GUERNSEY FINANCIAL SERVICES COMMISSION
ISLE OF MAN FINANCIAL SUPERVISION COMMISSION
JERSEY FINANCIAL SERVICES COMMISSION

DISCUSSION PAPER ON: BASEL III: LIQUIDITY

Issued: 7 JULY 2015

GLOSSARY OF TERMS

The following table sets out a glossary of terms used in this paper.

ASF	Available Stable Funding, as defined in the NSFR
Basel Committee	Basel Committee on Banking Supervision
Basel II	"*International Convergence of Capital Measurement and Capital Standards*", re-issued in comprehensive form in June 2006 by the Basel Committee
Basel III	collectively, a series of documents issued by the Basel Committee that either revise Basel II or establish new international standards regarding the financial management of international banks
Basel III DP	Discussion Paper on Basel III, issued by the Tri-party Group in September 2012
Basel III LCR standard	"*Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools*", issued by the Basel Committee in January 2013
Basel III NSFR standard	*"Basel III: The Net Stable Funding Ratio"*, issued by the Basel Committee in October 2014
CDs	Crown Dependencies – Guernsey, Isle of Man and Jersey
CDLCR	proposed local standard, closely aligned to the LCR, set out in this document
CDLMR	alternative proposed local standard, the "**CD Liquidity Mismatch Ratio**", set out in **Section 7**, that dispenses with the 75% cap (in the LCR) on projected inflows from group banks, provided that they are timely
CRD IV	EU package of proposals to address the Basel III requirements
CRR	Capital Requirements Regulation, part of CRD IV
D-SIB	domestic systemically important bank
EBA	European Banking Authority
GFSC	Guernsey Financial Services Commission
HQLA	High Quality Liquid Assets
ICAAP	Internal Capital Adequacy Assessment Process
IOMFSC	Isle of Man Financial Supervision Commission
JFSC	Jersey Financial Services Commission
LCR	Liquidity Coverage Ratio, global consolidated standard for international banks, defined in the Basel III LCR standard
LCR Delegated Act	"*Liquidity Coverage Requirement Delegated Act*" - the final EU version of the LCR – enacted by the EU on 10 October 2014
LCR Disclosure Rules	*"Liquidity coverage ratio disclosure standards"*, issued by the Basel Committee in January 2014, revised March 2014
LMP	Liquidity Management Policy
NSFR	Net Stable Funding Ratio, global consolidated standard for international banks, updated in the Basel III NSFR standard
PIC	personal investment company, as defined in the LCR Delegated Act
PIC deposit	a deposit from a PIC
RSF	Required Stable Funding, as defined in the NSFR
SPE	special purpose entity
SREP	supervisory review and evaluation process
Tri-Party Group	comprises the GFSC, IOMFSC and JFSC

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EXECUTIVE SUMMARY

Overview

This paper raises, and proposes outline solutions to, issues relating to regulatory requirements for liquidity management and reporting in the Crown Dependencies ("**CDs**"). It uses as its basis papers issued by the Basel Committee on Banking Supervision ("**Basel Committee"**). In so doing, it addresses the similar EU proposals incorporated in the Capital Requirements Regulation ("**CRR**").

This paper has been issued as part of the work of the CD supervisors (the "**Tri-party Group**") on applying Basel III in the CDs.

What is proposed?

It is proposed to:

- develop a consistent framework for monitoring short-term liquidity. This would incorporate limited flexibility to reflect particular jurisdictional circumstances;
- develop a common set of prudential reporting requirements that cover all aspects of liquidity; and
- address certain liquidity issues that arose in considering the above.

Who would be affected?

All banks that are incorporated in the CDs would be impacted by these proposals. It is not proposed to make branches subject to these proposals: branch reporting might be aligned at some point but this is not discussed in detail herein.

Feedback and next steps

Feedback should be sent to the local supervisor by 7 October 2015. This will be shared within the Tri-Party Group unless the submitter objects.

The Tri-Party Group intends to then develop a final set of proposals that reflect feedback received. These would be consulted on and implemented separately, in order to enable local considerations to be addressed, with the common aim of implementation before end 2018.

INTRODUCTION

1 Background

1.1 In June 2006, the Basel Committee issued, in comprehensive form, a framework for regulatory requirements for the capital adequacy of international banks. This document, "*International Convergence of Capital Measurement and Capital Standards*", became known as "**Basel II**".

1.2 Latterly, the Basel Committee has worked to revise Basel II. This work has resulted in a number of standards being issued that either revise Basel II or establish new international standards regarding the financial strength of international banks. Collectively, this initiative is described by the Basel Committee as "**Basel III"**, which encompasses liquidity measures as well as revised capital adequacy rules.

1.3 The Tri-Party Group - The Jersey Financial Services Commission ("**JFSC**"), Guernsey Financial Services Commission ("**GFSC**") and Isle of Man Supervision Commission ("**IOMFSC**") – sought to establish a unified approach, wherever possible, to implementing Basel II during the period 2005 to 2008.

1.4 The Tri-Party Group issued a Discussion Paper on Basel III in September 2012 (the **"Basel III DP")** to all banks that are incorporated in the CDs – Guernsey, Isle of Man and Jersey - to provide information on Basel III and an indication of the Group's initial views, and in order to solicit feedback.

1.5 The Tri-Party Group followed this with Discussion Papers on specific issues:

1.5.1 A December 2013 paper contained detailed proposals regarding capital adequacy, building on those in the Basel III DP and feedback received. In the main, these proposals responded to the revised requirements of Basel III set out in the paper "*A global regulatory framework for more resilient banks and banking systems*", issued December 2010 and revised June 2011;

1.5.2 A January 2014 paper addressed domestic systemically important banks ("**D-SIBS**") and recovery and resolution for such banks; and

1.5.3 A June 2014 paper addressed the leverage ratio proposals in Basel III, building on both the original Basel III proposals and the detailed reporting framework set out in the Basel Committee paper "*Basel III leverage ratio framework and disclosure requirements*", issued in January 2014.

1.6 This paper contains detailed proposals for liquidity management, building on those in the Basel III DP and related feedback. These address the proposals set out in "*Basel III: International framework for liquidity risk measurement, standards and monitoring*"[1], issued in December 2010 and revised in:

1.6.1 "*Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools*"[2] published in January 2013 and referred to herein as the "**Basel III LCR standard**"; and

1.6.2 "*Basel III: The Net Stable Funding Ratio*"[3], published in October 2014 by the Basel Committee and referred to herein as the "**Basel III NSFR standard**".

1.7 The Tri-Party Group is distributing this paper to all banks incorporated in the CDs to provide information on the proposed approach in the CDs and solicit feedback. A period of three months to 7 October 2015 has been set aside for this and banks are asked to submit views to their local supervisor but be aware that the content of feedback will be made available to the other CD supervisors on a no-names basis.

1.8 Consideration of other subject areas identified in the Basel III DP will follow in due course, enabling focussed consideration of each element in turn.

1.9 Some other aspects, including those relating to the Trading Book, are less relevant in some islands and hence will be addressed separately by each CD, rather than through further Tri-Party DPs, although no decisions have been reached on these at this time.

1.10 As in the Basel III DP, rather than considering Basel III as a block of standards that must all be implemented, individual elements are considered separately in this paper on their own merits. The Tri-party Group aims to implement only those elements that are relevant and appropriate.

1.11 Current regulation of branches does not include prudential requirements in respect of capital (in all CDs). In respect of liquidity, some elements are applied in all CDs but regulatory liquidity limits are only applied in Guernsey, not in Jersey or the Isle of Man. The Tri-party Group takes the view that prudential oversight is the responsibility, on a whole company basis, of the home supervisor. It is not, therefore, intended to extend the regulatory liquidity requirement proposals in this paper to branches. For the avoidance of doubt, in all CDs, branches would not be subject to the new local prudential liquidity regulations.

2 Related international developments

2.1 Any consideration of liquidity management requires an understanding of home regulators' requirements. The EU is particularly important, given the preponderance of EU banks in the CDs. Much of the work on the establishment of the EU's implementation of Basel III appears in a set of proposals known as "**CRD IV**", with the resultant relevant regulation being the CRR. Reference to EU application is made herein, where relevant, particularly where it differs to Basel III.

[1] http://www.bis.org/publ/bcbs188.htm
[2] http://www.bis.org/publ/bcbs238.htm
[3] http://www.bis.org/bcbs/publ/d295.htm

OUTLINE OF PROPOSALS

3 Overview

3.1 In the Basel III DP, it was noted that local banks are not necessarily considered to fall under the scope of Basel III, except on consolidation. However, it was explained that the Tri-Party Group considers that aspects of Basel III may be relevant in the CDs. In addition, the Tri-Party Group considers that a move to a more uniform minimum standard across the CDs is a worthwhile goal in itself, to meet industry's regular calls for commonality and to limit opportunities for regulatory arbitrage.

3.2 In response to the Basel III DP, some banks sought confirmation that Basel III would be fully adopted, with respondents pointing out that compliance with a different local standard would be more burdensome, as Basel III would be adopted at group level. However, there was some concern expressed on the liquidity calculation methodology, with a minority also expressing concerns about costs. Overall, the majority appeared to accept the proposed way forward, with dissenting views in the minority. Those favouring strict adherence to Basel III were approximately equal in number to those favouring no or more limited change.

3.3 The initially most obvious alternatives are to either broadly leave matters alone or implement the Liquidity Coverage Ratio ("**LCR**") with little change. The first is not feasible: a review of liquidity management is appropriate since the current requirements were introduced in the CDs before the financial crisis and it would not be appropriate to ignore the subsequent development of international standards. Neither is the latter considered desirable, as some aspects of the LCR are either not appropriate in the CDs or not relevant.

3.4 The Tri-party Group has therefore decided that a Basel III consistent approach should be implemented at local level. Hence, this paper aims to arrive at a common set of proposals that are appropriate for the management of liquidity in CD incorporated banks, based on relevant elements of the Basel III LCR and NSFR standards.

3.5 In general, using the definitions set out in Basel III would tend to limit compliance costs for banks, since most are part of groups that will need to meet Basel III requirements. The approach taken in this paper is to address each element separately, proposing a way forward which would, if implemented, be applicable to banks incorporated in the CDs, with limited jurisdictional variations.

3.6 Most of the paper concerns the LCR standard. This reflects three factors:

3.6.1 the need for standard short term liquidity metrics is well established in the CDs: all three regulators have been using these as part of liquidity regulation for a number of years;

3.6.2 the Basel III adoption timeline for the LCR, though phased, started this year (2015); and

3.6.3 the Basel III standard is largely final: the rules have been revised and are likely to be so again but the broad design appears to be stable.

3.7 In contrast, consideration of the Net Stable funding Ratio ("**NSFR**") is limited to data reporting (See **Section 4** for more detail on the rationale and **Section 31** for more detail on proposed reporting) and continued evaluation. This reflects:

3.7.1 the need for standard long term liquidity metrics has yet to be established in the CDs. Typically, banks will be part of groups that are required to be compliant at consolidated level and, over the longer timelines relevant to the NSFR, it is not apparent that there are significant barriers to providing liquidity within group, where needed;

3.7.2 the NSFR adoption timeline is much further out, compared to the LCR, in 2019;

3.7.3 the lack of available data to determine the impact of introduction; and

3.7.4 the Basel Committee has stated that it will review the standard during the period before adoption.

3.8 To facilitate the introduction of revised reporting requirements (**Section 31**), terminology used will be in line with the definitions in the Basel Committee paper "*Liquidity coverage ratio disclosure standards*"[4], ("**LCR Disclosure rules**"), issued in January 2014 and revised March 2014. This sets out a disclosure framework for internationally active banks regarding the LCR. The framework is a useful starting point and many of the banks incorporated in the CDs will be subject to either it or similar disclosure requirements on a consolidated level.

3.9 Timescales for implementation are uncertain at this time, principally due to practical constraints. The Tri-Party Group intends to have the new system fully operational and in place by the end of 2018 at the latest. Further transition details are provided in **Section 8.**

4 NSFR

4.1 It is considered that commencing the reporting of NSFR data and an NSFR ratio would be beneficial as:

4.1.1 the data would be useful in itself, providing a snapshot of the balance of longer term funding vs longer term lending. Whilst no minimum level would be established, trends in the data might highlight developments that are relevant, both to supervisors and banks themselves;

4.1.2 the data will enable the evaluation of the benefits of the NSFR and whether any changes should be made to it to reflect local circumstances; and

4.1.3 it is likely that including NSFR reporting within the proposed suite of reports for liquidity (see **Section 31**) will ease implementation of the overall reporting package. This is because it would enable the bulk of the work to be undertaken within one project.

[4] http://www.bis.org/publ/bcbs272.htm

Question 1 ***Do you consider that the proposals for introducing the reporting of the NSFR are appropriate?***

5 General approach to implementation of the Basel III LCR standard

5.1 The Basel III LCR standard is similar to the approaches currently prescribed locally in that:

5.1.1 it requires predicted outflows to be met by a mixture of predicted inflows and High Quality Liquid Assets ("**HQLA**"); and

5.1.2 predicted flows are based on a mixture of contractual and behaviourally based projections.

5.2 The main differences are:

5.2.1 the definition of HQLA in the Basel III LCR standard is different to the types of marketable assets used in the CDs; generally, the definition in Basel III is tighter;

5.2.2 the LCR limits the extent to which inflows may offset outflows and obviate the need to hold HQLA; HQLA must exceed 25% of adjusted outflows in all cases;

5.2.3 the allowance for depositor behaviour is different: the GFSC uses different fixed percentages whilst the IOMFSC and JFSC allow percentages that vary across banks, based on individual submissions; and

5.2.4 all three CD regulators apply in addition a one week metric.

5.3 The approach taken in this document is to look at each aspect separately, considering local approaches against the LCR, and propose a common approach across the CDs. Where the LCR approach appears appropriate, adoption is recommended; where it is seen as potentially valid, safeguards are proposed; and where it is seen as insufficient or inappropriate, approaches based on local dynamics are proposed.

5.4 Proposals are outlined in detail, rather than by simple reference to the LCR. The alternative – cross referring to the Basel document – would have shortened this document but it is considered that respondents might find it easier to assess the proposals without this being necessary.

5.5 The proposals are intended to establish a robust liquidity standard, whilst recognising international best practice. Whilst in some areas they diverge from Basel III, this reflects local circumstances, including the fact that almost all banks in the CDs are part of wider groups that manage liquidity on a consolidated basis.

5.6 Significant adverse impacts, if the LCR were implemented unaltered, would perhaps most likely arise from: (1) the treatment of fiduciary deposits; (2) more limited recognition of inflows; and (3) the tighter definition of liquid assets. **Sub-sections 5.7** to **5.9** describe the potential impacts in these areas and proposes measures to limit these.

5.7 Fiduciary deposits

5.7.1 Fiduciary deposits, for these purposes, include:

- "Swiss fiduciary deposits": amalgamated customer deposits placed by banks with other banks;
- Deposits from trustees on behalf of trusts, whether pooled or not;
- Deposits placed by investment firms on behalf of one or more clients, within an investment mandate; and
- Any other deposit that is known to be managed by a financial entity on behalf of a customer.

5.7.2 The Tri-Party Group considers that the LCR requirement for fiduciary deposits to be treated as a 100% contractual outflow, with no reflection of stickiness except in the case of certain operational deposits, does not reflect a balanced approach to fiduciary deposits. It would also be significantly negative for banks in the CDs, where currently:

- banks in Guernsey may apply a 50% outflow rate; and
- banks in Jersey and the Isle of Man may apply a rate lower than 100%, subject to the agreement of the respective supervisor being obtained, based on bank-specific behavioural data.

5.7.3 On 10 October 2014, the EU adopted the "*Liquidity Coverage Requirement Delegated Act*" ("**LCR Delegated Act**")[5], which effected EU implementation of the LCR. This provides that a deposit made by a personal investment company ("**PIC**") could be treated similarly to a deposit from a non-financial customer and hence attract a 40% outflow rate. A PIC is defined in the LCR Delegated Act as:

- *"… an undertaking or a trust whose owner or beneficial owner, respectively, is a natural person or a group of closely related natural persons, which was set up with the sole purpose of managing the wealth of the owners and which does not carry out any other commercial, industrial or professional activity. The purpose of the PIC may include other ancillary activities such as segregating the owners' assets from corporate assets, facilitating the transmission of assets within a family or preventing a split of the assets after the death of a member of the family, provided these are connected to the main purpose of managing the owners' wealth".*

5.7.4 The LCR Delegated Act states that deposits from PICs get a 40% outflow rate and, as such, is consistent with the original treatment in CRR and Basel III (since PICs are prima facie non-financial customers). However, some have construed this as also allowing the 40% outflow rate to be applied to a deposit placed on a fiduciary basis by a manager on behalf of a PIC, including where the manager places pooled deposits on behalf of several PIC

[5] http://ec.europa.eu/internal_market/bank/docs/regcapital/acts/delegated/141010_delegated-act-liquidity-coverage_en.pdf

clients. This is not permitted by the LCR, which explicitly states that fiduciary deposits must attract a 100% outflow rate. Neither CRR nor the LCR Delegated Act distinguish between deposits placed on a fiduciary basis from those placed directly by the client: they do not explicitly state that the 40% outflow rate would apply in such circumstances or explicitly require a 100% outflow rate to be applied in such circumstances.

5.7.5 It is proposed to amend the LCR to provide a specific beneficial treatment for PIC deposits (as per the EU) and that this should explicitly cater for the circumstance where PIC deposits are placed on a fiduciary basis. This is considered appropriate because:

- there is evidence locally of stickiness. This might not reflect the experience of overseas supervisors that have experienced a greater number of bank failures, which appears to have driven the very conservative approach set out in Basel III;
- Basel III is designed for implementation by a small number of internationally active institutions, whereas the LCR will apply to all CD incorporated banks; and
- Basel III is designed to be applied at the consolidated level, whilst it will apply at the solo level in the CDs.

