

**Prudential Standard RA01: Stays on Early-Termination Rights and Resolution Moratoria on Contracts of Designated Institutions in Resolution**

**Consultation Report**

1. **Purpose**
	1. Section 104 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) as amended by the Financial Sector Laws Amendment Act, 2021 (Act No. 23 of 2021) (the Act) stipulates that with each regulatory instrument, the maker must publish a consultation report which must include:

(a)     a general account of the issues raised in the submissions made during the consultation; and

(b)     a response to the issues raised in the submissions.

* 1. The purpose of this document is to set out, as required in terms of section 104 of the Act, a report on the consultation process undertaken in respect of the draft prudential standard relating to stays on early-termination rights and resolution moratoria on contracts of designated institutions in resolution.
1. **Summary of consultation process and general account of issues raised**
	1. On 15 September 2022, the Prudential Authority published the following documents for public comment, with the due date for comments being 4 November 2022:
2. Notice regarding the publication of the draft Prudential Standard – Stays on Early-Termination Rights and Resolution Moratoria on Contracts of Designated Institutions in Resolution (Standard) inviting comments on the Prudential Standard;
3. The Standard;
4. Statement of the need for, intended operation of and expected impact of the proposed Standard; and
5. A Comment Template.
	1. A total of 90 comments were received from 8 respondents through the public consultation process. The comments received were considered and where appropriate, these resulted in editorial refinements and updates to the proposed Standard.
	2. A general account of issues raised during the consultation process and the response of the Prudential Authority and the Reserve Bank (the Authorities) is set out in **Table 1** below. Details of the commentators and the full set of comments and the Authorities’ responses are detailed in **Table 2** and **Table 2.1** below.
	3. The published comment template included a set of questions to solicit industry inputs on the expected impact of implementing the proposed Standard. The industry inputs received in this regard have been used to update the statement of expected impact of the proposed Standard.
	4. As part of the public consultation process, the South African Securities Lending Association, the International Swaps and Derivatives Association as well as the International Capital Markets Association jointly with the International Securities Lending Association made submissions and proposals on certain policy issues that, while relevant for the broader resolution framework and the Act in particular, were found to fall beyond the scope of the proposed Standard. To ensure that the making of this prudential standard continues without undue interruptions, separate engagements have been initiated with the industry bodies concerned as well as the other authorities involved in the development of the South African resolution policy on these matters. A themed summary of these issues is provided in **Table 3** below.

**Table 1** – General account of issues raised

|  |  |  |
| --- | --- | --- |
| **Area** | **Summary of comment** | **Response** |
| Definitions | Request for reconsideration and/ or refinement of certain definitions and clarity on certain terms used in the draft Standard. | The definitions paragraph was amended in line with the comments received. * The definitions for “the Act”, “compliant covered contract”, “contractual recognition”, “covered contract”, “Reserve Bank”, and “termination right” were refined.
* The definitions for “master agreement” and “payment system” were expanded to provide more clarity.
* The definition of “pre-existing contracts” together with all references to “pre-existing” contracts were deleted from the revised proposed Standard to eliminate unintended ambiguity. The information related to covered contracts that exists before the coming into effect of the Standard will be extrapolated from the information on the inception date of the relevant contracts. Paragraph 8.4 of the revised standard has been expanded to include this under minimum required information.
* The definition of terms already included in the Act were deleted from the proposed Standard.
 |
| Application of the draft Standard | Request for clarification on the application of the draft Standard to other entities who are members of a designated financial conglomerate.  | Clarification was provided in the form of confirmation that the proposed Standard will apply to all designated institutions as defined in the Act. It is further clarified that in line with the provisions under section 29A(2) of the Act, the Governor is empowered to determine that the person or body that is a designated institution by virtue of being a member of a financial conglomerate is not a designated institution. Designated Institutions are advised to focus on the banking operations until further clarity in relation to resolution groups is provided by the Reserve Bank. |
| Contractual recognition requirements  | Request for clarification of the requirement for independent review of the legal enforceability of contractual provisions. | The wording in the relevant paragraphs of the proposed Standard (see paragraphs 7.4 and 10.4 of the revised proposed Standard) has been streamlined to provide clarity on the requirement for independent review of the legal enforceability of contractual provisions. |
| Governance | Request for clarification of the reporting requirements. | The wording under paragraph 10 has been refined to improve clarity of the reporting requirements therein. |
| General compliance requirements | Request for reconsideration of the proposed measures to be taken by the Prudential Authority in cases of non-compliance.  | The Authorities maintains that the stated consequences for non-compliance with the requirements under paragraph 9 of the revised proposed Standard are reasonable. |

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**Commentators and full set of comments**

