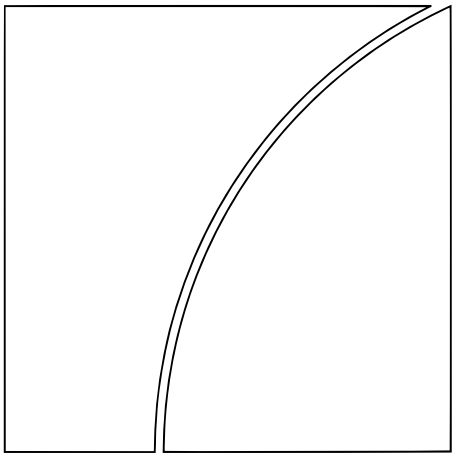
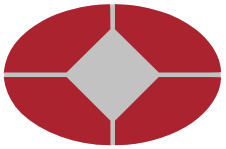
Basel Committee on Banking Supervision

LCR

Liquidity Coverage Ratio

This standard describes the Liquidity Coverage Ratio, a measure which promotes the short-term resilience of a bank's liquidity risk profile.





BANK FOR INTERNATIONAL SETTLEMENTS

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LCR10

Definitions and application

This chapter describes the scope of application of the Liquidity Coverage Ratio (LCR), the treatment of home / host liquidity requirements and liquidity transfer restrictions, and the currency in which the LCR should be met and reported.

Version effective as of 15 December 2019

First version in format of consolidated framework.

Scope of application

10.1

The application of the requirements of the liquidity coverage ratio (LCR) standard, set out in LCR, and the liquidity monitoring metrics, set out in SRP50, follow the existing scope of application set out in SCO10.1 to SCO10.4. The LCR standard and monitoring tools should be applied to all internationally active banks on a consolidated basis, but may be used for other banks and on any subset of entities of internationally active banks as well to ensure greater consistency and a level playing field between domestic and cross-border banks. The LCR standard and monitoring tools should be applied consistently wherever they are applied.

10.2

National supervisors should determine which investments in banking, securities and financial entities of a banking group that are not consolidated per LCR10.1 should be considered significant, taking into account the liquidity impact of such investments on the group under the LCR standard. Normally, a non-controlling investment (eg a joint venture or minority-owned entity) can be regarded as significant if the banking group will be the main liquidity provider of such investment in times of stress (for example, when the other shareholders are non-banks or where the bank is operationally involved in the day-to-day management and monitoring of the entity's liquidity risk). National supervisors should agree with each relevant bank on a case-by-case basis on an appropriate methodology for how to quantify such potential liquidity draws, in particular, those arising from the need to support the investment in times of stress out of reputational concerns for the purpose of calculating the LCR. To the extent that such liquidity draws are not included elsewhere, they should be treated under "Other contingent funding obligations", as described in LCR40.70.

10.3

Regardless of the scope of application of the LCR, in keeping with Principle 6 as outlined in the Principles for Sound Liquidity Risk Management and Supervision, a bank should actively monitor and control liquidity risk exposures and funding needs at the level of individual legal entities, foreign branches and subsidiaries, and the group as a whole, taking into account legal, regulatory and operational limitations to the transferability of liquidity.

Differences in home / host liquidity requirements

10.4

While most of the parameters in the LCR standard are internationally "harmonised", national differences in liquidity treatment may occur in those items subject to national discretion (eg deposit run-off rates, contingent funding obligations, market valuation changes on derivative transactions) and where more stringent parameters are adopted by some supervisors.

10.5

When calculating the LCR on a consolidated basis, a cross-border banking group should apply the liquidity parameters adopted in the home jurisdiction to all legal entities being consolidated except for the treatment of retail / small business deposits that should follow the relevant parameters adopted in host jurisdictions in which the entities (branch or subsidiary) operate. This approach will enable the stressed liquidity needs of legal entities of the group (including branches of those entities) operating in host jurisdictions to be more suitably reflected, given that deposit run-off rates in host jurisdictions are more influenced by jurisdiction-specific

factors such as the type and effectiveness of deposit insurance schemes in place and the behaviour of local depositors.

10.6

Home requirements for retail and small business deposits should apply to the relevant legal entities (including branches of those entities) operating in host jurisdictions if:

1. there are no host requirements for retail and small business deposits in the particular jurisdictions;
2. those entities operate in host jurisdictions that have not implemented the LCR; or
3. the home supervisor decides that home requirements should be used that are stricter than the host requirements.

Treatment of liquidity transfer restrictions

10.7

As noted in LCR30.21, as a general principle, no excess liquidity should be recognised by a cross-border banking group in its consolidated LCR if there is reasonable doubt about the availability of such liquidity. Liquidity transfer restrictions (eg ring-fencing measures, non-convertibility of local currency, foreign exchange controls) in jurisdictions in which a banking group operates will affect the availability of liquidity by inhibiting the transfer of high-quality liquid assets (HQLA) and fund flows within the group. The consolidated LCR should reflect such restrictions in a manner consistent with LCR30.21. For example, the eligible HQLA that are held by a legal entity being consolidated to meet its local LCR requirements (where applicable) can be included in the consolidated LCR to the extent that such HQLA are used to cover the total net cash outflows of that entity, notwithstanding that the assets are subject to liquidity transfer restrictions. If the HQLA held in excess of the total net cash outflows are not transferable, such surplus liquidity should be excluded from the LCR calculation.

10.8

For practical reasons, the liquidity transfer restrictions to be accounted for in the consolidated ratio are confined to existing restrictions imposed under applicable laws, regulations and supervisory requirements.[1] A banking group should have processes in place to capture all liquidity transfer restrictions to the extent practicable, and to monitor the rules and regulations in the jurisdictions in which the group operates and assess their liquidity implications for the group as a whole.

1 Footnote

1 *There are a number of factors that can impede cross-border liquidity flows of a banking group, many of which are beyond the control of the group and some of these restrictions may not be clearly incorporated into law or may become visible only in times of stress.*

Currencies

10.9

As outlined in LCR30.29, while the LCR must be met on a consolidated basis and reported in a

common currency, supervisors and banks should also be aware of the liquidity needs in each significant currency. As indicated in the LCR standard, the currencies of the stock of HQLA should be similar in composition to the operational needs of the bank. Banks and supervisors cannot assume that currencies will remain transferable and convertible in a stress period, even for currencies that in normal times are freely transferable and highly convertible.

LCR20

Calculation

This chapter explains how to calculate the Liquidity Coverage Ratio, the minimum requirement and banks' reporting obligations.

Version effective as of 15 December 2019

Updated to include the FAQs on climate-related financial risks published on 8 December 2022.

20.1

The Committee has developed the Liquidity Coverage Ratio (LCR) to promote the short-term resilience of the liquidity risk profile of banks by ensuring that they have sufficient high-quality liquid assets (HQLA) to survive a significant stress scenario lasting 30 calendar days.

20.2

The scenario for this standard entails a combined idiosyncratic and market-wide shock that would result in:

1. the run-off of a proportion of retail deposits;
2. a partial loss of unsecured wholesale funding;
3. a partial loss of secured, short-term financing with certain collateral and counterparties;
4. additional contractual outflows that would arise from a downgrade in the bank's public credit rating by up to and including three notches, including collateral posting requirements;
5. increases in market volatilities that impact the quality of collateral or potential future exposure of derivative positions and thus require larger collateral haircuts or additional collateral, or lead to other liquidity needs;
6. unscheduled draws on committed but unused credit and liquidity facilities that the bank has provided to its clients; and
7. the potential need for the bank to buy back debt or honour non-contractual obligations in the interest of mitigating reputational risk.

20.3

This stress test should be viewed as a minimum supervisory requirement for banks. Banks are expected to conduct their own stress tests to assess the level of liquidity they should hold beyond this minimum, and construct their own scenarios that could cause difficulties for their specific business activities. Such internal stress tests should incorporate longer time horizons than the one mandated by this standard. Banks should share the results of these additional stress tests with supervisors.

1 FAQ

FAQ1 *Should banks consider climate-related financial risks in conducting their own stress tests to assess the level of liquidity they should hold beyond the LCR minimum? Banks should consider material climate-related financial risks in their internal liquidity stress tests to assess their potential impact on net cash outflows or the value of liquidity buffer assets. These assessments may inform the level of liquidity they should hold beyond the LCR minimum. Material climate-related financial risks may be incorporated into internal liquidity adequacy assessment processes iteratively and progressively as the methodologies and data used to analyse these risks mature over time and analytical gaps are addressed.*

20.4

The LCR has two components:

1. value of the stock of HQLA in stressed conditions; and
2. total net cash outflows, calculated according to the scenario parameters outlined in

LCR30 and LCR40. $$\frac{\textit{Stock of HQLA}}{\textit{Total net cash outflows over the next 30 calendar days}} \geq 100\%$$

20.5

The LCR builds on traditional liquidity "coverage ratio" methodologies used internally by banks to assess exposure to contingent liquidity events. The total net cash outflows for the scenario are to be calculated for 30 calendar days into the future. The standard requires that, absent a situation of financial stress, the value of the ratio be no lower than 100% (ie the stock of HQLA should at least equal total net cash outflows) on an ongoing basis because the stock of unencumbered HQLA is intended to serve as a defence against the potential onset of liquidity stress. During periods of stress, however, 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 the circumstances.

20.6

In particular, supervisory decisions regarding a bank's use of its HQLA should be guided by consideration of the core objective and definition of the LCR. Supervisors should exercise judgement in their assessment and account not only for prevailing macrofinancial conditions, but also consider forward-looking assessments of macroeconomic and financial conditions. In determining a response, supervisors should be aware that some actions could be procyclical if applied in circumstances of market-wide stress. Supervisors should seek to take these considerations into account on a consistent basis across jurisdictions.

1. Supervisors should assess conditions at an early stage, and take actions if deemed necessary, to address potential liquidity risk.
2. Supervisors should allow for differentiated responses to a reported LCR below 100%. Any potential supervisory response should be proportionate with the drivers, magnitude, duration and frequency of the reported shortfall.
3. Supervisors should assess a number of firm- and market-specific factors in determining the appropriate response, as well as other considerations related to both domestic and global frameworks and conditions. Potential considerations include, but are not limited to:
    1. the reason(s) that the LCR fell below 100%. This includes use of the stock of HQLA, an inability to roll over funding or large unexpected draws on contingent obligations. In addition, the reasons may relate to overall credit, funding and market conditions, including liquidity in credit, asset and funding markets, affecting individual banks or all institutions, regardless of their own condition;
    2. the extent to which the reported decline in the LCR is due to a firm-specific or market-wide shock;
    3. a bank's overall health and risk profile, including activities, positions with respect to other supervisory requirements, internal risk systems, controls and other management processes, among others;
    4. the magnitude, duration and frequency of the reported decline of HQLA;
    5. the potential for contagion to the financial system and additional restricted flow of credit or reduced market liquidity due to actions to maintain an LCR of 100%; and
    6. the availability of other sources of contingent funding such as central bank funding,[2] or other actions by prudential authorities.
4. Supervisors should have a range of tools at their disposal to address a reported LCR below 100%. Banks may use their stock of HQLA in both idiosyncratic and systemic stress

events, although the supervisory response may differ between the two.

1. At a minimum, a bank should present an assessment of its liquidity position, including the factors that contributed to its LCR falling below 100%, the measures that have been and will be taken and the expectations on the potential length of the situation. Enhanced reporting to supervisors should be commensurate with the duration of the shortfall.
2. If appropriate, supervisors could also require actions by a bank to reduce its exposure to liquidity risk, strengthen its overall liquidity risk management, or improve its contingency funding plan.
3. However, in a situation of sufficiently severe system-wide stress, effects on the entire financial system should be considered. Potential measures to restore liquidity levels should be discussed, and should be executed over a period of time considered appropriate to prevent additional stress on the bank and on the financial system as a whole.

5. Supervisors' responses should be consistent with the overall approach to the prudential framework.

1 Footnote, 1 FAQ

2 *The Sound Principles require that a bank develop a contingency funding plan (CFP) that clearly sets out strategies for addressing liquidity shortfalls, in both firm-specific and market-wide situations of stress. A CFP should, among other things, "reflect central bank lending programmes and collateral requirements, including facilities that form part of normal liquidity management operations (eg the availability of seasonal credit)."*

FAQ1 *Should supervisors consider climate-related financial risks in decisions regarding a bank's use of HQLA?*
Supervisors should consider material climate-related financial risks among the range of other considerations in determining a response to a bank's use of its HQLA. For example, climate-related financial risks may impact both prevailing and forward-looking assessments of macroeconomic and financial conditions that are relevant in addressing a reported LCR below 100%, consistent with the overall approach to the prudential framework.

20.7

The LCR should be used on an ongoing basis to help monitor and control liquidity risk. The LCR must be reported to supervisors at least monthly, with the operational capacity to increase the frequency to weekly or even daily in stressed situations at the discretion of the supervisors. The time lag in reporting should be as short as feasible and ideally should not surpass two weeks.

20.8

Banks are expected to inform supervisors of their LCR and their liquidity profile on an ongoing basis. Banks must also notify supervisors immediately if their LCR has fallen, or is expected to fall, below 100%.

LCR30

High-quality liquid assets

This chapter defines the qualifying criteria for high-quality liquid assets.

Version effective as of 15 December 2019

Updated to include the following FAQ: LCR30.1 FAQ1.

Introduction

30.1

The numerator of the Liquidity Coverage Ratio (LCR) is the "stock of high-quality liquid assets (HQLA)". Under the standard, banks must hold a stock of unencumbered HQLA to cover the total net cash outflows (as defined in LCR40) over a 30-day period under the stress scenario prescribed in LCR20. In order to qualify as HQLA, assets should be liquid in markets during a time of stress and, ideally, be central bank eligible. The following paragraphs set out the characteristics that such assets should generally possess and the operational requirements that they should satisfy.[3]

1 Footnote, 1 FAQ

3 *Refer to the sections on "Definition of HQLA" (LCR30.30 to LCR30.47) and "Operational requirements" (LCR30.13 to LCR30.28) for the characteristics that an asset must meet to be part of the stock of HQLA and the definition of "unencumbered" respectively.*

FAQ1 *Regarding the reform of benchmark reference rates, what guidance can the Committee provide on the assessment of eligibility of instruments as HQLA? Solely for the purpose of implementing benchmark rate reforms, when a type of instrument that references an interbank offered rate (IBOR) and has historically qualified as eligible HQLA is being replaced with an equivalent type of instrument that references an alternative references rate, supervisors can take into account anticipated increases in the liquidity of the replacement instrument during the transition period when determining whether it qualifies as HQLA.*

Characteristics of HQLA

30.2

Assets are considered to be HQLA if they can be easily and immediately converted into cash 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. Nevertheless, there are certain assets that are more likely to generate funds without incurring large discounts in sale or repurchase agreement (repo) markets due to fire-sales even in times of stress. This section outlines 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. These factors should assist supervisors in determining which assets, despite meeting the criteria from LCR30.40 to LCR30.45, are not sufficiently liquid in private markets to be included in the stock of HQLA.

30.3

As outlined by the characteristics described below, 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. Lower-quality assets typically fail to meet that test. An attempt by a bank to raise liquidity from lower-quality assets under conditions of severe market stress would entail acceptance of a large fire-sale discount or haircut to compensate for high market risk. That may not only erode the market's confidence in the bank, but would also generate mark-to-market losses for banks holding similar instruments and add to the pressure on their liquidity position, thus encouraging further fire sales and declines in prices and market liquidity. In these circumstances, private market

liquidity for such instruments is likely to disappear quickly.

30.4

HQLA (except Level 2B assets as defined below in LCR30.44 to LCR30.46) should ideally be eligible at central banks[4] for intraday liquidity needs and overnight liquidity facilities. In the past, central banks have provided 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. That in turn would raise confidence in the safety and soundness of liquidity risk management in the banking system.

1 Footnote

4 *In most jurisdictions, HQLA should be central bank eligible in addition to being liquid in markets during stressed periods. In jurisdictions where central bank eligibility is limited to an extremely narrow list of assets, a supervisor may allow unencumbered, non-central bank eligible assets that meet the qualifying criteria for Level 1 or Level 2 assets to count as part of its stock (see Definition of HQLA beginning from LCR30.30).*

30.5

However, central bank eligibility does not by itself constitute the basis for the categorisation of an asset as HQLA.

Fundamental characteristics

30.6

Low 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 sensitivity to interest rate and market risk, low legal risk, low inflation risk and denomination in a convertible currency with low foreign exchange risk all enhance an asset's liquidity.

30.7

Ease and certainty of valuation: an asset's liquidity increases if market participants are more 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 exclude most structured or exotic products.

30.8

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.

30.9

Listed on a developed and recognised exchange: being listed increases an asset's transparency.

Market-related characteristics:

30.10

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

1. 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.
2. 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.

30.11

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 over benchmarks 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.

30.12

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.

Operational requirements

30.13

All assets in the stock of HQLA are subject to the following operational requirements. The purpose of the operational requirements is to recognise that not all assets outlined in LCR30.40 to LCR30.45 that meet the asset class, risk-weighting and credit-rating criteria should be eligible for the stock as there are other operational restrictions on the availability of HQLA that can prevent timely monetisation during a stress period.

30.14

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; and that the stock of assets 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.

30.15

A bank must periodically monetise a representative proportion of the assets in the stock 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. This requirement for periodic monetisation may be

satisfied by transactions carried out through a bank's normal course of business.

1 FAQ

FAQ1 *What is "a representative proportion of the assets in the stock" banks are supposed to "periodically monetise ... through repo or outright sale"?*
The extent, subject and frequency of HQLA monetisation necessary to comply with LCR30.15 should be assessed on a case by case basis. It is generally the responsibility of banks to incorporate the intent of LCR30.15 in their management of liquid assets and be able to demonstrate to supervisors an approach which is appropriate rather than ex ante stipulations.

30.16

All assets in the stock must be unencumbered. "Unencumbered" means free of legal, regulatory, contractual or other restrictions on the ability of the bank to liquidate, sell, transfer or assign the asset. An asset in the stock must 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.[5]

1 Footnote, 2 FAQs

5 *If a bank has deposited, pre-positioned or pledged Level 1, Level 2 and other assets in a collateral pool and no specific securities are assigned as collateral for any transactions, it may assume that assets are encumbered in order of increasing liquidity value in the LCR, ie assets ineligible for the stock of HQLA are assigned first, followed by Level 2B assets, then Level 2A and finally Level 1. This determination must be made in compliance with any requirements, such as concentration or diversification, of the central bank or PSE.*

FAQ1 *A bank has a reverse repurchase agreement, receiving collateral that consists of a pool of assets including non-HQLA. Can the whole portion of Level 1 and Level 2 assets of the collateral basket be counted towards HQLA (subject to the other requirements on HQLA-eligible assets)?*
An HQLA-eligible asset received as a component of a pool of collateral for a secured transaction (eg reverse repo) can be included in the stock of HQLA (with associated haircuts) to the extent that it can be monetised separately.

FAQ2 *If a bank pledges a pool of HQLA and non-HQLA collateral with a clearing entity such as a central counterparty against secured funding transactions, may it count any HQLA-eligible securities that are held as part of the collateral pool, but remain unused at end-of-day as part of the stock of HQLA? Does this requirement apply to derivatives as well?*
The bank may count the unused portion of HQLA-eligible collateral pledged towards its stock of HQLA (with associated haircuts). If the bank cannot determine which specific assets remain unused, it may assume that assets are encumbered in order of increasing liquidity value, consistent with the methodology set out in footnote 3 of LCR30. Assets in a pool that is intended to (exclusively or additionally) collateralise derivatives transactions are not readily available within the meaning of the operational requirements.

30.17

A bank must exclude from the stock those assets that, although meeting the definition of "unencumbered" specified in LCR30.16, the bank does 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 providing the function identified in LCR30.18 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.

