

2004-09-21

TO ALL BANKS, BRANCHES OF FOREIGN BANKS AND MUTUAL BANKS

BANKS ACT CIRCULAR 15/2004

NEW CAPITAL ACCORD (“BASEL II”) – GAP ANALYSIS AND READINESS ASSESSMENT

1. Executive Summary

In order to determine their readiness for the implementation of Basel II, all banks, branches of foreign banks and mutual banks (“banks”) in South Africa are requested to perform a self-assessment.

With a view to introducing the gap analysis and readiness assessment, as well as related templates, banks are invited to a meeting, which will be held on 5 October 2004, from 09:00 to 12:00, at the South African Reserve Bank Conference Centre, in Pretoria.

Banks are required to submit the results of the gap analysis and readiness assessment to this Office by 15 December 2004.

2. Introduction

On 26 June 2004, the Basel Committee on Banking Supervision issued a publication, titled [International Convergence of Capital Measurement and Capital Standards: a Revised Framework](#) and commonly referred to as Basel II.

It is envisaged that the implementation of Basel II in South Africa will include, *inter alia*, the following four key steps:

- (a) Familiarisation with Basel II and its implications.
- (b) Gap analysis and readiness assessment. This entails establishing both the current and the intended status of a bank with regard to the goal of implementing Basel II within the bank.
- (c) Impact study. The objective of the impact study is to establish the anticipated impact of Basel II implementation on a bank. Typically, this would also entail cost-benefit analyses. In addition to qualitative assessments, quantitative impact studies may be performed. This Office intends requiring banks to undertake a further quantitative impact study focusing on the impact of Basel II on capital requirements. Banks will be informed of the details in a circular to be released soon.
- (d) Based on the results of the foregoing, a bank would be in a position to generate a meaningful implementation plan for the proposed project. This Office will interact with banks regarding their implementation plans and implementation progress.

3. Indications of intended approaches under pillar 1 of Basel II

In Banks Act Circular 14/2003, banks were requested to indicate which of the approaches made available in terms of pillar I of Basel II they anticipated choosing. The results of the survey are summarised in the following table:

Risk area	Approach	Percentage distribution	
		Base: Total assets	Base: No. of banks
Credit	Simplified standardised	0,7%	40,6%
	Standardised	1,9%	10,8%
	Foundation internal ratings based ("IRB")	90,0%	27,0%
	Advanced IRB	7,4%	21,6%
Totals		100,0%	100,0%
Operational	Basic indicator	1,4%	43,2%
	Standardised	72,1%	32,4%
	Advanced measurement	26,5%	24,3%
Totals		100,0%	100,0%

4. Gap analysis and readiness assessment

In order to determine their readiness for the implementation of Basel II, all banks in South Africa are requested to perform a self-assessment of the gap between their current and their intended status with regard to the goal of implementing Basel II.

In order to achieve some comparability between and to draw conclusions from the outcomes of the self-assessments to be performed by banks, it was decided to furnish each bank with a standardised set of templates to be used in performing the gap analysis and readiness assessment.

An international firm consulting on Basel II has offered to make available, free of charge, its internally developed high-level gap-analysis and readiness-assessment templates for this purpose. Since international research has been incorporated into these templates, it was decided to accept the offer. Use of these templates, however, does not constitute an implicit or explicit endorsement of the firm or of the firm's gap-analysis and readiness-assessment templates by the South African Reserve Bank. In order to protect the firm's intellectual property rights in its gap-analysis and readiness-assessment templates, each bank using these templates is required to furnish the firm with a signed letter on the bank's letterhead, in the format set out in Annexure A. Please note that in terms of the agreement reached with the firm, only banks that have furnished this Office with such a signed letter may be furnished with copies of the gap-analysis and readiness-assessment templates. Accordingly, please ensure that the signed letters, marked for the attention of Carel Oosthuizen, reach this Office by not later than 5 October 2004.

Upon finalisation of the gap analysis and readiness assessment, banks are required to submit the results thereof to this Office by 15 December 2004, in electronic format and to the following e-mail address: Nicolette.VanZyl@resbank.co.za.

5. Meeting to introduce the gap analysis and readiness assessment, as well as related templates

In order to introduce the gap analysis and readiness assessment, as well as the related templates, a meeting will be held on 5 October 2004, from 09:00 to 12:00, at the South African Reserve Bank Conference Centre, which is attached to the South African Reserve Bank head office building, located at 370 Church Street, Pretoria. Each bank is requested to send at least one representative, ideally, the person responsible for Basel II implementation within the particular bank to this meeting.

Please furnish the information set out in Annexure B hereto to Nicolette van Zyl by 30 September 2004. Ms Van Zyl can be contacted at telephone number 012 313 4283, or telefacsimile number 012 313 4864, or by e-mail, at Nicolette.VanZyl@resbank.co.za.