**Table 2** - Details of the commentators

|  |  |  |  |
| --- | --- | --- | --- |
| **No.** | **Name of organisation** | **Acronym** | **Contact person** |
| **1.** | Banking Association South Africa | BASA | Benjamin AprilGeneral Manager: Prudential Division |
| **2.** | Bank of China Limited JHB Branch | BOCA | Ashley CameronSenior Executive Vice President |
| **3.** | Financial Sector Conduct Authority | FSCA | Hannelie HattinghSenior Manager Regulatory Framework |
| **4.** | The International Capital Markets Association**\*** | ICMA | Deena Seoudy Senior Director, Associate Counsel |
|  | The International Securities Lending Association**\*** | ISLA | Tina Baker Head of Legal Services |
| **5.** | International Swaps and Derivatives Association Inc. | ISDA | Dr Peter Werner Senior Counsel |
| **6.** | Nedbank Limited | Nedbank | Michelle Frederick |
| **7.** | South African Securities Lending Association | SASLA | Michael Wright |
| **8.** | Standard Bank Group | SBG | Annelie Schnaar-Campbell |
| **\***The ICMA and ISLA submitted their comments jointly and have been deemed as a single respondent for the purposes of this consultation report.  |

**Table 2.1** – Detailed comments and responses

| **No** | **Commentator** | **Paragraph** | **Comment** | **Responses** |
| --- | --- | --- | --- | --- |
| **COMMENTS ON STANDARD** |
| **Commencement** |
|  |  | 1 | NO COMMENTS |  |
| **Legislative authority** |
|  |  | 2 | NO COMMENTS |  |
| **Definitions and interpretation** |
|  | BASA | 3.1 | “Termination right” Termination rights should be defined with reference to an event of default. | The Authorities disagree with the proposal because it is inconsistent with the principle provided for under sections 166L and 166R(4) of the Act. These sections of the primary legislation only reference the placing or proposal to place a designated institution in resolution.  |
|  | BASA | 3.1 | “Payment System” The Financial Sector Laws Amendment Act refers to the definition in the National Payments Systems Act, 78 of 1998. It is recommended that a new definition not be created and that the cross-reference to the National Payment Systems Act be referenced. | The comment is noted. The definition has been amended in line with the comment. |
|  | BASA | 3.1 | “Governing Body” In the Financial Markets Act - “senior management” refers to the level of management that is directly accountable to the chief executive officer or the person in charge of an entity and includes the chief executive officer if that person is not a director of the entity OR refer to members of the controlling body (which could be the Board of Directors, all depending on the nature of the particular company). A specific reference to the Board can then be stipulated when required. It is recommended that the definition of “governing body” be replaced with “senior management” as defined in the Financial Markets Act. | The Authorities disagree with the proposal. It is an established principle that the governing body is ultimately responsible for the management of an entity. |
|  | BASA | 3.1 | “Master Agreement” - The definition of a master agreement is very specific, for instance, it omits the “Global Master Securities Lending Agreement” master agreements as published by the International Securities Lending Association (ISLA). It is recommended that the definition be defined more broadly. | The comment is noted. The definition has been amended to reference the definition in section 35B(2) of the Insolvency Act, 1936 (Act No. 24 of 1936). |
|  | BOCA | 3.1 | No comment. | Noted. |
|  | FSCA | 3.1 | “the Act” We recommend that the words “(FSR Act)” be removed from the definition as it does not serve a purpose. | The comment is noted. The definition has been amended in line with the comment. |
|  | FSCA | 3.1 | "Master agreement" is defined in section 35B of the Insolvency Act,1937. Is there a particular reason why the legal definition in the Insolvency Act has not been adopted as is in this Standard, even if it is by reference to the provision of the Insolvency Act? Or is the intention to exclude certain specific contracts? If so, has such a deviation considered the probable consequences of inconsistency when applied by Tribunals or Courts? | The comment is noted. The definition has been amended to reference the definition in section 35B(2) of the Insolvency Act, 1936 (Act No. 24 of 1936). |
|  | FSCA | 3.1 | “orderly resolution of a designated institution” This term is already defined in section 1 of the FSR Act and the preamble in the Standard states that in the Standard, any word or expression to which a meaning has been assigned bears the meaning so assigned to it by the Act. Defining the term in the Standard again therefore results in unnecessary duplication and is superfluous (practically and in law). Further, if the PA maintains that it wants to include it as a defined term, it is unclear why the definition repeats the content of the definition which is already included in the FSR Act (therefore not only defining the term is superfluous but defining the term and repeating the content is further superfluous). If the definition is to be retained, rather cross-reference the definition in the FSR Act (i.e., “has the meaning assigned to term in section 1 of the Act). There is also a slight misalignment between the content of the definition in the Standard and the definition in section 1 of the FSR Act, i.e. paragraph (a) of the definition in the Standard refers to “maintains financial stability” whilst paragraph (a) of the definition in the Act refers to “assists in maintaining financial stability”. There shouldn’t be any misalignment between the two definitions. | The comment is noted. Definitions of terms already defined in the Act have been deleted. |
|  | FSCA | 3.1 | “Payment system” It is unclear why a definition for “payment system”, that is separate and different from the definition of “payment system” in the National Payment System Act (NPS Act), is necessary. Shouldn’t there be alignment considering that the NPS Act is the primary law governing payment systems? We recommend that the NPS Act definition is rather cross-referenced unless there is specific reason why that definition is not appropriate in the context of this Standard. | The comment is noted. The definition has been amended in line with the comment. |
|  | FSCA | 3.1 | “Pre-existing contract” For the sake of clarity, it is recommended that this definition be revised to cater expressly for *prior to the coming into force…of [either the Standard or the Financial Sector Regulations Act as amended in Chapter 12A],* as the following wording in the definition is a bit vague/unclear (as it does not give an indication of the exact requirements this is referring to nor when those requirements came into effect):“coming into force of the provisions relating to stays on early termination rights and moratoria on contracts of designated institutions in resolution;”In addition, as a pre-existing contract is defined as a covered contract, does this mean all requirements in the Standard will immediately apply to all pre-existing contacts? If so, is this reasonable and/or should there be some transitional arrangements in this respect? | The comment is noted. Upon mature reflection and analysis and to effectively remedy the confusion arising from the use of this term/concept, a decision has been taken to delete the definition and all references to “pre-existing contracts” from the proposed Standard. The information that would have been obtained in relation to covered contracts that existed prior to the coming into force of the Standard can be obtained as part of the requirements under paragraph 8.4 of the revised proposed Standard. |
