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EBF Response to EBA Consultation on draft ITS amending ITS on supervisory reporting on Liquidity Coverage Ratio (EBA/CP/2014/45)

Preliminary Comments

- **EBF appreciates the opportunity to comment on the draft Implementation Technical Standard (ITS)** for the reporting of the Liquidity Coverage Ratio (LCR) as specified by the Delegated Act (DA). The timeline for those comments was extremely short (2 months) in light of the level of technical detail which had to be considered and even shorter when considering the end of the year holiday period. EBF is hopeful that the comments below will be useful to the European Banking Authority (EBA) and the European Commission (EC) to finalise this ITS. EBF would welcome any call for additional input.
- **The EBF has noticed several inconsistencies in the DA and has informed and communicated those inconsistencies to the European Commission, with recommendations to fix them. The EBF hopes that those inconsistencies will be fixed very soon so that the final ITS on LCR is made consistent with those modifications to the DA.** These inconsistencies relate to the definition of trade finance, the asymmetrical treatment of repos and reverse repos, the liquidity reserves in Central Banks which are not meeting the Credit Quality Step 1 requirement and are not recognised as Liquid Assets, and the definition of SMEs.
- For sake of clarity and to avoid misalignment between the DA and the ITS, the EBF strongly recommends that the ITS instructions systematically refer to the Article and exact wording of the DA. The draft ITS contains several instances of such misalignments that make the reporting and the LCR uncertain. Instructions should only complement, but not change the DA. So as to cope with any potential misalignment between the ITS instructions and the DA, the **EBF recommends that it is made clear that DA prevails over the ITS instructions** (i.e. make the hierarchy of texts clear).
- Seemingly, to the extent that there would be some remaining interpretation issues, the Question and Answer (Q&A) process may be helpful. However, **the Q&A process should be handled carefully to make sure that the EBA's proposals for interpretations do not create more uncertainty by not considering all the ramifications of its proposals** (as there are numerous connections between different LCR assumptions). Additionally, **EBF recommends that EBA's proposals for interpretations are accompanied with the basis for conclusions**, articulating them and the ramifications and connections on other LCR assumptions.
- Though it is mentioned in 5.1 of the CP ("LCR calculation tool") that the tool will not be part of the final ITS, **EBF recommends that the final calculation tool is made available to the banking industry** reflecting all the amendments made during the consultation phase. This will contribute to a better and more harmonised implementation by credit institutions.
- **EBF has noted that the draft ITS does not refer to DA-Art.2(3)** that mentions that in some circumstances, locally applicable LCR's percentages and/or liquid assets' eligibility criteria should be factored in the DA LCR. EBF would welcome clarification on which cells and how the values of those cells should be filled in.

Key Issues

Our main issues relate to the points listed below, described in further detail in the next section. **EBF recommends that:**

- **the report is made simpler by removing the unnecessary *Memorandum Items.***
- **compliance with the DA LCR will be based on credit institutions' own best effort estimates of their DA LCR's, and that the DA-ITS-LCR -reports on dates prior to the DA-ITS-LCR entry into force will not be required.**
- **the operational requirements on *Liquid Assets* apply to the assets in the *Liquidity Buffer*, and that the instructions for repos, reverse repos and collateral swaps are modified accordingly.**
- **the treatment of '*settlement and forward starting transactions*' in both inflows and outflow are clarified and made consistent with LCR assumptions.**
- **the reporting instructions for cross currency transactions are clarified, and the caps on inflows and buffer do not apply by currency.**
- **a guidance is added on when to apply for an early close-out cash flow, and that those cash flows are not subject to liquid asset haircut.**
- **pending the final Regulatory Technical Standard on this adverse market scenario, only the HBLA method as defined by the Basel Committee on Banking Supervision (BCBS) applies.**
- **the instructions for additional liquidity outflows are clarified, and in the meantime banks should be expected to report only the '*planned outflows related to renewal or extension of new retail or wholesale loans*'.**
- **the instruction for row 340 for outflows for derivatives should make clear that they should be netted out of received collateral as per Art.21.**

Detailed Comments

Reports

The EBF acknowledges the simplification of the suggested LCR DA report compared to the LCR CRR report, the first implementation date that is defined as at least 6 months after final ITS is adopted, and for the 30 day remittance period.

The EBF recommends that the report is made simpler by removing the *Memorandum Items* that are not necessary for the calculation of the LCR (which is the specific role of this report). Indeed, as the calibration phase for the LCR is over, it is not clear why some pure information items are still required for regulatory reporting purposes.