5.7.6 Specific intentions regarding the beneficial treatment are set out below (and expanded in **Appendix B**):

- It is proposed that adjustments be permitted for short-term deposits from PICs (using a similar definition for PIC to that in the LCR Delegated Act), where (1) the deposit is placed by the PIC itself or (2) it is placed on a designated basis by a fiduciary.
- Such deposits would be treated as deposits from non-financial corporates, and hence a 40% outflow assumption will apply. These are referred to herein as "**PIC deposits**".
- This is not intended to benefit all fiduciary deposits: clear parameters will be established and fiduciary deposits that fall outside of these (such as deposits placed on a pooled basis and deposits from trusts that do not meet the specific definition in **Appendix B**) would attract the 100% outflow assumption set in Basel III (unless they meet the definition of an operational deposit, see **Section 24**).

5.7.7 The adverse impact for fiduciary deposits that do not meet the definition of a PIC deposit (such as deposits placed on a pooled basis and deposits from trusts that do not meet the specific definition in **Appendix B)** but for which behavioural adjustments are currently applied would be that they would now attract a 100% outflow rate, requiring more liquidity to be held where the deposit matures within one month.

5.7.8 It is anticipated that the transitional period would enable banks to work with fiduciary managers to mitigate any negative consequences as follows:

- fiduciary managers could place deposits on a longer term basis to mitigate any consequential impact on the pricing of short-term deposits, should banks reflect the increased liquidity costs;
- products such as notice accounts could be used to balance the need for access versus liquidity cost. Where banks pursue such approaches, they should assess the impact on liquidity; and
- banks can and should reflect liquidity costs in pricing, in order to provide fiduciary managers with an incentive to place longer term deposits and reduce the net liquidity cost to the bank.

5.7.9 The Tri-Party Group is continuing to consider the specific case of Swiss fiduciary deposits, including whether such deposits have the same behavioural characteristics as more stable deposit categories.

Question 2 ***Do you consider that the proposals regarding fiduciary deposits would, if enacted across the CDS and against a backdrop of similar proposals being established as an international standard, be likely to give rise to a loss of business or profitability? If so, are there appropriate additional measures that could mitigate the impact of these proposals, including those regarding the treatment of Swiss fiduciary deposits? If so, please outline them, together with a brief assessment of pros and cons and provide relevant evidence.***

5.8 Limited recognition of inflows

5.8.1 The negative impact arising from the LCR's limited recognition of inflows stems from its limitation on outflows offsetting inflows by no more than 75% when determining the HQLA requirement.

5.8.2 Most banks in the CDs are part of larger groups that hold HQLA but in many cases these assets are held centrally, with loans from group used to provide liquidity to local banks when needed.

5.8.3 It is therefore proposed to establish, as an option, an "alternative standard" (the CDLMR, see **sub-section 7.1**), whereby projected inflows from group banks are permitted to fully offset projected outflows.

5.8.4 An inflow of cash, though, is only useful for this purpose if it occurs on or before the relevant cash outflow occurs. Therefore, it is proposed that projected inflows would only be recognised (1) where they are expected to occur within one week or (2) to the extent that they reduce projected outflows that are expected at a later date. Hence, projected inflows towards the end of the one month period would be excluded from the calculation if all projected outflows occurred earlier in the month (whereas under the LCR, they would be eligible for inclusion). This is outlined in **Section 7**, with fuller details provided in **Appendix C**.

5.9 Liquid assets

5.9.1 These proposals use the LCR definition of HQLAs, which is tighter than the CD supervisors' definitions of marketable assets used currently in the CDs. The impact will vary, depending on the assets banks currently use and the

extent to which they were already planning to switch to higher quality assets. The use of a common definition should aid group reporting and these assets should be eligible HQLA at group level, and aid meeting consolidated liquidity.

5.9.2 Some banks in the CDs have moved away from holding assets to meet liquidity needs that are unlikely to qualify as HQLA. In some cases, this reflects group requirements, in others the change in holdings was prompted by similar concerns regarding the appropriateness of these assets, given the experience of the financial crisis and also recent changes to deposit preference laws and bail-in regimes in some other countries. For these reasons, fewer banks in the CDs hold any marketable assets for liquidity management purposes that do not meet the HQLA criteria (outside of banks that are currently solely reliant on intragroup flows) and hence the expected impact on industry of the changed definition is expected to be relatively small.

5.9.3 However, banks will need to ensure that all relevant criteria are met and some might see higher net liquidity costs, if higher yielding marketable assets are found to be ineligible and hence need to be replaced with eligible HQLA.

Question 3 ***Do you consider that there are appropriate additional measures to those outlined in Section 5.8 and 5.9 that could mitigate the impact of these proposals? If so, please outline them, together with a brief assessment of pros and cons.***

6 Usability of liquidity reserves

6.1 The Basel Committee emphasised that HQLA are intended to be available for use in a crisis. The wording in the LCR is:

6.1.1 "*The Committee also reaffirms its view that, during periods of stress, it would be entirely appropriate for banks to use their stock of HQLA, thereby falling below the minimum. Supervisors will subsequently assess this situation and will give guidance on usability according to circumstances*."

6.2 It is proposed to adopt a similar view and that, therefore, the amended liquidity metric should be used as a trigger, rather than an absolute minimum. Banks would be required to immediately inform their supervisor of any actual or imminent breach and would be expected to put forward plans to remedy it. The supervisory response would depend on the specific circumstances, and the nature and scale of the breach.

6.3 It is accepted that extraordinary circumstances may lead to breaches even outside times of widespread stress but a pattern of repeated breaches should be avoided.

7 Specific calculation issues

7.1 Alternative standard

7.1.1 The proposed, optional, alternative standard would dispense with the 25% of projected outflow requirement to the extent that projected inflows relate to group-banks; HQLA would be required only to exceed projected outflows

minus (1) projected inflows from group banks and (2) other projected inflows up to 75% of projected outflows. But this has three consequences, two non-substantive and one more significant, which it is proposed to address as follows:

- It needs to be clearly distinguished from the LCR based proposal and hence it is referred to herein as the CD Liquidity Mismatch Ratio or "**CDLMR**", with the LCR based proposal referred to as the CD liquidity coverage ratio or "**CDLCR**";
- The LCR formulation - CDLCR = HQLA / (Projected outflows – Projected inflows) - does not work if the denominator can be zero or negative, as is the case if projected inflows are permitted to fully offset projected outflows. It is therefore proposed to state that the CDLMR = (HQLA plus projected inflows) / Projected outflows; and require that the CDLMR exceeds 100%;
- As per **paragraph 5.8.4**, projected inflows would only be recognised in the CDLMR where: (1) they are expected within one week or (2) they reduce projected outflows that are expected at a later date within the 30-day CDLMR period (i.e. not any inflows projected to arise later in the month than projected outflows).

7.1.2 It is proposed that banks would be required to use the CDLCR (default) or seek approval to use the CDLMR. Permission would depend on an assessment of specific circumstances, including the extent to which the bank's internal management of liquidity, as set out in its Liquidity Management Policy ("**LMP")**, relied on projected inflows as opposed to HQLA.

7.1.3 Full details of the proposed CDLMR are set out in **Appendix C.**

Question 4 ***Do you consider that the proposals set out in Appendix C for an alternative approach, as an option for banks that rely on inflows from group banks, would be appropriate for groups where HQLA is held centrally? Are there any changes that you consider should be made to improve the functioning of the alternative? Do you have any views on the proposal that banks should seek approval for the approach to be used, rather than both approaches being available to all banks in all circumstances?***

7.2 Five further issues are addressed in detail in **Appendix C**:

7.2.1 Avoidance of double counting.

7.2.2 **Bank's own assessment of liquidity requirements:** The proposals set out herein are intended to create a minimum requirement for all banks in the CDs (outside of periods of stress). A bank would be expected to also meet any limits it establishes in its own LMP. In particular, where it is prudent, banks should use higher projected outflow rates and lower projected inflow rates.

7.2.3 **Severity:** It is proposed to incorporate the stress assumptions in the LCR, including no mismatch being allowed to one month.

7.2.4 **Consolidated vs solo**: For local banks, it is considered that the solo position of a bank is the most important at times of stress. However, it may be considered necessary, on a case-by-case basis, to also consider the consolidated position but only where the CD bank has significant deposit-taking subsidiaries. In these cases, it is proposed to require that the consolidated position of the bank be subject to the same rules and reporting requirements as for the solo position.

7.2.5 **Currency:** It is proposed that the limit should be reported in a single currency. However, banks are expected to be able to meet their liquidity needs in each currency and maintain HQLA consistent with the distribution of their liquidity needs by currency.

Question 5 ***Do you consider that the proposals set out in Appendix C would give rise to particular operational issues for your bank? If so, please describe the issues and provide a counter-proposal that you consider would appropriately address these.***

8 Transition

8.1 During the transitional period, i.e. before 2019, the LCR allows banks to only hold a proportion of the HQLA required by the calculation, specifically:

Minimum LCR	1 January 2015	1 January 2016	1 January 2017	1 January 2018	1 January 2019
	60%	70%	80%	90%	100%

8.2 There does not appear to be any benefit locally from the added complexity of such a phased approach and an extended period during which both current and new reporting methods would apply is operationally complex and might lead to confusion.

8.3 Instead, the proposal is to introduce the new approach by the end of 2018 (at 100%), with compliance being required from a fixed date, announced one year or more in advance. The exact timing of this switch would be decided by the local supervisor, in order to allow for practicalities such as the development of revised reporting systems. In keeping with this approach, any parallel running or dual reporting will be decided by the local supervisor.

Question 6 ***Do you consider that a transitional approach is appropriate? Are there any particular measures that would ease transition?***

LIQUID ASSETS

9 Liquid assets – overview

9.1 Current liquidity rules in the CDs permit banks to recognise the marketability of assets. In practice, usage has been limited and this was reflected in feedback to the Basel III DP. In light of limited experience regarding the issues surrounding marketability, it is considered that divergence from the principles of the LCR is not justifiable in this area, both for the CDLCR and the CDLMR.

9.2 The following proposals regarding HQLA are based on those set out in paragraphs 24 to 54 of the LCR. **Appendix O** addresses problems that arise where a jurisdiction has a shortage of qualifying assets (relevant for banks that have branches, outside the CDs, in jurisdictions where this is the case).

9.3 There are two categories of assets that can be included in the stock of HQLA. Assets can be included in each category if the bank is holding them on the reporting date, irrespective of their residual maturity. "Level 1" assets can be included without limit, while "Level 2" assets can only comprise up to 40% of the stock.

9.4 Within Level 2, there is an additional class of assets - Level 2B assets (see **Section 14**). These assets can comprise no more than 15% of the total stock of HQLA. They must also be included within the overall 40% cap on Level 2 assets.

9.5 The 40% cap on Level 2 assets and the 15% cap on Level 2B assets should be determined after the application of required haircuts, and after taking into account the unwinding of short-term securities financing transactions and collateral swap transactions maturing within 30 calendar days that involve the exchange of HQLA.

9.6 Details of the calculation methodology for the application of caps are provided in **Appendix H**.

10 General requirements

10.1 Assets are considered to be HQLA if they can be easily and immediately converted into cash and at little or no loss of value. The liquidity of an asset depends on the underlying stress scenario, the volume to be monetised and the timeframe considered. There are certain assets that are more likely to generate funds (through an outright sale or a repo transaction) at or near face value even in times of stress.

10.2 **Appendix D** sets out the factors that influence whether or not the market for an asset can be relied upon to raise liquidity when considered in the context of possible stresses. Banks will be required to exclude potential HQLA items that do not have the requisite characteristics, even if they meet other criteria. These are based on the LCR.

Question 7 ***Are the general requirements set out in Appendix D clear? Are there any specific circumstances that you feel should be taken into account? If so, please outline the issues and any alternative proposals that you feel would address them.***

11 Operational requirements

11.1 All HQLAs are subject to the operational requirements set out in **Appendix E**. The purpose of the operational requirements is to recognise that not all assets outlined in **Sections 13** and **14**, i.e. that meet the asset class, risk-weighting and credit-rating criteria, should be eligible for the stock, because there are other operational restrictions that can prevent timely monetisation during a stress period.

11.2 These operational requirements are designed to ensure that the stock of HQLA is managed in such a way that the bank can, and is able to demonstrate that it can, immediately use the stock of assets as a source of contingent funds that is available for the bank to convert into cash through outright sale or repo, to fill funding gaps between cash inflows and outflows at any time during the 30-day stress period, with no restriction on the use of the liquidity generated.

11.3 The requirements are set out in **Appendix E** and are based on the LCR, except for two additional requirements separately identified in **sub-section E.4**, concerning HQLA held outside of the trading book:

11.3.1 HQLA held on an accruals basis can only be included to the extent that a deep and liquid repo market exists and must be valued (for this purpose) at the repo-value. This limits the risk that the sale of an asset leads directly or indirectly to an impact on capital adequacy due to the resulting realisation of losses; and

11.3.2 The bank must establish a robust daily process to determine the repo-value. This limits the risk that market conditions change, with counterparties refusing to accept the assets or requiring higher haircuts, reducing the repo-value.

Question 8 Are the operational requirements set out in Appendix E clear?

Question 9 Are there any specific circumstances that you feel should be taken into account? If so, please outline the issues and any alternative proposals that you feel would address them.

12 Diversification

12.1 The stock of HQLA should be well diversified across asset classes and within each. Although some asset classes are more likely to remain liquid irrespective of circumstances, it is not possible to know with certainty which ones will. It is therefore proposed that banks be required to develop policies and put appropriate limits in place in order to avoid concentration of asset and issuer types and currencies (consistent with the distribution of net cash outflows by currency) within asset classes. To evidence this, it is proposed that it be documented in each bank's LMP.

12.2 With respect to issuer risk, higher levels of concentration should only be permitted for:

12.2.1 sovereign debt issued by a jurisdiction in which the bank operates or where its group is headquartered;

12.2.2 accounts held with central banks; and

12.2.3 central bank debt securities.

Question 10 ***Do you anticipate any issues for your business arising from the need to develop policies and limits to ensure that HQLA is appropriately diversified?***

13 Level 1 HQLA

13.1 Level 1 assets can comprise an unlimited share of the pool. They should be measured at their current realisable value and are not subject to a regulatory haircut.

13.2 **Realisable value:** The proposed definition of realisable value for the purpose of determining the value of HQLA is the highest value for which the asset can be realised, being either of:

13.2.1 repo value (only assets for which a deep and active repo market exists): the maximum amount that would be received under a repo, applying prevailing market values and haircuts; and

13.2.2 sale value: the current bid-price of the asset.

13.3 It is proposed to use the definitions set out in the LCR, which are shown in **Appendix F**.

Question 11 ***Do you envisage holding Level 1 HQLA (as would be required under the CDLCR, as opposed to seeking approval to follow the CDLMR approach)? If so, would the definition of realisable value pose any issues and, if so, are there any specific changes that you would like to see that would address these?***

14 Level 2 HQLA

14.1 Level 2 assets (comprising Level 2A and Level 2B assets) can be included in the stock of HQLA, subject to the requirement that they comprise no more than 40% of the overall stock after haircuts have been applied. It is proposed to use the definitions set out in the LCR, which are shown in **Appendix G**. The methodology for calculating the caps on Level 2 and Level 2B assets respectively are set out in full in **Appendix H**.

Question 12 ***Do you envisage holding Level 2 HQLA? If so, would the definition of realisable value pose any issues and, if so, are there any specific changes that you would like to see that would address these?***

INFLOWS

15 Overview

15.1 When considering its available cash inflows, the bank should only include contractual inflows (including interest payments) from outstanding exposures that are fully performing and for which the bank has no reason to expect a default within the 30 day time horizon. Contingent inflows are not included.

15.2 Banks need to monitor the concentration of expected inflows in order to ensure that their liquidity position is not overly dependent on the arrival of expected inflows from one or a limited number of counterparties.

15.3 Under the CDLCR, and as set out in the LCR, there would be a cap on the recognition of projected inflows, being a maximum 75% of projected outflows.

15.4 Under the alternative CDLMR, the 75% limit would only apply to inflows that were not from group banks. However, projected inflows from group banks would only be recognised if they occur within one week (i.e. flows can be mismatched within one week, as per the current CD rules) or to the extent that they meet concurrent or later dated projected outflows.

15.5 The detailed rules regarding the treatment of different classes of inflows set out below follow those in the LCR. In places, these are significantly different to current CD rules and the reasons for this are explained.

15.6 Inflows may be excluded by a bank if the effort required to compute them on an accurate reliable basis is considered to outweigh the benefit of including them (a conservative approach). Such exclusions should be documented in its LMP.

Question 13 Do you have any concerns regarding the general treatment of inflows? If so, please detail these and outline a suggested alternative.

16 Reverse repos, securities borrowing and margin lending

16.1 It is proposed that a bank should assume that maturing reverse repurchase or securities borrowing agreements secured by Level 1 assets will be rolled-over and will not give rise to any cash inflows (0%).

16.2 However, banks may assume that maturing reverse repurchase or securities lending agreements secured by Level 2 HQLA will not roll-over. A cash inflow can therefore be recognised on the maturity date equal to the maturity amount less the amount recognised in HQLA (as this amount has already been accounted for). In practice, this is usually similar to the maturing amount multiplied by the relevant haircut for the specific assets.

16.3 Similarly, banks may assume no roll-over of maturing reverse repurchase or securities borrowing agreements secured by non-HQLA assets, and can assume receipt of 100% of the cash related to those agreements.

16.4 It is proposed that collateralised loans extended to customers for the purpose of taking leveraged trading positions (margin loans) should be treated similarly where the loan is made against HQLA assets. However, banks may recognise no more than 50% of

contractual inflows from maturing margin loans made against non-HQLA collateral. This treatment is in line with the assumptions outlined for secured funding in the outflows section.

16.5 As an exception to the above, if the collateral obtained is re-used (i.e. re-hypothecated), then no inflow should be recognised. See **Appendix I** for full details.

