



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Consultation Paper | CP27/14

CRD IV: Liquidity

November 2014

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This consultation paper proposes changes to the Prudential Regulation Authority (PRA) rules and guidance, to accommodate the introduction of the European Union liquidity coverage requirement.

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Responses are requested by Friday 27 February 2015.

Please address any comments or enquiries to:

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1 Overview

1.1 On 10 October 2014, the European Commission published a delegated act to supplement EU Regulation (EU) No 575/2013 with regard to the liquidity coverage requirement for credit institutions ('Delegated Act'). This legislation is due to enter into force by 31 December 2014. It will be directly applicable in the United Kingdom from 1 October 2015.⁽¹⁾

1.2 In light of this, the Prudential Regulation Authority (PRA) must revoke existing rules where appropriate, and restate its overall approach to regulating liquidity. The PRA proposes to revoke the liquidity standards contained in Chapter 12 of the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU 12) at the point at which the Delegated Act applies as a regulatory standard in the European Union (EU). New rules are proposed to implement the PRA's approach to liquidity supervision (Appendix 2). Consequential amendments will be made to the liquidity reporting requirements in Chapter 16 of the Supervision handbook (SUP 16), and to the PRA Fundamental Rules (Appendix 2). The PRA will consult on further consequential amendments to its rules that are necessary to implement its new liquidity regime.⁽²⁾

1.3 This consultation paper (CP) seeks views on draft rules and a draft supervisory statement (Appendix 1) which set out the PRA's proposed update to its liquidity regime. This consultation is relevant to UK banks, building societies and UK-designated investment firms ('firms').⁽³⁾ It is also relevant to third country firms that are banks or designated investment firms, and European Economic Area (EEA) credit institutions that have a branch in the United Kingdom.

Background

1.4 The Basel Committee on Banking Supervision (BCBS) introduced the Liquidity Coverage Ratio in 2013.⁽⁴⁾ This standard aims to ensure that a bank has an adequate stock of unencumbered liquid assets that consists of cash, or assets that can be converted into cash at little or no loss of value in private markets, to meet its liquidity needs for a thirty calendar day liquidity stress scenario. The BCBS highlighted the importance of liquidity to the functioning of financial markets and the banking sector, as demonstrated by the 2007–08 crisis: many banks experienced difficulties because they did not manage their liquidity in a prudent manner. This contributed to the failure of several institutions. The BCBS therefore introduced new liquidity standards as part of

'Basel III', a new international regulatory framework for banks, in June 2013.

1.5 In June 2013, the EU published legislation to implement Basel III. The legislation replaced the previous capital requirements directives with two new instruments: the Capital Requirements Directive (CRD)⁽⁵⁾ and the Capital Requirements Regulation (CRR),⁽⁶⁾ collectively known as CRD IV. The PRA implemented the majority of CRD IV, including several national discretions relating to the liquidity regime, in December 2013.⁽⁷⁾ The Delegated Act specifies the general liquidity coverage requirement (LCR) as per CRR Article 412, and the circumstances under which competent authorities have to impose specific inflow and outflow levels on credit institutions in order to capture the specific risk to which they are exposed, as per CRR Article 460.

1.6 In October 2009, the Financial Services Authority (FSA) introduced a far-reaching overhaul of the UK liquidity regime, in FSA PS09/16.⁽⁸⁾ This regime was implemented in BIPRU 12, which was subsequently designated by the PRA. Readers should note that the PRA's updated approach to supervising liquidity risk, as set out here and in the draft supervisory statement, carries forward the broad principles established in the previous liquidity regime. In particular, firms should note that liquidity buffers can — and should — be used in times of stress (see Appendix 1, paragraphs 6.1 to 6.3).

1.7 The PRA expects this CP to be read in conjunction with the Delegated Act, the draft supervisory statement and rules set out in the Appendices, and all relevant European Banking Authority (EBA) material, in order to gain a full understanding of the proposed update to its liquidity regime.

(1) European Commission: 'Commission Delegated Regulation (EU) [No.../.. of XXX] to supplement EU Regulation (EU) No 575/2013 with regard to liquidity coverage requirement for Credit Institutions', http://ec.europa.eu/internal_market/bank/docs/regcapital/acts/delegated/141010_delegated-act-liquidity-coverage_en.pdf.

(2) This will likely be in the form of an Occasional Consultation Paper.

(3) UK-incorporated investment firms regulated by the PRA are referred to as UK-designated investment firms. This distinguishes them from both non-UK incorporated designated investment firms and FCA-regulated investment firms.

(4) BCBS, 'Basel III: The Liquidity Coverage Requirement and liquidity risk monitoring tools', January 2013; www.bis.org/publ/bcbs238.pdf.

(5) Directive 2013/36/EU; <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:176:0338:0436:EN:PDF>.

(6) Regulation (EU) No 575/2013: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:321:0006:0342:EN:PDF>.

(7) PRA Policy Statement PS7/13, 'Strengthening capital standards: implementing CRD IV, feedback and final rules', December 2013; www.bankofengland.co.uk/pradocuments/publications/ps/2013/ps713.pdf.

(8) FSA Policy Statement 09/16, 'Strengthening liquidity standards', October 2009; www.fsa.gov.uk/pubs/policy/ps09_16.pdf.

1.8 The Delegated Act only applies to credit institutions. To ensure a consistent approach to liquidity supervision between UK banks and building societies and UK-designated investment firms, the PRA proposes to make a rule which will require UK-designated investment firms to comply with the obligations laid down in the Delegated Act (see Section III, Chapter 6). UK-designated investment firms should read any reference to the Delegated Act in this CP accordingly.

1.9 Until the EEA Joint Committee amends the EEA Agreement with a view to permitting simultaneous application of the CRR liquidity standards in the EEA States, the CRR liquidity standards only apply within the EU. The PRA proposes to make rules on the assumption that the EEA Joint Committee will incorporate the CRR liquidity standards into the EEA Agreement. Before this happens however, the PRA proposes transitional rules to ensure that:

- EEA credit institutions with their head offices outside the EU be treated, in relation to their UK branches, like third country firms; and
- the level of application of the proposed PRA's new liquidity regime mirrors the level of application of the CRR liquidity standards.

The PRA proposes to revoke these transitional rules when the CRR liquidity standards are incorporated into the EEA Agreement. The proposed transitional rules are set out in Appendices 2.A (Rule 15) and 2.D (Rule 4).

Structure

1.10 This CP is structured as follows:

- Section I details how the PRA proposes to carry out the transition to its new liquidity regime, taking into account the Delegated Act that will apply from 1 October 2015.
- Section II explains what requirements the PRA proposes to place on firms beyond meeting the LCR.
- Section III details the elements of the PRA's proposed new regime which will not be covered by EU legislation.
- Section IV contains a cost benefit analysis of the proposals.

1.11 The draft supervisory statement is included as Appendix 1; the draft rules are included as Appendix 2. Appendix 3 provides a mapping of BIPRU 12 rules to the Internal Liquidity Adequacy Assessment (ILAA) Part of the PRA Rulebook.

Statutory Obligations

1.12 In discharging its general functions of making rules and determining the general policy and principles, the PRA must, so far as is reasonably possible, act in a way that advances its two objectives: that is, its general objective to promote the safety and soundness of PRA-authorised persons,⁽¹⁾ and its secondary objective to facilitate effective competition.⁽²⁾

1.13 The purpose of the revised liquidity regime is to continue to address a number of market and regulatory failures in relation to firms' liquidity risk management, detailed in the cost benefit analysis section of this document: in this way it supports the PRA's general objective of promoting the safety and soundness of firms. In addition, by fully and clearly restating the whole liquidity regime, the PRA is helping firms understand its expectations of them, which also helps the PRA meet its safety and soundness objective.

1.14 In light of the introduction from 1 March 2014 of a statutory secondary competition objective for the PRA, the PRA has assessed whether the content of this consultation facilitates effective competition in markets for services provided by PRA-authorised persons in carrying out regulated activities. The PRA considers that the transition to the LCR will put internationally active UK firms on a level playing field with other, non-UK firms with an international presence: the LCR is being implemented, albeit in a different form, by all members of the Basel Committee, and the EU definition of the LCR will be applied across all EU Member States. Domestically, the new Pillar 1 regime⁽³⁾ will put both larger and smaller UK firms on a level playing field. However, the PRA recognises that the removal of the simplified Individual Liquidity Assessment Standards (ILAS)⁽⁴⁾ modification will increase the compliance costs for those firms that previously benefited from it. Offsetting this, at least partially, the PRA's Pillar 2 approach will be proportionate to each firm's business model.

1.15 In making its rules and establishing its practices and procedures the PRA must have regard to the Regulatory Principles.⁽⁵⁾ The PRA considers that this proposal is compatible with the Regulatory Principles. In particular, section 3B(1)(a) of the Financial Services and Markets Act (FSMA) provides that the resources of each regulator should be used in the most efficient and economic way. Section 3B(1)(b) of FSMA provides that the principle that a burden or restriction which is imposed on a person, or, on the carrying out of an activity, should be proportionate to the

(1) Section 2(b) of the Financial Services and Markets Act (FSMA) 2000 (General Objective).

(2) Section 2(h) of FSMA 2000 (Secondary Objective).

(3) Please see paragraph 2.3 and the associated footnote for a definition of the Pillar 1 standard.

(4) Please see Chapter 5 for a definition of ILAS.

(5) Section 138J(3)(b) of FSMA 2000.

benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction.

1.16 In addition, when consulting on draft rules, the PRA is required to consider:

- equality and diversity;
- the impact on mutuals; and
- the impact on competition.

1.17 The impact on competition is addressed in paragraph 1.14. The impact on mutuals, and equality and diversity, are considered below. The PRA is also required to perform a cost benefit analysis of the impact of its policy proposals: this is contained in Section IV.

Equality and Diversity

1.18 As a public body, the PRA is subject to the provisions of the Public Sector Equality Duty (PSED) which forms part of the Equality Act 2010. The PSED requires that when the PRA is exercising its public functions, it has due regard to the need for eliminating unlawful discrimination, advancing equality of opportunity and fostering good relations between people who share a protected characteristic. To meet this requirement, the PRA has performed an assessment of the equality and diversity implications of any new policy proposal considered. In general the PRA finds that the issues addressed in this CP do not give rise to equality and diversity implications.

1.19 The Delegated Act applies directly to PRA-regulated firms. It contains a number of derogations towards the eligibility of assets within a firm's High Quality Liquid Assets (HQLA) buffer that are only available to firms that are unable to hold interest-bearing assets for reasons of religious observance. These derogations support the ability of these firms to meet the requirements of the Delegated Act.

