

28 January 2015

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Comments on the Banks Amendment Bill [B17-2014]

1. Introduction

1.1. This letter has been prepared by STANLIB Credit Partners (Proprietary) Limited (**STANLIB**) in response to the invitation issued by the Standing Committee on Finance requesting written submissions on the Banks Amendment Bill [B17-2014] (**Bill**) by 12h00 on Wednesday 28 January 2015.

1.2. STANLIB's comments on the Bill are set out below.

2. Comments on the proposed amendments to Section 69(2C) of the Banks Act, 1990

2.1. The proposed amendments afford the curator and the Minister powers to make an unacceptable differentiation in the treatment of creditors

2.1.1 If the Bill were to be enacted, Section 69(2C)(b) of the Banks Act, 1990 (**Banks Act**) would allow a curator to:

2.1.1.1 dispose of any assets of the bank under curatorship;

2.1.1.2 transfer any of the liabilities of the bank under curatorship; or

2.1.1.3 dispose of any of the assets and transfer any of the liabilities of the bank under curatorship, other than in the ordinary course of business, provided the Minister of Finance (**Minister**) consents thereto.

The Minister may, in terms of the proposed Section 69(2C)(d), grant such approval if he considers the disposal, transfer, or disposal and transfer "*reasonably likely*" to promote a stable banking sector in South Africa or to maintain public confidence in the South African banking sector.

2.1.2 The proposed amendments to Section 69(2C)(b) of the Banks Act effectively empower the curator and the Minister to differentiate in how creditors are dealt with on an *ad hoc* and subjective basis, by treating some creditors less favourably than others. These amendments would afford the Minister powers which are too wide-ranging, without sufficient scope for measuring whether they are equitable, fair and reasonable. For this reason we submit that these proposed amendments are unacceptable, and should be subject to the types of checks and balances contemplated in section 155 of the Companies Act.

- 2.1.3 Moreover, to suggest that the benchmark and time of measurement should be that “a reasonable probability exists that a creditor will not incur greater losses, as at the date of the proposed disposal, transfer or disposal and transfer, than would have been incurred if the bank had been wound up under section 68 of this Act on the date of the proposed disposal, transfer or disposal and transfer”, does not have sufficient regard to the fact that:
- 2.1.3.1 The terms of such disposal and/or transfer may itself be inequitable; and
- 2.1.3.2 The time to make this measurement (which we don’t believe is appropriate in any event) is actually at the date on which the bank is placed under curatorship, since that is when the view is being taken that creditors are better off with the bank under curatorship.
- 2.1.4 Our proposed amendments to the Bill, which are intended to limit the aforementioned powers, are marked-up in the Bill attached as **Appendix 1** hereto.
- 2.2 The proposed amendments could result in the deprivation of creditors’ existing property rights:
- 2.2.1 The contractual rights of creditors in relation to a bank under curatorship comprise “*property*” within the meaning of the South African Constitution.
- 2.2.2 It is submitted that the proposed amendments to Section 69(2C) of the Banks Act authorise a deprivation of creditors’ property rights on an *ad hoc* basis at the discretion of the curator and (indirectly) of the Minister. The rights afforded to the curator and the Minister are too broadly framed and afford the curator and the Minister a virtually unfettered discretion to when and in what manner to deprive creditors of their property rights. This potential deprivation of property rights is moreover not sufficiently causally connected to the objective of promoting confidence in, or the stability of, the South African banking sector.
- 2.2.3 Our proposed amendments to the Bill, which are intended to limit the aforementioned powers, are marked-up in the Bill attached as **Appendix 1** hereto.
- 2.3 The proposed amendments could result in increased bank funding costs, with adverse knock-on effects for bank clients and the South African economy:
- 2.3.1 The proposed powers of the curator and the Minister to:
- 2.3.1.1 Make an unacceptable differentiation in the treatment of different creditors; and
- 2.3.1.2 Deprive bank creditors of their existing property rights,
- Introduces considerable uncertainty in relation to creditors’ rights upon a bank being placed under curatorship, and will likely result in an increased cost of funding for South African banks going forward. The banks will pass these costs on to their clients, with likely adverse effects for the South African economy.
- 2.3.2 This increase in banks’ cost of debt capital could have an adverse detrimental impact on the Banks Act’s objective of ensuring a stable banking sector in South Africa, and could furthermore erode public confidence in the South African banking sector.
- 2.3.3 Our proposed amendments to the Bill, which are intended to limit the aforementioned powers, are marked-up in the Bill attached as **Appendix 1** hereto.