16.6 Despite the roll-over assumptions set out above, a bank should manage its collateral such that it is able to fulfil obligations to return collateral whenever the counterparty decides not to roll-over any reverse repo or securities lending transaction. This is particularly the case for non-HQLA collateral, since such outflows are not captured in the LCR framework. The bank's LMP should document its policy in this respect.

Question 14 Is the proposed treatment of reverse repos, securities borrowing and margin lending clear? Do you anticipate any issues arising due to the treatment?

17 Facilities: committed and uncommitted

17.1 No credit facilities, liquidity facilities or other contingent funding facilities that the bank holds at other institutions for its own purposes can be assumed to be able to be drawn. Such facilities receive a 0% inflow rate, meaning that the LCR does not consider inflows from committed credit or liquidity facilities.

17.2 This represents a significant change to the current rules in the CDs. The LCR states that:

17.2.1 "*This is to reduce the contagion risk of liquidity shortages at one bank causing shortages at other banks and to reflect the risk that other banks may not be in a position to honour credit facilities, or may decide to incur the legal and reputational risk involved in not honouring the commitment, in order to conserve their own liquidity or reduce their exposure to that bank*."

17.3 It expected that a bank would draw on committed lines in advance of stressed conditions deteriorating to the point that it no longer became sensible to rely on them. This change reduces the likelihood that emergency action might become necessary as stressed conditions develop.

17.4 This is considered to be prudent and is only expected to have a modest and manageable impact on a small number of banks, since few rely to any significant extent on committed facilities.

17.5 In the case of group facilities, a group counterparty would be more likely to want to honour its commitment but in the LCR scenario (i.e. in circumstances where the banking group faces both a market-wide stress and a group specific stress, including a three notch downgrade) the need to conserve liquidity might trigger regulatory action to block payments or the group counterparty needing to prioritise the repayment of debt (where a default would lead to its collapse) over payments under a committed facility (where the failure to extend a loan could lead to it being sued for damages but would not be a trigger for cross-default clauses or insolvency).

Question 15 Are there any facilities that you consider should be capable of being relied upon? If so, please outline how the concerns expressed by the Basel Committee regarding reliability could be addressed.

18 Lending related inflows

18.1 For all other types of lending transactions, either secured or unsecured, the inflow rate will be determined by counterparty. In order to reflect the need for a bank to conduct ongoing loan origination/roll-over with different types of counterparties, even during a time of stress, a set of limits on contractual inflows by counterparty type is applied.

18.2 When considering loan repayments, the bank should only include inflows from fully performing loans. Inflows should only be allowed for at the latest possible date, based on the contractual rights available to counterparties. For revolving credit facilities, it should be assumed that the existing drawn element is rolled over and that any remaining facility is treated in the same way as a committed loan facility (see **Section 27**).

18.3 Inflows from loans that have no specific maturity should not be included; therefore, no assumptions should be applied as to when maturity of such loans would occur. Similarly, where a contract provides for "on-demand" repayment, such as now sometimes seen with mortgage lending, it is proposed not to allow this to be assumed. In both cases, it is considered that exercise in a stress scenario would be problematic, as (1) it could trigger concerns regarding the bank's health, (2) customers might well not be able to repay quickly and (3) the realisation of collateral within relevant (i.e. less than 30 days) timeframes cannot be relied upon in such stressed circumstances, if at all.

18.4 Two exceptions are proposed:

18.4.1 minimum payments of principal, fee or interest associated with an open maturity loan, to the extent that such payments are contractually due within 30 days. These minimum payment amounts should be captured as inflows at the rates prescribed in **paragraphs 18.5.1** and **18.5.2**; and

18.4.2 call accounts with banks (including central banks), where the full amount may be included.

18.5 The amount of the inflow that can be recognised depends on the nature of the counterparty, as follows:

18.5.1 **Retail and small business customer inflows.** The LCR scenario assumes that banks will receive all payments (including interest payments and instalments) from retail and small business customers that are fully performing and contractually due within a 30 day horizon. At the same time, however, banks are assumed to continue to extend loans to retail and small business customers, at a rate of 50% of contractual inflows. This results in a net recognised inflow of 50% of the contractual amount.

18.5.2 **Other (wholesale) inflows.** The LCR scenario assumes that banks will receive all payments (including interest payments and instalments) from wholesale customers that are fully performing and contractually due within the 30 day horizon. In addition, banks are assumed to continue to extend loans to wholesale clients, at a rate of 0% of inflows for financial institutions and central banks, and 50% for all others, including non-financial corporates, sovereigns, multilateral development banks, and PSEs. This will result in a net recognised inflow percentage of:

- 100% for financial institution and central bank counterparties; and
- 50% for non-financial wholesale counterparties.

18.6 This represents a significant change to current rules in the CDs, which permit 100% of inflows to be recognised. Whilst the change might be overly prudent in normal times, it addresses both (1) the likely need to maintain some level of activity to maintain confidence and (2) the risk that, in times of stress, even performing inflows may be subject to delays in payment.

Question 16 Please outline any specific circumstances (if any) where you consider a case can be made for applying a higher (or lower) rate than the 50% net rate established for loans from retail and non-financial wholesale counterparties in the LCR.

18.7 Inflows from securities maturing within 30 days **not included in the stock of HQLA** should be treated in the same category as inflows from financial institutions (i.e. 100% inflow). Banks may also recognise in this category inflows from the release of balances held in segregated accounts in accordance with regulatory requirements for the protection of customer trading assets, provided that these segregated balances are maintained in HQLA. This inflow should be calculated in line with the general treatment of inflows from that counterparty. Level 1 and Level 2 securities maturing within 30 days can be included in the stock of liquid assets, provided that they meet the relevant general, operational and specific requirements, as laid out in **Sections 10** to **14**.

18.8 **Operational deposits:** Deposits held at other financial institutions for operational purposes, as outlined in **Section 24**, such as for clearing, custody, and cash management purposes, are assumed to stay at those institutions, and no inflows can be counted for these funds – i.e. they will receive a 0% inflow rate.

19 Other cash inflows

19.1 **Cash inflows from derivatives:** the sum of all net contractual cash inflows should receive a 100% inflow factor. The amounts of derivatives linked cash inflows and outflows should be calculated in accordance with the methodology described in **Appendix M, sub-section M.1**.

19.2 Where derivatives are collateralised by HQLA, cash inflows should be calculated net of any corresponding cash or contractual collateral outflows that would result from contractual obligations for cash or collateral to be posted by the bank. This is in accordance with the principle that banks should not double-count liquidity inflows or outflows.

19.3 **Other contractual cash inflows:** Cash inflows related to non-financial revenues are not ordinarily taken into account in the calculation of the net cash inflows for the purposes of this standard. Where a bank wishes to include other contractual cash inflows, it should discuss the treatment with its supervisor, providing full details.

OUTFLOWS

20 Overview

20.1 Unless otherwise stated, outflows must be assessed on a contractual basis. That is to say that outflows must be reflected as the outflow amount, as per the contractually due date, after applying any adjustments, as set out in the relevant sections below.

20.2 For both the CDLCR and the CDLMR, banks must be able to categorise the projected outflows by maturity. For the CDLCR calculation, the requirement is to include those flows that would occur within one month. For the CDLMR a detailed breakdown is required by date, so that it can be determined whether the more detailed rules regarding inflows eligibility are met.

20.3 Projected outflows must include interest that is expected to be paid. Prudent estimations will be allowed of the amount due within the period, subject to initial supervisory notification of the methodology and ongoing documentation within the LMP.

21 Retail

21.1 General

21.1.1 Retail deposits are defined as deposits placed with a bank by a natural person. Deposits from legal entities, sole proprietorships or partnerships are captured in wholesale deposit categories. Retail deposits subject to the LCR include both demand deposits and term deposits.

21.1.2 Retail deposits are divided into various categories, with different treatments for each category.

21.1.3 The proposals in this section and **Appendix J**, which addresses specific issues, are in line with the LCR.

Question 17 ***Do you consider that the proposals set out in Section 21 (and Appendix J) strike a reasonable balance? Are there alternatives that you believe should be considered?***

21.2 Stable deposits

21.2.1 The LCR states that "stable deposits" comprise deposits that are:

- *"… fully insured by an effective deposit insurance scheme or by a public guarantee that provides equivalent protection and where:*
  - *the depositors have other established relationships with the bank that make deposit withdrawal highly unlikely; or*
  - *the deposits are in transactional accounts (e.g. accounts where salaries are automatically deposited)."*

21.2.2 "Effective deposit insurance scheme" is defined in the LCR, in accordance with the following:

- *"A scheme:*

  i. that guarantees that it has the ability to make prompt payouts,

  ii. for which the coverage is clearly defined and

  iii. of which public awareness is high.

- *The deposit insurer in an effective deposit insurance scheme has formal legal powers to fulfil its mandate and is operationally independent, transparent and accountable. A jurisdiction with an explicit and legally binding sovereign deposit guarantee that effectively functions as deposit insurance can be regarded as having an effective deposit insurance scheme.*
- *The presence of deposit insurance alone is not sufficient to consider a deposit "stable"."*

21.2.3 Tri-Party Group considers that the criteria established in **21.2.1** and **21.2.2** are not fully met in any jurisdictions. A compromise is therefore proposed to permit fully covered deposits to be treated as "stable", reflecting evidence that such deposits are the most stable class", rather than (as per the LCR) permitting the covered element of larger retail deposits to be treated as stable. Hence the proposed criteria are:

- the deposit is taken in either a CD head office / branch, an EU branch (of a CD incorporated bank) or a branch (of a CD incorporated bank) in a jurisdiction where its CD supervisor has agreed that an equivalent DCS scheme exists;
- the balance deposited by the customer is less than the compensation limit of the appropriate scheme; and
- the deposit either (1) is on demand or (2) has an original maturity of one week or less (and hence can be considered to be transactional).

21.2.4 It is proposed that, for such deposits, 5% of the total balance should be treated as an outflow. This is closely aligned to the LCR. It is considered that this outflow rate, although low compared to typical current CD outflow rates, is appropriate as it is in line with international standards developed post the financial crisis by jurisdictions where relevant data was available.

21.2.5 If a bank is not able to readily identify which retail deposits would qualify as "stable" according to the above definition (e.g. the bank cannot determine which deposits are covered by an effective deposit insurance scheme), it should place the full amount in the "less stable" buckets (see **sub-section 21.3** below).

21.2.6 The LCR permits a lower outflow percentage (3%) to be applied where deposit compensation coverage meets certain additional criteria[6] but it is considered that these are not fully met.

21.2.7 The CD supervisors will retain the right to require that a higher percentage be assumed as an outflow where there is evidence that deposits are less sticky. This might be as a result of individual bank data reflecting this or as a result of analysis of movements seen across banks, as set out in **sub-section C.3** of **Appendix C.** Banks should increase the rates used as they consider appropriate.

21.3 **Less stable retail deposits and other issues**

21.3.1 The LCR establishes a minimum run-off rate applicable to less stable retail deposits of 10%.

21.3.2 Banks will be required to classify deposits and determine appropriate outflow rates, in cases where they consider the minimum rate to be insufficiently conservative. Detailed proposals, together with consideration of issues around fixed and notice accounts, are set out in **Appendix J**.

21.3.3 The CD supervisors will retain the right to require that a higher number be assumed as an outflow where there is evidence that deposits are less sticky. This might be as a result of individual bank data reflecting this or as a result of analysis of movements seen across banks, as set out in **sub-section C.3** of **Appendix C.** Banks should increase the rates used as they consider appropriate.

22 Unsecured wholesale funding (deposits) from small businesses

22.1 Unsecured wholesale funding provided by small business customers is treated in the same way as retail deposits for the purposes of this standard, distinguishing between a "stable" portion of funding provided by small business customers and different buckets of less stable funding. Currently, no such funding can be considered stable in Jersey or Guernsey as local DCSs do not cover small businesses. In the Isle of Man, deposits lower than the limit for non-retail customers (£20,000) can be considered to be stable deposits (5% outflow). Otherwise, the same definitions and associated run-off factors apply as for less stable retail deposits.

22.2 This category consists of deposits from non-financial small business customers. “Small business customers” are all those that meet the rules for the definition of “retail” for

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[6] The additional criteria are:

- the insurance scheme is based on a system of prefunding via the periodic collection of levies on banks with insured deposits;
- the scheme has adequate means of ensuring ready access to additional funding in the event of a large call on its reserves, eg an explicit and legally binding guarantee from the government, or a standing authority to borrow from the government; and
- access to insured deposits is available to depositors in a short period of time once the deposit insurance scheme is triggered.

capital adequacy purposes, provided the total aggregated funding[7] raised from any one small business customer is less than €1 million (on a consolidated basis where applicable).

22.3 Term deposits from small business customers should be treated in accordance with the treatment for term retail deposits, as outlined in **Appendix J.**

23 Unsecured wholesale funding provided by non-financial corporates and sovereigns, central banks, multilateral development banks and PSEs

23.1 This category comprises all deposits and unsecured funding from non-financial corporate customers (that are not categorised as small business customers) and (both domestic and foreign) sovereign, central bank, multilateral development bank, and PSE customers that are not specifically held for operational purposes (as defined in **Section 24**). A run-off factor of 40% applies unless the criteria in **paragraph 23.3** are met.

23.2 It is proposed to permit PIC deposits to be included in this classification, provided that they meet the criteria established in **Appendix B.**

23.3 Unsecured wholesale funding provided by non-financial corporate customers, sovereigns, central banks, multilateral development banks and PSEs without operational relationships can receive a 20% run-off factor if the entire amount of the deposit is fully covered by an effective deposit insurance scheme. This would be unlikely to have any impact in Jersey or Guernsey (but is expected to have a small impact in the Isle of Man), but has been implemented so that if DCS coverage were provided/extended to a higher level, banks would benefit appropriately.

23.4 The CD supervisors will retain the right to require that a higher number be used where there is evidence that deposits are less sticky. This might be as a result of individual bank data or analysis of movements seen across banks, as set out in **sub-section C.3** of **Appendix C.** Banks should increase the rates used as they consider appropriate.

24 Operational deposits

24.1 General

24.1.1 Certain activities lead to financial and non-financial customers needing to place deposits with a bank in order to facilitate their access to payment and settlement systems. For a deposit to be classified as an operational deposit, the starting point is that the customer must have a substantive relationship with the bank.

24.1.2 The LCR establishes criteria which it is proposed to adopt, as set out in **Appendix K**.

[7] "Aggregated funding" means the gross amount (i.e. not netting any form of credit extended to the legal entity) of all forms of funding (eg deposits or debt securities or similar derivative exposure where the counterparty is known to be a small business customer). Applying the limit on a consolidated basis means that where one or more small business customers are affiliated with each other, they should be considered as a single creditor such that the limit is applied to the total funding received by the bank from this group of customers.

24.2 **Treatment**

24.2.1 It is proposed that operational deposits (all types) may be afforded the treatment proposed in the LCR. Hence, a minimum run-off factor of 25% would apply.

24.2.2 The portion of the operational deposits generated by clearing, custody and cash management activities that is fully covered by deposit insurance (if any) can receive the same treatment as "stable" retail deposits.

25 Unsecured wholesale funding provided by other legal entities

25.1 This category consists of all deposits and other funding from:

25.1.1 other institutions[8] (including banks, securities firms, insurance companies etc.);

25.1.2 fiduciaries[9];

25.1.3 beneficiaries[10];

25.1.4 conduits and special purpose vehicles;

25.1.5 affiliated entities of the bank; and

25.1.6 other entities,

that:

25.1.7 are not specifically held for operational purposes (as defined in Section **24**); or

25.1.8 do not meet the criteria set out in Sections **21** to **23**.

25.2 So, for example, deposits from fiduciaries that are not held for operational purposes and do not meet the definition of PIC deposits would fall within this category.

25.3 The run-off factor for these funds is 100%.

25.4 All notes, bonds and other debt securities issued by the bank (including structured products issued in bond form and short-term instruments such as certificates of deposit issued to customers) are included in this category regardless of the holder, unless the bond is sold exclusively in the retail market and held in retail accounts (including small business customer accounts treated as retail per **Section 22**), in which case the instruments can be treated in the appropriate retail or small business customer deposit

[8] An institution can be any type of organized corporation or society. It may be private and designed for the profit of the individuals composing it, or public and non-profit.

[9] "Fiduciary" is defined in this context as a legal entity that is authorised to manage assets on behalf of a third party. Fiduciaries include asset management entities such as pension funds and other collective investment vehicles.

[10] "Beneficiary" is defined in this context as a legal entity that receives, or may become eligible to receive, benefits under a will, insurance policy, retirement plan, annuity, trust, or other contract.

category. To be treated in this manner, it is not sufficient that the debt instruments are specifically designed and marketed to retail or small business customers. Rather, there should be limitations placed such that those instruments cannot be bought and held by parties other than retail or small business customers.

25.5 Customer cash balances arising from the provision of prime brokerage services should be considered separate from any required segregated balances related to client protection regimes imposed by national regulations, and should not be netted against other customer exposures included in this standard. These offsetting balances held in segregated accounts are treated as inflows only and should be excluded from the stock of HQLA.

26 Secured funding run-off

26.1 For the purposes of this standard, "secured funding" is defined as those liabilities and general obligations that are collateralised by legal rights over specifically designated assets owned by the borrowing institution in the event of bankruptcy, insolvency, liquidation or resolution.

26.2 It is proposed that, in line with the LCR, the assumption that the bank can continue to transact repurchase, reverse repurchase and other securities financing transactions is limited to transactions backed by HQLA. Collateral swaps should be treated as repurchase or reverse repurchase agreements, as should any other transaction with a similar form. Additionally, collateral lent to a bank's customers to effect short positions[11] should be treated as a form of secured funding. The bank should apply the following factors to all outstanding secured funding transactions with maturities within the 30 calendar day stress horizon, including customer short positions that do not have a specified contractual maturity. The amount of outflow is calculated based on the amount of funds raised through the transaction, and not the value of the underlying collateral.

