



SOUTH AFRICAN RESERVE BANK
Prudential Authority

Prudential Authority
PRUDENTIAL STANDARD: FLAC INSTRUMENT REQUIREMENTS
FOR DESIGNATED INSTITUTIONS

Consultation Report

December–February 2024 consultation period

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1. Summary of the consultation process

- 1.1 On 7 December 2023 the Prudential Authority (PA) published the following documents for public comment, with the comments due on 19 February 2024:
- (a) Draft Prudential Standard on Flac Instrument requirements for Designated Institutions (Standard);
 - (b) The Statement of need, expected impact and intended operation (Statement of expected impact);
 - (c) Guidance Notice on the Standard (Guidance Notice);
 - (d) the Prudential Communication; and
 - (e) comments templates.
- 1.2 The PA received a total of 87 comments from 4 respondents, broken down as follows:
- (a) 60 comments on the draft Prudential Standard;
 - (a) 16 comments on the Statement of expected impact; and
 - (b) 11 comments on the Guidance Notice.
- 1.3 The full set of comments raised during the consultation process and the responses are detailed in tables 1, 2, 3 and 4 below.
- 1.4 The term Authorities refers to the PA as directed by the Reserve Bank (in its capacity as the Resolution Authority (RA)) as well as the Reserve Bank in its capacity as the RA.

2. Respondent details

No.	Name of the organisation or individual	Name and designation of the contact person(S)	contact details
1.	Capitec Bank Holdings Limited	Anton Friend	AntonFriend@capitecbank.co.za
2.	FirstRand Bank, Group Treasury	Frikkie Kleinhans	Frederik.kleinhans@firstrand.co.za
3.	Standard Bank	Jan Brits	Jan.brits2@standardbank.co.za
4.	Banking Association South Africa (BASA)	Stephen Letsoenya	StephenL@banking.org.za

3. High-level summary of the comments

- 3.1 Table 1 summarises the comments that were received on the Standard and other supporting documentation. The comments in the summary are aggregated into common themes.

Table 1: Summary of the comments consolidated into common themes

Summary of the comments	Response by the Authorities
<p>Theme 1: Extension of timelines to accommodate preparations</p> <p>One respondent proposed that the phase-in of Flac requirements be extended beyond 2025 and 2027 to cater for the following, among other reasons:</p> <ul style="list-style-type: none"> a) requirements to create or update medium-term note (MTN) programmes; and b) various board and regulatory approvals must follow, together with JSE listing, legal work and other requirements. 	<ul style="list-style-type: none"> a) The Authorities appreciate that Flac requirements are a new requirement over and above the minimum regulatory capital requirements (with Basel III finalisation). Therefore, in calibrating the phase-in period, which is in line with international standards, the Authorities considered the following to provide designated institutions (DIs) with some headroom and flexibility: <ul style="list-style-type: none"> • The minimum Flac requirement (MFR) will, from the onset, only comprise one component (the bMFR), with

Summary of the comments	Response by the Authorities
	<p>the second component (the iMFR) being implemented at a later stage.</p> <ul style="list-style-type: none"> • Although the phase-in period for the bMFR is six years, the reporting requirements will only start in the third year after the implementation date. • The banks designated as systemically important financial institutions (SIFIs) have the option to fulfil the MFR with Flac instruments only or to issue the minimum required amount of Flac instruments and use 'available' excess regulatory capital to meet the difference. • The minimum amount of Flac instruments required (33.33% of total loss-absorbing capital (TLAC)) will also be phased in over the six-year period (with reporting requirements starting in year 3).
<p>Theme 2: Basel III reforms, including CCyB</p> <p>Respondents raised concerns regarding the impact of Basel III reforms on the industry and how they interplay with the Flac requirements.</p> <p>a) Three respondents raised the concern that the positive cycle-neutral (PCN) countercyclical buffer (CCyB) requirement of 1% (effective from 1 January 2026) will shrink the excess regulatory capital that could be used to contribute towards the MFR as a top-up.</p>	<p>a) Response to (a) and (b)</p> <p>b) The primary mechanism to fulfil the MFR is Flac instruments. The fact that the Standard provides for DIs to be able to use 'available' excess regulatory instruments to meet the difference does not mean that the Authorities require the DIs to do so. The DI will have the discretion, in accordance with the Standard's requirements, to determine the composition it deems suitable to fulfil its Flac requirement.</p> <p>c) Response to (c) and (d)</p>

Summary of the comments	Response by the Authorities
<p>b) Respondents also sought clarity as to whether the CCyB was considered in calculating the excess regulatory capital in the ex-ante impact study.</p> <p>c) One respondent raised concern on the implementation of output floors which could increase the risk-weighted assets (RWA) densities by as much as ~10% by 2030 (equivalent to a relative increase in RWA of ~23%), resulting in a point-in-time estimated increase in MFR of ~23% which will culminate in increased funding costs.</p> <p>d) One respondent proposed that the floor add-ons be excluded from the risk-weighted exposure used to derive the Flac calibration levels.</p> <p>e) One responded requested a Quantitative Impact Study (QIS) to be performed on all the in-flight prudential regulatory changes to better reflect the impact of the Flac requirements</p>	<ul style="list-style-type: none"> With regard to the other Basel III post-crisis reforms, the PA has published the relevant impact assessments that have been conducted. The latest reports published towards the end of 2023 include a report that also covered the impact of the output floor. The findings from the data collected from the industry paints a slightly different picture from what has been advanced by this comment. The PA's findings do not support the same magnitude of impact. In addition, the RA (responsible for setting the Flac requirements) does not have the mandate to change the minimum capital requirements set by the PA, but rather to ensure that the DI will be able to recapitalise to a level that ensures that the PA will allow the DI to continue operating and, in addition, to provide the market with confidence so that counterparties can continue trading with the DI, post resolution. Therefore if the PA requires add-ons to adequately provide for the level of risk related to a particular DI, Flac requirements have to 'mirror' the minimum regulatory requirements to ensure the DI can be adequately recapitalised in resolution. <p>d) Response to (e)</p> <ul style="list-style-type: none"> The PA endeavours to consider the cumulative impact of all proposed amendments to regulations. However,

Summary of the comments	Response by the Authorities
	challenges remain due to the timing and sequencing of regulations.
<p>Theme 3: Intermediate holding company</p> <p>a) Two respondents requested clarity on whether issuances out of an intermediate holding company (IHC) would meet the requirement of the Holding Company issuing Flac instruments externally.</p> <p>b) In addition, one responded recommended greater flexibility with regard to the entity that will issue Flac instruments externally (i.e. external issuance to be from Holding Company or the Operating Company) in order to satisfy possible future requirements for loss-absorbing capacity in markets, other than South Africa.</p>	<p>a) The revised final Standard clarifies that Flac instruments must be issued externally out of the 'ultimate' holding company and not the 'intermediate' holding company where such a structure is present.</p> <p>b) The Authorities clarified that the Standard is applicable to SIFI banks and their 'ultimate' holding companies within the South African (SA) jurisdiction. In addition, the Standard does not preclude loss-absorbing requirements by other host regulators in as far as those instruments (if issued externally by the SA 'ultimate' holding company) are not double counted (i.e. counted as Flac instruments under the SA requirements as well as loss-absorbing instruments to meet the host regulators requirements).</p>
<p>Theme 4: Investor mandates</p> <p>a) Three respondents raised concern regarding the investor mandates, specifically whether these mandates will allow investors to buy this convertible debt instrument (i.e. Flac instruments).</p>	<p>a) The Authorities view the investor mandates as part of the process to operationalise the Standard.</p> <p>b) The Authorities have engaged the investor community and will continue to do so. In addition, the Authorities continue to engage various relevant stakeholders (both internally and externally) to facilitate a smooth operationalisation process.</p>
<p>Theme 5: Conversion of Flac instruments</p>	

Summary of the comments	Response by the Authorities
<p>a) One respondent sought clarity on whether the treatment of Flac instruments will be more of a conversion than a write-off (as opposed to capital instruments which mostly make provision for a contractual write-off). They further commented that if Flac will be more of a conversion then banks will need to make provision to allow for sufficient authorised but unissued shares to be made available (which may require AGM approval).</p> <p>b) One responded requested clarity on the following:</p> <ul style="list-style-type: none"> • whether the SARB would allow the conversion of Flac instruments into other classes of more subordinated debt (i.e. convert Flac into AT1 and T2 instruments as well instead of just CET1); • whether the term ‘shareholders’ equity’ in the powers to bail-in includes preference shares (when referring to the conversion of Flac instruments into shareholders equity); and • confirmation as to whether preference shares can be counted as excess regulatory capital (i.e. preference shares that do not meet regulatory capital). <p>c) One respondent requested that unappropriated profits be allowed to account as excess regulatory capital for Flac purposes (even though for capital management purposes unappropriated profits do not count as regulatory capital until they are appropriated).</p>	<p>a) The Authorities clarified that the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (FSR Act) empowers the Reserve Bank to enter into any transaction, in relation to a DI in resolution, despite any law or agreement that would otherwise restrict or prevent it, including any law or agreement that requires consent or approval from specific persons.</p> <p>b) The Authorities provided the following clarification:</p> <ul style="list-style-type: none"> • The FSR Act provides the RA with powers to substitute (convert) unsecured liabilities into shareholders’ equity (and not other types of regulatory instruments such as debt instruments that qualify as regulatory capital). In addition, although the term ‘shareholders’ equity’ includes both ordinary and preference shares, the RA’s preference is to convert the unsecured liabilities into ordinary shares in a statutory bail-in. • Regarding preference shares and unappropriated profits that currently do not qualify as regulatory capital, the Authorities provided clarity that, as required by the Standard, instruments that can be used as a top-up must qualify as excess regulatory capital. In addition, that excess regulatory capital must not be used to contribute towards the minimum required regulatory capital.

Summary of the comments	Response by the Authorities
<p>Theme 6: Flac Characteristics</p> <p>a) Two respondent sought further guidelines on the initial terms to be approved by the SARB, specifically timelines and turnaround times for the approval process.</p> <p>b) One respondent requested that the notification to be provided to the SARB regarding subsequent issuances be given after the actual issuance has taken place (instead of prior to issuance).</p> <p>c) One respondent raised the following comments:</p> <ul style="list-style-type: none"> The minimum remaining period of 12 months is too penal (this will necessitate frequent issuances or longer term Flac instruments with higher costs) and it is recommended to introduce the T2 step-down approach. 	<p>a) The Authorities will endeavour to expediently and efficiently review the terms and conditions as soon as they are received.</p> <p>b) The Authorities clarified that the notification prior to the issuances serves a broader financial stability monitoring purpose and is not limited to Flac instrument issuances for a particular DI.</p> <p>c) The Authorities highlighted that, to implement the T2 step-down approach, T2 instruments need to be issued for a minimum period of five years. Since Flac instruments do not have a step-down approach but require a minimum remaining period of 12 months (and an initial maturity of 24 months), the Flac instrument criteria provide the DIs with more flexibility around the tenure of the instruments, as long as the minimum remaining period is met. The prescription of a higher minimum maturity period (i.e. five years) for Flac instruments could take away the flexibility and demand higher costs for the DI.</p>
<p>Theme 7: Application of the Standard</p> <p>a) Two respondents sought clarity on whether Flac is applicable at bank solo or bank consolidated level.</p>	<p>a) The Authorities clarified that Flac is only required for SA SIFI banks on a standalone basis, including foreign branches.</p>

Summary of the comments	Response by the Authorities
<p>Theme 8: Overall cost burden</p> <p>b) One respondent raised a comment regarding the overall cost burden to industry, not only in the form of interest costs and resources to calibrate the Flac requirements.</p> <p>c) Another respondent also raised concern on the internal structure changes to accommodate resolution requirements.</p> <p>d) Another respondent raised concern that the overall domestic investor pool might be a potential constraint and foreign issuances will come with added costs.</p>	<ul style="list-style-type: none"> • The Financial Stability Board's (FSB) Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attributes) (which include adequate loss-absorbing capacity through Flac instruments) endeavour to minimise the impact on financial stability, ensure criticality of economic functions and avoid exposing taxpayers to loss. • The Authorities need to balance the risks posed by the failure of a systemically important DI on financial stability as well as the fiscus, and the cost to industry to mitigate these risks. • Therefore, the Authorities acknowledge that a cost will be borne by industry to implement the FSB Key Attributes and thus consulted industry extensively on the Flac requirements. In addition, the Authorities implemented industry feedback which resulted in changes to the proposals set out in the 2021 discussion paper, including the increased use of excess regulatory capital as a top-up and a change in the calibration of the MFR.