|  | FSCA | 3.1 | “Termination right” It is recommended that ***to***preceding *prevent* in paragraph (b) be deleted. | The comment is noted. The definition has been amended in line with the comment. |
|  | ICMA and ISLA | 3.1 | No comment. | Noted. |
|  | ISDA | 3.1 | “Designated Institution in Resolution” Please clarify how the Draft Prudential Standard will operate and be applicable in respect of branches of foreign institutions established under the Banks Act, 1990 | The comment is noted. We confirm that the proposed Standard will be applicable to a branch because in terms of the Act, a bank is a designated institution whereas a bank is defined as –  “bank” means each of the following: 1. a bank as defined in the Banks Act;
2. a branch as defined in the Banks Act;
3. a mutual bank as defined in the Mutual Banks Act, 1993 (Act No. 124 of 1993); or
4. (d) a co-operative bank as defined in the Co-operative Banks Act, 2007 (Act No. 40 of 2007);
 |
|  | ISDA | 3.1 | “Contractual recognition approach” If a covered contract already includes an acknowledgement and acceptance of resolution stays in general, or of the resolution stays imposed in terms of EU, UK or US regimes, will it be necessary to include additional language in these contracts specifically referring to the stay that can be imposed by the South African Reserve Bank in terms of the Draft Prudential Standard? | The comment is noted. The contractual recognition approach as provided for in the proposed Standard aims to facilitate the recognition of South African resolution stays in covered contracts. It will therefore be necessary to make specific provision for South African resolution stays in the relevant contracts. |
|  | Nedbank | 3.1 | No comment. | Noted. |
|  | SASLA | 3.1 | the definitions of 'designated institution', 'designated institution in resolution', 'governing body', 'market infrastructure', 'orderly resolution of a designated institution' and 'payment system' are already defined in the Act and are therefore not needed and should be deleted.  | The comment is noted. Definitions of terms already defined in the Act have been deleted. |
|  | SASLA | 3.1 | The definition of 'compliant covered contract' should be amended to delete the words "agree to", as the provisions in the compliant covered contract are the agreement. | The comment is noted. The definition has been amended in line with the comment. |
|  | SASLA | 3.1 | The definition of 'master agreement' as being an ISDA restricts the applicability of 5.6(e) to ISDAs only, meaning that while a securities lending transaction may be a covered contract, the GMSLA governing it may not be. In line with our comments in the Annexure, the definition of 'master agreement' should rather cross-refer to the definition of 'master agreement' in section 35B(2) of the Insolvency Act. | The comment is noted. The definition has been amended to reference the definition in section 35B(2) of the Insolvency Act, 1936 (Act No. 24 of 1936). |
|  | SASLA | 3.1 | should the definition of 'pre-existing contract' not refer to contracts concluded prior to a designated institution's entry into resolution? This would avoid confusion as to whether the effect of the moratoria or the effect of the stays (which could be at a different time) is the cut-off time for the definition. | The comment is noted. Upon mature reflection and analysis and to effectively remedy the confusion arising from the use of this term/concept, a decision has been taken to delete the definition and all references to “pre-existing contracts” from the proposed Standard. |
|  | SASLA | 3.1 | For consistency the definition of 'SARB' should be deleted and the defined term 'Reserve Bank' from the Act should be used throughout the draft Standard. | The comment is noted. Where relevant, the proposed Standard has been amended in line with the comment. |
|  | SBG | 3.1 | No comment. | Noted. |
| **Roles and responsibilities** |
|  |  | 4 | NO COMMENTS |  |
| **Application** |
|  | BASA | 5.4. | Is the intention for the Standard to apply to the entire group, i.e., all covered contracts within all group entities or only entities that provide critical functions? This will be significantly more intensive where it applies across all group entities irrespective of its country of incorporation. | The proposed Standard applies to all designated institutions as defined. It is however worth noting the provisions under section 29A(2) of the Act which empowers the Governor to determine that the person or body that is a designated institution by virtue of being a member of a financial conglomerate is not a designated institution. Designated Institutions are advised to focus on the banking operations until further clarity in relation to resolution groups is provided by the Reserve Bank. |
|  | BASA | 5.5. | Termination right is defined but not early termination right. Hence the suggestion that termination right is defined with reference to an event of default. | The Authorities disagree with the proposal. The proposed Standard is consistent with the primary legislation which only reference the placing or proposal to place a designated institution in resolution.  |
|  | BASA | 5.6. | Section 5.5 states that the Standard applies to “covered contracts governed under foreign law and with early termination rights. Section 5.6 states that, further to paragraph 5.4, the Standard applies to specific financial contracts. | The comment is noted. Paragraph 5 of the proposed Standard has been revised to improve clarity and readability. The wording under 5.5 has been repositioned under the definitions part of the proposed Standard. |
|  | BOCA | 5. | No comment. | Noted. |
|  | FSCA | 5.3. | We note the proposed exclusions, but there is no information in the e.g. Statement of Need, Impact etc (SoN) explaining why these exclusions are necessary (e.g. in relation to market infrastructures and payment systems). We strongly recommend that the SoN expands on the proposed scope, and specifically the exclusions. | The comment is noted. the Statement explaining the need for, the intended operation of and the expected impact of the proposed Standard (the Statement) has been revised to expand and refine the relevant paragraph in line with the comment.  |
|  | FSCA | 5.5. | It is recommended that the part reflected in the extract below is rather moved to the definition paragraph (paragraph 3.1) and replace the proposed definition of “covered contract”, which currently merely cross-reference to the extract below. We submit that this will be a ‘cleaner’ approach.“For purposes of this Standard, ‘covered contracts’ mean contracts that: 1. are governed under foreign law; and
2. contain provisions for early termination rights.”

