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**ANNEXURE 2A: DRAFT NOTICE – SECURITIES LENDING TRANSACTIONS**

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**FINANCIAL SERVICES BOARD**

No. \_\_\_\_\_

\_\_\_\_\_ 2010

I, Dube Phineas Tshidi, Registrar of Pension Funds, hereby prescribe the conditions for securities lending transactions for pension funds as per Regulation 28(3) of the Regulations made under the Pension Funds Act, 1956 (No. 24 of 1956) as set out in the Schedule below.

This Notice takes effect on the date of publication thereof.

**DP TSHIDI**

**Registrar of Pension Funds**

**DRAFT**

## SECURITIES LENDING TRANSACTIONS

### 1. Definitions

Any word or expression to which a meaning has been assigned in Regulation 28, for purposes of this notice, shall have the meaning so assigned to it.

### 2. Disclosure of securities lending transactions

For purposes of disclosure of the securities lending transaction for annual financial statements and regulation 28, the lent securities must be disclosed as the asset held by the fund, the claim against the borrower must be disclosed as a note to the financial statements.

### 3. Conditions

- 3.1 A fund may engage in a securities lending transaction only if such securities lending transaction(s) -
- 3.1.1 are undertaken in a safe and prudent manner and in accordance with the lending policies and procedures that are approved by its board to provide additional income or fees for the benefit of the fund;
  - 3.1.2 where appropriate, professional advice is sought to ensure that controls and procedures relating to such transactions are comprehensive and sound;
  - 3.1.3 where the administration of a securities lending transaction is outsourced, -
    - (a) the institution to which it is outsourced has the necessary experience and expertise to perform the required duties in a competent and responsible manner; and

- (b) administrative and reporting arrangements are clearly set out and agreed to in writing;
- 3.1.4 a proper assessment of the counterparty credit risk is performed prior to entering into a securities lending transaction;
- 3.1.5 counterparties for purposes of a securities lending transaction shall be limited to:
  - (a) South African and foreign banks, as defined in Regulation 28 of the Regulations made under the Pension Funds Act, 1956 (No. 24 of 1956);
  - (b) A collective investment scheme as defined in the Collective Investment Schemes Control Act, 2002 (Act No. 45 of 2002);
  - (c) A long-term insurer, as defined in Regulation 28 of the Regulations made under the Pension Funds Act, 1956 (No. 24 of 1956); and
  - (d) Broking members of an exchange as defined in Regulation 28 of the Regulations made under the Pension Funds Act, 1956 (No. 24 of 1956);and
- 3.1.6 collateral security is held in a manner which is legally enforceable.
- 3.2 Trustees of funds must be fully cognizant of any additional risks stemming from securities lending transactions and must ensure that they have the systems and controls in place to identify and control such risks. Controls should include a list of borrowers, approved in accordance with the insurer's approved securities lending transaction policies, with specified lending limits for each borrower, which list should be –
  - 3.2.1 available at all times to the personnel responsible for administering securities lending transactions; and
  - 3.2.2 reviewed regularly by appropriate senior management.
- 3.3 Trustees of funds must, at least annually, review and have its securities lending policies approved by its board, specifically in respect of –
  - 3.3.1 the general credit worthiness standards used in establishing the list of approved borrowers; and

- 3.3.2 the overall and individual securities lending limits, taking into account the other exposures of the fund;
- 3.4 The trustees and auditors of the fund must verify at appropriate intervals –
  - 3.4.1 that the insurer has followed the internal procedures and standards established in determining the quality of a borrower;
  - 3.4.2 that securities accepted as collateral are consistent with the approved securities lending policies of the insurer; and
  - 3.4.3 the existence of securities lent, the title to and the value placed on the collateral.

#### **4. General requirements**

- 4.1 A fund may only engage in a securities lending transaction where –
  - 4.2 securities involved in the security lending transaction consist of listed securities or term deposits;
  - 4.3 adequate collateral is held by the insurer at all times to protect itself against the risks associated with the securities lending transaction;
  - 4.4 the amount of collateral taken for securities lending is in accordance with the guidance set out below;
  - 4.5 the trustees ensure that the margin of collateral in excess of the fair value of the securities lent is appropriate at all times, provides adequate protection against volatility and liquidity concerns that may arise for securities lent and for securities held as collateral;
  - 4.6 securities are not lent out for a period exceeding 12 months; and
  - 4.7 any securities lent are subject to an unqualified right of recall by the fund.

#### **5. Securities lending transaction limits**

- 5.1 Any securities that are subject to a securities lending transaction remains assets of the fund and must be disclosed in the financial statements of the fund as assets of the fund. The following information in respect of any

securities lending transaction must be disclosed in the notes to the financial statements of the fund -

5.1.1 a description and the fair value of the securities;

5.1.2 the counterparty to the securities lending transaction;

5.1.3 the type and fair value of collateral security held in the name of the fund or a nominee; and

5.1.4 the expiry date of the securities lending transaction.

5.2 the aggregate value of all securities that are the subject of a securities lending transaction may not at any time throughout the reporting period exceed 50% of the fair value per category of assets referred to in column 1 of Table 1;

5.3 the aggregate value of securities lent or offered to be lent to a single counterparty does not at any time throughout the reporting period exceed 20% of the fair value of any of the categories of assets referred to in Column 1 of Table 1;

## **6. Collateral**

6.1 Collateral security for the securities lent is held in the name of the fund or a nominee for the benefit of the fund, and is at all times at least –

6.2 cash equal to at least 105% of the fair value of the total assets lent out to a counterparty; or

6.3 securities of which the fair value is equal to at least 110% of the fair value of the total assets lent out to a counterparty; or

6.4 a combination of cash and securities of which the fair value are equal to at least 110% of the fair value of the assets lent to a counterparty;

## **7. Contractual requirements**

7.1 Any securities lending transaction must be undertaken in terms of a legally binding written agreement with the borrower. When an agent is involved, there should be an agreement between the fund and the agent, and between the borrower and the agent.

- 7.2 The agreement(s) must set out the rights and obligations of all the parties to the agreement.
- 7.3 The agreement(s) must at least -
  - 7.3.1 identify the insurer and the borrower;
  - 7.3.2 describe the securities that will form part of the securities lending transaction;
  - 7.3.3 describe the type and value of collateral security that will be provided and state if the collateral security will be held in the name of the fund or a nominee on behalf of the fund;
- 7.4 Set out criteria to address situations where-
  - 7.4.1 the aggregate value of the collateral exceeds or falls below the value of the securities lent;
  - 7.4.2 the aggregate value of the collateral exceeds or falls below the agreed upon value of the collateral in relation to the value of the securities lent;
  - 7.4.3 state the period for which the securities will be lent out;
  - 7.4.4 provide for a notice period for termination of the securities lending transaction;
  - 7.4.5 where the fund will not remain entitled to the benefits (such as corporate actions, dividends or other income) associated with the lent securities, provide for payments or settlements to be made by the borrower to the insurer in lieu of dividends or other income accrued or paid in respect of the securities that are subject of the securities lending transaction;
  - 7.4.6 specify the fees or charges payable by the borrower to the fund;
  - 7.4.7 reserve the fund's right of execution without a court order and provide for the immediate transfer to the fund of the ownership and other rights, including voting rights, attached to the collateral security, in the event that the borrower defaults or becomes insolvent; and
  - 7.4.8 provide for an undertaking by the borrower to deliver to the fund securities equivalent to any rights in respect of the loaned securities that may become exercisable before redelivery of the lent securities.