26.3 Due to the high-quality of Level 1 assets, no reduction in funding availability against these assets is assumed to occur. Moreover, no reduction in funding availability is expected for any maturing secured funding transactions with the bank's domestic central bank. A reduction in funding availability will be assigned to maturing transactions backed by Level 2 assets equivalent to the required haircuts. A 25% factor is applied for transactions with the bank's domestic sovereign, multilateral development banks or domestic PSEs that have a 20% or lower risk weight, when the transactions are backed by assets other than Level 1 or Level 2A assets, in recognition that these entities are unlikely to withdraw secured funding from banks in a time of market-wide stress. This, however, gives credit only for outstanding secured funding transactions, and not for unused collateral or merely the capacity to borrow.

26.4 For all other maturing transactions the run-off factor is 100%, including transactions where a bank has satisfied customers' short positions with its own long inventory.

Question 18 ***Would the rules set out in Section 26 regarding secured funding have a significant impact on your bank? If so, please explain these and provide any suggested alternatives.***

27 Commitments

27.1 It is proposed to follow closely the treatment set out in the LCR, full details of this being set out in **Appendix L**.

27.2 In the case of committed lending facilities, this sets out fixed percentages. This differs to existing rules in the CDs. It is considered that adopting the LCR in this respect is

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[11] A customer short position in this context describes a transaction where a bank's customer sells a security it does not own, and the bank subsequently obtains the same security from internal or external sources to make delivery into the sale. Internal sources include the bank's own inventory of collateral as well as rehypothecatable collateral held in other customer margin accounts. External sources include collateral obtained through a securities borrowing, reverse repo, or like transaction.

appropriate; historically, the absence of local data made the establishment of appropriate factors problematic locally.

27.3 In the case of cancellable loan commitments and commitments that do not relate to lending, it is proposed to require banks to propose treatments individually or apply a rate of 100% except in the case of cancellable loan facilities, where the bank can apply the rate that would apply in the case of a committed loan facility.

27.4 This is intended to permit banks that have significant relevant activity to seek adjustments based on historical patterns that are appropriate for their customer bases without requiring banks with immaterial exposures to undertake such work. This is consistent with the LCR approach.

27.5 Although this treatment differs to that currently established locally, the impact is expected to be relatively small for most banks due to the low level of such facilities locally.

Question 19 ***Do you consider that the proposals set out in Appendix L would have a significant impact on your bank? If so, please explain why and provide any suggested alternatives.***

28 Derivatives and other outflows

28.1 **Appendix M** sets out, in line with the LCR, the proposed treatment of a variety of other funding aspects, of which perhaps only derivatives are likely to be relevant to most banks.

28.2 Any other contractual cash outflows not covered within any of the above sections or **Appendix M** must be captured fully, such as outflows to cover unsecured collateral borrowings, uncovered short positions, dividends or contractual interest payments, without adjustment.

28.3 In a departure from the LCR, outflows related to operating costs should be included, either according to projections or in accordance with an estimation method that is notified to the relevant supervisor in advance of use and documented in the bank's LMP. This reflects the fact that such payments would be unavoidable during a crisis.

28.4 Flows should reflect contractual terms, using an earliest case basis.

28.5 None of these proposals is believed to be significantly harsher than prevailing local rules.

Question 20 ***Do you consider that the proposals set out in Appendix M would have a significant impact on your bank? In particular, would the inclusion of operating cost outflows in the liquidity standard have a material impact on your institution or give rise to any concerns? If so, please explain why and provide any suggested alternatives.***

OTHER ISSUES

29 Cashflow projections

29.1 Many of the approaches documented herein rely, in part, on contractual cashflow projections. Three issues are addressed here:

29.1.1 **On-demand loans.** Where banks extend loans on terms that include the ability of the bank to demand immediate repayment, this should not be reflected unless the security is in the form of HQLA;

29.1.2 **Interest payments.** Interest payments should only be included on the date they are due. If banks cannot determine these cashflows, they should be excluded; and

29.1.3 **Impairments.** Inflows from impaired loans must be excluded. Where impairment is only identified at portfolio level, the impairment level should be applied pro-rata to all inflows relating to that portfolio.

30 Liquidity management and stress testing

30.1 This document is not intended to provide comprehensive guidance on liquidity management or stress testing. However, it is considered that for each stress testing scenario conducted by a bank, it should assess the impact on the regulatory ratio (the CDLCR or CDLMR) and in particular if a breach would occur.

30.2 More generally, banks should consider using the regulatory ratio as a metric for management purposes. For example, if banks currently set internal limits based on current liquidity mismatch approaches, it is expected that they should consider reformulating these limits to utilise the approach used for regulatory reporting. This does not mean that the regulatory ratio must be used as the only or primary metric; banks will remain free to develop liquidity metrics that are appropriate to their specific circumstances provided that they also monitor and report the regulatory ratio.

30.3 As noted in **Appendix C**, banks' stress testing plans should include assessing whether the inflow and outflow percentages are prudent.

30.4 As part of changes required to liquidity management in general, stress testing and supervisory practices, each CD supervisor will engage separately on changes to requirements. For example, the expectations on what should be contained in banks' LMPs, stress testing, contingency funding plans, monitoring and reporting, and frequency of regulatory assessments will be subject to review.

30.5 In due course, this might lead to the current behavioural adjustment processes applied in Jersey and the Isle of Man being developed into processes similar to the internal capital adequacy assessment ("**ICAAP**") and supervisory review and evaluation process ("**SREP**") used for capital adequacy assessments. Combining capital and liquidity assessments into one process will be considered. In Guernsey, liquidity stress testing is already reviewed as part of the SREP and the GFSC will consider setting minimum liquidity requirements at a higher level where necessary as a consequence of this review.

Question 21 ***Would the development of a common CD approach to stress testing requirements be useful?***

REPORTING AND MONITORING

31 Reporting and monitoring

31.1 Six groups of reports for monitoring of liquidity are proposed, covering:

31.1.1 Regulatory ratio (CDLCR and CDLMR versions);

31.1.2 CDLCR or CDLMR by significant currency;

31.1.3 Contractual maturity mismatch;

31.1.4 Net Stable Funding Ratio;

31.1.5 HQLA; and

31.1.6 Concentration of funding.

31.2 Of these, only the first and fourth are set out here in detail. For the remainder, a high level description of the proposal is provided. It is proposed that the Tri-Party Group would endeavour to align report formats and completion guidance. The drafts provided and guidance is intended to provide an indication only of the data elements that are likely to be required.

31.3 Branch reporting might, at some point, be aligned by replacing the various mismatch reports used with reports based on those for banks incorporated in the CDs. This alignment would be intended to ease reporting for branches of companies that have their head-office in the CDs and others where the home regulator has adopted Basel III.

Question 22 ***Does the approach to reporting set out in Section 31 give rise to any concerns? If so, please comment on specific measures that could be taken to alleviate these.***

Question 23 ***Are the reporting formats set out in Appendix N appropriately detailed? If not, please suggest additions (or deletions).***

31.4 **Regulatory ratio reporting (CDLCR or CDLMR)**

31.4.1 The LCR requires monthly reporting, with the ability to require more frequent reporting in times of stress.

31.4.2 Locally, it is proposed that:

- banks should calculate the ratio (CDLCR or CDLMR) daily;
- at quarter–end, a full regulatory ratio report will be required, as part of the prudential return. An outline of the proposed specifications is provided in **Appendix N**;
- in order to enable adequate internal monitoring and to facilitate more frequent regulatory reporting, if required in times of stress, banks should produce an internal report daily. This must be as detailed as the regulatory ratio report, except that categories may be omitted if no data exists; and

- on a quarterly basis, a summary (e.g. highest, lowest and average) of the ratios for days in the quarter will be required to be provided, within the prudential return.

31.5 CDLCR or CDLMR by significant currency reports

31.5.1 As noted in **C.6** of **Appendix C**, it is intended to also seek reports for the CDLCR or CDLMR in each significant currency.

31.5.2 These would be based on a slightly simplified version of the regulatory ratio report. Specifically:

- categories will be combined; but
- a separate category within derivative flows will be included, in order to allow flows relating to FX derivatives to be separately identified.

31.6 Contractual maturity mismatch report

31.6.1 In order to provide a full picture of all cashflows, reports will be required similarly to those currently used in the CDs but with categories revised to align with the categories proposed in the regulatory ratio report. Required time bands to be used in such a report will be determined but may be different from the current buckets used in the CDs.

31.7 Net Stable Funding Ratio report

31.7.1 The Basel Committee issued the Basel III NSFR standard in October 2014. As set out in **Section 4,** it is intended to develop a prudential report based on that standard. At this time, there is no intention to establish a minimum ratio or to require more frequent monitoring.

31.7.2 An outline of the proposed specification is provided in **Appendix N.**

31.8 HQLA reports

31.8.1 The Tri-Party Group intends to develop reports that provide sufficient detail on the make-up of HQLA to show to what extent assets are encumbered. At quarter–end, a full report will be required as part of the prudential return.

31.8.2 In order to enable adequate internal monitoring and in order to facilitate more frequent regulatory reporting, if required in times of stress, banks will be required to produce an internal report daily, in a similar format.

31.9 Concentration of funding reports

31.9.1 It is proposed to develop funding concentration reports, building on and replacing existing reports on large deposits, looking at:

- single name funding concentrations;
- linked concentrations; and
- inflow concentrations.

SUMMARY OF QUESTIONS

REFERENCE	PAGE	QUESTION
Question 1	10	Do you consider that the proposals for introducing the reporting of the NSFR are appropriate?
Question 2	13	Do you consider that the proposals regarding fiduciary deposits would, if enacted across the CDS and against a backdrop of similar proposals being established as an international standard, be likely to give rise to a loss of business or profitability? If so, are there appropriate additional measures that could mitigate the impact of these proposals, including those regarding the treatment of Swiss fiduciary deposits? If so, please outline them, together with a brief assessment of pros and cons and provide relevant evidence.
Question 3	14	Do you consider that there are appropriate additional measures to those outlined in **Section 5.8** and **5.9** that could mitigate the impact of these proposals? If so, please outline them, together with a brief assessment of pros and cons.
Question 4	15	Do you consider that the proposals set out in **Appendix C** for an alternative approach, as an option for banks that rely on inflows from group banks, would be appropriate for groups where HQLA is held centrally? Are there any changes that you consider should be made to improve the functioning of the alternative? Do you have any views on the proposal that banks should seek approval for the approach to be used, rather than both approaches being available to all banks in all circumstances?
Question 5	16	Do you consider that the proposals set out in **Appendix C** would give rise to particular operational issues for your bank? If so, please describe the issues and provide a counter-proposal that you consider would appropriately address these.
Question 6	17	Do you consider that a transitional approach is appropriate? Are there any particular measures that would ease transition?
Question 7	18	Are the general requirements set out in **Appendix D** clear? Are there any specific circumstances that you feel should be taken into account? If so, please outline the issues and any alternative proposals that you feel would address them.
Question 8	19	Are the operational requirements set out in **Appendix E** clear?
Question 9	19	Are there any specific circumstances that you feel should be taken into account? If so, please outline the issues and any alternative proposals that you feel would address them.
Question 10	20	Do you anticipate any issues for your business arising from the need to develop policies and limits to ensure that HQLA is appropriately diversified?
Question 11	20	Do you envisage holding Level 1 HQLA (as would be required under the CDLCR, as opposed to seeking approval to follow the CDLMR approach)? If so, would the definition of realisable value pose any issues and, if so, are there any specific changes that you would like to see that would address these?

REFERENCE	PAGE	QUESTION
Question 12	20	Do you envisage holding Level 2 HQLA? If so, would the definition of realisable value pose any issues and, if so, are there any specific changes that you would like to see that would address these?
Question 13	21	Do you have any concerns regarding the general treatment of inflows? If so, please detail these and outline a suggested alternative.
Question 14	22	Is the proposed treatment of reverse repos, securities borrowing and margin lending clear? Do you anticipate any issues arising due to the treatment?
Question 15	22	Are there any facilities that you consider should be capable of being relied upon? If so, please outline how the concerns expressed by the Basel Committee regarding reliability could be addressed.
Question 16	24	Please outline any specific circumstances (if any) where you consider a case can be made for applying a higher (or lower) rate than the 50% net rate established for loans from retail and non-financial wholesale counterparties in the LCR.
Question 17	25	Do you consider that the proposals set out in **Section 21** (and **Appendix J**) strike a reasonable balance? Are there alternatives that you believe should be considered?
Question 18	31	Would the rules set out in **Section 26** regarding secured funding have a significant impact on your bank? If so, please explain these and provide any suggested alternatives.
Question 19	32	Do you consider that the proposals set out in **Appendix L** would have a significant impact on your bank? If so, please explain why and provide any suggested alternatives.
Question 20	32	Do you consider that the proposals set out in **Appendix M** would have a significant impact on your bank? In particular, would the inclusion of operating cost outflows in the liquidity standard have a material impact on your institution or give rise to any concerns? If so, please explain why and provide any suggested alternatives.
Question 21	34	Would the development of a common CD approach to stress testing requirements be useful?
Question 22	35	Does the approach to reporting set out in **Section 31** give rise to any concerns? If so, please comment on specific measures that could be taken to alleviate these.
Question 23	35	Are the reporting formats set out in **Appendix N** appropriately detailed? If not, please suggest additions (or deletions).

APPENDICES

Appendix A List of bodies that have been sent this consultation paper

- Jersey Bankers' Association
- Jersey Finance Limited
- Association of Guernsey Banks
- Isle of Man Bankers' Association
- Isle of Man Government Department of Economic Development
- Banks incorporated in Jersey, Guernsey or the Isle of Man

Appendix B Fiduciary deposits – exercise of local discretion

B.1 Overview

B.1.1 The below establishes an outline proposal for the preferential treatment of fiduciary deposits.

B.2 PICs

B.2.1 Where a bank accepts a deposit from a PIC meeting the local definition it may, subject to three conditions being met, treat such PIC deposits as being from a non-financial customer. These would be treated like all other deposits from non-financial corporates (see **Section 23)**, and hence would attract an outflow rate of 40%.

B.2.2 The four conditions are:

- The PIC must meet the CD supervisor's definition. It is intended to base this on the definition set out in the LCR Delegated Act (see **paragraph 5.7.3**);
- Deposits must either (1) be held on a designated account (not pooled) and not be managed through a brokerage arrangement or (2) be placed by the PIC itself;
- The adjustment should only be applied to deposits where the choice of the bank is not actively managed in order to achieve an investment return. Banks will be expected to assess against criteria they establish and document in their LMPs. Deposits representing long-term investments, which must include all deposits placed with an original maturity exceeding three months, may not be adjusted; and
- Where the deposit is held on a designated account, the deposit mandate must either (1) not require the deposits to be moved in the event of a downgrade below a certain level or (2) in the case that it does require this, the bank must be more than three notches above that level.

Appendix C Specific calculation issues

C.1 CDLMR

C.1.1 The LCR limits the liquidity value accorded to inflows by imposing a ceiling on the extent to which they can be viewed as offsetting outflows. This is prudent as inflows may become less reliable in times of stress.

C.1.2 The Tri-Party Group considers that it is appropriate to limit the extent to which third party wholesale and retail inflows can be relied upon. However, there are circumstances where greater recognition of inflows is appropriate. The main example is where a local bank is part of a group that is subject to consolidated liquidity requirements similar to the LCR. An alternative approach, the CDLMR, is proposed which would permit greater recognition of inflows in such circumstances.

C.1.3 The three key areas considered here are:

- Source of inflows;
- Prudent treatment of inflows; and
- Appropriate monitoring by banks and reporting to supervisors.

C.1.4 **Source of inflows**: the CDLMR is intended for banks that rely to a significant extent on group bank inflows. Only inflows from these sources will be allowed to fully offset outflows. Inflows from other sources may not offset more than 75% of outflows, in keeping with the LCR.

C.1.5 This means that a bank must hold HQLA or have qualifying projected inflows from group banks that together total at least 25% of projected outflows i.e. analogous to the LCR.

C.1.6 **Prudent treatment of inflows:** The LCR allows projected outflows to be offset by later dated projected inflows, provided they occur within the one-month period. The US is understood to have identified this as an issue and has proposed to address it by bringing in rules that are stricter than Basel III:

- *"Covered companies … would be required to hold HQLA against their largest net cumulative cash outflow day within a 30-day liquidity stress period, rather than the net cumulative cash outflow as of the end of the period."*[12]

C.1.7 The US proposal is similar to the historic Bank of England "sterling stock liquidity" approach, whereby banks were required to hold liquidity sufficient to meet fixed percentages of retail deposit products and all of the highest net wholesale cumulative cash outflow arising on a contractual basis.

[12] http://www.federalreserve.gov/aboutthefed/boardmeetings/board-memo-lcr-20131024.pdf

C.1.8 It is intended to also address this issue in the CDLMR as follows:

- All projected inflows falling within one week will be recognised; and
- Later dated projected inflows will be recognised to the extent that there are equivalent amounts of later dated projected outflows.

C.1.9 This has the effect that:

- undated and sight to one week projected outflows would need to be met by a combination of projected inflows within one week and HQLA; and
- projected inflows for dates after one week will only be permitted to be included to the extent that they meet projected outflows that occur on the same day or at a later date.

C.1.10 **Appropriate monitoring by banks and reporting to supervisors**. It is proposed to formulate the CDLCR and CDLMR as follows:

- The CDLCR must exceed 100% and is calculated as HQLA / [projected outflows minus projected inflows[13]] and
- The CDLMR must exceed 100% and is calculated as [HQLA plus projected inflows[14])] / projected outflows.

C.1.11 As set out in **Section 31**, it is proposed to require banks to provide data on the contractual profile of inflows and outflows as well as projected inflows and outflows. In the case of banks using the CDLMR, it is proposed that such reporting should provide enough detail to evidence the correct application of the rules regarding permitted offsetting of flows.