Table 2: Full set of comments received on the draft Prudential Standard

No.	Commentator	Paragraph	Comment	Response
1. Commencement				
1.	FirstRand	Section 1.1	<p>The proposed commencement date of January 2025 coincides with other regulatory changes (proposed implementation of the final Basel reforms and the proposed cycle-neutral countercyclical buffer (PCN CCYB) requirement in 2025). Given the impact of these new requirements on the levels of capitalisation for the bank, and therefore the Flac calibration, it is proposed that the implementation and transition of the Flac requirement be extended beyond 2025 and 2027, respectively. It is generally expected that the final Basel reforms will change risk-weighted assets (RWA), while the proposed PCN CCYB will lift the total loss-absorbing capacity (LAC) requirement given the increased capital requirement (against which the 33% minimum Flac is calibrated) and reduce the surplus (CREG) that can be used to meet the 'top up' Flac requirement. The PCN CCyB can remove as much as R9 billion for FirstRand Bank and is considered to be material from a planning perspective.</p> <p>In addition, the Resolution Authority has only recently initiated the resolution planning process after officially being granted the necessary resolution powers contained in the FSLAA. Considering the level of work and development required to have workable</p>	<p><i>Regulatory capital requirements and Flac requirements serve different purposes.</i></p> <p><i>Regulatory capital takes care of capital requirements on a going-concern basis, while Flac takes care of recapitalisation capacity in the event of a resolution. In the case of a failure of a systemically important DI, the consequences could be severe to the extent of negatively impacting financial stability due to the size, complexity, interconnectedness, contagion effects etc.</i></p> <p><i>In considering the phase-in period, which is in line with international standards, the Authorities considered the following:</i></p> <p><i>1. The phase-in period is over six years; however, the reporting requirements only start in the third year after the implementation date.</i></p> <p><i>2. The requirements from the onset will only comprise of one component (the bMFR) with the second component (the iMFR) to be implemented at a later stage.</i></p> <p><i>3. The SIFI banks have the option to fulfil the minimum Flac requirement (MFR) with Flac instruments only or to issue the minimum required amount of Flac instruments and use 'available' excess regulatory capital to meet the difference.</i></p>

			<p>resolution plans in place, including structure changes required to facilitate effective resolution planning, enhancements required to meet the new resolution standards (currently RA01, RA02 and RA03) and reliable resolvability assessments, which will impact the Flac calibration, we feel this supports the above proposal for the implementation and transition of the Flac requirement to be extended beyond 2025 and 2027, respectively.</p> <p>Requirements to create or update medium term note (MTN) programmes (to allow for the issuance of these instruments) are extensive. Various board and regulatory approvals must follow, together with JSE listing, legal work and other requirements. If it is the intention to offer these instruments offshore, a European MTN must also be created. Significant investor work, together with changes to fund mandates, have to be effected before issuance can commence.</p> <p>From a FirstRand perspective, capital planning is performed on a three-year forward-looking basis, and regulatory updates are incorporated once near-final assessments are available. Given additional lack of final certainty on Basel reforms (areas of national discretion) and PCN CCyB, a delay of at least 12 to 18 months in the implementation of the Flac standard (together with the commensurate transition dates), will not only allow banks to appropriately incorporate the new changes without a disruption to normal capital</p>	<p><i>4. The minimum amount of Flac instruments required (33.33% of TLAC) will also be phased in over the six-year period (with reporting requirements only starting from the third year after the implementation date).</i></p> <p><i>The Authorities need to balance the risks posed by the failure of a systemically important DI on financial stability as well as the fiscus, and the cost to industry to mitigate these risks.</i></p>
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			planning and business origination, but also allow for investor work to ensure updated mandates and fair pricing for instruments that will be issued in very large quantities over the next few years.	
2. Legislative Authority				
3. Definitions and interpretations				
2.	Capitec	‘post-resolution or post-loss balance sheet’ means the DI’s balance sheet calculated by deducting the losses incurred (before and in resolution) from its assets, according to the risk weights assigned to the relevant assets in terms of the bank’s capital adequacy legislation	<p>The post-loss balance sheet assumes that the point-in-time regulatory capital buffers have reduced to zero. The going concern effective risk-weight percentage is then applied to the post-loss balance sheet to determine the final Flac requirement.</p> <p>The point of non-viability (PONV) would theoretically be triggered before the point of resolution (POR). At the PONV, a bank’s recovery actions may include the sale of certain predefined assets. Consideration should be given in the definition of the post-loss balance sheet and effective risk weights where the sale of these recovery assets are a key component of the recovery plan.</p>	<p><i>In an event where the PONV occurs before the POR, and the viable recovery options were implemented, the updated balance sheet at the POR should already account for the implemented recovery options and the related risk weightings.</i></p> <p><i>It is not possible to estimate the impact of potential implementation of recovery options without the guarantee as to whether the recovery options will be viable or not under the particular stress scenario.</i></p>
3.	FirstRand	Section 3.1	<p>Refers to issuance by the holding company of the designated institution. Clarity is required on whether external issuance by an intermediate holding company would also comply with this requirement.</p> <p>To note that the intermediate holding company will be the holding company of the designated institution.</p>	<p><i>The Authorities require the Flac instruments to be issued externally by the ultimate holding company, not the intermediate holding company (where such a structure is present).</i></p> <p><i>The Standard has been amended to provide this clarity.</i></p>

4.	Standard Bank	Paragraph 3.1 and Paragraph 8.2(a)	<p>The standard requires external Flac to be issued by the holding company of designated institutions. Market access, at holding company level, for Flac instruments in certain emerging market currencies (if required in future) may be limited, while pre-positioning of loss absorbency capacity in, for example, USD may not match local funding requirements or satisfy regulatory rules with respect to funding in non-local currencies.</p> <p>We recommend greater flexibility (considering individual resolution plans) with respect to issuance entity requirements to satisfy possible future requirements for loss absorbing capacity in other markets than South Africa. In this regard, we note the EU application that allows banks to issue Flac equivalent instruments from either OpCo or HoldCo.</p>	<p><i>The Standard is applicable to SIFI banks and their holding companies within the SA jurisdiction.</i></p> <p><i>This requirement for SA SIFI banks and their holding companies does not preclude any other host jurisdiction requiring the entities within their relative jurisdictions to hold loss-absorbing instruments. However, DIs must ensure that those instruments (if issued externally by the SA ultimate holding company) are not double counted (i.e. counted as Flac instruments under the SA requirements as well as to meet other loss absorbency requirements by host jurisdictions).</i></p>
5.	BASA	3.1 Definition: 'additional Flac requirement'	<p>We propose the following amendment to the definition to add clarity to the term and to align to other definitions which will mitigate misinterpretation:</p> <p><i>['additional Flac requirement' refers to the additional amount of Flac instruments (and/or other qualifying instruments) to be held over and above the <u>base</u> minimum Flac requirement, in terms of this Standard or a Determination issued by the Prudential Authority or the Reserve Bank;]</i></p>	<p><i>The definition for additional Flac requirement has been amended to provide clarity and it now reads as follows:-</i></p> <p><i>'additional Flac requirement' refers to the additional amount of <u>Flac instruments or Flac instruments and other qualifying instruments</u> to be held over and above the base minimum Flac requirement, in terms of this Standard or a Determination issued by the PA or the Reserve Bank.</i></p>
6.	BASA	3.1 Definition: 'base Flac requirement'	<p>Beyond the definition section, the term 'base Flac requirement' is not used to in the rest of the Standard, but rather 'base minimum Flac requirement' is used.</p> <p>We propose that the definition be amended to align to the rest of the standard. In addition, we also propose</p>	<p><i>The Standard has been amended as follows:</i></p>

			<p>an amendment to the definition to include the scenario where the bMFR is composed of both Flac instruments and other qualifying instruments (i.e. excess regulatory capital) as follows:</p> <p><i>['base minimum Flac requirement' refers to the required minimum amount of Flac instruments and/or other qualifying instruments, to be held by all the relevant designated institutions;]</i></p>	<p><i>1.the Standard now refers to the 'base minimum Flac requirement' consistently instead of using 'base Flac requirement' as well.</i></p> <p><i>2.the definition for the 'base minimum Flac requirement' is amended to state that it refers to the minimum amount of Flac instruments or Flac and other qualifying instruments, to be held by all relevant DIs.</i></p>
7.	BASA	3.1 Definition: 'total loss-absorbing capacity'	<p>The definition for 'total loss-absorbing capacity' is defined in the context of calibrating the minimum amount of Flac instruments that need to be issued to meet MFR.</p> <p>In reality, however, the DI's total loss-absorbing capacity will include all regulatory capital instruments (including both excess regulatory capital and all regulatory buffers) as well as Flac instruments (i.e. TLAC = total qualifying amount of capital and reserve funds + Flac instruments), which also aligns to the definition of 'loss-absorbing capacity' defined in RA03: <i>['loss-absorbing capacity' refers to the eligible instruments, minimum regulatory capital and instruments that otherwise qualify as regulatory capital held by designated institutions that are able to absorb losses in resolution;].</i></p> <p>We propose differentiating between loss-absorbing capacity for the purpose of calibrating the minimum Flac instruments requirement (which will exclude regulatory buffers and, in most cases, a portion of excess regulatory capital) and actual total loss-absorbing capacity of the institution (which will include regulatory buffers and all excess regulatory capital).</p>	<p><i>The Authorities disagree with the recommendation.</i></p> <p><i>The term total loss-absorbing capacity (TLAC) is a term that originated from the Financial Stability Board (FSB), which includes both the loss absorbing and recapitalisation capacity.</i></p> <p><i>TLAC, however, excludes regulatory buffers (capital buffer requirements (CBR)) as those buffer requirements must be usable in line with Basel III requirements. In addition, TLAC does not incorporate excess regulatory capital, as that portion of capital is not a minimum requirement by the regulator.</i></p>

			<i>['total loss absorbing capacity for Flac calibration purposes'] refers to the sum of the minimum required amount of capital and reserve funds (prior to buffers) and the minimum Flac requirement, used for loss absorption and recapitalisation capacity;]</i>	
8.	BASA	3.1 Definition: 'core business lines'	There is no reference to core business lines in the draft standard. Suggest removal of the definition.	<i>Core business lines definition has been removed</i>
9.	BASA	3.1 Definition: 'Board'	Suggest including the cross reference to the Companies Act, 2008.	<i>'The Board' is a commonly understood term and therefore does not need to be referenced/defined further.</i>
10.	BASA	Definition: 'excess regulatory capital'	<p>From the definition of excess regulatory capital (extracted below for ease of reference), we note that excess regulatory capital is defined as qualifying capital in excess of the minimum amount of capital, including the regulatory buffers (the countercyclical, conservation and D-SIB buffer).</p> <p><i>'Excess regulatory capital' refers to the difference between the total minimum required amount of capital and reserve funds including countercyclical, conservation and Domestic Systemically Important Bank (DSIB) buffers) and the total qualifying amount of capital and reserve funds as specified in the bank's capital adequacy legislation.</i></p> <p>Given the publication of the proposed directive on the implementation of a positive cycle-neutral countercyclical capital buffer (PcN CCyB) of 1% with effect from 1 January 2026, we note that this will directly impact on the amount of excess regulatory capital available to DIs to use to 'top-up' MFR requirements, which could potentially have a 'double-buffer' effect to the extent that the excess regulatory</p>	<i>The primary mechanism to fulfil the MFR is Flac instruments. The fact that the Standard provides for DIs to use 'available' excess regulatory instruments to meet the difference, does not mean that the Authorities require the DIs to do so. The DI will have the discretion, in accordance with the Standard's requirements, to determine the composition it deems suitable to fulfil its Flac requirement.</i>

