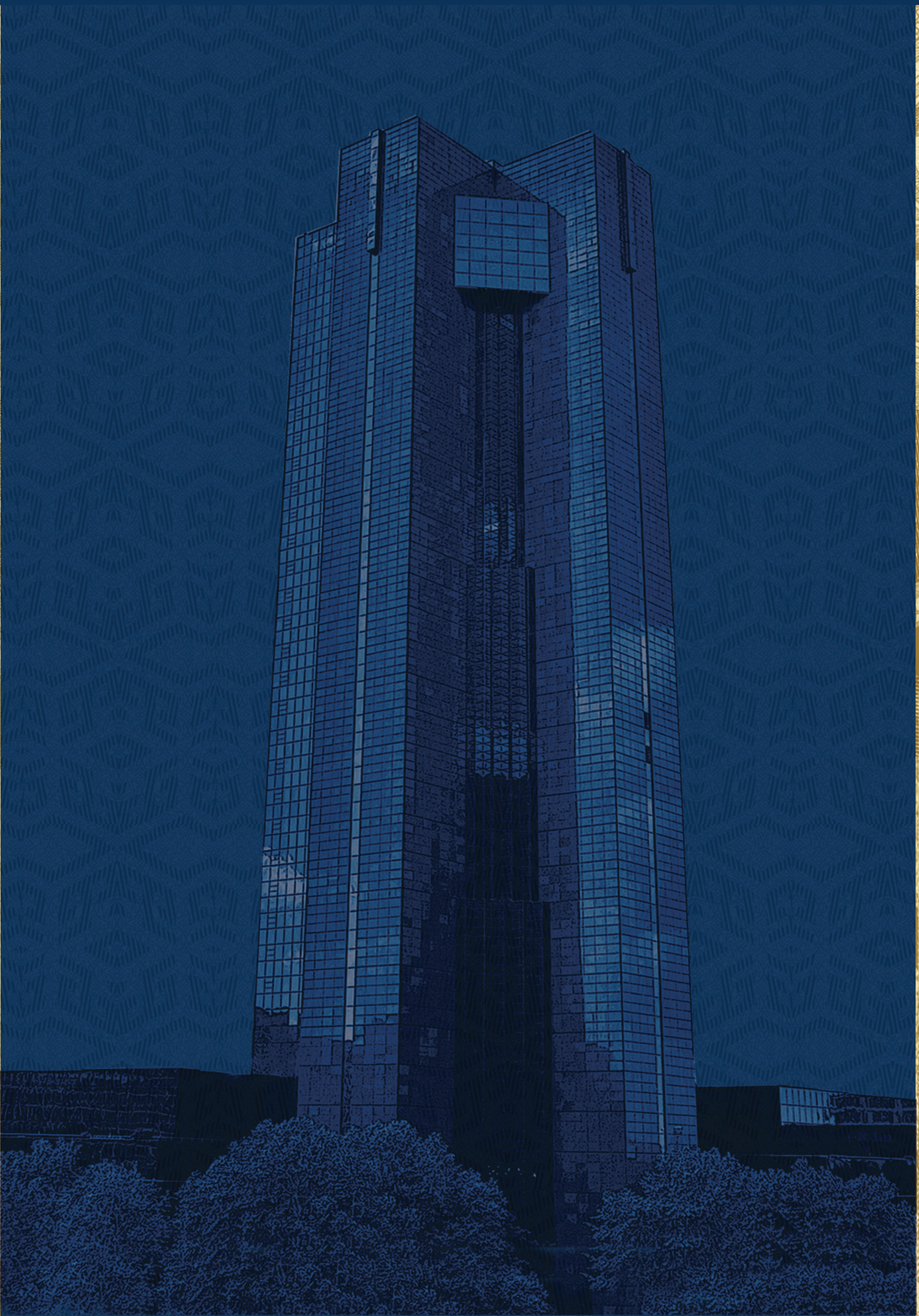
Bank Supervision Department

Annual Report 2015



South African Reserve Bank

Bank Supervision Department

Annual Report 2015

South African Reserve Bank

Vision

A sound, well-functioning and internationally competitive banking system.

Mission

To promote the soundness of the banking system and contribute to financial stability.

Business philosophy

Market principles inform all our activities and decisions, and we strive to act with professionalism, integrity, credibility and impartiality at all times. We liaise with each individual bank through a single point of entry – a relationship manager, assisted by a team with diverse competencies. We follow a risk-based supervisory approach and our objective is to add value. We place emphasis on empowering our staff to ensure that all interaction and service delivery is characterised by professionalism, and a high premium is placed on ethical behaviour at all levels of activity. A relationship of mutual trust between the Bank Supervision Department and all other key players is regarded as essential and is built up through regular open communication. In our endeavours to foster a stable banking sector, we contribute to creating the foundation for sustainable growth in the economy.

Purpose of the *Annual Report*

Legal basis for the *Annual Report*

The *Annual Report* is issued in terms of section 10 of the Banks Act 94 of 1990 which prescribes the following:

> 10. *Annual report* by Registrar
> (1) The Registrar shall annually submit to the Minister a report on his or her activities in terms of this Act during the year under review.
> (2) The Minister shall lay a copy of the report referred to in subsection (1) upon the Tables in Parliament within 14 days after receipt of such report, if Parliament is then in ordinary session, or, if Parliament is not then in ordinary session, within 14 days after the commencement of its next ensuing ordinary session.

This issue of the *Bank Supervision Department Annual Report 2015* focuses mainly on the 12-month period ending 31 December 2015. However, selected developments up to the time of finalisation were also reported on. Data presented were updated on 16 February 2016. Latest data are available at: http://www.resbank.co.za.

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1.1 Introduction

Over the past year, the global economic outlook has become more uncertain, driven in part by strong financial market reactions to the unabated decline in international commodity prices, with the oil price in particular slipping to its lowest level since 2004. Tightening financial conditions and lower commodity prices are providing significant headwinds to growth going forward.

The South African economy also experienced serious challenges during 2015, including a possible change of the South African sovereign credit rating to sub-investment grade. Growth continued to be constrained by weaker global trade and commodity price declines. The commodity price declines pose downside risks to the economic growth outlook in South Africa and many parts of Africa due to a high reliance on mining for employment, export growth and government revenue. Various South African banks have operations across Africa and are therefore exposed (directly and indirectly) to the downturn in the commodity super cycle. More idiosyncratic factors such as electricity shortages and the effects of the prolonged severe drought on the agricultural sector were also prevalent.

Consumers remained constrained against the backdrop of slow employment growth, declining disposable income and rising inflation. This, combined with tighter affordability criteria following the implementation of amendments to the National Credit Regulations, resulted in subdued growth in retail credit exposure.

Credit extension to the corporate sector, by contrast, has been buoyant. However, several increases in the repurchase rate of the South African Reserve Bank (the Bank) during the past 24 months, together with the economic backdrop and sovereign risk issue described above, require renewed focus on the sector's management of credit risk.

The Bank Supervision Department (Department) continued to monitor the impact of market conditions on South African banks' respective risk exposures, including credit risk profiles and portfolios, liquidity risk and market risk through a number of initiatives.

Against this backdrop, the South African banking sector remained financially sound and profitable during 2015. The sector was, and continues to be supported by a regulatory and supervisory framework that creates an environment which promotes the safety and soundness of individual banks and the whole banking system, as well as supporting an environment conducive to sustainable investment. However, effective banking supervisory practices, which form a key component of such a framework, are not static. The global financial crisis that started in 2007 highlighted the importance of a comprehensive and coordinated response from regulators and policymakers to carefully reform the internationally agreed regulatory and supervisory frameworks and standards, to secure and promote the safety and soundness of the global banking system.

In this regard, members of the Basel Committee on Banking Supervision (Basel Committee), including South Africa, finalised and implemented comprehensive amendments to their respective regulatory and supervisory frameworks during the past number of years to not only promote the safety and soundness of individual banks registered to conduct the business of a bank in their respective jurisdictions, but also the safety and soundness of the wider group of entities to which that bank belongs.

As part of its post-crisis reform efforts, the Basel Committee established the Regulatory Consistency Assessment Programme (RCAP)[1] to assess members' implementation of the Basel standards. The year under review saw the completion of South Africa's RCAP which focused on the local implementation of the Basel framework's risk-based capital standards and liquidity coverage ratio (LCR) standards. Following the implementation of selected amendments to the Regulations relating to Banks (Regulations) described in more detail in section 3.3 of this report, the RCAP assessment team found the local implementation of the risk-based capital regulations

1. For background information on RCAP, refer to clause 1.13 of the 2014 *Bank Supervision Department Annual Report*.

to be 'compliant' with the Basel standards as all 14 components were assessed as 'compliant'.[2] South Africa's prudential regulations were also assessed and reported as 'compliant' with the standards on LCR and the LCR disclosure standards.[3]

During 2015 the Department continued to exercise its enforcement powers in terms of the Banks Act 94 of 1990 (Banks Act) with regard to illegal deposit-taking, as well as its supervisory responsibilities in terms of the Financial Intelligence Centre Act 38 of 2001 (FIC Act). With regard to the latter, the Department conducted routine supervisory inspections of banks' control measures for anti-money laundering and combating the financing of terrorism (AML/CFT). The Bank consequently imposed administrative sanctions on selected banks, which included financial penalties and the requirement that certain remedial actions be taken. Administrative sanctions were not imposed because banks were found to have facilitated transactions involving money laundering or the financing of terrorism, but as a result of weaknesses in their control measures.

The curatorship of African Bank Limited (African Bank) continued throughout the year under review. Significant progress was made to establishing the new 'Good Bank'. The curator appointed designate membership to the Board of Directors (Board) and senior management for the proposed new entity. Furthermore, the curator received support, in principle, from both the senior unsecured debt holder committee and the Tier II debt holder committee for the restructuring proposal of the Good Bank.[4] An application for a banking licence was received and approved.[5]

The remainder of this chapter includes the discussion of the Department's strategic focus areas (SFAs), key local banking-sector trends and regulatory developments, results of the South African RCAP, international regulatory developments (including the Department's participation in those forums) and areas requiring attention during 2016.

1.2 Bank Supervision Department's strategic focus areas

The SFAs guide the activities of the Department to focus resources where the need is most pertinent. Each year the Department reviews its SFAs taking into consideration the changing external environment, changes emanating from international regulatory developments and emerging and actual trends in the South African banking sector.

Substantial progress was made in achieving the objectives of the SFAs, which included:

- embedding the principles of a forward-looking approach into the supervisory framework;
- participating in the design and implementation of the Twin Peaks regulatory framework,[6] as elaborated on in section 1.6.1;
- assessing risks arising from the continued expansion of South African banking groups into the African continent;
- influencing international regulatory standards in the interest of South Africa specifically and the African continent in general; and
- building and strengthening the Department's human resource capacity.

The Department's strategy in 2016/17 will be guided by the establishment of the Prudential Authority (PA) within the Bank and related provisions in the enacting legislation relating to the Twin Peaks system of financial regulation – the Financial Sector Regulation Bill (FSR Bill).

2. The full report is available at http://www.bis.org/bcbs/publ/d322.pdf

3. The full report is available at http://www.bis.org/bcbs/publ/d323.pdf

4. For further information, refer to African Bank Sens announcements, available at https://www.africanbank.co.za/about-us/investors.

5. The new African Bank was launched on 4 April 2016.

6. The Twin Peaks system recognises the different skill sets required for prudential and market conduct regulation. Prudential regulation is designed to maintain safety, soundness and solvency of financial institutions or funds, while market conduct regulation requires the perspective of a customer, which is a different regulatory perspective and philosophy.

1.3 High-level overview of key banking-sector trends

1.3.1 Introduction

The number of entities that has been registered with the Department since 2006 is presented in Table 1.1. As at the end of December 2015, 32[7] banking institutions were reporting data to the Department. A total of 40 international banks operated authorised representative offices in South Africa as at December 2015. As at the end of December 2015 African Bank remained under curatorship.

Detailed commentary regarding the entities registered or licensed with the Department at the end of 2015 is presented in appendices 2 to 5 and 7.

7. This number excludes mutual and cooperative banks, but includes one institution conducting banking business in terms of an exemption from the provisions of the Banks Act, namely Ithala SOC Limited.

Table 1.1 Banking entities registered in South Africa

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Banks*	19	19	19	18	17	17	17	17	17	17
of which: banks under curatorship	0	0	0	0	0	0	0	0	1	1
Banks in final liquidation	2	2	2	2	2	2	2	2	2	2
Mutual banks	2	2	2	2	2	2	3	3	3	3
Cooperative banks	0	0	0	0	0	2	2	2	2	2
Local branches of international banks	14	14	14	13	13	12	14	14	14	15
Representative offices	43	46	43	42	41	43	41	43	40	40
Controlling companies	16	16	16	16	16	16	16	16	16	16

* Includes active banks and banks exempted by the Registrar of Banks (with effect from 1 July 1996) in terms of the Supervision of Financial Institutions Rationalisation Act 32 of 1996 and section 1(cc) of the Banks Act 94 of 1990

1.3.2 Total asset structure of the South African banking sector

The total asset structure of the South African banking sector[8] is presented in Figure 1.1. South Africa's banking sector is dominated by the five largest banks which collectively held 89,2 per cent (December 2014: 90,6 per cent) of the total banking assets as at 31 December 2015. Local branches of international banks contributed 7,3 per cent (December 2014: 5,8 per cent) as at 31 December 2015. The remaining banks accounted for 3,5 per cent (December 2014: 3,6 per cent) of total banking assets.

8. Based on the aggregation of data submitted during 2014 and 2015 from individual South African-registered banks, including local branches of international banks, but excluding offshore branches and subsidiaries of South African banks, mutual banks and cooperative banks.

Figure 1.1 Total asset structure of the South African banking sector

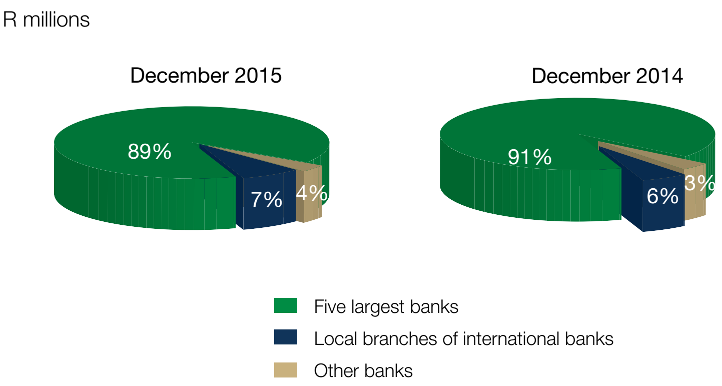


Table 1.2 Selected indicators for the South African banking sector

	Dec 2014	Mar 2015	Jun 2015	Sep 2015	Dec 2015
Balance sheet					
Total assets (R billions)	4 176	4 369	4 434	4 617	4 831
Total assets: Year-on-year growth (per cent)	8,71	10,28	10,17	12,03	15,69
Gross loans and advances (R billions)	3 236	3 368	3 441	3 537	3 601
Gross loans and advances: Year-on-year growth (per cent)	9,06	9,19	8,93	10,25	11,29
Total equity (R billions)	318	322	332	335	342
Profitability					
Cost to income (smoothed) (per cent)	54,71	54,45	55,00	56,25	55,39
Return on equity (smoothed) (per cent)	13,86	15,39	15,86	16,05	17,09
Return on assets (smoothed) (per cent)	1,02	1,12	1,15	1,15	1,21
Capital adequacy					
Common equity Tier 1 capital adequacy ratio (per cent)	11,40	11,00	11,12	11,09	11,03
Tier 1 capital adequacy ratio (per cent)	11,94	11,44	11,56	11,52	11,44
Capital adequacy ratio (per cent)	14,76	14,12	14,35	14,33	14,19
Credit risk					
Impaired advances (R billions)	105	108	114	113	112
Impaired advances as a percentage of total advances (per cent)	3,24	3,21	3,31	3,21	3,12
Specific credit impairments as a percentage of impaired advances (per cent)	49,09	49,19	45,65	46,32	47,80
Specific credit impairments as a percentage of gross loans and advances (per cent)	1,59	1,58	1,51	1,49	1,49

Note:

This table presents an overview of the financial and risk information, compiled by means of the aggregation of data submitted during 2014 and 2015 from individual South African-registered banks (including local branches of international banks but excluding offshore branches and subsidaries of South African banks, mutual banks and cooperative banks). Information represents aggregated banks-solo information. Smoothed refers to calculations based on a 12-month moving average. Information is subject to change without notice. Banking-sector data are available at http://www.resbank.co.za/RegulationAndSupervision/BankSupervision/Banking%20sector%20data/Pages/default.aspx.

Total banking-sector assets grew by 15,7 per cent year on year to R4 831 billion at the end of December 2015 (December 2014: R4 176 billion). The annual growth in banking-sector assets is mainly attributed to the annual growth of 11,3 per cent in gross loans and advances and 89,2 per cent in derivative financial instruments. Gross loans and advances accounted for 74,5 per cent of the banking-sector assets at the end of December 2015 (December 2014: 77,5 per cent) and amounted to R3 601 billion (December 2014: R3 236 billion). The increase in gross loans and advances was mainly due to increases in other loans to customers, which grew by R126 billion year on year (specifically in the categories of foreign currency loans, other loans and overnight loans) and term loans, which recorded an R85 billion year-on-year growth.

The banking-sector assets were mainly funded by deposits, current account and other creditors, which constituted 84,1 per cent of total banking-sector liabilities as at 31 December 2015 (December 2014: 88,2 per cent). Derivative financial instruments and term debt instruments accounted for 10,4 per cent and 3,6 per cent respectively of total liabilities at the end of December 2015. As at the end of December 2015 the banking-sector deposits comprised mainly of fixed and notice deposits (27,8 per cent), current accounts (19,6 per cent), call deposits (18,4 per cent) and other deposits and loan accounts (15,2 per cent). Deposits from corporate customers remained the largest component of total deposits for banks during 2015 and amounted to 40,7 per cent of total deposits at the end of December 2015 (December 2014: 43 per cent). Other major sources of banking-sector deposits during 2015 included deposits from retail customers (25,2 per cent), banks (14 per cent) and securities firms (9,5 per cent).

The 12-month moving average cost to income ratio deteriorated slightly during 2015, ending the year at 55,4 per cent (December 2014: 54,7 per cent). The 12-month moving average on return on equity (ROE) and return on assets (ROA) increased during 2015 and amounted to 17,1 per cent and 1,2 per cent respectively at the end of December 2015 (December 2014: 13,9 per cent and 1 per cent respectively). The increase in both the ROE and ROA ratios as at 31 December 2015 is mainly due to the increase in operating profit, which increased by 20,8 per cent year on year, compared to 7,4 per cent year-on-year growth recorded at the end of December 2014. The increase in operating profit was mainly due to increases in net-interest income and non-interest revenue, as well as a decrease in credit losses.

Total banking-sector equity increased by 7,4 per cent from R318 billion in December 2014 to R342 billion in December 2015. Total equity primarily comprised retained earnings and share capital throughout 2015, accounting for 51,6 per cent and 45,1 per cent respectively of total equity at the end of December 2015 (December 2014: 51,1 per cent and 40 per cent respectively).

Banks' operations in South Africa (bank solo) remained adequately capitalised. However, capital adequacy ratios (CARs) decreased slightly compared to December 2014. Total CAR decreased to 14,2 per cent at the end of December 2015 (December 2014: 14,8 per cent). Common equity Tier 1 CAR and Tier 1 CAR amounted to 11 per cent and 11,4 per cent respectively at the end of December 2015 (December 2014: 11,4 per cent and 11,9 per cent respectively). The decrease in the CARs is mainly due to the increase in credit risk-weighted exposures.