Impact on mutuals

1.20 The proposal will affect mutuals as they are within scope of the proposed new rules. The PRA does not expect the impact on mutuals to be significantly different from the impact on other firms.⁽¹⁾ Based on a recent survey of the costs to firms of compliance with Common Reporting (COREP) and Financial Reporting (FINREP), the PRA estimates that the impact on mutuals of the LCR reporting requirements will not be substantially different from that on other similarly sized (non-mutual) institutions. However, the simplified regime that was available under BIPRU 12 (ILAS regime), to firms operating a relatively simple business model, will no longer apply: firms previously operating under this simplified regime will have to calculate the same LCR as other firms, whereas previously they were able to calculate their liquid asset buffer requirement through a simplified formula. They will also need to apply the same stress testing approach as other firms. This means that, aside from reporting costs, the new regime will

impose a higher burden on some smaller firms, including mutuals, than the current BIPRU 12 regime. That burden, however, will not be higher than that imposed on other firms in the new regime. And, as explained above, the PRA's Pillar 2 approach will be proportionate to each firm's business model, which will offset this higher burden, at least partially.

Key proposals

1.21 The main proposals put forward in this CP are as follows:

- To revoke BIPRU 12. This includes revoking the simplified ILAS regime and the requirement on firms to undertake standardised stress testing.
- To carry forward the broad principles established in BIPRU 12 into the new regime.
- To apply a transition to 100% LCR on 1 January 2018 in the following steps: an 80% requirement from 1 October 2015, rising to 90% on 1 January 2017.
- To carry forward existing add-ons not covered in the LCR as the new Pillar 2 add-ons, until each firm's next liquidity review.
- To establish a new rule to require that firms ensure their systems and processes enable them to report all COREP liquidity returns daily, as required by the PRA.
- To maintain reporting of FSA047 and FSA048 for a period of up to two years after the introduction of the full suite of COREP liquidity returns in 2015.
- To require that firms integrate fully the operational requirements outlined in Delegated Act Article 8.
- To propose that if pre-positioned assets are not eligible for inclusion in the HQLA buffer, they cannot be used to meet the PRA's quantitative liquidity guidance.
- To propose that UK-designated investment firms be subject to the obligations stated in the Delegated Act, with any necessary amendments, to bring their obligations in line with those applied to UK banks and building societies.
- To propose that third country firms be subject to a requirement to provide liquidity information on a whole-firm basis.

(1) Section 138K(2) of FSMA 2000.

Responses and next steps

1.22 This consultation closes on Friday 27 February 2015. Views are welcomed on the proposals made in this CP and respondents are requested to structure their responses by chapter.

1.23 In particular respondents may wish to comment on:

- The proposed transition path to the LCR, including the proposal for interim Pillar 2 add-ons.
- The proposal to retain reporting on FSA047 and FSA048 for up to two years after the introduction of the full suite of COREP liquidity returns in 2015.

- How the PRA is intending to apply requirements beyond the LCR.
- The PRA's specific proposals for UK-designated investment firms, and for third country firms.
- The content of the draft supervisory statement.

1.24 The PRA intends to discuss with firms their preparations for the introduction of the LCR, and would welcome their views on issues arising from its implementation.

1.25 The PRA intends to publish a policy statement with feedback, final rules and a supervisory statement in 2015.

Section I:

Transition to the new liquidity regime

2 Switching off BIPRU 12 and phasing in the LCR

2.1 This chapter sets out the PRA's proposal for switching off the current BIPRU 12 regime, withdrawing existing firm-specific Individual Liquidity Guidance (ILG),⁽¹⁾ and phasing in the LCR in accordance with CRR Article 412(5). It also details the PRA's interim approach to setting Pillar 2 requirements in the new regime, and includes a proposal for collecting LCR returns in the event that reporting on the revised template is delayed until after the LCR is introduced on 1 October 2015.⁽²⁾

2.2 Delegated Act Article 38 provides for a phasing-in of the LCR ratio from 1 October 2015 until 1 January 2018. Competent authorities are permitted by CRR Article 412(5) to require domestically authorised institutions, or a subset of those institutions, to maintain a higher LCR than the minimum phase-in path, up to 100%, until the LCR is fully introduced at a rate of 100% in accordance with CRR Article 460.

2.3 The LCR is a Pillar 1 standard, ie it is a set of measures that applies to all firms in the same way.⁽³⁾ CRD Articles 104 and 105 provide discretion for competent authorities to set additional Pillar 2 liquidity requirements. The existing UK regime is not based on a Pillar 1/Pillar 2 approach. But it is similar in effect: an individual firm's ILG is based on a standardised stress test, and add-ons reflect firm-specific risks.

2.4 The draft supervisory statement is in Appendix 1, and the draft rules are contained in Appendix 2.B.

Proposals

Revoking BIPRU 12 and withdrawing existing ILG

2.5 The PRA proposes to revoke the liquidity standards contained in BIPRU 12 and to withdraw firm-specific guidance on liquid asset buffers contained in firms' ILG, at the point at which the LCR comes into effect (1 October 2015). This includes revoking the simplified ILAS regime. The PRA will send new guidance letters to firms as appropriate, and notably where firms have existing add-ons. In the interim, the transitional provisions outlined in the rest of this chapter apply as a default.

2.6 These proposals ensure that firms are subject to a single set of liquidity standards at any one time. The PRA

understands that it would be operationally difficult for firms to operate to two such sets at the same time.

LCR phase-in

2.7 The PRA proposes to set the LCR at 80% from 1 October 2015. This requirement would apply until the end of 2016. The requirement would then rise to 90% on 1 January 2017. It would reach 100% on 1 January 2018, as required by CRR (Table A).

Table A Comparison of liquidity coverage requirements during the transition period

Date	Minimum path — CRR Article 460	Proposed PRA path
From 1 October 2015	60%	80%
From 1 January 2016	70%	80%
From 1 January 2017	80%	90%
From 1 January 2018	100%	100%

2.8 In choosing the initial minimum requirement for the LCR, the PRA had regard to the Financial Policy Committee's (FPC's) recommendation to the PRA in June 2013 which stated that: 'In assessing the liquidity of banks and building societies, the PRA should employ, among other measures, the Liquidity Coverage Ratio (LCR) as defined in the EU's implementation of the Basel standard. The minimum requirement should be set at 80% until 1 January 2015, rising thereafter to reach an LCR of 100% on 1 January 2018.'⁽⁴⁾ The FPC concluded that as a

- (1) Readers should note that when used with capital letters, or as the acronym ILG, the term 'Individual Liquidity Guidance' refers to the quantitative liquidity requirement set on firms under BIPRU 12. When used without capital letters, and fully spelt out, the term 'individual liquidity guidance' refers to the more general guidance given to firms, including qualitative elements.
- (2) The Pillar 2 review is any activity on the part of a supervisor to assess a firm's compliance with the overall Pillar 2 rule. The review includes an assessment of the strategies, processes and systems a firm has in place to identify and manage the risks to which it is exposed or might be exposed and the risk that it might not be able to meet the obligations in Part Three of the CRR. One part of this review is an assessment of the adequacy of the financial resources a firm must hold to comply with any Pillar 1 requirements as well as those resources held for risks not covered under Pillar 1.
- (3) Note, however, that the LCR is not a Pillar 1 'minimum': falling below the applicable LCR is not automatically associated with breaching the PRA's Threshold Conditions. Please see Section 6 of the draft supervisory statement (Appendix 1) for further details on the PRA's expectations of firms that fall below the level of quantitative individual liquidity guidance.
- (4) Bank of England, 'Record of the Financial Policy Meeting', 18 June 2013, page 2; www.bankofengland.co.uk/publications/Documents/records/fpc/pdf/2013/record1307.pdf.

general policy, setting this transition path would provide the banking system with greater flexibility and could support economic recovery without compromising financial stability. In particular, the FPC noted that the impact of looser liquidity requirements on credit conditions was uncertain. But by removing possible impediments to an expansion of credit supply, it intended to give the banking system more flexibility to lend.⁽¹⁾ The PRA confirmed on 28 August 2013 that it would implement this recommendation.⁽²⁾

2.9 The PRA considers that the proposal would provide a balance between: on the one hand, ensuring that the new requirements imposed on firms do not represent a significant weakening of existing standards; and, on the other hand, ensuring that the transition is not overly abrupt and does not risk temporarily constraining banks' ability to extend credit to the real economy.

2.10 **Question:** The PRA invites comments on its proposed transition path to 100% LCR in 2018.

Interim Pillar 2 approach

2.11 As detailed in Section 3 of the draft supervisory statement, the PRA plans to adopt an interim Pillar 2 approach based on firms' existing ILG add-ons. Where current add-ons relate to risks not captured in the LCR, the PRA proposes to continue applying them at the same absolute amounts as previously: these will become the new Pillar 2 add-ons, as an interim measure until the PRA can carry out a liquidity review of the firm. Specifically, fixed add-ons that are applicable on 30 September 2015 would continue to apply from 1 October 2015 at the same absolute amounts: this covers all add-ons except those relating to prime brokerage and derivatives. Box 1 illustrates the proposed approach with an example. Initially, and until the PRA can carry out a liquidity review of the firm, each add-on will apply at the individual level. In addition, if the firm must comply with CRR Part 6 (Liquidity) on a consolidated level, then the add-on will also apply at the consolidated level.

2.12 The type of HQLA held to meet interim ILG add-ons should be no wider than defined in the Delegated Act, and it should follow the same composition set out in the Delegated Act for Levels 1, 2A and 2B assets.

2.13 In due course and as the PRA's resources permit a review of each firm's liquidity, the PRA intends to revise its approach to assessing liquidity risk management in line with the 'Draft Guidelines for common procedures and methodologies for the supervisory review and evaluation process under Article 107 (3) of Directive 2013/36/EU' ('EBA SREP guidelines').⁽³⁾ The PRA expects firms to have robust processes in place to identify and manage their liquidity risks until the PRA is able to set refreshed firm-specific guidance.

Box 1 Interim add-on illustration

Under BIPRU 12, a firm has an intraday liquidity risk requirement of £1 billion. If it is required to hold £500 million of liquidity as an add-on against this risk as at 30 September 2015, then £500 million is the amount that would apply as the new Pillar 2 add-on as at 1 October 2015, and until the PRA can conduct the firm's next liquidity review.

2.14 **Question:** The PRA invites comments on its proposed interim Pillar 2 approach.

Reporting

2.15 Delegated Act Article 4(5) requires firms to calculate and monitor their liquidity positions against the LCR as specified in the Delegated Act. CRD Article 4(2) also requires the PRA, as the competent authority, to monitor institutions' compliance with CRD IV.

2.16 The EBA is revising the COREP LCR template to reflect the Delegated Act.⁽⁴⁾ Firms may face tight deadlines in implementing the new reporting template. In the event that reporting on the revised template is delayed until after the LCR is introduced on 1 October 2015, the PRA will retain the option to collect the returns via alternative methods for a limited period, for example using Excel spreadsheets.

2.17 CRD Article 104(1)(j) enables the PRA to impose additional or more frequent reporting on liquidity positions. The PRA proposes to make a rule requiring firms to have systems and controls in place to enable firms to submit all liquidity COREP returns daily, as required by the PRA. Firms may also be required to provide additional information necessary for the purpose of liquidity supervision.

2.18 **Question:** The PRA invites comments on options for collecting LCR returns, in the event of a delay in the implementation of the updated COREP LCR templates.