30.18

The stock must be under the control of the function charged with managing the liquidity of the bank (eg 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 intent for use as a source of contingent funds, or by demonstrating that the function can monetise the asset at any point in the 30-day stress period and that 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.

30.19

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 must 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).

30.20

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.

30.21

As noted in LCR10.7 and LCR10.8, qualifying HQLA that are held to meet statutory liquidity requirements at the legal entity or sub-consolidated level (where applicable) may only 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.

30.22

In assessing whether assets are freely transferable for regulatory purposes, banks should be aware that assets may 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 to the extent that they can be freely transferred to other entities that

could monetise the assets.

30.23

In certain jurisdictions, large, deep and active repo markets do not exist for eligible asset classes, and therefore such assets are likely to be monetised through outright sale. In these circumstances, a bank must 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 requirements to hold such assets, including, but not limited to, statutory minimum inventory requirements for market-making.

30.24

Banks must not include in the stock of HQLA any assets, or liquidity generated from assets, 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.[6]

1 Footnote

6 *Refer to LCR40.79 for the appropriate treatment if the contractual withdrawal of such assets would lead to a short position (eg because the bank had used the assets in longer-term securities financing transactions).*

30.25

Assets received as collateral for derivatives 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 as set out in LCR40.49.

30.26

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 and thus contribute to the smooth functioning of payment and settlement systems. Banks and regulators should be aware that the LCR stress scenario does not cover expected or unexpected intraday liquidity needs.

30.27

While the LCR must be met and reported in a single currency, banks should be able to meet their liquidity needs in each currency and maintain HQLA consistent with the distribution of their liquidity needs by currency. The bank should be able to use the stock to generate liquidity in the currency and jurisdiction in which the net cash outflows arise. As such, the LCR by currency should be monitored and reported to allow the bank and its supervisor to track any potential currency mismatch issues that could arise, as outlined in SRP50. In managing foreign exchange liquidity risk, the bank should take into account the risk that its ability to swap currencies and access the relevant foreign exchange markets may erode rapidly under stressed conditions. It 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.

30.28

In order to mitigate cliff effects that could arise, if an eligible liquid asset became ineligible (eg due to rating downgrade), a bank is permitted to keep such assets in its stock of liquid assets

for an additional 30 calendar days. This would allow the bank additional time to adjust its stock as needed or replace the asset.

Diversification of the stock of HQLA

30.29

The stock of HQLA should be well diversified within the asset classes themselves (except for sovereign debt of the bank's home jurisdiction or from the jurisdiction in which the bank operates; central bank reserves; central bank debt securities; and cash). Although some asset classes are more likely to remain liquid irrespective of circumstances, ex ante it is not possible to know with certainty which specific assets within each asset class might be subject to shocks ex post. Banks should therefore have policies and limits in place in order to avoid concentration with respect to asset types, issue and issuer types, and currency (consistent with the distribution of net cash outflows by currency) within asset classes.

Definition of HQLA

30.30

The stock of HQLA should comprise assets with the characteristics outlined in LCR30.2 to LCR30.12. This section describes the type of assets that meet these characteristics and can therefore be included in the stock.

30.31

There are two categories of assets that can be included in the stock. Assets to be included in each category are those that the bank is holding on the first day of the stress period, 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.

30.32

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 Committee has developed alternative treatments for holdings in the stock of HQLA, which are expected to apply to a limited number of currencies and jurisdictions. These alternative treatments and the eligibility criteria are set out in LCR31.

30.33

Supervisors may also choose to include within Level 2 an additional class of assets (Level 2B assets). If included, these assets must not comprise more than 15% of the total stock of HQLA. They must also be included within the overall 40% cap on Level 2 assets.

30.34

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

30.35

The maximum amount of adjusted Level 2 assets 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.[7]

1 Footnote

[7] *When determining the calculation of the 15% and 40% caps, supervisors may, as an additional requirement, separately consider the size of the pool of Level 2 and Level 2B assets on an unadjusted basis.*

30.36

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

30.37

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 LCR30.13 to LCR30.25. 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 LCR30.13 to LCR30.25. 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 LCR30.13 to LCR30.25. In cases where collateral received in a short-term secured lending or collateral swap transaction would meet the operational requirements if held unencumbered, but has been rehypothecated in a short-term secured funding or collateral swap transaction, both transactions must be unwound for the purpose of calculating the adjusted HQLA amounts. In this context, short-term transactions are transactions with a maturity date up to and including 30 calendar days. Relevant haircuts must be applied prior to calculation of the respective caps.

30.38

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

$$Stock\ of\ HQLA = Level 1 + Level 2A + Level 2B - Adjustment\ for\ 15\%\ cap - Adjustment\ for\ 40\%\ cap$$

30.39

In the formula in LCR30.38, the adjustments for the 15% and the 40% are calculated as follows:

$$Adjustment\ for\ 15\%\ cap = max\left(\left(\begin{array}{l} adjusted\ Level\ 2B - \\ \frac{15}{85} \times \left(adjusted\ Level\ 1 + adjusted\ Level\ 2A\right) \end{array}\right), \left(\begin{array}{l} adjusted\ Level\ 2B - \\ \frac{15}{60} \times \left(adjusted\ Level\ 1\right) \end{array}\right), 0\right)$$

$$Adjustment\ for\ 40\%\ cap = max\left(\left(\begin{array}{l} adjusted\ Level\ 2A + \\ adjusted\ Level\ 2B - \\ Adjustment\ for\ 15\%\ cap \end{array}\right) - \frac{2}{3}\left(adjusted\ Level\ 1\right), 0\right)$$

Level 1 assets

30.40

Level 1 assets can comprise an unlimited share of the pool and are not subject to a haircut under the LCR.[8] However, national supervisors may wish to require haircuts for Level 1 securities based on, among other things, their sensitivity to interest rate and market risk, credit and liquidity risk, and typical repo haircuts.

1 Footnote

8 *For purpose of calculating the LCR, Level 1 assets in the stock of HQLA must be measured at an amount no greater than their current market value.*

30.41

Level 1 assets are limited to:

1. coins and banknotes;
2. central bank reserves (including required reserves),[9] to the extent that the central bank policies allow them to be drawn down in times of stress;[10]
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, the European Stability Mechanism, the European Financial Stability Facility or multilateral development banks,[11] and satisfying all of the following conditions:
    1. assigned a 0% risk weight under the standardised approach to credit risk;[12]
    2. traded in large, deep and active repo or cash markets, characterised by a low level of concentration;
    3. have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions; and
    4. not an obligation of a financial institution or any of its affiliated entities.[13]
4. 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
5. 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.

5 Footnotes, 2 FAQs

9 *In this context, central bank reserves would include banks' overnight deposits with the central bank, and term deposits with the central bank: (i) that are explicitly and contractually repayable on notice from the depositing bank; or (ii) that constitute a loan against which the bank can borrow on a term basis or on an overnight but automatically renewable basis (only where the bank has an existing deposit with the relevant central bank). Other term deposits with central banks are not eligible for the stock of HQLA; however, if the term expires within 30 days, the term deposit could be considered as an inflow per LCR40.87.*

10 *Local supervisors should discuss and agree with the relevant central bank the extent to which central bank reserves should count towards the stock of liquid assets, ie the extent to which reserves are able to be drawn down in times of stress.*

11 *The Basel III liquidity framework follows the categorisation of market participants applied in CRE20, unless otherwise specified.*

12 *This paragraph includes only marketable securities that qualify for CRE20.7. When a 0% risk-weight has been assigned at national discretion according to the provision in CRE20.8, the treatment should follow LCR30.41(4) or LCR30.41(5).*

13 *This requires that the holder of the security must not have recourse to the financial institution or any of the financial institution's affiliated entities. In practice, this means that securities, such as government-guaranteed issuance during the financial crisis, which remain liabilities of the financial institution, would not qualify for the stock of HQLA. The only exception is when the bank also qualifies as a PSE under CRE20 where securities issued by the bank could qualify for Level 1 assets if all necessary conditions are satisfied.*

FAQ1 *Does "the sovereign" in LCR30.41(4) and LCR30.41(5) refer to the bank's home country, host country, the country in which the bank does not have any presence but has liquidity risk exposure denominated in that currency, or all of them?*
Sovereign and central bank debt securities, even with a rating below AA–, should be considered eligible as Level 1 assets only when these assets are issued by the sovereign or central bank in the bank's home country or in host countries where the bank has a presence via a subsidiary or branch. Therefore, LCR30.41(4) and LCR30.41(5) do not apply to a country in which the bank's only presence is liquidity risk exposures denominated in the currency of that country.

FAQ2 *In LCR30.41(5), could a bank use non-0% risk-weighted sovereign or central bank debt securities issued in foreign currencies to offset the amount of that specific foreign currency exposure in a country other than the issuing sovereign's or central bank's home country?*
In LCR30.41(5), the amount of non-0% risk-weighted sovereign/central bank debt issued in foreign currencies included in Level 1 is strictly limited to the foreign currency exposure in the jurisdiction of the issuing sovereign/central bank.

Level 2 assets

30.42

Level 2 assets (comprising Level 2A assets and any Level 2B assets permitted by the supervisor) 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 method for calculating the cap on Level 2 assets and the cap on Level 2B assets is set out in LCR30.34 to LCR30.39.

30.43

A 15% haircut is applied to the current market value of each Level 2A asset held in the stock of HQLA. Level 2A assets are limited to the following:

1. Marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs or multilateral development banks that satisfy all of the following conditions:[14]
    1. assigned a 20% risk weight under CRE20;
    2. traded in large, deep and active repo or cash markets characterised by a low level of concentration;
    3. have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions (ie 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
    4. not an obligation of a financial institution or any of its affiliated entities.[15]
2. Corporate debt securities (including commercial paper)[16] and covered bonds[17] that satisfy all the following conditions:
    1. in the case of corporate debt securities: not issued by a financial institution or any of its affiliated entities;
    2. in the case of covered bonds: not issued by the bank itself or any of its affiliated entities;
    3. either:
    (i)

    have a long-term credit rating from a recognised external credit assessment institution (ECAI) of at least AA-[18] or in the absence of a long-term rating, a short-term rating equivalent in quality to the long-term rating; or

    (ii)

    do not have a credit assessment by a recognised ECAI but are internally rated as having a probability of default (PD) corresponding to a credit rating of at least AA-;

    4. traded in large, deep and active repo or cash markets characterised by a low level of concentration; and
    5. have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions: ie maximum decline of price or increase in haircut over a 30-day period during a relevant period of significant liquidity stress not exceeding 10%.

5 Footnotes, 1 FAQ

14 *LCR30.41(4) or LCR30.41(5) may overlap with LCR30.43(1) in terms of sovereign and central bank securities with a 20% risk weight. In such a case, the assets can be assigned to the Level 1 category according to LCR30.41(4) or LCR30.41(5), as appropriate.*

15 *This requires that the holder of the security must not have recourse to the financial institution or any of the financial institution's affiliated entities. In practice, this means that securities, such as government-guaranteed issuance during the financial crisis, which remain liabilities of the financial institution, would not qualify for the stock of HQLA. The only exception is when the bank also qualifies as a PSE under CRE20 where securities issued by the bank could qualify for Level 1 assets if all necessary conditions are satisfied.*

16 *Corporate debt securities (including commercial paper) in this respect include only plain-vanilla assets whose valuation is readily available based on standard methods and does not depend on private knowledge, ie these do not include complex structured products or subordinated debt.*

17 *Covered bonds are bonds issued and owned by a bank or mortgage institution and are subject by law to special public supervision designed to protect bondholders. Proceeds deriving from the issue of these bonds must be invested in conformity with the law in assets which, during the whole period of the validity of the bonds, are capable of covering claims attached to the bonds and which, in the event of the failure of the issuer, would be used on a priority basis for the reimbursement of the principal and payment of the accrued interest.*

18 *In the event of split ratings, the applicable rating should be determined according to the method used in the standardised approach for credit risk. Local rating scales (rather than international ratings) of a supervisor-approved ECAI that meet the eligibility criteria outlined in CRE21.2 can be recognised if corporate debt securities or covered bonds are held by a bank for local currency liquidity needs arising from its operations in that local jurisdiction. This also applies to Level 2B assets.*

FAQ1 *While corporate debt securities with a rating between A+ and BBB– whose maximum decline of price does not exceed 20% may be included in Level 2B according to LCR30.45(2), and corporate debt securities with a rating of at least AA– whose maximum decline of price does not exceed 10% may be included in Level 2A according to LCR30.43(2), there is no explicit assignment of corporate debt securities with a rating of at least AA– whose maximum decline of price is between 10 and 20%?*
Corporate debt securities with a rating of at least AA– whose maximum decline of price or increase in haircuts over a 30-day period during a relevant period of significant liquidity stress is between 10 and 20% may count towards Level 2B assets provided that they meet all other requirements stated in LCR30.45(2).

Level 2B assets

30.44

Certain additional assets (Level 2B assets) may be included in Level 2 at the discretion of national authorities. In choosing to include these assets in Level 2 for the purpose of the LCR,

supervisors must ensure that such assets fully comply with the qualifying criteria. Supervisors should also ensure that banks have appropriate systems and measures to monitor and control the potential risks (eg credit and market risks) that banks could be exposed to in holding these assets.

30.45

A larger haircut is applied to the current market value of each Level 2B asset held in the stock of HQLA. Level 2B assets are limited to the following:

1. Residential mortgage backed securities (RMBS) that satisfy all of the following conditions may be included in Level 2B, subject to a 25% haircut:
    1. not issued by, and the underlying assets have not been originated by, the bank itself or any of its affiliated entities;
    2. have a long-term credit rating from a recognised ECAI of AA or higher, or in the absence of a long-term rating, a short-term rating equivalent in quality to the long-term rating;
    3. traded in large, deep and active repo or cash markets characterised by a low level of concentration;
    4. have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions, ie 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;
    5. the underlying asset pools are restricted to residential mortgages and cannot contain structured products;
    6. the underlying mortgages are “full recourse” loans (ie 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
    7. the securitisations are subject to “risk retention” regulations which require issuers to retain an interest in the assets they securitise.
2. Corporate debt securities (including commercial paper)[19] that satisfy all of the following conditions may be included in Level 2B, subject to a 50% haircut:
    1. not issued by a financial institution or any of its affiliated entities;
    2. either:
    (i)

    have a long-term credit rating from a recognised ECAI of at least BBB- or in the absence of a long-term rating, a short-term rating equivalent in quality to the long-term rating; or

    (ii)

    do not have a credit assessment by a recognised ECAI but are internally rated as having a PD corresponding to a credit rating of at least BBB-;

    3. traded in large, deep and active repo or cash markets characterised by a low level of concentration; and
    4. have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions, ie 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.

3. Common equity shares that satisfy all of the following conditions may be included in Level 2B, subject to a 50% haircut:
    1. not issued by a financial institution or any of its affiliated entities;
    2. exchange-traded and centrally cleared;
    3. a constituent of major stock index (or indices) of the home jurisdiction where the liquidity risk is taken, as decided by the supervisor in the jurisdiction where the index is located;
    4. 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;
    5. traded in large, deep and active repo or cash markets characterised by a low level of concentration; and
    6. have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions, ie a maximum decline of price not exceeding 40% or increase in haircut over a 30-day period not exceeding 40 percentage points during a relevant period of significant liquidity stress.

1 Footnote, 8 FAQs

19 *Corporate debt securities (including commercial paper) in this respect include only plain-vanilla assets whose valuation is readily available based on standard methods and does not depend on private knowledge, ie these do not include complex structured products or subordinated debt.*

FAQ1 *Does the maximum LTV criterion of 80% mean that the average pool LTV is to be less than 80% or that each loan has to have less than 80% LTV?*
The LTV requirement in LCR30.45(1) refers to the weighted average (by loan balance) LTV of the portfolio of underlying mortgages, not to any individual mortgage, ie mortgages that have an LTV greater than 80% are not excluded per se.

FAQ2 *Does "at issuance" in LCR30.45(1) refer to the issuance of the RMBS or of the underlying mortgages?*
"At issuance" refers to the time when the RMBS are issued, ie the average LTV of the underlying mortgages at the time of the issuance of the RMBS must not be higher than 80%.

FAQ3 *While corporate debt securities rated BBB+ to BBB– may be included in Level 2B according to LCR30.45(2), there is no explicit assignment of sovereign debt securities with such a rating. How should those securities be treated?*
Sovereign and central bank debt securities rated BBB+ to BBB– that are not included in the definition of Level 1 assets according to LCR30.41(4) or LCR30.41(5) may be included in the definition of Level 2B assets with a 50% haircut within the 15% cap for all Level 2B assets.

FAQ4 *Securities representing claims on PSEs are not part of the definition of Level 2B assets in LCR30.45. Can such securities from PSEs whose risk weight under the standardised approach for credit risk is higher than 20%, but which have a rating of at least BBB– and whose maximum price decline does not exceed 20% still be classified as Level 2B?*
Yes, PSE debt securities with a rating of at least BBB– whose maximum decline of price or increase in haircuts over a 30-day period during a relevant period of significant liquidity stress does not exceed 20% may count towards Level 2B assets provided that they meet all other requirements stated in LCR30.45(2).

FAQ5 *LCR30.45(3)(c) refers to a "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". It is not clear what is meant by "taking a risk".*
Equities that are a constituent of a major stock index can only be assigned to the stock of HQLA if the stock index is located within the home jurisdiction of the bank or if the bank has liquidity risk exposure through a branch or other legal entity in that jurisdiction.

FAQ6 *When considering which common equity shares might satisfy the criteria for Level 2B assets of a maximum decline of share price not exceeding 40% over a "relevant period of significant liquidity stress", we assume that this criterion does not need to be applied for time periods prior to the shares' inclusion in the major index. Indicators of volatility prior to the shares' inclusion in the index will not be representative of current or future pricing.*
The criterion must be satisfied by all equity shares that enter the stock of HQLA. A consistent stressed period should be used for justification and whether the share was part of the index during that timeframe is not relevant.

FAQ7 *LCR30.45(3)(f) only allows equity securities that have not experienced a 40% drop in price during a 30-day period. Most stocks with a long history have dropped more than 40% (eg via crashes in 1999, 2002, 2009). In our study we saw that only young companies with a short history on the market qualify for this requirement. Hence, young risky stocks can be included but not the more stable companies/stocks. Was this really the intention?*
Determining the appropriate stress period for meeting market performance requirements is a matter of national discretion. However, it is not the intention of the Basel Committee to exclude all established companies and include only young companies.

FAQ8 *Equities eligible as Level 2B HQLA must be a constituent of a major stock index as decided by the supervisor in the jurisdiction where the index is located. Could confirmation be given on a centralised basis by the Basel Committee as to which indices are deemed to be "major" ones?*
The issue is the responsibility of national authorities. The Basel Committee will not provide such a list.

30.46

In addition, supervisors may choose to include within Level 2B assets the undrawn value of any contractual committed liquidity facility (CLF) provided by a central bank, where this has not already been included in HQLA in accordance with LCR31.12. When including such facilities within Level 2B assets, the following conditions apply:

1. The facility (termed a restricted-use committed liquidity facility, or RCLF) must, in normal times, be subject to a commitment fee on the total (drawn and undrawn) facility amount

that is at least the greater of:

1. 75 basis points per annum; or
2. at least 25 basis points per annum above the difference in yield on the assets used to secure the RCLF and the yield on a representative portfolio of HQLA after adjusting for any material differences in credit risk.

2. In periods of market-wide stress the commitment fee on the RCLF (drawn and undrawn amount) may be reduced, but remain subject to the minimum requirements applicable to CLFs used by countries with insufficient HQLA (set out in LCR31).
3. The RCLF must be supported by unencumbered collateral of a type specified by the central bank. The collateral must be held in a form which supports immediate transfer to the central bank should the facility need to be drawn and sufficient (post-haircut) to cover the total size of the facility. Collateral used to support a RCLF cannot simultaneously be used as part of HQLA.
4. Conditional on the bank being assessed to be solvent, the RCLF contract must otherwise be irrevocable prior to maturity and involve no other ex post credit decision by the central bank. The commitment period must exceed the 30-day stress period stipulated by the LCR framework.
5. Central banks that offer RCLFs to banks in their jurisdiction should disclose their intention to do so and, to the extent that facilities are not available to all banks in the jurisdiction, to which class(es) of banks they may be offered. National authorities should also disclose whether RCLFs (offered domestically, or by central banks in other jurisdictions) are able to be included within the HQLA of banks within their jurisdiction. National authorities should disclose when they consider there to be a market-wide stress that justifies an easing of the RCLF terms.

Treatment of Shari’ah compliant banks

30.47

Shari’ah compliant banks face a religious prohibition on holding certain types of assets, such as interest-bearing debt securities. Even in jurisdictions that have a sufficient supply of HQLA, an insurmountable impediment to the ability of Shari’ah compliant banks to meet the LCR requirement may still exist. In such cases, national supervisors in jurisdictions in which Shari’ah compliant banks operate have the discretion to define Shari’ah compliant financial products (such as Sukuk) as alternative HQLA applicable to such banks only, subject to such conditions or haircuts that the supervisors may require. The intention of this treatment is not to allow Shari’ah compliant banks to hold fewer HQLA. The minimum LCR standard, calculated based on alternative HQLA (post-haircut) recognised as HQLA for these banks, should not be lower than the minimum LCR standard applicable to other banks in the jurisdiction concerned. National supervisors applying such treatment for Shari’ah compliant banks should comply with supervisory monitoring and disclosure obligations similar to those set out in LCR31.

1 FAQ

FAQ 1 *According to LCR30.47, "national supervisors in jurisdictions which Shari'ah compliant banks operate have the discretion to define Shari'ah compliant financial products (such as Sukuk) as alternative HQLA applicable to such banks only". What about Shari'ah-compliant financial products that do not need alternative treatment, ie that meet the operational requirements as set out in LCR30.13 to LCR30.28 as well as the relevant conditions of the corresponding asset type as set out in LCR30.29 to LCR30.31, LCR30.33, LCR30.34, LCR30.40 to LCR30.45 and generally feature the characteristics as set out in LCR30.2 to LCR30.12, can non-Shari'ah compliant banks hold these as HQLA?*
Yes. The limitation to Shari'ah compliant banks applies only to Shari'ah compliant financial products that would not otherwise meet HQLA requirements. For Shari'ah-compliant financial products that meet the requirements for recognition as HQLA as set out above, any bank can count them towards its stock of HQLA. Competent authorities may further specify the HQLA eligibility of Shari'ah compliant financial products in their jurisdictions.

LCR31

Alternative liquidity approaches

This chapter describes alternative liquidity approaches available in jurisdictions with an insufficient supply of Level 1 high-quality liquid assets in their domestic currency.

Version effective as of 15 December 2019

First version in the format of the consolidated framework.

Introduction

31.1

Some jurisdictions may have an insufficient supply of Level 1 high-quality liquid assets (HQLA), or both Level 1 and Level 2 HQLA,[20] in their domestic currency[21] to meet the aggregate demand of banks with significant exposures in this currency. To address this situation, the Basel Committee has developed alternative treatments for holdings in the stock of HQLA, which are expected to apply to a limited number of currencies and jurisdictions.

2 Footnotes

20 *Insufficiency in Level 2 assets alone does not qualify for the alternative treatment.*

21 *For member states of a monetary union with a common currency, that common currency is considered the "domestic currency".*

31.2

Eligibility for such alternative treatment will be judged on the basis of the principles and qualifying criteria set out in LCR31.20 and explained further in LCR31.24 to LCR31.61.

31.3

There are three alternative treatments available:

1. contractual committed liquidity facilities from the relevant central bank, for a fee (Option 1);
2. foreign currency HQLA to cover domestic liquidity needs (Option 2); and
3. additional use of Level 2 assets with a higher haircut (Option 3).

General rules governing the use of alternative liquidity approaches

31.4

Jurisdictions are not limited to one option. However, the usage of any of the above options must be constrained by a limit specified by supervisors in jurisdictions whose currency is eligible for the alternative treatment. The limit should be expressed in terms of the maximum amount of HQLA associated with the use of the options (whether individually or in combination) that a bank is allowed to include in its Liquidity Coverage Ratio (LCR), as a percentage of the total amount of HQLA the bank is required to hold in the currency concerned.[22] HQLA associated with the options refer to:

1. in the case of Option 1, the amount of committed liquidity facilities granted by the relevant central bank, for a fee;
2. in the case of Option 2, the amount of foreign currency HQLA used to cover the shortfall of HQLA in the domestic currency; and
3. in the case of Option 3, the amount of Level 2 assets held (including those within the 40% cap).

1 Footnote

22 *The required amount of HQLA in the domestic currency includes any regulatory buffer (ie above the 100% LCR standard) that the supervisor may reasonably impose on the bank concerned based on its liquidity risk profile.*

31.5

If, for example, the maximum level of usage of the options is set at 80%, it means that a bank adopting the options, either individually or in combination, would only be allowed to include HQLA associated with the options (after applying any relevant haircut) up to 80% of the required amount of HQLA in the relevant currency.[23] Thus, at least 20% of the HQLA requirement would need to be met by Level 1 assets in the relevant currency. The maximum usage of the options is constrained by the bank's actual shortfall of HQLA in the currency concerned.

1 Footnote

23 *For example, if a bank has used Option 1 and Option 3 to the extent that it has been granted an Option 1 facility of 10%, and held Level 2 assets of 55% after haircut (both in terms of the required amount of HQLA in the domestic currency), the HQLA associated with the use of these two options amount to 65% (ie 10%+55%), which is still within the 80% level. The total amount of alternative HQLA used is 25% (ie 10% + 15%; additional Level 2A assets used).*

31.6

The maximum level of usage should be consistent with the projected size of the HQLA shortfall faced by banks subject to the LCR in the currency concerned, taking into account all relevant factors that may affect the size of the shortfall over time. The supervisor should explain how this level is derived, and justify why this is supported by insufficient HQLA in the banking system.

31.7

A bank must keep its supervisor informed of its usage of the options so as to enable the supervisor to manage the aggregate usage of the options in the jurisdiction and to monitor, where necessary, that banks using such options observe the relevant supervisory requirements.

31.8

While bank-by-bank approval by the supervisor is not required for use of the alternative liquidity approaches, individual supervisors may still consider providing specific approval for banks to use the options should this be warranted based on their jurisdiction-specific circumstances. For example, use of Option 1 will typically require central bank approval of the committed facility.

31.9

In general, a bank that needs to use the options should not be allowed to use such options above the level required to meet its LCR (including any reasonable buffer above the 100% standard that may be imposed by the supervisor), however supervisors may consider whether this should be accommodated under certain circumstances. Banks may wish to do so for a number of reasons. For example, they may want to have an additional liquidity facility in anticipation of tight market conditions. Supervisors should have a process (eg through periodic

reviews) for ensuring that the alternative HQLA held by banks are not excessive compared with their actual need. In addition, banks should not intentionally replace their stock of Level 1 or Level 2 assets with ineligible assets to create a larger liquidity shortfall for economic reasons or otherwise.

31.10

A bank must demonstrate that it has taken reasonable steps to use Level 1 and Level 2 assets and reduce the amount of liquidity risk (as measured by reducing net cash outflows in the LCR) to improve its LCR, before applying an alternative treatment. Holding an HQLA portfolio is not the only way to mitigate a bank's liquidity risk. For example, a bank could improve the matching of its assets and liabilities, attract stable funding sources, or reduce its longer-term assets. Banks should not treat the use of the options simply as an economic choice that maximises the profits of the bank through the selection of alternative HQLA based primarily on yield considerations. The liquidity characteristics of an alternative HQLA portfolio should be considered to be more important than its net yield.

31.11

In order to ensure that banks' usage of the options is not out of line with the availability of Level 1 assets within the jurisdiction, supervisors may set a minimum amount of Level 1 assets to be held by each bank that is consistent with the availability of Level 1 assets in the market. A bank must then ensure that it is able to hold and maintain Level 1 assets not less than the minimum amount when applying the options.

Option 1 – Contractual committed liquidity facilities from the relevant central bank, for a fee

31.12

Under Option 1, banks may access contractual committed liquidity facilities provided by the relevant central bank (ie relevant given the currency in question) for a fee. These committed liquidity facilities should be distinct and separate from regular central bank standing arrangements, as these committed liquidity facilities must meet certain criteria. In particular, these facilities must be established 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 must not involve an ex post credit decision by the central bank. Such facilities must also incur a fee for the facility which is charged regardless of the amount, if any, drawn down against that facility; and the fee must be set so that both banks that claim the facility to meet the LCR and banks that do not have similar financial incentives to reduce their exposure to liquidity risk. That is, the fee should be set so that the net yield on the assets used to secure the facility should not be higher than the net yield on a representative portfolio of Level 1 and Level 2 assets, after adjusting for any material differences in credit risk. A jurisdiction seeking to adopt Option 1 should justify that the fee is suitably set in a manner as prescribed in this paragraph.

Option 2 – Foreign currency HQLA to cover domestic liquidity needs

31.13

Under Option 2, supervisors may permit banks that evidence a shortfall of HQLA in the domestic currency (ie insufficient domestic currency HQLA relative to domestic currency liquidity risk) to hold HQLA in a currency that does not match the currency of the associated

liquidity risk. However, the resulting currency mismatch positions must be justifiable and controlled within limits agreed by their supervisors. Supervisors should restrict such positions within levels consistent with the bank's foreign exchange risk management capacity and needs and ensure that such positions relate to currencies that are freely and reliably convertible, are effectively managed by the bank, and would not pose undue risk to its financial strength. In managing those positions, the bank should take into account the risk that its ability to swap currencies and its access to the relevant foreign exchange markets may erode rapidly under stressed conditions. It should also take into account that sudden, adverse exchange rate movements could sharply widen existing mismatch positions and alter the effectiveness of any foreign exchange hedges in place.

31.14

To account for foreign exchange risk associated with foreign currency HQLA used to cover liquidity needs in the domestic currency, such liquid assets must be subject to a minimum haircut of 8% for major currencies that are active in global foreign exchange markets.[24] For other currencies, jurisdictions should increase the haircut to an appropriate level on the basis of historical (monthly) exchange rate volatilities between the currency pair over an extended period of time.[25] If the domestic currency is formally pegged to another currency under an effective mechanism, the haircut for the pegged currency may be lowered to a level that reflects the limited exchange rate risk under the peg arrangement. To qualify for this treatment, the jurisdiction concerned should demonstrate the effectiveness of its currency peg mechanism and assess the long-term prospect of keeping the peg.

2 Footnotes

24 *These refer to currencies that exhibit significant and active market turnover in the global foreign currency market (eg the average market turnover of the currency as a percentage of the global foreign currency market turnover over a ten-year period is not lower than 10%).*

25 *As an illustration, the exchange rate volatility data used for deriving the foreign exchange haircut may be based on the 30-day moving foreign exchange price volatility data (mean + 3 standard deviations) of the currency pair over a ten-year period, adjusted to align with the 30-day time horizon of the LCR.*

31.15

Haircuts for foreign currency HQLA used under Option 2 must apply to HQLA in excess of a threshold specified by supervisors which must not be greater than 25%.[26] This is to accommodate a certain level of currency mismatch that may commonly exist among banks in their ordinary course of business.

1 Footnote

26 *The threshold for applying the haircut under Option 2 refers to the amount of foreign currency HQLA used to cover liquidity needs in the domestic currency as a percentage of total net cash outflows in the domestic currency. Hence under a threshold of 25%, a bank using Option 2 must apply the haircut to that portion of foreign currency HQLA in excess of 25% that are used to cover liquidity needs in the domestic currency.*

31.16

A bank using Option 2 must demonstrate that its foreign exchange risk management system is able to measure, monitor and control the foreign exchange risk resulting from the currency-mismatched HQLA positions. In addition, the bank must show that it can reasonably convert the currency-mismatched HQLA to liquidity in the domestic currency when required, particularly in a stress scenario. To mitigate the risk that excessive currency mismatch may interfere with the objectives of the framework, the bank supervisor should only allow banks that are able to measure, monitor and control the foreign exchange risk arising from the currency mismatched HQLA positions to use this option. As the HQLA that are eligible under Option 2 can be denominated in different foreign currencies, banks must assess the convertibility of those foreign currencies in a stress scenario. As participants in the foreign exchange market, they are in the best position to assess the depth of the foreign exchange swap or spot market for converting those assets to the required liquidity in the domestic currency in times of stress. The supervisor should also restrict the currencies of the assets that are eligible under Option 2 to those that have been historically proven to be convertible into the domestic currency in times of stress.

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

31.17

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. Under this option, supervisors may permit banks that evidence a shortfall of HQLA in the domestic currency (ie relative to domestic currency liquidity risk) to hold additional Level 2A assets in the stock of HQLA. These additional Level 2A assets must be subject to a minimum haircut of 20%, ie 5% higher than the 15% haircut applicable to Level 2A assets that are included in the 40% cap. The higher haircut should cover any additional price and market liquidity risks arising from increased holdings of Level 2A assets beyond the 40% cap and provide a disincentive for banks to use this option based on yield considerations.[27] Supervisors must conduct an analysis to assess whether the additional haircut is sufficient for Level 2A assets in their markets, and should increase the haircut if this is warranted to achieve the purpose for which it is intended. Supervisors should explain and justify the outcome of the analysis (including the level of increase in the haircut, if applicable). Any Level 2B assets held by the bank must remain subject to the cap of 15%, regardless of the amount of other Level 2 assets held.

1 Footnote

27 *Supervisors should seek to avoid a situation where the cost of holding a portfolio that benefits from this option is lower than the cost of holding a theoretical compliant portfolio of Level 1 and Level 2 assets, after adjusting for any material differences in credit risk.*

31.18

A bank using Option 3 must be able to manage the price risk associated with the additional Level 2A assets. As the quality of Level 2A assets is lower than that for Level 1 assets, increasing its composition would increase the price risk and hence the volatility of the bank’s stock of HQLA. To mitigate the uncertainty of performance of this option, banks must demonstrate that the values of the assets under stress are sufficient. At a minimum, they must be able to conduct stress tests to ascertain that the value of its stock of HQLA remains sufficient to support its LCR during a market-wide stress event. The bank should take a higher haircut (ie higher than the supervisor-imposed Option 3 haircut) on the value of the Level 2A

assets if the stress test results suggest that the minimum haircut imposed by supervisors would be insufficient to cover the assets' price and market liquidity risks.

31.19

A bank using Option 3 must show that it can reasonably liquidate the additional Level 2A assets in a stress scenario. With additional reliance on Level 2A assets, it is essential to ensure that the market for these assets has sufficient depth. This standard may be implemented in several ways, but should be more severe than the requirements associated with Level 2 assets within the 40% cap, because increased reliance on Level 2A assets would increase concentration risk on an aggregate level, thus affecting market liquidity. The supervisor may:

1. require that Level 2A assets that exceed the 40% cap meet higher qualifying criteria (eg minimum credit rating of AA+ or AA instead of AA-, central bank eligible);
2. set a limit on the minimum issue size of the Level 2A assets that qualify for use under this option;
3. set a limit on the bank's maximum holding as a percentage of the issue size of the qualifying Level 2A asset;
4. set a limit on the maximum bid-ask spread, minimum volume, or minimum turnover of the qualifying Level 2A asset; and
5. any other criteria appropriate for the jurisdiction.

Principles for assessing eligibility for alternative liquidity approaches

31.20

All of the following principles must be satisfied in order for a jurisdiction to qualify for alternative treatment.

1. To use the alternative treatment under the LCR, a jurisdiction must demonstrate and justify that insufficient HQLA denominated in the domestic currency exists, taking into account all relevant factors affecting the supply of, and demand for, such HQLA (Principle 1).
    1. The supply of HQLA in the domestic currency of the jurisdiction must be insufficient, in terms of Level 1 assets only or both Level 1 and Level 2 assets, to meet the aggregate demand for such assets from banks operating in that currency. The jurisdiction must be able to provide adequate information (quantitative and otherwise) to demonstrate this aggregate shortfall.
    2. The determination of insufficient HQLA by the jurisdiction under LCR31.20(1)(a) should address all major factors relevant to the issue. These include, but are not limited to, the expected supply of HQLA in the medium term (eg three to five years), the extent to which the banking sector can and should run less liquidity risk, and the competing demand from banks and non-bank investors for holding HQLA for similar or other purposes.
    3. Insufficient HQLA faced by the jurisdiction must be caused by structural, policy and other constraints that cannot be resolved within the medium term (eg three to five years). Such constraints may relate to the fiscal or budget policies of the jurisdiction, the infrastructural development of its capital markets, the structure of its monetary system and operations (eg the currency board arrangements for jurisdictions with pegged exchange rates), or other jurisdiction-specific factors leading to the shortage or imbalance in the supply of HQLA available to the banking sector.

2. A jurisdiction that intends to adopt one or more of the options for alternative treatment must be capable of limiting the uncertainty of performance, or mitigating the risks of non-performance, of the option(s) concerned (Principle 2).
    1. For Option 1 (ie the provision of contractual committed liquidity facilities from the relevant central bank for a fee), the jurisdiction must have the economic strength to support the committed liquidity facilities granted by its central bank. To ensure this, the jurisdiction should have a process in place to control the aggregate amount of such facilities to within a level that can be measured and managed.
    2. For Option 2 (ie use of foreign currency HQLA to cover domestic currency liquidity needs), the jurisdiction must have a mechanism in place to control the foreign exchange risk of its banks' foreign currency HQLA holdings.
    3. For Option 3 (ie use of Level 2A assets beyond the 40% cap with a higher haircut), the jurisdiction must only allow Level 2 assets that are of a quality (credit and liquidity) comparable to that for Level 1 assets in its currency to be used under this option. The jurisdiction should be able to provide quantitative and qualitative evidence to substantiate this requirement.
3. A jurisdiction that intends to adopt one or more of the options for alternative treatment must be committed to observing all of the obligations set out below (Principle 3).
    1. The jurisdiction must maintain a supervisory monitoring system to ensure that its banks comply with the rules and requirements relevant to their usage of the options, including any associated haircuts, limits or restrictions.
    2. The jurisdiction must document and update its approach to adopting an alternative treatment, and make the approach explicit and transparent to other national supervisors. The approach should address how it complies with the applicable criteria, limits and obligations set out in the qualifying principles, including the determination of insufficient HQLA and other key aspects of its framework for alternative treatment.
    3. The jurisdiction must review periodically the determination of insufficient HQLA at intervals not exceeding five years, and disclose the results of review and any consequential changes to other national supervisors and stakeholders.
    4. The jurisdiction must permit an independent peer review of its framework for alternative treatment to be conducted as part of the Basel Committee's work programme and address the comments made.

31.21

The eligibility for a jurisdiction to adopt an alternative liquidity approach treatment should be based on a fully implemented LCR standard (ie 100% requirement).

31.22

The principles in LCR31.20 may not, in all cases, be able to capture specific circumstances or unique factors affecting individual jurisdictions having insufficient HQLA. Hence, a jurisdiction may provide additional information or explain other factors that are relevant to its compliance with the Principles, even though such information or factors may not be specified in the Principles.

31.23

Where a jurisdiction uses estimations or projections to support its case to use alternative liquidity approaches, the rationale and basis for those estimations or projections should be clearly set out. In order to support its case and facilitate independent peer review, the

jurisdiction should provide information, to the extent possible, covering a long enough time series (eg three to five years depending on data availability).

Guidance on meeting Principle 1 – insufficiency of HQLA

31.24

In order to qualify for alternative treatment, the jurisdiction must be able to demonstrate that there is an HQLA shortfall in the domestic currency as it relates to the needs in that currency. The jurisdiction must demonstrate this with regard to the three criteria set out above.