Impaired advances[9] increased by 7 per cent to R112 billion at the end of December 2015 (December 2014: R105 billion), due to an increase in impaired corporate exposures (excluding specialised lending and small and medium-sized corporate exposures). The ratio of impaired advances to gross loans and advances, a key indicator of credit quality in the banking sector, remained largely unchanged at an average of 3,2 per cent during 2015 and amounted to 3,1 per cent at the end of December 2015 (December 2014: 3,2 per cent). Specific credit impairments increased by 4,2 per cent to R54 billion at the end of December 2015. Expressed as a percentage of impaired advances, specific credit impairments decreased from 49,1 per cent at the end of December 2014 to 47,8 per cent at the end of December 2015. Expressed as a percentage of gross loans and advances, specific credit impairments remained largely unchanged at an average of 1,5 per cent during 2015 and amounted to 1,5 per cent at the end of December 2015 (December 2014: 1,6 per cent).

9. Impaired advances are those advances in respect of which a bank has raised a specific impairment and include any advance or restructured credit exposure subject to amended terms, conditions or concessions that are not formalised in writing.

1.3.3 Group structures: approval of local and foreign expansions by South African banking groups

Table 1.3 presents the number of applications the Department has approved since 2006 in terms of section 52 of the Banks Act. The majority of the applications received in 2015 was submitted by the five largest banking groups (refer to Appendix 8 for more information in this regard).

Table 1.3 Group structures: number of approvals for local and foreign expansions granted in terms of section 52 of the Banks Act 94 of 1990

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Local	16	12	15	10	16	19	12	19	13	40
Foreign*	8	25	19	26	22	27	14	21	25	19
Total	24	37	34	36	38	46	26	40	38	59

* Excludes transactions undertaken by Investec plc

1.4 Enforcement

1.4.1 Introduction

Enforcement actions vary from implementing preventative and corrective actions to enforcing compliance. The Department performs ongoing reviews of banks' operations to assess whether to continue with unaltered supervision of a particular bank, or to enact any of, or a combination of the following:

- focused supervisory scrutiny;
- specific directives;
- increased minimum capital requirements;
- inspections in terms of the Banks Act and other relevant legislation; and
- administrative sanctions such as penalties and fines.

The type of enforcement action required is informed by a particular bank's willingness and promptness in taking preventative or corrective actions and the seriousness and extent of any non-compliance or risks identified.

1.4.2 Curatorship of African Bank Limited

African Bank was placed under curatorship on 10 August 2014 and the discussions of the events leading to the curatorship are contained in the Department's 2014 *Annual Report*.

10. The new African Bank was launched on 4 April 2016.

During 2015, Mr Tom Winterboer of PriceWaterhouseCoopers who was appointed by the Registrar of Banks (the Registrar) as the curator of African Bank continued his responsibility of managing the bank, while the bank continued to operate in a stable manner. Significant progress was made to establish the new 'Good Bank'. The curator appointed designate board membership and senior management for the proposed new entity. Furthermore, the curator received, in principle, support from both the senior unsecured debt holder committee and the Tier II debt holder committee for the restructuring proposal of the Good Bank. An application for a banking licence was received and approved.[10]

1.4.3 Administrative sanctions imposed for AML/CFT non-compliance

In terms of the FIC Act, the Bank, through the Department, is mandated to supervise and enforce banks' compliance with the FIC Act. The FIC Act also stipulates that a supervisory body may impose an administrative sanction on an accountable institution for its failure to comply with the provisions of the FIC Act.

In line with its supervisory mandate, the Department conducted a routine inspection at Deutsche Bank AG Johannesburg Branch (Deutsche Bank) during 2014, with the aim to assess whether appropriate measures and controls were in place to ensure compliance with the relevant provisions of the FIC Act. During the same period, Capitec Bank Limited (Capitec) notified the Bank of instances of non-compliance relating to the cash-threshold reporting requirements as set out in the FIC Act.

Based on the available facts and findings of the inspection, the Department imposed administrative sanctions in terms of the FIC Act with a combined value of R15 million on Deutsche Bank and Capitec during 2015. In addition, the banks were directed to take remedial action to address the identified deficiencies. Table 1.4 provides a breakdown of the administrative sanctions imposed.

Table 1.4 Penalities imposed on banks in 2015

Bank	Non-compliance	Administrative sanction
Deutsche Bank	· Identifying and verifying customer details (known as "Know-Your-Customer"); and	Financial penalty: R10 million
	· Controls and systems relating to the detection of property associated with terrorism and related activities.	Directive: To take remedial action to address identified deficiencies
Capitec	· Failure to report cash-threshold transactions above R24 999,99 to the Financial Intelligence Centre.	Financial penalty: R5 million
		Directive: To take remedial action to address identified deficiencies

It should be noted that the decision to impose administrative sanctions was not based on any evidence that Deutsche Bank or Capitec facilitated transactions relating to money laundering and/or the financing of terrorism activities.

1.4.4 Illegal deposit-taking

The Banks Act mandates the Registrar to control certain activities of persons who are not registered as a bank or authorised to carry on the business of a bank.

During the year under review the Department received a number of enquiries and complaints, with supporting documentary evidence, pertaining to the business activities of certain person/s and/or entity/ies that were suspected of accepting deposits from the general public as a regular feature of their business without being registered as a bank.

In fulfilling its mandate, it should be noted that the Department's involvement is limited to potential contraventions of the Banks Act in the Republic of South Africa and does not extend to fraud or other related white-collar crimes. Such matters are referred to the relevant regulator. The Department is not a prosecuting authority, but can only report the alleged contravention to the South African Police Service and National Prosecuting Authority for criminal investigation and prosecution.

Generally, illegal schemes are only reported by investors when they fail to receive their promised returns. This typically occurs when the funds have already been depleted and the scheme is on the brink of collapse. As such, the prospects of recovering funds for repayment to investors are limited. However, it is encouraging to note that in the period under review, there has been a shift towards proactive notification and intervention, which has resulted in securing accounts prior to the dissipation of funds. In addition, the process of effecting repayment in one of the large schemes commenced, with the first dividend having being paid in November 2015.

The Department, however, remains concerned about the prevalence of illegal schemes in the country and the apparent willingness of individuals to participate in such ventures. Members of the general public are again cautioned to exercise vigilance and prudence in their investment choices.

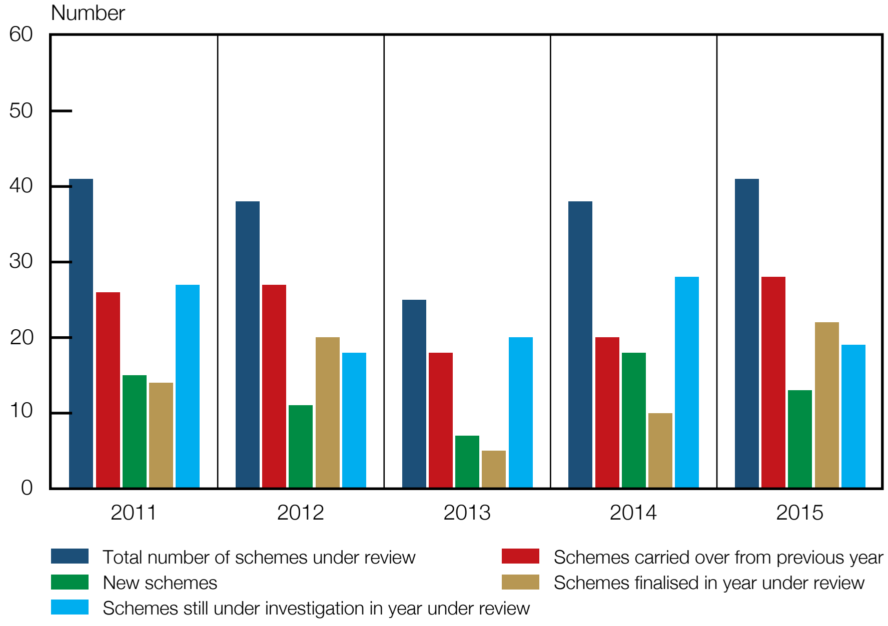
The Department has compiled a five-year review of schemes investigated from January 2011 to December 2015 (refer to Table 1.5 and Figure 1.2). During this period, the Department appointed temporary inspectors and in some cases repayment administrators for 64 cases relating to illegal deposit-taking schemes. A total of 71 schemes were finalised during the above-mentioned five years. In 2015 the Department investigated 41 schemes, consisting of 28 schemes which were carried over from previous years and 13 new schemes in 2015. On 31 December 2015, a total of 19 schemes were still active, after the finalisation of 22 schemes during the year under review.

Table 1.5 Inspections relating to illegal deposit-taking schemes

Year	Total number of schemes under review*	Schemes carried over from previous years	New schemes in year under review	Schemes finalised in year under review	Schemes still under investigation in year under review
2011..................	41	26	15	14	27
2012..................	38	27	11	20	18
2013..................	25	18	7	5	20
2014..................	38	20	18	10	28
2015..................	41	28	13	22	19

* Includes schemes carried over from previous years

Figure 1.2 Inspections relating to illegal deposit-taking schemes



1.5 Regulatory Consistency Assessment Programme South Africa

The Basel Committee places significant emphasis on the implementation of regulatory standards underpinning the Basel III framework and more so the consistent implementation of these standards by all member jurisdictions, within the internationally agreed timeframes. The RCAP was therefore established to assess members' implementation of the Basel standards (Basel II, Basel 2.5 and Basel III) as part of the Committee's post-crisis reform efforts.

As a member of the Basel Committee, South Africa was also subjected to such an RCAP assessment, which commenced during the latter part of 2014 and for which the final report was issued in June 2015. The RCAP for South Africa focused on both risk-based capital regulations and Basel III LCR standards. The assessments were performed by teams of experienced international banking supervisory peers. It provided valuable insight into the Department's policies and processes, confirmed areas of strength and identified areas that required further development or refinement.

To ultimately eliminate all material inconsistencies, the Department enhanced South Africa's regulatory framework by implementing amendments required by the assessment team, as explained in further detail in section 3.3 of this report.

Following the implementation of the aforesaid amendments, the RCAP assessment team found the local implementation of the risk-based capital regulations to be 'compliant' with the Basel standards as all 14 components were assessed as 'compliant'.[11] South Africa's prudential regulations were also assessed and reported as 'compliant' with the Basel III standards on LCR and the LCR disclosure standards.[12]

This was a significant achievement for the Department since South Africa was the first country to achieve an overall 'compliant' assessment in respect of risk-based capital regulations and the Basel III standards on LCR and the LCR disclosure standards at the time.

11. The full report is available at http://www.bis.org/bcbs/publ/d322.pdf

12. The full report is available at http://www.bis.org/bcbs/publ/d323.pdf

1.6 Regulatory developments affecting the domestic banking sector

1.6.1 Implementing the Twin Peaks[13] system of financial regulatory architecture in South Africa

On the domestic front, South Africa is in the throes of one of the most significant financial regulatory architectural reforms since the 1980s. In 2015, the FSR Bill, which recommends the establishment of two main regulatory peaks – the PA in the Bank and the Financial Sector Conduct Authority (FSCA) to replace the current Financial Services Board (FSB) – was tabled in Parliament.

The key philosophical underpinning of the Twin Peaks framework is the so-called 'regulation by objective approach', which argues that given the different (although complementary) set of key objectives for regulation, that is, institutional soundness (or prudence/solvency) and conduct of business (or consumer protection), the institutional arrangements to deliver on these two sets of objectives should be separate and streamlined, built on a different set of skills and expertise.

A common set of principles will anchor and serve as the foundation of both the PA and the FSCA. These principles, which are elaborated on in the policy document *A safer financial sector to serve South Africa better* (published by National Treasury in 2011),[14] emphasise that the regulatory and the supervisory frameworks of the Twin Peaks system will aim to be:

- appropriate, intensive and intrusive;
- outcomes-focused;
- risk-based; and
- aligned with applicable international standards.

The establishment of the PA will see the consolidation of prudential regulation and supervision of financial conglomerates, banks, insurers and financial market infrastructures (FMIs) in the Bank. The two-key approach, which will require licensing by both regulators where an entity is to be supervised by both, is critical to the operationalisation of the Twin Peaks model.

Preparations by the Bank for the operationalisation of the PA are ongoing and a communication strategy will be rolled out to apprise all relevant stakeholders on the meaning and impact of expected changes. It is envisaged that the PA will be established once the FSR Bill has been approved by Parliament and promulgated as an Act of Parliament.

13. The Twin Peaks system recognises the different skill sets required for prudential and market conduct regulation. Prudential regulation is designed to maintain safety, soundness and solvency of financial institutions or funds, while market conduct regulation requires the perspective of a customer, which is a different regulatory perspective and philosophy.

14. Available at http://www.treasury.gov.za/documents/national%20budget/2011/A%20safer%20financial%20sector%20to%20serve%20South%20Africa%20better.pdf

1.6.2 Developing an effective resolution framework for key financial institutions

Through the introduction of the Financial Stability Board's *Key Attributes for Effective Resolution Regimes for Financial Institutions* (key attributes)[15] global systemically important banks (G-SIBs) are now subject to more robust resolution requirements and additional regulatory minimum capital requirements.

These reforms seek to minimise the public costs of financial crises, in particular those emanating from the failure of financial institutions perceived as too big to fail. In order to progress in this area of work domestically, in 2015, the Bank jointly with National Treasury and FSB published a Resolution Framework Policy paper (Resolution paper) which clearly outlines the approach to the implementation of the key attributes and which will lead to the drafting of a Resolution Bill for banks and other systemically important financial institutions.

The Resolution paper also outlines the role of the Bank as the Resolution Authority. Importantly, the Resolution paper also introduces the possibility of a depositor guarantee scheme, in line with South Africa's commitment as a member of the Financial Stability Board to establish a robust framework for the resolution of systemically important financial institutions and market infrastructures, with adequate safety nets for financial customers. A public consultation process on the Resolution paper is currently underway.

15. Available at http://www.financialstabilityboard.org/wp-content/uploads/r_111104cc.pdf?page_moved=1

1.7 Key international developments, recommendations and focus areas

South Africa is committed to the development of an effective global financial regulatory architecture. In this regard, the Bank is an active member and participates in relevant and strategic international forums including the Group of Twenty (G-20) and the Financial Stability Board. As such, influencing the global financial reform-agenda has been an integral part of the work of the Bank. Since the commencement of the global financial crisis in 2007 the international financial reform-agenda has mainly focused on the development of adequate responses to the causes and effects of the crisis.

Given this global financial reform-agenda, this work has significantly informed the focus of the Basel Committee, which the Department is a member of. The Department subscribes to the full, timely and consistent implementation of internationally agreed reforms. This is done in a way that acknowledges and takes into account domestic economic and financial system conditions.

The core elements of the G-20's comprehensive programme of reforms comprised the following:

- building a more resilient financial system;
- ending the 'too big to fail' conundrum;
- making derivative markets safer; and
- transforming shadow banking into more resilient market-based finance.

In the main, these reforms include requirements to ensure that banks build higher and better quality levels of capital which should result in a fundamental re-appraisal of banks' exposures to various types of on-balance-sheet and off-balance-sheet risks. Reforms also entailed the introduction of new liquidity requirements – the LCR and the net stable funding ratio (NSFR). These requirements promote banks' resilience to both short-term and longer-term liquidity stresses and also aim to reduce the over-reliance of the banking system on volatile short-term wholesale funding.

16. The key matters communicated by the Basel Committee in respect of these documents and requirements are summarised in Appendix 10.

In addition, the Basel Committee issued a number of documents in 2015,[16] which have a significant impact on the regulation and supervision of banks and banking groups. The relevant requirements will be incorporated into the regulatory framework, over the next few years, in accordance with the internationally agreed timelines. The following list highlights some of these documents:

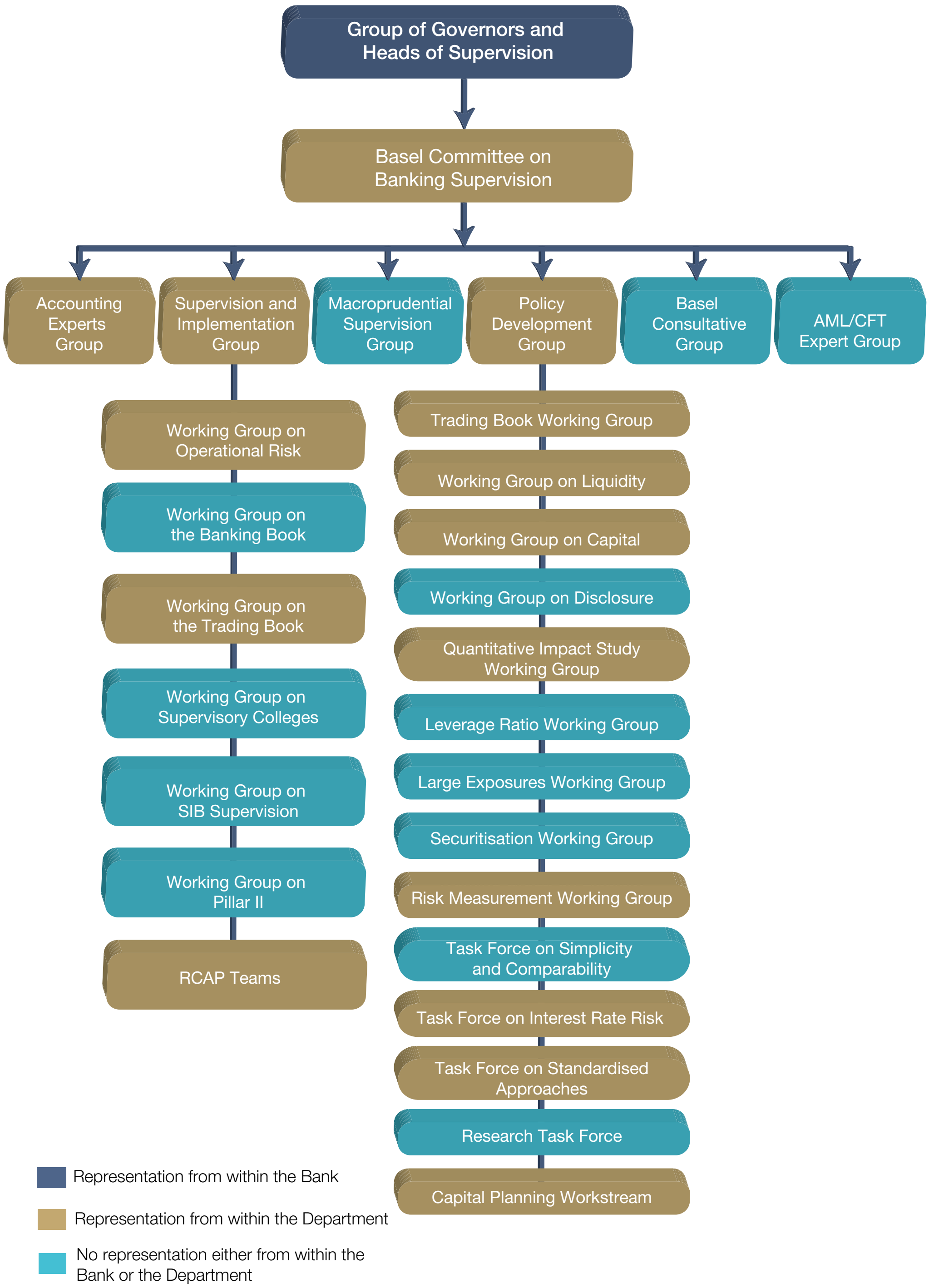
- revised Pillar 3 disclosure requirements, issued on 28 January 2015;
- revisions to the implementation of margin requirements for non-centrally cleared derivatives issued jointly by the Basel Committee and the International Organization of Securities Commissions (IOSCO), on 18 March 2015;
- removal of selected national discretions and reply to a frequently asked question on funding valuation adjustment, issued on 21 April 2015;
- final NSFR disclosure requirements, issued on 22 June 2015;
- frequently asked questions on the Basel III leverage ratio framework, issued on 7 July 2015;
- revised principles on corporate governance for banks, issued on 8 July 2015;
- guidelines for identifying and dealing with weak banks, issued on 16 July 2015;
- final criteria for identifying 'simple, transparent and comparable' securitisations issued by the Basel Committee and IOSCO on 23 July 2015;
- Basel III: the standardised approach for measuring counterparty credit risk (CCR) exposures: Frequently asked questions, issued on 19 August 2015;
- report on the regulatory consistency of risk-weighted assets for CCR, issued on 1 October 2015;
- supporting information for the implementation of the countercyclical capital buffer, issued on 19 October 2015;
- information on G-SIBs, issued on 3 November 2015;

- reports related to Total Loss Absorbing Capacity (TLAC), issued on 9 November 2015; and
- guidance on credit risk and accounting for expected losses, issued on 18 December 2015.