C.2 Avoidance of double counting

C.2.1 Banks should not double count items. Specifically, if an asset is included as part of the “stock of HQLA” the associated cash inflows cannot also be counted as cash inflows. For example, coupons due on government bonds held as HQLA should be ignored. This is a simplifying assumption in the LCR – the haircuts and valuation rules for HQLA would need to be adjusted if coupons were to be included in projected inflows, since the realisable value of an asset includes value attributable to any coupons due.

C.2.2 Similarly, where there is the potential that an item could be counted in multiple outflow categories, a bank only has to assume up to the maximum contractual outflow for that product.

C.3 Bank’s own assessment of liquidity requirements

C.3.1 The LCR establishes a minimum level of liquidity for internationally active banks. The proposals set out herein are intended to create a minimum ratio that all banks in the CDs should adhere to (outside of periods of stress).

[13] Projected inflows will be subject to a 75% of projected outflows cap.
[14] Projected inflows, other than from group banks, will be subject to a 75% of projected outflows cap.

C.3.2 A bank would be expected to meet this standard as well as meeting any limits imposed by its own Liquidity Management Policy ("**LMP**"), which should itself be consistent with "Principles for Sound Liquidity Risk Management and Supervision" ("**Sound Principles**"), published by the Basel Committee in 2008, and any guidelines established by its supervisor.

C.3.3 Specifically, these proposals are not intended to address intraday liquidity management. As stated in Principle 8 of the Sound Principles, a bank should actively manage its intraday liquidity positions and risks to meet payment and settlement obligations on a timely basis under both normal and stressed conditions. Relevant policies and processes should be documented in each banks' LMP.

C.3.4 More generally, the Tri-Party Group considers that, where prudent, projected inflow rates should be decreased, outflow rates should be increased or the required CDLCR or CDLMR ratio should be increased (e.g. to a level above 100%). This reflects the LCR, which notes:

- "[para 6] *It should be stressed that the LCR standard establishes a minimum level of liquidity for internationally active banks. Banks are expected to meet this standard as well as adhere to the Sound Principles. Consistent with the Committee's capital adequacy standards, national authorities may require higher minimum levels of liquidity. In particular, supervisors should be mindful that the assumptions within the LCR may not capture all market conditions or all periods of stress. Supervisors are therefore free to require additional levels of liquidity to be held, if they deem the LCR does not adequately reflect the liquidity risks that their banks face."*

C.3.5 Current rules vary across the CDs and the proposals differ both to existing rules and to those in the LCR. The intent is to provide for variation, where prudent, whilst standardising the treatment where this is appropriate.

C.3.6 Specifically:

- Banks should assess the extent to which the outflow percentages set out here are appropriate. The outcome of reviews should be documented in LMPs.
- Where a bank considers a higher projected outflow to be appropriate for a class, these should be used in place of the minimum.
- CD Supervisors reserve the right to review bank assessments/data and determine higher outflow rates, lower inflow rates or a higher minimum CDLCR or CDLMR (e.g. above 100%), either on a bank-by-bank basis or on a wider basis, such as for all banks.

C.3.7 A short term metric is not, on its own, sufficient to measure all dimensions of a bank's liquidity profile. A set of monitoring tools is proposed in **Section 31** in respect of liquidity risk supervision, including the assessment of longer term liquidity risks. Banks would be expected to consider the use of similar monitoring tools for internal purposes, including NSFR reporting.

C.4 Severity

C.4.1 It is proposed to incorporate the assumptions in the LCR regarding the severity of the stress implicit in the LCR. In particular, no mismatch will be allowed (i.e. outflows must be met or exceeded by a combination of inflows and HQLA) and calibration will be based on the stressed conditions described in the LCR. As an example, it is proposed to adopt, almost unchanged, the rules regarding HQLA, in place of the less prescriptive current rules regarding marketable assets in use in the CDs.

C.5 Consolidated vs solo

C.5.1 For local banks, it is considered that the solo position of a CD bank is the most important at times of stress. This does not mean that surplus liquidity held in subsidiaries of the CD bank cannot be used to provide liquidity to it but does mean that the contractual relationship will be considered key in determining this. For example, if a subsidiary held £100m of cash it could lend that cash on a long-term (over one month) basis to the CD bank to invest in HQLA, which would boost the ratio, whereas if the cash was placed on a call account, it would not.

C.5.2 Conversely, if a subsidiary of a CD bank had a similar scale liquidity deficit, the CD bank could sell £100m of HQLA and lend the proceeds on a long-term (over one month) basis to the subsidiary to invest in HQLA, which would restore the subsidiary's ratio, whilst lowering the parent's ratio.

C.5.3 However, it may be considered necessary, on a case-by-case basis, to also consider the consolidated position where significant subsidiaries exist. This is most likely to be the case where the bank has one or more deposit-taking subsidiaries. In these cases, the proposal is to require that the measures also be applied to the consolidated position of the bank and those subsidiaries.

C.6 Currency

C.6.1 It is proposed that the requirements should be met in a single currency and a single currency report is proposed for this purpose. However, banks are expected to be able to meet their liquidity needs in each currency and maintain HQLA consistent with the distribution of their liquidity needs by currency.

C.6.2 The bank should be able to use the HQLA stock to generate liquidity in the currency and jurisdiction in which net cash outflows arise. As such, it is proposed that the liquidity requirement and liquidity held would be required to be monitored for significant currencies and reported quarterly to allow the bank and its supervisor to track any potential currency mismatch issues that could arise. Details of this are provided in **Section 31**.

C.6.3 Currency mismatches would not be subject to any general regulatory limit, though it is possible that circumstances could lead to limitations being agreed if warranted in times of particular stresses and firms should consider internal limits within their LMPs.

C.6.4 In managing foreign exchange liquidity risk, banks should take into account the risk that their ability to swap currencies and access the relevant foreign exchange markets may erode rapidly under stressed conditions. They should be aware that

sudden, adverse exchange rate movements could sharply widen existing mismatched positions and alter the effectiveness of any foreign exchange hedges in place.

Appendix D HQLA - general requirements

D.1 General requirements

D.1.1 Banks should assess assets and exclude any that, despite meeting the criteria set out in **Sections 11** and **12**, are not sufficiently liquid (setting aside liquidity provided by central banks or governments) to be included in the stock of HQLA. This assessment process must be described in a bank's LMP and should cover the following:

- Fundamental characteristics (see **sub-section D.2**); and
- Market-related characteristics (see **sub-section D.3**).

D.1.2 The test of whether liquid assets are of "high quality" is that, by way of sale or repo, their liquidity-generating capacity is assumed to remain intact even in periods of severe idiosyncratic and market stress.

D.1.3 HQLA should ideally be eligible at central banks for intraday liquidity needs and overnight liquidity facilities. Central banks can provide a further backstop to the supply of banking system liquidity under conditions of severe stress. Central bank eligibility should thus provide additional confidence that banks are holding assets that could be used in events of severe stress without damaging the broader financial system.

D.1.4 Banks that have direct access to central banks, including via overseas branches, should determine whether assets are eligible. Banks that do not have direct access should still carry out the work but only consider assets to be eligible if (1) the assets are eligible at a central bank via a group counterparty and (2) there is a tried and tested operational route to access funding from that central bank via that counterparty.

D.2 Fundamental characteristics

D.2.1 **Low credit risk:** assets that are less risky tend to have higher liquidity. High credit standing of the issuer and a low degree of subordination increase an asset's liquidity. Low duration, low legal risk, low inflation risk and denomination in a convertible currency with low foreign exchange risk all enhance an asset's liquidity.

D.2.2 **Ease and certainty of valuation:** an asset's liquidity is aided if market participants are likely to agree on its valuation. Assets with more standardised, homogenous and simple structures tend to be more fungible, promoting liquidity. The pricing formula of a high-quality liquid asset must be easy to calculate and not depend on strong assumptions. The inputs into the pricing formula must also be publicly available. In practice, this should rule out the inclusion of most structured or exotic products.

D.2.3 **Low correlation with risky assets**: the stock of HQLA should not be subject to wrong-way (highly correlated) risk. For example, assets issued by financial institutions are more likely to be illiquid in times of liquidity stress in the banking sector.

D.2.4 **Listed on a developed and recognised exchange:** being listed significantly aids an asset's transparency.

D.3 Market-related characteristics

D.3.1 **Active and sizable market:** the asset should have active outright sale or repo markets at all times. This means that:

- There should be historical evidence of market breadth and market depth. This could be demonstrated by low bid-ask spreads, high trading volumes, and a large and diverse number of market participants. Diversity of market participants reduces market concentration and increases the reliability of the liquidity in the market.
- There should be robust market infrastructure in place. The presence of multiple committed market makers increases liquidity as quotes will most likely be available for buying or selling HQLA.

D.3.2 **Low volatility:** assets whose prices remain relatively stable and are less prone to sharp price declines over time will have a lower probability of triggering forced sales to meet liquidity requirements. Volatility of traded prices and spreads are simple proxy measures of market volatility. There should be historical evidence of relative stability of market terms (eg prices and haircuts) and volumes during stressed periods.

D.3.3 **Flight to quality:** historically, the market has shown tendencies to move into these types of assets in a systemic crisis. The correlation between proxies of market liquidity and banking system stress is one simple measure that could be used.

Appendix E Operational requirements

E.1 General requirements

E.1.1 A bank should periodically monetise a representative proportion of its HQLAs through repo or outright sale, in order to test its access to the market, the effectiveness of its processes for monetisation, the availability of the assets, and to minimise the risk of negative signalling during a period of actual stress.

E.1.2 All assets in the stock should be unencumbered. "Unencumbered" means free of legal, regulatory[15], contractual or other restrictions on the ability of the bank to liquidate, sell, transfer, or assign the asset. An asset in the stock should not be pledged (either explicitly or implicitly) to secure, collateralise or credit-enhance any transaction, nor be designated to cover operational costs (such as rents and salaries). Assets received in reverse repo and securities financing transactions that are held at the bank, have not been rehypothecated and are legally and contractually available for the bank's use can be considered as part of the stock of HQLA. In addition, assets which qualify for the stock of HQLA that have been pre-positioned or deposited with, or pledged to, the central bank or a public sector entity (PSE) but have not been used to generate liquidity may be included in the stock.

E.1.3 A bank should exclude from the stock those assets that, although meeting the definition of "unencumbered" specified in **paragraph E.1.2**, the bank would not have the operational capability to monetise to meet outflows during the stress period. Operational capability to monetise assets requires having procedures and appropriate systems in place, including the function identified in **paragraph E.1.1**, with access to all necessary information to execute monetisation of any asset at any time. Monetisation of the asset must be executable, from an operational perspective, in the standard settlement period for the asset class in the relevant jurisdiction.

E.1.4 The stock should be under the control of the function charged with managing the liquidity of the bank (e.g. the treasurer), meaning the function has the continuous authority, and legal and operational capability, to monetise any asset in the stock. Control must be evidenced either by maintaining assets in a separate pool managed by the function with the sole purpose being use as a source of contingent funds, or by documenting in its LMP how it has and will verify from time to time that (1) the function can monetise the asset at any point in the 30-day stress period and (2) the proceeds of doing so are available to the function throughout the 30-day stress period, without directly conflicting with a stated business or risk management strategy. For example, an asset should not be included in the stock if the sale of that asset, without replacement throughout the 30-day period, would remove a hedge that would create an open risk position in excess of internal limits.

[15] Regulatory restrictions might include, for example, statutory minimum inventory requirements for entities that undertake market making.

E.1.5 A bank is permitted to hedge the market risk associated with ownership of the stock of HQLA and still include the assets in the stock. If it chooses to hedge the market risk, the bank should take into account (in the market value applied to each asset) the cash outflow that would arise if the hedge were to be closed out early (in the event of the asset being sold).

E.1.6 In accordance with Principle 9 of the Sound Principles, a bank "*should monitor the legal entity and physical location where collateral is held and how it may be mobilised in a timely manner*". Specifically, it should have a policy in place that identifies legal entities, geographical locations, currencies and specific custodial or bank accounts where HQLA are held. In addition, the bank should determine whether any such assets should be excluded for operational reasons and therefore, have the ability to determine the composition of its stock on a daily basis.

E.1.7 Banks should assess whether it has access to large, deep and active repo markets for each eligible asset class. Where this is not the case, assets can only be included if it is likely that they could be monetised through outright sale. In these circumstances, a bank should exclude from the stock of HQLA those assets where there are impediments to sale, such as large fire-sale discounts which would cause it to breach minimum solvency requirements, or any requirements to hold such assets, including, but not limited to, statutory minimum inventory requirements for market making.

E.1.8 In order to mitigate cliff effects that could arise if HQLA became ineligible (eg due to a rating downgrade), an asset remains eligible as HQLA for 30 calendar days from the date it fails to meet one or more criteria. This should allow the bank sufficient additional time to adjust its stock as needed or replace the asset.

E.2 Consolidated reporting

E.2.1 The following is only relevant to banks where consolidated reporting of the bank is required.

E.2.2 Qualifying HQLA that are held to meet statutory liquidity requirements at the legal entity or sub-consolidated level (where applicable) may be included in the stock at the consolidated level to the extent that the related risks (as measured by the legal entity's or sub-consolidated group's net cash outflows in the LCR) are also reflected in the consolidated LCR. Any surplus of HQLA held at the legal entity can only be included in the consolidated stock if those assets would also be freely available to the consolidated (parent) entity in times of stress.

E.2.3 In assessing whether assets are freely transferable for regulatory purposes, banks should be aware that assets might not be freely available to the consolidated entity due to regulatory, legal, tax, accounting or other impediments. Assets held in legal entities without market access should only be included in the HQLA calculation to the extent that they can be freely transferred to other entities that could monetise the assets.

E.3 Rehypothecated assets

E.3.1 Banks should not include in the stock of HQLA any assets, or related calculated liquidity generated by them that, they have received under right of rehypothecation, if the beneficial owner has the contractual right to withdraw those assets during the 30-day stress period.

E.3.2 Assets received as collateral for derivative transactions that are not segregated and are legally able to be rehypothecated may be included in the stock of HQLA provided that the bank records an appropriate outflow for the associated risks.

E.4 Proposed additional requirements

E.4.1 In order to minimise the risk that a sale creates a loss, assets must normally be held at fair value in order to be eligible. However, if a bank can demonstrate that a deep and active repo market exists, it may use an accruals basis for valuing assets in its financial statements but must compute the realisable value (see **paragraph 13.2**) using the repo value – i.e. disregarding the sale value.

E.4.2 For assets held in the banking book, the bank must put in place processes to ensure that it holds up to date information on bid prices and on repo haircuts applicable to assets that it wishes to designate as HQLA. Such information must be refreshed daily.

Appendix F Level 1 HQLA specification

F.1 Level 1 HQLA can consist of:

F.1.1 coins and banknotes;

F.1.2 central bank reserves (including required reserves), to the extent that the central bank policies allow them to be drawn down in times of stress;

F.1.3 marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs, the Bank for International Settlements, the International Monetary Fund, the European Central Bank and European Community, or multilateral development banks, and satisfying all of the following conditions:

- assigned a 0% risk-weight for capital adequacy purposes. In the case of sovereigns, central banks and PSEs, the relevant sovereign credit rating must be AA- or higher;
- traded in large, deep and active repo or cash markets characterised by a low level of concentration;
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions (i.e. maximum decline of price not exceeding 10% or increase in haircut not exceeding 10 percentage points over a 30-day period during a relevant period of significant liquidity stress);
- not an obligation of a financial institution or any of its affiliated entities. In practice, this means that securities issued by a financial institution would not qualify for the stock of HQLA, even where the issuance is government guaranteed;
- where the sovereign has a non-0% risk weight, sovereign or central bank debt securities issued in domestic currencies by the sovereign or central bank in the country in which the liquidity risk is being taken or in the bank's home country; and
- where the sovereign has a non-0% risk weight, domestic sovereign or central bank debt securities issued in foreign currencies are eligible up to the amount of the bank's stressed net cash outflows in that specific foreign currency stemming from the bank's operations in the jurisdiction where the bank's liquidity risk is being taken.

Appendix G Level 2 HQLA specification

G.1 General

G.1.1 It is proposed that Level 2 assets (comprising Level 2A and 2B assets) can be included in the stock of HQLA, subject to the requirement that they comprise no more than 40% of the overall stock after haircuts have been applied. The methodology for calculating the cap on Level 2 assets and the cap on Level 2B assets is set out in full in **Appendix H**, though most of the full detail will only be relevant where a bank uses HQLA as part of short-term securities financing transactions.

G.1.2 A 15% haircut is applied to the current realisable value (see **13.2**) of each Level 2A asset held in the stock of HQLA.

G.1.3 Level 2A assets are limited to the following:

- Marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs or multilateral development banks that satisfy all of the following conditions (and that are not eligible as Level 1 assets):
  - assigned a maximum 20% risk weight for capital adequacy purposes;
  - traded in large, deep and active repo or cash markets characterised by a low level of concentration;
  - have a proven record as a reliable source of liquidity (via repo or sale) even during stressed market conditions (i.e. maximum decline of price not exceeding 10% or increase in haircut not exceeding 10 percentage points over a 30-day period during a relevant period of significant liquidity stress); and
  - not an obligation of a financial institution or any of its affiliated entities. In practice, this means that securities issued by an affiliate of a financial institution would not qualify for the stock of HQLA, even where the issuance is government guaranteed.
- Corporate debt securities (including commercial paper) and covered bonds that satisfy all of the following conditions:
  - in the case of corporate debt securities: not issued by a financial institution or any of its affiliated entities;
  - in the case of covered bonds: not issued by the bank itself or any of its affiliated entities;
  - the relevant credit rating for capital adequacy purposes is at least AA-;
  - traded in large, deep and active repo or cash markets characterised by a low level of concentration; and
  - have a proven record as a reliable source of liquidity (via repo or sale) even during stressed market conditions (i.e. maximum decline of price or increase in haircut over a 30-day period during a relevant period of significant liquidity stress not exceeding 10%).