2.4 The proposed amendments could result in an adverse impact on the phasing-in regulations introduced to phase-in Basel III:

2.4.1 The Basel III global bank regulatory standards proposed by the Basel Committee on Banking Supervision were implemented in South Africa on 1 January 2013 by effecting amendments to the Regulations Relating to Banks (**Regulations**). Regulations 38(14)(b) (i) and (ii) of the Regulations provide that the proceeds of instruments issued prior to 1 January 2013 (and which therefore do not meet with the Basel III regulatory capital requirements including the ability of the Registrar of Banks to write-off or convert a regulatory capital instrument) still count as regulatory capital for the issuer subject to the regulatory capital phase out for such instruments contained in Regulation 38(14)(c) of the Regulations.

2.4.2 If one has regard to the foregoing, then authorising the Minister to write-off debt of a bank (owed to creditors under instruments predating 1 January 2013) placed under curatorship, where the proceeds of the debt issuance in question counted towards that bank's regulatory capital, would be contrary to the principles contained in Regulation 38(14)(b) of the Regulations which deal with the phasing in of Basel III.

2.4.3 Our proposed amendments to the Bill, which are intended to limit the aforementioned consequence, are marked-up in the Bill attached as **Appendix 1** hereto.

3. The proposed amendments to Section 69(3)(j) of the Banks Act, 1990

3.1. The proposed amendments could result in an adverse retrospective impact on the rights of creditors, which creditors would have priced for this eventuality had it been a possibility at the time of their initial investment:

3.1.1. To the extent that the contractual arrangements between a bank and its creditors contains a negative pledge prohibiting the bank from encumbering its assets, the proposed enactment of amendments to Section 69(3)(j) of the Banks Act, potentially empowers a bank curator to expose its creditors to unforeseen consequences that would not have been contemplated at the time when they executed their contractual relationship with the bank under curatorship.

3.1.2. The aforementioned proposed amendments to Section 69(3)(j) of the Banks Act will therefore have a detrimental impact on the rights of creditors of a bank placed under curatorship because such creditors would in all likelihood have accounted for these potential retrospective consequences in their initial pricing demands, had they anticipated the possibility of the negative pledge provisions being overridden at the time that they contracted with the bank in question. In fact, this retrospective impact on the risk assumed by banks senior unsecured creditors is the same argument accepted by the South African Reserve Bank when bond market investors argued (a few years ago) against the promulgation of legislation that would have allowed banks to issue so-called "covered bonds" (i.e. bonds secured by a pool of mortgage loans as collateral).

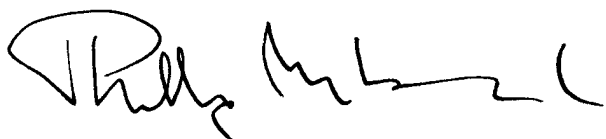
3.1.3. Our proposed amendments to the Bill, which are intended to limit the aforementioned retrospective consequence, are marked-up in the Bill attached as **Appendix 1** hereto

3.2. The proposed amendments could result in the deprivation of creditors' existing property rights:

3.2.1. The proposed amendments to Section 69(3)(j) of the Banks Act would allow the curator to override the contractual rights of the bank's creditors.