1.8 Participation in international regulatory and supervisory forums

The Department participated in a number of international regulatory and supervisory forums. Participation in those forums that form part of the Basel Committee structures is described in sections 1.8.1 to 1.8.15. Participation in other forums is set out in sections 1.8.16 to 1.8.18.

Figure 1.3 Department's participation in the structures of the Basel Committee on Banking Supervision



1.8.1 Basel Committee on Banking Supervision

The Department represents South Africa on the Basel Committee and on several of its subcommittees. Representation is aimed at influencing the formulation of global regulatory standards so that the distinct financial and social environment South African institutions are exposed to be recognised in the rules which the Department expects South African banks to adhere to.

1.8.2 Accounting Experts Group

The Accounting Experts Group (AEG), which is a subcommittee of the Basel Committee and is chaired by the Registrar, takes an active role in the development of international accounting and auditing standards by standard-setting bodies such as the International Accounting Standards Board (IASB). The aim of the subcommittee is to ensure that these standards and practices promote sound risk management at banks, support market discipline through transparency and reinforce the safety and soundness of the banking system. The AEG also develops prudential reporting guidance where necessary.

The audit subgroup of the AEG promotes reliable financial information by exploring key audit issues from a banking supervision perspective. International auditing standard-setting developments come under its attention, as well as any other documents emanating from the International Auditing and Assurance Standards Board, the International Ethics Standards Board for Accountants and audit quality issues.

During 2015, the AEG continued its close monitoring of developments relating to accounting standards for forward-looking expected credit losses (ECL) by both the IASB and the Federal Accounting Standards Board. In December 2015, the Basel Committee issued the guidance on credit risk and accounting for expected losses. This document sets out guidelines on accounting for ECL regardless of the applicable accounting standards. As a member of the Basel Committee, the Bank adopted this guidance which strives to ensure a high-quality, robust and consistent implementation of ECL accounting frameworks by banks without unduly increasing cost and complexity.

1.8.3 Supervision and Implementation Group

The Supervision and Implementation Group (SIG) is the peer review committee of the Basel Committee. Its mandate is to help foster financial stability by supporting strong national and international supervision and regulation of banks. It has two primary objectives, firstly to foster the timely, consistent and effective implementation of the Basel Committee's standards and guidelines, and secondly, to advance improvements in practices in banking supervision, particularly across Basel Committee member countries.

The results of the level 2 RCAP studies commissioned by the Basel Committee are discussed at the SIG's meetings prior to publication.

The Basel Committee work programme identified four themes for 2015, namely:

- policy development;
- ensuring an adequate balance between simplicity and risk sensitivity across the regulatory framework;
- monitoring and assessing implementation of the Basel framework; and
- improving the effectiveness of supervision.

1.8.4 Working Group on Operational Risk

The Working Group on Operational Risk (WGOR) is a permanent working group that addresses operational risk policy and implementation issues. It reports to both the SIG and the Policy Development Group (PDG).

The WGOR develops policies and considers the practical challenges relating to the successful development, implementation and maintenance of operational risk.

Focus areas for 2015 were:

- developing a simple standardised measure of operational risk (Standardised Measurement Approach) to replace the existing simpler approaches;
- finalising and publishing a consultative document in relation to the aforementioned revision;
- drafting an amended version of the Principles for the Sound Management of Operational Risk to be considered for consultation in the near future; and
- considering the proposed withdrawal of internal modelling approaches for operational risk from the Basel framework.

South Africa was represented at all meetings and further participated in various sub-working groups.

1.8.5 Working group on the Trading Book

The Supervision and Implementation Group - Trading Book Subgroup (SIG-TB) is a work stream under the SIG established in 2012 to analyse reasons for differences in risk-weighted assets (RWA) in the trading book across different jurisdictions. This analysis is part of a wider RCAP initiated by the Basel Committee in 2012.

During the period under review, the SIG-TB extended its analysis to include CCR models. The exercise was the first to study variability of CCR models and included the remaining aspects of RWA variability of internal models for trading book assets. The work of the SIG-TB culminated in the *Regulatory Consistency Assessment Programme* (RCAP) - *Analysis of risk-weighted assets for counterparty credit risk*[17] report which was published by the Basel Committee in October 2015. The report presents a number of policy recommendations for consideration by the Basel Committee to reduce excessive variability in outcomes across banks, further harmonise supervisory practices and reduce the complexity of the CCR framework. The report includes observed sound practices in the modelling of CCR that can assist banks and supervisors to implement and supervise these models. The report could be particularly useful for supervisors that oversee banks that apply the internal model method (IMM) and advanced credit valuation adjustment (CVA) models.

17. Available at http://www.bis.org/bcbs/publ/d337.pdf

The SIG-TB was mandated to continue work on the possible divergences in practices across banks regarding the proxy spread methodologies used for the Basel III advanced CVA capital charge. In addition, the SIG-TB will be investigating the modelling choices employed by banks in an environment of low interest rates. This study builds on previous exercises conducted by the SIG-TB in prior years and the aim of the study includes:

- identification of drivers of counterparty exposure variability related to interest rate modelling within the IMM framework, focusing on the modelling choices made by banks in a low interest rates environment and potential risks when interest rates increase; and
- assessment of the integrity of banks' underlying pricing models, sensitivities for traded interest rate products, and the identification of the degree, nature and drivers of variation.

1.8.6 Regulatory Consistency Assessment Programme teams

As discussed in section 1.5 of this report, the Basel Committee adopted the RCAP to assess its members' implementation of the relevant internationally agreed standards. The RCAP is administered with the support of specialist contributors drawn from the Basel Committee's membership group.

Assessments are conducted at various levels, including risk-specific themes. During assessments, a team of specialists reviews information submitted by a specific jurisdiction's banking authority, clarifies statements made and requests supportive information or data to ascertain the materiality of deviations before conducting further review work on the premises of the relevant banking authority. Discussions with banks form an integral part of the jurisdictional assessment. Following the finalisation of the assessment team's report, a review team independently examines the findings before a review panel concludes the assessment, where after the draft reports are submitted to the Basel Committee for approval before the results are published.

Specialists in the Department have also been selected to lead or support the work of the assessment teams in other jurisdictions and are also members of review teams. Jurisdictions whose assessments the Department's staff contributed to include India, the United States, Mexico, Saudi Arabia, Russia, Indonesia and South Korea.

1.8.7 Policy Development Group

The PDG assesses proposed changes to banking regulations developed by its subgroups and other work streams of the Basel Committee. The group serves the Basel Committee by identifying issues, commissioning research, overseeing quantitative analysis and making recommendations on policy to the Basel Committee. It also reviews emerging supervisory issues aimed at promoting a sound banking system and high supervisory standards. The PDG has several executive subgroups and workgroups reporting to it on a wide range of risk and capital issues. The Department is represented on the PDG and many of the subgroups where the subject matters are relevant to South Africa.

1.8.8 Trading Book Group

The Trading Book Group (TBG) is a working group of the PDG, a subcommittee of the Basel Committee. It was established in 2005 to deal with market risk in its various forms, including the trading book. South Africa has been a member of the TBG since 2007.

The global financial crisis that started in 2007 exposed significant flaws in the regulatory capital approach to market risk and trading activities at the time. While some of the issues have been addressed in the revisions to the market risk capital framework that was released in July 2009, the Basel Committee agreed that a fundamental review of the framework was required, in particular of whether or not the distinction between the banking and trading books should be maintained, how trading activities are defined, and how risks in the trading books (and possibly market risk more generally) are captured by regulatory capital. It is in this regard that the TBG embarked on what came to be known as the fundamental review of the trading book (FRTB).

18. Available at http://www.bis.org/bcbs/publ/d352.pdf

The FRTB has been concluded with the final market risk text published in January 2016.[18] The revised market risk framework will come into effect on 1 January 2019. The FRTB focused on developing regulatory practices in the following areas in market risk management:

- A revised internal model-based approach (IMA): the new approach comprises a more rigorous model approval process, more consistent identification and capitalisation of material risk factors across banks, and introduces constraints on the capital-reducing effects of hedging and diversification.
- A revised standardised approach for market risk: an enhanced approach that is sufficiently risk sensitive to act as a credible fall-back and floor for the IMA, while still being appropriate for banks that do not require a sophisticated treatment for market risk.
- The shift from value at risk (VaR) to an expected shortfall (ES) measure of risk: this will help to ensure a more prudent capture of 'tail risk' and capital adequacy during periods of significant financial market distress.
- Incorporating the risk of market illiquidity: varying liquidity horizons are incorporated into the revised standardised approach for market risk and IMA to mitigate the risk of sudden and severe impairment of market liquidity across asset markets. This replaces the static 10-day horizon assumed for all traded instruments in the current framework.

- A revised boundary between the trading book and banking book: a more objective boundary that reduces the potential for arbitrage between the two regulatory books, while still being aligned with banks' risk management practices. This includes a careful calibration of credit risk for non-securitisation and securitisation exposures in the trading book.

1.8.9 Working Group on Liquidity

The primary focus of the Working Group on Liquidity (WGL) is policy development. The WGL also deals with the practical challenges accompanying the successful development, implementation and maintenance of a liquidity risk framework that addresses the requirements and expectations of the Basel Committee's regulatory requirements relating to liquidity and funding.

The WGL developed, over several years, appropriate standards for measuring and mitigating liquidity risks in banks. Currently, the WGL deals with the two main standards relating to liquidity and funding, namely the LCR and NSFR.

With the finalisation of the LCR and NSFR standard, and the LCR becoming a prudential requirement from 1 January 2015, the focus of the WGL has shifted towards refining the broad understanding of the rules and their implementation by dealing with frequently asked questions on the two standards and dealing with post-implementation issues of the LCR.

1.8.10 Working Group on Capital

The Working Group on Capital (WGC) was established early in 2013 by merging two groups that dealt with issues related to capital: the Definition of Capital Subgroup and the Contingent Capital Working Group. The WGC is responsible for handling all policy issues associated with the definition of capital and capital-like instruments under Basel III.

During 2015 the WGC formulated, in conjunction with the Financial Stability Board, the minimum eligibility criteria for TLAC instruments. The Financial Stability Board published the *Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution*: *Total Loss-Absorbing Capacity (TLAC) Term Sheet*[19] during November 2015.

19. Available at http://www.fsb.org/2015/11/total-loss-absorbing-capacity-tlac-principles-and-term-sheet/

The objective of the minimum TLAC requirements is to reduce the probability and the impact of the failure of global systemically important financial institutions (G-SIFIs). However, for regulators to ensure G-SIFIs are no longer 'too-big-to-fail' and would not expose public funds to a loss, such G-SIFIs should have sufficient loss-absorbing and recapitalisation capacity necessary to ensure that during or immediately after the resolution, the critical functions can be continued without public funds or financial stability being put at risk.

The WGC published a *Consultative document on TLAC Holdings* during November 2015.[20] This consultative document sets out proposals to reduce the risk of contagion and proposals on the treatment of investments in TLAC.

20. Available at http://www.bis.org/bcbs/publ/d342.pdf

1.8.11 Quantitative Impact Study Working Group

The biannual international Basel III implementation monitoring by the Basel Committee continued during 2015 in the form of quantitative impact studies (QIS).

As a result of the implementation of Basel III in member countries, the focus of the quantitative analyses produced by the PDG working groups (i.e. the Capital Monitoring Group (CMG) and the QIS working group) shifted towards monitoring of Basel III implementation. As a result, the QIS working group merged with the CMG. The combined group will, in particular, remain responsible for the design of the capital monitoring reporting templates and the analysis of bank-level parameters (e.g. capital and risk-weighted exposures).

In addition to Basel III implementation monitoring, the focus of the 2015 QIS exercise was on collecting data for the assessment of policy initiatives. These included the impact of proposals on the fundamental review of the trading book, CVA risk, the operational risk measurement framework, large exposures, sovereign exposures and interest rate risk in the banking book. Future exercises will expand to also include the impact assessment of provisioning and step-in risk.

The Basel Committee published the *Basel III Monitoring Report*[21] during September 2015 and the *Fundamental review of the trading book - interim impact analysis*[22] and the *TLAC Quantitative Impact Study Report*[23] during November 2015. These documents detail the results of the QIS exercise as at 31 December 2014. The reports incorporated the data of the South African participating banking groups. Furthermore, it is the intent of the Basel Committee to continue publishing the results of the Basel III monitoring exercise.

21. Available at http://www.bis.org/bcbs/publ/d334.pdf

22. Available at http://www.bis.org/bcbs/publ/d346.pdf

23. Available at http://www.bis.org/bcbs/publ/d334.pdf

Both the Department and the participating banks continued to benefit from participating in these studies and will continue to actively participate.

Following the merger of the CMG with the QIS working group, the Department continued with the submission of specific data obtained from the Supervisory Reporting System, to enhance the analysis and monitoring of capital and credit related data. The combined group will in particular remain responsible for the design of the capital monitoring reporting templates and the analysis of bank-level parameters, for example, capital requirements, eligible capital and capital ratios.

1.8.12 Risk Measurement Working Group

During 2015 the Department joined the Risk Measurement Working Group (RMG), a working group that reports directly to the PDG. The RMG deals with advanced risk measurement and management practices that are used for regulatory purposes. One of the RMG's main tasks is to develop possible modifications to the framework for the internal ratings-based (IRB) approach, to narrow the modelling choices available to banks, particularly in areas for which the use of models may not be suitable for calculating regulatory capital.

1.8.13 Task Force on Interest Rate Risk

Proceeding from work carried out under the FRTB by the TBG, the Basel Committee, under the PDG, created a Task Force on Interest Rate Risk (TFIR) to examine options for capturing interest rate risk and credit spread risk in the banking book within the capital framework. The aim was to consider an obligatory charge (so-called Pillar 1 charge) for interest rate risk associated with exposures in the banking book. Exposures in the trading book already carry a capital charge for interest rate risk in terms of the market risk rule set. Currently the framework does not require banks to hold capital for this risk in the banking book unless the supervisor, in terms of a Pillar 2 assessment, has determined it to be necessary.

During 2015 the TFIR released a consultation paper based on both a Pillar 1 and Pillar 2 option for these risk types. A QIS exercise was also conducted during 2015 on the potential capital impact of a Pillar 1 option on banks globally. Comments received on the consultation paper together with results of the QIS exercise will be taken into consideration in the development of the final rules for these risk types. It is expected that the final rules will be published during 2016.

1.8.14 Task Force on Standardised Approaches

In response to issues arising from the global financial crisis, the Basel Committee established, in 2013, the Task Force on Standardised Approaches (TFSA) with the primary mandate to propose revisions to the standardised approach for credit risk. Apart from ensuring that the standardised approach continues to provide a suitable regulatory capital framework for banks using this approach, the revision also aims to reduce the mechanistic reliance placed by the approach on external credit ratings and introduce supplementary measures for risk classification. The revision will also seek to strengthen the link between the standardised approach and the IRB approach.

Towards the end of 2015 the TFSA issued two consultative papers for public comments. A QIS exercise, to assess the likely impact on risk-weighted assets, is planned for the first quarter of 2016. Finalisation of the rules is expected by December 2016.

1.8.15 Anti-money Laundering and Combating the Financing of Terrorism Expert Group

The Basel Committee's AML/CFT Expert Group assists both financial institutions and regulators to implement AML/CFT elements of the Core Principles for Effective Banking Supervision (Core Principles) in accordance with the Financial Action Task Force (FATF) standards by producing technical and practical guidance that is applicable to national and international banks and banking groups. The group also contributes to the standards set by the FATF relating to AML/CFT matters.

The Department participated in the revision of the *General guide to account opening and customer identification*, first issued in 2003. This revised guide takes into account significant enhancements to the FATF Recommendations and related guidance. It builds in particular on the February 2012 version of the FATF Recommendations as well as on two supplementary FATF publications relevant for this guide: *the Guidance for a risk-based approach for the banking sector and the Transparency and beneficial ownership*, both issued in October 2014.

1.8.16 Eastern and Southern Africa Anti-Money Laundering Group

The Department attended the 15th Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) Council of Ministers meeting and the 30th Task Force of Senior Officials meeting which was held in Johannesburg, South Africa, from 23 to 27 August 2015.[24]

During these meetings South Africa was appointed to take over the presidency of the ESAAMLG for the year 2015/2016. A representative of the Department was also appointed to be a Reviewer of ESAAMLG's Post Evaluation Implementation Process.

24. As at August 2015 the members of ESAAMLG were South Africa, Angola, Botswana, Ethiopia, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe.

1.8.17 Financial Action Task Force meetings

The FATF is an inter-governmental body that has developed the international standard for combating money laundering and the financing of terrorism.

The Department was represented at all three FATF plenary meetings held in 2015, and also participated in working group discussions and policy development. Some matters of importance that are relevant for the banking sector, where the Department made contributions to the FATF include:

- guidance on the risk-based approach for effective supervision and enforcement by AML/CFT supervisors of the financial sector and law enforcement;
- emerging terrorism financing risks;
- a FATF report on terrorism financing control measures compiled for G-20 leaders;
- a series of public statements to correspondent banks urging caution against the phenomenon of de-risking on the basis of compliance with the FATF recommendations; and
- guidance for a risk-based approach to virtual currencies.

1.8.18 Community of African Bank Supervisors of the Association of African Central Banks

The Community of African Bank Supervisors (CABS) is a committee of the Bureau of the Association of African Central Banks (AACB) Governors. A work plan was established during 2014 by the CABS working committee resulting in the Bank being elected to lead a working group on cross-border banking supervision, which is one of the two working groups to be established.

The purpose of the cross-border banking supervision working group is to:

- effectively contribute to the formulation of sufficient methods to improve cross-border supervision on the African continent;
- improve the quality of data available to banking supervisors; and
- be the preferred platform where experiences are shared and ideas are discussed in order to promote the strengthening of effective supervision of cross-border banking operations.

The inaugural cross-border banking supervision working group meeting was held on 18 May 2015 and was attended by a number of AACB member countries. Further working groups will be held during the course of 2016.

1.9 Participation in international surveys

During the year under review, the Department participated in numerous international surveys, as indicated in sections 1.9.1 to 1.9.3 below.

1.9.1 African Development Bank survey on the financial sector in Africa

The Department participated in the second edition of the African Development Bank (AfDB) survey on the financial sector in Africa. The purpose of the survey was to obtain an overview of the financial infrastructure and regulatory framework of the financial sector. The first part of the questionnaire explored various aspects, including the regulatory framework, regulations on ownership, competition, restrictions or guidelines on lending, liquidity and diversification, and accounting and auditing standards. The second part of the questionnaire focused mainly on issues pertaining to financial structure, access to banking services, assets of financial institutions, deposits collected by financial institutions, lending activities of financial institutions and market share of the largest banks.