The programme for the meeting is as follows.

Starting time	Topic	Speaker
08:30	Registration and refreshments	
09:00	Welcome and logistics	Carel Oosthuizen
09:15	Basel II and South Africa	Errol Kruger
10:00	Refreshments	
10:30	Gap analysis and readiness assessment: Introduction to and application of the templates	Trevor Adams
12:00	Wrap-up and closing	

6. Acknowledgement of Receipt

Two additional copies of this circular are enclosed for the use of your institution's independent auditors. The attached acknowledgement of receipt, duly completed and signed by both the chief executive officer of the institution and the said auditors, should be returned to this Office at the earliest convenience of the aforementioned signatories.

E M Kruger
Registrar of Banks

The previous circular issued was Banks Act Circular 14/2004 dated 20 September 2004.

Annexure A

30 September 2004

Messrs Mercer Oliver Wyman
99 Park Avenue
New York, NY 10016
United States of America

Attention: Alexander Lis

Dear Sirs

USE OF BENCHMARKING TOOLS

We understand that we are being provided with a set of benchmarking tools prepared by Mercer Oliver Wyman, a division of Mercer Management Consulting, Inc. ("MOW"), and relating to Basel II compliance, more specifically the *Basel II Business Requirements and Readiness Assessment* (collectively, the "Tools").

In consideration for receiving the Tools, we ("the Bank") hereby acknowledge and agree that:

- a. the Tools may be used by the Bank for internal benchmarking purposes only, and shall not be used for any commercial purpose;
- b. only those of the Bank's employees who need to access the Tools, in connection with the Bank's proper use thereof, shall be permitted such access, and each such employee shall be made aware of, and shall agree to abide by, the terms of this letter prior to having such access;
- c. the Bank shall not distribute or otherwise communicate the Tools (in whole or in part) to any person without the prior written consent of MOW, which may be withheld for any reason;
- d. the terms of this letter shall apply to any additional or supplementary information related to the Tools that is provided to the Bank, in whatever format, either in writing or orally;
- e. MOW makes no representation or warranty regarding the Tools, and is not providing any advice or recommendation to the Bank with respect to the Tools;
- f. MOW shall not have any liability to the Bank in respect of the Tools or the Bank's use thereof; save that MOW warrants that it has the legal right to give possession and use of the Tools to the bank as contemplated; and

- g. the Bank shall indemnify and hold MOW harmless from and against any liability, loss, damage, cost or expense that MOW may incur resulting or arising from the use of the Tools by the Bank, or the breach by the Bank of any of the terms of this letter; save that MOW indemnifies the Bank against any claims to the extent brought against the bank as a consequence of the breach by MOW of the warranty relating to the legal right to give possession and use of the Tools in clause (f) above.

In addition to the foregoing, in the light of the fact that the Tools will be provided to the Bank by the Office of the Registrar of Banks (the "ORB"), the Bank hereby acknowledges and agrees as follows:

- b. The involvement of the ORB in the distribution and delivery of the Tools, and/or any additional or supplementary information related to the Tools, shall not in any way, directly or indirectly, be construed as any –
 - (i) representation or warranty regarding the tools;
 - (ii) provision of advice or recommendation in respect of the Tools; or
 - (iii) endorsement, confirmation or promotion of the Tools.

- b. The ORB, in its distribution and delivery of the Tools, and/or any additional or supplementary information related to the Tools –
 - (i) does not act as an agent, mandatory or representative of MOW; and
 - (ii) shall not, directly or indirectly, be liable towards MOW, the Bank or to any other party to whom it has distributed or delivered the same.

This letter shall be governed by the laws of England. All disputes arising out of or relating to this letter shall be settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with such Rules.

By signing and delivering this letter to MOW (c/o Carel Oosthuizen, Bank Supervision Department, South African Reserve Bank, PO Box 8432, Pretoria, 0001), we hereby evidence our understanding and agreement with the foregoing.

Yours sincerely

.....
(Signature)

.....
(Print Name)

.....
(Title)

.....

(Date)

Acknowledged and Agreed:

Mercer Oliver Wyman, a division of Mercer Management Consulting, Inc.

.....
(Signature)

.....
(Print Name)

.....
(Title)

.....
(Date)

Annexure B

Name of Bank	
Name of first representative attending meeting	
Contact details of representative <ul style="list-style-type: none"> • Phone • Fax • Cell • E-mail 	<hr/> <hr/> <hr/>
Vehicle registration no.	
Name of second representative attending meeting	
Contact details of representative <ul style="list-style-type: none"> • Phone • Fax • Cell • E-mail 	<hr/> <hr/> <hr/>
Vehicle registration no.	
Name of third representative attending meeting	
Contact details of representative <ul style="list-style-type: none"> • Phone • Fax • Cell • E-mail 	<hr/> <hr/> <hr/>
Vehicle registration no.	