- 3.2.2. It is submitted that the aforementioned powers could potentially result in the unconstitutional deprivation of creditors' property rights on the basis of the same arguments discussed in paragraph 2.1.4 above.
- 3.2.3. Our proposed amendments to the Bill, which are intended to limit the aforementioned powers, are marked-up in the Bill attached as **Appendix 1** hereto.
- 3.3. The proposed amendments could result in increased bank funding costs, with adverse knock-on effects for bank clients and the South African economy:
- 3.3.1. Since the proposed amendments to Section 69(3)(j) of the Banks Act allow a curator to expose creditors to unforeseen consequences that could not have been contemplated by them at the time when they initially entered into their contractual relationship with the bank under curatorship, this will likely result in an increased cost of funding for South African banks going forward.
- 3.3.2. An increase in bank funding costs will have adverse knock-on effects for banks' clients and ultimately prove erode public confidence in banks generally and prove detrimental for the Banks Act objective of ensuring a stable banking sector in South Africa.
- 3.3.3. Our proposed amendments to the Bill, which are intended to limit the aforementioned powers, are marked-up in the Bill attached as **Appendix 1** hereto.

Yours faithfully,



Phillip Myburgh
CEO



Walter Hirzebruch
COO

Appendix 1

Section 69 of the Banks Act 1990, incorporating all the amendments proposed by the Banks Amendments Bill [B17-2014], with tracked changes marked to show our proposed amendments

69. Appointment of curator to bank

- (1) (a) If, in the opinion of the Registrar, any bank will be unable to repay, when legally obliged to do so, deposits made with it or will probably be unable to meet any other of its obligations, the Minister may, if he or she deems it desirable in the public interest, by notifying the chief executive officer or the chairperson of the board of directors of that bank in writing, appoint a curator to the bank.
- (b) The Registrar may appoint a person other than a person who is in the employ of the bank under curatorship, who in the opinion of the Registrar has wide experience of and is knowledgeable about the specific field of activities in which the bank under curatorship is predominantly engaged, to assist the curator in the management of the affairs of the bank under curatorship.
- (c) The person appointed in terms of paragraph (b) shall in respect of the services rendered by that person pursuant to his or her appointment be paid such remuneration out of the funds of the bank under curatorship as the Registrar may after consultation with the curator determine.
- (2) The Minister shall appoint a curator by letter of appointment which shall set out –
- (a) the name of the bank in respect of which the curator is appointed and the address of its head office;
- (b) directions in regard to the security which the curator has to furnish for the proper performance of his or her duties;
- (c) directions in regard to the remuneration of the curator; and
- (d) such other directions as to the management of the bank concerned or any matter incidental thereto, including directions in regard to the raising of money by that bank, as the Minister may deem necessary.
- (2A) On appointment of a curator-
- (a) the management of the bank concerned shall vest in the curator, subject to the supervision of the Registrar, and any other person vested with the management of the affairs of that bank shall be divested thereof; and
- (b) the curator shall recover and take possession of all the assets of the bank.
- (2B) The curator shall-
- (a) subject to the supervision of the Registrar, conduct the management contemplated in subsection 2(A)(a) in such a manner as the Registrar may deem to best promote the interests of the creditors of the bank concerned and of the banking sector as a whole and the rights of employees in accordance with relevant labour legislation;
- (b) comply with any direction of the Registrar;

- (c) keep such accounting records and prepare such annual financial statements, interim reports and provisional annual financial statements as the bank or its directors would have been obliged to keep or prepare if the bank had not been placed under curatorship;
- (d) convene the annual general meeting and any other meeting of members of the bank provided for the Companies Act and, in that regard, comply with all the requirements with which the directors of the bank would in terms of the Companies Act have been obliged to comply if the bank had not been placed under curatorship; and
- (e) have the power to bring or defend in the name and on behalf of the bank any action or other legal proceedings of a civil nature and, subject to the provisions of any law relating to criminal proceedings, any criminal proceedings.

(2C) (a) Notwithstanding the provisions of subsection (3) and section 51(1)(b), the curator may –

- (i) dispose of any of the bank's assets;
 - (ii) transfer any of its liabilities; or
- dispose of any of its assets and transfer any of its liabilities, in the ordinary course of the bank's business.

(b) Except in the circumstances contemplated in paragraph (a) the curator may not, notwithstanding the provisions of section 112 of the Companies Act-

- (i) dispose of any of the bank's assets;
- (ii) transfer any of its liabilities; or
- (iii) dispose of any of its assets and transfer any of its liabilities, otherwise than in accordance with the provisions of section 54 of this Act and section 155 of the Companies Act.