1.9.2 African Development Bank survey on understanding the trade finance landscape in Africa

The AfDB undertook a second survey on the trade finance landscape in Africa. The purpose of the survey was to build on the knowledge gained from the first survey and improve the design of the AfDB's Trade Finance Programme and align it with the needs of financial institutions in Africa.

1.9.3 Bank for International Settlements questionnaire on changing patterns of financial intermediation

The Bank for International Settlements conducted a survey on the changing patterns of financial intermediation and the associated implications for central banks. The purpose of the survey was to ascertain how the changes in financial intermediation have affected the transmission mechanism of monetary policy and its sensitivity to global monetary shocks in emerging-market economies. The questionnaire also sought to determine the potential influence that macro-prudential policy might have on the transmission mechanism of monetary policy.

1.10 Participation in domestic regulatory and supervisory forums

During the year under review the Department continued to serve on, and participate in numerous domestic committees, forums, task groups and working groups to consult with banking industry participants and bodies, external audit bodies, government departments and other financial regulatory authorities on relevant matters.

These bodies include National Treasury, the Banking Association of South Africa (BASA), the South African Institute for Chartered Accountants (SAICA), the Committee for Audit Standards, the FSB, the National Credit Regulator (NCR), the FIC and the Independent Regulatory Board for Auditors (IRBA).

Some of the forums and initiatives which the Department participated in during 2015 are highlighted below:

- The FIC together with National Treasury drafted amendments to the current FIC Act in order to transform the money laundering control regime in South Africa toward a more risk-based approach, in line with FATF standards. The Department provided comprehensive commentary to the FIC Amendment Bill and participated in a series of discussions with key stakeholders on the proposed provisions of the Bill and its impact on the banking industry;
- As discussed in section 1.6.2 of this report, the Bank, jointly with National Treasury and the FSB, published a Resolution paper;
- The International Financial Reporting Standards 9 (IFRS 9) Implementation Working Group was formed in June 2015, comprising representatives from the Department, the banks, audit firms and other regulatory or industry bodies such as IRBA and SAICA, as discussed in section 2.2.2 of this report; and
- The emergence of conduct risk led the FSB and the Bank to jointly produce the foreign exchange review report and a draft code of conduct for the South African over the counter (OTC) markets as outlined in section 2.4.4 of this report.

1.11 Regional cooperation and interaction

1.11.1 ESAAMLG: mutual evaluation of the Republic of Uganda

The ESAAMLG conducts peer reviews of each member on an ongoing basis to assess levels of implementation of the FATF Recommendations, providing in-depth description and analysis of each country's system for preventing criminal abuse of the financial system.

The Department was nominated to take part in the ESAAMLG 2nd round of AML/CFT mutual evaluation of the Republic of Uganda, which started in the beginning of 2015.

The Department shares its expertise with AML/CFT supervisors in countries where South African banks have operations, by providing technical assistance and training in a wide range of AML/CFT supervisory areas.

In 2015 the Department was also part of a mission to the Kingdom of Swaziland to provide technical assistance to the financial sector regulators.

1.12 Issues to receive particular attention during 2016

The Department intends to continually review, amend and update the regulatory and legislative framework in accordance with the latest internationally agreed regulatory and supervisory practices and standards.

Other areas that will receive particular attention during 2016 include the:

- ongoing implementation of the PA in terms of the Twin Peaks model of financial regulation;
- continued monitoring of the banking sector's capital adequacy and compliance with the Regulations thereto;
- continued focus on internal capital adequacy assessment processes (ICAAPs) and in particular economic capital modelling, stress testing and capital planning;
- assessment of the implementation readiness of both banks and external auditors of banks relating to the IASB's IFRS 9 on accounting for ECL;
- continued focus on banks' abilities to mitigate and respond to risks arising from information security, including cyber security;
- continued focus by the Department in conjunction with the industry in search of a viable clearing solution for OTC derivatives;
- ongoing periodic assessment of the impact on the banking sector of a possible change of the South African sovereign credit rating to sub-investment grade;
- monitoring of the banking industry's readiness to implement and comply with the NSFR as of 1 January 2018;
- introduction of a risk-based approach framework and an AML/CFT self-assessment questionnaire, which will have to be completed by all banks and mutual banks on an annual basis; and
- thematic reviews to assess the progress made by banks in improving the configuration of their sanctions-screening systems after the review that was conducted in 2014.

1.13 Expression of gratitude

I would like to express my appreciation to the Ministry of Finance, for the input on the Department's requests in terms of statutory requirements. To the Governor and Deputy Governors of the Bank: thank you for your ongoing cooperation, guidance and support during 2015.

My sincere appreciation also goes to the staff members of the Department for their continued efforts and willingness to repeatedly go beyond the call of duty to meet the challenges and demands of an ever-changing supervisory and regulatory landscape.

René van Wyk
Registrar of Banks

Chapter 2: Overview of supervisory activities

2.1 Introduction

The Department monitors banks' compliance with the regulatory framework and specifically prudential requirements, as part of its risk-based supervisory approach. Understanding banks' risk profiles, their business models and the environment in which they operate is paramount to effective risk-based supervision by the Department. To this end the Department follows a structured, forward-looking supervisory review and evaluation process (SREP) that incorporates on- and off-site supervision, as well as quantitative and qualitative supervisory tools.

The SREP is designed to:

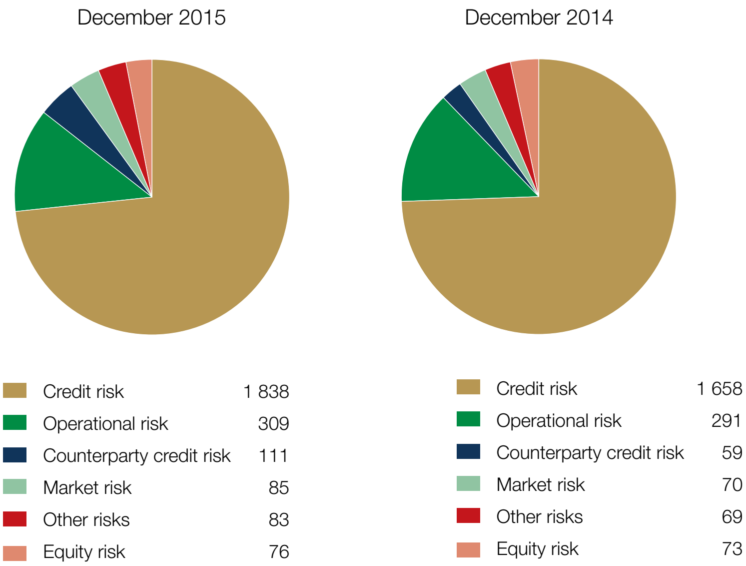
- identify key risk factors and the build-up of risks which could impact individual banks and the banking sector as a whole;
- assess the risk management policies, processes, practices and structures that are used to mitigate risks; and
- deploy resources accordingly to address the most critical risk areas and intervene early where required.

This chapter provides an overview of the operations of the Department during the period under review at an industry level and according to aspects of bank supervision that are common across banks. These operations include work undertaken with respect to thematic topics, risk-based reviews, consolidated supervision, and disclosure assessments.

Figure 2.1 gives an indication of the aggregated risk profile of the banking sector as at 31 December 2014 and 31 December 2015, reflecting Pillar 1 risks that are quantifiable in terms of the Regulations and for which the sector is required to hold regulatory capital. The banking sector is also exposed to other risks that are not quantified in terms of regulatory capital requirements, such as liquidity risk and interest rate risk in the banking book that are monitored specifically through the application of the Department's SREP and assessed under Pillar 2 supervisory activities.

Figure 2.1 Composition of risk-weighted exposure

(R billions)



2.2 Thematic topics for 2015

2.2.1 Introduction

25. Available at http://www.resbank.co.za/Publications/Pages/BanksActGuidance.aspx.

The Department identifies certain themes (or flavour-of-the-year topics) to be discussed with banks' Boards annually as part of its ongoing supervisory interventions. Guidance Note 2 of 2015[25] identified the following two topics for 2015:

- IFRS 9; and
- shadow banking.

Banks' Boards were requested to make presentations and engage with the Department on each topic. A review of the Department's interactions related to these topics is detailed in sections 2.2.2 and 2.2.3.

2.2.2 IFRS 9

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments, which will replace International Accounting Standard 39 (IAS 39). The most significant change in the standard was the change from an incurred loss impairment model to an expected loss impairment model. Effective from 1 January 2018, entities applying IFRS will have to account for loan loss impairments on the expected loss model.

In light of this development and to ensure that banks are on track to implement the standard by the effective date, the Department included IFRS 9 as a flavour-of-the-year discussion topic for meetings with the Boards of directors of banks and executive committees of local branches of international banks (collectively referred to as Boards). The discussions were positioned to gain insight into the processes that banks have embarked on and to instigate banks to gear up for the implementation of IFRS 9 by the due date, which is the reporting period that commences in 2018. The Department also needs to review the impact this new standard could have on the banks' financial statements, and therefore the investors' perspective.

The Department stressed that the priority at the planning stages was to ensure that a robust implementation process was followed and that the planning was comprehensive enough to ensure that the impairment figures to be produced through these processes are accurate and reflect, as far as possible, the behaviour of the accounts and the expected future cash flows therefrom. Discussions held with Boards revealed that the majority of the banks embarked on formal initiatives for the implementation of IFRS 9, evidenced by the establishment of project teams to oversee the implementation. The project teams focused on areas such as governance, modelling requirements, accounting and credit policies, as well as data requirements. However, certain aspects had to be addressed for most banks including staff training, internal and external audit involvement, and interpretation of key terms used in the standard, for example, significant increase in credit risk.

Meetings were also held with audit firms to discuss the Department's expectations with regard to implementation readiness, including the involvement of audit firms during banks' planning and implementation stages and the impact the new standard would have on the audit firms and their audit approaches.

In addition to the aforementioned meetings held during the year, the IFRS 9 Implementation Working Group was formed in June 2015, comprising representatives from the Department, banks, audit firms and regulatory or industry bodies such as IRBA and SAICA. The working group was established in an effort to facilitate a high-quality implementation of IFRS 9 across the industry and, where possible, promote consistent application. Meetings of the working group provide a platform where industry players can deliberate on policy modelling and disclosure issues related to the IFRS 9 standard and produce a set of principles and/or guidelines that promote consistent understanding and comparability across the banking industry. Where identified, additional guidance would be issued by the regulatory bodies to assist with interpretive or policy matters that would impact the application of the standard.

During December 2015, the Basel Committee issued the final version of its *Guidance on accounting for expected credit losses*,[26] which sets out the supervisory requirements on sound credit-risk practices associated with the implementation and ongoing application of ECL provisioning frameworks. The Department expects this guidance to be incorporated by banks as part of their processes for the implementation of IFRS 9. Discussions on IFRS 9 will continue as a topic for discussion during Board meetings in 2016, with the emphasis being on progress made, the results of an impact analysis and post-implementation maintenance procedures to be adopted by banks.

26. http://www.bis.org/bcbs/publ/d350.pdf

2.2.3 Shadow banking

Increased disintermediation, both globally and within the South African financial system remains a key focus area for regulators.[27] Non-bank channels can also become a source of systemic risk, especially when structured to perform bank-like functions and where there is strong interconnectedness with the banking system.

27. Refer to the Financial Stability Board's report called 2014 *Global Shadow Banking Monitoring Report*, available at http://www.fsb.org/wp-content/uploads/r_141030.pdf.

Banks' Boards were required to engage with the Department regarding their strategic perspective on shadow banking type activities. Presentations by banks addressed the associated risks and benefits of shadow banking type activities, the extent of each bank's activities within the realm of shadow banking, future strategic initiatives and the potential impact of shadow banking activities on each bank and its business model. Banks' presentations included a discussion of recent asset and liability disposals that may have been executed in pursuit of a shadow banking objective.

From the discussions, it was evident that the majority of banks understood shadow banking market activities as well as their associated risks and benefits. However, a potential area of improvement identified by the Department was that banks' Boards could apply increased business foresight in their assessment of the potential risks and benefits arising from shadow banking type activities and the conceivable impact on their business models.

2.3 Credit risk

2.3.1 Introduction

Consumers remained constrained against the backdrop of slow employment growth, declining disposable income and rising inflation. Combined with tighter affordability criteria, following the implementation of amendments to regulations of the NCR, this resulted in subdued growth in retail credit exposure. Credit extension to the corporate sector, by contrast, has been buoyant. However, several increases in the repurchase rate of the Bank during the past 24 months require renewed focus on the sector's management of credit risk. The Department continued to monitor the impact of market conditions on South African banks' credit risk profiles and portfolios through a number of initiatives.

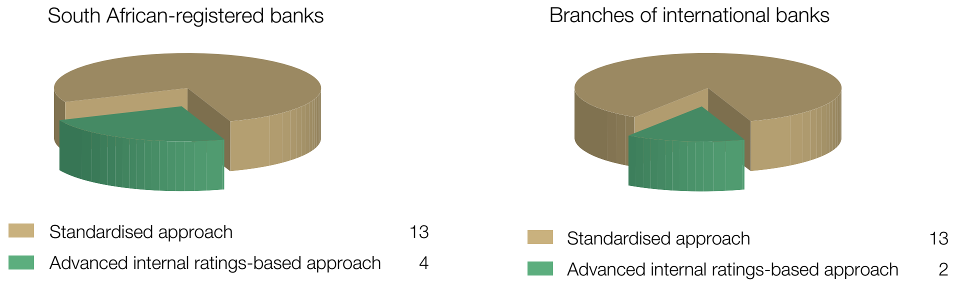
2.3.2 Methodologies to calculate minimum required regulatory capital relating to credit risk

Under the regulatory framework employed in South Africa, banks can choose from the following three methodologies to calculate their minimum required regulatory capital relating to credit risk:

1. the standardised approach (STA), including the simplified standardised approach;
2. the foundation IRB approach; and
3. the advanced IRB approach.

The number of banks using each of the aforementioned approaches is depicted in Figure 2.2.

Figure 2.2 Credit risk methodologies applied by banks as at 31 December 2015



As mentioned in Chapter 1 of this report, significant progress has been made in terms of the revision of the STA. In addition, the Basel Committee is continuing to review possible modifications to the IRB framework to narrow the modelling choices available to banks, particularly in areas for which the use of models might not be suitable for calculating regulatory capital. The Department continued to closely follow regulatory developments in this regard and to monitor any potential impact on the South African banking sector.

2.3.3 Thematic on-site reviews

During 2015 the Department's review team conducted on-site reviews of different credit portfolios, including unsecured personal loans, corporate, small and medium-sized enterprises (SMEs) and retail loans portfolios at four banks, focusing primarily on credit risk methodologies and impairment levels.

The reviews generally encompassed an assessment of the following:

- appropriateness of lending practices and adherence thereto;
- adequacy of the methodology applied in the process of determining the level of specific credit impairments, taking into account the requirements of IAS 39;
- efficiency of the credit risk methodologies or systems with regard to classification/ageing of loans and the valuation of collateral, and how such practices relate to regulation 24(5)(c) of the Regulations and the approved collections and recovery policies;
- appropriateness of write-off practices and policies, and procedures relating to the rescheduling/restructuring of loans and the correct application thereof;
- adequacy and the robustness of governance arrangements in respect of those loans in the legal, collections and recovery process; and
- risk weights assigned for the purpose of calculating regulatory capital required for the SME Corporate portfolio.

Shortcomings and areas of non-compliance were identified and discussed with the respective banks. The banks affected committed to remediate deficiencies identified during the reviews and, progress by these banks on remediating the deficiencies will be closely monitored by this Department.

2.3.4 On-site meetings relating to credit risk models

During 2015 the Department conducted on-site meetings related to credit risk models used by banks in order to gain an industry perspective on model-related topics, which covered model governance, scope and depth of validation performed, model usage with specific focus on overrides, treatment of unrated deals or delays in the re-rating of deals, model materiality definitions, discount rate used in loss given default (LGD) models, incorporation of multiple defaults in LGD models, and identifying the downturn period and methodologies used to determine the downturn LGD and downturn exposure at default estimates.

In addition to conducting these meetings at the banks, the Department obtained guidance from other international regulators on the above-mentioned topics. Bank-specific feedback was provided to the individual banks' senior management and once research embarked on by the Department on this matter is concluded, the Department will provide the industry with further guidance.

2.3.5 Changes to credit risk models

The Department continued to follow a robust review and approval process for changes to credit risk models used for the calculation of required capital and reserve funds for credit risk by banks that adopted the IRB approach as highlighted in the Department's 2013 *Annual Report*. During 2015 this Department received 18 notifications of non-material changes and 27 submissions of material changes to the IRB banks' rating systems.

2.3.6 Eligible External Credit Assessment Institutions

The Regulations stipulates that for the calculation of minimum required capital and reserve funds relating to credit risk in terms of the STA, and for the treatment of relevant securitisation and re-securitisation exposures, banks shall apply the ratings or assessments issued by eligible external credit assesment institutions (ECAIs).

During 2015, after a robust review process, the Department approved Global Credit Rating Co. (Pty) Limited (GCR) as an eligible ECAI. Directive 9 of 2015 was issued to inform banks and/or affected persons of the mapping of the international scale ratings of GCR to the prescribed risk weights specified in regulation 23 of the Regulations.

2.3.7 Directives and circular related to credit risk

The following directives and circular were issued during the period under review:

- Directive 4 of 2015: the directive specified areas of the legal framework requiring amendment in order to ensure that the legal framework appropriately reflects local and international market developments, and complies with the ever-evolving international regulatory and supervisory standards and best practices.

- Directive 7 of 2015: the directive provided clarity on how banks should identify restructured credit exposures and how to treat them for purposes of the definition of "default" as defined in regulation 67 of the Regulations. Furthermore, the directive also addressed the reporting of restructured credit exposures and the rehabilitation of non-performing loans using restructuring.

- Directive 9 of 2015: the directive informed banks and/or affected persons of the mapping of the international scale ratings of GCR to the prescribed risk weights specified in regulation 23 of the Regulations.

- Circular 5 of 2015: the circular informed banks that the use of credit risk support not specifically provided for in regulations 23(7), 23(9), 23(12) or 23(14) of the Regulations is prohibited in a bank's credit risk rating process and in the calculation of minimum required capital and reserve funds.

2.4 Market risk

2.4.1 Introduction

The global markets trading environment was particularly challenging for South African banks in 2015 due to a combination of market and regulatory factors. Most of these factors were discussed with banks in the scheduled supervisory meetings as discussed below.

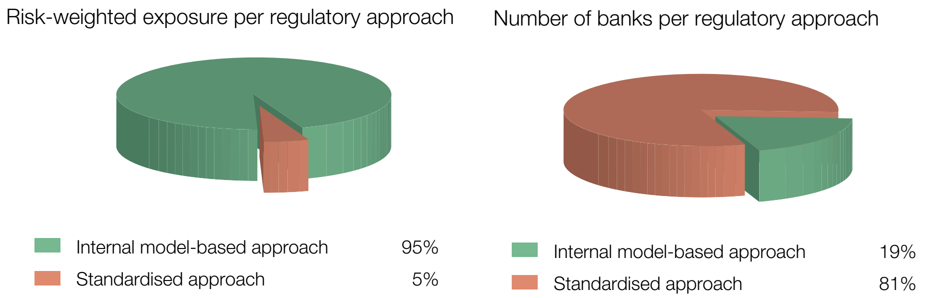
2.4.2 Methodologies to calculate minimum required regulatory capital relating to market risk

Under the regulatory framework employed in South Africa, banks can choose from the following two methodologies to calculate their minimum required regulatory capital relating to market risk:

1. the standardised approach; and
2. the IMA.

The risk-weighted exposure for the two approaches in comparison to the proportion of banks per approach is depicted in Figure 2.3.