The EBF would like to point out operational issues that the LCR reports create and calls for adopting any potential solution to alleviate those issues.

As the DA LCR enters into force from October 2015 and the DA-ITS-LCR enters into force at a later date (December 2015 at the earliest), the EBF would welcome clarification on how the DA LCR will be supervised in-between those two dates. **The EBF understands that compliance to the DA LCR will be based on credit institutions' own best effort estimates of their DA LCR's, and that the DA-ITS-LCR -reports on as of dates prior to the DA-ITS-LCR entry into force will not be required** (i.e. no ex-post reports). EBF Members would welcome confirmation of this understanding.

Issues that applies to Liquid Assets, Collateral Swaps, Outflows and Inflows:

In the DA, *Liquid Assets* are defined in Chapter 2 ('Liquid Assets') of Title II. The operational requirements described in Article 8 in Chapter 1 of Title II relate to the *Liquidity Buffer*. Hence, assets in the *Liquidity Buffer* should meet the definition of Liquid Assets (i.e. characteristics that are intrinsic to the assets) *and* the operational requirements.

In the draft ITS, it is suggested that Liquid Assets, even those which are not part of the Liquidity Buffer, should meet the operational requirements described in Article 8, which is not the EBF's understanding of the DA. The adoption of EBA proposal would lead to the odd situation for which a short term repo on

a Level 1 bond would lead to 0% outflow if it is executed by the treasury function while it would lead to 100% outflow otherwise as the Level 1 bond would not meet the operational requirement Art.8(3). Such an interpretation would be highly detrimental to market making activities, the existence of which is a fundamental assumption and building block of the LCR since it is based on market-liquidity. It should be noticed that currently applicable banking laws require that the treasury function is not co-mingled with capital market activities, such as market making, which would make Art.8(3) impossible to meet, with the dramatic consequences on market making activity.

EBF urges to clarify that operational requirements on *Liquid Assets* apply to the assets in the *Liquidity Buffer*. It can be simply done through not tempering on the DA text to define Liquid Assets. For instance, **the instructions for collateral swaps should be modified as illustrated below**:

- §8 *Institutions shall only report the Level 1, 2A and 2B assets that qualify as liquid assets in accordance with Title II. For collateral lent, this refers to assets that would qualify upon maturity as liquid assets in accordance with Title II~~, including general and operational requirements as defined in Articles 7 and 8 of the Delegated Act~~.*
- §9 *Institutions shall only report the Level 1, 2A and 2B assets that qualify as liquid assets in accordance with Title II. For collateral lent, this refers to assets that would qualify upon maturity as liquid assets in accordance with Title II~~, including general and operational requirements as defined in Articles 7 and 8 of the Delegated Act~~.*

As for the treatment of '*settlement and forward starting transactions*' in both inflows and outflow, the EBF recommends that

- **it is clarified that this applies to all transactions that have been contractually agreed (i.e. 'traded') before the reporting date and that whose settlement dates are within the next 30 days** (without any distinction between forward starting and forward settling transactions). This would clarify (and be substituted) to the sentence '*The following transactions do not have any impact on a credit institution's LCR and shall be ignored: Forward transactions entered into subsequent to the reporting date*'.
- **the cash flows should be reported on a *net* basis**, and not on a *gross* basis. A gross basis approach has no specific legal basis, and would create gross up cash flows and make the cap on inflow more binding for no reason. A net approach would be consistent with treatment of transactions such as collateral swaps (for which a net basis applies) and secured funding (for which the cash inflows/outflows are consistent with a net approach).
- **the flow of assets** (inflow of assets or outflow of assets) **should be considered for their *cash-flow value equivalent* by applying the liquidity value haircut to the market value of the assets**.
- **for transactions with maturity date within the next 30 days, the inflow or outflow at their maturity dates should be calculated with the applicable LCR assumption for this type of transaction that matures in the next 30 days** (disregarding that those specific transactions had settlements in the 30 days). This would be clarified (and be substituted) through the sentence '*The following transactions do not have any impact on a credit institution's LCR and shall be ignored: […] Forward transactions that start prior to and mature after the 30-day horizon.*'

These clarifications would ensure consistency with LCR assumptions.

The reporting instructions for cross currency transactions, such as a repo or a reverse repo with a cash leg in one currency and an asset in another currency (this would apply to collateral swaps too) **are not clear, and should be illustrated with examples**.

The EBF recommends that it is clarified that the cap on inflows and buffer do not apply by currency.

The **EBF recommends that it is made clear that only principal flows are considered for securities** (on the asset side or liability side), and that interest rate coupons are disregarded.