(bA) For the avoidance of doubt, any transfer of liabilities in terms of paragraphs (a) or (b) above shall be a transfer of all the liabilities of the bank which rank the same for payment outside of a winding up of the bank.

(c) ~~In respect of any seeking consent for a disposal of assets or transfer of liabilities or such disposal and transfer in terms of paragraph (b), the curator shall report to the Minister and Registrar, as the case may be, on the expected effect on the bank's creditors and whether—~~

- ~~(i) the creditors are to be treated in an equitable manner; and~~
- ~~(ii) a reasonable probability exists that a creditor will not incur greater losses, as at the date of the proposed disposal, transfer or disposal and transfer, than would have been incurred if the bank had been wound up under section 68 of this Act on the date of the proposed disposal, transfer or disposal and transfer.~~

(d) The Minister must, in addition to the requirements of section 54, consider the curator's report as provided in paragraph (c) in making his or her decision in terms of section 54: Provided that notwithstanding the fact that the effects in paragraph (c)(i) and (ii) are not satisfied of the disposal, transfer or disposal and transfer, will be that creditors are to be treated inequitably, the Minister may, subject to section 54, consent to the disposal, transfer or disposal and transfer if it is, in his or her opinion, reasonably likely to promote the maintenance of—

- (i) a stable banking sector in the Republic; or
- (ii) public confidence in the banking sector in the Republic;

(iii) the person or entity to which the disposal of assets or transfer of liabilities or such disposal and transfer is to be made is a going concern and has a reasonable possibility of paying its debts and meeting all obligations in respect of any liabilities so transferred; and

(iv) and such disposal, transfer, or disposal and transfer has been adopted and approved in accordance with the provisions of section 155 of the Companies Act.

(2D) If at any time the curator is of the opinion that there is no reasonable probability that the continuation of the curatorship will enable the bank to pay its debts or meet its obligations and become a successful concern, the curator shall forthwith in writing inform the Registrar of such opinion.

(2E) Any money of the bank that becomes available to the curator shall be applied by him or her in paying the costs of the curatorship and in the conduct of the bank's business in accordance with the requirements of the curatorship and, as far as the circumstances permit, in the payment of the claims of creditors which arose before the date of the curatorship.

(2F) (a) Every disposition of its property, which if made by an individual could for any reason be set aside in the event of such individual's insolvency, may, if made by a bank that is unable to pay its debts, be set aside by a court at the suit of the curator in the event of that bank being placed under curatorship, and the provisions of the law relating to insolvency, shall *mutatis mutandis* apply in respect of such disposition.

(b) For the purpose of this subsection the event which shall be deemed to correspond with a sequestration order under the Insolvency Act, 1936 (Act No. 24 of 1936), in the case of an insolvent, shall be the presentation to the Court of the letter of appointment of the curator.

(2G) The period during which any bank that is a mortgage debtor in respect of any mortgage bond is subject to curatorship in terms of this section shall be excluded in the calculation of any period of time for the purpose of determining whether such mortgage bond confers any preference in terms of section 88 of the Insolvency Act, 1936, as applied to the winding-up of banks in terms of this Act.

(3) The Minister may, in the letter of appointment or at any time subsequent thereto, empower the curator in his or her discretion, but subject to any condition which the Minister may impose and notwithstanding section 51(1)(b) -

(a) to suspend or reduce, as from the date of the curator's appointment as such or any subsequent date, the right of creditors of the bank concerned to claim or receive interest on any money owing to them by that bank;

(b) to make payments, whether in respect of capital or interest, to any creditor or creditors of the bank concerned at such time, in such order and in such manner as the curator may deem fit;

(c) to cancel any agreement between the bank concerned and any other party to advance moneys due after the date of the curator's appointment as such, or to cancel any agreement to extend any existing facility, if, in the opinion of the curator such advance or any loan under such facility would not be adequately secured or would not be repayable on terms satisfactory to the curator or if the bank lacks the necessary funds to meet its obligations under any such agreement or if it would not otherwise be in the interests of the bank;

(d) to convene from time to time, in such manner as the curator may deem fit, a meeting of creditors of the bank concerned for the purpose of establishing the nature and extent of the bank's indebtedness to such creditors and for consultation with such creditors in so far as their interests

may be affected by decisions taken by the curator in the course of the management of the affairs of the bank concerned;