Figure 2.3 Market risk methodologies applied by banks as at 31 December 2015



2.4.3 Market risk reviews

The Department performed both compliance-based and risk-focused supervision of market risk during the period under review. Market risk reviews conducted in 2015 focused on banks using the IMA for regulatory purposes. Reviews of certain banks' treasury and securities operations also took place. The Department also concluded one review on equity risk in the banking book, with further reviews scheduled for 2016. In addition, the Department conducted CCR reviews on selected banks.

2.4.4 Key findings

The following issues featured prominently in the discussions with the banking industry in 2015, to the extent that they impact the markets trading businesses:

- Commodity prices continued to decline sharply in 2015, with the oil price in particular slipping to its lowest level since 2004. The commodity price decline poses downside risks to the economic growth outlook in South Africa and many parts of Africa due to a high reliance on mining for employment, export growth and government revenue. Various South African banks have operations across Africa and are therefore exposed (directly and indirectly) to the downturn in the commodity super cycle.

- The availability of liquidity in the trading market has been declining during 2015 and the Department consistently engaged with banks to assess the impact of reduced liquidity on banks' ability to transfer risk in the market. Banks became more cautious with their trading risk assumptions.

- Conduct risk, a thematic topic of the Department in 2014, received a significant amount of attention by banks in their trading operations given the widespread and severe fines issued for misconduct globally during 2015. While there were no significant South African industry-wide concerns in this regard, banks have on a sporadic basis experienced some internal breaches of set policies and procedures. The emergence of this risk type has led to the FSB and the Bank's joint efforts to produce the foreign exchange review report as well as the draft code of conduct for the South African OTC markets. Both documents were published in October 2015, namely *Report of the Foreign Exchange Review Committee on the Operations of Authorised Dealers in the South African Foreign Exchange Market and Draft Code of Conduct for the South African Over-the-Counter Markets*.[28]

- Algorithmic trading also came to the fore during 2015 and has been cited as one of the contributors to the increased volatility in global markets.

- Concerns related to a possible change of the South African sovereign credit rating to sub-investment grade have been discussed with market participants for the past two to three years. The banking industry was urged to embark on stress testing exercises to determine the effects of a possible downgrade on their trading portfolios. South Africa's five-year credit derivative spreads approximately doubled over the 2015 calendar year, exceeding levels of spreads for Turkey and trending at the same level as Russia towards the end of 2015.

28. Both reports are available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6928

2.4.5 Counterparty credit risk thematic reviews

Central clearing will affect OTC trading activities world-wide. The banking industry is moving towards the use of central counterparties (CCPs) to clear OTC derivatives in order to reduce systemic risks associated with bilateral OTC derivatives markets. These risks include the long and legally cumbersome transaction close-out process in the event of a major default which CCPs can mitigate by establishing and enforcing close-out rules.

In terms of Core Principle 17, supervisors must be satisfied that banks have a CCR management process that takes into account their risk appetite, risk profile and market and macroeconomic conditions. This includes appropriate policies and processes to identify, measure, evaluate, monitor, report and control or mitigate this risk on a timely basis.

In order for the Department to discharge its duties relating to Core Principle 17, it therefore conducted CCR thematic reviews, based on a questionnaire that was sent to specific banks in the South African banking industry for completion. On-site supervisory meetings were subsequently held at the respective banks to discuss key issues emanating from the documents and any topics on which the Department may require clarity.

The thematic review process encompassed all areas required to be covered under Core Principle 17, as well as additional aspects related to the Basel III framework for risk measurement, standards and monitoring, together with pending regulatory reforms.

2.4.6 Equity risk in the banking book

During 2015 the Department continued with the thematic review that focused on exposures related to equity risk in the banking book. These exposures are generally held for long-term investment purposes and are included in the banking book for regulatory purposes, thus receiving a capital treatment that is independent of the market risk charge.

For supervisory purposes, equity risk in the banking book is regulated together with market risk, and the reviews are aimed at gaining insight into areas where this risk arises and management of the risk over the life cycle of these investments. This risk type has been diminishing over recent years as banks reduce this type of investment activity. Further assessments will continue during 2016, in this area, for selected banks.

2.4.7 Directive related to market risk

Directive 10 of 2014 was cancelled and Directive 5 of 2015 was issued with effect from 1 April 2015. The directive informs banks of the capital requirements for OTC derivatives not transacted through a CCP. Based on the relevant requirements specified in the Regulations, the full capital requirements for CVA risk emanating from a bank's exposure to ZAR-OTC and local-OTC derivatives[29] should be maintained.

29. For the purposes of Directive 5 of 2015, local-OTC derivatives mean OTC derivatives entered into bilaterally between South African counterparties. Locally registered branches of foreign banks are regarded as South African counterparties for this purpose. Local-OTC derivatives may include OTC-derivatives not denominated solely in ZAR.

2.5 Operational risk

2.5.1 Introduction

Operational risk and information technology (IT) risk have continued to occupy the risk landscape globally, from miss-selling, fines and penalties being levied against various institutions to the ever-increasing threat of cyber risk and other emerging technology risks. This happened despite the fact that, internationally, losses attributable to these risks seemed to have decreased year on year. Domestically the number of loss events increased slightly but the total gross loss amount decreased noticeably.

A turbulent 2016 has been predicted for the South African economy and this is normally associated with an increase in operational risk losses, albeit at a lag in terms of occurrence and impact. The Department expects a focus shift from the measurement of these types of risks to the management thereof based on the proposed amendments in terms of the operational risk approaches.

2.5.2 Methodologies to calculate minimum required regulatory capital relating to operational risk

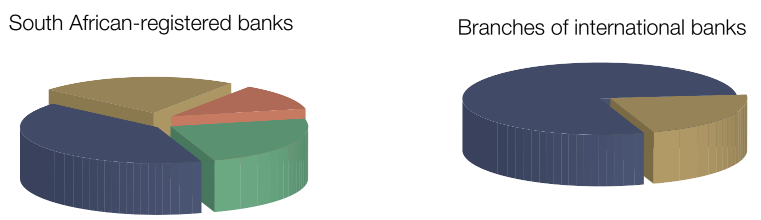
Under the regulatory framework employed in South Africa, banks can choose from the following four methodologies to calculate their minimum required regulatory capital relating to operational risk:

1. the basic indicator approach (BIA);
2. the standardised approach;
3. the alternative standardised approach; and
4. the advanced measurement approach (AMA).

During the period under review, one application for a local branch of an international bank licence was approved and the said branch opted for the default BIA in the measurement of operational risk (see Figure 2.4).

The number of banks using each of the aforementioned approaches is depicted in if Figure 2.4

Figure 2.4 Operational risk methodologies applied by banks as at 31 December 2015



South African-registered banks	
Basic indicator approach	7
Standardised approach	4
Alternative standardised approach	2
Advanced measurement approach	4

Branches of international banks	
Basic indicator approach	12
Standardised approach	3
Alternative standardised approach	0
Advanced measurement approach	0

2.5.3 Operational risk reviews

During the year under review, the Department continued its focused operational risk reviews at selected banks, with an emphasis on management, measurement, frameworks, processes, profiles and reporting of operational risks. The main findings of these reviews were:

- Governance and resourcing: banks generally have sound governance committee structures in place, which provide adequate operational risk management oversight. However, banks have been facing challenges in terms of scarcity of operational-risk skills, especially in cases where high staff turnover was prevalent.
- African footprint: local banks operating in the rest of Africa are still experiencing many risk, control and system issues. The Department is closely monitoring developments in this space.
- Risk control self-assessments (RCSAs), key risk indicators (KRIs) and control failures: the Department is concerned that RCSAs and KRIs are sometimes not completed appropriately. Moreover, control inefficiencies and failures remain prevalent in some institutions. A concerted effort by banks in reaching resolution on these matters is required.
- AMA: banks making use of internal models for calculating their operational risk-charge have maintained their efforts in refining, enhancing and in some instances researching and developing 'new-generation' models. Even though the Basel Committee has during the latter part of the year proposed the removal of the AMA, the Department is of the view that the use of models would still be critical for internal measurement purposes and that quantitative analytical skills will continue to play a pivotal role in the assessment of operational risk. Furthermore, these skills can also be applied in so far as data are concerned.
- Operational risk losses: in the midst of continuous challenging economic conditions, there has been a noticeable decrease in operational risk losses in 2015 compared to 2014. The losses emanated mainly from execution delivery and process management and external fraud event types.
- Audit reports related to operational risk management: during the reviews, closed sessions with banks' internal auditors were held to ascertain if a comprehensive review of operational risk was attained. In several instances the root cause analysis indicated that 'people' and 'negligence' were the main contributors to control breakdowns. The Department urged banks to address the matter urgently.

2.5.4 Operational risk long-form reviews

The long-form review process for operational risk was finalised late in 2013 after the finalised template was published on the Bank's website.[30]

The review has now been completed as two AMA banks in 2014 and two AMA banks in 2015 were subjected to this review. The results from these reviews were generally satisfactory with specific findings being highlighted. The Department will continue to monitor progress in closing the particular highlighted gaps. In addition, similar reviews could be considered in the foreseeable future.

30. Available at http://www.resbank.co.za/RegulationAndSupervision/BankSupervision/TheBaselCapitalAccord(Basel%20II)/Pages/Advance-measurement-approach-.aspx

2.5.5 Outsourcing

Outsourcing remained a focus area for the Department and there has been a marked increase in terms of either applications for approval by banks, notifications or merely requests for guidance and engagement. A return dealing with outsourcing was introduced during 2015 to better understand banks' outsourcing risk exposures, to ensure effectiveness and efficiency of managing these outsourcing exposures and to ascertain the level of concentration in the industry. The first submission in terms of Directive 8 of 2015 on the reporting of material outsourced service providers and critical third-party service providers was received, analysed and feedback was discussed with the relevant stakeholders. Some concerns were highlighted and ongoing monitoring and effort is required from both the Department and the respective banks, especially in terms of contingencies and dependence on providers that have a dominant presence in the market.

The team further provided input into several applications with regard to outsourcing of functions within banks in terms of Guidance Note 5 of 2014.

2.5.6 Information technology risk

Following the 2014 IT project governance flavour-of-the-year interactions, banks' investment in IT infrastructure was analysed to determine whether it was sufficient to ensure that IT systems were operationally 'fit'. The Department also engaged the banking industry to ensure that banks were adequately prepared for a worst-case scenario should a national blackout of the power grid or prolonged power disruptions occur.

Cyber security remains a concern and will continue to receive attention. The Department will also consider further regulatory interventions. The Department also benchmarked local IT risk practices against international best practices during international visits.

The Department continued to monitor global trends and noted changes with regard to central banks becoming more involved in dealing with financial technology innovation. South African banks have taken steps to prepare themselves for dealing with these technologies, including developing their position on adopting some of these technologies, such as cloud computing.

2.5.7 Information technology risk reviews

During 2015 focused IT risk on-site meetings continued. Topics covered included IT risk appetite, business continuity and disaster recovery, emerging technologies, project governance and maintenance, and information security, including cyber security. The key findings were as follows:

- Some instances of insufficient capacity of IT risk resources were noted and instances of governance structure changes that were still being embedded were identified.
- Banks had to deal with sizeable and complex projects while being faced with resource constraints. However, projects were receiving appropriate oversight and overall practices improved.
- Considerable effort has gone into information security controls and banks are exerting substantial time and resources to enhance their ability to detect and respond to security incidents, especially with a heightened focus on cyber security.
- IT governance in some of the rest of Africa countries was a concern.

The Department will continue to observe the maturity of processes within banks, specifically with regard to keeping its IT current and minimising control failures.

2.5.8 Risk data aggregation and risk reporting

The Basel Committee issued the *Principles for the effective risk data aggregation and risk reporting*[31] in January 2013, noting that the principles would initially only be applicable to systemically important banks. The Department has since issued Guidance Note 3 of 2014[32] informing the banking industry that the principles applied to all South African banks, including local branches of international banks. Subsequently, Directive 2 of 2015[33] was issued, advising domestic systemically important banks (D-SIBs) to comply with the requirements by 1 January 2017 and the implementation timelines for non-D-SIBs to be considered on a case-by-case basis.

The Department requested banks to compete self-assessments and continued interactions with banks on a bilateral basis, to inform and monitor progress made. This approach will endure

31. Available at http://www.bis.org/bcbs/publications.htm?a=1&mp=any&pi=title&page=4

32. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6114

33. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx? sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6629

and will be complemented with meetings with BASA. Banks, especially the larger organisations, have been making a concerted effort in progressing towards compliance.

2.5.9 Directives and guidance note related to operational risk

The following directives and guidance note were issued during the period under review:

- Directive 2 of 2015:[34] the purpose of this directive was to inform banks to implement robust risk management practices that include specified matters related to risk data aggregation and risk reporting.
- Directive 4 of 2015:[35] the purpose of this directive was to specify identified areas of the legal framework requiring amendments, including specified regulations, circulars, directives or guidance notes to ensure that the legal framework for the regulation and supervision of banks and banking groups in South Africa remains relevant and current.
- Directive 8 of 2015:[36] the purpose of this directive was to direct all banks to submit specified information in respect of their outsourcing arrangements within indicated timelines.
- Directive 10 of 2015:[37] this directive sets out the requirements for the approval and notification of changes to AMA banks' existing operational risk management and measurement systems.
- Guidance Note 3 of 2015:[38] the purpose of this guidance note was to inform all banks of the process to be followed and the information to be submitted when applying to adopt the AMA. This guidance note relates to all future applications to obtain the relevant approval from the Registrar and the fact that banks that received approval previously do not have to reapply.

2.6 Asset and liability management risk

2.6.1 Focused reviews

According to the Core Principles, a supervisor is required to determine that banks have in place certain minimum standards in respect of liquidity risk and interest rate risk in the banking book. During 2015 the Department conducted several reviews covering both major banks and smaller individual banks to evaluate their current practices. The Department sent out a questionnaire covering banks' policies, procedures and internal controls relating to liquidity risk and interest rate risk in the banking book.

Following an off-site review of the responses received, the Department conducted on-site meetings to discuss the responses and to probe any relevant additional information to ascertain the level and intensity of supervisory action required.

2.6.2 Participation in liquidity risk simulations

The Department continued to participate in ad hoc liquidity risk simulation exercises at banks, which were facilitated by an independent external party in order to assess the adequacy and effectiveness of banks' liquidity risk management frameworks.

Representatives of the Department fulfilled an observer role during these exercises. These simulation exercises continued to be of great value both to the Department and participating banks by highlighting areas of improvement and by demonstrating the need for robust liquidity risk management.

34. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6629

35. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6664

36. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6786

37. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6995

38. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6617

2.6.3 Sovereign rating change scenario

In line with the continued risk of South Africa receiving a sub-investment grade sovereign credit rating and the subsequent impact it might have on the banking sector, the Department requested all banks to participate in a stress scenario to assess the potential impact.

2.6.4 Regulatory developments

The Department continues to monitor implementation of the NSFR standard by banks. This process commenced on 1 January 2013 and will continue until the NSFR becomes a regulatory requirement as from 1 January 2018.

Through its membership on the TFIR, the Department continued to participate in the development of the international framework to measure and potentially implement a regulatory capital requirement for interest rate risk in the banking book.

In 2015 the Department continued to engage with the South African banking sector through BASA to monitor and discuss international regulatory developments and the impact thereof on liquidity risk and interest rate risk in the banking book.

2.7 Capital management

2.7.1 Overview of internal capital adequacy assessment process reviews and key findings

The Department issued Guidance Note 4 of 2015 during August 2015 to provide guidance on expectations with respect to ICAAPs as well as the contents of ICAAP-documents of banks.

During 2015 the Department also continued with focused reviews on ICAAPs, in particular on improvements of credit risk economic capital models, capital management, stress testing, validation of economic capital and stress testing models and a continued focus on the 'use test'.

On-site reviews during 2015 highlighted the following:

- Banks' capital planning was generally robust and regularly challenged by management. Forecasts for capital and leverage indicated that South African banks remained adequately capitalised.
- Risk appetite frameworks of smaller banking institutions required improvements.
- Large and complex banks use economic capital models to accurately measure risks and to relate the risks to capital requirements. The results of these models are used in decision-making; therefore, management should continue to ensure economic capital models are validated and are still appropriately calibrated post the financial crisis.
- In certain instances banks applied the STA to calculate capital requirements for credit risk, especially relating to exposures in foreign operations. The Department imposed additional capital requirements in such instances where the STA was found not to be a true reflection of the underlying risk.
- The identification, measurement, monitoring and mitigation of credit concentration risk, model risk and business risk required improvements at some banks.
- It was found to be beneficial for banks to be capable of performing ad-hoc stress testing to investigate the impact of any possible changes in the economic environment within a short turnaround time.

2.7.2 Regulatory and economic capital data collection exercise

The Department continued to collect and monitor regulatory and economic capital forecasts from D-SIBs, biannually, in order to supplement the ICAAPs. During 2015 a data assessment template was standardised in order to automate and simplify the monitoring and analysis of regulatory versus economic capital data.

The data collected also included projected regulatory capital planning data. The aforementioned data continue to enhance the Department's assessment of risk coverage and capital planning at banks.

2.7.3 Domestic systemically important banks

The Department continuously applies its D-SIB methodology to assess which banks are regarded as systemically important and the extent to which they are systemically important. During November 2015, updated D-SIB loss absorbency capital buffer requirements were communicated to bank-controlling companies and banks that were classified as D-SIBs.

Since 2013 the Department kept D-SIBs informed of changes to the size of their D-SIB capital buffer requirements. This communication allowed banks and bank-controlling companies sufficient time to adequately plan and manage the aforementioned capital buffer requirements.

The phasing-in of the D-SIB loss absorbency capital requirement together with capital buffers forming part of the capital conservation range, that is, the capital conservation buffer and the countercyclical capital buffer commenced on 1 January 2016. During times of stress, CARs might fall below the aforementioned buffer requirements; however, restrictions on the level of distributions apply with effect from 1 January 2016.

2.8 Pillar 3: disclosure

2.8.1 Overview of key activities

During 2015 the Department reviewed disclosures by banks in terms of Pillar 3 requirements, with specific focus on the newly implemented Pillar 3 disclosure standards relating to the composition of capital, LCR and the leverage ratio. In some instances, although the banks disclosed some of the required information, mandatory disclosure templates were not always used and some banks failed to comply with all of the disclosure requirements. The Department will continue to monitor compliance with Pillar 3 disclosure requirements, with emphasis on areas where banks are still lacking.

2.8.2 Directives related to disclosure

Directive 3 of 2015 titled *Matters related to composition of Pillar 3 disclosure requirements*[39] was amended and reissued following the RCAP review. Amendments effected to the directive were, in the main, related to the frequency of the reconciliation of regulatory capital to the financial statements. The said reconciliation is now required semiannually instead of annually.

Directive 11 of 2015 titled *Matters related to revised Pillar 3 disclosures requirements*[40] was issued to ensure timeous implementation of the revised *Pillar 3 Standards: revised Pillar 3 disclosure requirements*, issued by the Basel Committee in January 2015. Banks are expected to publish their first Pillar 3 reports in accordance with the revised framework with their annual reports that relate to the 2016 financial year end.

39. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=6660

40. Available at http://www.resbank.co.za/publications/detail-item-view/pages/publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=7003

2.9 Consolidated supervision

2.9.1 Nedbank Group Limited's Supervisory College

The Department is committed to conducting effective consolidated supervision, as proposed by the Basel Committee. The Department's consolidated supervision framework includes the hosting of supervisory colleges. The overarching objective of a supervisory college is to assist the home- and host-country supervisors in gaining a better understanding of the banking group's risk profile.

In line with the Department's consolidated supervision framework and international best practices, the Department held a supervisory college for supervisors of Nedbank Group Limited's (NGL) African banking operations from 9 to 10 November 2015. NGL is involved in six countries in Africa, including South Africa, and a total of eight supervisors from four countries attended the supervisory college for the African operations of NGL.