			<p>buffer is eroded and additional Flac instruments are required as to ensure that MFR (or bMFR) is met.</p> <p>To the extent that the binding constraint of Flac $\geq 33.33\%$ of TLAC allows for the utilisation of excess regulatory capital as MFR, noting that a 1% decrease in excess regulatory capital could, for more than one SIFI, directly result in additional Flac requirements, having a 'double-buffer' effect and increasing the funding costs of the organisation, despite TLAC ratios estimated to reach international GSIB levels by the end-state of implementation.</p> <p>We propose that the consequential impact of the PCN CcyB on the industry Flac requirement be considered to ensure that there are no unintended consequences in terms of increasing buffers and increasing funding costs.</p>	
11.	BASA	Definition: 'post-resolution or post-loss balance sheet'	<p>We note that the post-resolution balance sheet is calculated using the going concern RWA densities as per the definition below (extracted for ease of reference):</p> <p>'post-resolution or post-loss balance sheet' means the designated institution's balance sheet calculated by deducting the losses incurred (before and in resolution) from its assets, according to the risk weights assigned to the relevant assets in terms of the bank's capital adequacy legislation.</p> <p>We further estimate the upcoming Basel reforms and the implementation of the output floors could increase RWA densities by as much as ~10% by 2030 (equivalent to a relative increase in RWA of ~23%), resulting in a point-in-time estimated increase in MFR of ~23% which will culminate in increased funding costs and could potentially result in excess market</p>	<p><i>The events of a stress scenario that will lead to a resolution is unknown. Therefore, without knowing how the balance sheet of the DI might change or the potential change in the riskiness of the assets, it is prudent to use the current RWAs and RWA densities.</i></p> <p><i>The output floor Basel III reform seeks (among other things) to mitigate model abuse, to ensure that an adequate amount of capital (which reflects the riskiness of the assets) is held for going-concern purposes.</i></p> <p><i>Similarly the PCN CCyB buffer is a Basel III requirement for going-concern purposes.</i></p> <p><i>Flac requirements aim to deal with the consequences of a DI that has failed or is</i></p>

			<p>supply where the required Flac issuance volume could potentially exceed demand for Flac instruments.</p> <p>We propose that the implications of the Basel III reforms be considered to mitigate any unintended consequences, particularly when considered in conjunction with the proposed introduction of the PCN CcyB buffer of 1%. The cost of maintaining TLAC ratios above that of international G-SIB requirements will have significant cost implications that will inevitably make its way through to the real economy.</p>	<p><i>likely to fail (and thus no longer a going concern) and seeks to ensure that the failure of that DI does not negatively impact financial stability and avoids exposing taxpayers to loss.</i></p>
4. Roles and responsibilities				
5. Application				
12.	BASA	Par 5.1 & Par 11	<p>Par 5.1 notes the Standard applies to banks which have been designated as SIFIs and their holding companies. Par 11 defines the minimum Flac requirement (MFR). Please confirm whether the MFR is calculated considering the Bank Consolidated or Standalone (i.e. Solo) capital requirements of each of the designated institutions. By way of an example, a Bank classified as a SIFI has foreign subsidiaries that are not subject to Flac in their respective jurisdictions. Would the MFR be calculated considering the total asset, RWA and minimum capital adequacy requirements of the Bank Solo or Bank Consolidated?</p>	<p><i>Flac is only required for SA SIFI banks on a standalone basis (including foreign branches).</i></p>
13.	BASA	Par 5.2	<p><i>Any reference to a designated institution in this Standard, only refers to institutions defined under paragraph 5.1.</i></p> <p>Suggest that the definition of designated institution be consistent in all standards as per the definition in the FSR Act.</p> <p>Recommend using the terminology introduced in the 2020 discussion paper titled 'Group structure reporting requirements for resolution planning' where</p>	<p><i>Comment noted.</i></p>

			the term Resolution Group and Resolution Entity are defined. If the SA SIFI is deemed a 'resolution entity' and the only resolution entity that will be in scope for the purposes of calculating the Flac requirement, the rest of the paper will be clearer.	
6. Principles on loss-absorbing and recapitalisation capacity				
14.	FirstRand	Section 6.4	<p>Currently, most of the capital instruments issued by banks make provision for the contractual write-off of instruments (although it is still at the discretion of the PA that these instruments be converted into equity). To allow for the conversion into equity, banks are required to carry enough authorised but unissued shares.</p> <p>Given that Flac is mostly a recapitalisation instrument (rather than absorption of losses as is the case with equity and other capital instruments), is it the intention that banks will have to rather make contractual provision for the conversion of Flac instruments as opposed to write-off?</p> <p>To enable this, banks will have to ensure that enough authorised but unissued share capital is available, which may require AGM approval.</p> <p>In the example where Flac meets a minimum 33% of the TLAC requirement and the remainder is met with, say, other Tier 2 capital instruments, will it provide a</p>	<p>Authorised but unissued shares <i>Section 166S(1) of the FSR Act states that if the Reserve Bank deems it necessary for an orderly resolution, the DI in resolution can enter into a particular transaction despite any law or agreement that would otherwise restrict or prevent it including any law or agreement that requires consent or approval from specific persons.</i></p> <p><i>In a resolution scenario, the Reserve Bank as the RA (not the DI itself) will make the conversion or write-off of instruments and therefore the Reserve Bank does not need to comply with any law or agreement to do so.</i></p> <p>Fair outcome to instrument holders with the same ranking:</p> <p><i>Section 166U(4)(a)-(c) of the FSR Act states that the Reserve bank will treat creditor claims that have the same ranking in the insolvency equally, unless it</i></p>

			<p>fair outcome to all Tier 2 investors (where some of the instruments are written off, and other instruments converted into equity)? In the extreme scenario, some Tier 2 investors may be in the same position as Flac investors (post conversion) even though a larger perceived risk premium has been taken by the Tier 2 investors. Additional guidance on the treatment would support greater investor understanding and education.</p>	<p><i>determines that it is necessary to treat the claims differently to effect an orderly resolution.</i></p> <p><i>Therefore, as a first step, the principle of parri-passu will be applied to instruments that have the same ranking.</i></p> <p><i>In addition, the Reserve Bank will apply the No Creditor Worse Off than in Liquidation (NCWOL) rule as per section 166V of the FSR Act, to ensure that no resolution action would result in a shareholder or creditor receiving less than they would have, if the DI had been wound up.</i></p> <p><i>This process may involve conversion rates to ensure fair compensation; however, the intention is to provide detail and guidance around these aspects during the operationalisation phase, post the promulgation of the Standard.</i></p>
15.	BASA	6.4 Principles of loss-absorption and recapitalisation in resolution and 2.3 Statement of need	<p><u>Paragraph 6.4:</u></p> <p><i>Statutory bail-in enables the Reserve Bank to perform the following actions, in a manner that respects the creditor hierarchy -</i></p> <p><i>(a) write-down shareholders' equity and unsecured subordinated debt instruments to the extent necessary to absorb losses; and</i></p> <p><i>(b) convert all or parts of unsecured debt instruments into shareholders' equity to recapitalise the designated institution in resolution.</i></p>	<p><i>Section 166T of the FSR Act provides the RA with powers to substitute (convert) unsecured liabilities into shareholders' equity (and not other types of regulatory instruments such as debt instruments that qualify as regulatory capital). In addition, although the term 'shareholders' equity' includes both ordinary and preference shares, the RA's preference is to convert the unsecured liabilities into ordinary shares in a statutory bail-in.</i></p>

			<p>Comment:</p> <p>Paragraph 6.4 (b) states that unsecured debt instruments will only be converted into shareholders equity (CET1) to recapitalise the bank and does not mention the ability / power of the Reserve Bank to convert subordinated debt instruments into other forms of capital instruments such as AT1 (additional Tier1) or T2 (Tier 2) instruments.</p> <p>During the bail-in process, if subordinated debt instruments are only converted into CET1, the bank will be recapitalised with only CET1, having no AT1 or Tier2 instruments immediately following the bail-in process. This will result in a CET1 at > 9%, which will be proportionally mis-aligned with its peers and will significantly increase the weighted average cost of capital.</p> <p>Assuming 0% Pillar 2B (for the sake of simplicity, given the confidential nature of Pillar2B requirements), the capital adequacy legislation allows for the ~9% MinCAR to comprise of 5,0% CET1 + 1.75% AT1 + 2,25% Tier2.</p> <p>In this instance, recapitalisation to the minCAR of 9%, as per paragraph 6.4 will result in a bank that is capitalised at [9% CET 1 + 0% AT1 + 0% Tier2] with reduced Flac holding, effectively increasing the weighted cost of capital, and placing the bank in a competitive disadvantage relative to peer banks.</p> <p>Consequently, the bank will not be optimally capitalised and will therefore incur excessive funding costs at a critical point in time following the bail-in weekend. This could result in an unsustainable capital</p>	
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			<p>stack where the weighted average cost of capital will exceed that of its peer banks.</p> <p>It could be beneficial for the Regulator to have at its discretion, the ability to recapitalise the bank with not only CET1, but also with other capital instruments to allow the bank in resolution the best possible opportunity of recapitalising to an optimal, sustainable capital structure, in line with the allowances made for AT1 and Tier 2 instruments in the bank's capital adequacy legislation.</p> <p>This will also promote the objective stated in paragraph 2.2 of the 'Statement of need on Flac' that <i>"Recapitalisation through bail-in must enable a designated institution (DI) to continue operating during a resolution and to exit resolution as a viable entity. This requires the recapitalisation to be sufficient to restore the capital levels of a DI to meet regulatory capital requirements (as set out in the Regulations relating to Banks or prudential standards that deal with a bank's capital adequacy (bank's capital adequacy legislation)) and restore the confidence of the market that a DI can continue to successfully conduct business."</i></p> <p>To allow for the conversion of subordinated debt instruments into a more subordinated instrument (i.e. Flac to be converted into either T2, AT1 or CET and potentially for Tier2 to be converted into either AT1 or CET1), we propose the following amendment to paragraph 6.4, point (b):</p> <p><i>"Statutory bail-in enables the Reserve Bank to perform the following actions, in a manner that respects the creditor hierarchy -</i></p>	<p><u>Clarity questions</u></p> <p>Reduced claims:</p> <ul style="list-style-type: none"> Reduced claims do not include conversion to a more subordinated instrument. <p>Cancellation of instruments: As the definition states, the action will result in the following:</p> <ul style="list-style-type: none"> the value of instruments and/or claims held by shareholders and creditors of the DI being reduced;
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			<p>(a) write-down shareholders' equity and unsecured subordinated debt instruments to the extent necessary to absorb losses; and</p> <p>(b) convert all or parts of unsecured debt instruments into shareholders' equity or a lower more subordinated instrument to recapitalise the designated institution in resolution."</p> <p>Furthermore, we note that Section 3.1 defines 'Bail-in' as a resolution action taken by the Reserve Bank, in terms section 166S and section 166T of the Act, that results in the value of instruments and/or claims held by shareholders and creditors of the designated institution reduced, and/or the cancellation of instruments held by shareholders (without value).</p> <p>We kindly request clarity on the following:</p> <ul style="list-style-type: none"> • Please confirm whether "reduced claims" includes conversion to a more subordinated instrument? • The definition refers to "<i>and/or the cancellation of instruments held by shareholders (without value).</i>" Please confirm whether this will also include the cancellation of instruments held by creditors? • Please clarify whether 'Shareholder holders' equity refers to ordinary shares only or includes ordinary shares and preference shares? • Please provide clarity regarding creditor hierarchy and the conversion of Flac. This is a 	<ul style="list-style-type: none"> • and/or the instruments held by shareholders being cancelled (without value). <p>The creditors' claims/instruments will be reduced, noting that the term 'reduced' can mean reduced to zero.</p> <p>Section 166S (7) and (8) of the FSR Act provides the Reserve Bank with powers to reduce the amount that is or may become payable or to cancel the agreement.</p> <p>Shareholders' equity: Shareholders' equity includes both ordinary shares and preference shares (that qualify as equity).</p> <p>Creditor hierarchy:</p> <ul style="list-style-type: none"> • Section 166W of the FSR Act sets out the ranking of claims. • Flac instruments are senior to regulatory capital instruments and junior to other unsecured debt instruments. • In a resolution scenario, statutory bail-in would follow the creditor hierarchy. • Furthermore, Flac can only be bailed in (following the creditor hierarchy), in a resolution (i.e. not before the DI is placed in resolution).
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			key concern for potential investors in Flac instruments.	
7. Statutory powers				
8. Qualifying criteria for Flac instruments				
16.	Capitec	8.3 (c)(i)	Please provide clarity whether this statement should be based on the point-in-time calculation of Flac, or be based on a forecasted balance sheet and projected growth in Risk-weighted exposures (RWA)?	<i>Paragraph 8.3(c)(1) should be based on point-in-time calculations (i.e. the Flac minimum requirements must be met without considering future issuances).</i>
17.	FirstRand	Section 8.6	Initial terms of Flac instruments need to be approved by the Reserve Bank – will additional guidance be provided around the timing and turnaround time for application and approvals. It should be noted that holding company issuance programmes will need to be amended/created to address the requirements of the Flac instrument, and this is expected to be a lengthy process requiring legal amendments, internal sign-off, JSE approval, etc (as noted earlier).	<i>The Authorities will endeavour to expediently and efficiently review the terms and conditions as soon as they are received.</i>
18.	Standard Bank	Paragraph 8.6	The qualifying criteria for Flac instruments specify that subsequent issuances (i.e. issuances following the initial approval of instrument terms) require notification to the Reserve Bank prior to issuance. Issuers often offer instruments with various tenors to the market as part of the same issuance / auction process. As issuance size in various tenors and price clearance levels are not known before the issuance / auction we would recommend that notification of issuances be provided to the SARB after issuances have taken place.	<i>The Authorities' preference is to receive the notification prior to the issuance, as the actual issuance will form part of the reporting process.</i> <i>The purpose of the notification prior to the issuance is to serve a broader proactive financial stability monitoring process.</i>
19.	BASA	Par 8.2(f)	The minimum remaining maturity of 12 months is quite penal. This means the maximum period a FLAC	<i>To implement the T2 step-down approach, T2 instruments need to be issued for a</i>

