CHAPTER 4

DEVELOPMENTS RELATED TO BANKING LEGISLATION

The purpose of this chapter is to provide a brief overview of the most important developments regarding banking legislation during 1994.

AMENDMENTS TO THE BANKS ACT, 1990

Extensive proposed amendments to the Banks Act, 1990 (Act No. 94 of 1990 – "the Banks Act"), were presented to Parliament towards the end of 1994 and were promulgated as the Banks Amendment Act, 1994 (Act No. 26 of 1994), on 2 December 1994. It should be noted, however, that the **said Amendment Act will come into operation only on a date to be fixed by the President by proclamation in the *Government Gazette* and that different dates may be fixed for different provisions of the Amendment Act**. Amendments that are considered to be significant are the following:

- The Registrar of Banks, although not responsible for approving the appointment of any officer or employee of a banking institution, is of the opinion that not only directors and executive officers of banks and bank controlling companies, but also bank employees who are in charge of a risk-management function, even if they are not at general manager level, ought to be subject to an equal degree of scrutiny. Since the current definition of "executive officer" in the Banks Act does not provide for such bank employees, the definition has been amended accordingly. The issue as to which categories of bank employee will have to submit the statutorily required form DI 020 once the amendment comes into operation still has to be finally resolved in consultation with the parties concerned.

  A sanction has been introduced for a failure to render the required information in respect of the appointment of a proposed director or executive officer. In terms thereof, such appointments will have no force or effect unless the required information is furnished to the Registrar.

- The procedure of provisional registration of new banks, followed by final registration, has been replaced by a single, once-off registration of banks, subject to the prescribed conditions and any further conditions that the Registrar may determine.

- In view of the opening up of international trade with South Africa and modern banking trends, such as the establishment of cross-border interests by banks and the need for reciprocal treatment by foreign and domestic supervisory authorities, it has been deemed appropriate to allow foreign banks to conduct the business of a bank in South Africa through branches.

  The Banks Act in effect prevented the establishment of branches in South Africa by foreign banks and, therefore, had to be amended accordingly.

- After consultation with the South African Institute of Chartered Accountants, it was decided that more specific guidelines were required with regard to matters to be reported to the Registrar by the external auditor of a bank.

  In terms of the amendment to section 63 of the Banks Act, the external auditor of a bank will have to report to the Registrar any matter that, "in the opinion of such auditor, may endanger the bank's ability to continue as a going concern or may impair the protection of the funds of the bank's depositors or may be contrary to principles of sound management (including risk management) or amounts to inadequate maintenance of internal controls".

- Practical experience has shown that legal uncertainty exists as to the effect of the suspension or cancellation of the registration of a bank whilst such bank is under judicial management or curatorship, or is being wound up, on the order placing such bank under judicial management, curatorship or liquidation. Express provisions have been inserted into the Banks Act to the effect that the relevant judicial management, curatorship or liquidation will be pursued to its normal conclusion, despite the suspension or cancellation, in the interim, of the registration of the bank in question.

- Because of delays experienced with the investigation of possible improper conduct by the directors, executive management or other employees of a bank that has fallen into financial difficulties culminating in such a bank being placed under curatorship, a provision to improve the situation has been inserted into the Banks Act.

  In essence, the insertion provides for a commissioner, appointed by the Registrar, to investigate the business of a bank under curatorship

or of any of its associates. Such a commissioner is required to complete his investigation within a period of five months as from the date of his appointment and is furthermore required to submit a written report to the Registrar within 30 days after the completion of the investigation.

- Present-day financial realities tend to indicate that the minimum level of capital of R10 million to be maintained by banks in terms of the Banks Act is insufficient. In order to create a sufficient cushion against solvency risk, and in order to impose adequate discipline on a bank's management as regards the level of growth of the bank's assets, it was felt necessary to increase the capital requirement of the Banks Act substantially.

  The minimum net qualifying capital required in terms of the Banks Act has therefore been increased to an amount of R50 million.

- The provisions of the Banks Act relating to the gathering of information from banks and other related financial institutions were not yet fully in line with international guidelines, which stipulate that consolidated supervision should comprise an assessment of a financial group as a whole, including the non-financial entities in such a group.

  The relevant sections of the Banks Act have now been amended to empower the Registrar to obtain, for purposes of consolidated supervision, information from institutions other than banks that fall within the same group of companies as a bank.

AMENDMENTS TO THE REGULATIONS UNDER THE BANKS ACT, 1990

Although the Regulations relating to Banks ("the Regulations") were rewritten in their entirety in 1993, it became evident that certain further amendments had become necessary and that certain issues required further clarification. Banks Act Circular 5/94, containing proposed amendments and interpretation guidelines, was therefore issued to all banks in July 1994. Although these amendments to the Regulations were expected to be promulgated only early in 1995, banks were requested to implement the proposed amendments and interpretation guidelines in the interim.

The most significant proposed amendments and interpretation guidelines contained in the circular are the following:

- **Regulation 6(6) – Audit report**

  The regulation will be amended to include the reporting, by the auditor of a bank, of any instances of non-compliance with regulation 39(1)(a), concerning the statement (form DI 020) to be submitted by serving or prospective directors or executive officers.

- **Regulation 23(6)(c) – Capital-adequacy risk weightings**

  Loans secured by a mortgage on urban residential dwellings and where the monthly instalments on such loans are overdue attract a risk weighting of 100 per cent. Since the Regulations contain no definition of "overdues", regulation 23(6)(c) will be amended to reintroduce a definition of overdue amounts in respect of home loans **only**. Failure to do so will result in inconsistencies in the allocation of the relevant risk weightings. The proposal is not more onerous on banks than the requirements that were in force before January 1994.

- **Form DI 310 – Calculation of cash-reserve requirement**

  Until such time as the capital-adequacy requirements for non-banking security traders have been determined, the instructions previously contained in the Regulations as regards the reductions in respect of repurchase agreements were reintroduced. These instructions relate to the completion of line item numbers 4 to 7 and line item number 8, respectively, of form DI 310.

- **Form DI 402 – Counterparty risk**

  Additional clarifying comments have been included, along the lines of the guidelines adopted by the Basle Committee on Banking Supervision.

- **Form DI 500 – Credit risk**

  In a continued effort not to be prescriptive and to ensure that the risk-based returns reflect the management accounts of banks, the arbitrary

definition of "overdues", being an amount that is overdue for four months or longer, was deleted from the Regulations that were published on 28 December 1993. The Department has subsequently received valuable inputs from the banking sector, the results of which are reflected in paragraph 1 of the revised form DI 500 that was issued under cover of Banks Act Circular 5/94.

In summary, a more accurate description of "overdues" has been developed. Overdues are described as amounts in respect of those accounts that banks have identified, in terms of their policy, as being overdue. Also included are amounts rescheduled, being those accounts that were previously classified as overdue, and the terms of which have subsequently been renegotiated, resulting in these accounts no longer being classified as overdue.

MUTUAL BUILDING SOCIETIES ACT, 1965, AND MUTUAL BANKS ACT, 1993

The Mutual Building Societies Act, 1965, was repealed by section 95(1) of the Mutual Banks Act, 1993, except for those provisions of the first-mentioned Act governing the operations of terminating mutual building societies. This was necessary as a temporary measure pending the promulgation, under the Banks Act, 1990, of suitable subordinate legislation for the regulation of the activities of institutions such as terminating mutual building societies, "stokvels", credit unions and savings clubs.

Such subordinate legislation has since been promulgated in the form of Government Notice No. 16 of 5 January 1994, published in *Government Gazette* No. 15416. In the circumstances, the retention of the aforementioned provisions of the Mutual Building Societies Act, 1965, had become redundant and the Mutual Banks Amendment Act, 1994 (Act No. 25 of 1994), was promulgated to delete the relevant provisions from section 95(1) of the Mutual Banks Act, 1993, and, consequently, also to delete the definition of "terminating mutual building society" in section 1(1) of the Mutual Banks Act, 1993.