G.1.4 Certain additional assets (Level 2B assets) may be included in Level 2. A larger haircut is applied to the current realisable value (see **paragraph 13.2**) of each Level 2B asset held in the stock of HQLA. Level 2B assets are limited to the following:

- Residential mortgage backed securities ("**RMBS**") that satisfy all of the following conditions may be included in Level 2B, subject to a 25% haircut:
  - not issued by, and the underlying assets have not been originated by, the bank itself or any of its affiliated entities;
  - the relevant credit rating for capital adequacy purposes is at least AA;
  - traded in large, deep and active repo or cash markets characterised by a low level of concentration;
  - have a proven record as a reliable source of liquidity (via repo or sale) even during stressed market conditions (i.e. maximum decline of price or increase in haircut over a 30-day period during a relevant period of significant liquidity stress not exceeding 20%);
  - the underlying asset pool is restricted to residential mortgages and cannot contain structured products;
  - the underlying mortgages are "full recourse'' loans (i.e. in the case of foreclosure the mortgage owner remains liable for any shortfall in sales proceeds from the property) and have a maximum loan-to-value ratio (LTV) of 80% on average at issuance; and
  - the securitisations are subject to "risk retention" regulations which require issuers to retain an interest in the assets they securitise.
- Sovereign/Corporate debt securities (including commercial paper) that satisfy all of the following conditions may be included in Level 2B, subject to a 50% haircut:
  - not issued by a financial institution or any of its affiliated entities;
  - the relevant credit rating for capital adequacy purposes is at least BBB-;
  - traded in large, deep and active repo or cash markets characterised by a low level of concentration; and
  - have a proven record as a reliable source of liquidity (via repo or sale) even during stressed market conditions, i.e. a maximum decline of price not exceeding 20% or increase in haircut over a 30-day period not exceeding 20 percentage points during a relevant period of significant liquidity stress.
- Common equity shares that satisfy all of the following conditions may be included in Level 2B, subject to a 50% haircut:
  - not issued by a financial institution or any of its affiliated entities;
  - exchange traded and centrally cleared;
  - a constituent of the major stock index in the home jurisdiction or where the liquidity risk is taken, as decided by the supervisor in the jurisdiction where the index is located;

- denominated in the domestic currency of a bank’s home jurisdiction or in the currency of the jurisdiction where a bank’s liquidity risk is taken;
- traded in large, deep and active repo or cash markets characterised by a low level of concentration; and
- have a proven record as a relatively reliable source of liquidity (via repo or sale) even during stressed market conditions, i.e. a maximum decline of share price not exceeding 40% or increase in haircut not exceeding 40 percentage points over a 30-day period during a relevant period of significant liquidity stress.

Appendix H Calculation of the cap on Level 2 assets with regard to short-term securities financing transactions

H.1 Explanation

H.1.1 This annex seeks to clarify the appropriate method for the calculation of the cap on Level 2 (including Level 2B) assets with regard to short-term securities financing transactions.

H.1.2 As stated in **Section 9**, the calculation of the 40% cap on Level 2 assets should take into account the impact on the stock of HQLA of the amounts of Level 1 and Level 2 assets involved in secured funding, secured lending and collateral swap transactions maturing within 30 calendar days. The maximum amount of adjusted Level 2 assets in the stock of HQLA is equal to two-thirds of the adjusted amount of Level 1 assets after haircuts have been applied. The calculation of the 40% cap on Level 2 assets will take into account any reduction in eligible Level 2B assets on account of the 15% cap on Level 2B assets.

H.1.3 Further, the calculation of the 15% cap on Level 2B assets should take into account the impact on the stock of HQLA of the amounts of HQLA assets involved in secured funding, secured lending and collateral swap transactions maturing within 30 calendar days. The maximum amount of adjusted Level 2B assets in the stock of HQLA is equal to 15/85 of the sum of the adjusted amounts of Level 1 and Level 2 assets or, in cases where total Level 2 assets exceed 40% of Level 1 assets, up to a maximum of 1/4 of the adjusted amount of Level 1 assets, both after haircuts have been applied.

H.1.4 The adjusted amount of Level 1 assets is defined as the amount of Level 1 assets that would result after unwinding those short-term secured funding, secured lending and collateral swap transactions involving the exchange of any HQLA for any Level 1 assets (including cash) that meet, or would meet if held unencumbered, the operational requirements for HQLA set out in **Appendix E**.

H.1.5 The adjusted amount of Level 2A assets is defined as the amount of Level 2A assets that would result after unwinding those short-term secured funding, secured lending and collateral swap transactions involving the exchange of any HQLA for any Level 2A assets that meet, or would meet if held unencumbered, the operational requirements for HQLA set out in **Appendix E**.

H.1.6 The adjusted amount of Level 2B assets is defined as the amount of Level 2B assets that would result after unwinding those short-term secured funding, secured lending and collateral swap transactions involving the exchange of any HQLA for any Level 2B assets that meet, or would meet if held unencumbered, the operational requirements for HQLA set out in **Appendix E**.

H.1.7 In **paragraphs H.1.4** to **H.1.7**, short-term transactions are transactions with a maturity date up to and including 30 calendar days. Relevant haircuts should be applied prior to calculation of the respective caps.

H.2 Formula

H.2.1 The formula for the calculation of the stock of HQLA is as follows:

H.2.2 Stock of HQLA = Level 1 + Level 2A + Level 2B – Adjustment for 15% cap – Adjustment for 40% cap.

H.2.3 Where:

H.2.4 Adjustment for 15% cap = Higher of:

- Adjusted Level 2B – 15/85 * (Adjusted Level 1 + Adjusted Level 2A);
- Adjusted Level 2B - 1/4 * Adjusted Level 1; and
- 0.

H.2.5 Adjustment for 40% cap = Higher of:

- (Adjusted Level 2A + Adjusted Level 2B – Adjustment for 15% cap) – 2/3 * Adjusted Level 1 assets; and
- 0.

Appendix I Secured lending inflows

I.1 Treatment of inflows relating to short position

I.1.1 As an exception to the treatment set out in **Section 16**, if the collateral obtained through reverse repos, securities borrowing, or collateral swaps, which matures within the 30-day horizon, is re-used (i.e. rehypothecated) and is used to cover short positions that could be extended beyond 30 days, a bank should assume that such reverse repo or securities borrowing arrangements will be rolled-over and will not give rise to any cash inflows (0%), reflecting its need to continue to cover the short position or to re-purchase the relevant securities. Short positions include both instances where in its 'matched book' the bank sold short a security outright as part of a trading or hedging strategy and instances where the bank is short a security in the 'matched' repo book (i.e. it has borrowed a security for a given period and lent the security out for a longer period).

I.1.2 In the case of a bank's short positions, if the short position is being covered by an unsecured security borrowing, the bank should assume the unsecured security borrowing of collateral from financial market participants would run-off in full, leading to a 100% outflow of either cash or HQLA to secure the borrowing, or cash to close out the short position by buying back the security. This should be recorded as a 100% other contractual outflow. If, however, the bank's short position is being covered by a collateralised securities financing transaction, the bank should assume the short position will be maintained throughout the 30-day period and receive a 0% outflow.

Appendix J Specific issues regarding retail deposits

J.1 General approach

J.1.1 As established in **Appendix C**, **sub-section C.3**, the minimum projected outflow rate of 10% might be increased by banks or supervisors in circumstances where this is appropriate.

J.2 Less stable deposits – short-term approach

J.2.1 The first approach is designed for call and short term fixed deposits.

J.2.2 Banks should allocate deposits to one or more sub-classes, based on a combination of product type, size, interest rate and currency, which have similar liquidity characteristics.

J.2.3 For each class, the outflow rate should be determined as per **sub-section C.3.** The allocation should ensure that products are grouped with similar products, particularly in the case of new products. However, where a product is offered in a different currency or with a significantly different interest rate, the bank should consider allocating it separately if data evidences different liquidity characteristics.

J.2.4 The percentage used should be applied to the total recorded on the bank's balance sheet, including accrued interest, for each product.

J.3 Less stable deposits – long-term approach

J.3.1 The second approach is designed for longer-term fixed deposits.

J.3.2 Allocations should be decided as per **paragraph J.2.2** except that they may differ where maturity is significantly different.

J.3.3 The key difference is that these run-off rates are applied only to the amount contractually maturing within the period, rather than the full balance. The percentage used should therefore be applied to the balance maturing plus any interest due for each product.

J.4 Issues re fixed and notice accounts

J.4.1 Cash outflows related to retail term deposits with a residual maturity or withdrawal notice period of greater than 30 days will be excluded from total expected cash outflows if the depositor has no legal right to withdraw deposits within the 30-day horizon of the LCR, or if early withdrawal results in a significant penalty that is materially greater than the loss of interest.

J.4.2 If a portion of the term deposit can be withdrawn without incurring such a penalty only that portion should be treated as a demand deposit. The remaining balance of the deposit may be treated as a term deposit.

J.4.3 If notice is given on a deposit with a minimum withdrawal period, the amount impacted should be treated as an outflow on the date when the notice expires, without adjustment. The remainder is unaffected.

J.4.4 If a bank allows a depositor to withdraw fixed or notice deposits without applying the corresponding penalty or despite a clause that says the depositor has no legal right to withdraw, the entire category of these funds would then have to be treated as demand deposits (i.e. regardless of the remaining term). Banks may choose to outline exceptional circumstances that would qualify as hardship, under which the term deposit could exceptionally be withdrawn by the depositor without changing the treatment of the entire pool of deposits. This is subject to supervisory review and must be documented in a bank's LMP.

Appendix K Operational deposits: clearing, custody and cash management

K.1 Qualifying criteria

K.1.1 Activities in this context refer to clearing, custody and cash management activities that meet the following criteria:

- The customer is reliant on the bank to perform these services as an independent third party intermediary in order to fulfil its normal banking activities over the next 30 days;
- The services are provided under a legally binding agreement to institutional customers; and
- The termination of such agreements are subject either to a notice period of at least 30 days or significant switching costs (such as those related to transaction, information technology, early termination or legal costs) to be borne by the customer if the operational deposits are moved before 30 days.

K.1.2 Qualifying operational deposits generated by such an activity are ones where:

- The deposits are by-products of the underlying services provided by the banking organisation and not sought out in the wholesale market in the sole interest of offering interest income. Specifically, brokered deposits are excluded; or
- The deposits are held in specifically designated accounts (not pooled) and priced without giving an economic incentive to the customer (not limited to paying market interest rates) to leave any excess funds on these accounts. In the case that interest rates in a jurisdiction are close to zero, it would be expected that such accounts are non-interest bearing. Banks should be particularly aware that during prolonged periods of low interest rates, excess balances (as defined below) could be significant.

K.1.3 Banks must determine the methodology for identifying excess deposits that are excluded from this treatment. This assessment should be conducted at a sufficiently granular level to adequately assess the risk of withdrawal in an idiosyncratic stress. The methodology should take into account relevant factors such as the likelihood that wholesale customers have above average balances in advance of specific payment needs, and consider appropriate indicators (eg ratios of account balances to payment or settlement volumes or to assets under custody) to identify those customers that are not actively managing account balances efficiently.

K.1.4 Notwithstanding these operational categories, if the deposit under consideration arises out of correspondent banking or from the provision of prime brokerage services, it must be treated as if there were no operational activity for the purpose of determining run-off factors.

K.1.5 The following paragraphs describe the types of activities that may generate operational deposits. A bank should assess whether the presence of such an activity does indeed generate an operational deposit as not all such activities qualify due to differences in customer dependency, activity and practices:

- A clearing relationship, in this context, refers to a service arrangement that enables customers to transfer funds (or securities) indirectly through direct participants in domestic settlement systems to final recipients. Such services are limited to the following activities: transmission, reconciliation and confirmation of payment orders; daylight overdraft, overnight financing and maintenance of post-settlement balances; and determination of intra-day and final settlement positions;
- A custody relationship, in this context, refers to the provision of safekeeping, reporting, processing of assets or the facilitation of the operational and administrative elements of related activities on behalf of customers in the process of their transacting and retaining financial assets. Such services are limited to the settlement of securities transactions, the transfer of contractual payments, the processing of collateral, and the provision of custody related cash management services. Also included are the receipt of dividends and other income, client subscriptions and redemptions. Custodial services can furthermore extend to asset and corporate trust servicing, treasury, escrow, funds transfer, stock transfer and agency services, including payment and settlement services (excluding correspondent banking) and depository receipts; and
- A cash management relationship, in this context, refers to the provision of cash management and related services to customers. Cash management services, in this context, refers to those products and services provided to a customer to manage its cash flows, assets and liabilities, and conduct financial transactions necessary to the customer's ongoing operations. Such services are limited to payment remittance, collection and aggregation of funds, payroll administration and control over the disbursement of funds.

Appendix L Treatment of commitments

L.1 Drawdowns on committed credit and liquidity facilities

L.1.1 For the purpose of the standard, credit and liquidity facilities are defined as explicit contractual agreements or obligations to extend funds at a future date to retail or wholesale counterparties. For the purpose of the standard, these facilities only include contractually irrevocable (committed) or conditionally revocable agreements to extend funds in the future. Unconditionally revocable facilities that are unconditionally cancellable by the bank (in particular, those without a precondition of a material change in the credit condition of the borrower) are excluded from this section and included in "*Other contingent funding obligations*". These off-balance sheet facilities or funding commitments can have long or short-term maturities, with short-term facilities frequently renewing or automatically rolling-over. In a stressed environment, it may become difficult for customers drawing on facilities of any maturity, even short-term maturities, to be able to quickly pay back the borrowings. Therefore, for the purposes of this standard, all facilities that are assumed to be drawn (as outlined in the paragraphs below) will remain outstanding at the amounts assigned throughout the duration of the test, regardless of maturity.

L.1.2 For the purposes of this standard, the currently undrawn portion of these facilities is calculated net of any HQLA that has already been posted as collateral by a counterparty or that are contractually obliged to be posted when the counterparty draws down the facility (eg a liquidity facility structured as a repo facility), if the bank is legally entitled (and operationally capable) to re-use the collateral in new cash raising transactions once the facility is drawn, and there is no undue correlation between the probability of drawing the facility and the market value of the collateral. The collateral can be netted against the outstanding amount of the facility to the extent that this collateral is not already counted in the stock of HQLA, in line with the principle that items cannot be double-counted.

L.1.3 A liquidity facility is defined as any committed, undrawn credit facility that would be utilised to refinance the debt obligations of a customer in situations where the customer is unable to rollover that debt in financial markets (eg pursuant to a commercial paper programme, secured financing transactions or obligations to redeem units). For the purpose of this standard, the amount of the commitment to be treated as a liquidity facility is the amount of the currently outstanding debt issued by the customer (or proportionate share, if a syndicated facility) maturing within a 30 day period that is backstopped by the liquidity facility. The portion of a liquidity facility that is backing debt that does not mature within the 30-day window is excluded from the scope of the definition of a facility. Any additional capacity of the facility (i.e. the remaining commitment) would be treated as a committed credit facility with its associated drawdown rate. General working capital facilities for corporate entities (eg revolving credit facilities in place for general corporate or working capital purposes) will not be classified as liquidity facilities, but as credit facilities.

L.1.4 Notwithstanding the above, any facilities provided to hedge funds, money market funds and special purpose funding vehicles (for example a special purpose entity

or "**SPE**") or conduits, or other vehicles used to finance the bank's own assets, should be captured in their entirety as a liquidity facility to other legal entities.

L.1.5 For that portion of financing programs that are maturing or have liquidity puts that may be exercised in the 30-day horizon, banks that are providers of associated liquidity facilities do not need to double count the maturing financing instrument and the liquidity facility.

L.1.6 Any contractual loan drawdowns from committed facilities and estimated drawdowns from revocable facilities within the 30-day period should be fully reflected as outflows.

L.1.7 Committed credit and liquidity facilities to retail and small business customers: Banks should assume a 5% drawdown of the undrawn portion.

L.1.8 Committed credit facilities to non-financial corporates, sovereigns and central banks, PSEs and multilateral development banks: Banks should assume a 10% drawdown of the undrawn portion.

L.1.9 Committed liquidity facilities to non-financial corporates, sovereigns and central banks, PSEs, and multilateral development banks: Banks should assume a 30% drawdown of the undrawn portion.

L.1.10 Committed credit and liquidity facilities extended to banks subject to prudential supervision: Banks should assume a 40% drawdown of the undrawn portion of these facilities.

L.1.11 Committed credit facilities to other financial institutions, including securities firms, insurance companies, fiduciaries, and beneficiaries[16]: Banks should assume a 40% drawdown of the undrawn portion.

L.1.12 Committed liquidity facilities to other financial institutions, including securities firms, insurance companies, fiduciaries, and beneficiaries: Banks should assume a 100% drawdown of the undrawn portion.

L.1.13 Committed credit and liquidity facilities to other legal entities (including SPEs, conduits and special purpose vehicles, and other entities not included in the prior categories): Banks should assume a 100% drawdown of the undrawn portion.

L.2 Contractual obligations to extend funds within a 30-day period.

L.2.1 Any contractual lending obligations to financial institutions not captured elsewhere in this standard should be captured here at a 100% outflow rate.

L.2.2 If the total of all contractual obligations to extend funds to retail and non-financial corporate clients within the next 30 calendar days (not captured in the prior categories) exceeds 50% of the total contractual inflows due in the next 30

[16] As per footnote 9 in **Section 25**, "Beneficiary" is defined in this context as a legal entity that receives, or may become eligible to receive, benefits under a will, insurance policy, retirement plan, annuity, trust, or other contract.

calendar days from these clients, the difference should be reported as a 100% outflow.

L.3 Other contingent funding obligations

L.3.1 The local supervisor will work with banks in their jurisdictions to determine the liquidity risk impact of these contingent liabilities. The default outflow is 100%, unless otherwise stated. Floors are proposed here, broadly in line with the LCR.