			instrument, with an initial maturity of 24 months (being the minimum), would qualify as FLAC is 12 months (the qualifying period). This will necessitate frequent issuances to offset the maturities. Issuing longer term FLAC instruments to extend the qualifying period will result in higher costs. The PA is requested to reconsider the minimum remaining maturity. The proposal is to allow the instrument to qualify for a longer period or to introduce a step-down approach similar to Tier 2 instruments leading up to the maturity of the instrument.	<i>minimum period of five years. While Flac instruments do not have a step-down approach but require a minimum remaining period of 12 months (and an initial maturity of 24 months), the Flac instruments criteria provide the DIs with more flexibility around the tenure of the instruments, as long as the minimum remaining period is met. The prescription of a higher minimum maturity period (i.e. five years) for Flac instruments could take away the flexibility and demand higher costs for the DI.</i>
20.	BASA	Par 8.2i	<p>FLAC instruments may not have derivative linked features. Clarification is sought around what constitutes an embedded derivative with focus on the following questions:</p> <p>a. Are optional redemptions dates viewed as embedded derivatives given the intention to issue Flac instruments with such features, aimed at keeping issuances outside of the 12-month maturity window. (To adhere to 8.2 (g) – Annexure A, the issuing SIFI needs the ability to call and replace. A similar practice has been followed in issuance of regulatory capital instruments and is the norm for international FLAC and MREL issuances)</p>	<p><i>Paragraph 8.2(i) states that the unsecured subordinated debt instrument must not contain any derivative-linked features. There is no mention of embedded derivatives in the Standard.</i></p> <p><i>In addition, the minimum criteria for Flac instruments are stated in paragraph 8 of the draft Standard.</i></p>

			<p>b. Are fixed rate issuances deemed to have an embedded derivative?</p> <p>c. Are Capped / Mixed rate issuances deemed to have an embedded derivative?</p> <p>d. Are CPI-linked instruments deemed to have an embedded derivative?</p> <p>e. How is linkage to sustainable or green metrics treated with respect to the concept of embedded derivatives?</p> <p>NB: Derivative linkages allow the issuing SIFI to access multiple pools of liquidity as purchasers of Flac may require return profiles that suit different investor mandates. Perhaps derivative linkage can be allowed and the recognizable Flac is net of embedded derivatives.</p>	
21.	BASA	Par 8.2(k)	<p><i>(k) not contain any acceleration clauses in the contractual terms and conditions;</i></p> <p>Per Regulation 38(12(a)(v) of the Banks Regulations with regards to issuances it states: “the investor shall not have any right to accelerate the repayment of future scheduled payments, such as coupon or principal, except in the case of bankruptcy and/or liquidation;”</p> <p>Should Flac issuances not be aligned by including the exception of bankruptcy and/or liquidation.</p>	<p><i>The FSR Act deals with early termination provisions and the Insolvency Act provides for the treatment of instruments in liquidation.</i></p>

22.	BASA	Par 8.2(l)	<p><i>l) be for a sum equal to or more than the prescribed minimum denomination, when converted to South African rands.</i></p> <p>The current Commercial Paper Exemption Notice may change in future to exclude bonds and long-term debt instruments and, to address the possible complications that might arise from changes in the various exchange rates and the impact thereof on the valuation of the instruments, we recommend setting a prescribed minimum ZAR value</p>	<p><i>The prescribed minimum is excluded from the Standard as it might change from time to time. Therefore, Authorities have created an enabling provision to determine the prescribed minimum. The amount of the prescribed minimum will be specified in a determination and consulted on.</i></p>
23.	BASA	Par 8.3	<p>Written approval is required in order repurchase qualifying FLAC instruments. What is the envisioned SARB approval process with respect to new issuance, redemption and/or switches?</p> <p>In annexures A – C, there is a strong implication that Flac instruments will replace Bank senior issuances. Is there flexibility with respect to SARB requests to give the bank broad approvals when executing?</p> <p>A requirement to be given approval with each redemption may be onerous and not allow banks to incorporate Flac issuance into daily liquidity management processes. It is proposed that an annual approval is granted with an overall quantum as opposed to individual applications as each redemption occurs.</p>	<p><i>The approval for early redemptions is not prescriptive to the extent that it requires ad hoc approvals for each early redemption. The approval process may include that DIs submit redemption plans, setting out their planned redemptions for the financial year, for approval by the RA.</i></p>
24.	BASA	Par 8.4	<p>Kindly provide guidance on the specific terms envisaged with respect to “contractual terms that promote the ability of the Reserve Bank to conduct a resolution”.</p>	<p><i>The Authorities are not prescriptive regarding the specific contractual terms to be used and the terms might even differ for each DI.</i></p> <p><i>The requirement is for the DI to ensure that whatever contractual terms accompany the Flac issuances, the specific terms therein must promote the ability of the Reserve Bank to conduct a resolution and for the</i></p>

				<i>instruments to be subject to bail-in under SA law.</i>
25.	BASA	Par 8.6 Qualifying criteria for Flac instruments	<p>As per Par 8.6, DIs must submit the initial terms of the Flac instruments (or amendments thereto) to the SARB for approval prior to issuance. Kindly advise on the applicable timeline for such submission to the SARB.</p> <p>Please clarify the length of time required for the approval process by the RA of the initial terms of the Flac instruments.</p> <p>Please clarify if specific disclosure requirements will be required of Flac issuances (if there be any Pillar 3 disclosure requirements like those that are required for the main features' templates for capital instruments).</p> <p>Please clarify if there will be changes to the BA700 for disclosure to the SARB of the amount of Flac recognised.</p>	<p><i>Timeline for initial approval of Flac instruments:</i></p> <p><i>The Authorities will endeavour to expediently and efficiently review the terms and conditions, as soon as they are received.</i></p> <p><i>Disclosure requirements and changes to BA700:</i></p> <p><i>Paragraph 14.1 states “The form, manner and period for regulatory reporting for this Standard will be determined by the PA as directed by the Reserve Bank and published on the PA’s website”.</i></p>
9. Location of instruments				
10. General requirements				
26.	Capitec	10.1 Designated institutions must provide counterparties and market participants with sufficient information on the nature and contractual terms of Flac instruments to enable them to make informed decisions on the risk profile of these instruments.	<p>Please provide clarity with regards to the timelines and requirements to engage with other regulators (such as the JSE) especially with regards to certain listing and companies Act requirements that require prior board and shareholder’s approval to issue convertible instruments.</p> <p>Certain shareholder approvals for FY2025 are due in FY2024, and it is not clear if Flac requires approval before issuance by other regulators such as the JSE.</p>	<p><i>The envisioned effective date for the Standard is 1 January 2025; however, DIs will only be required to start reporting from the third year after the implementation date.</i></p> <p><i>Regarding the approval of the terms and conditions, the Authorities can only approve the terms and conditions after the Standard has been made by the PA.</i></p>

27.	BASA	Par 10.1	<p><i>Designated institutions must provide counterparties and market participants with sufficient information on the nature and contractual terms of Flac instruments to enable them to make informed decisions on the risk profile of these instruments.</i></p> <p>Recommend that clear, specific guidance be provided to banks to enable them to inform the market appropriately about the risks they are undertaking when investing in these instruments. Specific clarity around the interplay between point of resolution versus point of non-viability would be welcomed as This would ensure consistent messaging and provide confidence in Flac by external investors.</p>	<p><i>The POR and PONV fall within different frameworks under the purview of different authorities.</i></p> <p><i>The PA is responsible for the PONV, which is a Basel III requirement and mainly deals with capital.</i></p> <p><i>The RA is responsible for the POR, which is an FSB Key Attributes requirement, and deals with issues broader than capital, including large liquidity outflows and other issues that may lead a DI to fail.</i></p> <p><i>These two points may occur simultaneously, the PONV may occur before the POR, or the DI may be put in resolution before it reaches PONV. However, if the PA intends to invoke the PONV, it first needs to obtain SARB concurrence.</i></p>
28.	BASA	Par 10.2 General Requirements	<p>Par 10.2: <i>“Designated institutions must ensure that their operations will support the bail-in of their Flac instruments in a resolution and document the relevant processes (including governance), in a bail-in playbook.”</i></p> <p>Please advise on whether the PA intends to issue a guidance note on this requirement to provide further details, including the timing of this requirement?</p>	<p><i>Authorities intend to issue further guidance on the bail-in playbook.</i></p>
29.	BASA	Par 10.3 General Requirements	<p>Par. 10.3: <i>“Designated institutions must update and maintain their management information systems to be able to provide the Reserve Bank with all relevant</i></p>	<p><i>Specific guidance regarding the relevant information required will be provided as per paragraph 14.1 which states: “The form, manner and period for regulatory reporting</i></p>

