



DRAFT FOR CONSULTATION

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

Prudential Standard RA02 - Transfer of assets and liabilities of designated institution in resolution

Objectives and key requirements of this Standard

This Standard sets out the principles and requirements for the transfer or creating an interest in the assets and liabilities of designated institutions in resolution which must be complied with by all designated institutions, in line with sound principles, practices and processes for the orderly resolution of a designated institution.

This Standard gives effect to the objective(s) and requirements of the Financial Sector Regulation, 2017 (Act No. 9 of 2017) as amended by the Financial Sector Laws Amendment Act, 2021 (Act No. 23 of 2021) relating to the transfer or creating an interest in the assets and liabilities of designated institutions in resolution.

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1 Commencement`

1.1 This Standard comes into effect on Day-Month-Year.

Version number	Commencement date
01	Day-Month-Year

2 Legislative authority

2.1 This Standard is made under section 105(2)(c) of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017).

3 Definitions and interpretation

3.1 In this Standard, **'the Act'** means the Financial Sector Regulation, 2017 (Act No. 9 of 2017) as amended by FSLA Act and any word or expression to which a meaning has been assigned bears the meaning so assigned to it by the Act unless the context indicates otherwise –

'asset management company' means a legal entity that currently exists or is created to manage the impaired or non-performing assets transferred to it from a designated institution in resolution in order to maximise the value through an eventual sale or an orderly wind-down;

'bridge institution' means a company incorporated in terms of section 166F of the Act;

'core business lines' means business lines and associated services which represent material sources of revenue or profit and are essential for the overall sustainability of the designated institution;

'core shared services' means activities performed by a designated institution or outsourced to a third party where failure would impair a designated institution's ability to continue its core business lines;

'covered deposit' means covered deposit as defined under section 1 of the Act;

'critical function' means, as defined under section 1 of the Act, in relation to a designated institution, a function that is –

- (a) essential to, or that contributes substantially to, financial stability and is performed by the designated institution; or
- (b) provided to, and essential to the continued operation of, the designated institution;

'critical shared services' means, activities performed by or within the designated institution or outsourced to a third party, where failure would lead to the designated institution's inability to perform critical functions;

'designated institution' means a designated institution as defined in section 29A (1) of the Act;

'designated institution in resolution' means, as defined under section 1 of the Act, a designated institution in respect of which a determination in terms of section 166J (2) of the Act is in force;

'essential services' means the core shared services and critical shared services that enable the maintenance of core business lines and the provision of critical functions by a designated institution;

'financial contracts' means types of financial contracts entered into by the designated institution which include -

- (a) Securities contracts, including -
 - (i) contracts for the purchase, sale or loan of a security, a group or index of securities;
 - (ii) options on a security or group or index of securities; and
 - (iii) repurchase or reverse repurchase transactions on any such security, group or index.
- (b) Commodities contracts, including -
 - (i) contracts for the purchase, sale or loan of a commodity or group or index of commodities for future delivery;
 - (ii) options on a commodity or group or index of commodities; and
 - (iii) repurchase or reverse repurchase transactions on any such commodity, group or index.

- (c) Futures and forwards contracts, including contracts for the purchase, sale or transfer of a commodity or property of any other description, service, right or interest for a specified price at a future date.
- (d) Swap contracts, including -
 - (i) swaps and options relating to interest rates; spot or other foreign exchange contracts; currency; an equity index or equity; a debt index or debt; commodity indices or commodities; weather; emissions or inflation;
 - (ii) total return, credit spread or credit swaps; and
 - (iii) any contracts or transactions that are similar to an agreement referred to under subparagraphs (a) or (b) which are the subject of recurrent dealing in the swaps or derivatives markets.

Master agreements entered into by the designated institution in respect of any of the types of financial contracts referred to above;

'flac instrument' means a flac instrument as defined under section 1 of the Act;

"FSLA Act" means Financial Sector Laws Amendment Act, 2021 (Act No.23 of 2021);

'governing body' means the governing body as defined in section 1 of the Act;

'hard interconnections' means interconnections that are too costly or too difficult to remove or mitigate;

'market infrastructure' means a market infrastructure as defined under section 1 (1) of the Financial Markets Act, 2012 (Act 19 of 2012);

'netting arrangements' refers to an arrangement in terms of an agreement entered into by the designated institution under which a number of claims or obligations can be converted into a single net claim or obligation;