Liquid Assets

In the draft ITS, there is a requirement to consider the cash flow resulting from early close-out of hedges, which are subject to the Liquid Asset's applicable haircut. We think this should not be systematic:

- the early close-out cash flow impact of a Liquid Asset's hedge should be considered when the liquidation needs to be done through a sale. A liquidation through repo would not require unwinding the Liquid Asset's hedge.
- when the early close out needs to be considered:
  - it does not make sense to apply the Liquid Asset's haircut: it should be recognised in full, as for derivatives' payables and receivables.
  - the effect of the hedge being collateralised should be taken into account. Hence, when the hedging derivative is collateralised, there is no net impact of unwinding the hedging derivative.
- In case of macro-hedges it is not operationally possible to derive a corresponding hedge cash flow. Such treatment is only feasible for micro-hedges. It should be included in the guidance that a cash flow from early close of hedges only applies to micro-hedges.

The EBF recommends to insert a guidance on when to apply for an early close-out cash flow, such as '*For Liquid Assets in the Liquidity Buffer whose market risk is micro-hedged, an early close out cash flow should be reported like derivatives' payables or derivative's receivables, net of potential offsetting collateral flow value, when the liquidation mode is expected to be through a sale process. The value of Liquid Assets in the Liquidity Buffer should not be adjusted from any early close out cash flow.*' The example p17 of the CP should be modified accordingly.

In §3, the references to 10 (d) and 12 (c) should be replaced by 10 **(1)** (d) and 12 **(1)**(c).

For rows 020 and 030**,** it is unclear if and under what circumstances the standard weight can deviate from the applicable weight. In draft XXV, p. 3, row 030, it is stated that '*Applicable weights may reflect, but are not limited to, firm-specific and national discretions.*' **To our understanding, the standard weight will always equal the applicable weight as DA does not provide for any additional firm- or national-discretion on the applicable haircut for Liquid Assets.**

In row 590, the reference to row 500 should be replaced by row 580.

In reporting template, the Item column related to Row 420 should be amended accordingly to instructions (suppress reference to corporate bonds and shares).

Liquid assets that are reported as part of the memorandum items are not included in the LCR's buffer. However the memorandum items include 'member state guaranteed banks assets subject to grandfathering'. This is not consistent with the text in the LCR DA because grandfathering provisions aim to *include* these assets as liquid assets.

Collateral swaps

Please refer to our comments on the section above for the definition of Liquid Assets.

In §7 ('*Collateralised derivatives flows within 30 days shall be reported on this Template in Columns 090-120, not in Columns 010-080.*'), **it is unclear, why collateralised derivatives in general are to be reported here**. Derivative flows receive an adequate capture in the outflows and inflows section. Art 28 (4) for

outflows and Art 32 (3) (e) for inflows only refer to collateral swaps, not to collateralised derivatives in general.

According to the EBA Public Hearing in London on 15 January, information on collateralised derivatives is needed for LCR calculation purposes: However, Art 17 (2) DA LCR refers only to secured funding, secured lending and collateral swaps, but does not refer to collateralised derivatives other than collateral swaps. **The reporting requirement for collateralised derivatives cannot be derived from the Delegated Act and should be removed.**

We appreciate additional guidance on the reporting of collateral swaps. However, the following questions remain:

- How do we treat collateral swaps with collateral pools with multiple types of collateral that cannot be assigned to individual transactions (i.e. if they are managed at the level of the counterparty)? Can these collateral pools be allocated proportionally to the individual transactions?
- How should we report cash in these collateral pools? Can cash in collateral pools be reported in the template for collateral swaps?

It is unclear why the *Memorandum Items* are needed for collateral swaps. They increase high implementation burden for collateral swaps without any obvious added value for supervisors. As for our general call, the **EBF recommends removing *Memorandum Items*** for collateral swaps.

Outflows

There is no dedicated category to report outflows for deposits from *Personal Investment Companies* (PICs) or *Brokered Deposits*. **EBF would like clarification that deposits from PICs and Brokered Deposits are included in Annex XXV, outflows item 1.1.3.3** (‘*deposits by other customers*’), referring to Article 28.1 of DA which includes these items.

The impact of adverse market scenarios is broken down in categories that the EBA suggested (Historical Look Back approach, Advance Method for Additional Outflows) in rows 310 to 330. **However, it should be made clear that, pending the final Regulatory Technical Standard on this issue, only the HBLA method as defined by the Basel Committee on Banking Supervision (BCBS) applies.**

The template requires breaking down short positions into sub-categories (covered by collateralised SFTs, other in rows 360 and 370), for no reason. This break down is unnecessary. **The EBF recommends removing rows 360 and 370 and to report the short positions in row 350** (‘*short positions’*).

