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Delegated regulation on liquidity coverage requirement for credit institutions

Scope, context and entry in force of this Regulation

On 10 October 10 2014, the European commission published a regulation under the delegated act that lays down rules to specify in detail the liquidity coverage requirement provided for in Article 412(1) of Regulation (EU) No. 575/2013 (i.e. CRR).

Having considered the specificities of the EU banking system, the Commission adopted in this regulation a number of adjustments in comparison to the Basel LCR standard to account for the diverse population of entities operating in the EU. Unless the European Parliament and Council issue objections regarding this regulation, the commission suggests an entry into force as from 1 October 2015 with the following transitional provisions:

a. 60% of the liquidity coverage requirement as from 1 October 2015
b. 70% as from 1 January 2016;
c. 80% as from 1 January 2017;
d. 100% as from 1 January 2018;

The scope of application of this detailed LCR regulation has been limited to credit institutions, investment firms being still subject to the general liquidity requirement under article 412(1) of the CRR.

Significant innovations of the Commission Delegated Regulation (EU) of 10 October 2014

List of eligible liquid assets

The commission has enlarged the pool of assets eligible for the LCR calculation, giving recognition to some covered bonds and securitised assets that showed excellent liquidity performance during the liquidity crisis. Shares, corporate debt, restricted-use committed liquidity facilities, units in CIUs or deposits in specific institutions are also eligible as liquid assets, under certain conditions and up to a certain amount.

Composition of the liquidity buffer

Eligible assets are split in three groups: Level 1 (“extremely high liquidity and credit quality”), Level 2A and Level 2B (“high liquidity and credit quality”). The part of Level 2 assets shall not exceed 40% as illustrated below.

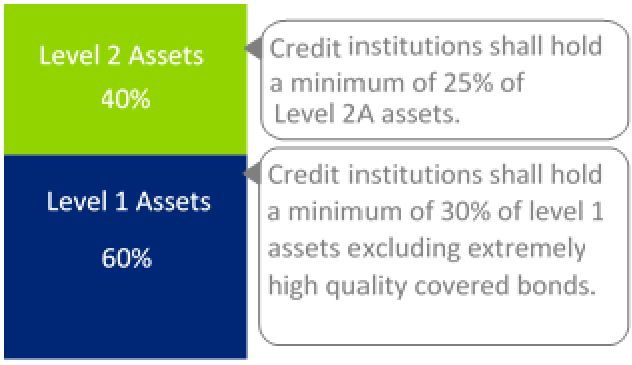

Figure 1 - Composition of the liquidity buffer by asset level

Some further caps have been introduced, limiting the portion of the pool of liquid assets to 70% for covered bonds eligible as Level 1, 40% for each individual category of Level 2A assets and 15% for each individual category of Level 2B assets. Furthermore, haircuts (ranging from 7% to 50%) should be applied to the market value of those various assets.

Net liquidity outflows and exemptions to the inflow cap

The principle for the calculation of the net liquidity outflows remains unchanged. However, the Commission made amendments to and provided further clarifications on some technical features. Of particular interest, the net liquidity outflows are precisely defined, with some inflows being fully or partially exempted from the inflow cap. Subject to the prior approval of the competent authority and under certain constraints, credit institutions may fully or partially exempt the following liquidity inflows from the cap:

- Inflows where the provider is a parent or a subsidiary of the credit institution;
- Inflows from deposits placed with other credit institutions within a group of entities qualifying for the treatment set out in Article 113(6) or (7) of Regulation (EU) No 575/2013;
- Inflows with inter-dependent outflows.

Under specific conditions and subject to the prior approval of the competent authority, specialised credit institutions may be subject to a cap on inflows of 90%.

These exemptions are important for the Luxembourg market place as these inflows are commonly encountered in banks. The possibility to calculate some outflows on a net basis when interdependent inflows exist should be closely analysed and minimum criteria that must be met to benefit from this option should be duly assessed.

The information provided in this alert focuses on the key elements of the regulation and multiple other technical details are provided to guide credit institutions through the calculation of the LCR, which is to be reported to the CSSF on a monthly basis. We trust this information is of assistance and remain at your disposal for any question on the subject.

We trust this information is of assistance and remain at your disposal for any further questions.

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