'new acquiring institution' means an independent third party, who is not a bridge institution or an asset management company, who purchases the assets and liabilities of a designated institution in resolution;

‘orderly resolution of a designated institution’ means, as defined under section 1 of the Act, the management of the affairs of the designated institution as provided for under chapter 12A in a way that –

- (a) maintains financial stability;
- (b) ensures that the critical functions performed by the designated institution continue to be performed; and
- (c) in the case of a bank, protects the interests of depositors;

‘partial transfer’ means the transfer of some, but not all, assets and liabilities of a designated institution in resolution;

‘residual institution’ means the remaining entity after the transfer of assets and liabilities to a new acquiring institution or a bridge institution, which will be subject to liquidation or an orderly wind-down;

‘resolution resilient’ means that as long as the substantive obligations for services continue to be performed by the designated institution in resolution, the relevant contracts –

- (a) cannot be terminated, amended or suspended on the grounds of resolution;
- (b) can be transferred to a new recipient on the grounds of resolution; and
- (c) will support transfers necessitated by resolution;

‘resolution strategy’ refers to the strategy used by the SARB to manage the affairs of a designated institution in resolution;

‘SARB’ means the South African Reserve Bank in its capacity as the resolution authority in terms of section 166A of the Act;

‘separability’ means the designated institution’s ability to transfer legal entities, business lines, assets and liabilities in a short space of time to an independent third party, a bridge institution or an asset management company. Separability seeks to ensure that the complexities, structures and interdependencies of the designated institution do not pose barriers to the identified resolution strategy and the implementation of the relevant resolution tools;

‘separability analysis’ refers to the analytical process of assessing and describing all relevant aspects of the proposed transfer transaction, by the designated institution;

‘soft interconnections’ means interconnections that can be mitigated or removed with relative ease and minimal cost;

‘surviving institution’ means the remaining part of the designated institution in resolution that needs to continue after the impaired or non-performing assets have been separated and transferred to an Asset Management Company;

‘transfer playbook’ refers to an operational document to be used by the designated institution itself to demonstrate their ability to implement the transfer of the proposed assets and liabilities in resolution; and

‘transitional service agreement (TSA)’ refers to an agreement where the designated institution in resolution agrees to continue providing certain services related to the transferred assets and liabilities for a set period, to ensure a smooth transition, until the acquiring institution has the required capabilities in place.

4 Roles and responsibilities

- 4.1 The governing body, as defined in the Act, is ultimately responsible for ensuring that the designated institution has adequate measures in place to demonstrate the required capabilities and facilitate compliance with the requirements set out in this Standard, on a continuous basis.

5 Application

- 5.1 This Standard applies to all designated institutions, unless exempted by the Prudential Authority, based on the resolution strategy set by the SARB.
- 5.2 This Standard must be read in conjunction with the Act and other relevant laws.

6 Statutory transfer powers

- 6.1 Section 166S (1) of the FSLA Act confers powers to the SARB to enter into a particular transaction it deems necessary for the orderly resolution of a designated institution in resolution, without consent or approval from any specified person and despite law or agreement that would otherwise prevent the SARB from doing so.
- 6.2 The specific transactions covered by this Standard relates to the transferring or creating an interest in or dealing in any other way with the assets and liabilities of a designated institution in resolution, provided for under section 166S(2)(a) of the FSLA Act. These transactions are known as resolution transfer tools.
- 6.3 This Standard sets out the requirements for designated institutions to comply with, to enable the SARB to execute transfer tools which include the following -
- (a) transfer to a new acquiring institution, which entails the transfer of all or parts of assets and liabilities of a designated institution in resolution, as an immediate sale;
 - (b) transfer to a Bridge Institution, which entails the transfer of all or parts of assets and liabilities of a designated institution in resolution to a temporary entity with the objective to effect a sale to a new acquiring institution in the future; and
 - (c) transfer to an Asset Management Company, which entails the transfer of the impaired or non-performing assets of the designated institution in resolution to an Asset Management Company to maximise the value or recovery of the impaired assets. This is also known as an “asset separation tool”. This asset separation tool can only be used in conjunction with another resolution tool such as bail-in or transfer. The aim is to allow the designated institution to continue with its remaining viable business or to make the designated institution more marketable for a potential transfer to a new acquiring institution or a bridge institution.