(1) *Bank of England Financial Stability Report*, June 2013, page 70; www.bankofengland.co.uk/publications/Documents/fsr/2013/fsrfull1306.pdf.

(2) Bank of England News Release, 28 August 2013; www.bankofengland.co.uk/publications/Pages/news/2013/099.aspx.

(3) EBA, 'Guidelines for common procedures and methodologies review and evaluation process (SREP)', www.eba.europa.eu/documents/10180/748829/EBA-CP-2014-14+%28CP+on+draft+SREP+Guidelines%29.pdf. Please note that these are being finalised and that the EBA expects to issue the final version at the end of 2014.

(4) The Bank is party to this working group.

3 Maintaining the current PRA regulatory returns

3.1 This chapter sets out the PRA's proposals for maintaining existing liquidity returns alongside the new reporting requirements, for a limited, transitional period. These are delivered by proposed rules changes to SUP 16.12 and to the Glossary of definitions, both contained in Appendix 2.

Proposals

3.2 In order to facilitate the supervision of liquidity in the initial period following the introduction of the LCR as a regulatory requirement, the PRA proposes to keep in place, for a limited period, the requirement to report some of the PRA's current liquidity returns. The PRA proposes to retain the requirement to submit the 'daily flows' and 'enhanced mismatch' reports (FSA047 and FSA048) for up to two years after the introduction of the full suite of COREP liquidity returns, but in any event not beyond the point at which the LCR must be phased in at 100% in accordance with the Delegated Act. These reports are central to the PRA's supervision of liquidity. They provide a daily breakdown of firms' inflows and outflows, which will not be available in the new COREP LCR templates.⁽¹⁾

3.3 The PRA further proposes to stop requiring returns FSA050, FSA052 and FSA054 in the new regime. The last reporting date for these returns would be as at 30 September 2015 for FSA050 and FSA054. For FSA052 (a weekly report), the last reporting date would be 2 October 2015. In the event that the introduction of the additional liquidity monitoring metrics (AMMs) is delayed, the PRA proposes to maintain the requirement to report returns FSA050, FSA052 and FSA054, until the first date at which the AMMs start being collected by the PRA.⁽²⁾ The PRA proposes to maintain FSA051 and FSA053 beyond 1 October 2015, but expects that this will be for not more than six months, unless the AMMs are delayed by more than this. These two reports provide valuable information on sources of wholesale funding (FSA051) and Financial Services Compensation Scheme coverage (FSA053). The PRA will need time to assess how to replace these data.

3.4 Following the application of the LCR, the PRA will no longer retain responsibility for the supervision of branches of EU credit institutions. The PRA therefore proposes to stop collecting liquidity reports in relation to these branches from

1 October 2015. UK branches of EEA firms that have their head office outside the EU (ie Iceland, Liechtenstein and Norway) should follow the transitional reporting arrangements proposed for UK branches of third country firms outlined in Chapter 7.

3.5 During the transition, the PRA proposes that firms that currently report on the basis of a Defined Liquidity Group (DLG) by modification or DLG by default should continue to do so.⁽³⁾ However firms in a UK DLG by modification will no longer be required to submit solo returns. Third country firms that have a whole-firm liquidity modification (WFLM) granted under BIPRU 12 in relation to their UK branches should continue to report on the basis of the whole firm (or at any other reporting level or frequency the whole-firm liquidity modification may require), for a transitional period as detailed in paragraphs 7.15 and 7.16. The PRA will be prepared to consider changes to the reporting basis or frequency if requested by a firm (for example, if firms are supervised as a single liquidity subgroup under Article 8 of the CRR, they may want to avoid reporting on two concurrent sets of liquidity subgroups).

3.6 In making these proposals, the PRA aims to ensure a smooth transition to the new regime in two ways:

- i. The PRA and firms will be able to use data from the PRA's current returns to facilitate the process of assuring the quality of the new data, especially with regard to the contractual maturity ladder. The PRA's experience in implementing the current regime indicates that firms need time to bring new reporting up to the required standard: a transition without an initial period of dual reporting may jeopardise the PRA's safety and soundness objective.

(1) A daily breakdown up to seven days will be available in the additional monitoring metrics, when these reports start being collected.

(2) EBA, 'Implementing Technical Standards (ITS) on additional liquidity monitoring metrics', www.eba.europa.eu/regulation-and-policy/liquidity-risk/draft-implementing-technical-standards-on-additional-liquidity-monitoring-metrics.

(3) See PRA glossary for a definition of the terms Defined Liquidity Group by modification or by default; <http://fshandbook.info/FS/html/PRA/Glossary>.

- ii. The PRA will have time to assess the differences between the information currently submitted and the data to be submitted under the new regime. This will allow it to refine the framework for Pillar 2, for example with regard to standardised stress testing. As part of this, the PRA will study further the combined and final set of COREP liquidity returns and, in light of this, will consider the case for setting up any new PRA reporting requirement beyond the COREP liquidity returns. The PRA notes that it would be unhelpful to switch off current PRA reporting requirements, only to reinstate them at a later stage.

3.7 The PRA's intention in temporarily retaining existing reporting is not to hold firms to a shadow regulatory standard. From the cutover date of 1 October 2015, firms' liquidity positions will no longer be measured against the ILG.

3.8 As explained in Chapter 5, BIPRU 12.5 will be revoked. Nonetheless, for reporting purposes, firms should continue to use the guidance currently contained in BIPRU 12.5 regarding what classifications to use when completing the returns (for example, for the classification of their Type A/Type B corporate or retail deposits).

3.9 **Questions:** The PRA invites comments on its proposals to:

- Retain the requirement to submit the 'daily flows' and 'enhanced mismatch' reports (FSA047 and FSA 048) for up to two years after the introduction of the full suite of COREP liquidity returns in 2015.
- Stop requiring returns FSA050, FSA052 and FSA054. The last reporting date for these returns would be as at 30 September 2015 for FSA050 and FSA054. For FSA052 (a weekly report), the last reporting date would be 2 October 2015. In the event that the introduction of the AMMs is delayed, the requirement to report returns FSA050, FSA052 and FSA054 would be maintained until the first date at which the AMMs start being collected by the PRA.
- Maintain FSA051 and FSA053 beyond 1 October 2015, with the expectation that this will be for not more than six months, unless the AMMs are delayed by more than this.

4 Modifications granted under the current regime

4.1 This chapter sets out the PRA's proposals in relation to the treatment of BIPRU 12 and SUP 16.12 liquidity modifications granted to firms in accordance with section 138A of FSMA.

4.2 The PRA offers three kinds of modifications under its current liquidity regime:

- i. Intragroup liquidity modification: this permits PRA-regulated firms incorporated in the United Kingdom to rely on liquidity support from elsewhere in their group. Such modifications create either a UK DLG where all the firms are established in the United Kingdom, or a non-UK DLG where the UK firm is reliant on its overseas parent. For UK DLGs, the PRA sets liquidity guidance at the level of the group (although the individual legal entities within the DLG typically continue to report at the legal entity level, albeit on a less frequent basis).
- ii. WFLM: this permits an overseas bank, in relation to its UK branch, to rely on the availability of liquidity resources from elsewhere within the firm.
- iii. Simplified ILAS waiver: for firms that operate a relatively simple business model, this allows a firm to calculate the size and content of its liquid assets buffer according to a simplified approach.

4.3 As set out in Chapter 2, the Delegated Act is due to apply from 1 October 2015, and the PRA will update its existing liquidity regime accordingly and revoke BIPRU 12. This means that after that time, firms will no longer be able to rely on these modifications and will not be expected to comply with them.

4.4 Under CRR Article 8, firms can apply for a permission which has a similar purpose to the intragroup liquidity modification: the PRA, as the competent authority, may waive (in full or in part) the application of the liquidity requirements in the CRR to a firm and to all or some of its subsidiaries and may supervise them as a single liquidity subgroup.

4.5 Following the revocation of BIPRU 12, WFLMs will cease to have effect. There is no equivalent to the WFLM in the CRR. Once the LCR applies in the EU, responsibility for regulating

the liquidity risk of UK branches of EU credit institutions will pass to the EU home state regulator.

4.6 UK branches of non-EU credit institutions are not subject to the liquidity provisions of the CRR. As such, responsibility for their liquidity supervision will remain with the PRA. When BIPRU 12 ceases to be in force, the WFLMs which UK branches of non-EU credit institutions have in place will cease to have effect.

4.7 For a period of transition, non-EU credit institutions would continue to submit their PRA regulatory returns in relation to their UK branches, in line with their previous modification: the PRA will modify SUP 16.12, and the definition of WFLM in the PRA Glossary, to reflect this. Chapter 7 sets out in full the PRA's proposals for liquidity requirements in respect of UK branches of third country firms, including transitional arrangements.

4.8 UK branches of EEA credit institutions that have their head office outside the EU (ie Iceland, Liechtenstein and Norway) will be subject to the same regime as for non-EEA States, as per paragraph 1.9.

4.9 The simplified ILAS waiver has no equivalent in the CRR or the Delegated Act. Once the PRA revokes BIPRU 12, simplified ILAS waivers will no longer have effect. All firms in scope must meet the LCR.

4.10 Firms that have been granted WFLMs, intragroup liquidity modifications and simplified ILAS modifications that expire before BIPRU 12 ceases to have effect on 30 September 2015 will need to apply for a renewal if they want to continue to rely on the modification up to that point.

4.11 Given the short period of time for which these renewals will be in place, the PRA has established a streamlined process for these three types of modification, with the aim of minimising the resource burden on both firms and the PRA, while continuing to ensure that the statutory tests in section 138(A) of FSMA are met.⁽¹⁾

(1) See www.bankofengland.co.uk/pr/Pages/authorisations/waivers/extending_modifications.aspx.

4.12 Firms that wish to renew or vary other types of PRA liquidity modifications, or that wish to apply for a liquidity modification for the first time, should contact their supervisor.

Section II:

Requirements on firms beyond
meeting the LCR

5 Requirements on firms beyond meeting the LCR

5.1 This chapter explains the PRA's proposals for requirements on firms with regard to liquidity that go beyond the obligations laid down in the Delegated Act. The chapter also explains the PRA's approach to assessing whether firms meet these requirements — its review and evaluation process.

5.2 The LCR is a Pillar 1 standard, ie it applies to all firms in the same way. As such it could fail to capture some important sources of liquidity risk for particular firms. Therefore, it is appropriate to set additional requirements on firms, such as requirements relating to their liquidity risk management: such measures are sometimes described as Pillar 2 requirements.

5.3 The introduction of CRD IV and the recent consultation on the EBA SREP guidelines have prompted the PRA to review its approach to liquidity and funding risk: this chapter provides an overview of how the PRA is updating its overall approach to regulating liquidity risk.

5.4 The proposed new rules are contained in the ILAA Part of the Rulebook (see Appendix 2.A). The PRA's expectations on how firms should comply with these rules are provided separately in the draft supervisory statement (see Appendix 1). The draft rules, the draft supervisory statement, and the EBA SREP guidelines should be read together to gain a full understanding of the updated liquidity regime and of the PRA's expectations of firms.

