks to comply with specified requirements related to covered deposits and fund liquidity contributions in relation to regulations 23 and 26 of the Regulations.

1. Introduction

- 1.1. The Corporation is established to give depositors reasonable access to their covered deposits when their bank has failed.
- 1.2. In terms of the Corporation's funding model, banks must provide the Corporation with a fund liquidity contribution, the details of which were specified in the draft Fund Liquidity Prudential Standard¹, which was published on 12 June 2023. Contributions by banks to the fund liquidity are interest-bearing loans to the Corporation that will be guaranteed by the South African Reserve Bank (SARB) and will impact the banks' treatment of the covered deposits and fund liquidity contributions in relation to regulations 23 and 26 of the Regulations.

2. Reference to the Regulations

- 2.1. Regulation 23 of the Regulations specifies the respective risk estimates and the risk weights that apply to banks that have adopted the IRB approaches and the STA approach, respectively, for the calculation of the minimum required regulatory capital and reserve funds relating to credit risk. The Regulations also make provision for risk mitigation and the treatment of guaranteed exposures under both approaches.
- 2.2. Regulations 26(12) and 26(14) of the Regulations specify the minimum regulatory requirements relating to the LCR and NSFR, respectively.

3. Directive

- 3.1. Based on the aforesaid and in accordance with the provisions of section 6(6) of the Banks Act, 1990 (Act No. 94 of 1990), banks are hereby directed to comply with the requirements specified in paragraphs 3.2 to 3.3.2.4 below.

3.2. Minimum regulatory requirements relating to Credit Risk

- 3.2.1. In the calculation of the minimum required capital and reserve funds related to credit risk exposure to the Corporation; banks must apply the minimum requirements outlined as follows:
 - 3.2.1.1. For banks that have adopted the STA approach, regulation 23(9)(c)(iii) of the Regulations specifies that when a bank that has adopted the STA approach obtains a protection against loss relating to an exposure or potential exposure to credit risk in the form of an eligible guarantee, the risk weight applicable to the guaranteed transaction or guaranteed exposure may be reduced to the risk weight applicable to the guarantor. Hence, banks under the STA approach will apply a 0% risk weight for the exposure to the Corporation based on the explicit guarantee provided by the

¹ [Prudential Communication 6 of 2023 - Fund Liquidity \(resbank.co.za\)](https://resbank.co.za/prudential-communication-6-of-2023-fund-liquidity)

SARB. The STA banks' exposure to the Corporation must be reported in line item 17 of the form BA 200.

3.2.1.2. For banks that have obtained approval to adopt the FIRB approach, regulation 23(12)(d)(iii)(A)(ii) of the Regulations allows them to substitute the probability of default (PD) estimate related to the Corporation with the PD estimate related to the guarantor (SARB). FIRB banks may also substitute the loss-given default (LGD) ratio of the underlying transaction with the relevant regulatory prescribed LGD ratio related to the guaranteed position, not with the LGD related to the SARB.

3.2.1.3. For banks that have obtained approval to adopt the AIRB approach, regulation 23(14)(d)(iii)(A)(i) of the Regulations allows them to substitute either the PD or the LGD estimate related to the Corporation with the PD or LGD estimate related to the SARB.

3.2.1.4. The IRB banks' exposure to the Corporation must be reported in line item 133 of the form BA 200.

3.3. Minimum regulatory requirements relating to the LCR and NSFR

3.3.1. LCR

3.3.1.1. The Corporation only partially adheres to the requirements set out in regulations 26(12)(d)(i)(D) and 26(12)(d)(i)(F) of the Regulations; therefore, banks are required to apply a five per cent run-off factor to retail deposits covered by the Corporation when calculating the LCR, except in the instances specified in regulations 26(12)(d)(i)(G) and 26(12)(d)(i)(H) of the Regulations.

3.3.1.2. As the Corporation evolves, the PA will re-evaluate the run-off factor applied to retail covered deposits when calculating the LCR.

3.3.1.3. When a bank's total covered deposits decrease from one month to the next, its fund liquidity tier balance with the Corporation must be adjusted by the Corporation, refunding the adjustment amount to the bank. Such an excess must be reported in line item 186 of the form BA 300 and receive a hundred per cent inflow factor when calculating the bank's LCR.

3.3.1.4. When a bank's total covered deposits increase from one month to the next, its fund liquidity tier balance with the Corporation must be increased. Such a shortfall must be assigned a hundred per cent run-off factor when calculating the bank's LCR.

3.3.2. NSFR

3.3.2.1. Deposits covered by the Corporation must be reported in accordance with Table 1 of regulation 26(14)(b)(i)(C) of the Regulations when calculating the bank's NSFR.

- 3.3.2.2. A required stable funding (RSF) factor of hundred per cent must be applied to the fund liquidity contribution requirement (i.e., a specified percentage of a bank's total covered deposits) when calculating the bank's NSFR.
- 3.3.2.3. An RSF factor of fifty per cent must be applied to a shortfall as envisaged in paragraph 3.3.1.4.
- 3.3.2.4. An available stable funding (ASF) factor of fifty per cent must be applied to excess balances as envisaged in paragraph 3.3.1.3.

4. Invitation for comment

- 4.1. Banks and other interested persons are hereby invited to submit their comments with respect to the proposed directive to SARB-PA@resbank.co.za, Cristel.Bakker@resbank.co.za and Bongani.mtsweni@resbank.co.za by no later than 28 February 2024.

Fundi Tshazibana
Chief Executive Officer

Date: