Being better informed

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Executive summary

Irwin Lim Ah Tock
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Welcome to the third edition of "Being better informed", our quarterly FS regulatory, accounting and audit bulletin, which aims to keep you up to speed with significant developments and their implications across all financial services sectors.

The last quarter has been characterised by significant regulatory and legislative activity, both at the global and domestic level.

In August, National Treasury issued the long awaited discussion document 'Strengthening South Africa's Resolution Framework for Financial Institutions' which follows on the G20 commitment to develop a framework to deal with large and important financial institutions, in particular systemically important financial institutions (SIFIs).The paper introduces a range of key considerations relevant to the South African financial services industry, including addressing critical areas such as deposit insurance and proposing locating the functions of the 'resolution authority' within the SARB.

At the same time, the SARB has entered into a key agreement with South Africa's BRICS counterparts and signed a Memorandum of Understanding on Renminbi Clearing Arrangements in South Africa for the purpose of implementing the Contingent Reserve Arrangement first discussed at the 2014 BRICS summit. Similarly, the FSB have had a busy quarter, having issued Board Notice 18 to the Collective Investment Schemes Control Act which sets out the capital requirements managers of collective investment schemes (CISs) in participation bonds must comply with, and together with National Treasury, signing a declaration for the regulation of hedge funds (HFs) in South Africa.

At the global level, there's certainly still a lot happening from a regulatory perspective – including both prudential and conduct regulation – and global FS firms will no doubt have their hands full working out how different regulatory initiatives (with lots of acronyms) apply to them. But it's not just the regulators who will be busy in the coming months. Global FS firms, particularly in the UK, will be expediting their implementation programmes for big topics like Solvency II and MiFID II, while Financial Conduct Authority firms will be preparing recovery plans. Many banks globally will continue to be working out how and to what extent the LCR impacts them, while global insurers focus on tackling the rules proposed by the Prudential Regulation Authority in the Bank of England in relation to implementation proposals for non-Solvency II firms.

Our feature this quarter profiles a key piece of global PwC thought leadership that seeks to provide insight into a fundamental question – "are capital markets participants and users prepared and capable to reimagine the future, innovate and compete against this still unfolding backdrop?" Capital Markets: 2020 provides our insights and understanding into the future of the industry, which either as a 'participant' in or a 'user' of capital markets is critical to your actions today and to your plans for the future.

We hope you will continue to find our latest edition of Being Better Informed to be an insightful read. Any thoughts or comments you may have on how we can continue to enhance the publication are welcomed.

Irwin Lim Ah Tock
Banking and Capital Markets
Regulatory Practice Leader
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Capital markets 2020: Will they change for good?

Summarised by Rivaan Roopnarain

The future of capital markets is a subject of increasing focus since the 2008 financial crisis. The vitality of capital markets is critical if the world is to return to an environment conducive of sustainable economic growth. To be most beneficial, capital markets must be able to function freely, rewarding strong performers and penalising those who are unable to deploy capital effectively. Looking forward to 2020, capital markets will play an increasingly important role in providing everything from financing to the world's most innovative companies to generating the investment returns needed to support an ageing population in the developed world.

http://www.pwc.com/gx/en/banking-capital-markets/capital-markets-2020/index.jhtml

Our survey of top capital market executives clearly demonstrates that leaders believe it is important to have a better understanding and a more clearly articulated vision of their place in the capital market industry in 2020 than they do today. We wholeheartedly agree – this is an area of strong interest not only for the 'participants' (i.e. investment banks, broker-dealers, financial market utilities and the like), but also for the 'users' (i.e. private equity firms, pension funds, hedge funds, other non-bank financial intermediaries and corporates), who rely on global capital markets for funding, risk management and transactional banking services. Furthermore, other stakeholders such as policymakers and regulators also need to develop the right balance between investor and system protection and the need for markets to function freely and efficiently in order to support economic growth.

As global interconnectivity and ubiquitous access to financial markets increase, we see a world where well-functioning, deep capital markets are needed more than ever. Industry leaders must address the continually changing market forces and prove that they can operate within this new equilibrium, which includes justifying their social utility.

Today's challenges

The challenges for capital market players are vast and include pressures from clients, stakeholders and regulators. Despite this difficult environment, though, 84% of surveyed executives indicated that they feel somewhat or fully prepared for the challenges within the industry, although many players are struggling to meet the more stringent risk and capital requirements while maintaining acceptable levels of profitability. Users of capital markets face a number of their own challenges – from finding yield in a period of pervasively low interest rates to adhering to complex regulations that they had not been subject to before. Meanwhile, incumbent and emergent financial market utilities (FMUs) are finding their places within the new capital market landscape and need to reach sufficient economies of scale to operate effectively over the long term. This point of view is consistent with that of our surveyed executives, whose top challenges were found to range from increasing client profitability (36%) and attracting and retaining talented employees (33%), to adapting to new technologies (33%).

Complying with growing and changing regulations remains a significant challenge, as reported by 19% of executives. Capital market participants are still struggling to get ahead of regulation and to develop a proactive stance with their regulators. The bottom line is that regulatory developments are profoundly changing operations, markets and cost

structures. So who benefits? Our survey participants believe that global banks will benefit the most from proactively addressing these changes – likely due to their ability to leverage scale to manage the cost and complexity. Responses suggest also that smaller banks (such as community and regional banks, and credit unions) and broker-dealers will be threatened the most.

Executives are highly concerned about the threat posed by shadow banking players such as crowd funders and peer-to-peer lenders. Seventy per cent believe they pose a moderate to severe threat to traditional banks, 20% believe they present innovative partnership opportunities and the remaining 10% believe that non-traditional players only pose a threat to those with inferior technologies. Our survey participants see this threat coming from disparate areas within the industry's ecosystem (i.e. distribution channels, payments and asset management/ brokerage systems). Finally, 16% of industry players believe that this shadow banking world may expand beyond its current 25% market share of financial assets, while two-thirds of executives expect that shadow banking assets will show flat to moderate growth by 2020.

The future landscape

The demands of the new capital market equilibrium will require businesses to transform. Technology and straight-through processing (STP) are rapidly morphing from being expensive challenges to becoming critical-to-success components that create client value and enable efficiency. Meanwhile, both non-traditional players and regional broker-dealers (many of whom have little legacy infrastructure) are challenging the established order by supplying capital and becoming leaders in product innovation. To ensure that capital markets in 2020 are able to function efficiently and freely to provide financing to corporations and returns to investors, both participants and users will need to take on a leadership role within the capital market ecosystem. Being reactive to regulators, public opinion and market idiosyncrasies is no longer an option.

We believe that the winners in 2020 and beyond need to relentlessly execute against today's imperatives; they must radically innovate; and they have to transform in order to meet the client and industry needs of the future.

Top five scenarios survey participants saw as being most likely to occur

Source:PwC Capital Markets 2020 Survey

Cross-sector regulations

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South Africa

Strengthening of South Africa's SIFI resolution regime

The National Treasury issued the much awaited discussion document *'Strengthening South Africa's Resolution Framework for Financial Institutions'* on 13 August 2015. This paper follows on the G20 commitment to develop a framework and standards to deal with large and important financial institutions, in particular systemically important financial institutions (SIFIs). While various initiatives such as Basel III are focused on ending the 'too big to fail' (TBTF) debate, there remains a possibility that these institutions may indeed fail. The paper therefore sets out proposals for strengthening South Africa's resolution regime so that if a financial institution should indeed fail, it can be managed in a way that mitigates the impact thereof on South Africa's financial stability while minimising the macroeconomic costs. Discussion points in the paper include the following:

- The rationale behind resolution legislation;
- Gaps identified when benchmarking South Africa's current framework against international best practice;
- The governance and administrative features of the bill (objectives, scope, roles of the South African Reserve Bank (SARB) etc.) and the resolution process; and
- Areas of alignment with existing legislation.

Some of the key points in the paper include the designation of the SARB as the resolution authority; the requirement that all SIFIs (banks and non-banks) should have a recovery and resolution plan; an agreement in principle to introduce a deposit guarantee scheme in South Africa giving preferential treatment to qualifying depositors (mainly retail, and small and medium-sized enterprises (SMEs)) – currently, no distinction is made between depositors and unsecured creditors; and the removal of curatorship provisions in the Banks Act and their incorporation in the Resolution Bill.

Comments are invited from the public.

Agreement on activities, establishment and operation of EIB's regional office in South Africa

Rivaan Roopnarain

On 24 July 2015, *Government Notice 640* was issued by the Department of International Relations and Co-operation. This notice sets out an agreement reached between the South African government and the European Investment Bank (EIB) regarding the activities, establishment and operation of the EIB's regional office in South Africa. The EIB is the financing institution of the European Union (EU) and is the only bank owned by, and representing the interests of, the EU's member states.

A framework agreement for financial co-operation between the Republic of South Africa and the EIB has been in place since June 2000. In it, provisions are laid down to ensure certain rights and privileges for the EIB and its officials and employees. The current agreement formalises a range of operational, legal and administrative functions relating to the EIB's physical presence and legal standing within South Africa. In particular, the agreement seeks to further strengthen and develop relations and co-operation between South Africa and the EIB through additional terms concerning the privileges and immunities of the EIB and its personnel, in particular those assigned to carry out tasks in the country.

The EIB has been financing investment projects in South Africa since 1995, and the current agreement is expected to further facilitate investment relations with the entity. According to its *website*, the EIB is the largest multilateral borrower and lender by volume in the EU, and provides finance and expertise for investment projects which contribute to furthering its policy objectives. Since 2004, the EIB has supported development and economic activity in South Africa with loans and equity investment worth over EUR 2.5 billion. In South Africa, the EIB acts upon mandates entrusted to it by the European Council. These mandates cover the EIB's activities in relation to both private and public sector operations.

International regulations

IOSCO report on good practice in the use of CRAs

On 8 June 2015, the International Organisation of Securities Commissions (IOSCO) published Good practices on reducing reliance on CRAs [credit rating agencies] in asset management. The report highlights the following good practices:

- Firms should be able to make their own determinations on the credit quality of a financial instrument before investing in and holding it.
- When firms use external ratings, they should be able to understand the methodology, parameters and basis underlying the assessment for the credit rating awarded.
- Where external credit ratings are used, a downgrade should not automatically trigger the immediate sale of an asset.
- Firms should disclose to investors their policies with regard to external credit ratings when assessing the credit quality of their counterparties or collateral. Asset managers should not rely solely on external credit ratings and should consider alternative quality parameters as well.

The report is addressed to national regulators, asset managers and investors. IOSCO accepts that credit ratings are useful and at times necessary benchmarks for asset managers and investors. It also appreciates the fact that there is no satisfactory alternative.

FATF to assess de-risking

The press release of the Financial Action Task Force (FATF) on 26 June 2015, Drivers for 'de-risking' go beyond anti-money laundering / terrorist financing, outlines the work it intends undertaking on evidencing the causes, scale and impact of de-risking by financial institutions. This follows after FATF received intelligence that financial institutions are terminating or restricting relationships with categories of customers in situations beyond anti-money laundering (AML) and counter-terrorist financing.

FATF is going to:

- clarify the relationship between its standards on correspondent banking (FATF Recommendation 13) and other intermediated relationships with standards on customer due diligence (FATF Recommendation 10) and wire transfers (FATF Recommendation 16);
- consult with regulators and the private sector to inform its work;
- consider the efforts of supranational organisations on account closure and correspondent banking, including the Committee on Payments and Market Infrastructures (CPMI), the Union of Arab Banks, the International Monetary Fund (IMF) and the Basel Committee on Banking Supervision (BCBS); and
- develop guidance on the risk-based approach to money or value transfer services.

FATF has reminded financial institutions that a risk-based approach to de-risking is a fundamental requirement of its standards. This statement comes three months after the Financial Conduct Authority (FCA) warned banks that wholesale de-risking was not a legal or regulatory requirement of any domestic or international standards.

Recovery planning

Recovery plan template for FCA firms

On 27 August 2015, the FCA published a suggested recovery plan template for IFPRU 730K firms, subject to simplified obligations under the Bank Recovery and Resolution Directive (BRRD).

The template provides a format to aid with the initial development of a recovery plan. But given the high-profile nature and complexity of the requirements, it is still important for firms to ensure they dedicate sufficient focus and attention to the recovery planning process. This will mean establishing an appropriate recovery and resolution planning (RRP) governance framework, selecting adequate options and designing effective triggers tailored to their business model, size, complexity and risk profile.

The requirements for firms subject to both general and simplified obligations are broadly similar, and the FCA expects all firms in scope to follow the technical standards and guidelines issued by the European Banking Authority (EBA) which complement the BRRD.

The rules came into force on 19 January 2015, with the exception of the rules on contractual recognition of bail-in, which will come into force on 1 January 2016. The first submission deadline is 31 December 2015 for the largest firms that are required to apply simplified obligations.

Conduct

IOSCO backs greater transparency

IOSCO published Post-Trade Transparency in the Credit Default Swaps Market: Final Report on 7 August 2015. This followed on a survey conducted among market participants and observers on the use of publicly available post-trade data and the perceived impact of such data on the market. In this report, it analyses the survey results in combination with its own quantitative analysis of the US, where mandatory post-trade transparency in certain credit default swap (CDS) markets is now in effect.

It found that the introduction of the transparency regime has not had a substantial effect on market risk exposure or market activity for credit default swaps. The report also cites a study performed by the Federal Reserve Bank of New York when disclosure was voluntary. That study found that dealers do not typically hedge large transactions by trading in the opposite direction on the same product type on the same day or the day after a trade is executed.

After considering the potential costs and benefits, IOSCO suggests that it would be valuable to make the price and volume of individual CDS transactions publicly available. It also recommends increasing post-trade transparency in the global corporate bond and structured finance product markets, given the positive impact on transaction costs.

In the EU, the transparency regime forms part of MiFID II, which will come into effect on 3 January 2017.

Market infrastructure

ESMA recommends procyclicality margin

On 13 August 2015, the European Securities and Markets Authority (ESMA) published recommendations to the European Commission (EC) on strengthening the role of European Market Infrastructure Regulation (EMIR) margin requirements in addressing procyclicality. All authorised central counterparties (CCPs) have implemented measures to mitigate procyclical effects, but ESMA wants to amend EMIR to require:

- regular testing of procyclical metrics that takes into account the interaction between risk factors and credit/business cycles, specificities of product offerings and risk management policies;
- that CCPs make public (or at least share with clearing members) the entire history of margin parameter revisions, along with the justifications for the changes;
- that procyclical impacts be taken into account when setting and revising acceptable collateral and haircuts; and
- enhancements to the rigour of available procyclical treatment options, for example mandating that buffers are exhausted when margins increase.

ESMA is of the opinion that the above will minimise the potential for harmful procyclical dynamics.

ESMA considers EMIR clearing member margin

On 27 August 2015, ESMA published a discussion paper, Review of Article 26 of RTS No 153/2013 with respect to client accounts, that deals with EMIR clearing member margin standards. ESMA is exploring whether it would be appropriate to shorten the time horizon for the liquidation period of non-OTC (over the counter) derivatives from two days to one day. This change would align EU standards with the US approach for the purposes of CCP equivalence.

CCPs are required to collect margin by both the EU and US so that they have sufficient resources to manage their exposure during the period between the clearing a member's default and the liquidation of that member's positions. While the EU requires CCPs to collect net margin for non-OTC instruments that is sufficient to cover at least a two-day exposure window, the US approach of having only a one-day minimum potentially leads to enhanced CCP stability, because the US rules also require that margin must be collected on a gross basis (rather than a net basis). ESMA's paper seeks stakeholder feedback to inform its assessment of whether it should adopt an approach more in line with that of the US.

The comments period closed on 30 September 2015.

Reporting

IOSCO guidance on UTIs

IOSCO consulted on harmonisation of the UTI (unique trade identifier) on 19 August 2015. IOSCO supports international transaction reporting initiatives that form part of wider OTC derivatives reform. In looking at the elements of effective UTIs, IOSCO focused on traceability challenges around linking related UTIs (such as with package transactions, where separate UTIs are assigned to the different components of the transaction).

Following the consultation, IOSCO laid out a number of approaches to linking UTIs that have been generated over the lifecycle of a transaction. It concluded that approaches which accommodate new transactions that consist of the consolidation of a number of previous transactions, such as with portfolio compression, are more likely to be successful.

IOSCO went on to outline when life cycle events would require a new UTI and when they would not. It observed that changes in any counterparty should be considered a new transaction with a separate UTI; however, revaluations, end-of-life events (such as early termination) and contractually determined changes to notional amounts should not trigger the need for a new UTI.

The consultation closed for comments on 30 September 2015.

Banking

South Africa

NCA – Temporary suspension of the Affordability Assessment Regulations

Ryno Swart

In our previous issue, we discussed the new affordability guidelines under the National Credit Act, which were published and became effective immediately on 13 March 2015. In our article, we raised concerns that credit providers would most likely not have the flexibility in their systems and processes to respond to the required changes immediately. This view was also widely echoed across the industry.

On 21 August, the Minister of Trade and Industry issued a suspension of the Affordability Assessment Regulations for six months. The extension provides welcome temporary reprieve for credit providers. However, in our experience, the six months that credit providers have had to become compliant may still not be sufficient to implement system-driven solutions, and manual processes will likely be required as a temporary workaround.

Payments

SARB Directive 1 of 2015: Conduct within the National Payment System in respect of the Financial Action Task Force Recommendations for Electronic Funds Transfers

Carmen Maisenbacher

Background and purpose

With the rise of terrorism in recent years, it has been necessary for financial institutions to implement measures to combat the financing of terrorism and prevent money laundering practices.

Within South Africa, the SARB has the responsibility to monitor and regulate all payment, clearing and settlement systems, utilising the provisions of the National Payment System (NPS) Act. The NPS covers the payment process as a whole, from payer to beneficiary, and includes all mechanisms, systems and procedures involved in effecting payments and facilitating the exchange of value between parties.

In February 2012, FATF released a revised version of its International Standards on Combating Money Laundering and Financing of Terrorism and Proliferation (FATF recommendations). These standards apply to 'wire transfers', or electronic funds transfers (EFTs [1]), as they are known in South Africa. The SARB supports the recommendations of the FATF and is collaborating with the drafters of the Financial Intelligence Centre Act, 2001 (FICA) to ensure South Africa's compliance with the applicable FATF recommendations and any supporting guidelines.

The SARB has directed that any bank or clearing system participant that originates, facilitates or enables an EFT, as well as the beneficiary of the payment, must implement procedures to ensure that all requirements relating to the FATF recommendations (refer to key points below), FICA and relevant payment clearing house agreements are met.A declaration of such compliance, prepared by the chief executive officer (CEO) and an AML compliance officer with the assistance of the internal audit function, must be submitted to the NPS department of the SARB by no later than 31 March on an annual basis.

Relevance

All banks and clearing system participants are required to comply with the SARB's directive and the corresponding FATF recommendations. Failure to do so is an offence in terms of the NPS Act.

Banks and clearing system participants must ensure that the appropriate information is retained for all qualifying transfers. This will increase administrative, operational and reporting requirements.

The key points of the International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation – The FATF Recommendations – as published in February 2012 are discussed below.

[1]EFTs are originated by banks and clearing system participants or their customers. They are processed and forwarded, often through an intermediary bank or clearing system participant, to credit the beneficiary account, utilising computerised systems.

Financial institutions must ensure that they retain the following information:

- They must retain accurate originator and beneficiary information relating to the EFT throughout the payment chain process. This information is required for all transfers and payments, except for credit or debit card transactions, settlements from one financial institution to another, and certain transfers below an adopted threshold.
- They must retain the name, account number, address or identity number of the originator, as well as the name, account number or unique transaction reference number of the beneficiary.

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Further details can be found in Annexure A of the SARB directive.

Conclusion

This directive has been implemented by the SARB with a view to preventing, and detecting, the movement of terrorist and illegal criminal funds. By ensuring that basic information about the originator and beneficiary of an EFT is immediately available, it makes it possible to investigate any suspicious or unusual activity, after which prohibited transactions can be reported and frozen in accordance with the United Nations Security Council's resolutions.

These transfers contain information regarding the originator, the beneficiary and the value of the payment. EFTs can be either domestic or cross-border.

The ability to trace all wire transfers, or EFTs, should go a long way towards making terrorist financing more difficult for criminals, and should help ensure that suspicious and illegal financing activities are detected and subsequently terminated.

http://www.gov.za/sites/www.gov.za/files/38894_gon538.pdf

Outsourcing

Reporting requirements relating to material outsourced service providers and critical third-party service providers (Directive 8/2015)

Ryno Swart

In recent years, there has been a substantial increase in the outsourcing of certain operations by local banks. Outsourcing exposes a bank to risk, creating the need for supervisors to assess and evaluate how well the bank is managing and mitigating this risk.

In addition, concentration of outsourcing within the banking sector to specific service providers could result in mutual or common exposure to operational risk or potential vulnerability across the banking sector.

In order to effectively monitor and manage this risk, starting from 30 June 2015 the SARB requires banks to submit an annual return providing specified information on material outsourcing arrangements and third-party service providers.

The return will highlight, amongst other things, who the material service providers are, why they are classified as material, the nature of the services they provide, whether contingency plans or alternative service providers are in place and the value of the exposure to each service provider.

The return will include service providers such as Eskom and Telkom, over whom banks have no control. It will also include industry service providers such as SBV and BankServ.

ICAAP

Expectations of the SARB with respect to ICAAP process and document (Guidance Note 4/2015)

Stephen Owuyo

GN4/2015 was issued on 2 August 2015 with the aim of setting out the high-level requirements for an internal capital adequacy assessment process (ICAAP), as well as the responsibilities of the Bank Supervision Department (BSD) and of banks. While the principles in the Guidance Note are aligned to those in Basel III and these are therefore not new requirements, the Appendix provides a convenient format for banks to follow in drafting their ICAAP documents. Intended as a guide to drafters of the ICAAP document, the format should make the review process for both the BSD and the banks more effective and efficient. It is, however, not intended to be exhaustive, nor is it a substitute for the full content of the regulations.

Liquidity

Provision of a committed liquidity facility by the SARB (Guidance Note 5/2015)

Ryno Swart

The Basel III framework introduced requirements for banks to maintain a minimum liquidity coverage ratio (LCR) in order to provide sufficient high-quality liquid assets (HQLAs) to survive a month-long significant stress scenario. The SARB has approved the provision of a committed liquidity facility (CLF) to local banks to assist them in meeting the LCR requirements.

Although previous guidance has been issued in this regard, Guidance Note 5/2015 aims to address some of the uncertainty that has been identified around CLFs and to provide updated information on acceptable collateral and other related requirements.

The Guidance Note covers the following key provisions:

- CLFs will be capped at 40% of total forecast required HQLA.
- Banks have to apply annually for a CLF for the following year, based on estimated HQLA requirements.
- The amount that can be drawn down will be limited to the lesser of the value of collateral (after required haircuts) and the facility granted.
- Where assets pledged have been transferred to a separate special purpose institution (SPI), the 'look-through principle' will apply for the purposes of calculating capital requirements relating to credit risk, and these assets have to be classified and risk-weighted as if they were still on the bank's balance sheet.
- Banks will have to report on assets included in the SPI on a quarterly basis.
- Banks will pay a commitment fee on a sliding scale, based on the size of the facility, and interest will be charged on drawn balances at the SARB's repo rate plus 100 basis points.

Although the CLFs provide important support to banks in meeting Basel III LCR requirements, we believe the banks will still face some challenges, including:

- It will be difficult for banks to forecast their HQLA requirements accurately a year in advance when applying for the facilities. This could lead to their requesting insufficient facilities, or excessive facilities with resultant higher facility fees.
- In volatile markets, such as banks are currently facing, the fair value of collateral could vary quite significantly. This could, in turn, affect the value of available facilities.
- The creation of SPIs and additional administrative and reporting requirements will result in additional costs to banks.

Other regulation

The South African Reserve Bank and People's Bank of China sign a memorandum of understanding on renminbi clearing arrangements in South Africa

Rivaan Roopnarain

In July 2015, the *SARB and the People's Bank of China announced* the signing of a memorandum of understanding regarding the clearing and settlement of the Chinese currency, the renminbi, in South Africa. According to the press release issued by the SARB, the two central banks agreed to co-ordinate and co-operate on the supervision, oversight and clearing of renminbi in South Africa and to exchange information in order to facilitate the improvement and development of bilateral trade between South Africa and China.

In light of China's status as South Africa's largest export trading partner, a clearing centre in South Africa that caters to renminbi-denominated transactions will facilitate the clearing of transactions in the Chinese currency, with parties to cross-border transactions between South Africa and China benefiting from easier, and potentially cheaper, trading conditions.

In addition, 'the memorandum of understanding signifies another important milestone reached in the continuous joint effort to build capabilities in the South African financial markets to better serve bilateral trade, investment and financial flows between China and South Africa.'

SARB signs inter-central bank agreement with BRICS counterparts

Rivaan Roopnarain

In July 2015, the *SARB announced* the signing of a multilateral inter-central bank agreement among the central banks of Brazil, Russia, India, China and South Africa (BRICS). The agreement was designed for the purpose of implementing the contingent reserve arrangement which was announced in July 2014 at the BRICS summit in Brazil, and effectively provides

a framework for the provision of liquidity to BRICS countries through currency swap arrangements in terms of the contingent reserve arrangement treaty agreed to by member countries at the BRICS summit.

With the ratification by all BRICS countries of the contingent reserve arrangement treaty, which was the precursor to the finalisation of the inter-central bank agreement, the contingent reserve arrangement, with an initial size of US$100 billion, becomes effective.

The purpose of the contingent reserve arrangement is to assist individual BRICS countries to:

- mitigate short-term liquidity pressures;
- promote and facilitate additional co-operation between BRICS countries; and
- strengthen the global financial safety net.

In effect, the existence of the contingent reserve arrangement also provides valuable insurance to the BRICS countries, increasing their resilience to financial and economic shocks and, in so doing, adding to investor confidence in their economies through increasing access to financial resources in the event of actual or potential balance of payments pressures.

The inter-central bank agreement is the first multilateral financial safety net arrangement which South Africa has entered into following the bilateral swap arrangement that was signed with China in April 2015

International regulations

Capital and liquidity

Basel Committee targets interest rate risk

The Basel Committee published a consultation paper on assessing interest rate risk in the banking book (IRRBB) on 8 June 2015.

The Basel Committee points out that banks are more vulnerable to interest rate risk now, because interest rates have been very low for several years and are likely to rise at some point in the future. Also, the Basel Committee wants to limit opportunities for arbitrage by requiring a broadly similar treatment of interest rate risk in the banking book and the trading book.

The paper proposes two approaches to assessing IRRBB and invites comments from the industry on each:

- Moving the IRRBB assessment from its current home in the subjective Pillar 2 framework to a more prescriptive calculation that would be part of Pillar 1; or
- Leaving the IRRBB component in Pillar 2, but making it more prescriptive.

Once finalised, the new Basel IRRBB policy will apply to 'large internationally active banks'. National regulators will be able to extend the new treatment to smaller banks if they wish.

The consultation closed on 11 September 2015.

NSFR disclosure templates

The Basel Committee published a set of net stable funding ratio (NSFR) disclosure templates on 22 June 2015.

National regulators must incorporate the new disclosure templates into their rules and require internationally active banks to complete and publish them annually from 2018 onwards. The new disclosure process will ultimately be aligned with the existing Pillar 3 disclosures. Regulators can extend their application to smaller and/or domestic banks if they wish.

The Basel Committee acknowledged that excessive disclosure can lead to undesirable market effects but has nevertheless decided to proceed with the new disclosure requirements.

Bringing proportionality to CRD IV

On 19 August 2015, EBA announced that it intends to conduct further analysis on the NSFR and leverage ratio, as requested by the EC. Specifically, it will focus on proportionality for banks with different business models and potential future reporting requirements. It will also cover the scope of application and how calibrating the two requirements will impact markets.

The EBA is mandated to produce a report on the NSFR by the end of 2015 and another on the leverage ratio by October 2016. It expects to complete the leverage ratio report by July 2016.

Reverse stress testing in ICAAP

The Prudential Regulation Authority (PRA) added reverse stress testing to the ICAAP and the supervisory review and evaluation process (SREP) through the issuance of SS31/15 on 3 August 2015. SS31/15 replaces SS5/13 and SS6/13 – stress testing, scenario analysis and capital planning – and applies to credit institution and investment (CRD IV) firms.

Firms in scope of Chapter 14 of the PRA's internal capital adequacy assessment (ICAA) rulebook must carry out reverse stress testing, including testing their business plan to the point where the market loses confidence in a firm (i.e. counterparties are unwilling to transact and/or shareholders refuse to provide further capital).

The PRA states:

- It may request that firms quantify what level of financial resource they consider will place it in a business failure situation, should the adverse circumstances they have identified materialise.
- The test should take into account the sources of risks identified as per GENPRU 1.2.30R(2) (which is required by Rule 15.2 of ICAA).
- The test should be tailored to the nature, size and complexity of a firm's business.
- The test should consider scenarios that include the failure of one or more counterparties or a significant market disruption due to the failure of a major market participant.
- Any changes to the firm's business plan should be documented in the results referred to in rule 15.4 ICAA.

The PRA suggests that firms may wish to use reverse stress testing as a starting point for recovery plan scenarios.

FAQs on measuring counterparty credit risk

On 19 August 2015, the Basel Committee published Basel III: the standardised approach for measuring counterparty credit risk exposures: frequently asked questions. The FAQs relate to the standardised approach for measuring counterparty credit risk (SA-CCR), which is replacing the current exposure method and the standardised method, and cover:

- the general formula
- the PFE add-on
- specific derivatives, and
- miscellaneous edits.

Also, the Basel Committee has made a technical amendment to the SA-CCR framework which applies where the perimeters of the margin agreement and the netting set differ, particularly where one margin agreement covers multiple netting sets.

Update on Basel III monitoring

The Basel Committee released the following updated documents on 26 August 2015 in respect of its June 2015 monitoring exercise:

- Updated instructions for more recent reporting templates;
- A qualitative questionnaire covering interest rate risk in the banking book; and
- The closed-form questions to be used in a quantitative impact assessment when carrying out a fundamental review of the trading book.

The changes to the December 2013 versions of the reporting templates cover the NSFR worksheet as well as worksheets on large exposures, exposures to sovereigns, operational risk and interest rate risk in the banking book. Worksheets for a quantitative impact assessment during the fundamental review of the trading book, the review of the standardised approach to credit risk and TLAC have been removed.

Insurance and investment management

South Africa

Collective investment

Capital requirements with which managers of CISs in participation bonds must comply

Julanie Basson, Bruce Otto, Rikus Bouwer and Shiraz Hassim

On 17 July 2015 (effective date), the FSB issued *Board Notice (BN) 138 https://www.fsb.co.za/Departments/cis/Documents/Board%20Notice%20138%20of%202015.pdf* (Collective Investment Schemes Control Act: Capital requirements with which managers of collective investment schemes (CISs) in participation bonds must comply).

A participation mortgage bond scheme is one where a licensed scheme accepts money from investors and lends it to institutions or individuals in order to develop property. A mortgage bond is registered over the property, making the property the security for the loan.

The participation bond collective investments schemes (PBCIS) industry in South Africa is a niche market which currently has four registered CISs (one of which is in the process of being terminated).

The capital to be maintained by a manager of a PBCIS must be calculated in relation to the financial statements as prepared in terms of International Financial Reporting Standards (IFRS) in the manner as set out in BN 138. The regulatory capital requirement consists of eligible capital (share capital, non-distributable reserves, retained income etc.) less any adjustments for non-liquid items (as defined in BN 138 – intangible assets, guarantees, net deferred tax assets etc.) less any required capital (as defined in BN 138 – 13 weeks' annual fixed expenditure plus R1m seed capital per fund (reduced for each portfolio exceeding a net asset value of R10m)).

Impact on South African hedge funds not registered under CISCA

On 6 March 2015, the National Treasury and the Financial Services Board (FSB) released a signed *declaration* for the regulation of hedge funds (HFs) in South Africa.

The new regulation allows for the establishment of two types of HFs: one for retail investors and the other for qualified investors. Retail hedge funds (RHFs) will be regulated more strictly than qualified investor hedge funds (QIHFs).

As of 1 April 2015, the HF industry has had to comply with the regulations as set out in Collective Investment Scheme Controls Act, Act No. 45 of 2002 (CISCA) as prescribed by the Minister of Finance. All HFs that were unregulated as of 31 March 2015 had to apply to be registered under CISCA by no later than 30 September 2015.

Funds that had not submitted registration documentation to the FSB by 30 September 2015 and that have continued operating HFs after this date without authorisation have been doing so in contravention of the regulation, and will as a consequence be subject to regulatory and enforcement action by the FSB.

One example of possible enforcement action highlighted is the issuance of a suspension of trade notice, effectively making it impossible for funds to take in any new investors or for current investors to disinvest from impacted funds.

This could result in operational and reputational risk for the relevant HFs as well as their managers.

Draft default regulations on retirement funding

Julanie Basson and Neil Gerryts

Members of modern-day defined contribution retirement funds are faced with several important decisions related to their retirement savings:

- How much to contribute to the retirement fund;
- How to invest these savings;
- What to do with the benefits when changing employment; and
- How to invest their savings at retirement in order to provide an adequate lifetime pension.

Often, though, people lack the necessary financial expertise to make these life-changing decisions, as can be seen from the low preservation rate when employees change jobs. As a result, on 22 July 2015, the National Treasury published the long-awaited draft regulations on defaults. The aims of default options include:

- Encouraging members to make appropriate financial decisions by offering *default options* that are suitable for their circumstances;
- Reducing the charges in the retirement fund system by removing performance fees and exit penalties on default options; and
- Improving confidence in the retirement system by ensuring that the default options are appropriate for the intended membership and increasing the transparency of the options in terms of operation and costs.

The regulations will require funds (including retirement annuity funds) to:

- Set up default investment portfolios;
- Create in-fund preservation options and accept transfers into the fund in respect of active members. This effectively means members who leave a fund will, by default, keep their benefits in that fund (earning investment returns) unless they decide to transfer it to the fund of their new employer or take the benefit in cash; and
- Provide default annuity options for members at retirement.

The draft regulations also specify the requirements of these default options.