Further, is this definition not perhaps too wide? | The comment is noted. The proposed Standard has been amended in line with the comment. Regarding the possibility of the definition being too wide, the word “specified” has been inserted in the definition to limit the scope of thereof.  |
|  | FSCA | 5.6. | See our comment in respect of the definition of “pre-existing contracts”. It is unclear whether the existing contracts already make provision for these requirements. If they do not, there will need to be a transition period for the insurers to recontract accordingly. | The comment is noted. Upon mature reflection and analysis and to effectively remedy the confusion arising from the use of this term/concept, a decision has been taken to delete the definition and all references to “pre-existing contracts” from the proposed Standard. |
|  | FSCA | 5.7. – 5.9. | Paragraphs 5.7 to 5.9 does not seem to impose any legal obligations (which is what subordinate legislation is supposed to do). Paragraph 5.7 merely restates the law (FSR Act) and paragraphs 5.8 and 5.9 seems to give guidance. We submit that it would therefore be more workable to deal with paragraphs 5.7 to 5.9 in guidance, the statement of need or a supporting communication, and not in subordinate legislation which is intended to impose legal requirements. We note that the Statement of Need also has provisions touching on this (starting from paragraph 3.3). Therefore, the best approach might be to move these paragraphs to that part of the Statement of Need. | The comment is noted. The proposed Standard has been amended in line with the comment and the content of the paragraphs in questions has been incorporated into the Statement. |
|  | ICMA and ISLA | 5. | No comment. | Noted. |
|  | ISDA | 5. | No comment. | Noted. |
|  | Nedbank | 5. | No comment. | Noted. |
|  | SASLA | 5.3. | The "Principles for Financial Market Infrastructures" must be defined. | The comment is noted. A definition of the principles for financial market infrastructures has been included in the revised proposed Standard. |
|  | SASLA | 5.6. | The reference to "paragraph 5.4 above" should refer to paragraph 5.5. | The comment is noted. The cross-referencing has been addressed in the revised proposed Standard. |
|  | SASLA | 5.6(e) | 'Master agreement' is defined in paragraph 3.1 as being an ISDA only, and thus paragraph 5.6(e) would apply to an ISDA covering derivatives, securities lending transactions and repo transactions (but not a GMSLA or a GMRA). The effect of the definition of 'master agreement', plus paragraph 5.6 (e) is that the Standard purports to limit the application of the Standard to ISDAs only. In line with our comments in the Annexure, the definition of 'master agreement' in 3.1 could refer to section 35B(2) of the Insolvency Act, 1936. | The comment is noted. The definition in the proposed Standard has been amended to reference the definition in section 35B(2) of the Insolvency Act, 1936 (Act No. 24 of 1936). |
|  | SBG | 5.5. | Please clarify if the Standard applies only to those contracts that are governed under foreign law?The definition of ‘covered contracts’ narrows the scope of s166L - there are other types of agreements which may contain acceleration events. Is it the intention to exclude other agreements from the application of these sections?We believe that Global Master Repurchase Agreements (“GMRA”) and Global Master Securities Lending Agreements (“GMSLA”) should be included in the “master agreement” definition and afforded the same protection as an International Swaps and Derivatives Association master agreement (“ISDA”), set out in paragraph 5.6(e). | The Authorities disagree with the comment as it relates to the definition of ‘covered contracts’. The proposed Standard complements the provisions under section 166L of the Act in that it facilitates the application of the South African resolution framework to specified contracts governed under foreign laws.Regarding the definition of ‘master agreement’, the definition has been amended in the revised proposed Standard to reference the definition in section 35B(2) of the Insolvency Act, 1936 (Act No. 24 of 1936). |
| **Contractual recognition in contracts governed by foreign law** |
|  | BASA | 6. | No comment. | Noted. |
|  | BOCA | 6. | No comment. | Noted. |
|  | FSCA | 6. | No comment. | Noted. |
|  | ICMA and ISLA | 6. | No comment. | Noted. |
|  | ISDA | 6. | No comment. | Noted. |
|  | Nedbank | 6. | No comment. | Noted. |
|  | SASLA | 6.1. | The stay in paragraph 166L is not temporary, as it states that certain provisions of an agreement are of no effect. The word "temporary" in paragraph 6.1 should be deleted. Furthermore, this appears to be saying the same thing as paragraph 7.1, but in slightly different words. | The comment is noted. The proposed Standard has been amended in line with the comment. |
|  | SBG | 6. | No comment. | Noted. |
| **Contractual recognition requirements** |
|  | BASA | 7.4. | This section requires a designated institution to undertake an “independent review” of the legal enforceability of its contractual provisions. Section 7.4 then requires the review to be carried out by the designated institution’s legal function or independent third party. It is not clear what is meant by “independent” given that an internal legal review will suffice. | The comment is noted. The proposed Standard has been amended in line with the comment. The requirement for an independent review has been moved to paragraph 10.4 of the revised proposed Standard. |
|  | BOCA | 7. | No comment. | Noted. |
|  | FSCA | 7. | No comment. | Noted. |
|  | ICMA and ISLA | 7. | No comment. | Noted. |
|  | ISDA | 7. | No comment. | Noted. |
|  | Nedbank | 7. | No comment. | Noted. |