			<p><i>information regarding all liabilities that may be subject to bail-in.”</i></p> <p>Please advise if the relevant information will be specified by the PA to ensure that all the information required by the PA is readily available.</p>	<p><i>for this Standard will be determined by the PA as directed by the Reserve Bank and published on the PA’s website”.</i></p>
11. Minimum Flac requirements				
30.	Capitec	11.1(d)	<p>We understand that the resolvability assessments in FY2024 will inform the resolvability rebate. Please confirm if the SARB will publish principles to assist banks in proactively managing this rebate closer to the maximum allowable percentage to reduce Flac? Is there a time period when these resolvability rebates will be communicated to banks?</p>	<p><i>Once the Authorities have embarked on the Resolvability Assessment Processes (RAP), they will communicate to the DIs information pertinent to this process. It is premature at this stage to comment on what will be communicated with regard to resolvability rebates, timelines etc.</i></p>
31.	FirstRand	Section 11.1 (b)	<p>The MFR is based on <u>risk-weighted exposure</u> as per the bank’s capital adequacy legislation. The current regulations include RWA floor-addons specified by the regulator. In addition, upon implementation of the final Basel reforms (specifically the output floor calculations), it could result in an output floor add-on (based on standardised approaches). These add-ons provide an additional level of conservatism for capital purposes, and it is proposed that these floor add-ons be excluded from the risk-weighted exposure used to derive the Flac calibration levels.</p> <p>Is it the intention that Flac instruments be carried for model uncertainty and other regulatory floors (whether input floor or output floor)?</p> <p>A specific example would be an additional (and temporary) RWA add-on for a bank that may be implementing a new regulatory model. Given that the Flac instruments will be issued for a relatively long period (general expectation is around 3 years), it</p>	<p><i>The PA is responsible for setting minimum requirements for regulatory capital (including risk-weighted exposures). Flac is meant to recapitalise the DI to a level that meets minimum regulatory capital requirements and provide the market with confidence. As far as the minimum regulatory capital requirements are concerned, the RA does not have the mandate to change what those minimum requirements should include or exclude, but rather to ensure that the recapitalisation capacity will be able to recapitalise the DI to a level that meets the minimum requirements set by the PA.</i></p> <p><i>Therefore, if the PA requires add-ons to adequately provide for the level of risk that the DI is carrying, Flac requirements have</i></p>

			seems overly conservative to calibrate Flac to these additional regulatory requirements that may be temporary in nature. It is proposed that these regulatory floors and buffers be removed from RWA for Flac calibration purposes.	<i>to 'mirror' the minimum regulatory requirements to ensure the DI can be adequately recapitalised in resolution.</i>
32.	FirstRand	Section 11.2 (d)	$\text{iMFR} = \text{minprCAR} (P_m - R_r) + \text{prPillar2B}$ <p>Given that the Pillar 2B is included in the minprCAR, as well as added (prPillar2B) – this results in an element of double counting. Consider removing the duplication.</p>	<p><i>There is no double counting.</i></p> <p><i>The minprCAR is the basis for determining the additional Flac (Pm-Rr). Therefore prPillar 2B is applied the same way in which the baseprCAR and prPillar 2A are applied as a basis to determine the additional Flac.</i></p>
33.	FirstRand	Section 11.3 (a)	<p>A post loss balance sheet needs to be used to calculate the levels of Flac issuances required.</p> <p>It is unclear if the current point-in-time balance sheet should be used or a forward-looking view. Bank will need to clearly understand the interplay these calculations and their resolution plans and resolvability assessments.</p>	<i>The point-in-time balance sheet should be used.</i>
34.	Standard Bank	Paragraph 11.5 and draft statement of expected impact	The standard requires excess regulatory capital that contributes towards minimum Flac requirements not to be recognised as qualifying capital for the purposes of meeting the total minimum required capital and reserve funds. Details of the application of the standard to the capital framework have not been provided and it is unclear whether these considerations have been fully incorporated in the industry impact assessment.	<i>The primary mechanism to fulfil the MFR is Flac instruments. The fact that the Standard provides for DIs to use 'available' excess regulatory instruments to meet the difference does not mean that the Authorities require the DIs to do so. The DI will have the discretion, in accordance with the Standard's requirements, to determine the composition it deems suitable to fulfil its Flac requirement.</i>

			We recommend that details of the application of the standard to the capital framework and the resultant industry impact assessment be incorporated and/or fully articulated in the next iteration of the draft standard.	
35.	BASA	Par 11	The effective date of the inputs used in the MFR is not clear. For example, when determining the MFR for a specific reporting period, which effective date will apply for the following inputs: MinCAR, Pillar 2A requirement, Pillar 2B requirement and Total Assets?	<i>The effective dates will be clarified with the reporting requirements. Paragraph 41.1 states: “The form, manner and period for regulatory reporting for this Standard will be determined by the PA as directed by the Reserve Bank and published on the PA’s website”.</i>
36.	BASA	Par 11.1 (b)	<p><i>The minCAR comprises of the following elements - (i) the relevant specified base requirement of no less than 8% of the risk-weighted exposures (baseCAR), standard for all banks; plus (ii) the relevant specified Pillar 2A requirement for systemic risk, standard for all banks; and (iii) the relevant specified Pillar 2B requirement for idiosyncratic risk, which is institution specific.</i></p> <p>Systemic risk is currently addressed by the D-SIB buffer, the capital conservation buffer, and the Pillar 2A (which is a specific add-on for South Africa i.e., is not aligned to Basel requirements and other jurisdiction). The inclusion of the Pillar 2A in the minCAR, will increase the total systemic buffer incrementally.</p> <p>Suggest the removal of Pillar 2A from the minCAR. Please confirm that if the proposed positive neutral countercyclical buffer (PCN CCyB) is implemented, the PCN CCyB will form part of the CBR?</p>	<p>Pillar 2A</p> <p><i>The RA does not have the mandate to change the components of the minimum capital adequacy requirements but rather to ensure that the recapitalisation capacity of the DI will be able to recapitalise the DI to a level that meets the minimum capital adequacy requirements as set by the PA. Should the PA change the minimum adequacy requirements in the future, then the Flac requirements (recapitalisation requirement levels) will automatically adjust to those changes as well.</i></p> <p>CCyB</p> <p><i>For purposes of this proposed prudential Standard and related documents, the PCN CCyB will form part of the CBR (as defined in the Statement of impact).</i></p>

37.	BASA	Par 11.1 (c)	<p><i>Designated institutions must increase their ability to obtain funding in the market after resolution, which will require the market to have confidence in the designated institution's ability to continue operating as a going concern. This will attract a market confidence premium (Pm), which will fall within a range of 0-25 percentage points, as determined by the Reserve Bank for each specific designated institution. This Pm will constitute firm specific, additional Flac above the minCAR.</i></p> <p>The market confidence premium will add to the amount of base Flac requirements for the designated institution. Clarify how often the market confidence premium will be reviewed and communicated.</p> <p>Clarify what factors will drive the market premium and what measures banks can take to manage the market confidence premium.</p> <p>Will each bank's market premium be evaluated at the same time?</p>	<p><i>Once the Authorities have embarked on the RAP, they will communicate to the DIs information pertinent to this process. It is premature at this stage to comment on any details pertaining to the Market Premium and Resolvability Rebate.</i></p>
38.	BASA	Par 11.1 (d)	<p><i>The Reserve Bank will consider the resolvability rebate (Rr) of each designated institution as a deduction to the additional Flac, which will fall within a range of 0-15 percentage points.</i></p> <p>Will the resolvability assessments be linked to the recovery plan reviews or will this be a new/separate process and review?</p> <p>What criteria will be used to determine the exact Rr imposed to the designated institution since it is specified as a range?</p> <p>Will the bank be given guidance on what areas should be refined to manage their Rr following an assessment?</p>	<p><i>Once the Authorities have embarked on the RAP, they will communicate to the DIs information pertinent to this process. It is premature at this stage to comment on any details pertaining to the Market Premium and Resolvability Rebate.</i></p>

39.	BASA	Par 11.2 (d)	<p><i>Additional Flac comprises of the Pm and the Rr, expressed as a percentage of the bMFR plus prPillar 2B (which together form the total minCAR). The sum of the post-loss bMFR plus prPillar 2B is denoted as minprCAR. Therefore = iMFR = minprCAR (Pm – Rr) + prPillar2B</i></p> <p>In the formula: $MFR = minprCAR (Pm - Rr) + prPillar2B$, should minprCAR not be replaced by bMFR as prPillar2B is added separately. By including it, we are increasing the institution-specific element.</p>	<p><i>MinprCAR should not be replaced by bMFR. MinCAR is a sum of bMFR and Pillar 2B.</i></p> <p><i>Additional Flac is determined as a factor of the minCAR (which includes the baseCAR, Pillar 2A and Pillar 2B).</i></p>
40.	BASA	Par 11.4 (d)	<p><i>Excess regulatory capital - (i) can be used as a top-up to meet the MFR, after taking into account the minimum Flac instrument issuances required to contribute towards the MFR (as set out in paragraph 11.4(b)(ii) above); and (ii) must absorb losses ahead of Flac issuances in line with the creditor hierarchy envisaged in the Insolvency Act.</i></p> <p>We request confirmation that preference shares can be taken into account in meeting the Flac requirement i.e. historic preference shares that do not qualify as regulatory capital?</p> <p>We request that preference shares above be included as excess capital.</p>	<p><i>The Standard requires that instruments that can be used as a top-up must qualify as excess regulatory capital. In addition, that excess regulatory capital must not be used to contribute towards the minimum required regulatory capital.</i></p>
12. Governance				
13. Compliance				

41.	Capitec	13.1, 13.1(b) and 13.1(d)	<p>Given the significant costs associated with holding more regulatory capital rather than Flac, we propose to remove the power of the SARB to increase regulatory capital requirements.</p> <p>As an alternative, we recommend that the Internal Capital Adequacy Assessment Process (ICAAP) by the Prudential Authority governs regulatory capital requirements (as currently the case), and let any non-compliance rather be considered within the resolvability rebate or market risk premium add-on.</p> <p>We also recommend specifying what any other actions can imply as this statement overrides any of the previous actions listed above.</p>	<p><i>The PA, not the RA, has the power to increase regulatory capital. However, where there is non-compliance, the RA can request the PA to impose penalties such as an increase in regulatory capital.</i></p> <p><i>Any other action includes any other action within the ambit of the RA or the PA that constitutes a penalty or sanction to the DI. Other actions may, in severe cases, also include invoking the point of resolution.</i></p>
14. Reporting requirements				
42.	BASA	Par 14.2	<p><i>Minimum reporting requirements will include the disclosure of granular information on all liabilities that may be subject to bail-in, according to the creditor hierarchy.</i></p> <p>Request for further details to be provided on the nature and extent of “granular” information to be disclosed.</p>	<p><i>The nature and extent of granular information will be provided when disclosure requirements are published as per paragraph 14.1.</i></p>
15. Transitional arrangements				
43.	BASA	Par 15.1(a)i	<p>Minimum FLAC contribution to TLAC penalises banks that have an existing level of excess capital adequacy by stipulating a minimum amount of Flac requirement. We note the extent of expected FLAC requirements in the market implies that most of the senior institutional liabilities would need to be converted to FLAC (which fixed income mandates currently rarely allow and is not where money market funds operate). Additionally, it would imply an erosion of capital adequacy as AT1 and T2 is also switched to meet the minimum FLAC</p>	<p><i>The minimum requirement for bail-in instruments of 33.33% (which for SA consists of Flac instruments) is in line with international requirements as set by the FSB’s TLAC requirements.</i></p> <p><i>In addition, the RA has made provision in paragraph 15.1(a)(i) of the Standard for the 33.33% to be phased in over the six-year period as well.</i></p>

			requirement. Would a reduction from the phased in 33.33% be considered? Moreso, a cap on contribution of own funds in reducing the additional Flac requirement is atypical when compared to European approaches.	
44.	BASA	Par 15.1	Please confirm the basis of the proposed phase-in timeline. Placing the quantum of Flac issuance required will be difficult considering the proposed timelines. The current timeline allows each SIFI to meet the requirements over the next c. 6 years. Due to the size of the local Institutional market, such instruments would be suitable for Fixed Income funds but will need substitution of maturing senior unsecured debt to meet the new issuance. Further, there seems to be a critical assumption that investor mandates can accept the added risk that come with Flac issuance relative to the existing senior unsecured obligations issued out of the Bank operating company. A longer Phase-in period should be considered to allow investors to process risks and update mandates with end investors.	<p><i>The proposed phase-in period of six years is in line with international standards.</i></p> <p><i>The rest of the comments are noted.</i></p>
45.	BASA	Par 15.2	<p><i>iMFR will be effective and phased in when the RAP for the designated institutions have been performed. The Prudential Authority will communicate the effective date and the phase-in period for this component, as directed by the Reserve Bank.</i></p> <ul style="list-style-type: none"> • What is the expected date for completion of the RAP? • Will the phase in period of the iMFR be 5 years? 	<p><i>Once the Authorities have embarked on the RAP, they will communicate to the DIs information pertinent to this process. It is premature at this stage to comment on any details pertaining to the RAP.</i></p>