While members may still exercise their own decisions, the defaults will provide an option that is appropriate for them based on their circumstances.

International regulations

Asset management

Market-based finance: SMA chair discusses CMU and asset management systemic risk

On 1 June 2015, Steven Maijoor, ESMA chair, gave a speech outlining the key role that asset management has played, and will continue to play, in integrating the EU's financial system as part of the EC's proposed Capital Markets Union (CMU). He cited undertakings for the collective investment in transferable securities (UCITS) as a model, observing the importance of the management company passport and the facilitation of cross-border fund mergers and master-feeder structures. But he argued that the CMU could be used as an opportunity to make the following changes, which he believes would strengthen asset management's contributions even further:

- Limit member state discretion as to gold plating;
- Introduce increased uniformity around costs and fees, instead of simple disclosure requirements; and
- Create uniform requirements around fund lending.

In addition, Maijoor touched on the international debates around the systemic risk posed by asset management. While he highlighted some of the concerns, he also observed that the EU has implemented mitigating regulatory requirements around liquidity, leverage and re-used collateral risks, especially for UCITS funds. Maijoor went on to caution that regulation should always take into account the differences between the banking and asset management sectors.

Retail products: Standardising CIS fees

IOSCO published Consultation report on elements of international regulatory standards on fees and expenses of investment funds on 25 June 2015. The organisation originally issued fees and expenses recommendations in 2004 and is now updating them. It notes the number of investment fund regulatory and market developments in the period which may need to be reflected, including more disclosures and low interest rates.

IOSCO focuses on key areas where new recommendations could be made:

- Types of fees permitted – Regulators could specify the fees that can be taken out of a fund's property, new fees should only be charged after approval by the responsible entity (such as the executive board of the operator or a regulator) and the scope of fees taken from funds should be disclosed to investors.
- Performance fees – There should be a local regulatory regime setting standards for the calculation and disclosure to investors of performance fees.
- Disclosure – The manner in which fees are disclosed should be easily understandable by investors. It can be provided via electronic media, as long as investors can request hard copies.
- Transaction costs – Regulators should define which activities are included in transaction costs, and this information should be disclosed to investors.
- Hard and soft commissions – Transactions should only be entered into if they benefit the fund and not to generate order flow or commission, and regulators should consider providing guidance on the services and activities that commissions can and cannot pay for, while operators should implement procedures aimed at avoiding conflicts of interests in their dealing activities.
- Investing in other funds – The management fees of both funds should be disclosed to investors.
- Changes to a fund – Investors should be given suitable notice before the change takes effect.

Supervision: IOSCO zones in on asset management

On 17 June 2015, IOSCO released IOSCO: Meeting the Challenges of a New Financial World, covering developments arising from its annual conference in London. It has decided that a full review of asset management activities and products in the global financial context should be the immediate focus of international efforts to identify potential systemic risks and vulnerabilities. It thinks this review should take precedence over further work on methodologies for the identification of systemically important asset managers.

At the conference, the IOSCO Board discussed its strategic direction through 2020, which will be implemented via 43 initiatives covering priority areas such as:

- Research and risk identification
- Standard setting and developing guidance
- Implementation monitoring
- Capacity building
- Co-operation and information exchange, and
- Collaboration and engagement with other international organisations.

IOSCO also dedicated time during the conference to discuss proposals for work on OTC retail-leveraged products and the functioning of the Credit Determinations Committee and CDS auction processes of the International Swaps and Derivatives Association (ISDA).

Finally, the Board agreed to consider what work IOSCO should undertake to further strengthen the current global framework to address misconduct by firms and individuals in retail and wholesale markets.

Regulation

IAIS revises insurance core principles

The International Association of Insurance Supervisors (IAIS) published Consultation on Revision of Insurance Core Principles on 17 June 2015. It first developed the insurance core principles (ICPs) as a global framework for the regulation and supervision of the insurance sector in 2011. It is consulting on some minor clarifications and amendments to its ICPs following a 2014 self-assessment and peer review, with the intention of aligning them with corresponding FSB and Basel Committee principles and standards. It has also strengthened its approach to group-wide supervision and amended various key definitions related to governance and group supervision.

The IAIS plans to adopt the final ICPs in November 2015.

G-SIIs holding more capital

The IAIS published Consultation on Higher Loss Absorbency (HLA) requirements for G-SIIs on 25 June 2015. The FSB defines G-SIIs as insurers 'of such size, market importance, and global interconnectedness that their distress or failure would cause significant dislocation in the global financial system and adverse economic consequences across a range of countries'. The IAIS is developing a capital requirement for G-SIIs made up of a basic capital requirement (BCR) plus an uplift (presently estimated at 33% of BCR) plus HLA, split between insurance and non-insurance (NI) elements. It developed the BCR and HLA principles in 2014 and has now published several options of a draft HLA for consultation.

The IAIS is not focusing on specific formulas for the HLA in this consultation, but is instead concerned with risk sensitivity, robustness and simplicity. It proposes that the HLA capital requirement for both insurance and NI will be calculated by multiplying an exposure by a factor. It has identified three main areas for consultation:

- Bucketing (to specify which factor to apply to which G-SII) and how many buckets to have;
- Choice of HLA formulas (to specify the exposure) and how much emphasis should be placed on non–traditional insurance (NT) and NI activities; and
- Calibration of outcomes (to specify the size of the factors) and what extent the impact of the HLA is to have on G-SIIs, both on average and in particular.

The IAIS does not expect the HLA-required capital to be more than 20% of the sum of the BCR and uplift for the average G-SII. The HLA capacity requirements are to be met by the highest-quality capital. The HLA is due to be endorsed by the G20 in November 2015, for implementation from January 2019.

See our Hot Topic G-SII – a new era of global insurance regulation for background information.

Conduct in inclusive insurance market

The IAIS published Draft issues on conduct of business [COB] in inclusive insurance on 19 June 2015. It defines inclusive insurance as 'all insurance products aimed at the excluded or underserved market. In developing countries, the bulk of the population often classify as un- or underserved.' It considers the difference between the inclusive insurance market

and the conventional insurance market, and the fair treatment of customers buying these policies. The differences that the IAIS examines include their development as a product, their distribution, disclosure of information, customer acceptance, premium collection, claims settlement and the handling of complaints by the insurer.

The IAIS concludes with recommendations for regulators and supervisors when designing and implementing inclusive insurance COB supervision in their jurisdictions.

PRA approach to Solvency II reporting

The PRA published CP25/15: Solvency II: Reporting and public disclosure – options provided to supervisory authorities on 10 August 2015. It sets out the PRA's proposed approach where there are alternatives available in following areas:

- Solvency II reporting
- Currency exchange rates
- Accident or underwriting year reporting
- Claim size brackets for loss distribution risk profile
- Sum-insured-size brackets for non-life distribution of underwriting risks by sum insured
- Lines of business to be reported for non-life distribution of underwriting risks by sum insured
- Reporting of annuities stemming from non-life obligations by currency
- Development of the distribution of claims reported but not settled – reporting number of claims
- Reporting external credit ratings, and
- Group reporting where the PRA is the group supervisor and there are no consolidated financial statements at the head of the insurance or reinsurance group.