|  | SASLA | 7.1. | This paragraph says the same thing as paragraph 6.1. | The comment is noted. We are of the view that while the paragraphs in question are closely aligned, they differ in, albeit marginally, in that paragraph 6.1 merely requires the adoption of the contractual recognition approach, while paragraph 7.1 addresses the practical aspect of the contractual recognition approach. |
|  | SASLA | 7.3. | This paragraph should refer to covered contracts. | The comment is noted. The proposed Standard has been amended in line with the comment. |
|  | SBG | 7. | No comment. | Noted. |
| **Governance requirements** |
|  | BASA | 8.2. | What is meant by “in a timely manner”? | The phrase is meant to be case dependent and has the ordinary meaning which means “*to complete/perform within the required time*”. |
|  | BOCA | 8. | No comment. | Noted. |
|  | FSCA | 8. | No comment. | Noted. |
|  | ICMA and ISLA | 8. | No comment. | Noted. |
|  | ISDA | 8. | No comment. | Noted. |
|  | Nedbank | 8. | No comment. | Noted. |
|  | SASLA | 8. | No comment. | Noted. |
|  | SBG | 8. | No comment. | Noted. |
| **General compliance requirements** |
|  | BASA | 9.2. | It is unclear as to what would constitute non-compliance with the standard. Is it that after the phase-in period one contract that should have included clauses to amend the contract has not? Does it matter if best efforts (multiple reaches out to clients were undertaken and requirements explained)? | The phrase bears the ordinary meaning. The proposed Standard does not make provision for best efforts in the context of compliance. The test for compliance will be an objective test |
|  | BASA | 9.2. | The actions listed under section 9.2 are severe relative to the risk introduced to financial stability: * Is the Flac holdings increase a reference to a lower resolvability rebate as stipulated in the “Proposed principles and requirements for Flac instruments” discussion paper?
* An increase in capital requirements (the increment of which is unclear) is disproportionate to the failure to comply with the Standard, as well as the purpose that the Standard is trying to achieve as increased capital requirements lower profitability and thus erode risk-bearing capacity.
* Clarification is requested on the reason for the “acceleration in the triggering of resolution” as a consequence of non-compliance.
 | The Authorities maintains that the proposed consequences for non-compliance with the proposed Standard are reasonable. The point raised in relation to the resolvability of designated institutions is correct. It is worth noting that the proposed Standard forms part of a suite of measures that are being developed to improve the resolvability of designated institutions in the South African market. The acceleration in the triggering of resolution relates to instances where a designated institution that is non-compliant with the requirements under the proposed Standard is facing challenges given that non-compliance imply lower resolvability.  |
|  | BOCA | 9. | No comment. | Noted. |
|  | FSCA | 9.2(a) | Should the term “Flac instrument” perhaps be defined, or is the general meaning of the term sufficiently understood? | The comment is noted. The term is already defined in the Act. |
|  | ICMA and ISLA | 9. | No comment. | Noted. |
|  | ISDA | 9. | No comment. | Noted. |
|  | Nedbank | 9. | No comment. | Noted. |
|  | SASLA | 9. | No comment. | Noted. |
|  | SBG | 9. | No comment. | Noted. |
| **Reporting requirements** |
|  | BASA | 10.1. | Section 10.1 requires that a designated institution “must” report whereas section 10.2 states that a designated institution must “on request by the Prudential Authority” report. | The comment is noted. The proposed Standard has been amended to address the unintended confusion. |
|  | BASA | 10.3. | Section 10.3 is vague and refers to compliant covered contracts, non-compliant covered contracts, and pre-existing covered contracts. It is not clear why there is a need to separately refer to pre-existing covered contracts unless the intention is that the Standard does not apply to pre-existing covered contracts. | The comment is noted. References to “pre-existing” contracts have been deleted from the proposed Standard. |
|  | BOCA | 10. | No comment. | Noted.  |
|  | FSCA | 10.2. | Is the reporting contemplated in 10.2 not already covered by the reporting requirements in 10.1? | The comment is noted. The proposed Standard has been amended to address the unintended confusion. |
|  | FSCA | 10.3. | Should this be limited to the bilateral resolution planning work programme (and should the latter be defined/explained)? It might be more practical to merely phrase this more general, e.g. requesting further details as and when the SARB so requires (as opposed to limiting it to the work programme). | The comment is noted. The proposed Standard has been amended in line with the comment. |
|  | ICMA and ISLA | 10. | No comment. | Noted. |
|  | ISDA | 10. | No comment. | Noted. |
|  | Nedbank | 10. | No comment. | Noted. |
|  | SASLA | 10. | No comment. | Noted. |
|  | SBG | 10. | No comment. | Noted.  |
| **GENERAL COMMENTS** |
|  | BASA | N/A | No comment. | Noted. |
|  | BASA | N/A | No comment. | Noted. |
|  | BOCA | General | It is suggested that the SARB PA consider a reasonable time for the remediation (if any) of the legacy contracts to bring the latter into compliance with this Standard, possibly a two-year period. | The comment is noted. A reasonable time for implementation of the proposed Standard will be considered.  |
|  | FSCA | N/A | No comment. | Noted. |
|  | FSCA | N/A | No comment. | Noted. |
|  | ICMA and ISLA | N/A | No comment. | Noted. |
|  | ISDA | N/A | No comment. | Noted. |
|  | Nedbank | N/A | No comment. | Noted. |
|  | SASLA | N/A | No comment. | Noted. |
|  | SBG | N/A | No comment. | Noted. |