It should be clarified that for additional outflows related to excess collateral, due collateral or substitutable collateral (row 380,390,400), the liquidity value of the collateral should be reported.

In row 430, it is required that bank look through the maturity of the debt instruments issued by asset backed commercial papers, conduits, securities investment vehicles and other; which is not possible. **The ITS instruction should be aligned with the DA Art. 30 (9) ‘*Credit institutions shall assume a 100% outflow for loss of funding on asset-backed commercial papers, conduits, securities investment vehicles and other such financing facilities. This 100% outflow rate shall apply to the maturing amount or to the amount of assets that could potentially be returned or the liquidity required.*’**

For sake of simplicity, without losing any information, the EBF recommends to report '*assets borrowed on an unsecured basis*' (row 440) as '*short positions*' (row 350).

The instructions to fill in (and in fact the DA Art. 23 (1) on) the additional liquidity outflows in rows 720 to 870, are unclear (except for '*planned outflows related to renewal or extension of new retail or wholesale loans*' for which Example 4 p19 of the CP provides useful illustration). The articulation with the other LCR assumptions should be made clear as it seems to us as a double counting process. The EBF is also very concerned on the discrepancies that this could lead to between different jurisdictions exercising their national discretions.

For Example 4, it should be clarified:

- How this example articulates the treatment for credit and liquidity facilities;
- What are the 'customer group' 1, 2, 3 and 4 listed in the table. Our understanding, based on EBA Q&A answer ref 2014_897 is that this calculation is not to be made on a client by client basis;
- That column B "contractual commitment to extend funding' is the total amount of the commitment and not solely the unused part;
- That the amount calculated in column D is already weighted (as per DA article 32) (as it is is not correctly implemented in the LCR calculator provided)

The EBF calls for clarifying the instructions for additional liquidity outflows, and in the meantime banks should be expected to report only the '*planned outflows related to renewal or extension of new retail or wholesale loans*'.

The instruction for row 030 is unclear and most probably contains typos (bolded and comment in italic bracket *[]*): '*In accordance with Article 28 (6) of Commission delegated regulation (EU) No XXX/2015 credit institutions shall also report within the appropriate retail deposit category the amount of the notes, bonds and other securities issued which are sold exclusively in the retail market and held in a retail account. Credit institutions will consider for this category of* ***assets [? They are liabilities]*** *the applicable outflow rates provided for by the Commission delegated regulation (EU) No XXX/2015 for the different categories of retail deposits. Accordingly, credit institutions shall report as applicable weigh the average of the relevant applicable weights for all these* ***bonds [? What does it mean? Shall be read as 'deposits' rather than 'bonds'?]****.*'

The instruction for row 340 for outflows for derivatives should make clear that they should be netted out of received collateral as per Art.21 ('*For the purposes of this Article, net basis shall be considered to be* net of collateral to be received provided that it qualifies as a liquid asset *under Title II of this Regulation.*').*

The instructions for reporting undrawn committed credit facilities provided to retail customers refers to the retail deposit definition. We do not see how banks can apply this definition to off balance sheet exposures as it does not concern deposits.

Undrawn committed credit facilities provided to financial customers (not being banks) receive an outflow of 100% in the current templates. However, Art. 31 (4) (c) of the DA LCR includes the possibility of applying 10% outflows to these facilities.

The instructions for facilities to promotional loans (row **510/520/530 for credit facilities and 650/660/670/680 for liquidity facilities) are not clear.** We understand that 510 and 520 captures the first

sentence of Art. 30 (9) and is to be reported only by promotional credit institutions. It is unclear where and how the second sentence of Art. 30 (9) is captured in the Outflow template and if the second sentence is to be reported only by promotional credit institutions or also other credit institutions ("By way of derogation from Art. 32 (3) (g) where those promotional loans are extended as pass through loans via another credit institution acting as an intermediary, a symmetric inflow and outflow may be applied by credit institutions.") The same applies to 660 and 670 for liquidity facilities. More guidance would be welcome for the treatment of promotional loans.

For committed Credit and Liquidity Facilities within group or Institutional Protection Scheme (IPS) in rows 550 and 690, the EBF would welcome confirmation that by "preferential rate" it is meant that both facilities are allowed: *lower* outflow rate according to DA Art. 29 with a group or IPS, and *higher* outflow rate to be applied symmetrically when the opposite counterparty receiving the facility has benefited from a higher inflow rate according to DA Art.34 within a group or IPS.