The college afforded all an opportunity to gain knowledge and share information. Also, networks were built between home and host regulators, which will contribute to a more effective consolidated supervision. Information sharing and enhanced cooperation between supervisory authorities are key to strengthening cross-border supervision of banking groups.

2.9.2 Supervisory meetings with the FSB

Throughout the year the Department and the FSB maintained regular interactions. Conglomerates operating within the South African jurisdiction were discussed ensuring appropriate supervisory processes were in place. These meetings serve as a platform where valuable information is shared between the relevant supervisory authorities thereby enhancing supervision effectiveness of conglomerate groups.

2.9.3 Supervisory colleges hosted by the FSB

As mentioned in the Department's previous annual reports, the FSB and the Department have always enjoyed a close working relationship by virtue of the regular supervisory discussion meetings. This relationship has been further strengthened during the year under review by increasing cooperation, information sharing and communication between the two supervisory bodies in anticipation of the imminent establishment of the PA.

In August 2015 the FSB hosted supervisory colleges for all South African insurance groups with a presence in Africa. Representatives from the Department were also invited due to the interconnectedness between banking groups and insurance groups.

During the supervisory college sessions each country provided insights into the host entity's operations, including, but not limited to financial highlights, strategic objectives and pertinent risk areas.

The information and interactions obtained at the supervisory college sessions proved extremely valuable in the Department's continued risk assessment and analysis of the banking groups with insurance subsidiaries.

2.10 Anti-money laundering and combating the financing of terrorism

2.10.1 Thematic sanctions review

In 2014, the Department, with the assistance of a third party service provider, conducted a banking-wide off-site thematic review of the sanctions-screening controls employed by South African banks. The thematic review evaluated if banks' sanctions-screening systems were adequately configured to protect the South African banking industry against being used for the financing of terrorism and related activities and whether or not banks effectively comply with combating of terrorism legislation.

During the course of 2015, the AML team received quarterly progress reports from all 31 participant banks and worked closely with those banks that required additional support, re-testing and guidance. The deadline for remediation of deficiencies identified in the 2014 exercise was November 2015 when all banks were expected to have addressed their specific areas of concern.

2.10.2 On-site inspections

On an annual basis, the Department follows an AML/CFT risk-based approach to determine which banks to inspect during the year. A total of seven AML/CFT local on-site inspections in terms of section 45B of the FIC Act were conducted during 2015. All local inspections undertaken in 2015 were on average conducted over a period of three weeks.

The most pertinent findings arising from local on-site inspections conducted during 2015, indicated that banks required enhanced focus and strengthening of their controls in relation to compliance with the FIC Act in various areas, but in particular the following:

- documentation and implementation of client identification and verification as well as record-keeping procedures;
- implementation of effective working methods pertaining to the identification and reporting of cash transactions above the prescribed amount;
- implementation of effective working methods pertaining to the detection and investigation of suspicious and unusual transactions;
- implementation of effective controls relating to the identification and reporting of property associated with terrorism and related activities; and
- development and implementation of AML/CFT targeted training programmes on specialised business areas, that is, in line with employees' responsibilities, activities and skills.

In addition to testing banks' compliance with the FIC Act, the Department also assessed banks' adopted AML/CFT risk-based approaches, including their treatment of politically exposed persons in line with the FATF recommendations.

The most pertinent finding arising from these assessments indicated that banks required enhanced focus and strengthening of their controls in relation to the review and implementation of effective controls relating to management of transactions of high-risk clients (including politically exposed persons), products, services and channels.

In 2015 the Department visited two cross-border banking subsidiaries of South African registered banks in order to assess the operations level of compliance with:

- the global AML/CFT standards of the FATF 40 Recommendations;
- the Basel Committee's guidance on sound management of risks related to money laundering and financing of terrorism; and
- country-specific AML/CFT legislation.

Each visit took a week and was conducted in collaboration with the specific regulators of that country. The inspection findings revealed, among other things, that there was still a need for parent companies to enhance their efforts to assist, guide and perform adequate oversight of their cross-border operations' AML/CFT frameworks.

Table 2.1 reflects the details of the inspections conducted and also provides a comparison of the inspections conducted from 2012 to 2015.

Table 2.1 On-site inspections

Nature of inspection		2012*	2013	2014	2015
Routine........................	Large banks	2	3	0	1
	Small banks	6	2	8	6
	Cross-border (Africa)	0	0	1	2
Non-routine	Large banks	0	1	0	0
	Small banks	0	1	0	0
Total		8	7	9	9

* AML/CFT inspections commenced in April 2012

2.10.3 Off-site supervision

Throughout 2015 the Department conducted various workshops and prudential meetings with select locally registered banks. Topics discussed at such meetings included:

- challenges faced by banks to comply with the FIC Act;
- banks' readiness to implement the FIC Act Amendment Bill with regard to policies, procedures, systems and controls;
- issues emanating from international best practice standards, such as the FATF Recommendations;
- AML/CFT compliance resource staffing and capacity;
- compliance monitoring and oversight in respect of automated and/or manual monitoring systems and record-keeping processes;
- the use of alternative processes and/or technological advancements to identify and record customer identification and information verification;
- progress made by banks in remediating AML/CFT inspection findings;
- innovative ways to further financial inclusion, while still meeting AML/CFT requirements in the context of the risk-based approach relating to product offerings, customer due diligence and risk assessment and controls; and
- ways in which banks perceive and manage the AML/CFT risks of money value transfer service providers as clients and/or products.

This is an ongoing element of the Department's supervisory calendar that is continued on an annual basis.

2.11 Recovery planning

In the past the main objective of banking regulations was to reduce the risk of bank failures and the focus was on recovery planning. Currently, resolution planning has come to the fore with the main objective of reducing the negative impact and consequences of a bank failure. Banks are responsible for the development of their own recovery plans and supervisory authorities are responsible for the development of resolution plans.

Supervisory interaction with regard to recovery plans was as follows:

- The Financial Stability Board issued a document titled *Key attributes of effective resolution regimes for financial institutions*[41] in 2011. In this document, the Financial Stability Board recommended that all systemically significant financial institutions have recovery and resolution plans in place.
- In 2012, the Department requested that all banks start developing recovery plans. In order to review the progress made by banks in the development of their draft recovery plans, a series of workshops was held with each of the large South African banking groups since 2013. These recovery plans were benchmarked against guidance provided by the Financial Stability Board and feedback was given to the banks on the gaps identified by the Department. The banks were required to have a first version of a board-approved recovery plan in place by the end of 2013.
- The Department, in conjunction with the Bank's Financial Stability Department, continued the process of reviewing the board-approved recovery plans of these banking groups during 2014 and 2015. This assisted the banks to improve their recovery plans. Further refinement of the recovery plans is considered to be an ongoing process.
- The Department issued Directive 1 of 2015 on the minimum requirements for recovery plans[42] as further guidance against which banks can benchmark their recovery plans.

41. Available at http://www.fsb.org/wp-content/uploads/r_111104cc.pdf?page_moved=1

42. Available at http://www.resbank.co.za/Publications/Pages/Bank-Actdirectives.aspx

Chapter 3: Developments relating to banking legislation

3.1 Introduction

The Department continues striving to ensure that the legal framework for the regulation and supervision of banks and banking groups in South Africa remains relevant and current. Ideally, the legal framework pertaining to banking regulation has to reflect local and international market developments, and should comply with the applicable international regulatory and supervisory standards and best practices. The Department therefore reviews banking legislation, including the Banks Act, the Regulations issued in terms thereof and other pieces of related banking legislation on an ongoing basis. The Department makes recommendations to the Minister of Finance to effect the necessary amendments thereto.

3.2 The Banks Act 94 of 1990

As was reported in the Department's 2014 *Annual Report*, proposals were made to amend certain provisions contained in section 69 of the Banks Act. During the year under review, the proposed amendments were approved and the Banks Act was amended by the Banks Amendment Act 3 of 2015 (Banks Amendment Act) promulgated on 29 June 2015.

The objectives of the Banks Amendment Act are to:

- enable the application of the provisions on arrangements and compromises in the Companies Act 71 of 2008, to banks under curatorship;
- expand the basis on which a curator may dispose of all or part of the business of a bank to enable an effective resolution of a bank under curatorship; and
- provide for the application of the Promotion of Administrative Justice Act 3 of 2000, to any administrative action taken in terms of the Banks Act.

Additionally, efforts continued to be focused on providing comments on the proposed FSR Bill issued by National Treasury in order to establish the Twin Peaks financial regulatory architecture. Public comments on the FSR Bill closed on 2 March 2015 and the Bill was tabled before Parliament during October 2015. The FSR Bill will result in consequential amendments to the Banks Act, which will be finalised once the Bill has been approved by Parliament and promulgated as an Act of Parliament.

3.3 Update regarding amendments to the Regulations relating to Banks

The framework in terms of which the Department regulates and supervises banks and banking groups is subject to regular assessments and reviews by various international standards-setting bodies, such as the Basel Committee, the Financial Stability Board, the International Monetary Fund and the World Bank, to assess and review the extent to which domestic regulations are aligned to the minimum internationally agreed standards and requirements.

In this regard, the Basel Committee implemented its comprehensive RCAP[43] to monitor, assess and evaluate the implementation by member jurisdictions of the respective frameworks (Basel II, Basel 2.5 and Basel III) issued by the Basel Committee, as discussed in section 1.5 of this report.

43. Available online at: http://www.bis.org/publ/bcbs264.htm

As part of the assessment phase of South Africa's RCAP during the first quarter of 2015, the RCAP assessment team requested that selected amendments be effected to the Regulations in respect of matters that were regarded by them as sufficiently material to be incorporated into the Regulations instead of forming part of directives, circulars or guidance notes, or the

Department's supervisory review and evaluation processes. These required amendments to the Regulations were effected by means of *Government Gazette* No. 38616[44] published on 27 March 2015, essentially addressing matters related to banks' risk-based capital, and *Government Gazette* No. 38682,[45] published on 10 April 2015, essentially addressing matters related to the Basel III standards on liquidity.

The RCAP assessment team found that, overall and in respect of all the key components, the South African prudential regulations were compliant with all the respective components and standards prescribed under the respective Basel frameworks. Specific areas that nevertheless required refinement or further amendments were also identified during the RCAP process.[46]

Furthermore, based on various other requirements, best practices and standards recently finalised by international standard-setting bodies such as the Basel Committee, further proposed amendments to the Regulations were necessary during 2015. In addition, the global financial crisis highlighted the need for enhanced data with regard to international banking statistics, including major banking systems' funding and lending patterns. In this regard, it became necessary to replace the forms BA 940 and BA 950 with a single amended form BA 940. The amended form BA 940 not only combines information required for locational statistics by requesting information on both residence and nationality, but also requires a more granular sectoral breakdown by banks.

Based on the aforesaid, on 2 September 2015 and 5 November 2015, further proposed amendments to the Regulations were published for public comment. The proposed amendments essentially related to:

- composition of capital disclosure requirements - Rules text;
- LCR and liquidity risk monitoring tools;
- LCR disclosure standards;
- LCR and restricted-use committed liquidity facilities;
- monitoring tools for intraday liquidity management;
- Basel III leverage ratio framework and disclosure requirements; and
- amendments to various returns submitted to the Department and the Economic Research and Statistics Department of the Bank, including the amended form BA 940.

In order to ensure that all relevant key players remain updated in respect of all relevant comments submitted, discussions held and questions raised in respect of the proposed amended Regulations, various staff members of the Department attended and actively participate in all relevant working groups, task groups or forums established by key players, such as those by the BASA.

The proposed amended Regulations have accordingly been finalised and it is expected that amended Regulations will be published during 2016.

The Department will continue to monitor, among other things, the developments relating to the G-20 discussions and the press releases, publications and directives issued by the Basel Committee and the Financial Stability Board, including further work being conducted by the Basel Committee related to the Basel III framework, in order to identify possible further areas that would necessitate amendments or refinements to the Regulations.

44. Available online at: http://www.resbank.co.za/Lists/News%20and%20Publications/Attachments/6670/Amended%20Reg%20re%20Banks_Matters%20excl%20liquidity%20risk.pdf

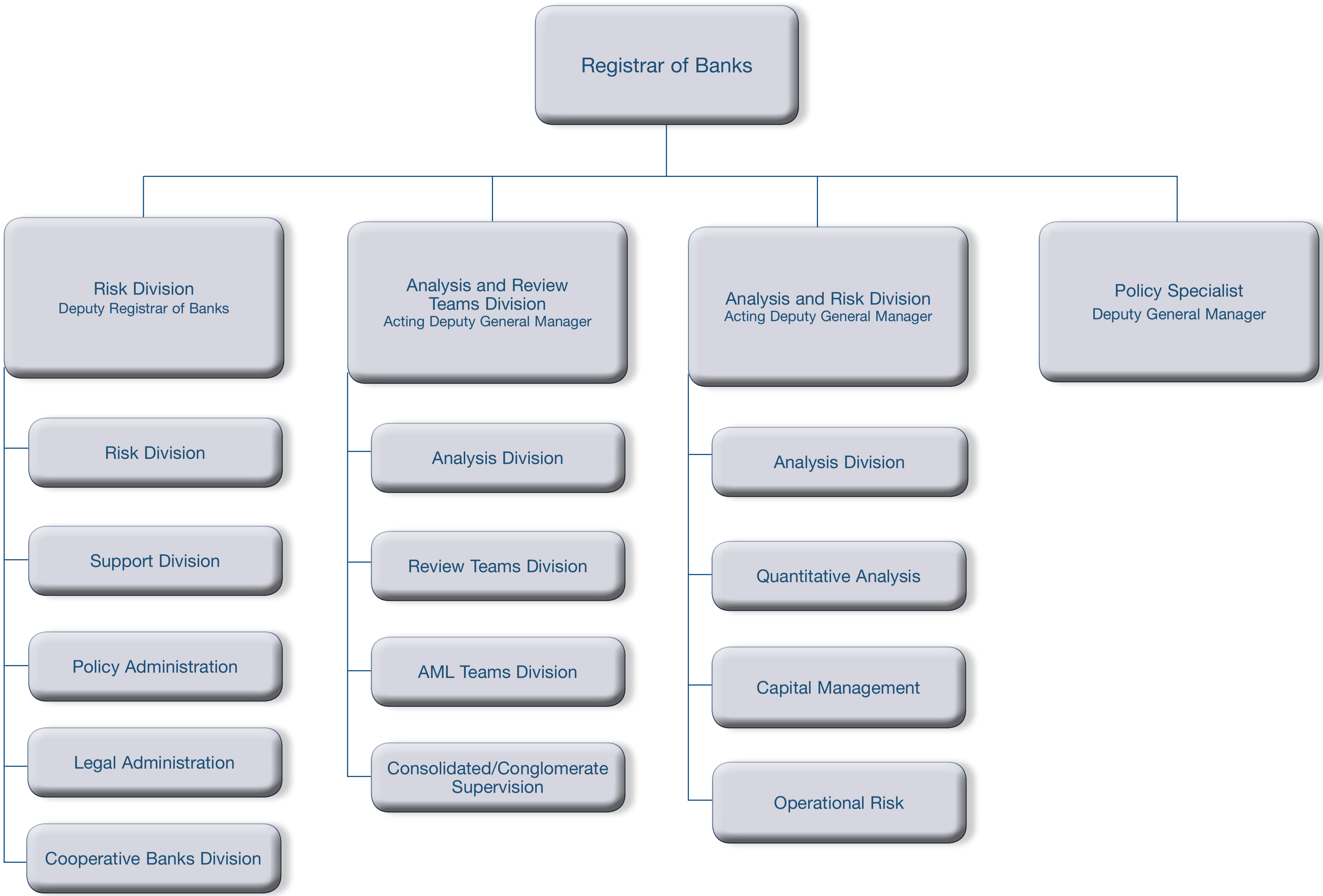
45. Available online at: http://www.resbank.co.za/Lists/News%20and%20Publications/Attachments/6670/Amended%20Reg%20re%20Banks_%20Liquidity%20risk.pdf

46. The RCAP reports for South Africa are available online at: Assessment of Basel III risk-based capital regulations https://www.bis.org/bcbs/publ/d322.pdf and Assessment of Basel III LCR regulations https://www.bis.org/bcbs/publ/d323.pdf

Appendices

Appendix 1

Organisational structure of the Bank Supervision Department



Appendix 2

Registered banks, local branches of foreign banks and mutual banks as at 31 December 2015

Registered banks

	Institution	Address	Total assets at 31 December 2014 (R millions)	2015 (R millions)	Annual growth (per cent)
1	Absa Bank Limited	P O Box 7735, Johannesburg, 2000	804 271	926 526	15,20
2	African Bank Limited	Private Bag X170, Midrand, 1685	51 341	54 800	6,74
3	Albaraka Bank Limited	P O Box 4395, Durban, 4000	4 792	5 026	4,88
4	Bidvest Bank Limited	P O Box 185, Johannesburg, 2000	4 722	6 017	27,42
5	Capitec Bank Limited	P O Box 12451, Die Boord, Stellenbosch, 7613	51 877	61 970	19,46
6	FirstRand Bank Limited	P O Box 650149, Benmore, 2010	856 911	979 920	14,35
7	Grindrod Bank Limited	P O Box 3211, Durban, 4000	9 283	11 262	21,32
8	Habib Overseas Bank Limited	P O Box 62369, Marshalltown, 2107	1 207	1 318	9,20
9	HBZ Bank Limited	P O Box 1536, Wandsbeck, 3631	3 848	4 413	14,67
10	Investec Bank Limited	P O Box 785700, Sandton, 2146	310 142	377 046	21,57
11	Mercantile Bank Limited	P O Box 782699, Sandton, 2146	8 384	9 632	14,89
12	Nedbank Limited	P O Box 1144, Johannesburg, 2000	714 408	813 287	13,84
13	Sasfin Bank Limited	P O Box 95104, Grant Park, 2051	4 735	5 583	17,91
14	The South African Bank of Athens Limited	P O Box 784921, Sandton, 2146	2 284	2 510	9,91
15	The Standard Bank of South Africa Limited	P O Box 7725, Johannesburg, 2000	1 099 713	1 213 528	10,35
16	Ubank Limited (formerly known as Teba Bank Limited)	Private Bag X101, Sunninghill, 2157	4 250	4 691	10,37

Appendix 2

Registered banks, local branches of foreign banks and mutual banks as at 31 December 2015 (continued)

Registered local branches of foreign banks

	Institution	Address	Total assets at 31 December 2014 (R millions)	Total assets at 31 December 2015 (R millions)	Annual growth (per cent)
1	Bank of Baroda	Premises No.14, 2nd floor, Sandton City Twin Towers, (East Wing), Sandton, 2196	2 053	2 269	10,51
2	Bank of China Limited Johannesburg Branch (trading as Bank of China Johannesburg Branch)	P O Box 782616, Sandton, 2146	22 440	35 836	59,70
3	Bank of India	P O Box 653589, Benmore, 2010	347	478	38,08
4	Bank of Taiwan South Africa Branch	P O Box 1999, Parklands, 2121	1 420	1 592	12,08
5	BNP Paribas South Africa	Postnet Suite #457, Private Bag X1, Melrose Arch, 2075	2 817	14 499	414,64
6	Canara Bank	11th Floor, Sandton City Office Towers, Cnr 5th Street and Rivonia Road, Sandhurst Ext. 3, Sandton, 2196	299	400	33,58
7	China Construction Bank Corporation – Johannesburg Branch	Private Bag X10007, Sandton, 2146	26 169	32 621	24,65
8	Citibank NA	P O Box 1800, Saxonwold, 2132	48 687	76 511	57,15
9	Deutsche Bank AG	Private Bag X9933, Sandton, 2146	17 300	22 757	31,54
10	HSBC Bank plc – Johannesburg Branch	Private Bag X785434, Sandton, 2146	41 641	49 806	19,61
11	ICICI Bank Limited	Private Bag X785261, Sandton, 2146	–	250	100,00
12	JPMorgan Chase Bank, NA (Johannesburg Branch)	Private Bag X9936, Sandton, 2146	29 745	57 059	91,83
13	Société Générale Johannesburg Branch	P O Box 6872, Johannesburg, 2000	11 573	11 726	1,32
14	Standard Chartered Bank (Johannesburg Branch)	P O Box 782080, Sandton, 2146	32 239	34 420	19,17
15	State Bank of India	P O Box 2538, Saxonwold, 2132	5 006	6 995	39,73

