

Statement of the need for, expected impact of and intended operation of the draft Prudential Standard relating to the requirements for funding and liquidity in resolution



SOUTH AFRICAN RESERVE BANK
Prudential Authority

Statement of the need for, expected impact of and intended operation of the draft Prudential Standard relating to the requirements for funding and liquidity in resolution

(Draft for Consultation)

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1. Introduction

- 1.1 The Statement of the need for, expected impact and intended operation of the proposed Prudential Standard (the proposed Standard) relating to the requirements for funding and liquidity in resolution (the Statement) is prepared and published by the Prudential Authority (PA). This is in accordance with and in fulfilment of the requirements under section 101 of the Financial Sector Regulation Act 9 of 2017 (the FSR Act).
- 1.2 The proposed Standard is made in terms of section 105(2)(c) read with section 30(1A) of the FSR Act and sets out the principles and requirements for funding and liquidity in resolution that must be complied with by all designated institutions. The proposed Standard for funding and liquidity in resolution is aligned to the sound principles, practices and processes for the orderly resolution of a designated institution.
- 1.3 In the aftermath of the global financial crisis, the Financial Stability Board (FSB) as part of its considerations, has identified funding and liquidity as important themes to be addressed in resolution planning and has issued related publications¹ to complement the Key Attributes of Effective Resolution Regimes for Financial Institutions² (Key Attributes).
- 1.4 The Key Attributes represents a framework for dealing with the failure of certain systemic financial institutions and constitutes the international standard that is expected to be adhered to by all the Group of 20 (G20) member jurisdictions in formulation of their resolution frameworks.

2. Statement explaining the need for the proposed Standard

- 2.1 Section 166A(1) of the FSR Act designates the Reserve Bank as the resolution authority. In terms of section 166E of the FSR Act, the Reserve Bank must

¹ Guiding principles on the temporary funding needed to support the orderly resolution of a global systemically important bank (G-SIB), August 2016 <https://www.fsb.org/2016/08/guiding-principles-on-the-temporary-funding-needed-to-support-the-orderly-resolution-of-a-global-systemically-important-bank-g-sib/>; and Funding Strategy Elements of an Implementable Resolution Plan, June 2018 <https://www.fsb.org/2018/06/funding-strategy-elements-of-an-implementable-resolution-plan-2/>.

² Key Attributes of Effective Resolution Regimes for Financial Institutions (revised version 2024) <https://www.fsb.org/2024/04/key-attributes-of-effective-resolution-regimes-for-financial-institutions-revised-version-2024/>

take adequate and appropriate steps to plan for the potential need for the orderly resolution of a designated institution.

- 2.2 To achieve its resolution objectives as set out in the FSR Act, the Reserve Bank is required to perform its resolution functions in relation to a designated institution and ensure that the affairs of a designated institution in resolution are managed in order to maintain financial stability, as far as practicable.
- 2.3 Failure by a designated institution to adequately estimate and access sufficient funding and liquidity in resolution to ensure the continued provisioning of critical functions and the ability to meet its obligations as they fall due may impede the Reserve Bank's ability to execute an orderly resolution of a designated institution.
- 2.4 To address this potential impediment to resolution, a designated institution must have capabilities and arrangements in place, such that in the lead up to and during resolution, it may reasonably anticipate its funding and liquidity needs in resolution and appropriately measure, monitor and mobilise funding and liquidity effectively.
- 2.5 The proposed Standard complements the principles and resolution objectives stipulated in the Key Attributes and the FSR Act. It sets out the requirements for designated institutions to have in place prior arrangements and capabilities for funding and liquidity in resolution that must be complied with by all designated institutions.
- 2.6 The requirements provided for in the proposed Standard will, if adequately and appropriately implemented, improve the resolvability of designated institutions, thereby enhancing the Reserve Bank's ability to execute an orderly resolution, without unduly exposing taxpayers to financial losses.
- 2.7 Internal liquidity resources and market-based funding sources are the preferred sources of funding and liquidity for a designated institution in resolution. Designated institutions must consider various assumptions as set out in the proposed Standard to estimate funding and liquidity requirements in resolution and include the liquidity needs in the run-up to, during resolution,

as well as, when it ceases to be in resolution. These assumptions should include the likelihood that the market may not immediately have confidence in a designated institution during resolution, and as such, it may be challenging to attract sufficient funding for some time.

- 2.8 Temporary liquidity support by the South African Reserve Bank (SARB) in its role as a participant in the financial safety net may be required to foster financial stability and promote market confidence in instances where internal liquidity and market-based sources of funding are temporarily insufficient or have been exhausted.
- 2.9 Any such temporary liquidity support by the SARB would be subject to the relevant processes, requirements and conditions as may be set by the SARB. For instance, designated institutions have the option to apply for emergency liquidity assistance (ELA), which is subject to approval by and at the discretion of the SARB and will be considered in line with the eligibility criteria outlined in the SARB's policy framework for the provision of ELA.
- 2.10 A designated institution in resolution may have access to the SARB's normal liquidity facilities, subject to applicable eligibility criteria. In addition, the SARB has discretion to provide committed liquidity facilities, e.g., restricted committed liquidity facility (R-CLF) to designated institutions.

3. Statement of the expected impact of the proposed Standard

- 3.1. Without pre-empting the outcome of the consultation, it is expected that the cost of implementing the proposed Standard may vary across designated institutions, given the differences in their business structures, business models or state of readiness in ensuring the availability of sufficient funding and liquidity sources in resolution.
- 3.2. It is worth noting that there exist leverage opportunities between the requirements set out in the proposed Standard and the risk management processes, procedures and arrangements already implemented by designated institutions to manage liquidity risk, including the work undertaken in the development of recovery plans.

- 3.3. To better understand the impact of the proposed Standard, and to identify any potential unintended consequences, the Reserve Bank and the PA have issued a questionnaire for industry consultation.
- 3.4. Interested stakeholders are encouraged to respond to the questions designed to identify any potential risks or unintended consequences that might arise from the implementation of the proposed Standard.
- 3.5. Following the consultation process, the PA may make any necessary changes to the proposed Standard and this Statement in order to better reflect the expected impact of the proposed Standard based on the submissions received.
- 3.6. The proposed Standard and Statement will be published for another round of public consultation (formal consultation) process in terms of section 98 of the FSR Act.

4. Statement explaining the intended operation of the proposed Standard

- 4.1. Once finalised, the Standard will apply to all designated institutions. The proposed Standard is envisaged to become effective 24 months after it is made. Once finalised, the governing body of a designated institution will be responsible for ensuring continuous compliance with the requirements set out in the Standard.
- 4.2. The form, manner and period for reporting obligations related to the proposed Standard, where such requirements have not been specified in the proposed Standard, will be determined by the PA as directed by the Reserve Bank. These will be published on the PA's website.
- 4.3. Following the implementation of the Standard, the Reserve Bank will continuously assess and evaluate its effectiveness to ensure that any unintended consequences on the sector and general public are adequately addressed.

5. Conclusion

- 5.1. The requirements specified in the proposed Standard will form part of South Africa's resolution framework. The proposed Standard will assist designated institutions to adequately prepare for resolution thereby improving their resolvability and facilitating the continuity of their critical functions to the economy.
- 5.2. In addition, the requirements set out in the proposed Standard will enable the Reserve Bank to prepare a credible and feasible resolution plan. This will in turn enhance the Reserve Bank's ability to execute an orderly resolution of a designated institution to achieve its resolution objectives as outlined under Chapter 12A of the FSR Act.