Some instructions may require the correction of typos: In row 570, 1.1.5.1.6.2 should be replaced by 1.1.5.1.7., and the reference to Art. 31(7) should be replaced by Art. 31 (8)(c). In row 710, 1.1.5.2.7.2 should be replaced by 1.1.5.2.8, and the reference to Art. 31 (7) should be replaced by Art. 31 (8)(c). The guidance and the decision tree should be adapted accordingly. Furthermore, sentences do not apper finished in instructions for rows 720-730, and row 1050. In row 880, the reference to Art. 31 (9) should be replaced by Art. 31 (10).

In the instruction to row 900 ('Other liabilities'/'*in the form of debt securities if not treated as retail deposits*'), the last sentence ('*This amount includes also coupons that come due in the next 30 calendar days referred to all these securities*') should be deleted as it would be inconsistent with Art. 6 and all the rest of instructions on reporting principal amounts.

Inflows

In row 060, it is unclear what definition of retail customers is referred to.

In rows 120 and 130, it will be very difficult for banks to obtain information from counterparties, as to whether they treat outflows from the depositing institution as operational. In some cases, this information may be considered proprietary.

On row 200, the instruction should be aligned with DA Art. 32(3) '*assets with an undefined contractual end date shall be taken into account with a 20% inflow rate, provided that the contract allows the credit institution to withdraw **or** to request payment within 30 days;*' (the instruction wrongly substitutes 'or' by 'and').

In row 360, 1.2.1.8 is a sub-position of collateral that qualifies as liquid assets. Such restriction to liquid assets collateral cannot be derived from DA Art. 32 (3)(b). It also applies to collateral that does not qualify as liquid assets.

In row 490 (Annex XXIV, ID 4.3 – secured transactions), "secured transactions" refer to secured lending (as per DA Art.32(3)(b) whose collateral are financial instruments. The EBF would welcome confirmation.

Table C74, Inflows, rows 430 – our understanding is that only column "exempted from the cap on inflows" can be booked. Entities which inflow have been capped to 75% and 90% cannot have inflows in excess of 100% of NCOs as required by Art. 2 (3) (e).

Calculation tool

The calculation tool does not correctly unwind collateral swap transactions: In the calculation tool the securities borrowed are removed from the liquidity buffer but not from the outflows. When adjusting the Liquidity Buffer for unwinding collateral swaps the corresponding outflow or inflow should also be eliminated.

The calculation tool does not correctly apply the composition requirements on the LCR. The composition adjustments now apply to the minimum of the three caps/floors, while in principle all composition requirements should be met, adjustments based on one requirement do not necessarily result in a liquidity buffer where all requirements are met.

Q1: The EBA deems it appropriate to keep the remittance dates unchanged in a steady state regime. While the content of the templates is changed, the objective of the supervisory reporting keeps unchanged and the present ITS constitutes only an update of the current existing reporting requirements for the LCR. This means that, once the current ITS is adopted, and after a transition phase, credit institutions would have to remit the monthly reports on each following 15th calendar day as this will be the case starting 1 January 2015 under the existing ITS on reporting for the LCR. Nevertheless, the EBA deems it appropriate to introduce longer remittance dates for the first reference dates during the first months, to be limited to a period of six months.
Do respondents have arguments to put forward a change on these aspects?

The EBF supports EBA's proposal.

Q2: Do respondents agree with longer remittance dates for the first reference dates for the new templates for the first six months?

The EBF supports the EBA's proposal for 30 day remittance period and recommends it applies under normal circumstances (i.e. beyond the first months), and is shortened only when necessary (i.e. emerging or actual liquidity crisis).

Q3: Do respondents agree with the implementation period suggested?

The EBF supports EBA's proposal.

Q4: Do respondents agree to the structure and content of the proposed new LCR templates added for credit institutions? Particularly comments from respondents on specific rows, columns or any other item would be very valuable and appreciated including comments on the treatment of secured transactions.

Please refer to our detailed comments of our letter.

Q5: Do respondents find the new LCR instructions for credit institutions clear? Particularly comments from respondents on specific rows, columns or any other item would be very valuable and appreciated.

Please refer to our detailed comments of our letter.

Q6: Do respondents consider that the "LCR calculation tool" appropriately translates the use of the different templates for informative purposes?

Yes, the LCR calculation tool is indeed helpful, as it enables banks to understand how the correct calculation is to be undertaken.