The consultation closed on 21 September 2015.

Solvency II for branches

The PRA published CP31/15: Solvency II: Third-country insurance and pure reinsurance branches on 28 August 2015. It consults on revisions to SS10/15 – Solvency II: Third-country branches concerning the PRA's approach to third-country insurance and pure reinsurance branches under the Solvency II Directive. In the UK, all third-country branches will have to comply with the Branch Guidelines of the European Insurance and Occupational Pensions Authority (EIOPA) as well as the relevant requirements in the PRA Rulebook. This includes pure reinsurance branches even if they are officially outside the scope of EIOPA's Branch Guidelines.

Branches will have to submit a regulatory supervisory report (RSR) (or summary of material changes if a full RSR is not required annually) and quantitative reporting templates (QRTs) within 14 weeks of the financial year end, quarterly QRTs within five weeks, and the own risk and solvency assessment (ORSA) supervisory report two weeks after concluding the assessment.

EIOPA's Branch Guidelines allow the PRA to decide which QRTs a branch needs to submit based on the nature, scale and complexity of the branch's business. The PRA plans to do this by dividing branches into one of the following reporting groups:

- Group 1 – Branches designated by the PRA as category one, two or three undertakings
- Group 2 – Branches designated by the PRA as category four or five undertakings, or
- Group 3 – Branches that are pure reinsurance branches.

Branches allocated to Group 1 will be subject to the full reporting requirements, but the PRA is proposing to allow branches allocated to Groups 2 and 3 some dispensations. However, all branches will be expected to submit a full set of Day 1 QRTs and the quarterly minimum capital requirement (MCR) QRTs (S.28.01.01 and S.28.02.01). Branches need to contact the PRA to confirm which QRTs to complete. The PRA is proposing that branches must use the XBRL format for reporting.

The PRA is also expecting branches to provide an analysis of their home country's winding-up regime. If the winding-up regime applicable to a third-country branch undertaking does not deliver the protection to branch policyholders required by Solvency II, reported branch assets will depend on an analysis of how they would be distributed on winding up. Affected branches need to agree a reasonable timescale with the PRA for this to be obtained as well as the basis on which branch assets should be reported on in the meantime.

Branches also have to agree with the PRA how they are going to satisfy the narrative reporting requirements regarding the whole undertaking's solvency.

The comment period ended on 30 September 2015.

Taxation

In this section:

Life tax reform

Tax changes applicable to the short-term insurance industry

Hedge funds re-characterised as CISs

Draft Taxation Laws Amendment Bill, 2015

Seema Ranchhoojee, Riate Fisher, Melissa Hadfield, Gareth Bullock, Stefan Botha

In terms of the Draft Taxation Laws Amendment Bill (DTLAB), released on 22 July 2015, the changes discussed below specifically relating to the financial services industry have been proposed.

Life tax reform

Refinement to risk insurance business of long-term insurers

Long-term insurers are granted a once-off election to move all existing risk policies, with their accompanying assets and liabilities, to the risk policy fund (RPF). This irreversible election results in a tax-exempt transfer and must be exercised in the tax return for the year of assessment ending on or after 31 December 2015.

Uncertainty continues to exist around the definition of a 'risk policy', with no indication of clarification on this topic from National Treasury in this calendar year. Given the implementation date of 1 January 2016, this represents a significant practical challenge for the industry.

Tax issues resulting from the introduction of the SAM basis

From 1 January 2016, both the 'value of liabilities' and the 'adjusted IFRS value' definitions (previously limited to the RPF) are to be extended to all policyholder funds.

Tax changes applicable to the short-term insurance industry

Tax deduction for technical reserves

There are two main drivers for the change in the tax deductions for technical reserves:

- The release of the Insurance Bill, 2015

With the introduction of SAM, it is proposed that tax deductions in respect of insurance reserves under section 28(3) of the Income Tax Act, 58 of 1962 ('the Tax Act') no longer be calculated with reference to section 32(1)(a) and section 32(1)(b) of the Short-Term Insurance (STI) Act (read with BN 169 of 2011), but rather with reference to IFRS. Therefore, the liabilities relating to claims incurred but not reported (IBNR), claims reported but not yet settled (OCR) and unearned premiums will be deductible under the new proposed section 28(3) of the Tax Act.

Deductions that will be allowed in respect of IBNR claims and OCR claims will be net of the amount for policies of reinsurance.

Inclusion of micro-insurance businesses (MIBs) in the taxation of STIs

As specified in the Insurance Bill, an MIB may conduct business as an STI or as a long-term insurer.

It is proposed that MIBs, as defined in the Insurance Bill, be deemed to be STIs for purposes of the Tax Act. The effective date is proposed to be the date on which an insurer qualifies as a micro-insurer, as defined in the Insurance Bill.

CFCs conducting STI business outside the Republic

It is proposed that controlled foreign companies (CFCs) conducting STI business outside the Republic should claim deductions using the new provisions of section 28(3) of the Act.

Hedge Funds re-characterised as Collective Investment Schemes

With effect from 1 April 2015, the business of HFs is regarded to be that of CISs for tax purposes. HFs are classified under two distinct categories, namely retail investor hedge funds (soliciting investments from all investors) and qualified investor hedge funds (soliciting and accepting investments from a restricted pool of qualified investors).

Consequently:

- HFs are required to operate in accordance with CISCA once they have been registered, i.e. within six months from 1 April 2015; and
- the CIS tax principles as per section 25BA of the Act apply to all regulated and approved HFs.

The CIS aspects of section 25BA now applicable to HFs are:

- All income distributed by the CIS within 12 months of accrual or receipt (interest) will not be taxable in the hands of the CIS.
- Any capital gains/losses realised on the disposal of a portfolio by a CIS must be disregarded in terms of paragraph 61(3) of the Eighth Schedule.
- All income retained within the CIS, including dividends, for a period of greater than 12 months from accrual or receipt (interest) will be taxed as revenue in the hands of the CIS.

The DTLAB proposed that no capital gain or normal tax will arise on the transfer of the assets by the holder of an interest in the HF to the portfolio of a hedge fund CIS, since rollover relief will be provided in terms of section 42. The transaction will also be exempt from securities transfer tax (STT).

Accounting updates

In this section:

International Financial Reporting Standards (IFRS)

Challenges for insurers implementing IFRS 9

IFRS News

EBA and ESMA comment on IFRS 9

EBA and ESMA both commented on the draft endorsement advice of the European Financial Reporting Advisory Group (EFRAG) on the adoption of IFRS 9 in letters. The EBA's view on the adoption of IFRS 9: Financial Instruments and ESMA's EFRAG draft endorsement advice on the adoption thereof occurred on 26 and 29 June 2015 respectively.

Both support the prompt adoption of IFRS 9 in the EU for accounting periods beginning on or after 1 January 2018, and so aligned with the introduction of IFRS globally.