31.25

LCR31.20(1)(a) requires the jurisdiction to provide sufficient information to demonstrate the insufficient HQLA in its domestic currency. This insufficiency must principally reflect a shortage in Level 1 assets, although Level 2 assets may also be insufficient in some jurisdictions.

31.26

To illustrate that a currency does not have sufficient HQLA, the jurisdiction must provide all relevant information and data that have a bearing on the size of the HQLA shortfall faced by banks operating in that currency that are subject to LCR requirements ("LCR banks"). These should, to the extent practicable, include the following information.

1. The current and projected stock of HQLA denominated in its currency,[28] including:
    1. the supply of Level 1 and Level 2 assets broken down by asset classes;
    2. the amounts outstanding for the last three to five years;
    3. the projected amounts for the next three to five years; and
    4. any other information in support of its stock and projection of HQLA, including, should the jurisdiction feel that the true nature of the supply of HQLA cannot be simply reflected by the numbers provided, further information to explain sufficiently the case.
2. The jurisdiction should provide a detailed analysis of the nature of the market for the above assets. Information relating to the market liquidity of the assets would be of particular importance. The jurisdiction should present its views on the liquidity of the HQLA based on the information presented. The following details should be provided:
    1. for the primary market for the above assets:
    (i)

    the channel and method of issuance;

    (ii)

    the issuers;

    (iii)

    the past issue tenor, denomination and issue size for the last three to five years; and

    (iv)

    the projected issue tenor, denomination and issue size for the next three to five

years;

2. for the secondary market for the above assets:
   (i)

   the trading size and activity;

   (ii)

   types of market participants; and

   (iii)

   the size and activity of its repo market; and

3. where possible, the jurisdiction should provide an estimate of the amount of the above assets (Level 1 and Level 2) required to be in free circulation for them to remain genuinely liquid, as well as any justification for these figures.

3. With regard to demand for HQLA by LCR banks, the jurisdiction should provide:
   1. the number of LCR banks under its purview;
   2. the current demand (ie net 30-day cash outflows) for HQLA by these LCR banks for meeting the LCR or other requirements (eg collateral for intraday repo);
   3. the projected demand for the next three to five years based on banks' business growth and strategy;
   4. an estimate of the percentage of total HQLA already in the hands of banks; and
   5. commentaries on cash flow projections where appropriate to improve their persuasiveness. The projections should take into account observed behavioural changes of the LCR banks and any other factors that may result in a reduction of their 30-day cash outflows.

4. The jurisdiction may provide information on the demand for Level 1 and Level 2 assets by the other HQLA holders in support of its application. These entities are not subject to the LCR but will likely take up, or hold on to, a part of the outstanding stock of HQLA. Such entities include: banks, branches of banks and other deposit-taking institutions which conduct bank-like activity (such as building societies and credit unions) in the jurisdiction but are not subject to the LCR: other financial institutions which are normally subject to prudential supervision, such as investment or securities firms, insurance or reinsurance companies, pension / superannuation funds, mortgage funds, and money market funds; and other significant investors which have demonstrated a track record of strategic "buy and hold" purchases which can be presumed to be price-insensitive. This would include foreign sovereigns, foreign central banks and foreign sovereign / quasi-sovereign funds, but not hedge funds or other private investment management vehicles. Historical demand for such assets by these holders is not sufficient. The alternate holders of HQLA must at least exhibit the following qualities:
   1. price-inelastic: the holders of HQLA are unlikely to switch to alternate assets unless there is a significant change in the price of these assets; and
   2. proven to be stable: the demand for HQLA by the holders should remain stable over the next three years as they require these assets to meet specific purposes, such as asset-liability matching or other regulatory requirements.

1 Footnote

[28] *To avoid doubt, if the jurisdiction is a member of a monetary union operating under a single currency, debt or other assets issued in other members of the union in that currency is considered available for all jurisdictions in that union. Hence, the jurisdiction should take into account the availability of such assets which qualify as HQLA in its analysis.*

31.27

The jurisdiction should be able to come up with a reasonable estimate of the HQLA shortfall faced by its LCR banks (current and over the next three to five years), based on credible information. In deriving the HQLA shortfall, the jurisdiction should first compare:

1. the total outstanding stock of its HQLA in domestic currency; with
2. the total liquidity needs of its LCR banks in domestic currency.

31.28

The jurisdiction should then explain the method of deriving the HQLA shortfall, taking into account all relevant factors, including those set out in LCR31.20(1)(b), which may affect the size of the shortfall. A detailed analysis of the calculations should be provided (eg in the form of a template), explaining any adjustments to supply and demand and justifications for such adjustments.[29] The jurisdiction should demonstrate that the method of defining insufficiency is appropriate for its circumstances, and that it can reflect the HQLA shortfall faced by LCR banks in the currency.

1 Footnote

[29] *For HQLA that are subject to caps or haircuts (eg Level 2 assets), the effects of such constraints should be accounted for.*

31.29

LCR31.20(1)(b) builds on the information provided by the jurisdiction in LCR31.7 to LCR31.10 and requires the jurisdiction to further explain the manner in which insufficient HQLA is determined, by listing all major factors that affect the HQLA shortfall faced by its LCR banks under LCR31.20(1)(a). There should be a commentary for each of the factors, explaining why the factor is relevant, the impact of the factor on the HQLA shortfall, and how such impact is incorporated into the analysis of insufficient HQLA. The jurisdiction should be able to demonstrate that it has adequately considered all relevant factors, including those that may improve the HQLA shortfall, so as to ascertain that the insufficiency issue is fairly stated.

31.30

On the supply of HQLA, there should be due consideration of the extent to which insufficient HQLA may be alleviated by estimated medium term supply of such assets, as well as the factors restricting the availability of HQLA to LCR banks. In the case of government debt, relevant information on availability can be reflected, for example, from the size and nature of other users of government debt in the jurisdiction; holdings of government debt which seldom appear in the traded markets; and the amount of government debt in free circulation for the assets to remain truly liquid.

31.31

On the demand of HQLA, there should be due consideration of the potential liquidity needs of

the banking sector, taking into account the scope for banks to reduce their liquidity risk (and hence their demand for HQLA) and the extent to which banks can satisfy their demand through the repo market (rather than through outright purchase of HQLA). Other needs for maintaining HQLA (eg for intraday repo purposes) may also increase banks' demand for such assets.

31.32

The jurisdiction should also include any other factors not mentioned above that are relevant to its case.

31.33

LCR31.20(1)(c) should establish that insufficient HQLA is caused by constraints that are not temporary in nature. The jurisdiction should provide a list of such constraints, explain the nature of the constraints and how the insufficiency issue is affected by the constraints, as well as whether there is any prospect of change in the constraints (eg measures taken to address the constraints) in the next three to five years. To demonstrate the significance of the constraints, the jurisdiction should support the analysis with appropriate quantitative information.

31.34

A jurisdiction may have fiscal or budget constraints that limit its ability or need to raise debt. To support this, the following information should, at a minimum, be provided:

1. Fiscal position for the past ten years: Consistent fiscal surpluses (eg at least six out of the past ten years or at least two out of the past three years)[30] can be an indication that the jurisdiction does not need to raise a significant amount of debt. On the contrary, it is unlikely that jurisdictions with persistent deficits (eg at least six out of the past ten years) will have a shortage in government debt issued.
2. Fiscal position as a percentage of gross domestic product (GDP) (ten-year average): This is another way of looking at the fiscal position. A positive ten-year average will likely suggest that the need for debt issuance is low. Similarly, a negative ten-year average will suggest otherwise.
3. Issue of government or central bank debt in the past ten years and the reasons for such issuance (eg for market operations or managing the yield curve). This is to assess the level and consistency of debt issuance.

1 Footnote

30 *Some deficits during economic downturns need to be catered for. Moreover, the recent surplus/deficit situation is relevant for assessment.*

31.35

The jurisdiction should also provide the ratio of its government debt to total banking assets denominated in domestic currency (for the past three to five years) to facilitate trend analysis of the government debt position versus a proxy indicator for banking activity (ie total banking assets), as well as comparison of the position across jurisdictions (including those that may not have the insufficiency issue). While this ratio alone cannot give any conclusive view about the insufficiency issue, a relatively low ratio (eg below 20%) may support the case if the jurisdiction also performs similarly under other indicators.

31.36

A jurisdiction may have underdeveloped markets that result in limited availability of corporate or covered bonds to satisfy market demand. Information to be provided may include the causes of this situation, measures that are being taken to develop the markets, the expected effect of such measures, and other relevant statistics showing the state of the markets.

31.37

There may also be other structural issues affecting the monetary system and operations. For example, the currency board arrangements for jurisdictions with pegged exchange rates could potentially constrain the issue of central bank debt and cause uncertainty or volatility in the availability of such debt to the banking sector. The jurisdiction should explain such arrangements and their effects on the supply of central bank debt (supported by relevant historical data in the past three to five years).

Guidance on meeting Principle 2 – managing performance

31.38

This Principle assesses whether and how the jurisdiction mitigates the risks arising from the adoption of any of the options, based on the requirements set out in the three criteria mentioned above. The assessment should also include whether the jurisdiction's approach to adopting the options is in line with the alternative treatment set out in LCR31.1 to LCR31.19.

31.39

The jurisdiction should explain its policy towards the adoption of the options, including which of the options will be used and the estimated (and maximum allowable) extent of usage by the banking sector. The jurisdiction should also justify the appropriateness of the maximum level of usage of the options to its banking system, in accordance with the relevant guidance set out in LCR31.4 to LCR31.6.

31.40

A jurisdiction intending to adopt Option 1 must demonstrate that it has the economic and financial capacity to support the committed liquidity facilities that will be granted to its banks.[31] The jurisdiction should, for example, have a strong credit rating (such as AA- or higher[32]) or be able to provide other evidence of financial strength and should not be exposed to adverse developments (eg a looming crisis) that may heavily impinge on its domestic economy in the near term.

2 Footnotes

31 *This is to enhance market confidence rather than to query the jurisdiction's ability to honour its commitments.*

32 *This is the minimum sovereign rating that qualifies for a 0% risk weight under CRE20.*

31.41

The jurisdiction should also demonstrate that it has a process in place to control the aggregate facilities granted under Option 1 within a level that is appropriate for its local circumstances. For example, the jurisdiction may limit the amount of Option 1 commitments to a certain

proportion of its GDP and justify why this level is suitable for its banking system. The process should address situations where the aggregate facilities are approaching or have breached the limit, and how the limit interplays with other restrictions for using the options (eg maximum level of usage for all options combined).

31.42

To facilitate assessment of compliance with requirements in LCR31.12, the jurisdiction should provide all relevant details associated with the extension of the committed facility, covering:

1. the commitment fee (including the basis on which it is charged,[33] the method of calculation[34] and the frequency of re-calculating or varying the fee). The jurisdiction should, in particular, demonstrate that the calculation of the commitment fee is in line with the conceptual framework set out in LCR31.12;
2. the types of collateral acceptable to the central bank for securing the facility and respective collateral margins or haircuts required;
3. the legal terms of the facility (including whether it covers a fixed term or is renewable or evergreen, the notice of drawdown, whether the contract is irrevocable prior to maturity,[35] and whether there are restrictions on a bank's ability to draw down on the facility);[36]
4. the criteria for allowing individual banks to use Option 1;
5. disclosure policies (ie whether the level of the commitment fee and the amount of committed facilities granted will be disclosed, either by the banks or by the central bank); and
6. the projected size of committed liquidity facilities that may be granted under Option 1 (versus the projected size of total net cash outflows in the domestic currency for Option 1 banks) for each of the next three to five years and the basis of projection.

4 Footnotes

33 *LCR31.12 requires the fee to be charged regardless of the amount, if any, drawn down against the facility.*

34 *LCR31.12 presents the conceptual framework for setting the fee.*

35 *LCR31.12 requires the maturity date to at least fall outside the 30-day LCR window and the contract to be irrevocable prior to maturity.*

36 *LCR31.12 requires the contract not to involve any ex post credit decision by the central bank*

31.43

A jurisdiction intending to adopt Option 2 should demonstrate that it has a mechanism in place to control the foreign exchange risk arising from banks' holdings in foreign currency HQLA under this option. This is because such foreign currency asset holdings to cover domestic currency liquidity needs may be exposed to the risk of decline in the liquidity value of those foreign currency assets should exchange rates move adversely when the assets are converted into the domestic currency, especially in times of stress.

31.44

This control mechanism should cover the following elements:

1. The jurisdiction should ensure that the use of Option 2 is confined only to foreign currencies which provide a reliable source of liquidity in the domestic currency in stressed market conditions. In this regard, the jurisdiction should specify the currencies and broad types of HQLA denominated in those currencies[37] allowable under this option, based on prudent criteria. The suitability of the currencies should be reviewed whenever significant changes in the external environment warrant a review.
2. The jurisdiction should explain why each of the allowable currencies is selected, including an analysis of the historical exchange rate volatility, and turnover size in the foreign exchange market, of the currency pair (eg based on statistics for each of the past three to five years). In case a currency is selected for other reasons,[38] the justifications should be clearly stated to support its inclusion for Option 2 purposes. The selection of currencies should take into account the following aspects:
    1. the currency should be freely transferable and convertible into the domestic currency;
    2. the currency should be liquid and active in the relevant foreign exchange market; the methodology and basis of this assessment should be documented;
    3. the currency should not exhibit significant historical exchange rate volatility against the domestic currency;[39] and
    4. in the case of a currency which is pegged to the domestic currency, there should be a formal mechanism in place for maintaining the peg rate; relevant information about the mechanism and past ten-year statistics on exchange rate volatility of the currency pair showing the effectiveness of the peg arrangement should be documented.
3. HQLA in the allowable currencies used for Option 2 purposes must be subject to haircuts as prescribed under this framework (ie at least 8% for major currencies[40]). The jurisdiction should set a higher haircut for other currencies where the exchange rate volatility against the domestic currency is much higher, based on a methodology that compares the historical (eg monthly) exchange rate volatilities between the currency pair concerned over an extended period of time. Where the allowable currency is formally pegged to the domestic currency, a lower haircut may be used to reflect limited exchange rate risk under the peg arrangement. To qualify for this treatment, the jurisdiction should demonstrate the effectiveness of its currency peg mechanism and the long-term prospect of keeping the peg. Where a threshold for applying the haircut under Option 2 is adopted (see LCR31.15), the level of the threshold must not be more than 25%.
4. Regular information should be collected from banks in respect of their holding of allowable foreign currency HQLA for LCR purposes to enable supervisory assessment of the foreign exchange risk associated with banks' holdings of such assets, both individually and in aggregate.
5. There should be an effective means to control the foreign exchange risk assumed by banks. The control mechanism, and how it is to be applied to banks, should be elaborated. In particular:
    1. there should be prescribed criteria for allowing individual banks to use Option 2;
    2. the approach to assessing whether the estimated holdings of foreign currency HQLA by individual banks using Option 2 are consistent with their foreign exchange risk management capacity (see LCR31.13) should be explained; and
    3. there should be a system for setting currency mismatch limits to control banks' maximum foreign currency exposures under Option 2.

4 Footnotes

37 *For example, clarification may be necessary in cases where only central government debt will be allowed, or Level 1 securities issued by multilateral development banks in some currencies will be allowed.*

38 *For example, the central banks of the two currencies concerned may have entered into special foreign exchange swap agreements that facilitate the flow of liquidity between the currencies.*

39 *This is relative to the exchange rate volatilities between the domestic currency and other foreign currencies with which the domestic currency is traded.*

40 *These currencies refer to those that exhibit significant and active market turnover in the global foreign currency market (eg the average market turnover of the currency as a percentage of the global foreign currency market turnover over a ten-year period is not lower than 10%).*

31.45

With the adoption of Option 3, the increase in holdings of Level 2A assets within the banking sector (to substitute for Level 1 assets which are of higher quality but in shortage) may give rise to additional price and market liquidity risks, especially in times of stress when concentrated asset holdings have to be liquidated. In order to mitigate this risk, the jurisdiction intending to adopt Option 3 should ensure that only Level 2A assets that are of comparable quality to Level 1 assets in the domestic currency are allowed to be used under this option (ie to exceed the 40% cap). Level 2B assets must remain subject to the 15% cap. The jurisdiction should demonstrate how this can be achieved in its supervisory framework, having regard to the following aspects:

1. The adoption of higher qualifying standards for additional Level 2A assets: apart from fulfilling all the qualifying criteria for Level 2A assets, additional requirements should be imposed to ensure the assets provide adequate liquidity value. For example, supervisors may require the minimum credit rating of these additional Level 2A assets to be AA or AA+ instead of AA-, and may impose more stringent qualitative and quantitative criteria. These assets may also be required to be central bank eligible.
2. The inclusion of a prudent diversification requirement for banks using Option 3: banks should be required to diversify holdings of Level 2 assets among different issuers and asset classes to the extent feasible in a given national market. The jurisdiction should illustrate how this diversification requirement is to be applied to banks.

31.46

The jurisdiction should provide statistical evidence to substantiate that Level 2A assets (used under Option 3) and Level 1 assets in the domestic currency are generally of comparable quality in terms of the maximum decline in price during a relevant historical period of significant liquidity stress.

31.47

The jurisdiction should also provide all relevant details associated with the use of Option 3, including:

1. the standards and criteria for allowing individual banks to use Option 3;
2. the system for monitoring banks' additional Level 2A asset holding under Option 3 to ensure that they observe the higher requirements;
3. the application of higher haircuts to additional Level 2A assets (see LCR31.17);[41] and
4. the existence of any restriction on the use of Level 2A assets (ie to what extent banks will be allowed to hold such assets as a percentage of their liquid asset stock).

1 Footnote

41 *Under LCR31.17, a minimum higher haircut of 20% must be applied to additional Level 2A assets used under this option. The jurisdiction must conduct an analysis to assess whether the 20% haircut is sufficient for Level 2A assets in its market, and should increase the haircut to an appropriate level if this is warranted in order to achieve the purpose of the haircut.*

Guidance on meeting Principle 3 – supervisory obligations

31.48

This Principle requires a jurisdiction intending to adopt any of the options to indicate the jurisdiction's commitment to observing the obligations relating to supervisory monitoring, disclosure, periodic self-assessment, and independent peer review of its eligibility for adopting the options, as set out in the criteria below. Whether these commitments are fulfilled in practice should be assessed in subsequent periodic self-assessments and, where necessary, in subsequent independent peer reviews.

31.49

The jurisdiction should demonstrate that it has a clearly documented framework for monitoring the usage of the options by its banks as well as their compliance with the relevant rules and requirements applicable to them under the supervisory framework. In particular, the jurisdiction should have a system to ensure that the rules governing banks' usage of the options are met, and that the usage of the options within the banking system are monitored and controlled. To achieve this, the framework should be able to address the aspects mentioned below.

31.50

The jurisdiction should set out the requirements that banks should meet in order to use the options to comply with the LCR. The requirements may differ depending on the option to be used as well as jurisdiction-specific considerations. The scope of these requirements will generally cover the following areas:

1. The jurisdiction should devise the supervisory requirements governing banks' usage of the options, having regard to the guidance set out in this chapter. Any bank-specific requirements should be communicated to the affected banks.
2. Banks using the options should be informed of the minimum amount of Level 1 assets that they are required to hold in the relevant currency. The jurisdiction should set a minimum level for banks in the jurisdiction. This should complement the requirement under LCR31.50(3) below.
3. In order to control the usage of the options within the banking system, banks should be informed of any supervisory restriction applicable to them in terms of the maximum

amount of alternative HQLA (under each or all of the options) they are allowed to hold. For example, if the maximum usage level is 70%, a bank should maintain at least 30% of its HQLA stock in Level 1 assets in the relevant currency. The maximum level of usage of the options set by the jurisdiction should be consistent with the calculations and projections used to support its compliance with Principles 1 and 2.

4. The jurisdiction may apply additional haircuts to banks that use the options to limit the uncertainty of performance, or mitigate the risks of non-performance, of the options used (see Principle 2). For example, a jurisdiction that relies heavily on Option 3 may observe that a large amount of Level 2A assets will be held by banks to fulfil their LCR needs, thereby increasing the market liquidity risk of these assets. This may necessitate increasing the Option 3 haircut for banks that rely heavily on these Level 2A assets.
5. The jurisdiction may choose to apply further restrictions to banks that use the options.

31.51

The jurisdiction should demonstrate that through its data collection framework (eg as part of regular banking returns), sufficient data can be obtained from its banks to ascertain compliance with the supervisory requirements as communicated to the banks. The jurisdiction should determine the reporting requirements, including the types of data and information required, the manner and frequency of reporting, and how the data and information collected will be used.

31.52

The jurisdiction should also indicate how it intends to monitor banks' compliance with the relevant rules and requirements. This may be performed through a combination of off-site analysis of information collected, prudential interviews with banks and on-site examinations as necessary. For example, an on-site review may be necessary to determine the quality of a bank's foreign exchange risk management in order to assess the extent which the bank should be allowed to use Option 2 to satisfy its LCR requirements.

31.53

The jurisdiction should demonstrate that it has sufficient supervisory powers and tools at its disposal to ensure compliance with the requirements governing banks' usage of the options. These will include tools for assessing compliance with specific requirements (eg foreign exchange risk management under Option 2 and price risk management under Option 3) as well as general measures and powers available to impose penalties should banks fail to comply with the requirements applicable to them. The jurisdiction should also demonstrate that it has sufficient powers to direct banks to comply with the general rules and/or specific requirements imposed on them. Examples of such measures are the power to issue directives to the banks, restriction of financial activities, financial penalties, increase of Pillar 2 capital, etc.

31.54

The jurisdiction should restrict a bank from using the options should it fail to comply with the relevant requirements.

31.55

The jurisdiction should demonstrate that it has a documented framework that is disclosed (whether on its website or through other means) upon the adoption of the options for alternative treatment. The document should contain clear and transparent information that will enable other national supervisors and stakeholders to gain a sufficient understanding of its

compliance with the qualifying principles for adoption of the options and the manner in which it supervises the use of the options by its banks.

31.56

The disclosure should cover the following:

1. the jurisdiction's self-assessment of insufficient HQLA in the domestic currency, including relevant data about the supply of, and demand for, HQLA, and major factors (eg structural, cyclical or jurisdiction-specific) influencing the supply and demand. This assessment should correspond with the self-assessment required under LCR31.57 to LCR31.61 below;
2. the jurisdiction's supervisory approach to applying the alternative treatment, including the option(s) allowed to be used by banks, any guidelines, requirements and restrictions associated with the use of such option(s) by banks, and approach to monitoring banks' compliance with them;
3. if Option 1 is adopted, the terms of the committed liquidity facility, including the maturity of the facility, the commitment fee charged (and the approach adopted for setting the fee), securities eligible as collateral for the facility (and margins required), and other terms, including any restrictions on banks' usage of this option;
4. if Option 2 is adopted, the foreign currencies (and types of securities under those currencies) allowed to be used, haircuts applicable to the foreign currency HQLA, and any restrictions on banks' usage of this option; and
5. if Option 3 is adopted, the Level 2A assets allowed to be used in excess of the 40% cap (and the associated criteria), haircuts applicable to Level 2A assets (within and above the 40% cap), and any restrictions on banks' usage of this option.

31.57

The jurisdiction should update the disclosed information whenever there are changes to the information (eg updated self-assessment of insufficient HQLA performed).

31.58

The jurisdiction should perform a review of its eligibility for alternative treatment every five years after it has adopted the options. The primary purpose of this review is to determine that there remains insufficient HQLA in the jurisdiction. The review should be in the form of a self-assessment of the jurisdiction's compliance with each of the Principles set out in this chapter.

31.59

The jurisdiction should have a credible process for conducting the self-assessment, and should provide sufficient information and analysis to support the self-assessment. The results of the self-assessment should be disclosed (on its website or through other means) and accessible by other national supervisors and stakeholders.

31.60

Where the self-assessment reflects that insufficient HQLA no longer exists, the jurisdiction should devise a plan for transition to the standard HQLA treatment under the LCR and notify the Basel Committee accordingly. If the issue of insufficiency remains but weaknesses in the jurisdiction's relevant supervisory framework are identified from the self-assessment, the jurisdiction should disclose its plan to address those weaknesses within a reasonable period.

31.61

If the jurisdiction is aware of circumstances (eg relating to fiscal conditions, market infrastructure or availability of liquidity, etc.) that have radically changed to an extent that may render insufficient HQLA no longer relevant to the jurisdiction, it must conduct a self-assessment promptly (ie without waiting until the next self-assessment is due) and notify the Basel Committee of the result as soon as practicable. The Basel Committee may similarly request the jurisdiction to conduct a self-assessment ahead of schedule if the Basel Committee is aware of changes that will significantly affect the jurisdiction’s eligibility for alternative treatment.

LCR40

Cash inflows and outflows

This chapter defines the denominator of the Liquidity Coverage Ratio: net cash outflows in the specified stress scenario for the subsequent 30 calendar days.

Version effective as of 15 December 2019

FAQ published on 30 March 2023 added.

Definition of total net cash outflows

40.1

The term total net cash outflows[42] is defined as the total expected cash outflows minus total expected cash inflows in the specified stress scenario for the subsequent 30 calendar days. Total expected cash outflows are calculated by multiplying the outstanding balances of various categories or types of liabilities and off-balance sheet commitments by the rates at which they are expected to run off or be drawn down. Total expected cash inflows are calculated by multiplying the outstanding balances of various categories of contractual receivables by the rates at which they are expected to flow in under the scenario up to an aggregate cap of 75% of total expected cash outflows.

$$\textit{Total net cash outflows over the next } 30 \textit{ days} = \textit{Total expected cash outflows} - \min\left(\textit{Total expected cash inflows}, 75\% \textit{ of total expected cash outflows}\right)$$

1 Footnote

42 *Where applicable, cash inflows and outflows should include interest that is expected to be received and paid during the 30-day time horizon.*

40.2

While most run-off rates, drawdown rates and similar factors are harmonised across jurisdictions as outlined in this standard, a few parameters are to be determined by supervisory authorities at the national level. Where this is the case, the parameters should be transparent and made publicly available.

40.3

LCR99 provides a summary of the factors that are applied to each category.

40.4

Banks will not be permitted to double-count items, ie if an asset is included as part of the stock of high-quality liquid assets (HQLA) (ie the numerator), the associated cash inflows cannot also be counted as cash inflows (ie part of the denominator). Where there is potential that an item could be counted in multiple outflow categories (eg committed liquidity facilities granted to cover debt maturing within the 30 calendar day period), a bank only has to assume up to the maximum contractual outflow for that product.

Cash outflows – Retail deposit run-off

40.5

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 Liquidity Coverage Ratio (LCR) include demand deposits and term deposits, unless otherwise excluded under the criteria set out in LCR40.16 and LCR40.17.

2 FAQs

FAQ1 *If a deposit is contractually pledged to a bank as collateral to secure a credit facility or loan granted by the bank that will not mature or be settled in the next 30 days, should the pledged deposit be excluded from the calculation of the total expected cash outflows under the LCR?*
The pledged deposit may be excluded from the LCR calculation only if the following conditions are met:
-
the loan will not mature or be settled in the next 30 days;
-
the pledge arrangement is subject to a legally enforceable contract disallowing withdrawal of the deposit before the loan is fully settled or repaid; and
-
the amount of deposit to be excluded cannot exceed the outstanding balance of the loan (which may be the drawn portion of a credit facility).
The above treatment does not apply to a deposit which is pledged against an undrawn facility, in which case the higher of the outflow rate applicable to the undrawn facility or the pledged deposit applies.

FAQ2 *What is the treatment in the LCR of unsecured precious metals liabilities (such as deposits in precious metals received by a bank)? Are the run-off rates for retail deposits and unsecured wholesale funding according to LCR40.5 to LCR40.44 applicable?*
Deposits in precious metals received by a bank should be treated as retail deposits according to LCR40.5 to LCR40.18 or as unsecured wholesale funding according to LCR40.19 to LCR40.44 depending on the type of counterparty.
In deviation from this treatment, jurisdictions may alternatively allow a bank to assume no outflow if:
-
the deposit physically settles and the bank is able to supply the precious metals from its own inventories; or
-
contractual arrangements give the bank the choice between cash settlement and physical delivery and there are no market practices or reputational factors that may limit the bank's discretion to exercise the option in a way that would minimise the LCR-effective outflow, ie to opt for physical delivery if the bank is able to supply the precious metals from its own inventories.
Supervisors in such jurisdictions must publicly disclose the treatment should they opt for the alternative treatment.

40.6

These retail deposits are divided into "stable" and "less stable" portions of funds as described below, with minimum run-off rates listed for each category. The run-off rates for retail deposits are minimum floors, with higher run-off rates established by individual jurisdictions as appropriate to capture depositor behaviour in a period of stress in each jurisdiction.

Stable deposits (run-off rate = 3% and higher)

40.7

Stable deposits, which usually receive a run-off factor of 5%, are the amount of the deposits that are fully insured[43] by an effective deposit insurance scheme or by a public guarantee that provides equivalent protection and where:

1. the depositors have other established relationships with the bank that make deposit withdrawal highly unlikely; or

2. the deposits are in transactional accounts (eg accounts where salaries are automatically deposited).

1 Footnote

[43] *"Fully insured" means that 100% of the deposit amount, up to the deposit insurance limit, is covered by an effective deposit insurance scheme. Deposit balances up to the deposit insurance limit may be treated as "fully insured" even if a depositor has a balance in excess of the deposit insurance limit. However, any amount in excess of the deposit insurance limit must be treated as "less stable". For example, if a depositor has a deposit of 150 that is covered by a deposit insurance scheme, which has a limit of 100, where the depositor would receive at least 100 from the deposit insurance scheme if the financial institution were unable to pay, then 100 would be considered "fully insured" and treated as stable deposits while 50 would be treated as less stable deposits. However if the deposit insurance scheme only covered a percentage of the funds from the first currency unit (eg 90% of the deposit amount up to a limit of 100) then the entire 150 deposit would be less stable.*

40.8

For the purposes of this standard, an "effective deposit insurance scheme" refers to a scheme:

1. that guarantees that it has the ability to make prompt payouts;
2. for which the coverage is clearly defined;
3. of which public awareness is high; and
4. in which the deposit insurer has formal legal powers to fulfil its mandate and is operationally independent, transparent and accountable.

40.9

A jurisdiction with an explicit and legally binding sovereign deposit guarantee that effectively functions as deposit insurance may be regarded as having an effective deposit insurance scheme.

40.10

The presence of deposit insurance alone is not sufficient to consider a deposit "stable".

40.11

Jurisdictions may choose to apply a run-off rate of 3% to stable deposits in their jurisdiction, if they meet the above stable deposit criteria and the following additional criteria for deposit insurance schemes:[44]

1. the insurance scheme is based on a system of prefunding via the periodic collection of levies on banks with insured deposits;[45]
2. 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
3. access to insured deposits is available to depositors in a short period of time once the deposit insurance scheme is triggered.[46]

3 Footnotes

44 *The Financial Stability Board has asked the International Association of Deposit Insurers (IADI), in conjunction with the Basel Committee and other relevant bodies where appropriate, to update its Core Principles and other guidance to better reflect leading practices. The criteria in this paragraph will therefore be reviewed by the Committee once the work by IADI has been completed.*

45 *The requirement for periodic collection of levies from banks does not preclude that deposit insurance schemes may, on occasion, provide for contribution holidays due to the scheme being well-funded at a given point in time.*

46 *This period of time would typically be expected to be no more than seven business days.*

40.12

Jurisdictions applying the 3% run-off rate to stable deposits with deposit insurance arrangements that meet the above criteria should be able to provide evidence of run-off rates for stable deposits within the banking system below 3% during any periods of stress experienced that are consistent with the conditions within the LCR.

Less stable deposits (run-off rates = 10% and higher)

40.13

Supervisory authorities should develop additional buckets with higher run-off rates as necessary to apply to buckets of potentially less stable retail deposits in their jurisdictions, with a minimum run-off rate of 10%. These jurisdiction-specific run-off rates should be clearly outlined and publicly transparent. Buckets of less stable deposits may include deposits that are not fully covered by an effective deposit insurance scheme or sovereign deposit guarantee, high-value deposits, deposits from sophisticated or high net worth individuals, deposits that can be withdrawn quickly (eg internet deposits) and foreign currency deposits, as determined by each jurisdiction.

40.14

If a bank is not able to readily identify which retail deposits would qualify as “stable” according to the above definition (eg the bank cannot determine which deposits are covered by an effective deposit insurance scheme or a sovereign deposit guarantee), it must place the full amount in the “less stable” buckets as established by its supervisor.

40.15

Foreign currency retail deposits are deposits denominated in any other currency than the domestic currency in a jurisdiction in which the bank operates. Supervisors will determine the run-off factor that banks in their jurisdiction should use for foreign currency deposits. Foreign currency deposits must be considered as “less stable” if there is a reason to believe that such deposits are more volatile than domestic currency deposits. Factors affecting the volatility of foreign currency deposits include the type and sophistication of the depositors, and the nature of such deposits (eg whether the deposits are linked to business needs in the same currency, or whether the deposits are placed in a search for yield).

40.16

Cash outflows related to retail term deposits with a residual maturity or withdrawal notice period greater than 30 days may 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.[47]

1 Footnote

47 *If a portion of the term deposit can be withdrawn without incurring such a penalty, that portion must be treated as a demand deposit. The remaining balance of the deposit should be treated as a term deposit.*

40.17

If a bank allows a depositor to withdraw such 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 must be treated as demand deposits (ie regardless of the remaining term, the deposits would be subject to the deposit run-off rates as specified in LCR40.6 to LCR40.15). Supervisors in each jurisdiction may choose to outline exceptional circumstances that would qualify as hardship, under which the exceptional term deposit could be withdrawn by the depositor without changing the treatment of the entire pool of deposits.

40.18

Notwithstanding the above, supervisors may also opt to treat retail term deposits that meet the qualifications set out in LCR40.16 with a higher than 0% run-off rate, if they clearly state the treatment that applies for their jurisdiction and apply this treatment in a similar fashion across banks in their jurisdiction. Such reasons could include, but are not limited to, supervisory concerns that depositors would withdraw term deposits in a similar fashion as retail demand deposits during either normal or stress times, concern that banks may repay such deposits early in stressed times for reputational reasons, or the presence of unintended incentives on banks to impose material penalties on consumers if deposits are withdrawn early. In these cases supervisors would assess a higher run-off against all or some of such deposits.

Cash outflows – unsecured wholesale funding run-off

40.19

For the purposes of the LCR, "unsecured wholesale funding" is defined as those liabilities and general obligations that are raised from non-natural persons (ie legal entities, including sole proprietorships and partnerships) and are not collateralised by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation or resolution. Obligations related to derivative contracts are excluded from this definition.

40.20

The wholesale funding included in the LCR is defined as all funding that is callable within the LCR's horizon of 30 days or that has its earliest possible contractual maturity date situated within this horizon (such as maturing term deposits and unsecured debt securities) as well as funding with an undetermined maturity. This should include all funding with options that are exercisable at the investor's discretion within the 30-calendar-day horizon. For funding with options exercisable at the bank's discretion, supervisors should take into account reputational factors that may limit a bank's ability not to exercise the option.[48] In particular, where the

market expects certain liabilities to be redeemed before their legal final maturity date, banks and supervisors should assume such behaviour for the purpose of the LCR and include these liabilities as outflows.

1 Footnote

48 *This could reflect a case where a bank may imply that it is under liquidity stress if it did not exercise an option on its own funding.*

40.21

Wholesale funding that is callable[49] by the funds provider subject to a contractually defined and binding notice period surpassing the 30-day horizon is not included.

1 Footnote

49 *This takes into account any embedded options linked to the funds provider's ability to call the funding before contractual maturity.*

Unsecured wholesale funding provided by small business customers: 5%, 10% and higher

40.22

Unsecured wholesale funding provided by small business customers is treated the same way as retail deposits for the purposes of this standard, effectively distinguishing between a "stable" portion of funding provided by small business customers and different buckets of less stable funding defined by each jurisdiction. The same bucket definitions and associated run-off factors apply as for retail deposits.

40.23

This category consists of deposits and other extensions of funds made by non-financial small business customers. "Small business customers" are defined in line with the definition of loans extended to small businesses in CRE30.20 to CRE30.22 that are managed as retail exposures and are generally considered as having similar liquidity risk characteristics to retail accounts provided the total aggregated funding[50] raised from one small business customer is less than €1 million (on a consolidated basis where applicable).

1 Footnote, 1 FAQ

50 *"Aggregated funding" means the gross amount (ie 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 for which the counterparty is known to be a small business customer). In addition, applying the limit on a consolidated basis means that where one or more small business customers are affiliated with each other, they may 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.*

FAQ1 *If a deposit is contractually pledged to a bank as collateral to secure a credit facility or loan granted by the bank that will not mature or be settled in the next 30 days, should the pledged deposit be excluded from the calculation of the total expected cash outflows under the LCR?*
The pledged deposit may be excluded from the LCR calculation only if the following conditions are met:
-
the loan will not mature or be settled in the next 30 days;
-
the pledge arrangement is subject to a legally enforceable contract disallowing withdrawal of the deposit before the loan is fully settled or repaid; and
-
the amount of deposit to be excluded cannot exceed the outstanding balance of the loan (which may be the drawn portion of a credit facility).
The above treatment does not apply to a deposit which is pledged against an undrawn facility, in which case the higher of the outflow rate applicable to the undrawn facility or the pledged deposit applies.

40.24

Where a bank does not have any exposure to a small business customer that would enable it to use the definition under CRE30.20 to CRE30.22, the bank may include such a deposit in this category provided that the total aggregate funding raised from the customer is less than €1 million (on a consolidated basis where applicable) and the deposit is managed as a retail deposit. This means that the bank treats such deposits in its internal risk management systems consistently over time and in the same manner as other retail deposits, and that the deposits are not individually managed in a way comparable to larger corporate deposits.

40.25

Term deposits from small business customers must be treated in accordance with the treatment for term retail deposits as outlined in LCR40.16 to LCR40.18.

Operational deposits generated by clearing, custody and cash management activities: 25%

40.26

Certain activities lead to financial and non-financial customers needing to place, or leave, deposits with a bank in order to facilitate their access and ability to use payment and settlement systems and otherwise make payments. These funds may receive a 25% run-off factor only if the customer has a substantive dependency with the bank and the deposit is required for such activities. Supervisory approval should be given to ensure that banks utilising this treatment actually are conducting these operational activities at the level indicated. Supervisors may choose not to permit banks to utilise the operational deposit run-off rates in cases where, for example, a significant portion of operational deposits are provided by a small proportion of customers (ie concentration risk).

1 FAQ

FAQ1 *Should deposits from a central counterparty be regarded as operational deposits, noting that such deposits are usually associated with clearing activities?*
As for any other qualifying operational deposits, the conditions set out in LCR40.26 to LCR40.36 must be fulfilled.

40.27

Qualifying activities in this context refer to clearing, custody or cash management activities that meet the following criteria.

1. The customer must be 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. For example, this condition would not be met if the bank is aware that the customer has adequate backup arrangements.
2. These services must be provided under a legally binding agreement to institutional customers.
3. The termination of such agreements must be 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.

40.28

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

1. 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.
2. The deposits are held in specifically designated accounts 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, such accounts should be non-interest bearing. Banks should be particularly aware that during prolonged periods of low interest rates, excess balances (as defined below) could be significant.

40.29

Any excess balances that could be withdrawn and would still leave enough funds to fulfil these clearing, custody and cash management activities do not qualify for the 25% factor. In other words, only that part of the deposit balance with the service provider that is proven to serve a customer’s operational needs can qualify as stable. Excess balances must be treated in the appropriate category for non-operational deposits. If banks are unable to determine the amount of the excess balance, then the entire deposit must be assumed to be excess to requirements and, therefore, considered non-operational.

40.30

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.

40.31

Operational deposits must receive a 0% inflow assumption for the depositing bank given that these deposits are required for operational reasons, and are therefore not available to the

depositing bank to repay other outflows.

40.32

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.[51]

1 Footnote

51 *Correspondent banking refers to arrangements under which one bank (correspondent) holds deposits owned by other banks (respondents) and provides payment and other services in order to settle foreign currency transactions (eg so-called nostro and vostro accounts used to settle transactions in a currency other than the domestic currency of the respondent bank for the provision of clearing and settlement of payments). Prime brokerage is a package of services offered to large active investors, particularly institutional hedge funds. These services usually include: clearing, settlement and custody; consolidated reporting; financing (margin, repo or synthetic); securities lending; capital introduction; and risk analytics.*

40.33

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:

1. transmission, reconciliation and confirmation of payment orders;
2. daylight overdraft, overnight financing and maintenance of post-settlement balances; and
3. determination of intraday and final settlement positions.

40.34

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.

40.35

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.

40.36

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

Treatment of deposits in institutional networks of cooperative banks: 25% or 100%

40.37

An institutional network of cooperative (or otherwise named) banks is a group of legally autonomous banks with a statutory framework of cooperation with common strategic focus and brand where specific functions are performed by central institutions or specialised service providers. So long as both the bank that has received the monies and the bank that has deposited participate in the same institutional network's mutual protection scheme against illiquidity and insolvency of its members, a 25% run-off rate may be given to the amount of deposits of member institutions with the central institution or specialised central service providers that are placed:

1. due to statutory minimum deposit requirements, which are registered at regulators; or
2. in the context of common task sharing and legal, statutory or contractual arrangements.

40.38

As with other operational deposits, these deposits must receive a 0% inflow assumption for the depositing bank, as these funds are considered to remain with the centralised institution.

40.39

Supervisory approval should be given to ensure that banks utilising this treatment actually are the central institution or a central service provider of such a cooperative (or otherwise named) network. Correspondent banking activities must not be included in this treatment and must receive a 100% outflow treatment, as must funds placed at the central institutions or specialised service providers for any other reason other than those outlined in LCR40.37, or for operational functions of clearing, custody, or cash management as outlined in LCR40.33 to LCR40.35.

Unsecured wholesale funding provided by non-financial corporates and sovereigns, central banks, multilateral development banks and public sector entities: 20% or 40%

40.40

This category comprises all deposits and other extensions of 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 public sector entity (PSE) customers that are not specifically held for operational purposes (as defined above). The run-off factor for these funds must be 40%, unless the criteria in LCR40.41 are met.

40.41

Unsecured wholesale funding provided by non-financial corporate customers, sovereigns, central banks, multilateral development banks and PSEs without operational relationships may receive a 20% run-off factor if the entire amount of the deposit is fully covered by an effective deposit insurance scheme or by a public guarantee that provides equivalent protection.

Unsecured wholesale funding provided by other legal entity customers: 100%

40.42

This category consists of all deposits and other funding from other institutions (including banks, securities firms, insurance companies, etc), fiduciaries,[52] beneficiaries,[53] conduits and special purpose vehicles, affiliated entities of the bank[54] and other entities that are not specifically held for operational purposes (as defined above) and not included in the prior three categories. The run-off factor for these funds must be 100%.

3 Footnotes, 1 FAQ

52 *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.*

53 *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.*

54 *Outflows on unsecured wholesale funding from affiliated entities of the bank are included in this category unless the funding is part of an operational relationship, a deposit in an institutional network of cooperative banks or the affiliated entity is a non-financial corporate.*

FAQ1 *There may be various cash inflows and outflows between a central counterparty (CCP) and its member banks. Can a bank net off such cash flows with respect to trades cleared with a CCP when calculating the LCR?*
There is no specific treatment of cash flows between CCPs and its member banks, ie netting is restricted to cases where it is permitted in the LCR framework (eg derivative cash flows that are subject to the same master netting agreement in LCR40.49).

40.43

All notes, bonds and other debt securities issued by the bank must be 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 LCR40.22 to LCR40.24), in which case the instruments may be treated in the appropriate retail or small business customer deposit 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.

40.44

Customer cash balances arising from the provision of prime brokerage services, including but not limited to the cash arising from prime brokerage services as identified in LCR40.32, must be considered separate from any required segregated balances related to client protection regimes imposed by national regulations, and must not be netted against other customer exposures included in this standard. These offsetting balances held in segregated accounts are treated as inflows in LCR40.87 and must be excluded from the stock of HQLA.

Secured funding run-off

40.45

For the purposes of this standard, “secured funding” is defined as those liabilities and general obligations that are collateralised by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation or resolution. Unless the counterparty is a central bank, secured funding does not include transactions collateralised by assets that are not tradable in financial markets such as property, plant and equipment.

40.46

Loss of secured funding on short-term financing transactions: In this scenario, the ability to continue to transact repurchase, reverse repurchase and other securities financing transactions is limited to transactions backed by HQLA or with the bank’s domestic sovereign, PSE or central bank.[55] Collateral swaps must be treated as repurchase or reverse repurchase agreements, as must any other transaction with a similar form. Additionally, collateral lent to the bank’s customers to effect short positions[56] must be treated as a form of secured funding. For the scenario, a bank must 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 must be calculated based on the amount of funds raised through the transaction, and not the value of the underlying collateral.

2 Footnotes, 1 FAQ

55 *In this context, PSEs that receive this treatment should be limited to those that are 20% risk weighted or better, and “domestic” can be defined as a jurisdiction where a bank is legally incorporated.*

56 *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.*

FAQ1 *Are client shorts covered by external securities borrowings subject to LCR40.79 (under "secured lending, including reverse repos and external securities borrowings") or LCR40.46 ("secured funding run-off")? Firm shorts covered by external securities borrowings are clearly covered by LCR40.79, and it seems more logical that client shorts covered by external securities borrowings should be as well. However, LCR40.46 makes references to customer shorts and the treatment is different.*
The treatments of customer shorts versus firm shorts are separate and distinct and for this reason are addressed in two separate paragraphs. Customer shorts are considered equivalent to other secured financing transactions, as the proceeds from the customer's short sale may be re-used by the facilitating bank to finance the purchase or borrowing of the shorted security. Contrary to firm short positions, customer short positions are initiated and maintained at the discretion of the customer, and therefore the availability of this financing may be uncertain during a period of stress. These characteristics explain why customer shorts are treated in accordance with the run-off assumption in LCR40.48.

40.47

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 must be assigned to maturing transactions backed by Level 2 assets equivalent to the required haircuts. A 25% factor may be applied for maturing secured funding 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 treatment, however, may be applied only to outstanding secured funding transactions. Unused collateral or merely the capacity to borrow, as determined at the end of the day for the reporting date, must not be given any credit in this treatment.

2 FAQs

FAQ1 *At what time is the "unused" assessment performed? Is it at the end of day in the respective jurisdiction?*
The assessment is at the end of the day of the reporting date in the respective jurisdiction.

FAQ2 *Should "domestic" also refer to a jurisdiction where a bank's branch or consolidated subsidiary is operating? (Note: it is not uncommon for a bank's overseas branch to conduct repo transactions with the central bank of the host jurisdiction, which is not the place of "incorporation" of the bank but the place in which the bank's overseas branch operates.)*
The application of the reduced outflow assumptions for secured funding transactions with "domestic" public counterparties should be principally limited to counterparties from the jurisdiction where a bank is legally incorporated. It may be expanded to other public counterparties where the reduced outflow rates in LCR40.48 can be expected to reflect the behaviour of the other public counterparties. For example, in terms of central banks, this may be assumed when the overseas branch has equal access to central bank funding as domestic banks and where it seems reasonable that this equal treatment will remain in the context of central bank measures in times of severe idiosyncratic or market-wide stress.

40.48

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. All secured transactions maturing within 30 days should be reported according to the collateral actually pledged as of close of business on the LCR measurement date. If the bank pledges a pool of assets and cannot determine which specific assets in the collateral pool are used to collateralise the transactions with a residual maturity greater than 30 days, it may assume that assets are encumbered to these transactions in order of increasing liquidity value, consistent with the methodology set out in LCR30.16, in such a way that assets with the lowest liquidity value in the LCR are assigned to the transactions with the longest residual maturities first. The table below summarises the outflow applicable to transactions maturing within 30 days.

Categories for outstanding maturing secured funding transactions	Amount to add to cash outflows
Backed by Level 1 assets or with central banks	0%
Backed by Level 2A assets	15%
Secured funding transactions with domestic sovereign, PSEs or multilateral development banks that are not backed by Level 1 or 2A assets. PSEs that receive this treatment are limited to those that have a risk weight of 20% or lower.	25%
Backed by residential mortgage-backed securities (RMBS) eligible for inclusion in Level 2B	25%
Backed by other Level 2B assets	50%
All others	100%

Cash outflows – Additional requirements

40.49

Derivatives cash outflows: The sum of all net derivative cash outflows must receive a 100% factor. Banks must calculate, in accordance with their existing valuation methodologies, expected contractual derivative cash inflows and outflows. Cash flows may be calculated on a net basis (ie inflows can offset outflows) by counterparty only where a valid master netting agreement exists. Banks should exclude from such calculations those liquidity requirements that would result from increased collateral needs due to market value movements or declines in value of collateral posted.[57] Options that can be exercised within the next 30 days, including options that expire in greater than 30 days (eg an American-style option), must be assumed to be exercised when they are "in the money" to the option buyer. For transactions involving a delivery obligation that can be fulfilled with a variety of asset classes, delivery of the least valuable asset possible ("cheapest to deliver") must be assumed. This should apply symmetrically to both the inflow and outflow perspective, such that the obligor is assumed to deliver the security with the lowest liquidity value. Cash flows arising from foreign exchange derivative transactions that involve a full exchange of principal amounts on a simultaneous

basis (or within the same day) may be reflected as a net cash flow figure, even where those transactions are not covered by a master netting agreement.

1 Footnote, 2 FAQs

57 These risks are captured in LCR40.52 and LCR40.56, respectively.

FAQ1 Would it be correct to assume that expected contractual derivatives cash inflows from "in the money" options for which the bank is the option holder can be included without contravening the high-level principle in LCR40.75 that contingent inflows are not to be recognised?
Yes, LCR40.49 states that "options should be assumed to be exercised when they are in the money to the option buyer", eg cash inflows from contractual derivatives that are "in the money" may count towards derivatives cash inflows in the LCR. This is an exception to both LCR40.75, which excludes contingent inflows, and LCR40.85, which excludes inflows with no specific date from the LCR.

FAQ2 Could you confirm that options with delivery settlement during the relevant period could be considered as cash flows to the extent of the liquidity value of the delivered assets? Or whether all options are assumed to be cash-settled?
Options with delivery settlement shall be considered according to the liquidity value of the delivered assets, ie the assets are subject to the haircuts that would be applied if these assets were collateral in secured transactions or collateral swaps. If contractual arrangements allow for both physical delivery and cash settlement, cash settlement may be assumed.

40.50

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.

40.51

Increased liquidity needs related to downgrade triggers embedded in financing transactions, derivatives and other contracts: 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. 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 must 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 must consider impacts on all types of margin collateral and contractual triggers which change rehypothecation rights for non-segregated collateral.

2 FAQs

FAQ1 *Do LCR40.51 to LCR40.55 apply in the same way to all derivative instruments, whether over-the-counter or on-exchange, whether cleared or not? In particular, can confirmation be given that margin posted for clearance through a central counterparty (CCP) and held for the benefit of the bank in accordance with the rules of such CCP should be recognised under the logic of these paragraphs, although the point is not addressed explicitly?*
Unless expressly specified otherwise, the provisions apply generally. Any Level 1 assets in segregated accounts held in a bank's name by the CCP will be treated in accordance with LCR40.52.

FAQ2 *LCR40.52 requires that if a bank has posted a non-Level 1 asset as collateral to secure its mark-to-market exposure under derivatives contracts or other transactions, the bank must hold additional stock of HQLA to cater for a potential reduction in the value of the collateral to the extent of 20% of the collateral value. Similar references to "other transactions" are also made in LCR40.51 and LCR40.56. Banks have queries on the scope of "other transactions". Is it the policy intent that LCR40.51, LCR40.52 and LCR40.56 are generally applicable to derivatives transactions only?*
LCR40.51, LCR40.52 and LCR40.56 are only applicable to derivatives and other transactions not specifically captured in the LCR framework. Thus, they are not applicable to secured funding transactions addressed in LCR40.45 to LCR40.48 and secured lending transactions addressed in LCR40.78 to LCR40.79.

40.52

Increased liquidity needs related to the potential for valuation changes on posted collateral securing derivative and other transactions: 20% of the value of non-Level 1 posted collateral. Observation of market practices indicates that most counterparties to derivatives 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 standardised approach to credit risk (CRE20). 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. 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) must be added to the stock of required HQLA by the bank posting such collateral. This 20% must 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 may only be used to offset outflows that are associated with payments that are eligible to be offset from that same account. No other form of netting (eg netting of offsetting collateral flows across counterparties) is permissible when calculating this outflow amount.

6 FAQs

FAQ1 *Do the bank's normal procedures apply to determine the notional amount pursuant to the penultimate sentence of LCR40.52?*
The notional amount to be collateralised in LCR40.52 is based on contractual terms (eg collateral agreements) that regularly include the methodology of calculating the amount to be covered ("notional amount").

FAQ2 *Do LCR40.51 to LCR40.55 apply in the same way to all derivative instruments, whether over-the-counter or on-exchange, whether cleared or not? In particular, can confirmation be given that margin posted for clearance through a central counterparty (CCP) and held for the benefit of the bank in accordance with the rules of such CCP should be recognised under the logic of these paragraphs, although the point is not addressed explicitly?*
Unless expressly specified otherwise, the provisions apply generally. Any Level 1 assets in segregated accounts held in a bank's name by the CCP will be treated in accordance with LCR40.52.

FAQ3 *LCR40.52 requires that an additional stock of HQLA be maintained for outflows where the bank is posting non-Level 1 collateral securing its derivatives. Can this be interpreted as applying on a net basis to the extent the bank uses non-Level 1 collateral received from one counterparty to secure derivative liability to another counterparty, if any decrease in the value of this collateral would affect both collateral posting to and by the bank?*
No. Netting of collateral inflows and outflows across counterparties is not provided for in LCR40.52 as the impacts of valuation changes (even of identical collateral) may be asymmetric across different counterparties.

FAQ4 *Assuming that a bank is a net poster of non-Level 1 collateral, can the net outflows under LCR40.52 be calculated taking into account any additional eligible non-Level 1 collateral that is unencumbered as of the date of the LCR or that would become unencumbered as a result of the stresses?*
No. The LCR framework provides no basis for separate sub-pools of (non-Level 1) HQLA dedicated to specific liquidity needs or for considering contingent inflows of collateral.

FAQ5 *Can it be assumed that a bank will post collateral in the most efficient manner practicable? For example, if a bank is currently a net poster of non-Level 1 collateral (with higher haircuts), it seems appropriate to assume that the bank would use its cash or lower-haircut Level 1 securities first, and not use that cash to purchase additional non-Level 1 collateral that would have a higher haircut.*
As with any other outflow captured in the LCR, the outflows addressed in LCR40.52 add to the bank's net cash outflow that must be met by Level 1 and/or Level 2 assets according to LCR30. No further assumptions have to be made in terms of what the bank actually "will post".

FAQ6 *LCR40.52 of the LCR text requires that if a bank has posted a non-Level 1 asset as collateral to secure its mark-to-market exposure under derivatives contracts or other transactions, the bank must hold additional stock of HQLA to cater for a potential reduction in the value of the collateral to the extent of 20% of the collateral value. Similar references to "other transactions" are also made in LCR40.51 and LCR40.55. Banks have queries on the scope of "other transactions". Is it the policy intent that LCR40.51, LCR40.52 and LCR40.55 are generally applicable to derivatives transactions only?*
LCR40.51, LCR40.52 and LCR40.55 are only applicable to derivatives and other transactions not specifically captured in the LCR framework. Thus, they are not applicable to secured funding transactions addressed in LCR40.45 to LCR40.48 and secured lending transactions addressed in LCR40.78 to LCR40.79.

40.53

Increased liquidity needs related to excess non-segregated collateral held by the bank that could contractually be called at any time by the counterparty: 100% of the non-segregated collateral (ie where the collateral is unencumbered and included in the stock of HQLA or where

a recall of collateral by the counterparty would need to use additional funding) that could contractually be recalled by the counterparty because the collateral is in excess of the counterparty's current collateral requirements.

1 FAQ

FAQ1 *Do LCR40.51 to LCR40.55 apply in the same way to all derivative instruments, whether over-the-counter or on-exchange, whether cleared or not? In particular, can confirmation be given that margin posted for clearance through a central counterparty (CCP) and held for the benefit of the bank in accordance with the rules of such CCP should be recognised under the logic of these paragraphs, although the point is not addressed explicitly?*
Unless expressly specified otherwise, the provisions apply generally. Any Level 1 assets in segregated accounts held in a bank's name by the CCP will be treated in accordance with LCR40.52.

40.54

Increased liquidity needs related to contractually required collateral on transactions for which the counterparty has not yet demanded the collateral be posted: 100% of the collateral that is contractually due but where the counterparty has not yet demanded the posting of such collateral.

1 FAQ

FAQ1 *Do LCR40.51 to LCR40.55 apply in the same way to all derivative instruments, whether over-the-counter or on-exchange, whether cleared or not? In particular, can confirmation be given that margin posted for clearance through a central counterparty (CCP) and held for the benefit of the bank in accordance with the rules of such CCP should be recognised under the logic of these paragraphs, although the point is not addressed explicitly?*
Unless expressly specified otherwise, the provisions apply generally. Any Level 1 assets in segregated accounts held in a bank's name by the CCP will be treated in accordance with LCR40.52.

40.55

Increased liquidity needs related to contracts that allow collateral substitution without the bank's consent to non-HQLA assets: 100% of the amount of non-segregated HQLA collateral that can be substituted with non-HQLA. For substitution of HQLA with other HQLA of a lower liquidity value, the outflow should be measured based on the difference between the LCR haircuts of the collateral currently held and the potential substitute collateral. If the substituted collateral can be of different liquidity value in the LCR, the outflow must be measured based on the potential substitute collateral with the lowest liquidity value. HQLA collateral held that remains unencumbered, but is excluded from the bank's stock of HQLA due to the operational requirements may be excluded from this outflow amount.

3 FAQs

FAQ1 *Which cash flow assumptions are applied for secured transactions where assets are received on the basis of a collateral pool that is subject to potential collateral substitution? And, does the concept of collateral substitution also apply to inflows for secured borrowing transactions, ie can a bank take an inflow where it has the contractual right to receive HQLA if it was able to pledge available non-HQLA collateral to a secured lender?*
The risks associated with collateral substitution on secured lending transactions with a residual maturity greater than 30 days should be considered as a contingent outflow in accordance with LCR40.55 of the LCR framework. The contractual right to substitute HQLA collateral for lower -quality or non-HQLA collateral would be a contingent inflow. As such, it is not considered in the LCR in line with LCR40.75.

FAQ2 *Do LCR40.51 to LCR40.55 apply in the same way to all derivative instruments, whether over-the-counter or on-exchange, whether cleared or not? In particular, can confirmation be given that margin posted for clearance through a central counterparty (CCP) and held for the benefit of the bank in accordance with the rules of such CCP should be recognised under the logic of these paragraphs, although the point is not addressed explicitly?*
Unless expressly specified otherwise, the provisions apply generally. Any Level 1 assets in segregated accounts held in a bank's name by the CCP will be treated in accordance with LCR40.52.