**Draft Prudential Standard RA01: Stays on Early-Termination Rights and Resolution Moratoria on Contracts of Designated Institutions in Resolution**

**Summary of policy issues raised by industry bodies**

**Table 3** – Summary of policy issues raised by industry bodies

| **Commentator** | **Submission summary** | **Response**  |
| --- | --- | --- |
| **General** |
| ICMA and ISLA | ICMA and ISLA fully support the principles underpinning orderly resolution of DIs and the need to maintain financial stability and protect the interests of depositors, creditors and shareholders of DIs in resolution. The comments set out in this letter are not intended to impede the process of finalising the Draft Standard. | The comment is noted. |
| ISDA | ISDA Inc. fully supports the principles underpinning orderly resolution of DIs and the need to maintain financial stability and protect the interests of depositors, creditors and shareholders of DIs in resolution. | The comment is noted. |
| SASLA | SASLA fully supports the aims of the FSLA Act and the Draft Standard, which respectively have established a framework for the Reserve Bank's resolution powers in respect of failing institutions and will clarify the Reserve Bank's specific powers to impose stays and moratoria on early termination rights. The comments are not intended to impede the process of finalising the Draft Standard. | The comment is noted. |
| **Legal certainty** |
| ICMA and ISLA | This current proposed treatment of GMSLA Transactions and GMRA Transactions gives rise to significant uncertainty and cuts across the manner in which these transactions have been dealt with in resolution regimes in Europe, the UK and elsewhere. If the Reserve Bank determines that it is necessary to cancel a GMSLA Transaction or a GMRA Transaction in terms of S166S(7)(b) of the FSRA, the consequence of such cancellation is unclear | The comment is noted. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately.  |
| ISDA | ISDA Inc. stresses that Chapter 12A of Financial Sector Regulation Act, 2017 (FSRA) cannot be declared effective until the fatal flaw discussed in these submissions has been remediedThe current language of the FSRA exposes securities lending and repo transactions to the SARB’s powers (i) to reduce amounts payable by the DI to its counterparty, and (ii) to cancel the agreement which documents the securities lending and repo transaction. | The comment is noted. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately.  |
| SASLA | The Reserve Bank has drafted the Resolution Framework in a way that maintains legal certainty in respect of ISDAs and derivative transactions, but not in respect of GMSLAs and GMRAs. Section 166S(9)(b) specifically provides that “derivatives” are excluded from the reduction and cancellation powers of the Reserve Bank in section 166S(7) when acting in its new role as resolution authority, but does not provide similar protection to repurchase and securities lending transactions. The result is a lack of clarity on how parties are to close out their GMSLAs and GMRAs on a cancellation by the resolution authority. | The comment is noted. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately.  |
| **Safeguards provided for in the Act** |
| ICMA and ISLA | We are aware of the proposed mitigating sections of the FSRA. None of the mitigating sections give sufficient clarity, objectivity, assurance or certainty for obtaining clean netting opinions that are a regulatory requirement in order for counterparties to be able to utilise close-out netting in the calculation of their regulatory capital requirements.Securities lending transactions and Repo transactions, can be documented under an ISDA. In fact, ISDA has recently published SFTR definitions, and the ISDA netting opinion includes securities lending and repo transactions. It is unclear why securities lending transactions and repo transactions would be excluded from the scope of S166S(7) if documented under an ISDA, but not if they are documented under a GMSLA/GMRA, the documents most widely used globally for securities lending transactions and Repo transactions.We understand that a view has been expressed that securities lending transactions and repo transactions may be sufficiently protected under Sections 166U, 166V and 166W of the FSRA. We note that: * there is significant uncertainty in relation to this point of view and that a number of market participants are of the view that these sections do not give adequate certainty in the case of securities landing and repo transactions.
* there is a suggestion that further subordinate legislation and prudential standards may be published in an attempt to clarify the treatment of securities lending transactions and repo transactions, but we are aware of the fact that there is concern in the market that subordinate legislation cannot extend beyond the scope of the enabling legislation (here the FSRA) and that the ability to effect any necessary changes through subordinate legislation is likely to be limited.