L.3.2 These contingent funding obligations may be either contractual or non-contractual and are not pure lending commitments. Non-contractual contingent funding obligations include associations with, or sponsorship of, products sold or services provided that may require the support or extension of funds in the future under stressed conditions. Non-contractual obligations may be embedded in financial products and instruments sold, sponsored, or originated by the institution that can give rise to unplanned balance sheet growth arising from support given for reputational risk considerations. These include products and instruments for which the customer or holder has specific expectations regarding the liquidity and marketability of the product or instrument and for which failure to satisfy customer expectations in a commercially reasonable manner would likely cause material reputational damage to the institution or otherwise impair ongoing viability.

L.3.3 Some of these contingent funding obligations are explicitly contingent upon a credit or other event that is not always related to the liquidity events simulated in the stress scenario, but may nevertheless have the potential to cause significant liquidity drains in times of stress.

L.3.4 For this standard, each bank should consider which of these other contingent funding obligations may materialise under the assumed stress events. The potential liquidity exposures to these contingent funding obligations are to be treated as a nationally determined behavioural assumption where it is up to the supervisor to determine whether and to what extent these contingent outflows are to be included in the LCR. All identified contractual and non-contractual contingent liabilities and their assumptions should be reported, along with their related triggers. Banks should, at a minimum, use historical behaviour in determining appropriate outflows but would also be expected to consider the likely impact of a stress event.

L.3.5 Non contractual contingent funding obligations related to potential liquidity draws from joint ventures or minority investments, which are not consolidated, should be captured where there is the expectation that the bank will be the main liquidity provider when the entity is in need of liquidity.

L.3.6 In the case of contingent funding obligations stemming from trade finance instruments, the floor for the rate is 5%. Trade finance instruments consist of trade-related obligations directly underpinned by the movement of goods or the provision of services, such as:

- documentary trade letters of credit, documentary and clean collections, import bills, and export bills; and

 Issued: 7 JULY 2015

- guarantees directly related to trade finance obligations, such as shipping guarantees.

L.3.7 Lending commitments, such as direct import or export financing for non-financial corporate firms, are excluded from this treatment and banks will apply the draw-down rates specified in **sub-section L.1**.

L.3.8 Other contingent funding obligations for which run-off rates must be determined should include products and instruments such as:

- unconditionally revocable "uncommitted" credit and liquidity facilities (capped at the rate that would apply if the facility was fully committed, as per **sub-section L.1**);
- guarantees and letters of credit unrelated to trade finance obligations;
- non-contractual obligations such as:
  - potential requests for debt repurchases of the bank's own debt or that of related conduits, securities investment vehicles and other such financing facilities;
  - structured products where customers anticipate ready marketability, such as adjustable rate notes and variable rate demand notes (VRDNs); and
  - managed funds that are marketed with the objective of maintaining a stable value such as money market mutual funds or other types of stable value collective investment funds.

L.3.9 For issuers with an affiliated dealer or market maker, there may be a need to include part of the outstanding debt securities (unsecured and secured, term as well as short-term) having maturities greater than 30 calendar days, to cover potential repurchase.

L.3.10 Non contractual obligations where customer short positions are covered by other customers' collateral: A minimum 50% run-off factor of the contingent obligations should be applied where banks have internally matched client assets against other clients' short positions where the collateral does not qualify as Level 1 or Level 2, and the bank may be obligated to find additional sources of funding for these positions in the event of client withdrawals.

Appendix M Other cash outflows: proposed treatment

M.1 Explanation

M.1.1 This annex establishes the outflow percentages that would apply to cashflow items not connected with maturing funding.

M.2 Derivatives cashflows

M.2.1 Derivative cashflows (inflows and outflows) should receive a 100% factor. Banks should calculate, in accordance with their existing valuation methodologies, expected contractual derivative cash inflows and outflows. Cash flows may be calculated on a net basis (i.e. inflows can offset outflows) by counterparty, only where a valid master netting agreement exists and the flows are on the same day or later outflows are offset by earlier inflows. Banks should exclude from such calculations those liquidity requirements that would result from increased collateral needs due to market value movements or falls in value of collateral posted. Options should be assumed to be exercised when they are 'in the money' to the option buyer.

M.2.2 Where derivative payments are collateralised by HQLA, cash outflows should be calculated net of any corresponding cash or collateral inflows that would result, all other things being equal, from contractual obligations for cash or collateral to be provided to the bank, if the bank is legally entitled (and operationally capable) to re-use the collateral in new cash raising transactions once the collateral is received. This is in line with the principle that banks should not double count liquidity inflows and outflows.

M.3 Increased liquidity needs related to downgrade triggers embedded in financing transactions, derivatives and other contracts

M.3.1 Projected outflow percentage: 100% of the amount of collateral that would be posted for, or contractual cash outflows associated with, any downgrade up to and including a 3-notch downgrade.

M.3.2 Often, contracts governing derivatives and other transactions have clauses that require the posting of additional collateral, drawdown of contingent facilities, or early repayment of existing liabilities upon the bank's downgrade by a recognised credit rating organisation. The scenario therefore requires that for each contract in which "downgrade triggers" exist, the bank assumes that 100% of this additional collateral or cash outflow will have to be posted for any downgrade up to and including a 3-notch downgrade of the bank's long-term credit rating. Triggers linked to a bank's short-term rating should be assumed to be triggered at the corresponding long-term rating in accordance with published ratings criteria. The impact of the downgrade should consider impacts on all types of margin collateral and contractual triggers which change rehypothecation rights for non-segregated collateral.

M.4 Increased liquidity needs related to the potential for valuation changes on posted collateral securing derivatives and other transactions

M.4.1 Projected outflow percentage: 20% of the value of non-Level 1 posted collateral.

M.4.2 Observation of market practices indicates that most counterparties to derivative transactions typically are required to secure the mark-to-market valuation of their positions and that this is predominantly done using cash or sovereign, central bank, multilateral development banks, or PSE debt securities with a 0% risk weight under the Basel II standardised approach. When these Level 1 liquid asset securities are posted as collateral, the framework will not require that an additional stock of HQLA be maintained for potential valuation changes.

M.4.3 If however, counterparties are securing mark-to-market exposures with other forms of collateral, to cover the potential loss of market value on those securities, 20% of the value of all such posted collateral, net of collateral received on a counterparty basis (provided that the collateral received is not subject to restrictions on reuse or rehypothecation) will be added to the stock of required HQLA by the bank posting such collateral. This 20% will be calculated based on the notional amount required to be posted as collateral after any other haircuts have been applied that may be applicable to the collateral category. Any collateral that is in a segregated margin account can only be used to offset outflows that are associated with payments that are eligible to be offset from that same account.

M.5 Increased liquidity needs related to excess non-segregated collateral held by the bank that could contractually be called at any time by the counterparty

M.5.1 Projected outflow percentage: 100% of the non-segregated collateral that could contractually be recalled by the counterparty because the collateral is in excess of the counterparty's current collateral requirements.

M.6 Increased liquidity needs related to contractually required collateral on transactions for which the counterparty has not yet demanded the collateral be posted

M.6.1 Projected outflow percentage: 100% of the collateral that is contractually due but where the counterparty has not yet demanded the posting of such collateral.

M.7 Increased liquidity needs related to contracts that allow collateral substitution to non-HQLA assets

M.7.1 Projected outflow percentage: 100% of the amount of HQLA collateral that can be substituted for non-HQLA assets without the bank's consent that have been received to secure transactions that have not been segregated.

M.8 Increased liquidity needs related to market valuation changes on derivatives or other transactions

M.8.1 As market practice requires collateralisation of mark-to-market exposures on derivative and other transactions, banks face potentially substantial liquidity risk exposures to these valuation changes. Inflows and outflows of transactions executed under the same master netting agreement can be treated on a net basis. Any outflow generated by increased needs related to market valuation changes

should be calculated by identifying the largest absolute net 30-day collateral flow seen during the preceding 24 months. The absolute net collateral flow is based on both realised outflows and inflows. Supervisors may adjust the treatment flexibly according to circumstances.

M.9 Loss of funding on asset-backed securities, covered bonds and other structured financing instruments

M.9.1 The scenario assumes the outflow of 100% of the funding transaction maturing within the 30-day period, when these instruments are issued by the bank itself (as this assumes that the re-financing market will not be functioning).

M.10 Loss of funding on asset-backed commercial paper, conduits, securities investment vehicles and other such financing facilities

Potential Risk Element	**HQLA Required**
Debt maturing within the calculation period	100% of maturing amount
Embedded options in financing arrangements that allow for the return of assets or potential liquidity support	100% of the amount of assets that could potentially be returned, or the liquidity required

M.10.1 Banks having structured financing facilities that include the issuance of short-term debt instruments, such as asset backed commercial paper, should fully consider the potential liquidity risk arising from these structures. These risks include, but are not limited to (i) the inability to refinance maturing debt and (ii) the existence of derivatives or derivative-like components contractually written into the documentation associated with the structure that would effectively allow the financing arrangement to be ended (“liquidity puts”) within the 30-day period (such as measures that permit the “return” of assets in a financing arrangement, or that require the original asset transferor to provide liquidity).

M.10.2 Where the structured financing activities of a bank are conducted through a SPE (such as a special purpose vehicle, conduit or structured investment vehicle), the bank should, in determining the HQLA requirements, look through to the maturity of the debt instruments issued by the entity and any embedded options in financing arrangements that may potentially trigger the “return” of assets or require liquidity to be provided to the SPE, irrespective of whether or not the SPE is consolidated.

Appendix N Draft reporting forms

N.1 CDLCR Form layout

CDLCR Draft Reporting Form

BCBS Item No.	TOTAL HIGH-QUALITY LIQUID ASSETS ("HQLA)	Balance Sheeet	Current Valuation	Eligible amount after haricuts
1	**Total HQLA, of which**	0	0	0
	Level 1			
	level 2			
	of which:			
	level 2A			
	level 2B			

BCBS Item No.	CASH OUTFLOWS	Balance Sheeet	Total relevant flows in period	After haircut / adjustment
2	**Retail deposits and deposits from small business customers, of which**			
3	**Stable deposits:**	0	0	0
3.1	of which: individuals			
3.2	of which: small businesses			
4	**Less stable deposits**	0	0	0
4.1	of which: individuals			
4.2	of which: small businesses			
4.3	of which: PIC deposits			
5	**Unsecured wholesale funding, of which**	0	0	0
6	Operational deposits (all counterparties)			
7	Non-operational deposits (all counterparties)			
8	Unsecured debt			
9	**Secured wholesale funding**			
10	**Additional requirements, of which**	0	0	0
11	Outflows related to derivatives exposures and other collateral requirements			
12	Outflows related to loss of funding on debt products			
13	Credit and liquidity facilities			
14	**Other contractual funding obligations**			
15	**Other contingent funding obligations**			
16	**TOTAL CASH OUTFLOWS**	0	0	0

BCBS Item No.	CASH INFLOWS	Balance Sheeet	Total relevant flows in period	After haircut / adjustment
17	Secured lending (eg reverse repos)			
18	Inflows from fully performing exposures			
19	Other cash inflows			
20	**TOTAL CASH INFLOWS**	0	0	0
	LIMIT (75% OF OUTFLOWS)			0
	INFLOWS ALLOWABLE (MAXIMUM OF 75% OF OUTFLOWS)			0
	HQLA REQUIREMENT			0
	CD LIQUIDITY COVERAGE RATIO (%)			

N.2 Notes

N.2.1 The "*BCBS Item No.*" column refers to the numbering used in the LCR.

N.2.2 For many items, totals are required plus a breakdown. In some cases, totals could be calculated from the breakdown. It is currently assumed that this would be done by the bank and entered in the report, rather than any automatic calculation.

N.2.3 Banks will be required to provide values for:

- "*Balance Sheet*" (partly to aid reconciliation): the amount recorded in the balance sheet for each item;
- "*Current Valuation*" (HQLA only): the current value of all items (expected to be equal or similar to the balance sheet value in most cases);
- "*Eligible amounts after haircuts*" (HQLA only): the amount eligible after applying haircuts and any restrictions on eligibility, including the limits on the amount of level 2 assets that are eligible;
- "*Total relevant flows in period*" (flows only): the total projected flows falling with one month, unadjusted; and
- "*After haircut/adjustment*" (flows only): the total adjusted projected flows falling with one month.

N.2.4 Then the key totals would be calculated, as follows:

- "*Total HQLA*" would be automatically derived from the individual inputs;
- "*Total cash outflows*" would be automatically derived from the individual inputs;
- "*Total cash inflows*" would be automatically derived from the individual inputs;
- "*Limit (75% of outflows)*" would be automatically derived, being 75% multiplied by *Total cash outflows;*
- "*Inflows allowable (maximum 75% of outflows)*" would be automatically derived, being the lower of *Total cash inflows* and *Limit (75% of outflows)*;
- "*HQLA Requirement*" would be automatically derived from Total cash outflows minus Inflows allowable (maximum 75% of outflows)"; and
- "*CD Liquidity Coverage Ratio*" (i.e. the CDLCR) would be automatically derived from "*Total HQLA*" divided by *HQLA Requirement*.

N.2.5 An Excel mock-up of the proposed report will be made available to banks along with this Discussion Paper.

N.3 CDLMR Forms layout

CDLMR Draft Reporting Form

BCBS Item No.	TOTAL HIGH-QUALITY LIQUID ASSETS (“HQLA)	Balance Sheeet	Current Valuation	Eligible amount after haricuts
1	**Total HQLA, of which**	0	0	0
	Level 1			
	level 2			
	of which:			
	level 2A			
	level 2B			

BCBS Item No.	CASH OUTFLOWS	Balance Sheeet	Total relevant flows in period	After haircut / adjustment	1 week or less	More than 1 week
2	**Retail deposits and deposits from small business customers, of which**					
3	**Stable deposits:**	0	0	0	0	0
3.1	of which: individuals					
3.2	of which: small businesses					
4	**Less stable deposits**	0	0	0	0	0
4.1	of which: individuals					
4.2	of which: small businesses					
4.3	of which: PIC deposits					
5	**Unsecured wholesale funding, of which**	0	0	0	0	0
6	Operational deposits (all counterparties)					
7	Non-operational deposits (all counterparties)					
8	Unsecured debt					
9	**Secured wholesale funding**					
10	**Additional requirements, of which**	0	0	0	0	0
11	Outflows related to derivatives exposures and other collateral requirements					
12	Outflows related to loss of funding on debt products					
13	Credit and liquidity facilities					
14	**Other contractual funding obligations**					
15	**Other contingent funding obligations**					
16	**TOTAL CASH OUTFLOWS**	**0**	**0**	**0**	**0**	**0**

BCBS Item No.	CASH INFLOWS	Balance Sheeet	Total relevant flows in period	After haircut / adjustment	1 week or less	More than 1 week	Eligible Cash Inflows
17	Secured lending (eg reverse repos)						
18	Inflows from fully performing exposures						
	of which: group bank or government						
19	Other cash inflows						
20	**TOTAL CASH INFLOWS**	**0**	**0**	**0**	**0**	**0**	**0**

	LIQUIDITY (HQLA PLUS CASH INFLOWS)	**0**
	LIQUIDITY REQUIREMENT	**0**
	CD LIQUIDITY MISMATCH RATIO (%)	

N.4 Notes

N.4.1 The "*BCBS Item No.*" column refers to the numbering used in the LCR.

N.4.2 For many items, totals are required plus a breakdown. In some cases, totals could be calculated from the breakdown. It is currently assumed that this would be done by the bank and entered in the report, rather than any automatic calculation.

N.4.3 Banks will be required to provide values for:

- "*Balance Sheet*" (partly to aid reconciliation): the amount recorded in the balance sheet for each item;
- "*Current Valuation*" (HQLA only): the current value of all items (expected to be equal or similar to the balance sheet value in most cases);
- "*Eligible amounts after haircuts*" (HQLA only): the amount eligible after applying haircuts and any restrictions on eligibility, including the limits on the amount of level 2 assets that are eligible;
- "*Total relevant flows in period*" (flows only): the total projected flows falling with one month, unadjusted;
- "*After haircut/adjustment*" (flows only): the total adjusted projected flows falling with one month.
- "*One week or less*" / "*More than 1 week*" (flows only): of the above, the amount falling due within one week / falling due later than one week; and
- "*Eligible cash inflows*" (inflows only): the amount of adjusted inflows eligible (either within one week or meeting a later outflow).

N.4.4 Then the key totals would be calculated, as follows:

- "*Total HQLA*" would be automatically derived from the individual inputs;
- "*Total cash outflows*" would be automatically derived from the individual inputs;
- "*Total cash inflows*" would be automatically derived from the individual inputs;
- "*Liquidity (HQLA plus cash inflows)*" would be automatically derived, being the sum of *Total HQLA* and *Total cash inflows*;
- "*Liquidity Requirement*" would equal *Total cash outflows*; and
- "*CD Liquidity Mismatch Ratio*" (i.e. the CDLMR) would be automatically derived from "*Liquidity*" divided by *Liquidity Requirement*.

N.4.5 An Excel mock-up of the proposed report will be made available to banks along with this Discussion Paper.

N.4.6 The make-up of the eligible cash inflows would be reported on a separate form, which is shown here, completed with mock data.