5.5 The chapter is structured as follows: first, it details the level of application of the ILAA rules. Second, it provides a checklist of those rules carried over or deleted from BIPRU 12. Finally, it provides a brief overview of the overall regime, as set out in the draft supervisory statement (Appendix 1) and draft rules (Appendix 2).

Level of application of the ILAA rules

5.6 The PRA proposes that the rules will apply on an individual basis, a consolidated basis, and a sub-consolidated basis where appropriate.

5.7 However, only those firms that are under an obligation to comply with CRR Part 6 on a consolidated basis must also comply with these PRA rules on a consolidated basis.⁽¹⁾ For

example, only a firm that is an EU parent institution must comply with the overall liquidity adequacy rule (OLAR) on a consolidated basis.⁽²⁾ This was not previously part of the BIPRU 12 regime.

5.8 Where firms have parent undertakings or subsidiaries not subject to the CRD, they must ensure that these implement arrangements, processes and mechanisms that are consistent and well integrated. Firms must also ensure that those parent undertakings or subsidiaries are able to produce any data and information relevant to the purpose of supervision. This is consistent with the PRA's current approach.⁽³⁾

5.9 The PRA is required under CRD IV to apply the Liquidity Supervisory Review and Evaluation Process (L-SREP)⁽⁴⁾ and any supervisory measures in accordance with the level of application of the requirements set out in the CRD IV framework. Therefore, the ILAA Part of the PRA Rulebook, including the requirement to carry out an Internal Liquidity Adequacy Assessment Process (ILAAP), applies on an individual basis. And it applies on a consolidated basis, where firms must comply with CRR Part 6 (Liquidity) on a consolidated basis. This enables the PRA to carry out L-SREPs and to apply supervisory measures at both individual and consolidated level, where appropriate.

Summary of rules carried forward and deleted⁽⁵⁾

5.10 The PRA currently sets out its requirements and expectations on firms in respect of their identification, measurement, management and monitoring of liquidity risk in BIPRU 12.2, 12.3, 12.4, 12.5 and 12.6. This section explains which rules the PRA proposes to maintain, and which rules it proposes to delete. It also explains one proposed new rule.

(1) The level of application of CRR Part 6 on a consolidated basis is set out in CRR Article 11(3) and Article 12.

(2) See the draft supervisory statement in Appendix 1 for a definition of OLAR.

(3) SYSC 12.1.13R(2)(e).

(4) See paragraphs 5.30 to 5.34 for more details on the L-SREP process.

(5) See Appendix 3 for a mapping of BIPRU 12 rules to the ILAA Part of the Rulebook.

Proposed new rule

5.11 As noted in paragraph 2.17, CRD Article 104(1)(j) enables the PRA to require additional or more frequent reporting on liquidity positions. And CRR Article 414 requires that firms submit liquidity returns daily when they do not meet, or expect not to meet, the LCR requirement (unless exempted by the relevant competent authority). As explained in paragraph 2.17, the PRA proposes a new rule to require that firms ensure that their systems and processes enable them to report all liquidity COREP returns daily, as required by the PRA.

5.12 **Question:** The PRA invites comments on its proposal for a new rule to require that firms ensure that their systems and processes enable them to report all COREP liquidity returns daily, as required by the PRA.

BIPRU 12 rules carried forward

5.13 For the ILAA rules, the PRA proposes to carry forward selected rules from BIPRU 12 which are relevant to the new regime. They include:

- the requirement that firms hold adequate liquidity;
- the requirement that firms assess whether they hold enough liquidity and document that assessment;
- the specification of some of the elements that firms need to undertake in carrying out that assessment (notably around liquidity stress testing); and
- requirements on specific aspects of liquidity risk management.

5.14 To ensure ongoing compliance with the CRD, the PRA proposes to carry forward the BIPRU 12 rules that relate to liquidity risk management and that transpose CRD Article 86.⁽¹⁾

5.15 BIPRU 12 rules which remain relevant to the new regime and which will therefore be carried forward include, substantially, those relating to:

- the overall liquidity adequacy rule;
- liquidity risk management (ie those rules that implement CRD Article 86);
- stress testing;
- ILAA; and
- asset encumbrance.

Proposals for rules to delete

5.16 The PRA is proposing to revoke the whole of BIPRU 12, as explained in Chapter 1. Firms should note that this means, in particular, that the following rules will cease to apply.

Simplified ILAS regime

5.17 The PRA proposes to delete BIPRU 12.6, as detailed in Chapter 4.

Standardised stress testing

5.18 The proposed ILAA rules contained in Appendix 2.A no longer specify the criteria of a standardised stress test of the type articulated in BIPRU 12.5.

5.19 The PRA proposes to maintain the granularity of assumptions around the risk drivers (currently in BIPRU 12.5). However this will be incorporated in the firm-specific stress test requirement.

Overview of regime

PRA's expectations of firms

Overall liquidity adequacy rule

5.20 The LCR is a Pillar 1 standard, ie it is a set of measures that applies to all firms in the same way. As such it could fail to capture some important sources of liquidity risk for particular firms. The LCR also does not measure whether firms have in place adequate systems and processes for managing liquidity risk. It follows that a firm cannot only rely on meeting the LCR in order to be confident that it is appropriately resilient to liquidity risk. Firms must ensure that their liquidity and funding risks are comprehensively captured and managed. The PRA sets this as a requirement through its overarching rule, OLAR.

5.21 The PRA views firms' responsibilities with regard to OLAR to be of paramount importance. Underlying OLAR is the PRA's expectation that firms manage their liquidity risk prudently and take responsibility themselves for doing so.

5.22 Quantitative requirements should encompass liquidity needs across all time horizons in severe but plausible stresses, for all relevant risk drivers.

5.23 Qualitative requirements cover the need for robust governance, strategies, policies, systems and processes, transfer pricing, collateral management, funding diversification, market access and funding plans, in order to identify, measure, manage and monitor liquidity risk over meaningful time horizons. All of these must be tailored to the firm. Qualitative requirements also include the requirement for firms to prepare a liquidity contingency plan, which should be informed by the results of firms' liquidity stress testing.

(1) CRD Article 86 ('Liquidity risk') requires that competent authorities ensure that firms have in place 'robust strategies, policies, processes and systems' for managing their liquidity risk, including in respect of several important specific aspects of liquidity risk management, including stress testing and liquidity recovery plans.

Internal Liquidity Adequacy Assessment Process

5.24 Firms are required to document their assessment of overall liquidity adequacy and their compliance with the ILAA rules. The document is referred to as the ILAAP document. It serves two main purposes:

- it provides the management body with all qualitative and quantitative information necessary to approve the risk appetite,⁽¹⁾ including a description of the systems, processes and methodologies for measuring and managing liquidity risk; and
- it provides a basis for the PRA's supervisory assessment of the firm's overall approach to liquidity management.

Stress testing

5.25 Firms' own stress testing remains the primary quantitative component of the overall liquidity adequacy assessment. Requirements and expectations are broadly unchanged compared to BIPRU 12, however the PRA proposes some changes with regard to risk drivers, set out below.

5.26 As explained in paragraph 5.18, there will no longer be a standardised stress test of the type articulated in BIPRU 12.5. The PRA proposes to move the rules requiring analysis of the risk drivers from BIPRU 12.5 so that they sit within the requirements for firms' own stress tests. While BIPRU 12.5 will cease to apply, the PRA views it as desirable to maintain the granularity and common language that the risk drivers have brought to the process of managing liquidity risk, and so this is captured in the draft supervisory statement.

5.27 The complete list of risk drivers contained in the draft supervisory statement combines the risk drivers listed in the EBA SREP guidelines and some additional risk drivers listed in the proposed rules. Firms should refer to the draft supervisory statement for a full list of risk drivers and analyse whether these are relevant to them. Firms should note that the PRA has enhanced the suite of risk drivers in the proposed rules to incorporate analysis of internalisation risk, where applicable to the firm.⁽²⁾

5.28 **Question:** The PRA invites, in particular, comments on the proposed risk driver on internalisation risk.

Asset encumbrance

5.29 The rule around the management of asset encumbrance was recently added to BIPRU 12 and the rule will be carried forward in substance.⁽³⁾ The requirement on firms to identify, monitor and manage the risks associated with asset encumbrance to within reasonable parameters will therefore continue to apply.

Liquidity Supervisory Review and Evaluation Process

5.30 The L-SREP builds upon the process known as the PRA's Supervisory Liquidity Review Process under BIPRU 12, and is a process consistent with the EBA SREP guidelines.

5.31 The draft supervisory statement in Appendix 1 provides information on the PRA's approach:

- to assessing whether firms have adequately covered their risks (replacing sections of BIPRU 12.9 primarily, also 12.2 and 12.5);
- to setting additional liquidity requirements (replacing BIPRU 12.5 and 12.9); and
- when firms fall below the level of quantitative individual liquidity guidance (replacing sections of BIPRU 12.9).

5.32 With regards to the last point, the information provided in the draft supervisory statement will replace the information in the PRA's legacy supervisory statement SS4/13 'Liquidity and capital regime for UK banks and building societies: adjustments in relation to FPC statement'.⁽⁴⁾ The information on liquidity in SS4/13 is specific to the BIPRU 12 regime and will cease to apply when BIPRU 12 is revoked.

5.33 As mentioned above, the proposed ILAA rules contained in Appendix 2.A no longer specify the criteria of a standardised stress test of the type articulated in BIPRU 12.5. In due course, the PRA may undertake standardised stress tests to assess risks not captured under the LCR, as a cross-check on the LCR and to support cross-firm analysis.

5.34 The standardised stress tests will be based on the LCR reporting templates and the AMMs, which may need to be augmented with further reporting. The PRA will conduct a gap analysis: additional data may be necessary.

Setting individual liquidity guidance

5.35 Following the L-SREP, the PRA will give firms liquidity guidance, advising a firm of the amount and quality of liquid assets which the PRA consider are appropriate, having regard to the liquidity risk profile of the firm. The draft supervisory

(1) The PRA expects firms to articulate for themselves the amount of risk they are willing to take across different business lines to achieve their strategic objectives. This risk appetite should be consistent with the PRA's objective, and the firm should pay appropriate attention to identifying, measuring and controlling risks, including those arising in unlikely but very severe scenarios. Please also see *The Prudential Regulation Authority's approach to banking supervision*, June 2014; www.bankofengland.co.uk/publications/Documents/prapproach/bankingappr1406.pdf.

(2) Internationalisation risk occurs where firm or customer long positions are funded using the proceeds from customer short trades. See paragraph 2.8(xiv) of the draft supervisory statement for a detailed definition.

(3) *PRA Policy Statement PS4/14*, 'Responses to CP5/14', May 2014; www.bankofengland.co.uk/pr/Documents/publications/ps/2014/ps414.pdf.

(4) *PRA Supervisory Statement SS4/13*, 'Liquidity and capital regime for UK banks and building societies: adjustments in relation to interim FPC statement', April 2013; www.bankofengland.co.uk/pr/Pages/publications/adjustmentstothepra.aspx.

statement outlines in more detail what a typical guidance would contain.