S166U of the FSLA Act ensures, inter alia, that the value of creditors' claims are not reduced by resolution action. It is unclear what the value is of a GMSLA or GMRA transaction counterparty's claim, when such counterparties are dependent on close-out netting rather than making claims in insolvent estates. In addition, this section operates in the Reserve Bank's subjective discretion and this introduces uncertainty as to whether or not S166U will apply. In addition, there does not appear to be any remedy for a counterparty that disagrees with the Reserve Bank's determination.S166W(1) is prefaced by the phrase: “Subject to the provisions of this Act...”. From a legal perspective, this wording creates doubt as it seems to suggest that the FSRA provisions in S166W(1) will override the Insolvency Act (which would negate any utility of S166W(1)).S166U and S166V both include language that suggests that the ostensible protections in these sections are subject to a subjective assessment by the Reserve Bank: “that in the Reserve Bank’s view” and “if it appears to the reserve Bank” and the Reserve Bank must “determine the amount of the shortfall” – these subjective assessments introduce uncertainty as to whether or not the ostensible protections contained in these sections are in fact available. If any resolution action taken in fact violates S166U to W, the remedies available to an affected counterparty are subject to an administrative process (which introduces timing risk to the market) and may leave the affected counterparty with an unsecured concurrent claim for compensation against the already distressed DI (which introduces the risk of not being settled in full). | The comment is noted. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately. |
| ISDA | During our meeting on 23 November 2021 and subsequent calls, we were advised that creditors under securities lending transactions and repo transactions would not be carved-out of the SARB’s bail-in powers in the same manner as “derivative instruments” (see section 166S(9)(b) of the FSRA) because counterparties must rather rely on the risk mitigants and purported safeguards set out in sections 166U and 166V of the FSRA. These sections do not provide the safeguards which were intended by the legislature.Section 166U(1) - The key principle of section 166U(1) of the FSRA is that resolution action must not be taken “if it appears to the Reserve Bank” that the action would result in a creditor’s claim being reduced. This provision does not provide legal certainty because the SARB has the sole discretion to determine whether or not a claim would be reduced.Section 166U(4) – the section attempts to provide a further safeguard by requiring that when resolution actions are taken, claims that would have the same ranking in insolvency must be treated equally. This safeguard does not mitigate risks as it will not apply if the SARB determines that it is necessary to treat the claims differently. This provision does not provide legal certainty because the SARB has the sole discretion to determine whether or not claims that have the same ranking in insolvency must be treated differently or equally.Section 166V - The key principle of section 166V(1) of the FSRA is that resolution action must not be taken if a creditor would receive less than what that creditor would have received had the DI been wound up. However, if a resolution is nonetheless taken and the SARB determines that the creditor has indeed received less than what it would have received had the DI been wound up, then the SARB must “determine the amount of the shortfall.”. This introduces risk as the SARB has a discretion in these circumstances. Of more concern is that if a shortfall indeed results, the creditor who has suffered the loss merely has a claim against the (already distressed) DI in resolution. | The comment is noted. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately. |
| SASLA | We are aware of the mitigating sections of the Act under the “creditor hierarchy and equality of claims” provisions (in section 166U), the “no creditor worse off rule” (in section 166V of the Act) and the preservation of the “ranking of creditors” (in section 166W of the Act), however, these mitigations should only apply to residual post-netting claims. None of the mitigating sections, (i.e. sections 166U, 166V and 166W) give sufficient clarity, protection or certainty for a clean netting opinion. Section 166U of the Act ensures, inter alia, that the value of creditors' claims are not reduced by resolution action. It is unclear what the value is of a GMSLA or GMRA counterparty's claim, when such counterparties are dependent on clean close-out netting rather than making claims in insolvent estates. This section operates in the Reserve Bank's discretion, and there does not appear to be any remedy for a counterparty that disagrees with the Reserve Bank's determination. Section 166V of the Act aims to ensure that no creditor receives less in resolution than the creditor would have received in a winding-up. Again, this section operates in the Reserve Bank's discretion, giving a counterparty that is "worse off" at best the potential for an unsecured claim against a financial institution that is already in uncertain financial circumstances. Section 166W of the FSLA act provides that claims against a designated institution in resolution will rank in the order provided in the Insolvency Act. The close-out netting provisions GMSLAs and GMRAs are intended to ensure that, to the extent possible, after effecting close-out netting the counterparties do not have claims. If they do have residual claims after close-out netting, these are unsecured claims.The purported remedies of section 166U, 166V and 166W of the Act are not sufficiently objective or certain to ensure that legal counsel can issue clean netting opinions in respect of GMSLAs and GMRAs once the Resolution Framework becomes effective in South Africa and these remedies should only apply to post-netting claims. | The comment is noted. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately. |
| **International practice** |
| ICMA and ISLA | Although derivative instruments concluded under an ISDA Agreement (ISDA Transactions) are exempted from S166S(7) of the FSRA, securities lending transactions concluded under a GMSLA (GMSLA Transactions) and sale and repurchase and reverse repurchase transactions (repos) concluded under a GMRA (GMRA Transactions) are not.This approach places South Africa out of step with the European EU Bank Resolution and Recovery Regime (BRRD) and United Kingdom (UK Banking Act, 2009 (UKBA) approach and international best practice in terms of which securities lending and repo transactions are treated in a similar manner to derivative transactions and are considered to be secured liabilities which are excluded from the ambit of the bail-in provisions of the resolution regimes, except in respect of residual claims arising after close-out netting. | The comment is noted. The Authorities remain committed to implementation of a resolution framework that is in line with international standards and best practices. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately. |
| ISDA | The current language of the FSRA exposes securities lending and repo transactions to the SARB’s powers (i) to reduce amounts payable by the DI to its counterparty, and (ii) to cancel the agreement which documents the securities lending and repo transaction. This is a significant departure from the global principles (in particular the European Union Bank Resolution and Recovery Regime and the United Kingdom Banking Act, 2009 (as per the Key Attributes)). | The comment is noted. The Authorities remain committed to implementation of a resolution framework that is in line with international standards and best practices. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately. |
| SASLA | The Resolution Framework, even as clarified by the Draft Standard, is inconsistent with international treatment of securities lending and repo transactions for banks in resolution. In the UK and European Union resolution regimes, securities lending and repo agreements are protected contracts and not subject to bail-in powers, except in respect of residual claims arising after close-out netting. | The comment is noted. The Authorities remain committed to implementation of a resolution framework that is in line with international standards and best practices. Efforts are underway to ensure that the concerns raised in the submission and during subsequent engagements between the Reserve Bank, the National Treasury and the industry bodies concerned are addressed adequately. |
| **Proposed remedy** |
| ICMA and ISLA | We are advised that there would be a relatively simple remedy to these undesirable consequences. The remedy would be to make it absolutely clear, in line with international practice, that securities lending transactions and repo transactions under a GMSLA / GMRA are intended to be treated in the same way as derivative transactions under an ISDA and are therefore: * subject to the stays per S166L of the FSRA (as will be the case per the Draft Standard);
* subject to the resolution moratoria per S166R of the FSRA (as will be the case per the Draft Standard); and
* exempt from S166S(7) of the FSRA, (which is not the case in the FSRA and has not been addressed in the Draft Standard or elsewhere).

