

DRAFT FOR INFORMAL CONSULTATION – MARCH 2020

Prudential Standard FC02

Intragroup Transaction and Exposures

Objectives and key requirements of Prudential Standard FC02

This Standard is made in terms of sections 105 and 164 of the Financial Sector Regulation Act, 2017 (Act No.9 of 2017) and requires the holding company of a financial conglomerate to operate within the principles and comply with the requirements relating to intragroup transactions and exposures.

It is the responsibility of the board of directors of the holding company of a financial conglomerate to ensure that the financial conglomerate meets the requirements for intragroup transactions and exposures on a continuous basis.

This Standard highlights the Prudential Authority's requirements in terms of the management of intragroup transactions and exposures, and sets down the reporting requirements for material transactions.

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1. Commencement

- 1.1 This standard commences on 1 January 2020 (proposed)

Version number	Commencement date
1	1 January 2021

2. Legislative authority

- 2.1 This Standard is made in terms of section 105 and 164 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017)(FSR Act).

3. Application

- 3.1 This Standard applies to all holding companies of financial conglomerates as designated by the Prudential Authority in terms of section 160 of the FSR Act.
- 3.2 Where a responsibility is placed on the holding company in terms of this Standard, it must be discharged by the board of directors (board) of the holding company and in respect of all the entities within the financial conglomerate.

4. Definitions and interpretation

- 4.1 The terms used in this Standard, unless indicated otherwise, are defined in the FSR Act and the financial sector laws, and have the same meaning in this Standard.
- 4.2 Intragroup transactions and exposures can take the form of direct or indirect claims between entities within a financial conglomerate.
- 4.3 The 'Objectives and key requirements of Prudential Standard FC02' that is italicised in the preamble of this Standard must not be used in the interpretation of any paragraph of this Standard.

5. Roles and responsibilities

- 5.1 The board of the holding company of a financial conglomerate is ultimately responsible for ensuring that the financial conglomerate complies with the principles and requirements of this Standard.
- 5.2 Where a financial conglomerate's control functions are required to perform certain functions in terms of this Standard, the board must ensure that the control functions regularly review and report to the board on the financial conglomerate's compliance with this Standard.
- 5.3 If requested to do so, the board of the holding company of the financial conglomerate and/or auditor must provide assurance to the Prudential Authority that the financial conglomerate complies with the requirements of this Standard.

6. Principles and requirements for intragroup transactions and exposures

- 6.1 Intragroup transactions and exposures are means by which financial conglomerates rationalise capital and funding to enhance cost and operational efficiencies. Material or significant intragroup transactions and exposures must be the focus of robust risk management practices due to the potential that such transactions can lead to contagion risk within the financial conglomerate.
- 6.2 The board of the holding company of a financial conglomerate must ensure that there is disclosure of material intragroup transactions and exposures to the Prudential Authority.
- 6.3 Intragroup transactions and exposures may originate through¹, among others:
- a. cross shareholdings;
 - b. trading operations whereby one group company deals with, or on behalf of, another group company;
 - c. central management of short-term liquidity within the financial conglomerate;
 - d. guarantees, loans and commitments provided to, or received from, other companies in the group;
 - e. the provision of management and other service arrangements (e.g. pension);
 - f. exposures to major shareholders (including loans and off-balance sheet exposures, such as commitments and guarantees);
 - g. material exposures arising through the placement of clients' assets with other group companies;
 - h. purchases or sales of assets with other members of the financial conglomerate;
 - i. transfer of risk through reinsurance to group companies;
 - j. transactions to shift third-party-related risk exposures between entities within the financial conglomerate, including transactions with special purpose vehicles or ancillary entities;
 - k. insurance, reinsurance and retrocession operations; and
 - l. transactions that consist of several connected transactions where assets or liabilities are transferred to entities outside of the financial conglomerate, but ultimately risk exposure is brought back within the financial conglomerate.

7. Material or significant intragroup transactions

- 7.1 An intragroup transaction shall be deemed to be material or significant if such a transaction can significantly influence the solvency or liquidity position of the financial conglomerate and is in excess of 1% of the eligible capital in terms of the capital assessment conducted in terms of Prudential Standard FC01: Capital Requirements for Financial Conglomerates - Technical. Consideration must be given to sequential transactions that on aggregation become material or significant to the financial conglomerate.

¹ For the purposes of this Standard, the manner through which intragroup transactions and exposures originate are in accordance with those contained in the Basel Committee on Banking Supervision: Joint Forum, *Intragroup Transactions and Exposures Principles*, December 1999.

- 7.2 The holding company of a financial conglomerate must identify material intragroup transactions, and must take at least the following into account:
- a. the specific structure of the financial conglomerate;
 - b. the complexity of the intragroup transactions;
 - c. the specific geographical location of the counterparty and whether or not the counterparty is a regulated entity;
 - d. the possibility of contagion effects within the financial conglomerate;
 - e. the possibility of a circumvention of sectoral rules;
 - f. the possibility of conflicts of interests;
 - g. the solvency and liquidity position of the counterparty;
 - h. transactions among entities belonging to different sectors of a financial conglomerate, if not already reported at sectoral level; and
 - i. transactions within a financial sector that are not already reported under the provisions of the sectoral rules.

8. Intragroup transactions and exposures policy

- 8.1 The holding company of the financial conglomerate must implement robust board-approved policies as well as risk-management processes and procedures relating to intragroup transactions or exposures, which policies, processes and procedures shall:
- a. capture all material intragroup transactions and exposures;
 - b. include limits on acceptable levels for intragroup transactions and exposures for the holding company of the financial conglomerate and its regulated and unregulated entities within the financial conglomerate;
 - c. ensure that adequate systems and controls are in place to identify, measure, manage, monitor and report on material intragroup transactions and exposures for the financial conglomerate in a timely manner;
 - d. for all material intragroup transactions and exposures outside the scope of solo and consolidated supervision, be adequately covered in the financial conglomerate intragroup transactions and exposures policy.

9. Reporting requirements

- 9.1 All material intragroup transactions and exposures must be reported to the Prudential Authority on a semi-annual basis.
- 9.2 The form and manner of regulatory reporting returns will be determined by the Prudential Authority and published on its website.

10. Regulatory Action

- 10.1 If in the view of the Prudential Authority, that intragroup transaction and exposure risks are not adequately covered or taken into account by the financial conglomerate, the Prudential Authority may take any regulatory action including requiring the financial conglomerate to hold or maintain additional capital.