FAQ3 *Does the outflow factor of 100% refer to the amount of HQLA collateral before or after the application of potential valuation haircuts (eg in the case of Level 2A collateral)?*
LCR40.55 does not require an outflow for potential collateral substitution that is greater than the liquidity value of the received HQLA collateral in the LCR. The 100% outflow factor refers to the market value of the received collateral that is subject to potential substitution after applying the respective haircut in the LCR.

40.56

Increased liquidity needs related to market valuation changes on derivative or other transactions: 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 may be treated on a net basis. Any outflow generated by increased needs related to market valuation changes must be included in the LCR calculated by identifying the largest absolute net 30-day collateral flow realised during the preceding 24 months. The absolute net collateral flow must be based on both realised outflows and inflows. Supervisors may adjust the treatment flexibly according to circumstances.

2 FAQs

FAQ1 *What does "the largest absolute net 30-day collateral flow" refer to?*
The largest absolute net 30-day collateral flow is the largest aggregated cumulative net collateral outflow or inflow at the end of all 30-day periods during the preceding 24 months. For this purpose, banks have to consider all 30-day periods during the preceding 24 months. Netting should be considered on a portfolio-level basis. Bank management should understand how collateral moves on a counterparty basis and is encouraged to review the potential outflow at that level. However, the primary mechanism for the "look-back approach" is collateral flows at the portfolio level.

FAQ2 *Should settlement payments (or receipts) made in the context of derivatives structured as "settled-to-market" (STM) be captured in LCR40.56?*
Yes, if the settlements are made in relation to market valuation changes. The economic cash flows exchanged between parties to STM and non-STM derivatives are identical and therefore the "collateral flows" mentioned in LCR40.56 include payments and receipts which are deemed to settle outstanding exposures from derivatives structured as STM as well.

40.57

Loss of funding on asset-backed securities,[58] covered bonds and other structured financing instruments: 100% outflow of funding transactions 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 exist). This outflow may be offset against HQLA that would become unencumbered and available upon the maturity of the instrument. Any surplus of the liquidity value of HQLA that would become unencumbered over redemption value for the maturing securities may be recognised as an inflow under LCR40.93. Any inflows representing Level 2 HQLA must reflect the market value reduced by, at a minimum, the respective LCR haircut.

1 Footnote

58 *To the extent that sponsored conduits/special purpose entities are required to be consolidated under liquidity requirements, their assets and liabilities will be taken into account. Supervisors should be aware of other possible sources of liquidity risk beyond that arising from debt maturing within 30 days.*

40.58

Loss of funding on asset-backed commercial paper, conduits, securities investment vehicles and other such financing facilities: 100% of maturing amount and 100% of returnable assets. Banks having structured financing facilities that include the issuance of short-term debt instruments, such as asset-backed commercial paper, must fully consider the potential liquidity risk arising from these structures. These risks include, but are not limited to, the inability to refinance maturing debt, and the existence of derivatives or derivative-like components contractually written into the documentation associated with the structure that would allow the “return” of assets in a financing arrangement, or that require the original asset transferor to provide liquidity, effectively ending the financing arrangement (“liquidity puts”) within the 30-day period. Where the structured financing activities of a bank are conducted through a special purpose entity[59] (or SPE, such as a special purpose vehicle, conduit or structured investment vehicle), the bank must, 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 the need for liquidity, irrespective of whether or not the special purpose vehicle is consolidated.

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

1 Footnote

59 *An SPE is defined in CRE40.21 as a corporation, trust, or other entity organised for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator or seller of exposures. SPEs, normally a trust or similar entity, are commonly used as financing vehicles in which exposures are sold to the SPE in exchange for cash or other assets funded by debt issued by the trust.*

40.59

Drawdowns on committed credit and liquidity facilities: 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. 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 LCR40.67. 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 will likely be difficult for customers drawing on facilities of any maturity, even short-term maturities, to be able to quickly pay back the borrowings. Therefore, all facilities that are assumed to be drawn (as outlined in the paragraphs below) must be assumed to remain outstanding without repayment, regardless of maturity.

40.60

The currently undrawn portion of these facilities may be calculated net of any HQLA eligible for the stock of HQLA, if the HQLA have already been posted as collateral by the counterparty to secure the facilities or that are contractually obliged to be posted when the counterparty will draw 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 may 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 in LCR40.4 that items must not be double-counted.

40.61

A liquidity facility is defined as any committed, undrawn backup facility that would be utilised to refinance the debt obligations of a customer in situations where such a customer is unable to rollover that debt in financial markets (eg pursuant to a commercial paper programme, secured financing transactions, obligations to redeem units). The amount of the commitment that must 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 facility. The portion of a liquidity facility that is backing debt that does not mature within the 30-day window may be excluded from the scope of the definition of a facility. Any additional capacity of the facility (ie the remaining commitment)

must be treated as a committed credit facility with its associated drawdown rate as specified in LCR40.64. General working capital facilities for corporate entities (eg revolving credit facilities in place for general corporate or working capital purposes) must not be classified as liquidity facilities, but as credit facilities.

1 FAQ

FAQ1 *Although LCR40.61 explicitly refers to "rollover" of debt, do these liquidity facilities also capture newly issued positions?*
Yes. A liquidity facility according to LCR40.61 is any type of commitment that backs up market funding needs of the customer.

40.62

Notwithstanding the above, any facilities provided to hedge funds, money market funds and special purpose funding vehicles, for example SPEs (as defined in LCR40.58) or conduits, or other vehicles used to finance the banks' own assets, must be captured in their entirety as a liquidity facility to other legal entities.

1 FAQ

FAQ1 *To what extent should this provision be applied to commercial conduits for clients?*
Facilities to SPEs and conduits are subject to the 100% drawdown rate of LCR40.64(7). The LCR framework does not provide any other category for these entities independent of their business purpose.

40.63

For that portion of financing programmes that are captured in LCR40.57, LCR40.58 and LCR40.64 (ie are maturing or have liquidity puts that may be exercised in the 30-day horizon), banks that are providers of associated liquidity facilities must not double count the maturing financing instrument and the liquidity facility for consolidated programmes.

40.64

Any contractual loan drawdowns from committed facilities[60] and estimated drawdowns from revocable facilities within the 30-day period must be fully reflected as outflows.

1. Committed credit and liquidity facilities to retail and small business customers: banks must assume a 5% drawdown of the undrawn portion of these facilities.
2. Committed credit facilities to non-financial corporates, sovereigns and central banks, PSEs and multilateral development banks: banks must assume a 10% drawdown of the undrawn portion of these credit facilities.
3. Committed liquidity facilities to non-financial corporates, sovereigns and central banks, PSEs and multilateral development banks: banks must assume a 30% drawdown of the undrawn portion of these liquidity facilities.
4. Committed credit and liquidity facilities extended to banks subject to prudential supervision: banks must assume a 40% drawdown of the undrawn portion of these facilities.
5. Committed credit facilities to other financial institutions, including securities firms, insurance companies, fiduciaries, and beneficiaries: banks must assume a 40% drawdown of the undrawn portion of these credit facilities.
6. Committed liquidity facilities to other financial institutions, including securities firms, insurance companies' fiduciaries and beneficiaries: banks must assume a 100%

drawdown of the undrawn portion of these liquidity facilities.

7. Committed credit and liquidity facilities to other legal entities (including SPEs as defined in LCR40.58, conduits and special purpose vehicles,[61] and other entities not included in the prior categories): Banks must assume a 100% drawdown of the undrawn portion of these facilities.

2 Footnotes

60 *Committed facilities refer to those which are irrevocable.*

61 *The potential liquidity risks associated with the bank's own structured financing facilities must be treated according to LCR40.57 and LCR40.58 (100% of maturing amount and 100% of returnable assets are included as outflows).*

40.65

Contractual obligations to extend funds within a 30-day period: Any contractual lending obligations to financial institutions, including central banks, not captured elsewhere in this standard must be captured here at a 100% outflow rate.

40.66

If the total of all contractual obligations to extend funds to retail and non-financial wholesale (eg including small or medium-sized entities and other corporates, sovereigns, multilateral development banks and PSEs) 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 calendar days from these clients, the difference must be reported as a 100% outflow.

40.67

Other contingent funding obligations: (run-off rates at national discretion). National supervisors may work with supervised institutions in their jurisdictions to determine the liquidity risk impact of these contingent liabilities and the resulting stock of HQLA that should accordingly be maintained. Supervisors should disclose the run-off rates they assign to each category publicly.

40.68

These contingent funding obligations may be either contractual or non-contractual and are not 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.

40.69

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. For

this standard, each supervisor and 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 should 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. Supervisors and banks should, at a minimum, use historical behaviour in determining appropriate outflows.

1 FAQ

FAQ1 *How does the LCR in the Basel Framework treat autocallable notes or those funding instruments that mature as soon as a pre-defined market-based trigger is reached or if a trigger is breached at a pre-defined date?*
Autocallable notes or those funding instruments with market-based maturity triggers issued by the bank should be treated as other contingent funding obligations according to LCR40.69 in connection with LCR40.67. Accordingly, competent authorities and banks should consider which trigger events may occur under the stress assumptions set out in LCR20.2 on the basis of prudent and appropriate analysis.

40.70

Non-contractual contingent funding obligations related to potential liquidity draws from joint ventures or minority investments in entities, which are not consolidated per LCR10.1, 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. The amount included should be calculated in accordance with the methodology agreed by the bank’s supervisor.

40.71

In the case of contingent funding obligations stemming from trade finance instruments, national authorities may apply a relatively low run-off rate (eg 5% or less). Trade finance instruments consist of trade-related obligations directly underpinned by the movement of goods or the provision of services, such as:

1. documentary trade letters of credit, documentary and clean collection, import bills, and export bills; and
2. guarantees directly related to trade finance obligations, such as shipping guarantees.

40.72

Lending commitments, such as direct import or export financing for non-financial corporate firms, must be excluded from the treatment in LCR40.71 and banks will apply the draw-down rates specified in LCR40.64.

40.73

National authorities must determine the run-off rates for the other contingent funding obligations listed below in accordance with LCR40.67. Other contingent funding obligations include products and instruments such as:

1. unconditionally revocable “uncommitted” credit and liquidity facilities;
2. guarantees and letters of credit unrelated to trade finance obligations (as described in LCR40.71);

3. non-contractual obligations such as:
    1. potential requests for debt repurchases of the bank's own debt or that of related conduits, securities investment vehicles and other such financing facilities;
    2. structured products where customers anticipate ready marketability, such as adjustable rate notes and variable-rate demand notes; and
    3. 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 etc;
4. for issuers with an affiliated dealer or market-maker, there may be a need to include an amount of the outstanding debt securities (unsecured and secured, term as well as short-term) having maturities greater than 30 calendar days, to cover the potential repurchase of such outstanding securities; and
5. non-contractual obligations where customer short positions are covered by other customers' collateral: a minimum 50% run-off factor of the contingent obligations must 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.

1 FAQ

FAQ1 *What is the appropriate treatment of using the collateral obtained through a margin loan to cover a customer short position? The margin loan will be a 50% inflow, but will the customer short be reflected by the minimum 50% outflow in LCR40.73 and/or the outflow due to LCR40.46 and LCR40.48? Regarding LCR40.73, how should it be determined whether or not to take a 50% outflow or a greater percentage?*
LCR40.73 should be applied to quantify the outflow arising from lending out a non-HQLA asset to affect a customer's short position if this asset is received as collateral to secure another customer's margin loan. Thus, the 50% inflow from borrowing the assets to secure a margin loan is symmetrical to the 50% outflow for lending these assets to cover another customer's short position, subject to national discretion.

40.74

Other contractual cash outflows: 100%. Any other contractual cash outflows within the next 30 calendar days must be captured in this standard, such as outflows to cover unsecured collateral borrowings, uncovered short positions, dividends or contractual interest payments. Outflows related to operating costs, however, are not included in this standard.

4 FAQs

FAQ1 *What is the treatment of inflows and outflows of cash and collateral during the next 30 days arising from forward transactions (eg forward repos)?*

The following transactions do not have any impact on a bank's LCR and can be ignored:

- *forward repos, forward reverse repos and forward collateral swaps that start and mature within the LCR's 30-day horizon;*
- *forward repos, forward reverse repos and forward collateral swaps that start prior to and mature after the LCR's 30-day horizon; and*
- *all forward sales and forward purchases of HQLA.*

For forward repos, forward reverse repos and forward collateral swaps that start within the 30-day horizon and mature beyond the LCR's 30-day horizon, the treatments are as follows.

- *Cash outflows from forward reverse repos (with a binding obligation to accept) count towards "other cash outflows" according to LCR40.74 and should be netted against the market value of the collateral received after deducting the haircut applied to the respective assets in the LCR (15% to Level 2A, 25% to RMBS Level 2B assets, and 50% to other Level 2B assets).*
- *Cash inflows from forward repos are "other contractual inflows" according to LCR40.93 and should be netted against the market value of the collateral extended after deducting the haircut applied to the respective assets in the LCR.*
- *In case of forward collateral swaps, the net amount between the market values of the assets extended and received after deducting the haircuts applied to the respective assets in the LCR counts towards "other contractual outflows" or "other contractual inflows" depending on which amount is higher.*

Forward repos, forward reverse repos and forward collateral swaps that start previous to and mature within the LCR's 30-day horizon are treated like repos, reverse repos and collateral swaps according to LCR40.46 to LCR40.48 and LCR40.78 to LCR40.81 respectively.

Note that HQLA collateral held by a bank on the first day of the LCR horizon may count towards the stock of HQLA even if it is sold or repoed forward.

Unsettled sales and purchases of HQLA can be ignored in the LCR. The cash flows arising from sales and purchases of non-HQLA that are executed but not yet settled at reporting date count towards "other cash inflows" and "other cash outflows".

Note that any outflows or inflows of HQLA in the next 30 days in the context of forward and unsettled transactions are only considered if the assets do or will count toward the bank's stock of HQLA. Outflows and inflows of HQLA-type assets that are or will be excluded from the bank's stock of HQLA due to operational requirements are treated like outflows or inflows of non-HQLA.

FAQ2 *Other contractual outflow is determined as 100% as per LCR40.74 of the LCR framework, while other contractual inflows are subject to national discretion as per LCR40.93. Some industry members are concerned about the potential asymmetrical treatment between the two items with respect to unsettled sales and purchases as addressed in LCR40.74 FAQ1. Does this requirement apply broadly to all unsettled trades, ie does it also apply to "open" and "failed" trades, or does it only apply to forwards? Banks which apply settlement date accounting for open trades would not have any "open trades" on their balance sheet and therefore this requirement might create an unlevel playing field for different accounting frameworks.*
Unsettled transactions are addressed in the second to last paragraph of the response to LCR40.74 FAQ1. It refers to any sales or purchases that are executed but not yet settled at reporting date and follows the approach set out for forward transactions. It captures both "open" and "failed" trades if settlement is expected within 30 days irrespective of the balance sheet treatment. In doing so, the response to LCR40.74 FAQ1 allows for a symmetrical treatment by applying "other cash outflows" to executed but not yet settled purchases of non-HQLA and, subject to national discretion, "other cash inflows" to executed but not yet settled sales, while unsettled sales/purchases of HQLA can be ignored.

FAQ3 *What is the treatment of Level 1 and Level 2 assets that are lent/borrowed without any further offsetting transaction (ie no repo/reverse repo or collateral swap) if the assets will be returned or can be recalled during the next 30 days? Are these assets eligible HQLA on the side of the lender or borrower?*
These assets do not count towards the stock of HQLA for either the lender or the borrower. On the side of the borrower, these assets do not enter the LCR calculation. On the lender's side, these assets count towards the "other contractual inflows" amounting to their market value – in the case of Level 2 assets after haircut.

FAQ4 *Does LCR40.74 FAQ3 apply to assets borrowed/lent on an unsecured basis only and not to secured transactions? Is it correct to interpret that the Basel Committee means "reused" when it uses the wording "further offsetting transaction"?*
LCR40.74 FAQ3 refers to assets borrowed/lent on an unsecured basis only. The wording "without any further offsetting transaction" means the absence of a corresponding transfer of cash or securities that would secure the securities borrowing/lending, such as in a repo, reverse repo or collateral swap. If the borrower has reused the securities, there would be an "other contractual cash outflow" to cover unsecured collateral borrowings according to LCR40.74.
The starting point and focus of LCR40.74 FAQ3 (as well as the response to it) is the HQLA eligibility of the assets on the part of either the borrower or the lender. In this context, it is assumed that the borrower has not reused the assets as this would have made the question of HQLA eligibility obsolete anyway. The reuse of the collateral by the borrower, however, introduces an outflow because the borrower may have to source these securities if the borrowing arrangement is not extended.

Cash inflows

40.75

When considering its available cash inflows, the bank must 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, including facilities obtained from a central bank or other party, must not be included in total net cash inflows.

1 FAQ

FAQ1 *Which cash flow assumptions are applied for secured transactions where assets are received on the basis of a collateral pool that is subject to potential collateral substitution? And, does the concept of collateral substitution also apply to inflows for secured borrowing transactions, ie can a bank take an inflow where it has the contractual right to receive HQLA if it was able to pledge available non-HQLA collateral to a secured lender?*
The risks associated with collateral substitution on secured lending transactions with a residual maturity greater than 30 days should be considered as a contingent outflow in accordance with LCR40.55. The contractual right to substitute HQLA collateral for lower-quality or non-HQLA collateral would be a contingent inflow. As such, it is not considered in the LCR in line with LCR40.75.

40.76

Banks and supervisors should monitor the concentration of expected inflows across wholesale counterparties in the context of banks' liquidity management 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 wholesale counterparties.

40.77

In order to prevent banks from relying solely on anticipated inflows to meet their liquidity requirement, and also to ensure a minimum level of HQLA holdings, the amount of inflows that can offset outflows must be capped at 75% of total expected cash outflows as calculated in the standard. This requires that a bank must maintain a minimum amount of stock of HQLA equal to 25% of the total cash outflows.

Cash inflows – secured lending, including reverse repos and securities borrowing

40.78

A bank must 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%). Maturing reverse repurchase or securities lending agreements secured by Level 2 HQLA must lead to cash inflows equivalent to the relevant haircut for the specific assets. A bank is assumed not to roll over maturing reverse repurchase or securities borrowing agreements secured by non-HQLA assets, and may assume to receive back 100% of the cash related to those agreements. Collateralised loans extended to customers for the purpose of taking leveraged trading positions ("margin loans") must also be considered as a form of secured lending; however, for this scenario banks must not recognise 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 LCR40.45 to LCR40.48 and LCR40.73(5).

1 FAQ

FAQ1 *Many margin loans are "overnight" and can be terminated at any time by either side. Others, however, have "term" provisions whereby the bank agrees to make funding available for a given period, but the client is not obliged to draw down on that funding, and where the client has drawn down on the funding, they can repay it at any time. May banks apply LCR40.78 to such margin loans with a contractual maturity beyond 30 days?*
No, LCR40.78 and the table in LCR40.79 are specific to secured loans with a contractual maturity up to and including 30 days. No inflow can be assumed for funds extended under such "term" provisions that give the client the possibility to repay after more than 30 days.

40.79

As an exception to LCR40.78, if the collateral obtained through reverse repo, securities borrowing, or collateral swaps, which matures within the 30-day horizon, is re-used (ie rehypothecated) and is used to cover short positions that could be extended beyond 30 days, a bank must assume that such reverse repo or securities borrowing arrangements will be rolled-over and not give rise to any cash inflows, reflecting its need to continue to cover the short position or to re-purchase the relevant securities. In these cases, the short position should be treated symmetrically and not give rise to any outflows. 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 (ie it has borrowed a security for a given period and lent the security out for a longer period). Short positions must be evaluated at the end of the calculation date; the ability to substitute collateral in the transaction creating the short position must not be considered in determining the inflow rate of the secured lending transaction.