5.36 The PRA will review its proposed quantitative assessment framework, including its interim Pillar 2 approach, at a later date. This review will consider the PRA's approach to trapped liquidity between different group entities and elements set out in the Delegated Act which require the PRA to take specific actions.

Managing HQLA buffers

5.37 Firms are reminded of their obligations to integrate fully the operational requirements set out in Delegated Act Article 8 in their liquidity and funding risk management when managing their HQLA buffer.

5.38 These obligations are covered in more detail in the draft supervisory statement. These cover in particular, but not only, the ability to demonstrate that:

- The HQLA buffer is appropriately diversified to enable the firm to monetise HQLAs in a short timeframe without significant loss of value. Firms are expected to have appropriate internal limits and controls in place to achieve this.
- The currency denomination of assets is not an obstacle to using assets when meeting outflows in a specific currency in stress. To restrict currency mismatches, Delegated Act Article 8(6) gives the PRA the option to set limits on the proportion of net liquidity outflows in a currency that can be met during stress by holding HQLAs not denominated in that currency.
- When liquid assets are being held in the held-to-maturity portfolio, this does not create barriers to a firm's ability to monetise these assets. Where appropriate, the PRA may ask a firm to review its policies and procedures to ensure that it retains full ability to monetise its HQLA buffer.

5.39 **Question:** The PRA invites comments on its proposals in relation to managing the HQLA buffer.

Shari'ah-compliant firms

5.40 The Delegated Act contains a number of derogations from the eligibility of assets within a firm's liquidity buffer. These derogations are only available to firms that are unable for reasons of religious observance to hold interest-bearing assets. The PRA expects that firms that currently qualify as Shari'ah-compliant — as per the Glossary of definitions in the PRA Handbook — would be eligible to benefit from these derogations. The general and operational requirements stated in Delegated Act Articles 7(6) and 8(6) may require these firms to apply judgement in determining whether they meet these requirements. The draft supervisory statement (Appendix 1) sets out the PRA's expectations in relation to these requirements.

Pre-positioning

5.41 The PRA, in line with the wider Bank of England, encourages participating firms to pre-position sufficient eligible collateral with the Bank of England at all times, to ensure they are able to draw under the Discount Window Facility (DWF) quickly and smoothly should the need arise. Firms are advised to pre-position eligible collateral at least a day before a drawing. In particular, firms seeking to pre-position loan collateral or own-name securitisations are advised to do so well in advance, given the longer time required to pre-position more complex assets.⁽¹⁾

5.42 A firm can count assets pre-positioned at the Bank of England to meet the PRA's quantitative individual liquidity guidance, if these assets are eligible for inclusion in the HQLA buffer under the Delegated Act. If pre-positioned assets are not eligible for inclusion in the HQLA buffer, they cannot be used to meet the PRA's quantitative liquidity guidance.

(1) Bank of England, 'The Bank of England's Sterling Monetary Framework', updated November 2014 ('Red Book'), paragraphs 63 (ILTR) and 75 (DWF); www.bankofengland.co.uk/markets/Documents/money/publications/redbook.pdf.

Section III:
Elements of the new regime not
covered by EU legislation

6 Investment firms

6.1 This chapter sets out the PRA's proposed approach to the treatment of UK-designated investment firms,⁽¹⁾ given that the Delegated Act only applies to credit institutions.

6.2 The PRA currently requires that UK-designated investment firms be subject to the same liquidity regime as PRA-authorized credit institutions, on the basis that a wide variety of business models can be adversely affected by the same liquidity stress event (as demonstrated in the recent financial crisis). CRR Article 412(5) provides Member States with the discretion to apply national provisions for liquidity requirements before binding standards are fully introduced in the EU. CRR Articles 6(4) and 11(3) also provide Member States with discretion to exempt investment firms from the liquidity provisions of CRR Part 6.

6.3 CRR Article 508(2) mandates the European Commission to report on whether and how the LCR should apply to investment firms and following the submission of that report, to submit a legislative proposal (if deemed appropriate). Following the conclusion of the European Commission review, the PRA will review the appropriateness of its proposed regime for UK-designated investment firms.

6.4 The PRA assesses that there would be benefits in applying the same liquidity regime to UK-designated investment firms as for credit institutions. In particular, an identical liquidity regime provides greater transparency over the availability of liquidity resources across a mixed banking group, which in turn supports more effective supervision by the PRA over these groups for liquidity purposes. A cost benefit analysis of the PRA's proposed regime, including for UK-designated investment firms, is presented in Chapter 9. The PRA notes that, if the European Commission review results in a different regime for investment firms, this may result in UK-designated investment firms incurring costs in order to make the transition to the new regime.

6.5 The proposed rules are contained in Appendix 2.C.

Proposals

Application of the LCR to investment firms

6.6 As noted above, the Delegated Act will apply directly to credit institutions. But it will not apply to investment firms. The PRA proposes to set the same requirements for UK-designated investment firms as for UK banks and building

societies. To achieve this outcome, the PRA proposes to make a rule by which UK-designated investment firms will be subject to the obligations stated in the Delegated Act, with any necessary amendments, to bring their obligations fully into line with those applying to UK banks and building societies.

Level of application of the LCR for investment firms

6.7 The PRA proposes that PRA-designated investment firms comply with the obligations laid down in the Delegated Act on an individual and on a consolidated level in line with the general level of application of the liquidity requirements in CRR Part 6.

6.8 Where the PRA is the consolidating supervisor and the consolidation group includes investment firms which may be subject to different national liquid assets buffer requirements, for the purpose of calculating the liquidity coverage ratio on a consolidated basis, the definitions of liquid assets and the outflow and inflow rates laid down in the Delegated Act should be used.

Reporting of the LCR by investment firms

6.9 Under CRR Part 6, Title II (liquidity reporting), UK-designated investment firms are required to report the current COREP LCR return. The EBA is developing an updated version of the COREP LCR template, in order to ensure alignment between the provisions of the Delegated Act and the reporting obligations stipulated in CRR Part 6, Title II.

6.10 However, this could result in UK-designated investment firms being required to submit both the original and new versions of the COREP LCR return.⁽²⁾ The PRA is proposing in this consultation to make rules which would avoid this potential situation. If it is clarified at a later date that the new LCR template will replace the original LCR template for investment firms, these rules will not be necessary.

6.11 Specifically, the PRA proposes to exercise the discretions contained in CRR Articles 6(4) and 11(3) to exempt UK-designated investment firms from the application of

(1) See footnote 3 on page 5 for a definition of UK-designated investment firms.

(2) The dual reporting requirement arises because, first, the provisions of CRR Part 6 Title II require that UK investment firms continue to report the original LCR template; and second, because the PRA proposes that UK investment firms report against the updated version of the COREP LCR template, as this will reflect the provisions of the Delegated Act.

CRR Part 6, Title II (liquidity reporting) and Title III (reporting on stable funding), and to make a rule requiring UK-designated investment firms to submit the updated COREP LCR return as well as the additional liquidity monitoring metrics and the stable funding return. This will ensure that UK-designated investment firms are held to only one set of COREP reporting requirements (the updated version).

6.12 The PRA's proposal to exercise the discretions contained in CRR Articles 6(4) and 11(3) is based on a consideration of the conditions contained in both Articles, namely that competent authorities should take account of the 'nature, scale and complexity' of the investment firms' activities. On the basis that the designation of investment firms for regulation by the PRA involves a consideration of their nature,

scale and complexity,⁽¹⁾ the PRA judges that it would be proportionate to exempt these firms from the provisions of CRR Part 6 Titles II and III, so that the PRA can apply a requirement that these firms report the new COREP LCR returns. The PRA would update the announcement made in PRA CP05/13, in which the PRA stated its intention not to apply the discretions contained in CRR Articles 6(4) and 11(3).⁽²⁾

6.13 The PRA's proposal only applies in the context of the PRA's approach to setting a reporting requirement for UK-designated investment firms under the LCR: it does not impact on the wider CRR requirements as these apply to investment firms.

(1) *PRA Statement of Policy*, 'Designation of investment firms for prudential supervision by the Prudential Regulation Authority', March 2013; www.bankofengland.co.uk/publications/Documents/other/pra/designationofinvestmentfirms.pdf.

(2) *PRA Consultation Paper CP5/13*, 'Strengthening capital standards: implementing CRD IV', August 2013; www.bankofengland.co.uk/pra/Documents/publications/cp/2013/cp513.pdf.

7 UK branches of third country firms

7.1 This chapter outlines the PRA's proposed treatment of UK branches of third country firms that are either banks or designated investment firms ('relevant third country firms') under the PRA's new liquidity regime.

7.2 The CRR does not apply to relevant third country firms.

7.3 In September 2014, the PRA published its approach to the supervision of branches of international banks (PS8/14⁽¹⁾ and SS10/14)⁽²⁾. Under this new approach, non-EEA branches that fall outside the PRA's risk appetite will not be allowed to operate in the United Kingdom.⁽³⁾ The proposed liquidity regime for UK branches of non-EEA credit institutions is aligned with this approach.

Proposals

7.4 The CRR does not apply to relevant third country firms. As BIPRU 12 is revoked, its requirements (OLAR, for example) will no longer apply to branches. However, the PRA proposes that relevant third country firms with UK branches be subject to a requirement to provide liquidity information on a whole-firm basis.

7.5 The PRA proposes to treat UK branches of EEA banks or designated investment firms that have their head office outside the EU⁽⁴⁾ in the same way as UK branches of relevant third country firms. This will apply until the EEA Agreement has been amended by the EEA Joint Committee with a view to permitting simultaneous application of the CRR liquidity standards in the EEA States (as explained in paragraph 1.9).

7.6 The proposed rules are contained in Appendix 2.D.

Reporting for UK branches of third country firms

7.7 The proposed liquidity regime in respect of UK branches of relevant third country firms is intended to ensure that the PRA has:

- assurance that the firm has adequate liquidity, consistent with the PRA's safety and soundness objective; and
- information on a firm's liquidity which is broadly equivalent to the information it receives on UK branches of EU firms that fulfil the provisions of CRD Article 158(2).

7.8 The PRA proposes that all relevant third country firms with UK branches that come within the PRA's risk appetite be required to submit liquidity data on a whole-firm basis. These firms will be required to submit a subset of the COREP liquidity reports, specifically the updated LCR template and contractual maturity ladder return. The PRA will require firms to submit this information in eXtensible Business Reporting Language (XBRL) format, consistent with the format adopted for the submission of the wider suite of COREP returns.

7.9 The PRA proposes that firms be required to submit these returns on a monthly basis, and that firms report the specified returns in a single, consolidated currency. PRA supervisors may ask firms to provide a currency breakdown if they have concerns over the convertibility of a specific currency that a firm has material business in, or if the PRA's supervisory approach requires the firm to report against all of its material currencies.