			<ul style="list-style-type: none"> Will the iMFR be publicly disclosed? <p>How often will the iMFR be assessed?</p>	
General				
46.	FirstRand	General	Clarity is required on whether the solo SA entity or the legal entity view needs to be used to calculate the Flac requirements.	<i>Refer to comment No.12.</i>
47.	FirstRand	General	Unappropriated profits qualify as capital once appropriated – it is proposed that these are considered when calculating the excess capital available to meet the top up requirement. Should banks rather be allowed to incorporate all unappropriated profits (less proposed dividend) in the calculation? It is counter-intuitive that Flac requirement increased during the year (as RWA expands) despite generation of profits and planned appropriations following the payment of the dividend.	<i>The Standard requires that instruments that can be used as a top-up must qualify as excess regulatory capital. In addition, that excess regulatory capital must not be used to contribute towards the minimum required regulatory capital.</i>
48.	FirstRand	General	What is the level of audit review required. Will these requirements translate to reporting on regulatory forms and external disclosures. Banks will also need to understand the linkages with current reporting returns and frequency of reporting.	<p><i>As per paragraph 14.1, the nature and extent of granular information will be provided when disclosure requirements are published..</i></p> <p><i>When the reporting requirements are published, a public comments period will be made available, which will give industry an opportunity to raise comments on the reporting 'returns'.</i></p> <p><i>At this stage, it is premature to comment on possible audit reviews and related requirements.</i></p>

49.	BASA	General	Guidance is required on how often the MFR calculation must be updated.	<i>As per paragraph 14.1, the period for reporting will be indicated in the reporting requirements.</i>
50.	BASA	General	Kindly provide clarity on whether the SARB has confirmed that investors in senior unsecured debt have mandates that allow them to invest in FLAC? If so, could this recent analysis be shared as it would be useful to the industry.	<i>The Reserve Bank has held several engagements with industry. The DIs will need to engage with their investors on the terms of their instruments and the mandates of the prospective investors.</i>
51.	BASA	General	The draft Standard does not address instances and the remedial actions required if a designated institution falls below its MFR or the minimum FLAC issuance requirement per 11.4(b)(ii). Kindly provide guidance.	<i>Paragraph 13 deals with the non-compliance of the requirements in the Standard.</i> <i>Remedial actions (which will be on a case-by-case basis) will be actions that the DI will need to take to ensure that they meet the requirements.</i>
52.	BASA	General	To the extent that liquidity and investor mandates do not cater for designated institutions to issue sufficient FLAC to cover their FLAC requirements, what is the process that must be followed? Further, if investor appetite is lacking, must designated institutions redeem their Tier 2 instruments and replace it with FLAC instruments? If so, what is the process that must be followed?	<i>It is not the responsibility of the RA to impose how the MFR must be fulfilled, but rather to set out the requirements for the DIs to meet. It is the responsibility of the DI to decide how the MFR will be fulfilled, in line with the stipulated requirements.</i> <i>If the DIs do not meet their minimum requirements, they should engage the Authorities and take note of the compliance requirements in paragraph 13 of the Standard.</i>

53.	BASA	General	Mention was previously made in the FLAC discussion paper issued by the SARB that FLAC must be externally issued out of the same entity that other subordinated instruments are issued from, that is FLAC, AT1 and Tier 2 must be externally issued by the same entity. Kindly confirm if this is still the expectation?	<i>The Flac discussion paper does not set out any requirements regarding instruments held for regulatory capital purposes but rather highlights that the bail-in process would be simplified if all instruments earmarked for bail-in in a resolution are located in the same entity, which is the ultimate holding company. It further mentions that this is an approach that the PA and RA can explore, but not an expectation.</i>
54.	BASA	General	Can FLAC be issued externally out of an intermediate holding company?	<i>Refer to comment No.3</i>
55.	BASA	General	Guidance is required on how often the MFR calculation must be updated.	<i>Refer to comment No.49</i>
56.	BASA	General	<p>Recommend allowing a threshold to allow for market making in Flac paper.</p> <p>In line with sections par xii of the FSBs TLAC Term Sheet “ Limitation of contagion” (Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution: Total Loss-absorbing Capacity (TLAC) Term Sheet (fsb.org)) the Basel Committee on Banking Supervision developed the TLAC Holding Standard (TLAC holdings standard (bis.org)), which allows for a 5% market making threshold. We request that Flac be allowed the same consideration and align with these considerations provided for G-SIBs.</p>	<i>The prohibition for market making has been removed from the Standard; however, DIs will need to obtain prior approval for the repurchase, repayment or redemption of any Flac instruments.</i>

57.	BASA	General	<p>We note the assumption and application of a loss of minCAR, is it the intention of the RA to use the minCAR assumption as a rule for the industry? Would this include the impact of resolution actions?</p> <p>In addition, the standard should address the link between resolution strategy and post-resolution balance sheet depletion which would inform the post resolution balance sheet by means of a scaling factor for transfer strategies.</p>	<p><i>The question is not clear. However, based on what the Authorities understand from the question, at a high level the purpose of the Standard is to determine the recapitalisation capacity for a DI, with an open-bank resolution strategy.</i></p> <p><i>The resolution process has two broad stages: the stabilisation phase and the restructuring phase.</i></p> <p><i>During the stabilisation phase, the main objective is to recapitalise the DI and restore confidence. Once the DI is stabilised, what follows is a restructuring phase in which other resolution tools such as transfer strategies might be employed to deal with the issues that led to resolution.</i></p>
58.	BASA	General	<p>Application of Risk Weighting to the post loss balance sheet.</p> <p>Will the RA provide guidance on the assumed application of risk weightings to the post loss balance sheet? The assumption that losses will be spread evenly over the entire balance sheet may not reflect reality. As such, would a more refined deduction of resolution losses be considered? In a similar vein, an adjusted risk weighting that reflects more targeted reductions in assets could be considered.</p>	<p><i>There is no assumption that speaks to losses being spread evenly in the Standard.</i></p> <p><i>Paragraph 11.3(a)(ii) and (iv) state that:</i></p> <p><i>(ii) estimated losses are to be deducted from the relevant asset class according to the current risk weighing assigned to these assets; and</i></p> <p><i>(iv) using the post-loss balance sheet, determine the amount of the base prCAR, prPillar 2A and prPillar 2B using the current capital requirements and the current risk weightings.</i></p>

59.	BASA	General	<p>The proposed framework is complex with much uncertainty over the role of the authority versus the role of the DI, and not enough clarity around criteria that must be considered when calibrating the FLAC requirement for a specific DI. The following concerns with the current proposed approach are noted:</p> <ul style="list-style-type: none"> • The calibration of requirements at an individual bank has a significant chance of over/under estimating the actual requirement of any bank in any variety of resolution circumstances. • The size of the investor pool in the domestic market is a potential constraint, with concerns over investment mandates for convertible instruments. • Foreign issuance, with the additional costs associated, would appear to be required to meet the overall issuance scale currently estimated for SA. This suggests there will be: <ul style="list-style-type: none"> ○ increased leakage of interest payments to offshore investors, ○ the possibility of offshore investors owning SA banks in the event of resolution, ○ the potential need for the SARB to vet the Flac investor base given they could be the owners of the bank post resolution if conversion to share equity is the mechanism used to bail-in versus write-off. ○ tax leakage for the fiscus • The overall burden on the industry in terms of additional costs, both direct in terms of higher 	<p><i>The Authorities are not clear on the comments made regarding uncertainty over the role of the Resolution Authority versus that of the DI. The Standard sets requirements for DIs to meet.</i></p> <p><i>In addition, the challenges as well as suggestions are noted.</i></p>
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			<p>interest costs and indirect in terms of the resource requirements to establish and verify the necessary Flac calibrations for every impacted bank is significant.</p> <p>We suggest that consideration should be given to adjusting the overall approach to recapitalisation in resolution, to a simpler and more cost-effective approach similar to the Singapore approach. We believe that this type of approach would significantly simplify the resolution capitalisation process, while reducing the cost impact to the industry and increasing the Resolution Authority's ability to address resolution situations more flexibly and with greater resource capacity. It could also help alleviate the issues raised above.</p>	
60.	BASA	General	<p>Requesting a detailed calculation example that would clearly demonstrate the phase-in periods for both components of the MFR as well as the FLAC issuances that contribute to the bMFR.</p>	<p><i>A calculation to phase in both components of the MFR is not possible until the iMFR can be accurately calculated (which is when the RAP process for DIs has been performed).</i></p> <p><i>Flac issuance:</i> <i>Figure F in the Statement of expected impact shows the phase-in of the bMFR as well as the minimum Flac portion.</i></p> <p><i>In addition, the Guidance Notice has been expanded to show the phasing in of the bMFR and the minimum Flac instrument issuances.</i></p> <p><i>See sections 7 and 8 of the revised Guidance Notice.</i></p>

Table 3: Full set of comments received on the Statement of need, intended operation and expected Impact

No.	Commentator	Paragraph	Comment	Response
1. Introduction				
2. The need for the Prudential Standard				
61.	Capitec	2.3 and 2.3(b)	<p>It appears the majority of the Bond funds still do not have mandates to buy this convertible debt and as such makes ability for banks to be able to issue the quantum of Flac issuance to be in doubt.</p> <p>We recommend proactive engagement by the SARB with this industry, in addition to the work already being done by the banks, to ensure that the relevant mandates are amended in order for these funds to be able to replace current senior unsecured debt holdings with Flac.</p>	<i>The comment is noted. The Reserve Bank continues to engage with industry on the implementation of the resolution framework and welcomes any input on possible areas that require specific engagement.</i>
62.	BASA	2.3 The need for the Prudential Standard	<p><u>Paragraph 2.3:</u> The FSR Act empowers the Reserve Bank to perform a bail-in, in resolution, by enabling it to perform the following (in a manner that respects the creditor hierarchy) - (a) write-down shareholders' equity and unsecured subordinated debt instruments to the extent necessary to absorb losses; and (b) convert all or parts of unsecured debt instruments into shareholders' equity to recapitalise a DI in resolution.</p> <p>Comment: Paragraph 2.3 (b) states that unsecured debt instruments will only be converted into shareholders equity (CET1) to recapitalise the bank and does not mention the ability / power of the Reserve Bank to convert subordinated debt instruments into other forms of capital instruments such as AT1 (additional Tier1) or T2 (Tier 2) instruments.</p> <p>During the bail-in process, if subordinated debt instruments are only converted into CET1, the bank will be recapitalised with only CET1, having no AT1 or Tier2</p>	<i>Refer to comment No.15 (under Table 2 above).</i>

			<p>instruments immediately following the bail-in process. This will result in a CET1 at > 9%, which will be proportionally mis-aligned with its peers and will significantly increase the weighted average cost of capital.</p> <p>Assuming 0% Pillar 2B (for the sake of simplify, given the confidential nature of Pillar2B requirements), the capital adequacy legislation allows for the ~9% MinCAR to comprise of 5,0% CET1 + 1.75% AT1 + 2,25% Tier2.</p> <p>In this instance, recapitalisation to the minCAR of 9%, as per paragraph 6.4 will result in a bank that is capitalised at [9% CET 1 + 0% AT1 + 0% Tier2] with a reduced Flac holding, effectively increasing the weighted cost of capital, and placing the bank in a competitive dis-advantage relative to peer banks.</p> <p>Consequently, the bank will not be optimally capitalised and will therefore incur excessive funding costs at a critical point in time following the bail-in weekend. This could result in an unsustainable capital stack where the weighted average cost of capital will exceed that of its peer banks.</p> <p>It could be beneficial for the regulator to have at its discretion, the ability to recapitalise the bank with not only CET1, but also with other capital instruments to allow the bank in resolution the best possible opportunity of recapitalising to an optimal, sustainable capital structure, in line with the allowance made for AT1 and Tier 2 instruments in the bank's capital adequacy legislation.</p> <p>This will also promote the objective stated in paragraph 2.2 of the 'Statement of need on Flac' that <i>"Recapitalisation through bail-in must enable a designated institution (DI) to continue operating during a resolution and to exit resolution as a viable entity. This requires the recapitalisation to be sufficient to restore the capital levels of a DI to meet regulatory capital requirements (as set out</i></p>	
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			<p><i>in the Regulations relating to Banks or prudential standards that deal with a bank's capital adequacy (bank's capital adequacy legislation)) and restore the confidence of the market that a DI can continue to successfully conduct business."</i></p> <p>To allow for the conversion of subordinated debt instruments into a more subordinated instrument (i.e. Flac to be converted into either T2, AT1 or CET and potentially for Tier2 to be converted into either AT1 or CET1), we propose the following amendment to paragraph 6.4, point (b):</p> <p><i>"Statutory bail-in enables the Reserve Bank to perform the following actions, in a manner that respects the creditor hierarchy -</i></p> <p><i>(a) write-down shareholders' equity and unsecured subordinated debt instruments to the extent necessary to absorb losses; and</i></p> <p><i>(b) convert all or parts of unsecured debt instruments into shareholders' equity or a lower more subordinated instrument to recapitalise the designated institution in resolution."</i></p>	
63.	BASA	2.4 The need for the Prudential Standard	<p>Paragraph 2.3 refers to the ability of the SARB to write-down and convert unsecured debt instruments. To align to paragraph 2.3, we propose that paragraph 2.4 also contain the conversion power of the SARB:</p> <p>The Reserve Bank's power to write down or convert unsecured subordinated debt extends to all liabilities of a DI (including depositors and operational creditors), except those specifically excluded by section 166S (9) of the FSR Act or an instrument issued by the Reserve Bank.</p>	<p><i>The Authorities disagree with the recommendation.</i></p> <p><i>Paragraph 2.4 is an emphasis of the powers contained in section 166S(7) of the FSR Act, which empowers the Reserve Bank to reduce the amount that is payable or may become payable or cancel the agreement.</i></p> <p><i>The aim is to emphasise the fact that all liabilities (except those listed under</i></p>