Maturing secured lending transactions backed by the following asset category	Inflow rate (if collateral is not used to cover short positions)	Inflow rate (if collateral is used to cover short positions)
Level 1 assets	0%	0%
Level 2A assets	15%	0%
Level 2B assets: eligible RMBS	25%	0%
Level 2B assets: all other	50%	0%
Margin lending backed by all other collateral	50%	0%
Other collateral	100%	0%

2 FAQs

FAQ1 *Are client shorts covered by external securities borrowings subject to LCR40.79 (under "secured lending, including reverse repos and external securities borrowings") or LCR40.46 ("secured funding run-off")? Firm shorts covered by external securities borrowings are clearly covered by LCR40.79, and it seems more logical that client shorts covered by external securities borrowings should be as well. However, LCR40.46 makes references to customer shorts and the treatment is different?*
The treatments of customer shorts versus firm shorts are separate and distinct and for this reason are addressed in two separate paragraphs. Customer shorts are considered equivalent to other secured financing transactions, as the proceeds from the customer's short sale may be re-used by the facilitating bank to finance the purchase or borrowing of the shorted security. Contrary to firm short positions, customer short positions are initiated and maintained at the discretion of the customer, and therefore the availability of this financing may be uncertain during a period of stress. These characteristics explain why customer shorts are treated in accordance with the roll-off assumption in LCR40.48.

FAQ2 *Can you confirm that the exception rule in LCR40.79 only applies where the reverse repo has a residual maturity of ≤ 30 days and the short position can be extended > 30 days? And, should the reporting institution also apply a 0% outflow to such short positions even if the contractual or expected residual maturity of the shorts is up to 30 days, given that the secured lending transactions covering such shorts are assumed to be extended?*
No, the inflow rates in the third column of the table in LCR40.79 apply to all reverse repos, securities borrowings or collateral swaps where the collateral obtained is used to cover short positions. The reference in the first sentence of LCR40.79 to "short positions that could be extended beyond 30 days" does not restrict the applicability of the 0% inflow rate to the portion of secured lending transactions where the collateral obtained covers short positions with a contractual (or otherwise expected) residual maturity of up to 30 days. Rather, it is intended to point out that the bank must be aware that such short positions may be extended, which would require the bank to roll the secured lending transaction or to purchase the securities in order to keep the short positions covered. In either case, the secured lending transaction would not lead to a cash inflow for the bank's liquidity situation in a way that it can be considered in the LCR. For customer shorts, LCR40.79 only refers to those that could be extended beyond the 30-day horizon, so the reverse repo can be considered to have a maturity within the 30-day LCR time horizon. For firm shorts, LCR40.80 applies a 0% cash inflow rate to the reverse repo, irrespective of the residual maturity, but does not assume any outflow associated with the closure of the firm's short position.

40.80

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 must be recorded as a 100% other contractual outflow according to LCR40.74. If, however, the bank's short position is being covered by a collateralised securities financing transaction, the bank must assume the short position will be maintained throughout the 30-day period and receive a 0% outflow.

40.81

Despite the rollover assumptions in LCR40.78 and LCR40.79, 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.[62] This is especially

the case for non-HQLA collateral, since such outflows are not captured in the LCR framework. Supervisors should monitor the bank's collateral management.

1 Footnote, 1 FAQ

62 *This is in line with Principle 9 of the Sound Principles.*

FAQ1 *Does LCR40.81 of the LCR framework mean to capture specific outflows/inflows or is it rather outlining liquidity risk principles?*
LCR40.81 does not address specific cash flows. Rather, it calls to mind that a bank should be prepared to return any received collateral as soon as it may be recalled by the provider irrespective of the treatment in the LCR.

Cash inflows – Committed facilities

40.82

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

Cash inflows – other inflows by counterparty

40.83

For all other types of transactions, either secured or unsecured, the inflow rate must 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 must be applied. Regarding financial institutions, the bank may generally assume a complete return of liquidity from such institutions, provided the funds are not supporting operational activities as described in LCR40.89. These assumptions may cover both loans and other placements (eg non-operational deposits).

40.84

When considering loan payments, the bank must only include inflows from fully performing loans. Further, inflows must only be taken at the latest possible date, based on the contractual rights available to counterparties. For revolving credit facilities, a bank must assume that the existing loan is rolled over and that any remaining undrawn balances are treated in the same way as a committed facility according to LCR40.64.

40.85

Inflows from loans that have no specific maturity (ie have non-defined or open maturity) must be excluded; therefore, a bank must not make assumptions as to when maturity of such loans would occur. This treatment must also apply to loans that can be contractually terminated

within 30 days, as any inflows exceeding those according the regular amortisation schedule would be “contingent” (in terms of a possible cancellation of the loan) in nature. As an exception to this approach, banks may include minimum payments of principal, fee or interest associated with an open maturity loan, provided that such payments are contractually due within 30 days. These minimum payment amounts should be captured as inflows at the rates prescribed in LCR40.86 and LCR40.87.

40.86

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 may result in inflows. However, banks must assume to continue to extend loans to retail and small business customers, at a rate of 50% of contractual inflows. This results in an inflow of 50% of the contractual amount.

1 FAQ

FAQ1 *What is the treatment in the LCR of unsecured loans in precious metals extended by a bank or deposits in precious metals placed by a bank? Is the treatment for retail and small business customer inflows and other wholesale inflows according to LCR40.86 to LCR40.90 applicable?*
Unsecured loans in precious metals extended by a bank or deposits in precious metals placed by a bank may be treated according to LCR40.86 to LCR40.90 if the loan or deposit uniquely settles in cash. In the case of physical delivery or any optionality to do so, no inflow should be considered.
In deviation from this treatment, jurisdictions may alternatively allow a bank to recognise a cash inflow according to LCR40.86 to LCR40.90 if:

- *contractual arrangements give the bank the choice between cash settlement physical delivery and*
  - *physical delivery is subject to a significant penalty, or*
  - *both parties expect cash settlement; and*
- *there are no factors such as market practices or reputational factors that may limit the bank’s ability to settle the loan or deposit in cash (irrespective of whether physical delivery is subject to a significant penalty).*

Supervisors in such jurisdictions must publicly disclose the treatment should they opt for the alternative treatment.

40.87

All payments (including interest payments and instalments) from wholesale customers that are fully performing and contractually due within the 30-day horizon may result in inflows. Banks must assume 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 results in an inflow percentage of:

1. 100% for financial institution and central bank counterparties; and
2. 50% for non-financial wholesale counterparties.

40.88

Inflows from securities maturing within 30 days not included in the stock of HQLA may be treated in the same category as inflows from financial institutions (ie 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 must be calculated in line with the treatment of other related outflows and inflows covered in this standard. Level 1 and Level 2 assets maturing within 30 days must be included in the stock of liquid assets and must not be considered as inflows, provided that they meet all operational and definitional requirements as laid out in LCR30.13 to LCR30.45. Payments arising from Level 1 and Level 2 assets which settle within 30 days that do not meet the operational requirements may be considered as inflows.

1 FAQ

FAQ1 *Can inflows from maturing securities in a collateral pool for covered bonds be considered as inflows?*
Yes, inflows are not subject to operational requirements. Hence, these inflows are not per se excluded from the LCR even if the maturing securities are (or have been) excluded from the stock of HQLA due to being "encumbered" according to LCR30.16. However, if the matured securities need to be substituted in the collateral pool within the 30-day horizon, an "other outflow" per LCR40.74 should be considered amounting to the liquidity value of these securities in the LCR.

40.89

Deposits held at other financial institutions for operational purposes, as outlined in LCR40.26 to LCR40.36, such as for clearing, custody, and cash management purposes, must be assumed to stay at those institutions – ie they must receive a 0% inflow rate, as noted in LCR40.31. The same methodology applied in LCR40.26 to LCR40.36 for operational deposit outflows should also be applied to determine if deposits held at another financial institution are operational deposits and receive a 0% inflow. As a general principle if the bank receiving the deposit classifies the deposit as operational, the bank placing it should also classify it as an operational deposit. Notwithstanding the exclusion of deposit liabilities raised from correspondent banking activities from the treatment of operational deposits, as described in LCR40.32, deposits placed for the purpose of correspondent banking are held for operational purposes and, as such, must receive a 0% inflow rate. However, a 100% inflow rate may be applied to the amount for which the bank is able to determine that the funds are "excess balances" in the sense of LCR40.29 to LCR40.30, ie they are not tied to operational purposes and may be withdrawn within 30 days.

40.90

The same treatment applies for deposits held at the centralised institution in a cooperative banking network, that are assumed to stay at the centralised institution, as outlined in LCR40.37 to LCR40.39; in other words, the depositing bank must not count any inflow for these funds – ie they must receive a 0% inflow rate.

Cash inflows – other cash inflows

40.91

The sum of all net derivative cash inflows must receive a 100% inflow factor. The amounts of derivatives cash inflows and outflows must be calculated in accordance with the methodology described in LCR40.49.

40.92

Where derivatives are collateralised by HQLA, cash inflows must be calculated net of any corresponding cash or contractual collateral outflows that would result, all other things being equal, from contractual obligations for cash or collateral to be posted by the bank, given these

contractual obligations would reduce the stock of HQLA. This is in accordance with the principle that banks must not double-count liquidity inflows or outflows.

40.93

Other contractual cash inflows may be included at national discretion. Inflow percentages may be determined as appropriate for each type of inflow by supervisors in each jurisdiction. Cash inflows related to non-financial revenues are not taken into account in the calculation of the net cash outflows for the purposes of this standard.

4 FAQs

FAQ1 *What is the treatment of inflows and outflows of cash and collateral during the next 30 days arising from forward transactions (eg forward repos)?*
The following transactions do not have any impact on a bank's LCR and can be ignored:

- *forward repos, forward reverse repos and forward collateral swaps that start and mature within the LCR's 30-day horizon;*
- *forward repos, forward reverse repos and forward collateral swaps that start prior to and mature after the LCR's 30-day horizon; and*
- *all forward sales and forward purchase of HQLA.*

For forward repos, forward reverse repos and forward collateral swaps that start within the 30-day horizon and mature beyond the LCR's 30-day horizon, the treatments are as follows.

- *Cash outflows from forward reverse repos (with a binding obligation to accept) count towards "other cash outflows" according to LCR40.74 and should be netted against the market value of the collateral received after deducting the haircut applied to the respective assets in the LCR (15% to Level 2A, 25% to RMBS Level 2B assets, and 50% to other Level 2B assets).*
- *Cash inflows from forward repos are "other contractual inflows" according to LCR40.93 and should be netted against the market value of the collateral extended after deducting the haircut applied to the respective assets in the LCR.*
- *In case of forward collateral swaps, the net amount between the market values of the assets extended and received after deducting the haircuts applied to the respective assets in the LCR counts towards "other contractual outflows" or "other contractual inflows" depending on which amount is higher.*

Forward repos, forward reverse repos and forward collateral swaps that start previous to and mature within the LCR's 30-day horizon are treated like repos, reverse repos and collateral swaps according to LCR40.46 to LCR40.48 and LCR40.78 to LCR40.81 respectively.
Note that HQLA collateral held by a bank on the first day of the LCR horizon may count towards the stock of HQLA even if it is sold or repoed forward.
Unsettled sales and purchases of HQLA can be ignored in the LCR. The cash flows arising from sales and purchases of non-HQLA that are executed but not yet settled at reporting date count towards "other cash inflows" and "other cash outflows".
Note that any outflows or inflows of HQLA in the next 30 days in the context of forward and unsettled transactions are only considered if the assets do or will count toward the bank's stock of HQLA. Outflows and inflows of HQLA-type assets that are or will be excluded from the bank's stock of HQLA due to operational requirements are treated like outflows or inflows of non-HQLA.

FAQ2 *Other contractual outflow is determined as 100% as per LCR40.74 of the LCR framework, while other contractual inflows are subject to national discretion as per LCR40.93. Some industry members are concerned about the potential asymmetrical treatment between the two items with respect to unsettled sales and purchases as addressed in LCR40.93 FAQ1. Does this requirement apply broadly to all unsettled trades, ie does it also apply to "open" and "failed" trades, or does it only apply to forwards? Banks which apply settlement date accounting for open trades would not have any "open trades" on their balance sheet and therefore this requirement might create an unlevel playing field for different accounting frameworks.*
Unsettled transactions are addressed in the second to last paragraph of the response to LCR40.93 FAQ1. It refers to any sales or purchases that are executed but not yet settled at reporting date and follows the approach set out for forward transactions. It captures both "open" and "failed" trades if settlement is expected within 30 days irrespective of the balance sheet treatment. In doing so, the response to LCR40.93 FAQ1 allows for a symmetrical treatment by applying "other cash outflows" to executed but not yet settled purchases of non-HQLA and, subject to national discretion, "other cash inflows" to executed but not yet settled sales, while unsettled sales/purchases of HQLA can be ignored.

FAQ3 *What is the treatment of Level 1 and Level 2 assets that are lent/borrowed without any further offsetting transaction (ie no repo/reverse repo or collateral swap) if the assets will be returned or can be recalled during the next 30 days? Are these assets eligible HQLA on the side of the lender or borrower?*
These assets do not count towards the stock of HQLA for either the lender or the borrower. On the side of the borrower, these assets do not enter the LCR calculation. On the lender's side, these assets count towards the "other contractual inflows" amounting to their market value – in the case of Level 2 assets after haircut.

FAQ4 *Does LCR40.93 FAQ3 apply to assets borrowed/lent on an unsecured basis only and not to secured transactions? Is it correct to interpret that the Basel Committee means "reused" when it uses the wording "further offsetting transaction"?*
LCR40.93 FAQ3 refers to assets borrowed/lent on an unsecured basis only. The wording "without any further offsetting transaction" means the absence of a corresponding transfer of cash or securities that would secure the securities borrowing/lending, such as in a repo, reverse repo or collateral swap. If the borrower has reused the securities, there would be an "other contractual cash outflow" to cover unsecured collateral borrowings according to LCR40.74.
The starting point and focus of LCR40.93 FAQ3 (as well as the response to it) is the HQLA eligibility of the assets on the part of either the borrower or the lender. In this context, it is assumed that the borrower has not reused the assets as this would have made the question of HQLA eligibility obsolete anyway. The reuse of the collateral by the borrower, however, introduces an outflow because the borrower may have to source these securities if the borrowing arrangement is not extended.

LCR90

Transition

This chapter transition requirements for countries receiving financial support for macroeconomic and structural reforms.

Version effective as of 15 December 2019

First version in format of consolidated framework.

90.1

The minimum Liquidity Coverage Ratio requirement of 100% is effective from 1 January 2019.

90.2

However, individual countries that are receiving financial support for macroeconomic and structural reform purposes may choose a different implementation schedule for their national banking systems, consistent with the design of their broader economic restructuring programme.

LCR99

Application guidance

This chapter summarises the components of high-quality liquid assets and the run-off factors applied to cash outflows and additional requirements under the Liquidity Coverage Ratio.

Version effective as of 15 December 2019

First version in format of consolidated framework.

99.1

The table below summarises the Liquidity Coverage Ratio (LCR; percentages are factors to be multiplied by the total amount of each item).

Item	Factor
Stock of high-quality liquid assets (HQLA)	
A. **Level 1 assets**	
- Coins and bank notes - Qualifying marketable securities from sovereigns, central banks, public sector entities (PSEs) and multilateral development banks - Qualifying central bank reserves - Domestic sovereign or central bank debt for non-0% risk-weighted sovereigns	100%
B. **Level 2 assets (maximum 40% of HQLA)**	
Level 2A assets: - Sovereign, central bank, multilateral development banks and PSE assets qualifying for 20% risk weighting - Qualifying corporate debt securities rated AA- or higher - Qualifying covered bonds rated AA- or higher	85%
Level 2B assets (maximum of 15% of HQLA)	
- Qualifying residential mortgage-backed securities (RMBS)	75%
- Qualifying corporate debt securities rated between A+ and BBB- - Qualifying common equity shares - Sovereign, central bank and PSE debt securities rated BBB- or higher that do not qualify as a Level 1 or Level 2A asset.	50%
Total value of stock of HQLA	
Cash outflows	
A. **Retail deposits**	
Demand deposits and term deposits (less than 30 days maturity):	
- Stable deposits (deposit insurance scheme meets additional criteria)	3%

- Stable deposits	5%
- Less stable retail deposits	10%
Term deposits with residual maturity greater than 30 days	0%
B. **Unsecured wholesale funding**	
Demand deposits and term deposits (less than 30 days maturity) provided by small business customers:	
- Stable deposits	5%
- Less stable deposits	10%
Operational deposits generated by clearing, custody and cash management activities	25%
- Portion covered by deposit insurance	5%
Cooperative banks in an institutional network (qualifying deposits with the centralised institution)	25%
Non-financial corporates, sovereigns, central banks, multilateral development banks and PSEs	40%
- If the entire amount fully covered by deposit insurance scheme	20%
Other legal entity customers	100%
C. **Secured funding**	
- Secured funding transactions with a central bank counterparty or backed by Level 1 assets with any counterparty	0%
- Secured funding transactions backed by Level 2A assets, with any counterparty	15%
- Secured funding transactions backed by non-Level 1 or non-Level 2A assets, with domestic sovereigns, multilateral development banks, or domestic PSEs as a counterparty - Backed by RMBS eligible for inclusion in Level 2B	25%
- Backed by other Level 2B assets	50%
- All other secured funding transactions	100%

D. **Additional requirements**	
Liquidity needs (eg collateral calls) related to financing transactions, derivatives and other contracts	3 notch downgrade
Market valuation changes on derivatives transactions (largest absolute net 30-day collateral flows realised during the preceding 24 months)	Look-back approach
Valuation changes on non-Level 1 posted collateral securing derivatives	20%
Excess collateral held by a bank related to derivative transactions that could contractually be called at any time by its counterparty	100%
Liquidity needs related to collateral contractually due from the reporting bank on derivatives transactions	100%
Increased liquidity needs related to derivative transactions that allow collateral substitution to non-HQLA assets	100%
Asset-backed commercial paper (ABCP), structured investment vehicles (SIVs), conduits, special purpose entities (SPEs) etc: - Liabilities from maturing ABCP, SIVs, SPEs etc (applied to maturing amounts and returnable assets) - Asset-backed securities (including covered bonds) applied to maturing amounts	100%
Currently undrawn committed credit and liquidity facilities provided to:	
- Retail and small business clients	5%
- Non-financial corporates, sovereigns and central banks, multilateral development banks and PSEs	10% for credit 30% for liquidity
- Banks subject to prudential supervision	40%
- Other financial institutions (include securities firms, insurance companies)	40% for credit 100% for liquidity
- Other legal entity customers, credit and liquidity facilities	100%
Other contingent funding liabilities (such as guarantees, letters of credit, revocable credit and liquidity facilities etc)	National discretion
- Trade finance	0-5%

- Customer short positions covered by other customers’ collateral	50%
Any additional contractual outflows	100%
Net derivative cash outflows	100%
Any other contractual cash outflows	100%
Total cash outflows	
Cash inflows	
Maturing secured lending transactions backed by the following collateral:	
Level 1 assets	0%
Level 2A assets	15%
Level 2B assets	
- Eligible RMBS	25%
- Other assets	50%
Margin lending backed by all other collateral	50%
All other assets	100%
Credit or liquidity facilities provided to the reporting bank	0%
Operational deposits held at other financial institutions (include deposits held at centralised institution of network of co-operative banks)	0%
Other inflows by counterparty:	
- Amounts to be received from retail counterparties	50%
- Amounts to be received from non-financial wholesale counterparties, from transactions other than those listed in above inflow categories	50%
- Amounts to be received from financial institutions and central banks, from transactions other than those listed in above inflow categories.	100%
Net derivative cash inflows	100%

Other contractual cash inflows	National discretion
Total cash inflows	
Total net cash outflows = Total cash outflows minus min [total cash inflows, 75% of gross outflows]	
LCR = Stock of HQLA / Total net cash outflows	