7 Planning and execution of a resolution transfer tool

7.1 Designated institutions must prepare a separability analysis and a transfer playbook to ensure adequate preparation for effective execution of a transfer tool.

7.2 A designated institution must undertake a separability analysis to reflect the extent to which the separation of critical functions or core business lines can be achieved under appropriate continuity arrangements and to ensure that the designated institutions' complexities, structures, and interdependencies do not present barriers to the implementation of the identified transfer tools.

7.3 The separability analysis must include the following elements, at a minimum-

- (a) identification of assets and liabilities to be transferred ("transfer perimeter");
- (b) assessment of interconnections;
- (c) financial analysis and business plan for the transfer perimeter;
- (d) market interest and capacity; and
- (e) management information system capabilities.

7.4 A designated institution must develop a transfer playbook that it will use to operationalise the execution of the transfer perimeter and demonstrate implementation ability.

8 Requirements

8.1 Requirements for the transfer perimeter

- (a) Designated institutions must define the transfer perimeter, based on the guiding principles provided by the SARB under section 10 of this Standard. Defining the assets and liabilities to be transferred will constitute the first layer of the transfer perimeter. The second layer will consist of identified interconnections between the first layer of transfer perimeter and the rest of the designated institution.

8.2 Requirements for interconnections

- (a) To ensure continuity of the transfer perimeter after separation from the rest of the designated institution, the designated institution must identify and assess the financial, legal, operational, and business interconnections of the first layer of the transfer perimeter to the rest of the designated institution, to identify those interconnections that need to be included in or excluded from the transfer perimeter.
- (b) The lists provided below for financial, legal, operational and business interconnections are not exhaustive.
- (c) For financial interconnections, the designated institution must identify -
 - (i) any financial contract arrangements in the transfer perimeter such as collateral, securitisations and netting arrangements;
 - (ii) hedges not covered under sub-paragraph (i) above;
 - (iii) intra-group guarantees, funding and liquidity relationships; and
 - (iv) financial aspects that may have an impact on the separability of the transfer perimeter such as access to currencies or continuity of back-to-back transactions.
- (d) For legal interconnections, the designated institution must -
 - (i) identify legal interconnections between the transfer perimeter and the rest of the designated institution, including but not limited to -
 - (aa) legal interconnections due to existing service obligations (whether under service level agreements or not);
 - (bb) employee contracts and collective agreements (including retirement obligations);
 - (cc) contractual provisions attached to the assets and liabilities of the business unit;

- (dd) taxation matters (including deferred tax assets and liabilities) and litigation (i.e. product related such as mis-selling); and
 - (ee) relevant contracts with exclusion clauses such as joint ventures and partnerships.
 - (ii) assess the legal interconnections through a legal review of existing contracts mapped to the transfer perimeter, which should -
 - (aa) highlight third-party contracts and include resolution resilient clauses for contracts relevant to the transfer perimeter;
 - (bb) clearly identify the sources of litigation and conclude on whether these can be left in the residual institution or be included in the transfer perimeter; and
 - (cc) include a tax assessment of separability with proposals on whether the transfer perimeter can be structured in a way that limits unnecessary tax losses.
 - (iii) identify other legal aspects with a potential impact on the transfer including third country law contracts.
 - (iv) ensure that all relevant contractual arrangements are documented and cost as well as pricing structures are transparent and at a fair market value.
- (e) For operational interconnections, the designated institution must -
 - (i) identify operational interconnections that have an impact on the transfer perimeter, based on its service delivery model. Operational interconnections should, at least include the following elements: essential services, operational assets (including Information Technology (“IT”) and other infrastructure), critical staff and market infrastructures;
 - (ii) ensure operational continuity arrangements for the transfer perimeter including the following -

- (aa) for identified essential services: ensure that mitigation actions are in place to enable transferability of the service provision to the acquirer or ensure continued service provision to the surviving institution;
 - (bb) for operational assets (i.e.IT systems, licences, intellectual property etc.): ensure mitigation actions or contingency plans are in place for changes or redesign to allow the continuity of critical shared services and access to all necessary parties and arrangements are in place for continued access to relevant operational assets such as licencing contracts that are resolution resilient;
 - (cc) for relevant staff or roles: ensure the relevant roles and required expertise are properly mapped and any labour law liabilities are identified. Establish mitigation actions, such as retention plans, to ensure all the relevant roles would be adequately staffed in resolution; and
 - (dd) for market infrastructures: analyse which contracts with market infrastructure service providers need to be included in the transfer perimeter and which should stay in the residual institution.
- (iii) ensure that the designated institutions' contingency plans related to market infrastructures are sufficient to provide continuity of access for the market infrastructure relationships in the transfer perimeter. Put in place temporary access through transitional service agreements or other mitigating actions such as identifying possible substitutes or possibilities for customer portability.
- (f) For business interconnections, the designated institution must -