7.10 The PRA will consider applications on a case-by-case basis, in relation to the following aspects of the reporting requirement placed on relevant third country firms operating a UK branch:

- Scope of liquidity information: firms may apply to submit their liquidity information on a consolidated group basis, rather than at the default whole-firm level, if they can demonstrate to the PRA that their home state liquidity requirements are set at a similar level.
- Frequency of liquidity reports: firms may apply to submit their liquidity information on a less frequent basis than the default monthly requirement. The PRA will take a range of factors into account when making a final decision on any individual application, including considering the firm's relative systemic importance and its liquidity risk profile.

(1) PRA Policy Statement PS8/14, 'Supervising international banks: the Prudential Regulation Authority's approach to branch supervision', September 2014; www.bankofengland.co.uk/prd/Documents/publications/ps/2014/ps814.pdf.

(2) PRA Supervisory Statement SS10/14, 'Supervising international banks: the Prudential Regulation Authority's approach to branch supervision', September 2014; www.bankofengland.co.uk/prd/Documents/publications/ss/2014/ss1014.pdf.

(3) Where the PRA would not be content with a firm operating as a branch in the United Kingdom in view of its lack of home state equivalence and/or the level of assurance over resolution, or where the PRA would not be content with a firm undertaking critical economic functions while operating as a branch in the United Kingdom.

(4) Namely, UK branches of third country firms that are either banks or designated investment firms with their head office in Iceland, Liechtenstein and Norway.

Firms wishing to apply for a specific permission to modify these requirements should submit a formal application through the PRA waiver process.

7.11 The PRA expects the incremental costs of these proposals to be low, and that they will be driven mainly by changes to firms' reporting systems. The majority of UK branches of relevant third country firms currently opt out of self-sufficiency (the default requirement under the PRA's current liquidity regime for both UK branches of EEA banks and non-EEA banks). Instead these firms hold a WFLM, which requires them to provide liquidity information on a whole-firm basis. In this respect, the proposed new regime is not significantly different to the current situation, in practice.

7.12 However, the incremental cost impact for relevant third country firms may be greater than for PRA-regulated UK incorporated firms, due to the costs associated with creating data according to the LCR. Chapter 9 of this CP contains more information on the cost benefit analysis of the proposed regime for relevant third country firms with UK branches.

7.13 The main benefit of the proposed regime is that it would facilitate greater comparability of liquidity information across firms supervised by the PRA, as the population of PRA-regulated firms would be required to submit this information through the designated COREP returns. This would allow PRA supervisory teams to conduct a more effective analysis in relation to a firm's liquidity risk profile.

7.14 **Question:** The PRA invites feedback on the potential costs involved in adjusting IT and reporting systems to meet the proposed regime.

Transition period for reporting

7.15 Relevant third country firms with branches in the United Kingdom should not be required to start reporting the COREP LCR return and contractual maturity ladders at the same time as firms which are directly subject to the CRR. Instead, the PRA proposes to give relevant third country firms a transition period during which to prepare the appropriate reporting systems. This will apply unless the implementation date for reporting for firms subject to the CRR is delayed. In

this interim period, firms that hold a WFLM will be required to continue reporting their existing PRA regulatory returns. Those firms that are currently required to meet the PRA's liquidity requirements at a branch level will continue to be subject to this self-sufficiency requirement. The PRA expects firms to re-apply for WFLMs if these expire during the transition period.

7.16 It is proposed that the transition regime will last for six months from the date at which the LCR applies. After this period, the PRA proposes that all relevant third country firms with branches in the United Kingdom be required to start reporting the updated LCR template and contractual maturity ladder return, at whole-firm level. In addition, all such firms would be required to continue reporting the regulatory returns FSA047, FSA048, FSA051 and FSA053 in line with the PRA's proposals for credit institutions and UK-designated investment firms detailed in Chapter 3.

Resolution planning

7.17 For a relevant third country firm to operate in the United Kingdom as a branch, the PRA must have received assurance over resolution, including the availability of liquidity in recovery or resolution situations: this is in line with the PRA's approach to supervising UK branches of international banks. The PRA's standard approach to liquidity supervision of UK branches of relevant third country firms is therefore to obtain whole entity liquidity information, and not to require the relevant third country firms to hold liquidity in their UK branches.

7.18 However, as the PRA implements its approach to the supervision of branches of international banks, there may be instances during the transition stage where there are material concerns over the level of assurance the PRA has gained from the home state supervisor over resolution or their liquidity regime. Even when the approach is fully implemented, assurance over resolution can change over time. In these circumstances, the PRA will consider using its powers to require relevant third country firms to hold liquidity resources in their UK branch until an appropriate level of assurance is received. The PRA expects this to be the exception rather than the norm. It will assess this on a case-by-case basis.

8 LCR disclosure

8.1 This chapter outlines the PRA's proposals with regards to disclosure requirements relating to the LCR.

8.2 The BCBS published an LCR disclosure template in January 2014.⁽¹⁾ These standards have not been implemented through CRD IV. The BCBS proposed an implementation date of 1 January 2015, although this was based on the LCR being adopted as a regulatory requirement on the same date. The LCR will only come into effect on 1 October 2015 in the EU.

8.3 An EBA working group is currently in the process of designing revised COREP templates for reporting the LCR as it is specified in the Delegated Act.⁽²⁾ There is a number of places where definitions are not yet fully standardised. It is only when firms start reporting their LCR according to the revised COREP templates that the PRA can begin to have some assurance that any LCR figures firms choose to disclose will be calculated using standardised definitions and calculation methods. Any earlier disclosure would be based on firms' own definitions and calculations. This would achieve neither transparency nor comparability. This position is consistent with the recommendations of the Enhanced Disclosure Task Force,⁽³⁾ which has cautioned about premature disclosure of new regulatory ratios where important elements of regulation remain subject to change.

8.4 Providing the disclosures set out in the BCBS template ought to enable market participants to make better assessments about the liquidity risk management of firms. It ought, too, to facilitate peer group comparison. As a result, firms' transparency will be increased. That may in turn

increase the effectiveness of market discipline and support the PRA's safety and soundness objective and financial stability.

8.5 However, disclosures enabling market participants to deduce the use of Bank of England liquidity assistance may make that assistance less effective and harm the financial system and the broader economy by undermining confidence. This is particularly the case if published information frustrates liquidity assistance being disclosed in an orderly way. These consequences could threaten the PRA's safety and soundness objective and be a cause of financial instability.

Proposals

8.6 The PRA recognises that investors expect firms to disclose some information regarding their performance against forthcoming regulatory standards, during the period of transition to these standards. The PRA will not set a disclosure requirement before the LCR is in effect as a regulatory requirement, supported by appropriate and reliable supervisory reporting, in October 2015. For year-end 2014 reporting, and until the PRA has made a decision, firms should provide a qualitative discussion of how they plan to meet the LCR.

8.7 Should firms choose to disclose information about their LCRs, the PRA expects them not to disclose information that could lead to premature disclosure of covert liquidity assistance, unless compliance with their legal obligations with regard to disclosure makes such disclosure unavoidable.

(1) BCBS, 'Liquidity Coverage Ratio disclosure standards', January 2014; www.bis.org/publ/bcbs272.pdf.

(2) The Bank is party to this working group.

(3) Enhanced Disclosure Taskforce, 'Enhancing the Risk Disclosure of Banks', 29 October 2012, pages 10 (Recommendation 4) and 31: www.financialstabilityboard.org/publications/r_121029.pdf.

Section IV: Cost benefit analysis

9 Cost benefit analysis

9.1 This chapter sets out an analysis of the costs and benefits of introducing the proposed update to the liquidity regime in the United Kingdom. This includes evaluating the policy choices proposed in regard of the national discretions permitted under the Delegated Act, and further proposals not covered under the new EU legislation. All numerical estimates are indicative as they are subject to substantial uncertainty and highly sensitive to the underlying assumptions.

9.2 A detailed exposition of the benefits of quantitative liquidity regulation is available in the EBA's December 2013 Report⁽¹⁾ and the FSA's 2007 Discussion Paper.⁽²⁾ This section is largely based on the key findings from both papers. It also draws from the PRA's 2013 Approach to Banking Supervision document ('the approach document').⁽³⁾

1 Analysis of market and regulatory failures being addressed

What are the market and regulatory failures being addressed?

9.3 Prudential regulation helps to address market failures that prevail in the banking industry. The approach document identifies the following broad categories:

- **Information asymmetries** mean that firms can underestimate the cost associated with liquidity stress and have inadequate liquidity risk management. These information asymmetries arise because liquidity risk is a complex area: assessing it requires technical expertise and access to a wide range of detailed, sensitive data. To some extent, the problem of information asymmetries arises for any corporate where ownership and control are separate. But it is particularly acute in the area of banks' liquidity management, due to the opacity of banks' balance sheets and the particular challenges of assessing liquidity risk. Even when data are available, it is very difficult to assess liquidity risk using statistical techniques, as liquidity crises are low probability, high impact events.
- **A separate collective action problem stems** from the difficulty of ascertaining the liquidity position of a firm. Investors and depositors may not be able to price a firm's liquidity risk correctly, and in a competitive environment this provides an incentive to underprice the risk: once one

firm has started underpricing, there is no incentive for other firms to price correctly.

- Information asymmetries are exacerbated by **collective action problems among depositors**: all depositors in a bank might withdraw their deposits at the same time, only because they all expect other depositors to do the same. The fear of a bank run is enough to generate a bank run.⁽⁴⁾
- Deposit guarantees and central bank facilities exist to mitigate this problem. But in turn this generates **moral hazard**, as the availability of these guarantees and facilities reduces firms' incentives to manage their liquidity risk prudently.

What are the consequences of these failures?

9.4 The above failures and externalities make banks more vulnerable to individual or market-wide liquidity stresses (eg a run on their deposits, or a closure of wholesale markets). In such situations, they are more likely to resort to asset 'fire sales' — offloading a substantial amount of assets to raise cash at short notice. This can put downward pressure on the price of the sold assets to such a degree that firms are unable to cover their outflows, raising the risk of an individual institution failing.

9.5 Increased vulnerability at one institution may have systemic implications: first, asset fire sales increase the risk of liquidity stress at other institutions as the price of all similar assets are affected, reducing the ability of other firms to raise cash from their liquid asset holdings; and second, because loss of confidence in one institution may quickly spread to others.

9.6 The cost of solving liquidity stresses may be shifted to public balance sheets, either through the extension of emergency liquidity assistance, or through injections of capital to vulnerable institutions.

(1) EBA (2013), 'Report on impact assessment for liquidity measures under Article 509(1) of the CRR', 20 December, page 24; www.eba.europa.eu/documents/10180/16145/EBA+BS+2013+415+Report+regarding+LCR+impact.pdf.

(2) FSA Discussion Paper 07/7, 'Review of the liquidity requirements for banks and building societies', December 2007, pages 16–20; www.fsa.gov.uk/pubs/discussion/dp07_07.pdf.

(3) *The Prudential Regulation Authority's approach to banking supervision*, June 2014, Box 3, page 12; www.bankofengland.co.uk/publications/Documents/praaapproach/bankingappr1406.pdf.