The solution would be to promulgate an amendment to the FSRA which replaces S166S(9)(b) of the FSRA in its entirety with the carve-out: *“transactions concluded under “master agreements” as defined in Section 35B(2) of the Insolvency Act.”.* | The comment is noted. The Reserve Bank and the National Treasury are considering the most viable approach to resolve the issue in line with the remedy proposed by the industry bodies.  |
| ISDA | We submit that an amendment to the primary legislation (ie the FSRA) should be promulgated (Amendment Act) to replace section 166S(9)(b) of the FSRA in its entirety with the carve-out: *“transactions concluded under “master agreements” as defined in section 35B(2) of the Insolvency Act.”* | The comment is noted. The Reserve Bank and the National Treasury are considering the most viable approach to resolve the issue in line with the remedy proposed by the industry bodies.  |
| SASLA | The only certain way to solve the issues described above would be to amend the Act to provide that GMSLAs and GMRAs are treated identically to ISDAs and derivative instruments in resolution (e.g. by amendment to section 166S(9) to include GMSLAs and GMRAs). SASLA proposes that section 166S(9)(b) of the Act is replaced with: "(b) *“transactions concluded under “master agreements” as defined in section 35B(2) of the Insolvency Act.”.* | The comment is noted. The Reserve Bank and the National Treasury are considering the most viable approach to resolve the issue in line with the remedy proposed by the industry bodies.  |