- (i) assess cross organisational business unit links such as synergies, cross-selling, client relationships and revenue generations driven by multiple business units; and
 - (ii) consider franchise impact on both the surviving institution or the acquirer.
- (g) For all the identified interconnections related to the transfer perimeter, the designated institution must -
 - (i) conclude on whether the identified interconnections are hard or soft and whether the designated institution can remove or mitigate them; and
 - (ii) where applicable, put arrangements in place for mitigating actions including the time and cost to implement as well as any foreseen potential barriers to implementation.
- (h) The designated institution must include all the hard interconnections in the transfer perimeter, to form the second layer of the transfer perimeter. The first plus the second layer will then constitute the final transfer perimeter.

8.3 Requirements for financial analysis and business plan

- (a) The designated institution must provide a historical financial analysis in the form of a business plan for the transfer perimeter. This financial analysis should include the following regarding the transfer perimeter -
 - (i) segments or portfolios to be included;
 - (ii) the resulting balance sheet and profit and loss;
 - (iii) key performance indicators; and
 - (iv) capitalisation as well as liquidity and funding (including potential funding sources).
- (b) The designated institution must provide, as part of the business plan, a detailed description of the costs of dealing with interconnections as follows -

- (i) removing interconnections by cancelling existing contracts and establishing new ones such as Transitional Service Agreements (TSA);
- (ii) mitigating interconnections by substituting existing contracts for ones with resolution-resilient clauses and modification to some contracts (i.e., re-designing IT infrastructure); and
- (iii) maintaining interconnections and calculating the possible impact when -
 - (aa) not terminating certain contracts (i.e. labour contracts with retirement fund rights); and
 - (bb) litigation liabilities that cannot be left in the residual institution.
- (c) The designated institution must propose alternative perimeters (which may deviate based on how the assessed interconnections could be addressed) and may use the financial analysis as the deciding factor to support the choice of the proposed transfer perimeter.

8.4 Requirements for market capacity and interest

- (a) The designated institution must propose a list of most suitable potential buyers and assess their suitability based on the following-
 - (i) business indications of appetite (i.e. recent mergers & acquisition transactions in the past 24 months);
 - (ii) strategic fit of the transfer perimeter (i.e. geographic coverage, distribution channels, client relationships, etc);
 - (iii) acquirer's financial strength given their available capital, for a transaction based on capital requirements and market access to raise new capital (based on recent issuances);
 - (iv) acquirer's operational capacity; and
 - (v) market concentration.

8.5 Requirements for management information systems

- (a) Designated institutions must have the ability to provide accurate and readily available information necessary for all assets and liabilities to be transferred, for the required valuations and the ability to provide access to necessary data to all relevant stakeholders (i.e. for a due diligence).
- (b) Designated institutions must have management information system capabilities to perform the following, at a minimum -
 - (i) identify the first layer of the transfer perimeter;
 - (ii) provide information on and assessment of interconnections related to the transfer perimeter;
 - (iii) identify the “hard interconnections” to be included in the transfer perimeter;
 - (iv) ensure operational continuity of the transfer perimeter;
 - (v) provide transfer perimeter valuation-related data; and
 - (vi) support the drafting of due diligence and marketing materials as part of the sales process.
- (c) Designated institutions’ management information system capabilities must support the transfer perimeter with the provision of pertinent information on the assets and liabilities including -
 - (i) mapping of critical functions and core business lines to each item in the transfer perimeter;
 - (ii) classification of items (i.e. type of assets and liabilities; counterparty information; type of collateral etc);
 - (iii) asset quality and risk indicators (i.e. non-performing loans, risk-weighted assets, high-quality liquid assets etc.);
 - (iv) legal aspects (i.e. governing law and any other contractual impediments to transferability); and
 - (v) accounting information (carrying amounts, off balance sheet amounts, loan-loss provisions) when relevant.