Pension accounting amendments proposed.

The IASB published ED/2015/5: Remeasurement on a plan amendment, curtailment or settlement/availability of a refund from a defined benefit plan (Proposed amendments to IAS 19 and IFRIC 14) on 22 June 2015. It sets out proposed narrow-scope amendments for pension accounting when a defined benefit plan is amended, curtailed or settled. It proposes that entities will have to update assumptions on the obligation and fair value of plan assets to calculate costs related to changes during a reporting period. They will have to use this updated information to determine current service cost and net interest for the remainder of a period following these changes. It has also clarified how these changes interact with the limit on a defined benefit asset.

The IASB is also proposing to amend IFRIC 14: IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction to address how the powers of other parties such as the trustees of the plan affect an entity's right to a refund of a surplus from the plan.

The consultation closes on 19 October 2015.

Historic cost or fair value

The International Accounting Standards Board (IASB) published a speech, Historical cost and fair value are not as far apart as they may seem, on 29 June 2015. It considers the benefits and challenges linked to various measurement models in terms of historical cost and current value, including fair value. It concludes that the approaches are not as different as they may initially seem and makes high-level, general observations on when historical cost and current value measurement could be most appropriate.

Significant decisions on insurance contracts

Proposed amendments to statement of cash flows

The IASB made several significant decisions relating to participating contracts on 25 June 2015:

- The variable fee approach will be required for direct participation contracts.
- A definition of direct participation contracts was agreed on.
- The recognition of the contractual service margin (CSM) in profit or loss for contracts following the variable fee approach should be based on the passage of time.

It also considered:

- issues surrounding the adoption of IFRS 9: Financial instruments by insurers before the new insurance standard is adopted and requested more input from users with a view to potentially changing the measurement of liabilities; and

- accounting mismatches that could result from the variable fee approach when an entity hedges against changing market variables using derivatives.

Challenges for insurers implementing IFRS 9

The IASB finished revising IFRS 9 (which replaces IAS 39) in July 2014, to take effective from 1 January 2018. IFRS 9 introduces significant changes for some insurers, particularly those who currently hold amortised cost assets and make significant use of the 'available for sale' (AFS) category under IAS 39.

To highlight these changes and assist insurers in their preparations, we published IFRS 9 for insurers on 25 June 2015. It considers the effects of IFRS 9 on insurers and what they should be doing now to meet the deadline. It also gives an overview of the new classifications under IFRS 9 and a useful summary of tools and accelerators that can be used to help with implementation.

IFRS

Accounting changes for associates and joint ventures postponed

The IASB published ED/2015/7 – Effective Date of Amendments to IFRS 10 and IAS 28 on 10 August 2015. It proposes to postpone the date when entities must change some aspects of how they account for transactions between investors and associates or joint ventures until after the IASB has carried out a fuller review, which may result in the approach being simplified. The areas affected cover how an entity should determine any gain or loss it recognises when assets are sold or contributed between the entity and an associate or joint venture in which it invests. The comment period ended on 9 October 2015.

PwC publications

IFRS News

The June/July/August edition of IFRS News covers:

- Conceptual Framework: IASB issues Exposure Draft.
- Segment disclosures: Proposed changes arising from the IFRS 8 PIR
- IFRS 9 and EFRAG: Close monitoring required
- Cannon Street Press:
  - IFRS 15 clarifications
  - Disclosure initiative
  - FICE research project
  - NIFRICs by numbers: IAS 1
- Revenue recognition – IFRS 15 ED
- Pension accounting requirements – ED on IAS 19 and IFRIC 14
- Revenue recognition – News from the Revenue TRG
- Cannon Street Press:
  - Insurance and IFRS 9
  - IFRS implementation issues
  - Fair value measurement
- Financial instruments with characteristics of equity
  - IFRIC rejections – IAS 2

Glossary

AFS	available for sale
AML	anti-money laundering
BCBS	Basel Committee on Banking Supervision
BCR	basic capital requirement
BN	Board Notice
BRICS	Brazil, Russia, India, China and South Africa
BRRD	Bank Recovery and Resolution Directive
BSD	Bank Supervision Department
CCP	central counterparty
CDS	credit default swap
CEO	chief executive officer
CFC	controlled foreign company
CIS	collective investment scheme
CISCA	Collective Investment Scheme Control Act, Act No. 45 of 2002
CLF	committed liquidity facility
CMU	Capital Markets Union
CPMI	Committee on Payments and Market Infrastructure
CRA	credit rating agencies
CRD IV	credit institution and investment
CSM	contractual service margin
DTLAB	Draft Taxation Laws Amendment Bill
EBA	European Banking Authority
EC	European Commission
EFRAG	European Financial Reporting Advisory Group
EFT	electronic funds transfer
EIB	European Investment Bank
EIOPA	European Insurance and Occupational Pensions Authority
EMIR	European Market Infrastructure Regulation
ESMA	European Securities and Markets Authortity
EU	European Union
FATF	Financial Action Task Force
FCA	Financial Conduct Authority
FICA	Financial Intelligence Centre Act, 2001
FSB	Financial Services Board
HF	hedge fund
HLA	higher loss absorbency
HQLA	high-quality liquid asset
IAIS	International Association of Insurance Supervisors
IASB	International Accounting Standards Board
IBNR	incurred but not reported

ICAA	internal capital adequacy assessment
ICAAP	Iinternal capital adequacy assessment process
ICP	insurance core principle
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IOSCO	International Organisation of Securities Commissions I
IRRBB	interest rate risk in the banking book
ISDA	International Swaps and Derivatives Association
LCR	liquidity coverage ratio
MCR	minimum capital requirement
MIB	micro-insurance business
NI	non-insurance
NPS	National Payment System
NSFR	net stable funding ratio
ORSA	own risk and solvency assessment
OTC	over the counter
PBCIS	participation bond collective investments schemes
PRA	Prudential Regulation Authority
QIHF	qualified investor hedge fund
QRT	quantitative reporting template
RHF	retails hedge fund
RPF	risk policy fund
RRP	recovery and resolution planning
RSR	regulatory supervisory report
SA-CCR	standardised approach for measuring counterparty credit risk
SAM	solvency assessment and management
SARB	South African Reserve Bank
SME	small and medium-sized enterprise
SPI	special purpose institution
SREP	supervisory review and evaluation process
STI	short-term insurance
STP	straight-through processing
STT	securities transfer tax
TBTF	too big to fail
UCITS	undertakings for the collective investment in transferable securities
UTI	unique trade identifier

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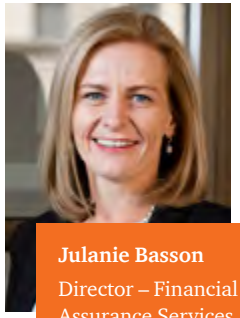

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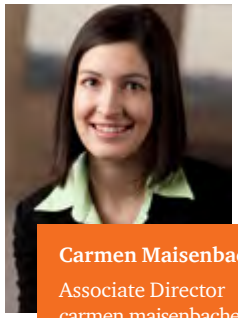

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