Appendix 2

Registered banks, local branches of foreign banks and mutual banks as at 31 December 2015 (continued)

Registered mutual banks

Institution		Address	Total assets at 31 December		Annual growth (per cent)
			2014 (R millions)	2015 (R millions)	
1	Finbond Mutual Bank	P O Box 2127, Brooklyn Square, 0075	1 422	1 421	–0,04
2	GBS Mutual Bank	P O Box 114, Grahamstown, 6140	1 041	1 136	9,19
3	VBS Mutual Bank	P O Box 3618, Makhado, 0920	362	717	98,15

Banks under curatorship

Institution		Curator	Date of order
1	African Bank Limited	Mr T Winterboer	10 August 2014

Banks in final liquidation

Institution		Liquidator	Date of order
1	Islamic Bank Limited	Mr A D Wilkens of Deloitte & Touche	13 January 1998
2	Regal Treasury Private Bank Limited	Mr T A P du Plessis of D&N Trust and Mr J Pema of Sekela Antrust (Pty) Limited	10 February 2004

Appendix 3

Name changes and cancellation of registration of banks and branches of foreign banks during the period 1 January 2015 to 31 December 2015

Name changes

Previous name	New name	Date of change
None		

Cancellation of registration

Institution	Date of order
None	

Appendix 4

Registered controlling companies as at 31 December 2015

	Institution	Address
1	African Bank Investments Limited	P O Box X170, Midrand, 1685
2	Barclays Africa Group Limited	P O Box 7735, Johannesburg, 2000
3	Bidvest Bank Holdings Limited	P O Box 185, Johannesburg, 2000
4	Capitec Bank Holdings Limited	P O Box 12451, Die Boord, Stellenbosch, 7613
5	FirstRand Limited	P O Box 650149, Benmore, 2010
6	Grindrod Financial Holdings Limited	P O Box 3211, Durban, 4000
7	Investec Limited	P O Box 785700, Sandton, 2146
8	Mercantile Bank Holdings Limited	P O Box 782699, Sandton, 2146
9	Nedbank Group Limited	P O Box 1144, Johannesburg, 2000
10	Sasfin Holdings Limited	P O Box 95104, Grant Park, 2051
11	Standard Bank Group Limited	P O Box 7725, Johannesburg, 2000
12	UBank Group Limited	Private Bag X101, Sunninghill, 2157

The following institutions are deemed to be controlling companies in terms of section 42 of the Banks Act 94 of 1990:

1	Albaraka Banking Group (in respect of Albaraka Bank Limited)	P O Box 1882, Manama, Kingdom of Bahrain
2	Habib Bank AG Zurich (in respect of HBZ Bank Limited)	59 Weinbergstrasse, Postfach, 8042, Zurich, Switzerland
3	National Bank of Greece (in respect of The South African Bank of Athens Limited)	86 Aiolou Street, Athens TT 121, Greece
4	Pitcairns Finance SA (in respect of Habib Overseas Bank Limited)	121, Avenue de la Faiencerie, L-1511 Luxemburg, RCS Luxemburg, B nr 33-106

Appendix 5

Foreign banks with approved local representative offices

	Institution	Address
1	AfrAsia Bank Limited	P O Box 55351, Northlands, 2116
2	African Banking Corporation Botswana Limited (trading as BancABC Botswana)	P O Box 970, Saxonwold, 2132
3	Banco BIC	30 Arena Close, H Santos Building, Bruma, 2198
4	Banco BPI, SA	P O Box 303, Bruma, 2026
5	Banco Nacional De Desenvolvimento Econômica E Social	Illovo Edge, 4th Floor, Building 1, Corner Fricker and Harries Road, Illovo, Sandton, 2196
6	Banco Santander Totta SA	P O Box 309, Bruma, 2026
7	Banif – Banco Internacional do Funchal, SA	P O Box 16838, Bruma, 2026
8	Bank Leumi Le-Israel BM	Private Bag X41, Saxonwold, 2132
9	Bank of America, National Association	P O Box 651987, Benmore, 2010
10	Bank One Limited	P O Box 25386, Gateway, 4321
11	Banque SYZ Suisse SA	P O Box 653641, Benmore, 2010
12	Caixa Bank	Fredman Drive 13, 9th floor, Fredman Towers, Sandton, 2146
13	Commerzbank AG Johannesburg	P O Box 860, Parklands, 2121
14	Credit Suisse AG	Private Bag X9911, Sandton, 2146
15	Doha Bank	P O Box 785553, Sandton, 2146
16	Ecobank	Block F, 8th floor, 135 Rivonia Road, Sandown, 2196
17	Export-Import Bank of India	2nd floor, Sandton City, Twin Towers East Wing, Sandton, 2196
18	First Bank of Nigeria	P O Box 784796, Sandton, 2146
19	Hellenic Bank Public Company Limited	P O Box 783392, Sandton, 2146
20	ICICI Bank Limited	P O Box 78261, Sandton, 2146
21	Industrial and Commercial Bank of China African Representative Office	P O Box 40, Cape Town, 8000
22	KfW Ipex-Bank GmbH	P O Box 2402, Saxonwold, 2132
23	Millenium BCP	P O Box 273, Bruma, 2026
24	Mizuho Bank Limited	P O Box 785553, Sandton, 2146
25	National Bank of Egypt	P O Box 55402, Northlands, 2116
26	Notenstein Private Bank Limited	100 New Church Street, Tamboerskloof, Cape Town, 8001
27	Novo Banco	P O Box 749, Bruma, 2026
28	Société Générale Representative Office for Southern Africa	P O Box 2805, Saxonwold, 2132
29	Sumitomo Mitsui Banking Corporation	Building Four, 1st Floor, Commerce Square, 39 Rivonia Road, Sandhurst, Sandton, 2196
30	Swedbank AB (Publ)	Private Bag X1, Dainfern, 2055
31	The Bank of New York Mellon	PostNet Suite 100, Private Bag X43, Sunninghill, 2157
32	The Bank of Tokyo-Mitsubishi UFJ Limited	P O Box 78519, Sandton, 2146
33	The Mauritius Commercial Bank Limited	P O Box 3009, Parklands, 2121

Appendix 5

Foreign banks with approved local representative offices (continued)

	Institution	Address
34	The Representative Office for Southern and Eastern Africa of the Export-Import Bank of China	Postnet Suite 158, Private Bag X91–BE, Benmore, 2010
35	UBS AG	P O Box 652863, Benmore, 2010
36	Unicredit Bank AG	P O Box 1483, Parklands, 2121
37	Union Bank of Nigeria plc	P O Box 653125, Benmore, 2010
38	Vnesheconombank	P O Box 413742, Craighall, 2024
39	Wells Fargo Bank, National Association	P O Box 3091, Saxonwold, 2132
40	Zenith Bank plc	P O Box 782652, Sandton, 2146

Report on representative offices

1. Introduction

The Regulations relating to Representative Offices of Foreign Banking Institutions (RO Regulations), issued under Government Notice No. 1370, in *Government Gazette* No. 22939 dated 13 December 2001, seek to ensure continuous oversight by the Department, of the activities of representative offices (ROs) of foreign banking institutions operating within the Republic of South Africa.

As at 31 December 2015 there were 40 RO's operating in South Africa, emanating from 22 jurisdictions.

2. Change in status of ROs during 2015

2.1 During the year under review the following ROs were deregistered:

i. Banco Angolano de Investementos
ii. Royal Bank of Scotland PLC

2.2 During the year under review the following ROs were registered:

i. Doha Bank with Mr André Snyman as Chief Representative Officer
ii. Caixa Bank with Mr Jose Maria Segurola Arregui as Chief Representative Officer

2.3 During the year under review the following ROs name changed:

i. Royal Bank of Canada changed its name to Banque SYZ Suisse SA

3. Events after 31 December 2015

ICICI Bank Limited's RO-licence was withdrawn retrospectively with effect from 26 September 2015 since ICICI Bank Limited obtained a banking licence as a registered local branch of a foreign institution.

4. Supervisory approach

In order to fulfill the Department's responsibilities in terms of the RO Regulations it follows the following supervisory approach:

- Regular interaction with the chief representative officers of the respective ROs.
- On-site visits at the offices of the ROs.
- Analysis of returns submitted by the ROs in terms of the RO Regulations and follow-up of any issues identified.
- Analysis of the internal control reports submitted by the ROs on an annual basis in terms of Banks Act Circular 3 of 2004.

Appendix 6

Circulars, directives and guidance notes issued in 2015

Banks Act Circulars issued in 2015

C1/2015	Status of previously issued circulars
C2/2015	Matters related to specified minority interests, i.e. non-controlling interests in shares and/or instruments qualifying as capital
C3/2015	Matters related to specified minority interests, i.e. non-controlling interests in shares and/or instruments qualifying as capital
C4/2015	Matters related to banks' compliance with the prescribed requirements related to the liquidity coverage ratio (LCR) and high-quality liquid assets (HQLA)
C5/2015	Matters related to the use of support in a bank's credit risk-rating process
C6/2015	Proposed amended Regulations relating to Banks
C7/2015	Proposed amended Regulations relating to Banks
C8/2015	Countercyclical capital buffer for South Africa based on the Basel III framework
C9/2015	Proposed amended Regulations relating to Banks

Banks Act Directives issued in 2015

D1/2015	Minimum requirements for the recovery plans of banks, controlling companies and branches of foreign institutions
D2/2015	Effective risk data aggregation and risk reporting
D3/2015	Matters related to the composition of Pillar 3 capital disclosure requirements
D4/2015	Amendments to the Regulations relating to Banks, and matters related thereto
D5/2015	Capital requirements for over-the-counter derivatives not transacted through a central counterparty
D6/2015	Matters related to liquidity risk and the liquidity coverage ratio (LCR)
D7/2015	Restructured credit exposures
D8/2015	Reporting requirements relating to material outsourced service providers and critical third-party service providers
D9/2015	Approval and mapping of the international scale rating symbols of Global Credit Rating Co. (Pty) Ltd to the prescribed risk weights available in terms of regulation 23 of the Regulations relating to Banks.
D10/2015	Matters related to changes to the AMA operational risk management and measurement system used for the calculation of required capital for operational risk
D11/2015	Matters related to revised Pillar 3 disclosure requirements

Banks Act Guidance Notes issued in 2015

G1/2015	Status of previously issued guidance notes
G2/2015	Meetings to be held during the 2015 calendar year with the boards of directors of banks and controlling companies
G3/2015	Application process to adopt the advanced measurement approach (AMA) for measuring banks' operational risk exposure
G4/2015	Expectations of the Bank Supervision Department (BSD) of the South African Reserve Bank (the Bank) with respect to the internal capital adequacy assessment process (ICAAP)
G5/2015	Provision of a committed liquidity facility by the South African Reserve Bank
G6/2015	Training on amended Regulations relating to Banks

Appendix 7

Exemptions and exclusions from the application of the Banks Act 94 of 1990

Section 1(1)(cc): Exemptions by the Registrar of Banks with approval of the Minister of Finance

Exemption Notice	*Government Gazette*	Expiry
Mining Houses	No. 16167 of 14 December 1994	Indefinite
Trade in Securities and Financial Instruments	No. 16167 of 14 December 1994	Indefinite
Commercial Paper	No. 16167 of 14 December 1994	Indefinite
Common Bond	No. 37903 of 15 August 2014	Indefinite
Securitisation Schemes	No. 30628 of 1 December 2008	Indefinite
International Finance Corporation (IFC)	No. 39411 of 13 November 2015	Indefinite

Section 1(1)(dd): Exemptions by the Minister of Finance

Exemption Notice	*Government Gazette*	Expiry
Participation Bond Schemes	No. 13003 of 31 January 1991	Indefinite
Unit Trust Schemes	No. 13003 of 31 January 1991	Indefinite
"Ithala SOC Limited" a wholly owned subsidiary of Ithala Development Finance Corporation Limited	No. 39252 of 2 October 2015	30 June 2016

Section 1(ff): Exemptions by the Registrar of Banks

Exemption Notice	*Government Gazette*	Expiry
Designation of Stockbrokers to pool funds	No. 15976 of 14 September 1994	Indefinite

Section 1(gg): Exemptions by the Registrar of Banks

Exemption Notice	*Government Gazette*	Expiry
Designation of JSE Limited members as persons authorised to accept money as mandatories and to deposit such money into banking accounts maintained by them	No. 19283 of 22 September 1998	Indefinite

Section 2(vii): Exclusions by the Minister of Finance

Exemption Notice	*Government Gazette*	Expiry
Post Office Savings Bank	No. 13744 of 24 January 1992	Indefinite
Industrial Development Corporation of South Africa	No. 16167 of 14 December 1993	Indefinite

Section 78(1)(d)(iii): Exemptions by the Registrar of Banks

Notice	*Government Gazette*	Expiry
Category of assets of a bank that may be held in the name of a person other than the bank concerned	No. 17949 of 2 May 1997	Indefinite

Appendix 8

Approval of applications in terms of section 52 of the Banks Act 94 of 1990 for local banking groups to acquire or establish foreign interests for the period 1 January 2015 to 31 December 2015

Name of controlling company	Date of approval	Name of interest (and percentage interest held, if not 100 per cent)	Domicile
Barclays Africa Group Limited	2015-02-16	Barclays Nigeria Holdings (Pty) Limited	Nigeria
Barclays Africa Group Limited	2015-02-24	Absa Capital Nominees (Pty) Limited	South Africa
Barclays Africa Group Limited	2015-09-16	First Assurance Holdings Limited	Kenya
Barclays Africa Group Limited	2015-09-16	First Assurance Company Limited (63,3 per cent)	Kenya
Barclays Africa Group Limited	2015-10-26	Culemborg Investment Properties (Pty) Limited (67 per cent)	South Africa
FirstRand Limited	2015-01-28	Corvest 200 (Pty) Limited (87,67 per cent)	South Africa
FirstRand Limited	2015-09-03	RMB Nigeria Nominees Limited	Nigeria
FirstRand Limited	2015-09-07	Ashburton Westport Fund Management Limited (25 per cent)	Mauritius
FirstRand Limited	2015-09-07	Ashburton Westport SLP (25 per cent)	Mauritius
FirstRand Limited	2015-10-05	Corvest 10 (Pty) Limited (86,29 per cent)	South Africa
FirstRand Limited	2015-10-14	Motovantage Holdings (Pty) Limited (81,22 per cent)	South Africa
FirstRand Limited	2015-10-14	OPSCO	South Africa
FirstRand Limited	2015-10-14	The Engine Room Direct Solutions (Pty) Limited	South Africa
FirstRand Limited	2015-10-14	Motorite Administrators (Pty) Limited	South Africa
FirstRand Limited	2015-10-14	Motorite Premium Securities (Pty) Limited	South Africa
FirstRand Limited	2015-10-14	Small Area Repair Technology Underwriting Managers (Pty) Limited	South Africa
FirstRand Limited	2015-10-14	Streamline Repairs Holdings (Pty) Limited	South Africa
FirstRand Limited	2015-11-13	Minera Seafield S.A.S.	Colombia
FirstRand Limited	2015-12-03	Atlantic Asset Management (Pty) Limited	South Africa
FirstRand Limited	2015-12-03	Atlantic Specialised Finance (Pty) Limited	South Africa
FirstRand Limited	2015-12-03	Atlantic Point General Partner (Pty) Limited	South Africa
FirstRand Limited	2015-12-03	Atlantic Infrastructure Finance (Pty) Limited	South Africa
Investec Limited	2015-01-30	Ampa Group (Pty) Limited	South Africa
Investec Limited	2015-02-26	Investec Wealth and Investment (Mauritius) Limited	Mauritius
Investec Limited	2015-06-12	Blue Strata Trading (Pty) Limited	South Africa
Investec Limited	2015-06-12	6 Bar Systems (Pty) Limited	South Africa
Investec Limited	2015-06-12	Motion Capital (Pty) Limited	South Africa
Investec Limited	2015-06-12	Brookthyme Investments (Pty) Limited	South Africa
Investec Limited	2015-07-27	Hlano Financial Services (Pty) Limited	South Africa
Investec Limited	2015-10-21	Itec Holdco (55 per cent)	South Africa
Investec Limited	2015-11-27	Business Venture Investments No. 1888 (Pty) Limited	South Africa
Investec Limited	2015-11-27	Business Venture Investments No. 1889 (Pty) Limited	South Africa
Investec Limited	2015-11-27	Business Venture Investments No. 1900 (Pty) Limited	South Africa
Investec Limited	2015-12-08	Investec Specialist Investments (RF) Limited	South Africa
Investec Limited	2015-12-21	Anfa Retail Finance Company	Morocco
Investec plc*	2015-08-25	Investec Investments Limited	United Kingdom

Appendix 8

Approval of applications in terms of section 52 of the Banks Act 94 of 1990 for local banking groups to acquire or establish foreign interests for the period 1 January 2015 to 31 December 2015 (continued)

Name of controlling company	Date of approval	Name of interest (and percentage interest held, if not 100 per cent)	Domicile
Sasfin Holdings Limited	2015-06-26	Fintech (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Fintech Underwriting (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Technologies Acceptances (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Corporate Finance Solutions (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Corporate Finance Solutions Receivables (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	TMS Hasler (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Bontlenyane Holdings (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Fintech Discretionary Fund (Pty) Limited	South Africa
Sasfin Holdings Limited	2015-06-26	Fintech Consumer Collections (Pty) Limited	South Africa
Standard Bank Group Limited	2015-02-02	The Standard Bank Tutuwa Community Foundation NPC	South Africa
Standard Bank Group Limited	2015-02-10	Stanbic Insurance Agency Limited	Kenya
Standard Bank Group Limited	2015-03-27	Liberty Insure Botswana (Pty) Limited (subsequently renamed Liberty General Insurance (Pty) Limited)	Botswana
Standard Bank Group Limited	2015-04-23	SB Wings Development Limited	Nigeria
Standard Bank Group Limited	2015-07-15	Liberty Viewpoint (Pty) Limited	South Africa
Standard Bank Group Limited	2015-07-23	Dotcoza (Pty) Limited	South Africa
Standard Bank Group Limited	2015-09-21	Standard Holdings Cote d'Ivoire S.A.	Cote d'Ivoire
Standard Bank Group Limited	2015-09-21	Standard Bank Cote d'Ivoire S.A.	Cote d'Ivoire
Standard Bank Group Limited	2015-11-13	Total Health Trust Limited	Nigeria
Standard Bank Group Limited	2015-11-30	Greystone Technologies (Pty) Limited	South Africa
Standard Bank Group Limited	2015-12-07	Vinnovations (Pty) Limited	South Africa
Standard Bank Group Limited	2015-12-08	Stanbic Insurance Brokers Zambia Limited	Zambia
Standard Bank Group Limited	2015-12-08	East African Underwriters Limited (51 per cent)	Uganda
Standard Bank Group Limited	2015-11-12	Liberty Life Tanzania Limited	Tanzania
Standard Bank Group Limited	2015-12-10	Exeo Capital (Pty) Limited in Mauritius	Mauritius

* All expansions undertaken by Investec plc were noted by the Bank Supervision Department in terms of the 2002 conditions of approval applicable to the dually listed company structure

Appendix 9

Memorandums of understanding concluded between the Bank Supervision Department of the South African Reserve Bank and foreign supervisors as at 31 December 2015

The purpose of a memorandum of understanding (MoU) is to provide a formal basis for bilateral working relationship and cooperation between supervisors, including the sharing of information and investigative assistance.