ELIGIBLE CASH INFLOWS									
								TOTAL	ELIGIBLE
GROUP BANK CASH INFLOWS WITHIN ONE WEEK, AFTER ADJUSTMENTS								40	40
OTHER CASH INFLOWS WITHIN ONE WEEK, AFTER ADJUSTMENTS								10	10
	DAY	CASH OUTFLOWS BEYOND ONE WEEK, AFTER ADJUSTMENTS	SAME OR LATER DATED OUTFLOWS	GROUP BANK CASH INFLOWS, BEYOND ONE WEEK (AFTER ADJUSTMENTS)	OTHER CASH INFLOWS, BEYOND ONE WEEK (AFTER ADJUSTMENTS)	LESS THOSE ALREDY MATCHED	MAXIMUM ELIGIBLE INFLOW	GROUP BANK ELIGIBLE CASH INFLOWS	OTHER ELIGIBLE CASH INFLOWS
	8	4	59	0	0	(49)	10	0	0
	9	0	55	0	0	(49)	6	0	0
	10	4	55	0	0	(49)	6	0	0
	11	2	51	0	0	(49)	2	0	0
	12	0	49	20	0	(46)	3	3	0
	13	0	49	0	0	(46)	3	0	0
	14	0	49	0	0	(46)	3	0	0
	15	6	49	0	8	(39)	10	0	7
	16	2	43	0	0	(39)	4	0	0
	17	1	41	0	0	(39)	2	0	0
	18	1	40	0	0	(39)	1	0	0
	19	0	39	0	0	(39)	0	0	0
	20	4	39	10	0	(33)	6	6	0
	21	2	35	0	0	(33)	2	0	0
	22	10	33	0	20	(14)	19	0	19
	23	0	23	0	0	(14)	9	0	0
	24	0	23	0	0	(14)	9	0	0
	25	0	23	0	0	(14)	9	0	0
	26	6	23	0	0	(14)	9	0	0
	27	2	17	0	10	(4)	13	0	10
	28	10	15	0	0	(4)	11	0	0
	29	1	5	0	0	(4)	1	0	0
	30	2	4	0	4	(1)	3	0	3
	31	2	2	0	1	0	2	0	1
TOTAL ELIGIBLE LATER DATED CASH INFLOWS								9	40
TOTAL ELIGIBLE LATER GROUP BANK CASH INFLOWS									49
TOTAL ELIGIBLE OTHER CASH INFLOWS									50
TOTAL ELIGIBLE INFLOWS									99
LIMIT ON OTHER INFLOWS (75% OF OUTFLOWS)									50

N.4.7 Banks will be required to provide values for:

- "*Cash inflows within one week, after adjustments*": this should correspond to the total reported on the CDLMR report;
- "*Cash inflows beyond one week, after adjustments*": this should be reported broken down by day. The total should correspond to the total reported on the CDLMR report;

- "*Cash outflows beyond one week, after adjustments*": this should be reported broken down by day. The total should correspond to the total reported on the CDLMR report;
- "*Same or later dated outflows*": calculated as the sum of all *Cash outflows beyond one week, after adjustments* falling on the same or a later date;
- "*Less those already matched*": calculated as the sum of all *Eligible cash inflows* falling on a later date;
- "*Maximum eligible inflows*": calculated as the sum of *Same or later dated outflows* and *Less those already matched*; and
- *"Eligible cash inflows"*: calculated as *Cash inflows beyond one week, after adjustments*, after applying a cap of *Maximum eligible inflows.* The total should correspond to the total reported on the CDLMR report.

N.5 NSFR Form layout

NSFR Draft Reporting Form

ITEM	Avaliable Stable Funding ("A**SF**")	Value	ASF Factor	ASF
1	Capital and long-term funding		100%	0
2	Stable retail deposits		95%	0
3	Less stable retail deposits		90%	0
4	Non-financial funding		50%	0
5	Operational deposits		50%	0
6	Other medium-term funding		50%	0
7	Other		0%	0
8	**TOTAL ASF**	**0**		**0**

ITEM	Required Stable Funding ("**RSF**") - balance sheet	Value	RSF Factor	RSF
9	Cash and central bank		0%	0
10	Trade date receivables		0%	0
11	Unencumbered Level I HQLA		5%	0
12	Level 1 HQLA secured short term lending to banks		10%	0
13	Other short-term lending to banks plus unencumbered Level 2A HQLA		15%	0
14	Unencumbered Level 2B HQLA		50%	0
15	Encumbered HQLA < 1 year		50%	0
16	Medium term lending to banks		50%	0
17	Operational deposits		50%	0
18	All other loans <1 year		50%	0
19	Residential Mortgages		65%	0
20	Loans >1 year, ex financial institutions, RW 35% or less		65%	0
21	Loans >1 year, ex financial institutions, RW >35%		85%	0
22	Securities and physically traded commoditiies		85%	0
23	Margin provided		85%	0
24	Encumbered assets > 1 year		100%	0
25	Derivatives		100%	0
26	Other assets		100%	0
27	**RSF - balance sheet**	**0**		**0**

ITEM	RSF - off balance sheet	Value	RSF Factor	RSF
28	Irrevocable facilities		5%	
29	Unconditionally revocable facilities;		0%	
30	Trade related obligations		0%	
31	Other commitments		0%	
32	**RSF - off balance sheet**	**0**	**0.05**	**0**
33	**Total RSF**			**0**
34	**Net Stable Funding Ratio ("NSFR") (%)**			

N.6 Notes

N.6.1 For individual items, a detailed breakdown by date is required based on the post adjustment values, i.e. reflecting the various adjustments required to arrive at the relevant amount for liquidity purposes. In addition, a summary of how the total of these amounts compares to the total predicted flows during the month and the total balance should also be entered.

N.6.2 For the avoidance of doubt, it should be emphasised that the reported NSFR will not be subject to a limit and the factors indicated here do not represent the Tri-Party Group's considerations: they are, instead, the minimum permitted in the Basel III NSFR standard. More details on definitions are provided in that document.

N.6.3 Available Stable Funding ("**ASF**") data should be input as follows, with the ASF being calculated as the amount input multiplied by the ASF Factor:

- *"1: Capital and long-term funding"*: The total amount of (1) regulatory capital and (2) long-term funding. ASF Factor = 100%. Regulatory capital and long term funding are defined, for these purposes, as:
    - Regulatory capital is all regulatory capital except for Tier 2 instruments with residual maturity of less than one year; and
    - Long-term funding is all capital instruments and liabilities with residual maturity of one year or more;
- *"2: Stable retail deposits"*: Stable non-maturity (demand) deposits and/or term deposits (as defined in **sub-section 21.2**) with residual maturities of less than one year provided by retail and small business customers. ASF Factor = 95%;
- *"3: Less stable retail deposits"*: Less stable (as defined in **sub-section 21.3**) non-maturity (demand) deposits and/or term deposits with residual maturities of less than one year provided by retail and small business customers. ASF Factor = 90%;
- *"4: Non-financial funding"*. Unsecured wholesale funding, non-maturity deposits and/or term deposits with a residual maturity of less than one year, provided by non-financial corporates (i.e. not banks or financial institutions, including fiduciaries), sovereigns, central banks, multilateral development banks and PSEs. ASF Factor = 50%;
- "5: *Operational deposits*". All operational deposits. ASF Factor = 50%;
- *"6: Other medium term funding"*: All other liabilities and equity categories not included in the above categories (principally non-operational deposits from banks), where the residual maturity is between 6 and 12 months. ASF Factor = 50%; and
- *"7: Other"*: All other liabilities and equity categories not included in the above categories. ASF Factor = 0%. Examples include:
    - Net derivative liabilities i.e. derivatives payable less variation margin posted less derivatives receivable (but only if the result is a positive figure); and

- o Trade date payables arising from the purchase of financial instruments, foreign currencies and commodities.

N.6.4 Required Stable Funding ("**RSF**") - the RSF for each item is calculated as the Balance Sheet amount input multiplied by the RSF factor. Please note that:

- in all cases, unless a specific treatment is stated, HQLA that is encumbered for a period of less than six months should be treated as unencumbered for these purposes; and
- all non-performing loans should be reported within item 26 "*Other Assets*".

N.6.5 Balance Sheet data should be input as follows:

- *"9: Cash and central bank":* Coins, banknotes, central bank reserves and all claims on central banks with a residual maturity of less than six months. RSF Factor = 0%;
- *"10: Trade date receivables":* Trade date receivables arising from the sale of financial instruments, foreign currencies and commodities. RSF Factor = 0%;
- *"11: Unencumbered Level I HQLA":* Unencumbered Level 1 assets, excluding coins, banknotes and central bank reserves. RSF Factor = 5%;
- *"12: Level I HQLA secured short-term lending to banks":* Unencumbered loans to banks with residual maturity of less than six months where the loan is secured against level I HQLA and where the bank has the ability to freely re-hypothecate the collateral received. RSF Factor = 10%;
- *"13: Other short-term lending to banks plus unencumbered level 2A HQLA"*: All other unencumbered loans to banks subject to prudential supervision with residual maturities of less than six months plus unencumbered Level 2A assets. RSF Factor = 15%;
- *14: "Unencumbered Level 2B HQLA":* Unencumbered Level 2B assets. RSF Factor = 50%;
- *"15: Encumbered HQLA < 1 year":* HQLA encumbered for a period of six months or more but less than one year. RSF Factor = 50%;
- *"16: Medium term lending to banks":* Loans to banks subject to prudential supervision with residual maturities six months or more and less than one year. RSF Factor = 50%;
- *"17: Operational deposits":* Deposits held at other financial institutions for operational purposes. RSF Factor = 50%;
- *"18: All other loans <1 year":* All other assets not included in the above categories with residual maturity of less than one year, including residential mortgages and loans to non-bank financial institutions, non-financial corporates, retail and small business customers, sovereigns, central banks and PSEs. RSF Factor = 50%;
- *"19: Residential Mortgages":* Unencumbered residential mortgages with a residual maturity of one year or more and with a risk weight of less than or equal to 35%. RSF Factor = 65%;

- *"20: Loans >1 year, excluding financial institutions, RW 35% or less":* Other unencumbered loans not included in the above categories, excluding loans to financial institutions, with a residual maturity of one year or more and with a risk weight of less than or equal to 35% (AA- rated corporates) under the Standardised Approach. RSF Factor = 65%;
- *"21: Loans >1 year, excluding financial institutions, RW >35%":* Other unencumbered performing loans with risk weights greater than 35% under the Standardised Approach and residual maturities of one year or more, excluding loans to financial institutions. RSF Factor = 85%;
- *"22: Securities and physically traded commodities":* Unencumbered securities that are not in default and do not qualify as HQLA, including exchange-traded equities plus physical traded commodities and gold. RSF Factor = 85%;
- *"23: Margin provided":* Cash, securities or other assets provided as initial margin for derivative contracts or provided to contribute to the default fund of a central counterparty, such as a clearing house. RSF Factor = 85%;
- *"24: Encumbered assets > 1 year":* All assets, including HQLA, that are encumbered for a period of one year or more. RSF Factor = 100%;
- *"25: Derivatives":* the sum of (A): (1) Net derivatives receivable less (2) derivatives payable less variation margin posted but only if the result is a positive figure plus (B) 20% of derivative liabilities, (i.e. the replacement cost for derivative contracts where the contract has a negative value). RSF Factor = 100%; and
- *"26: Other assets":* All other assets not included in the above categories, including non-performing loans, loans to financial institutions with a residual maturity of one year or more, non-exchange-traded equities, fixed assets, pension assets, intangibles, deferred tax assets, retained interest, insurance assets, subsidiary interests and defaulted securities. RSF Factor = 100%.

N.6.6 The treatment of lending to banks is the same as for lending to other counterparties for loans between six months and one year (50%), but:

- for shorter term loans, the treatment is less onerous (15% vs 50%), reflecting the fact that bank lending is less likely to be expected to be rolled-over, whilst
- for longer term loans, the treatment is more onerous (100% vs 65% to 85%), reflecting the fact that such lending is less likely to be re-financed.

N.6.7 Required Stable Funding ("**RSF**") – Off Balance Sheet data will be required to be input by banks as follows, with the RSF being calculated as the amount input multiplied by the RSF factor:

- *"28: Irrevocable facilities":* Irrevocable and conditionally revocable credit and liquidity facilities to any client. RSF Factor = 5%;
- *"29: Unconditionally revocable facilities":* Unconditionally revocable credit and liquidity facilities. RSF Factor = 0%;
- *"30: Trade related obligations":* Trade finance-related obligations (including guarantees and letters of credit). RSF Factor = 0%; and

- *"31: Other commitments"*. Other contingent funding obligations, including products and instruments, for which the RSF Factor will be 0%, such as:
    - Guarantees and letters of credit unrelated to trade finance obligations; and
    - Non-contractual obligations such as:
        - potential requests for debt repurchases of the bank's own debt or that of related conduits, securities investment vehicles and other such financing facilities;
        - structured products where customers anticipate ready marketability, such as adjustable rate notes and variable rate demand notes (VRDNs); and
        - managed funds that are marketed with the objective of maintaining a stable value.

N.6.8 The "*Net Stable Funding Ratio (%)*" is automatically calculated as the total *ASF* divided by the total *RSF*.

N.6.9 An Excel mock-up of the proposed report will be made available to banks along with this Discussion Paper.

Appendix O Treatment for jurisdictions with insufficient HQLA

O.1 Eligibility for alternative liquidity approaches

O.1.1 Some jurisdictions may have an insufficient supply of Level 1 assets (or both Level 1 and Level 2 assets) in their domestic currency to meet the aggregate demand of banks with significant exposures in this currency. To address this situation, the LCR sets out three alternative treatments for determining eligibility of HQLA, which are expected to apply to a limited number of currencies and jurisdictions.

O.1.2 Eligibility for such alternative treatment will be judged on the basis of the qualifying criteria set out in Annex 2 to the LCR and will be determined through an independent peer review process overseen by the Basel Committee.

O.1.3 The CD supervisors do not consider that the CDs meet these criteria. However, it is recognised that banks may operate through branches that are in jurisdictions that do.

O.1.4 To qualify for the alternative treatment, a jurisdiction would need to demonstrate that:

- there is an insufficient supply of HQLA in its domestic currency, taking into account all relevant factors affecting the supply of, and demand for, such HQLA;
- the insufficiency is caused by long-term structural constraints that cannot be resolved within the medium term;
- it has the capacity, through any mechanism or control in place, to limit or mitigate the risk that the alternative treatment cannot work as expected; and
- it is committed to observing the obligations relating to supervisory monitoring, disclosure, and periodic self-assessment and independent peer review of its eligibility for alternative treatment.

O.1.5 All of the above criteria have to be met to qualify for the alternative treatment.

O.2 Proposed approach in the CDs

O.2.1 Where one or more local alternative approaches have been established by a local supervisor and that approach has been determined to be appropriate by peer review, banks that have branches in that jurisdiction may utilise the local approach to the extent that the alternative assets held meet liquidity requirements arising from liabilities held in that jurisdiction that are not met by HQLA held in that jurisdiction.

O.2.2 Where no peer review has been published, a bank wishing to use a local treatment should provide the relevant supervisor with full details of the local approach, including any self-assessment published by the relevant authority, any published plans to carry out such a peer review and the bank's own assessment of the approach versus the parameters set out in the LCR.

O.2.3 Approval will depend on all relevant circumstances and might be temporary, including where the approach appears to meet required criteria and a peer review was planned but had not yet occurred. For example, this would address circumstances where Basel III had not been fully implemented.

O.3 Outline of alternative approaches

O.3.1 Three approaches are set out in the LCR. Each has its merits and issues and the below is only an outline of them. The LCR sets out parameters in full but for each local approach it is expected that this would be supplemented with detailed local implementation rules and that, in some cases, only one or two of the approaches will be developed locally.

O.3.2 Option 1 – Contractual committed liquidity facilities from the relevant central bank, with a fee.

- Banks would be granted access to contractual committed liquidity facilities provided by the relevant central bank (ie relevant to the currency in question), for a fee. These facilities should not be confused with regular central bank standing arrangements. In particular, these facilities are contractual arrangements between the central bank and the commercial bank with a maturity date which, at a minimum, falls outside the 30-day LCR window. Further, the contract must be irrevocable prior to maturity and involve no ex-post credit decision by the central bank. Such facilities are only permissible if there is also a fee for the facility which is charged regardless of the amount, if any, drawn down against that facility and the fee is set so that both banks which claim the facility line to meet the LCR, and banks which do not, have similar financial incentives to reduce their exposure to liquidity risk.

O.3.3 Option 2 – Foreign currency HQLA to cover domestic currency liquidity needs.

- Option 2 would allow supervisors to permit banks that evidence a shortfall of HQLA in the domestic currency to hold HQLA in a currency that does not match the currency of the associated liquidity risk, provided that the resulting currency mismatch positions are controlled within limits agreed by their supervisors.
- To account for foreign exchange risk associated with foreign currency HQLA used to cover liquidity needs in the domestic currency, such liquid assets should be subject to a minimum haircut of 8% for major currencies that are actively traded in global foreign exchange markets. If the domestic currency is formally pegged to another currency under an effective mechanism, the haircut for the pegged currency can be lowered to a level that reflects the limited exchange rate risk under the peg arrangement.

O.3.4 Option 3 – Additional use of Level 2 assets with a higher haircut.

- This option addresses currencies for which there are insufficient Level 1 assets, as determined by reference to the qualifying principles and criteria, but where there are sufficient Level 2A assets. In this case, supervisors may choose to allow banks that evidence a shortfall of HQLA in the domestic

currency to hold additional Level 2A assets in the stock. These additional Level 2A assets would be subject to a minimum haircut of 20%, i.e. 5% higher than the 15% haircut applicable to Level 2A assets that are included in the standard 40% cap. The higher haircut is applied to cover any additional price and market liquidity risks arising from increased holdings of Level 2A assets beyond the 40% cap, and to provide a disincentive for banks to use this option based on yield considerations.

O.3.5 Maximum level of usage of options for alternative treatment: the usage of any of the above options would be constrained by a limit specified by supervisors in relevant jurisdictions. For example, this might be set at 80% of the domestic currency HQLA requirement in a particular jurisdiction.

O.3.6 This would mean that a bank adopting the alternative(s) would be allowed to include HQLA that was only eligible under the alternative(s) (after applying any relevant haircut) to meet up to 80% of the HQLA requirement relating to domestic currency liabilities originated in the jurisdiction, with the HQLA requirement relating to foreign currency liabilities and the remaining 20% of that relating to domestic currency liabilities (and such liabilities arising outside of that jurisdiction), being required to be met by HQLA that meets the standard HQLA rules set out herein.