(4) Douglas, W and Diamond, F (2007), 'Banks and Liquidity Creation: A Simple Exposition of the Diamond-Dybvig Model', *Richmond Economic Quarterly*, Spring, Vol. 93, No. 2, pages 189–200; www.rich.frb.org/publications/research/economic_quarterly/2007/spring/pdf/diamond.pdf.

What are the benefits of the new legislation and the proposed transition?

9.7 The purpose of the new legislation is to ensure that individual firms internalise the true cost of liquidity risk, thereby reducing the likelihood of individual failure, of contagion to other firms, and of these private costs being borne by public balance sheets. The LCR will also enable a bank to survive a stress period for a few weeks: this provides authorities time to assess the situation and prepare an appropriate reaction.

9.8 The proposed transition ensures that the new requirements imposed on firms do not represent a significant weakening of banks' existing standards of liquidity risk management through the adjustment period. The gradual nature of the transition path will also allow firms more flexibility in adjusting their balance sheet structures and liquidity risk management to the new standard.

2 Scope

9.9 The scope of the proposals includes all UK banks, building societies and UK-designated investment firms. Firms in these categories will be required to maintain levels of liquidity buffers that enable them to meet their liabilities, including in periods of stress. Firms will be required to comply with the new regulatory requirements at an individual level, and at a consolidated level where appropriate.

9.10 Chapter 7 explains the PRA's proposals for both the transitional and end-state liquidity regime that will apply to third country firms in relation to their UK branches when the LCR comes into effect.

3 Estimating the costs of the discretionary elements

9.11 The CP focuses on three areas where the PRA has national discretion. This section considers the potential costs of each of these in turn.

National discretion to set Pillar 2 requirements

9.12 The PRA proposes to set required amounts of Pillar 2 buffers at a level that reflects material risks not covered by the LCR — but captured in the current BIPRU 12 regime. As explained in Chapter 2, the PRA intends to carry across the relevant add-ons at their current nominal values for each individual firm. As a result, the proposed transition for Pillar 2 will not involve any extra requirements on firms. As such, an impact analysis is not required.

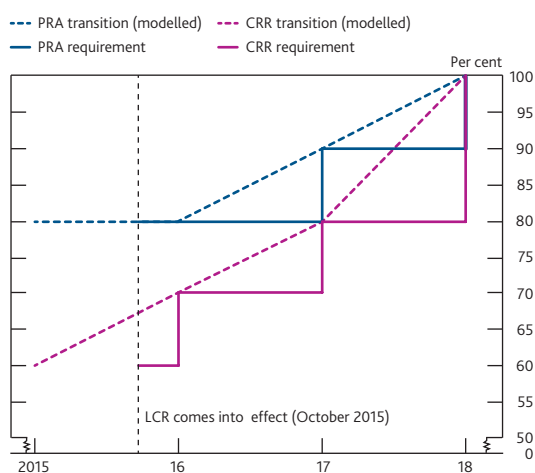
National discretion to retain existing quantitative requirements

9.13 The PRA proposes to revoke the existing liquidity standards in BIPRU 12 and withdraw firm-specific guidance contained in firms' ILGs when the LCR comes into effect (although individual add-ons will continue to apply, as detailed in paragraphs 2.11 to 2.13). However, the PRA proposes to continue with parts of the existing liquidity reporting until the transition to new reporting requirements is complete. This will act as a check for supervisors and firms to ensure that the new regime is adequately capturing all significant liquidity risks. However, there may be additional risks and costs from running dual reporting for some time.

National discretion to set the transition path up to LCR of 100% in 2018

9.14 The PRA proposes to set an initial LCR level of 80% in 2015 and 2016 and 90% in 2017. It would then reach 100% in 2018 as required in the CRR. However, CRR Article 460 allows for the transition path to start at 60% (Chart 1). Chapter 2 explains why the PRA is proposing a faster transition path.

Chart 1 PRA transition path compared to CRR transition path^(a)



Sources: Bank of England and CRR.

(a) The solid lines represent the CRR legal requirement and the proposed PRA transition path. The dashed lines represent the assumption made in this assessment regarding how banks will effect the transition in practice: namely that banks will adjust linearly to achieve the binding requirement on 1 January of each year.

9.15 This section analyses the costs and benefits of the proposal. It is structured as follows: it details the rationale behind the selection of a baseline scenario to assess the impact of the LCR and the transition period. It then describes the data used, including uncertainties about the chosen data. Next, it evaluates likely adjustment strategies at individual-bank level. Results are then aggregated to the UK industry level. Finally, this section evaluates the macroeconomic costs arising from the adjustment, and highlights potential sources of overestimation or underestimation of costs.

The policy baseline scenario

9.16 A baseline scenario is designed as the best possible projection of the macroeconomic and financial conjuncture, absent the proposed regulation or policy action. The baseline serves as a primary point of comparison for all proposed policy actions.

9.17 The following two counterfactual, hypothetical paths are used to assess the benefits and costs of the proposed transition path:

- i. a 'no change' scenario, where it is assumed that the current BIPRU 12 regime continues to apply as before and that the PRA would not apply the LCR. Although not applying the LCR is legally not an option, this provides an obvious starting point; or
- ii. a 'CRR path' scenario, where the PRA applies the lowest possible transition path allowed by the CRR.

9.18 It would be preferable to assess the costs and benefits of the proposed changes to a single counterfactual scenario. In this case, the obvious comparison would be to the CRR path. However, the CRR path starts at 60% LCR, a level much below the current average LCR of UK firms. So to use this as the starting point would imply loosening liquidity requirements for all UK firms in the early stages of the transition.

9.19 In addition, CRR Article 415(3) allows competent authorities to keep their own liquidity requirements in place until the end of the LCR transition period (1 January 2018). This means that it is appropriate for the PRA to consider the current UK regime as one valid alternative, for the period of time where the regime is stricter than the proposed CRR transition path.

9.20 The cost of the adjustment from the current regime to the minimum adjustment path allowed in the CRR (the compulsory element) is evaluated first. The incremental cost over and above the CRR minimum path of the faster adjustment path proposed in this CP (the discretionary element) is evaluated in a second step.

9.21 The existing UK liquidity regime means that most firms are already holding liquid assets well above the 60% threshold prescribed by the CRR for 2015. To reflect this, the PRA proposes a transitional path more in line with the level of liquid assets UK firms already hold. This transitional path will contribute to a swifter transition to the LCR and ensure that all firms continue to hold strong liquidity buffers to face adverse liquidity shocks, until the transition period is complete.

9.22 In addition, while there are ongoing costs to maintaining an existing liquidity buffer, these are lower than the costs of

building up such a buffer in the first place. By contrast, the benefits of holding a liquidity buffer are identical regardless of whether the buffer is new or pre-existing. So the PRA's proposed transition path — compared to the CRR path — will ensure that firms do not incur additional costs from having to rebuild liquidity buffers after a period where looser requirements applied (which would be the case if the PRA were to follow the CRR transition path).

9.23 As mentioned in paragraph 1.8, the Delegated Act only applies to credit institutions. To ensure a consistent approach to liquidity supervision between UK banks and building societies and UK-designated investment firms, the PRA proposes to make a rule which will require UK-designated investment firms to comply with the obligations laid down in the Delegated Act. This means that investment firms will be undergoing the same transition as credit institutions from BIPRU 12 to LCR. Therefore, the baseline scenarios proposed here also apply to investment firms.

Data, and dealing with the risk of sample bias

9.24 The simulation is based on data for 80 firms, including some investment firms. However, the new rules will apply to just over 200 firms. This means there is a risk that the sample is not sufficiently representative of the full population of firms. The following paragraphs explain why the assessment is based on a restricted sample, and discuss how data from alternative samples help mitigate concerns about the risk of sample bias.

9.25 The quantitative assessment undertaken for this paper uses data provided on a voluntary and best-efforts basis by 80 firms, in the context of the Basel Quantitative Impact study (QIS) undertaken in September 2013. These data are provided based on the Basel definition of the LCR, and do not reflect the EU definition agreed in the Delegated Act.⁽¹⁾ It is likely that the potential HQLA shortfall is overestimated in this analysis, owing to these differences. In order to improve the coverage of firms, an alternative would be to use the data currently reported by UK firms subject to the current regime and attempt to map this to the EU definition of the LCR. However, this mapping would be too unreliable and unsuitable for this impact assessment.

9.26 The 80-firm sample shows a high level of compliance with the proposed LCR. More than 97% of the firms in the sample already comply with the initial combined Pillar 1 and Pillar 2 requirements and just over 12% will need to increase their LCR through the transition to comply with the end-point requirement. In addition, the 80-firm sample does not show a

(1) To adjust for the particularities of some domestic banking systems, the Delegated Act allows a wider range of assets to be eligible for the LCR calculation compared to the Basel definition. It also includes some additional adjustments on the calculation of net outflows. However, the impact of these differences depends on each bank's business model. The data necessary to undertake a full comparison of the LCR based on the Basel III definition versus the Delegated Act definition are not yet available.

significant impact on those business models identified by the EBA as more vulnerable.⁽¹⁾ However, given the partial coverage of the population of firms that will be subject to the LCR there is a risk that the business models in the 80-firm sample are not sufficiently representative of the whole population.

9.27 Updates of these voluntary data are only used to assess progress over the period for the banks that report in both periods: they are not used as the basis for the actual calculations, owing to smaller sample sizes. In an update of the QIS with data as at December 2013, the majority of firms previously recorded as having an LCR below 100% in September improved their LCR in December. A further voluntary data sample from June 2014 shows that those banks with shortfalls in 2013 have continued to make progress to comply with either the transition path or the end-point requirement. However, these more recent samples are smaller and are therefore not entirely comparable with the September 2013 sample.

Evaluating the cost to firms — micro impact assessment

9.28 This section estimates the private costs to firms of adjusting their liquidity positions to the PRA's proposed LCR transition path, compared to the baseline scenarios outlined above. The PRA assessed first the costs to banks of adjusting from the counterfactual scenario (where firms are assumed to remain on the current regime) to the CRR minimum transition path (the compulsory element). The PRA subsequently assessed the incremental cost to firms transitioning to the slightly faster transition path proposed by the PRA (the discretionary element).

9.29 Most firms that provided data on a voluntary basis in the September 2013 QIS met an 80% LCR level already. As a result, the impact of a transition to 80% LCR in 2015 is small.

9.30 Improvements in LCR positions apparent in the December 2013 QIS data suggest that banks may be following a faster transition path than that proposed by the PRA. This may have been prompted by market and peer pressure to demonstrate compliance with the forthcoming LCR regulatory requirement. However, it is not possible to know with certainty whether this trend will continue. Therefore, it is assumed here that banks follow the proposed regulatory transitional path (modelled as per the dashed lines shown in **Chart 1**).