				<p><i>section 166S(9) of the FSR Act) are subject to bail-in.</i></p> <p><i>The conversion power is contained in section 166T of the FSR Act ,which is not the objective of paragraph 2.4.</i></p>
64.	BASA	2.6 The need for the Prudential Standard	<p>In line with the comments made on paragraphs 2.3 and 2.4, we propose the following amendment to paragraph 2.6:</p> <p><i>“To achieve a successful bail-in, a DI will need to maintain a sufficient level of Flac instruments (and other qualifying instruments) that will be available in resolution for loss absorption and recapitalisation (by being converted to regulatory capital that can be converted into any form of regulatory capital as deemed appropriate).”</i></p>	<p><i>The Authorities disagree with the recommendation.</i></p>
3.Statement of expected impact				
65.	Capitec	3.5.9	<p>Please confirm whether the Counter Cyclical Buffer (CCyB) add-on of 1%, proposed for 1 January 2026, have been included in the CREG calculations? If so, there will be a potential duplication of capital costs in the system. If not, it will potentially change the results and conclusions of the impact assessment.</p>	<p><i>The impact analysis was calculated using data as at 31 March 2023. Therefore the CCyB add-on that will become effective on 1 January 2026 was not incorporated in the impact analysis as the proposed changes had not come into effect then.</i></p> <p><i>In addition, the primary mechanism to fulfil the MFR is Flac instruments. The fact that the Standard provides for DIs to use ‘available’ excess regulatory instruments to meet the difference does not mean that the Authorities require the DIs to do so. The DI will have the discretion, in accordance</i></p>

				<i>with the Standard's requirements, to determine the composition it deems suitable to fulfil its Flac requirement.</i>
66.	Capitec	3.6.3 and 5.9	<p>Please provide clarity on the following:</p> <ul style="list-style-type: none"> • Will there be a separate Flac return or will existing information from BA returns be used by the PA to monitor actual versus required Flac issuances? • Will there be any disclosure requirements on Flac and how can these disclosures aid in preventing the market to reverse engineer a bank's confidential Pillar 2B? • At what reporting date is the 60% phase-in requirement of the total Flac set, or is this a moving target? • There will always be an inefficiency in the actual Flac held should the Flac target be updated monthly. Banks will always have to issue an excess of flac to ensure that they always comply to ensure that they are ahead of potential negative market events which will make the issuance of any type of debt problematic; e.g. the failure of African Bank in 2014 when the debt capital markets effectively closed. <p>To what extent will point-in-time or projected financial information be used to inform the relevant Flac targets?</p>	<p><i>Paragraph 14.1 states that the form, manner and period for regulatory reporting related to this Standard, where such requirements have not been specified in this Standard, will be determined by the PA as directed by the Reserve Bank and published on the PA's website.</i></p> <p><i>There will be a separate process to address reporting requirements. The comments have been noted.</i></p>
67.	FirstRand	Section 3.2.1	<p>It is noted that the Flac requirement is applicable to SIFI banks and their holding company.</p> <p>To confirm that the level of calibration will be based on the SA operating entity balance sheet?</p>	<i>Refer to comment No. 12 (under Table 2 above).</i>
68.	FirstRand	Section 3.6.2	Need to consider the level of Flac issuances above the level of SUDs to be replaced and the cost impacts on the DIs bottom line.	<i>Noted.</i>

69.	BASA	3.4 Background, 3.4.1 (a)	<p>A SIFIs total loss absorption capacity (TLAC) available to absorb losses consists of the sum of all qualifying regulatory capital instruments (including all buffers) and flac instruments. For Flac calibration purposes however, we note that TLAC = minCAR + MFR.</p> <p>Paragraph 3.4.1 states that MFR represents the total level of loss absorption and recapitalisation capacity which does not align with the definition of TLAC in the draft standards where MFR is a component of TLAC but does not constitute total TLAC.</p> <p><i>“3.4.1 The formulas stipulated in the Prudential Standard form the basis of the ex-ante estimation of the financial impact study. There are three main formulas in the standard –</i> <i>(a) the Minimum Flac Requirement (MFR): which represents the <u>total level of loss absorption and recapitalisation capacity</u>.”</i></p>	<p><i>Correction to respondents’ statement: TLAC refers to the sum of the minimum required amount of capital and reserve funds (prior to buffers) and the minimum Flac requirement, used for loss-absorbing and recapitalisation capacity.</i></p> <p><i>Section 3.4.1(a) of the Statement of impact has been amended accordingly to align to the definition of MFR.</i></p>
70.	BASA	3.4 Background 3.4.1 (a) (i)	<p><i>“(i) the base Minimum Flac Requirement (bMFR); is the base component of the MFR, and it is a standard requirement for all banks. This component is driven by the level of recapitalisation that will be required to restore a DIs capital (after losses have been absorbed) to the point where it complies with its minimum capital adequacy requirements (minCAR) as determined by the PA;”</i></p> <p>Kindly advise if the SARB envisages recapitalisation back to minCAR levels (after losses have been absorbed) to take place with only CET1 shareholders’ equity or if there would be scope to recapitalise back to minCAR utilising CET1, AT1 and T2 as is made allowance for in the minimum capital adequacy requirements for banks (by converting senior unsecured debt instruments).</p>	<p><i>Refer to comment No.15 (under Table 2 above).</i></p>

71.	BASA	3.7 Nature of MFR instruments, Figure F: Cumulative Flac instruments issuances (c) (ii)	<p>In the commentary based on Figure F, point (c) (ii), it states:</p> <p><i>“(ii) <u>For certain DIs, the minimum Flac issuance requirement of 33.33% of TLAC came out to be more than the required level of bMFR.</u> Therefore, for these specific DIs the nature of bMFR could only consist of Flac instruments, since the minimum that would determine the amount of Flac issuances was more than the bMFR itself.”</i></p> <p>Working through the calculations, we have:</p> $\begin{aligned} \text{Flac} &= 33.33\% \times \text{TLAC} \\ &= 33.33\% \times [\text{minCAR} + \text{MFR}] \\ &= 33.33\% \times [(\text{baseCAR} + \text{Pillar2A} + \text{Pillar2B}) + (\text{bMFR})] \text{ \{assuming MFR = bMFR as per the analysis\}} \\ &= 33.33\% \times [(\text{baseCAR} + \text{Pillar2A} + \text{Pillar2B}) + (\text{baseprCAR} + \text{prPillar2A})] \\ &= 33.33\% \times [(8\% + 1\% + 1\%) + (8\%_{pr} + 1\%_{pr})] \text{ \{assuming, conservatively, a 1\% Pillar2B requirement\}} \\ &= 33.33\% \times [(8\% + 1\% + 1\%) + (7,7\% + 0,95\%)] \\ &= 33.33\% \times [18,65\%] \\ &= 6,22\% \end{aligned}$ <p>Compared to</p> $\begin{aligned} \text{MFR} &= \text{bMFR} \\ &= \text{baseprCAR} + \text{prPillar2A} \\ &= 8\%_{pr} + 1\%_{pr} \\ &= 7,7\% + 0,95\% \\ &= 8,65\% \end{aligned}$	<p><i>Pillar 2B is not publicly disclosed in line with regulatory requirements, therefore the Authorities cannot provide the detail sought.</i></p> <p><i>In addition, there is a possibility that the commentators’ assumptions differed from the those of the RAs, including the fact that both the bMFR and the minimum Flac issuances were phased in as per paragraph 15.1 of the Standard for calculations used in Figure F.</i></p>
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			For our understanding, please advise how the Flac issuance requirement came out more than bMFR, unless Pillar 2B is greater than $8,65\% - 6,22\% = 2,43\%$?	
72.	BASA	3.7 Nature of MFR instruments, Figure G: TLAC in the form of Creditor Hierarchy (b)	<p>Given the publication of the proposed directive on the implementation of a positive cycle-neutral countercyclical capital buffer (PcN CCyB) of 1% with effect from 1 January 2026, we note that this will directly impact on the amount of excess regulatory capital available to DIs to use to 'top-up' MFR requirements, which could potentially have a 'double-buffer' effect to the extent that the excess regulatory buffer is eroded and additional flac instruments are required as to ensure that MFR (or bMFR) is met.</p> <p>To the extent that the binding constraint of $\text{Flac} \geq 33.33\%$ of TLAC allows for the utilisation of excess regulatory capital as MFR, noting that a 1% decrease in excess regulatory capital could, for more than one SIFI, directly result in additional Flac requirements, having a 'double-buffer' effect and increasing the funding costs of the organisation, despite TLAC ratios estimated to reach international GSIB levels by the end-state of implementation.</p> <p>We propose that the consequential impact of the PcN CcyB on the industry flac requirement be considered to ensure that there are no unintended consequences in terms of implementing buffers on buffers and the consequential impact on funding costs.</p>	<i>Refer to comment No.10 (under Table 2 above).</i>
73.	BASA	3.7 Nature of MFR instruments, Figure G: TLAC in the form of Creditor Hierarchy (b)	<p>From the commentary on Figure G, point (b), <i>"The R80bn difference (R236bn – R156bn) is the excess regulatory capital intended to contribute towards the bMFR, however it ranks lower in the creditor hierarchy."</i></p> <p>To fully explain the benefits, the statement could read "</p>	<i>From the Authorities' perspective, the excess regulatory capital (used to contribute towards the bMFR) increases the risk that, by the time the institution is placed into resolution, there might not be sufficient recapitalisation capacity in the form of</i>

			<p><i>“The R80bn difference (R236bn – R156bn) is the excess regulatory capital intended to contribute towards the bMFR, however it ranks lower in the creditor hierarchy which positively ranks lower in the creditor hierarchy meaning it can absorb losses before entering resolution, and thus contributing to increasing the distance to resolution.”</i></p>	<p><i>Flac instrument issuances, as regulatory capital would have absorbed losses on a going-concern basis (despite the intention of the DI to set it aside for resolution purposes).</i></p>
74.	BASA	3.7 Nature of MFR instruments, Figure G: TLAC in the form of Creditor Hierarchy (e) (i) and (ii)	<p>The analysis seems to encourage the max issuance scenario where TLAC comprise of less CET1 and more Flac compared to the min issuance scenario where the TLAC comprise of more CET1 and less Flac – the reason being is that there would, in the max issuance scenario, be more Flac available at POR.</p> <p>But in both instances, the TLAC is equal. But the max issuance scenario has the disadvantage of having less CET1 (i.e. smaller volumes of the most loss absorbing form of capital) and more Flac which effectively brings forward the POR as lower amounts of losses can be absorbed by the going-concern entity due to the lower CET1 vs. the alternative scenario. In summary:</p> <ul style="list-style-type: none"> • Min issuance Scenario: More CET1 = more going-concern loss absorption capacity = pushes POR out • Max issuance Scenario: Less CET1 = less going-concern loss absorption capacity = brings POR forward <p>All the while, the entity has the same loss absorption capacity in the form of TLAC, the purpose of which is to absorb losses at any point in time, where loss-given-failure (LGF) is ambivalent to whether it is covered by going or gone concern capital.</p>	<p><i>Authorities’ view of the maximum scenario, which guarantees 100% of MFR/bMFR to be available at POR, does not necessarily bring the POR forward – it merely indicates that going-concern capital is not ‘entangled’ with capital intended to be used for resolution (gone-concern capital). It brings clarity and transparency to the tranche of instruments set aside for resolution purposes.</i></p> <p><i>In a scenario where excess regulatory capital is used to meet the difference, meaning that it runs the risk of capital absorbing losses while the DI is a going concern, the RA will apply extra caution around the POR to ensure that going-concern loss-absorbing instruments are not depleted before resolution, since a portion of those going-concern instruments are meant for resolution purposes.</i></p> <p><i>The purpose of TLAC is not to absorb losses at any time. It is meant for adequate loss-absorbing capacity</i></p>