It should be noted that any MoU entered into by the Department does not modify or supersede any laws or regulatory requirements in force in, or applying to, the Republic of South Africa. Accordingly, an MoU sets forth a statement of intent and does not create any enforceable rights.

The following MoUs were concluded between the Bank Supervision Department of the South African Reserve Bank and foreign supervisors as at 31 December 2015:

	Domicile of foreign regulator (listed alphabetically)	Foreign banking supervisor	Effective from
1	Argentina	Superintendencia de Entidades Financieras y Cambiarias (Central Bank of Argentina)	18 August 2007
2	Australia	Australian Prudential Regulation Authority	4 July 2007
3	Brazil	Banco Central Do Brasil	4 July 2012
4	China	China Banking Regulatory Commission	17 November 2010
5	Germany	Bundesanstalt für Finanzdienstleitungsaufsicht	13 August 2004
6	Ghana	Bank of Ghana	26 October 2011
7	Guernsey	Guernsey Financial Services Commission	10 July 2015
8	Hong Kong	Monetary Authority of Hong Kong	12 December 2006
9	India	Reserve Bank of India	21 October 2011
10	Ireland	Irish Financial Services Regulatory Authority	21 July 2003
11	Isle of Man	Financial Supervision Commission of the Isle of Man	13 August 2001
12	Jersey	Jersey Financial Services Commission	11 June 2010
13	Kenya	Central Bank of Kenya	1 July 2010
14	Lesotho	Central Bank of Lesotho	27 August 2010
15	Malawi	Reserve Bank of Malawi	20 August 2015
16	Mauritius	Bank of Mauritius	25 January 2005
17	Mozambique	Banco de Mozambique	22 September 2011
18	Namibia	Bank Supervision Department of the Bank of Namibia	21 August 2015
19	Netherlands	De Nederlandsche Bank	23 March 2010
20	Nigeria	Central Bank of Nigeria	20 March 2008
21	Republic of South Sudan	Bank of South Sudan	14 November 2011
22	Swaziland	Central Bank of Swaziland	18 June 2010
23	Taiwan	Financial Supervisory Commission of the Republic of China (Taiwan)	14 March 2012
24	Tanzania	Bank of Tanzania	15 June 2010
25	Uganda	Bank of Uganda	15 June 2010
26	United Arab Emirates	The Dubai Financial Services Authority	8 August 2009
27	United Kingdom*	Financial Services Authority*	21 July 2006

* A letter of intent has been signed between the Bank Supervision Department of the South African Reserve Bank, the Financial Services Authority and Bank of England rendering the terms of the current MoU applicable to the Prudential Regulation Authority and Financial Conduct Authority as may be relevant.

Appendix 9

Memorandums of understanding concluded between the Bank Supervision Department of the South African Reserve Bank and foreign supervisors as at 31 December 2015 (continued)

MoUs with the following foreign supervisors are in the process of negotiation:

Domicile of foreign regulator (listed alphabetically)		Foreign banking supervisor
1	Bahrain	Central Bank of Bahrain
2	Botswana	Bank of Botswana
3	Colombia	Superintendencia Financiera de Colombia
4	France	French Banking Commission
5	Greece	The Banking Regulator
6	Japan	Financial Services Agency
7	Portugal	Banco de Portugal
8	Singapore	Monetary Authority of Singapore
9	Turkey	Banking Regulation and Supervisory Agency of Turkey
10	United Arab Emirates	Banking Supervision and Examination Department of the Central Bank of the United Arab Emirates
11	United States of America	Federal Reserve Bank of New York
12	Zambia	Bank of Zambia

Southern African Development Community – Protocol on Finance and Investment

The 15 Heads of State or Government of the Southern African Development Community (SADC) have signed a Protocol on Finance and Investment (PFI). The PFI, among other things, includes a section setting out the framework for cooperation and coordination in banking regulatory and supervisory matters. The 15 SADC countries are:

- Angola;
- Botswana;
- Congo;
- Lesotho;
- Madagascar;
- Malawi;
- Mauritius;
- Mozambique;
- Namibia;
- Seychelles;
- South Africa;
- Swaziland;
- Tanzania;
- Zambia; and
- Zimbabwe.

Appendix 10

Summary of key matters communicated by the Basel Committee on Banking Supervision

During 2015 the Basel Committee on Banking Supervision (Basel Committee) issued various documents and further requirements that will, over the next few years, materially impact on the regulation and supervision of banks and banking groups, on matters such as:

- revised Pillar 3 requirements;
- revisions to implementation of margin requirements for non-centrally cleared derivatives;
- Basel Committee removes selected national discretions and replies to frequently asked question on funding valuation adjustment;
- net stable funding ratio (NSFR) disclosure requirements finalised by the Basel Committee;
- frequently asked questions (FAQs) on the Basel III leverage ratio framework;
- revised principles on corporate governance for banks;
- guidelines for identifying and dealing with weak banks;
- final criteria for identifying 'simple, transparent and comparable' securitisations;
- Basel III: the standardised approach for measuring counterparty credit risk exposures: frequently asked questions;
- report on the regulatory consistency of risk-weighted assets for counterparty credit risk;
- supporting information for implementation of the countercyclical capital buffer;
- information on global systemically important banks (G-SIBs);
- reports related to total loss-absorbing capacity (TLAC); and
- guidance on credit risk and accounting for expected losses.

Revised Pillar 3 requirements

The Basel Committee issued revised disclosure requirements[1] during January 2015 to address shortcomings in Pillar 3 of the Basel framework. The aim thereof is to facilitate better comparisons of banks' disclosure of risk-weighted assets.

The revised disclosure requirements supersede the existing Pillar 3 disclosure requirements. Banks will be required to publish their first Pillar 3 report under the revised framework concurrently with their year-end 2016 financial reports.

Revisions to implementation of margin requirements for non-centrally cleared derivatives

On 18 March 2015 the Basel Committee and the International Organization of Securities Commissions (IOSCO) released revisions to the framework for margin requirements for non-centrally cleared derivatives.[2]

Following public consultations, the revisions will:

- delay the beginning of the phase-in period for collecting and posting initial margin on non-centrally cleared trades from 1 December 2015 to 1 September 2016;
- institute a six-month phase-in of the requirement to exchange variation margin, beginning 1 September 2016; and
- include a revised phase-in schedule.[3]

Basel Committee removes selected national discretions and replies to frequently asked question on funding valuation adjustment

On 21 April 2015 the Basel Committee published the removal of six national discretion items that were previously included in the Basel II capital framework.[4]

1 Available at http://www.bis.org/bcbs/publ/d309.pdf
2 Available at http://www.bis.org/bcbs/publ/d317.pdf
3 Available at http://www.bis.org/bcbs/publ/d317_summarytable.pdf
4 Available at http://www.bis.org/press/p150421.htm

The Basel Committee noted that the national discretion related to the internal ratings-based (IRB) approach treatment of equity exposures (Basel II capital framework, paragraph 267) will expire in 2016, as the discretion was to apply for a maximum of 10 years from the publication of the Basel II capital framework.

Further, the Basel Committee confirmed that a bank should continue to derecognise its debit valuation adjustment in full, whether or not it has adopted a funding valuation-type adjustment.

Net stable funding ratio disclosure requirements finalised by the Basel Committee

The Basel Committee finalised and published the NSFR standard[5] in October 2014. The final disclosure requirements to this standard were published on 22 June 2015.[6] The objectives of these requirements are to:

- improve the transparency of regulatory funding requirements;
- reinforce the *Principles for sound liquidity risk management and supervision*[7] and strengthen market discipline; and
- reduce uncertainty in the markets as the NSFR is implemented.

Internationally active banks in all Basel Committee member jurisdictions will be required to publish their NSFRs according to a common template, to promote consistency and usability of disclosures related to the NSFR.

Banks will be required to comply with these requirements from the date of the first reporting period after 1 January 2018.

Frequently asked questions on the Basel III leverage ratio framework

The Basel Committee published answers along with some technical elaboration of the standards text and interpretative guidance in response to FAQs during July 2015, to promote consistent global implementation of the Basel III leverage ratio framework and disclosure requirements.[8]

The questions and answers were grouped according to relevant areas:

- criteria for recognition of cash variation margin associated with derivative exposures;
- centrally cleared client derivative exposures;
- exposures and netting of securities financing transactions (SFTs);
- treatment of netting of SFTs and derivatives under a cross-product netting agreement;
- exposure measure under the additional treatment for credit derivatives; and
- treatment of long settlement transactions and failed trades.

Revised principles on corporate governance for banks

On 8 July 2015 the Basel Committee issued *Corporate governance principles for banks*[9] to replace previous guidance, and thereby emphasising the importance of effective corporate governance for the safe and sound functioning of banks. More specifically, the revised principles:

- expand the guidance on the role of the Board of Directors (Board);
- emphasise the importance of the Board's collective competence;
- strengthen the guidance on risk governance, including roles played by different parties of a bank involved in risk management, as well as underline the importance of a sound risk culture to drive risk management within a bank;
- provide guidance for bank supervisors in evaluating the selection processes used by banks regarding board members and senior management; and
- recognise compensation systems as a key component of the governance and incentive structure of a bank.

5 Available at http://www.bis.org/bcbs/publ/d295.pdf
6 Available at http://www.bis.org/bcbs/publ/d324.pdf
7 Available at http://www.bis.org/publ/bcbs144.pdf
8 Available at http://www.bis.org/bcbs/publ/d327.pdf
9 Available at http://www.bis.org/bcbs/publ/d328.pdf

Guidelines for identifying and dealing with weak banks

The Basel Committee originally published *Supervisory guidance on dealing with weak banks*[10] in 2002 and updated it in June 2014.[11] This was replaced with the final *Guidelines for identifying and dealing with weak banks*[12] published by the Basel Committee on 16 July 2015.

Key updates include:

- emphasising the need for early intervention and the use of recovery and resolution tools, and updating supervisory communication policies for distressed banks;
- providing further guidance for improving supervisory processes and reinforcing the importance of sound corporate governance at banks;
- highlighting the issues of liquidity shortfalls, excessive risk concentrations, misaligned compensation and inadequate risk management; and
- expanding guidelines for information-sharing and cooperation among relevant authorities.

Final criteria for identifying 'simple, transparent and comparable' securitisations

OIn December 2014 the Basel Committee and IOSCO published for consultation 14 criteria to identify certain features of simple, transparent and comparable securitisations.

In July 2015, following broad agreement from respondents, the Basel Committee and IOSCO published the final *Criteria for identifying simple, transparent and comparable securitisations*.[13] The purpose of these criteria is to assist the financial industry's development of simple, transparent and comparable securitisation structures. These criteria apply only to term securitisations and are non-exhaustive and non-binding. Criteria promoting simplicity refer to the homogeneity of underlying assets with simple characteristics, and a transaction structure that is not overly complex. Criteria on transparency provide investors with sufficient information on the underlying assets, the structure of the transaction and the parties involved in the transaction, thereby promoting a thorough understanding of the risks involved. The form in which the information is available should not hinder transparency, but should support investors in their assessment. Criteria promoting comparability could assist investors in their understanding of such investments and enable more straightforward comparison between securitisation products within an asset class.

Basel III: The standardised approach for measuring counterparty credit risk exposures: Frequently asked questions

The Basel Committee published FAQs related to the standardised approach for counterparty credit risk (SA-CCR).[14] The SA-CCR will replace both non-internal model approaches, the current exposure method (CEM) and the standardised method SM. The FAQs were published to help ensure consistent global implementation of its standards.

Report on the regulatory consistency of risk-weighted assets for counterparty credit risk

The Basel Committee published a report on the regulatory consistency of risk-weighted assets for counterparty credit risk.[15] The report presents the findings from a hypothetical test portfolio exercise to examine variability in banks' modelling of derivatives, and specifically in exposure modelling. The report focuses on the internal models method and the advanced credit valuation adjustment (CVA) risk capital charge for over-the-counter (OTC) derivative trades. It presents the key findings together with a number of observed good practices.

The report also highlights areas where banks and supervisors may seek to harmonise practices to reduce variability in outcomes. Further, based on the results of this study, the Basel Committee is considering whether it is necessary to narrow down certain modelling choices for banks and/or harmonise supervisory practices to enhance consistency in outcomes.

10 Available at http://www.bis.org/publ/bcbs88.pdf
11 Available at http://www.bis.org/publ/bcbs285.pdf
12 Available at http://www.bis.org/bcbs/publ/d330.pdf
13 Available at http://www.bis.org/bcbs/publ/d332.htm.
14 Available at http://www.bis.org/bcbs/publ/d333.pdf.
15 Available at http://www.bis.org/bcbs/publ/d337.pdf.

Supporting information for implementation of the countercyclical capital buffer

On 19 October 2015, the Basel Committee published FAQs and other information to promote consistent implementation of the Basel III countercyclical capital buffer.[16] The countercyclical capital buffer requirement will be phased in from 1 January 2016.

Information on global systemically important banks

The Financial Stability Board published an updated list of global systemically important banks (G-SIBs) on 3 November 2015[17], which was supported by a publication[18] on the same day by the Basel Committee which provided further information on these banks. This information included:

- a list of all the banks in the assessment sample;
- the denominators used to calculate the scores for banks in the exercise;
- the cut-off score that was used to identify the updated list of G-SIBs;
- the thresholds used to allocate G-SIBs to buckets for the purposes of calculating the specific higher loss absorbency requirements for each institution; and
- links to the disclosures of all the banks in the assessment sample in 2015.

The information was used to assign each G-SIB to a bucket that determines the higher loss absorbency requirement for each G-SIB. The higher loss absorbency requirements will be phased in from 1 January 2016, based on the end-2013 results, with the full amount of the requirement in effect by 1 January 2019, consistent with the implementation schedule for the capital conservation buffer.

Reports related to total loss-absorbing capacity

The Financial Stability Board published its *Principles on the Loss Absorbing and Recapitalisation Capacity of G-SIBs in Resolution and TLAC term sheet* on 9 November 2015.[19] On the same day, the Basel Committee published a consultative document[20] and a quantitative impact study (QIS) report.[21] The QIS report analyses the TLAC levels and shortfalls at G-SIBs based on the FSB's November 2014 consultative version of the TLAC term sheet. Among other things, the TLAC QIS examines the extent that G-SIBs and non-G-SIBs currently invest in TLAC instruments.

Guidance on credit risk and accounting for expected losses

On 18 December 2015, the Basel Committee issued guidelines on credit risk and accounting for expected credit losses (ECL).[22] The guidance sets out supervisory expectations for banks relating to sound credit risk practices associated with implementing and applying an ECL accounting framework. The move to ECL accounting frameworks by accounting standard setters is an important step forward in addressing the weakness identified during the financial crisis that credit loss recognition was not enough. The development of ECL accounting frameworks is also consistent with the April 2009 call by the G-20 leaders for accounting standard setters to "strengthen accounting recognition of loan loss provisions by incorporating a broader range of credit information". The document replaces the Basel Committee's *Sound credit risk assessment and valuation for loans* published in 2006.

16 Available at http://www.bis.org/bcbs/publ/d339.pdf.
17 Available at http://www.fsb.org/http://www.fsb.org/wp-content/uploads/2015-update-of-list-of-global-systemically-important-banks-G-SIBs.pdf.
18 Available at http://www.bis.org/press/p151103.htm.
19 Available at http://www.fsb.org/2015/11/total-loss-absorbing-capacity-tlac-principles-and-term-sheet/.
20 Consultative documents are excluded from the scope of this report.
21 Available at http://www.bis.org/bcbs/publ/d341.pdf.
22 Available at http://www.bis.org/bcbs/publ/d350.pdf.

Abbreviations

AACB	Association of African Central Banks
AEG	Accounting Experts Group
AfDB	African Development Bank
African Bank	African Bank Limited
AMA	advanced measurement approach
AML	anti-money laundering
Banks Act	Banks Act 94 of 1990
Banks Amendment Act	Banks Amendment Act 3 of 2015
BASA	Banking Association of South Africa
Basel Committee	Basel Committee on Banking Supervision
Basel III framework	'Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems' and 'Basel III: International Framework for Liquidity Risk Management, Standards and Monitoring'
BIA	basic indicator approach for operational risk
Board	Board of Directors
CABS	Community of African Bank Supervisors
Capitec	Capitec Bank Limited
CAR	capital adequacy ratio
CCP	central counterparty
CCR	counterparty credit risk
CEM	current exposure method for counterparty credit risk
CFT	combating the financing of terrorism
CMG	Capital Monitoring Group
Core Principles	Core Principles for Effective Banking Supervision
CVA	credit valuation adjustment
Department	Bank Supervision Department of the South African Reserve Bank
Deutsche Bank	Deutsche Bank AG Johannesburg Branch
D-SIB	domestic systemically important bank
ECAI	eligible credit assessment institution
ECL	expected credit losses
ES	expected shortfall
ESAAMLG	Eastern and Southern Africa Anti-Money Laundering Group
FAQ	frequently asked question
FATF	Financial Action Task Force
FIC	Financial Intelligence Centre
FIC Act	Financial Intelligence Centre Act 38 of 2001
FMI	financial market infrastructure
FRTB	fundamental review of the trading book
FSB	Financial Services Board
FSCA	Financial Sector Conduct Authority
FSR Bill	Financial Sector Regulation Bill
GCR	Global Credit Rating Co. (Pty) Limited
G-SIB	global systemically important bank
G-SIFI	global systemically important financial institution
G-20	Group of Twenty
IASB	International Accounting Standards Board
IAS 39	International Accounting Standard 39
ICAAP	internal capital adequacy assessment process
IFRS 9	International Financial Reporting Standard 9
IMA	internal model-based approach for market risk
IMM	internal model method for counterparty credit risk
IOSCO	International Organization of Securities Commissions
IRB	internal ratings-based
IRBA	Independent Regulatory Board for Auditors
IT	information technology
key attributes	Key Attributes of Effective Resolution Regimes for Financial Institutions
KRI	key risk indicator
LCR	liquidity coverage ratio

LGD	loss given default
MoU	memorandum of understanding
NCR	National Credit Regulator
NGL	Nedbank Group Limited
NSFR	net stable funding ratio
OTC	over the counter
PA	Prudential Authority
PDG	Policy Development Group
PFI	Protocol on Finance and Investment
QIS	quantitative impact study
RCAP	Regulatory Consistency Assessment Programme
RCSA	risk control self-assessment
Registrar	Registrar of Banks
Regulations	Regulations relating to Banks
Resolution paper	Resolution Framework Policy paper
RMG	Risk Measurement Working Group
RO	Representative Office
ROA	return on assets
ROE	return on equity
RO Regulations	Regulations relating to Representative Offices of Foreign Banking Institutions
RWA	risk-weighted assets
SA-CCR	standardised approach for counterparty credit risk
SADC	Southern African Development Community
SAICA	South African Institute of Chartered Accountants
SFA	strategic focus area
SIG	Supervision and Implementation Group
SIG-TB	Supervision and Implementation Group Trading Book
SME	small and medium-sized enterprise
SREP	supervisory review and evaluation process
STA	standardised approach for credit risk
TBG	Trading Book Working Group
TFIR	Task Force on Interest Rate Risk
TFSA	Task Force on Standardised Approaches
the Bank	South African Reserve Bank
TLAC	Total Loss Absorbing Capacity
VaR	value at risk
WGC	Working Group on Capital
WGL	Working Group on Liquidity
WGOR	Working Group on Operational Risk