- (e) to negotiate with any individual creditor of the bank concerned with a view to the final settlement of the affairs of such creditor with the bank;
- (f) to make and carry out any decision in respect of the bank which in terms of the provisions of the Companies Act, the bank's memorandum of incorporation or the rules of any securities exchange, on which any securities of the bank or its controlling company are listed, would have required an ordinary resolution or a special resolution of shareholders of the bank or its controlling company;
- (g) to cancel any lease of movable or immovable property entered into by the bank concerned prior to its being placed under curatorship: Provided that, notwithstanding the provisions of subsection (6), a claim for damages in respect of such cancellation may be instituted against the bank after the expiration of a period of one year as from the date of such cancellation;
- (h) deleted
- (i) to cancel any guarantee issued by the bank concerned prior to its being placed under curatorship, excluding such guarantee which the bank is required to make good within a period of 30 days as from the date of the appointment of the curator : Provided that, ~~notwithstanding the provisions of subsection (6), a claim for damages in respect of any loss sustained by or damage caused to any person as a result of the cancellation of a guarantee in terms of this paragraph, may be instituted against the bank after the expiration of a period of one year as from the date of such cancellation~~ such arrangement has been adopted and approved in accordance with section 155 of the Companies Act; and
- (j) to raise funding on behalf of the bank, and notwithstanding any contractual obligations on behalf of the bank to provide security over the assets of the bank in respect of such funding: Provided that, notwithstanding the provisions of subsection (6), any claim for damages in respect of any loss sustained by, or damage caused to any person as a result of such security, may be instituted against the bank after the expiration of a period of one year as from the date of such provision of security.

(3A) The curator shall duly record the nature of and the reasons for each act performed by the curator under any power conferred upon the curator in terms of subsection (3), and such records shall be examined as part of the normal audit performed in respect of the affairs of the bank concerned.

(4) The Minister may, at any time and in any manner, amend the directions in the letter of appointment, and the powers granted by the Minister under subsection (3) to the curator.

(5) deleted.

(6) While such bank is under curatorship -

(a) all actions, legal proceedings, the execution of all writs, summonses and other legal process against that bank shall be stayed and not be instituted or proceeded with without the leave of the court; and

(b) deleted;

(6A) While a bank is under curatorship the curator shall on a monthly basis furnish the Registrar with a written report containing an exposition of the affairs of the bank concerned and in which it is stated

whether or not, in the opinion of the curator, a reasonable probability exists that the bank will be able to pay its debts or to meet its obligations and to become a successful concern.

(6B) Notwithstanding any provision to the contrary contained in this Act, sections 35A, 35B and 46 of the Insolvency Act, 1936 (Act No. 24 of 1936), shall *mutatis mutandis* apply to the curator of any bank under curatorship and to such a bank as if the curator were a trustee of an insolvent estate and the bank were an insolvent or a sequestrated estate as contemplated in those sections;

(7) The Registrar shall as soon as is practicable announce the appointment of a curator and the powers granted to the curator on the appointment of the curator, and any amendment or withdrawal of such powers, by notice in the *Gazette*.

(8) Notwithstanding anything to the contrary contained in any law, the suspension, cancellation or termination of the registration of a bank while such bank is under curatorship in terms of this section shall not affect -

(a) any appointment made, direction issued, or any other thing done under this section in respect of such bank; or

(b) any power to be exercised or duty to be executed in respect of that bank under curatorship by the Minister, the Registrar or the curator, by virtue of the provisions of this section, and the Minister, the Registrar and the curator, respectively, shall until such time as the curatorship is terminated continue to exercise their respective powers and to execute their respective duties under this section in respect of the public company of which the registration as a bank has been so suspended, cancelled or terminated, as if such suspension, cancellation or termination had not taken place

(9) The Minister may-

(a) at any time withdraw the appointment of a curator;

(b) upon application by the Registrar withdraw the appointment of a curator.

(10) Curatorship of a bank shall lapse upon-

(a) the issue by the Minister of written notification to that effect to the curator; or

(b) the winding-up of the bank in terms of the provisions of section 68.