			<p>TLAC should be sufficient to cover LGF, and then re-calibrate the bank to the minimum capital requirement to ensure going-concern status of a SIFI.</p> <p>If TLAC and the mechanics of achieving the above are well crafted, then the issue is less about the composition of TLAC and more about the quantum of TLAC and the statutory bail-in mechanics.</p> <p>As mentioned above, max FLAC issuance strategy brings POR sooner i.e. it implies less excess of the most subordinated loss absorbing capacity (namely Reg Capital).</p> <p>One would have anticipated that pushing POR out was more preferable i.e. by allowing more (not less) pre-resolution bail-in Reg Capital to qualify. Flooring FLAC at 33.3% is tantamount to capping Reg Cap at 67.6% which is the same as capping a bank's ability to push POR out.</p> <p>When the Minister of Finance announces that a bank is in Resolution it will accelerate the possible risks of funding markets shutting down. At the height of a crisis, there would be benefit in delaying resolution and increasing the distance to POR with more excess Regulatory Capital and we expect that to be preferable to reaching the POR sooner.</p> <p>Given that Conservation buffers (2.5%) and DSIB buffers (1%) which, while not defined as part of minimum regulatory requirements in terms of Basel 3 TLAC requirements, do operationally form part of a banks going-concern loss absorbing capacity designed to cover LGF. Hence even though they are excluded for the purposes of</p>	<p><i>while the DI is a going concern and adequate recapitalisation capacity for use when the DI is placed into resolution.</i></p> <p><i>The rest of the comments are noted.</i></p>
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			calculating Excess Reg Cap, they do still reflect an extra buffer of protection over and above TLAC.	
4.Costs and benefits of implementing the Prudential Standard				
5.The intended operation of the Prudential Standard				
6.Conclusion				
General				
75.	FirstRand	General	Clarity required on whether this assessment caters for future regulatory changes (final Basel reforms and proposed cycle neutral CCyB).	<i>Refer to comment No. 65.</i>
76.	BASA	General	A QIS which takes into account the in-flight changes to the final prudential framework (Basel III) should be performed to gauge more accurately the final impact of this standard. Additionally, it should gauge investor appetite for Flac issuances.	<i>The PA endeavours to consider the cumulative impact of proposed amendments to regulations. However, challenges remain due to the timing and sequencing of regulations.</i>

Table 4: Full set of comments received on the Guidance Notice

No.	Commentator	Paragraph	Comment	Response
1.Introduction				
2.Overview of the Prudential Standard				
77.	BASA	Par 2.2	<p><i>A bail-in resolution tool will enable the Reserve Bank to assign losses to shareholders and creditors to absorb losses and recapitalise a DI in resolution, instead of relying on public funds to do so (which exposes taxpayers to loss). This tool, however, extends to all liabilities (with certain exceptions under section 166S (9)) which means operational creditor claims and uninsured deposits could be affected by a resolution bail-in.</i></p> <p>This statement is in line with the FSRA, while par 6.4 of the draft Standard implies that bail-in will only be applied to equity and unsecured debt instruments. We request clarity on whether bail-in will be limited to these instruments only.</p>	<i>In terms of the creditor hierarchy, operational creditors and uninsured deposits will be considered unsecured creditors.</i>
3.Context of the terms and definitions used on the Prudential Standard				
78.	FirstRand	3.2 Principle 1: The DI should be recapitalised to a level that meets the minCAR, excluding regulatory buffers, as determined by the PA.	The base minCAR currently includes the Pillar2A – in resolution, will banks not be allowed to dip into this buffer, similar to the temporary relief provided during the pandemic.	<i>The decision regarding the usage of Pillar 2A does not fall under the mandate of the RA and it is not for resolution purposes.</i>
79.	FirstRand	3.4 To determine the minCAR that a DI is required to meet, a current balance sheet would be utilised as well as the risk weights assigned to each class of assets.	Reference is made to the current balance sheet to calculate the minCAR – the current balance sheet capital requirements can differ materially to the balance sheet in 2025 (when the final Basel reforms are implemented) – this may result in volatility in the level of issuances required.	<i>Noted.</i>

4. Formulas in the Prudential Standard				
80.	BASA	Par 4.5 and 4.6	<p>4.5 The instruments to meet the MFR must consist of a minimum amount of Flac instruments, which is calculated as 33.33% of the total loss-absorbing capacity (TLAC). DIs then have an option to “top-up” the remaining MFR balance with excess regulatory capital (CREG9).</p> <p>4.6 It is important to note that the MFR is an additional requirement to the minimum capital adequacy requirement (minCAR) that is specified in the Regulations relating to Banks or prudential standards that deal with a bank’s capital adequacy (bank’s capital adequacy legislation). When added together, the MFR plus the minCAR equals TLAC. Therefore, to calculate the total going concern and gone concern capital requirements (excluding the capital buffer requirements), DIs must use the following formula - $TLAC = minCAR + MFR$</p> <p>Recommend using “Resolution Entity” that the Flac calibration is based on rather than Designated Institution that, under the FSRA refers to the entire group or subset of entities within a group, depending on the organisation’s structure.</p>	<p>The Authorities do not agree with the recommendation.</p> <p>The DI(s) referred to in the Standard are defined in paragraph 5.1 and 5.2 of the Standard.</p>
5. Guidance: Illustrative example of the MFR calculation				
6. Guidance: Illustrative example of the minimum Flac instruments				
81.	BASA	6.1 Annexure C - Guidance Note on Flac Illustrative Example	In the interim period where the iMFR has not yet been determined, will the phase in of Flac issuances be based only on the bMFR?	Refer to paragraph 15 of the Standard for the phasing in of the components of the MFR.
General				
82.	BASA	Example	Is the method applied in the example to derive MFR in Annexure C to determine a post resolution risk weighted assets (prRWA) the actual approach banks will employ once the Standard is effective? The method being:	Note that the examples provided in the Guidance Notice were used to provide a simplified high-level illustrative example.

			<p>pr RWA = Current RWA% x (Current Total Assets – Current Minimum Capital Requirement).</p> <p>Previous discussion documents alluded to a more scientific calculation.</p>	<p><i>It is expected that the actual calculations will be more involved due to the complex nature of the in-scope DIs' balance sheets and different risk weightings assigned to the various asset classes.</i></p> <p><i>The requirements for a post-loss balance sheet are specified in paragraph 11.3(a) of the Standard.</i></p> <p><i>Paragraph 11(a)(ii) of the Standard states that, to estimate the resolution post-loss balance sheet, the estimated losses must be deducted from the relevant asset class according to the current risk weighting assigned to those relevant assets.</i></p> <p><i>Note that there is no Annexure C in the Guidance Notice.</i></p>
83.	BASA	Example	<p>Subject to the response above; when estimating MFR, the example to calculated MFR in Annexure C reduces total assets by the minimum capital requirement to estimate the post resolution balance sheet.</p> <p>Before a loss can eliminate minimum capital requirement, it would also need to erode the portion of total capital more than the minimum requirement. We therefore suggest the post resolution total assets is best estimated as: Current Total Assets – Total Regulatory Capital Supply.</p>	<p><i>The recapitalisation requirements (excluding the additional Flac component) only need the DI to be recapitalised to a level that meets the minimum regulatory requirements as prescribed by the PA.</i></p> <p><i>Please note that there is no Annexure C in the Guidance Notice.</i></p>
84.	BASA	Footnote 3	<p><i>Flac is not an acronym, it is a term that refers to the new class of debt instruments defined in the Standard.</i></p> <p>Flac is mentioned here to not be an acronym, yet is mentioned as standing for “first loss after capital” on the</p>	<p><i>The Authorities hereby confirm that Flac is not an acronym.</i></p>

			SARB website (resolution planning (resbank.co.za)). We request alignment on whether this is an acronym or not.	
85.	BASA	Footnote 5	<p><i>Other qualifying instruments refers to the excess regulatory capital instruments, that DIs are allowed to use in addition to the minimum Flac instrument issuance requirement, to meet the minimum Flac requirement. Essentially DIs have two options to meet the minimum Flac requirement:</i></p> <p><i>Option 1 is to use Flac instruments only and;</i></p> <p><i>Option 2 is to issue the minimum amount of Flac instruments and use excess regulatory instruments as a top-up.</i></p> <p>Request clarification that Flac issuance is not limited to the minimum as per Option 2 or maximum per Option 1, but rather flexible at the bank's discretion.</p>	<p><i>The primary mechanism to fulfil the MFR is Flac instruments.</i></p> <p><i>The DI will have the discretion, in accordance with the Standard's requirements, to determine the composition it deems suitable to fulfil its Flac requirement (i.e using Flac instruments only or Flac instruments and other qualifying instruments (as a top-up)).</i></p>
86.	BASA	No reference	<p>Principle ii of the FSB's Principles on Loss-absorbing and Recapitalisation specifies that the individual requirement for specific firms must be calibrated by the relevant authority. Our reading of the consultative documents is that it will be the responsibility of individual banks to perform the calculation of Flac requirements. This appears to be is a divergence from the approach taken in other jurisdictions where the requirement is calculated by the relevant authority and published/notified to banks on an annual basis. Is our understanding correct that banks will be responsible for calculating their own Flac requirements applying the rates for market premium, and resolvability rebate that will be provided by the RA?</p> <p>We suggest that calculation of the requirement by the authority, using standardised criteria would be a preferable approach as it would ensure a proper degree of convergence so that banks with similar risk profiles</p>	<p><i>The FSB Key Attributes are international standards that must be applied by member jurisdictions. However, the Key Attributes allow for the adoption by jurisdictions in a manner that takes into account the characteristics of the particular jurisdiction and the regulatory structure of its financial sector. To this end, the RA calibrates the Flac requirement, including setting the requirement for the resolvability rebate and market premium, and DIs are then expected to apply these requirements.</i></p>

			and resolvability will have a similar requirement. Judgment by the authority over a number of qualitative criteria is also an important part of the final calibration.	
87.	BASA	No reference	<p>The draft standard does not make clear how the following will be considered in calibration of an individual bank's requirement:</p> <ul style="list-style-type: none"> a. Adjustment to post-resolution projected Pillar 2 requirements based on resolution strategy. b. If/how the authority will take into account the size, business model, funding model and risk profile of a DI when calibrating final Flac requirement and how liaison between the PA and RA will be established to avoid double counting of risk add-ons. 	<p><i>The PA supervises banks and is responsible for stipulating the minimum capital requirement for each bank (including Pillar 2B requirements based on the risk profile of that bank).</i></p> <p><i>The RA is responsible for the resolution of DIs. To effectively execute an open-bank resolution strategy, sufficient recapitalisation capacity (i.e. Flac requirements) is required.</i></p> <p><i>The basis for the Flac requirement is:</i></p> <ul style="list-style-type: none"> <i>1. to recapitalise the DI to a level that meets the minimum regulatory capital by the PA (meaning the RA does not stipulate the required minimum requirements, but uses what the PA has stipulated); and</i> <i>2. to provide the market with confidence that it will continue operating as a going concern, so that the DI can obtain funding post- resolution (this portion can only be performed when the RAP process has commenced).</i> <p><i>It is challenging to predict the eventualities of a stress and the actual impact thereof; therefore prudence is required in setting requirements to ensure there is sufficient resources for resolution purposes.</i></p>