8.6 Requirements for the transfer playbook

- (a) Designated institutions must prepare a Transfer Playbook, as an internal operational document for executing the relevant transfer tool, detailing the processes needed, business units involved, and operational steps necessary to -
 - (i) identify the transfer perimeter;
 - (ii) produce the documentation required;
 - (iii) implement the resolution transaction in the designated institutions' system and in legal terms.
- (b) The main elements of the transfer playbook, must include but not be limited to -
 - (i) governance arrangements (which include tasks to be conducted, clear indication of responsibilities, roles of committees and business units and senior management responsible for the separability execution);
 - (ii) implementation timelines;
 - (iii) steps to implement mitigation strategies for the identified barriers and potential impediments to execution;
 - (iv) analysis of interconnections and other separability aspects;
and
 - (v) communication with internal and external stakeholders.

9 Protected arrangements

- 9.1 The SARB will apply safeguards to protect the integrity of financial arrangements such as netting arrangements and collateralisation, particularly in a partial transfer, to protect the counterparties involved and the economic effect of the arrangement.
- 9.2 For liabilities that are secured, the SARB will ensure that the creditor claims are not separated from the assets securing the liability (collateral).

- 9.3 For financial contracts, the SARB will ensure there is no 'cherry picking' or selective transferring of individual contracts with a particular counterparty that are subject to the same netting arrangements. These contracts will either be transferred as a whole, or they will not be transferred at all.
- 9.4 Designated institutions must identify and disclose financial arrangements they deem to fall under protected arrangements to the SARB.
- 9.5 The SARB reserves the right to apply the safeguards to the extent that they do not compromise the feasibility and effectiveness of the relevant resolution transfer tool.

10 Requirements to define the transfer perimeter

- 10.1 When defining the transfer perimeter, the designated institution must consider at a minimum, that the assets and liabilities to be transferred constitute a perimeter that can -
- (a) preserve the continuity of critical functions and core business lines;
 - (b) be structured in a way that is financially, legally and operationally sound to enable efficient execution of the transfer;
 - (c) represent a clear set of assets and liabilities that attracts market interest and consider attractive features such as cash, other liquid assets or performing loans; and
 - (d) be absorbed by the market (considering investors with previous integration experience, sufficient funds, excess capital or sufficient access to the market, strategic fit as well as fit with regards to competition).
- 10.2 In addition to the requirements under 10.1 above, the designated institution must consider including, to the maximum extent possible, the following -
- (a) assets, rights and/or liabilities that belong to clients;
 - (b) covered deposits;
 - (c) liabilities that may give rise to no creditor worse off than in liquidation (NCWOL) claims if they remained in the residual institution; and

(d) liabilities protected under section 166S (9) of the FSLA Act.

10.3 For transfer to an Asset Management Company, the designated institution should highlight to the SARB any assets, rights and/or liabilities that meet the following criteria -

(a) the market for those assets is of such a nature that the liquidation of those assets could have an adverse effect on other financial markets;

(b) the transfer is necessary to enable the designated institution in resolution to function properly; and

(c) the transfer is necessary to maximise the value or the recovery of the impaired assets (compared to liquidation proceeds).

11 Governance requirements

11.1 A designated institution must have in place clearly defined policies and procedures, documented practices as well as internal system capabilities for monitoring and ensuring compliance with the requirements in this Standard.

11.2 These policies, procedures and capabilities must be established as part of resolution planning obligations, irrespective of whether an actual resolution is foreseen, and should be embedded in designated institutions' internal governance framework and risk management processes.

11.3 The development, monitoring, review and approval of the requirements set in this Standard, must be subject to an appropriate governance process with clearly assigned roles and responsibilities for operational staff, senior management and the governing body.

12 General compliance requirements

12.1 The SARB will, on an ongoing basis, assess a designated institution's compliance with the requirements in this Standard and failure by a designated institution to comply with this Standard may result in one or more of the following actions being taken by the Prudential Authority against such designated institution -

- (a) an increase in a designated institution's flac instrument holdings, where applicable;
- (b) an increase in a designated institution's required regulatory capital; and/or
- (c) an acceleration in the triggering of resolution action.

13 Reporting requirements

- 13.1 Designated institutions must perform ongoing reviews of information requirements contained in this Standard and the testing of Management Information System capabilities as well as arrangements to support the successful execution of a resolution transfer tool.
- 13.2 The form, manner and period for regulatory reporting on this Standard will be determined by the Prudential Authority as directed by the SARB and published on the Prudential Authority's website.