9.31 A study by the Bank of England and the Bank for International Settlements (BIS) of the transition by UK banks to the BIPRU 12 regime showed that, in response, banks adjusted both their asset and liability structures, with no overall impact on balance sheet size.⁽²⁾ This study found that UK banks increased the proportion of HQLAs and funding from more stable non-financial deposits while reducing the

proportion of short-term intra-financial sector loans and short-term wholesale funding. A related study by the EBA found that European banks followed a variety of strategies to maintain the same balance sheet size.⁽³⁾ These include:

- i. replacing non-HQLA assets with HQLAs;
- ii. adjusting liabilities only — reducing short-term unstable funding and increasing long-term funding; or
- iii. adjusting the structure of both their assets and liabilities.

The EBA study found that a combination of strategies could substantially reduce a bank's adjustment costs.

9.32 Consistent with these two studies, it is assumed that firms close their shortfall through pursuing a mixed strategy: it is assumed that firms replace some non-HQLAs with a mixed portfolio of HQLAs, and that they replace short-term intra-financial sector funding with longer-term deposits. Both elements of this strategy contribute equally to reducing firms' HQLA shortfall. This adjustment strategy might lead to a conservative estimate as banks might implement other adjustment strategies at a lower cost (as shown in the EBA LCR impact assessment), for example by reducing outflows or by increasing inflows.

9.33 Historical international data on spreads from 2004 to 2012⁽⁴⁾ are used to estimate the cost of replacing non-liquid assets with liquid assets. The higher the quality of an asset, the lower its yield tends to be: therefore, spreads between HQLAs and non-HQLAs are usually negative. In particular, in the data used here, spreads between Level 1 HQLAs and non-HQLAs range from -400 basis points to -170 basis points. The maximum observed range of spreads for the HQLA portfolio is applied in the scenario calculations. For the liability side it is assumed that firms replace interbank deposits due within one month (and therefore attracting a 100% outflow rate), with retail deposits that attract only a 5% outflow rate in the LCR calculation. Based on historical averages, it is assumed that this switch costs on average 200 basis points.⁽⁵⁾

(1) EBA, 'Report on impact assessment for liquidity measures under Article 509(1) of the CRR', 20 December 2013, page 12; www.eba.europa.eu/documents/10180/16145/EBA+BS+2013+415+Report+regarding+LCR+impact.pdf. In the EU as a whole a greater proportion of European banks from these categories appears to be affected by larger LCR shortfalls.

(2) Banerjee, R and Mio, H (2014), 'The impact of liquidity regulation on banks', *BIS Working Paper No 470*; www.bis.org/publ/work470.pdf.

(3) See footnote 1 above.

(4) From Bloomberg and other market data providers; spreads were calculated from average yields to maturity of Bank of America/Merrill Lynch bonds indices for each asset category.

(5) *Ibid*. This spread is an historical average calculated from several studies of European banks' data on the cost of terming out debt.

9.34 UK firms are currently close to compliance with an 80% LCR. If firms maintain current levels of liquidity the proposed PRA adjustment path will provide them with time to assess a range of options to either reduce outflows, increase inflows, or substitute non-HQLAs with HQLAs. By contrast, the CRR minimum path would take longer to bind, requiring firms to increase their buffers only from 2016.

9.35 The expected private cost to firms of reaching 100% LCR is the same under any transitional path, for given spreads between HQLAs and non-HQLAs, and given the same cost of adjustment the maturity of liabilities. However, the actual private cost to firms of adjusting over a longer transition period may be lower, if the transition gives firms more flexibility to choose alternative cost-effective adjustment strategies.

Evaluating the macroeconomic impact

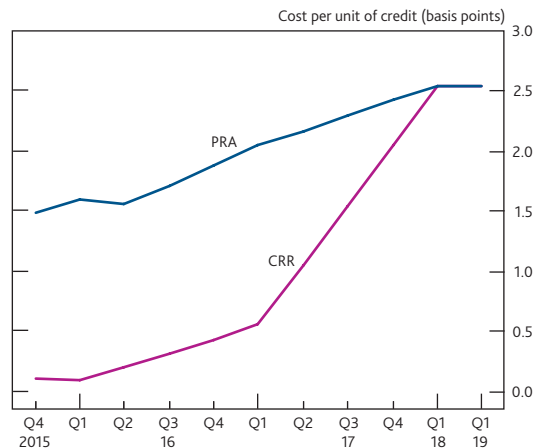
9.36 The macroeconomic impact assumes that banks pass on to their customers the incremental cost of substituting non-HQLAs with HQLAs and of replacing short-term wholesale funding with deposits. It is assumed that the average unit cost of bank credit rises in line with the cost of the adjustment strategy outlined. Bank of England banking sector data for 2013 Q4⁽¹⁾ are used to estimate the amount of deposits and the total portfolio of loans and other facilities for UK-resident and overseas customers.⁽²⁾ Based on these data, it is estimated that the proportion of loans available for repricing each quarter is 7.2% of the overall amount of loans outstanding.

9.37 The ability of banks to pass through those private costs to their customers might vary depending on the market they operate in. It is assumed that European banks are largely compliant with the 60% LCR starting requirement and dominate European markets: this limits UK firms' ability to re-price loans in these markets. It is therefore assumed that UK firms re-price loans in those markets according to the CRR minimum transition path described in **Chart 1**.

9.38 **Chart 2** shows the incremental cost of credit using a linear interpolation (as shown in **Chart 1**). The relatively small amount of loans that can be re-priced initially generates relatively higher pass through in the PRA path. **Note that the scale of the adjustment (in basis points) is very small. These estimates are in line with those of the EBA LCR impact assessment.**

9.39 The macroeconomic costs of the proposed transition path arise from the reduced provision of credit and its higher cost. For consistency with the analysis conducted to evaluate the costs and benefits of CRD IV,⁽³⁾ the PRA use the NiGEM model to evaluate these costs, per unit of credit.⁽⁴⁾ The cost estimates shown in **Chart 2** suggest that the costs are negligible or small and fall within the model's margin of error.

Chart 2 Cost pass through (per pound lent) under CRR and PRA transition paths



Sources: Bank of England and CRR.

In the PRA transition path the fall in the level of credit occurs earlier than in the CRR transition path, but by the end the total impact on the level of credit is the same in both cases. The overall level of credit falls by just under 0.18% in both transition paths compared with the hypothetical baseline of no LCR transition.

9.40 This very modest impact is in line with the results of the EBA impact assessment for the United Kingdom. By the end of the transition, the level of real GDP falls by 0.003% and 0.005% in the CRR and PRA paths respectively, driven by the higher cost of credit to households and businesses. In the long run, the higher cost of investment leads to a permanently lower level of physical capital, and a permanent reduction in the level of GDP, compared to the hypothetical baseline of no LCR transition. The initial, short-run fall in real GDP growth is counterbalanced by a fall in inflation: this reduces Bank rate, under the assumption that the inflation target remains unchanged. Therefore, in the long run, the impact on real GDP growth is negligible.

9.41 Finally, the macroeconomic benefits of the proposed transition path stem from a higher level of liquidity in the banking sector, with a positive impact on financial stability through mitigating the market and regulatory failures described at the start of the chapter. Here the probability of a crisis falls by 0.6 basis points in the long run in both

(1) Bank of England M4 and M4 lending, and monetary financial institutions consolidated balance sheet.

(2) Some studies find that the price of non-financial loans did not respond to the UK liquidity regulations imposed during the financial crisis (see Banerjee and Mio (2014)). Given the international scope of LCR, its proposed application to both credit institutions and investment firms, and the stronger growth of non-financial loans compared to when the Banerjee and Mio study was undertaken, this assessment assumes that banks will recover some of the private costs from their customers.

(3) *PRA Consultation Paper CP5/13*, 'Strengthening capital standards: implementing CRD IV', August 2013, Chapter 5; www.bankofengland.co.uk/pradocuments/publications/cp/2013/cp513.pdf.

(4) *FSA Occasional Paper Series No. 42*, 'Measuring the impact of prudential policy on the macroeconomy', May 2012; www.fsa.gov.uk/static/pubs/occpapers/op42.pdf.

scenarios.⁽¹⁾ In the case of the PRA path, the maximum incremental effect on financial stability is reached by the end of 2015, while in the case of the CRR path this maximum effect occurs later.

Potential sources of underestimation or overestimation of costs

9.42 In designing the scenarios, a number of assumptions have been made which could result in overestimating the likely cost of the proposed transition path. Other assumptions may result in underestimating these costs.

Potential sources of overestimation of the costs of the transition path

9.43 There are a number of assumptions which could make the assessment carried out above too conservative.

- As mentioned above, the data used to perform this assessment are based on the Basel definition of the LCR. It is likely that this results in overestimating firms' HQLA shortfall.
- It is assumed that banks adjust to the LCR transition path partly by replacing some non-liquid assets with lower-yielding, liquid assets eligible for the LCR. This is the most expensive adjustment strategy. That said, it was estimated in the EBA's impact assessment report that increasing HQLA holdings was the principal strategy adopted by firms adjusting to the new standard.⁽²⁾
- HQLAs generally carry lower capital risk weights than non-HQLAs. Therefore, all else equal, firms increasing their holdings of HQLAs will see their capital ratios rise, which should reduce their overall funding costs. Funding costs are also positively impacted by higher investor confidence in firms which are demonstrating higher levels of liquidity and better liquidity risk management.
- Given the small size of the shortfall and the diverse level of compliance to the LCR by European firms, there are uncertainties about how much competitive constraints bind on UK firms when repricing loans to overseas customers (ie in markets where UK firms are likely to be competing with European firms). The assumption made in paragraph 9.37 is therefore conservative.
- It is assumed that the size of banks' loan portfolios remains constant, and that new lending is generated through 'churn' (existing loans are renewed when they mature). Firms recover the cost of the transition path by repricing these new loans. However, if loan portfolios were to expand during the transition period, the costs of the transition to LCR would be spread out more widely, and therefore represent a smaller increase per unit of lending.

Potential sources of underestimation

9.44 The following assumptions may result in underestimating the cost of the transition to LCR.

- Firms might adjust more quickly than required by the PRA, particularly if there is market or peer pressure to demonstrate an ability to meet the steady-state LCR minimum requirement of 100% much sooner than 2018. A faster adjustment may be more costly: for example, if firms attempt to lengthen the term of existing sight deposits over a shorter period of time, they may be forced to seek types of funding that attract higher outflow rates (in the LCR calculation) than term retail deposits. However, the pressure from markets to adjust more quickly is not a direct response to the LCR transition path being proposed by the PRA.
- The effect of many banks in many different countries adjusting to the LCR standard will be to increase the demand for assets eligible as HQLAs. This could push up the price of such assets, reducing their yield. That could make the adjustment from higher-yielding assets to HQLAs more costly than estimated here. However, increasing the proportion of HQLAs is one of several possible adjustment strategies: banks can be expected to choose a combination of strategies which they deem to be most cost-effective. If the price of HQLAs was to increase markedly, banks would adjust strategies accordingly. In addition, the proposed transition path is spread out over three years, making it less likely to cause a sudden sharp increase in demand for HQLAs.

4 Additional compliance costs

9.45 In addition to the costs considered above, firms will need to adapt their systems to report the required data items relating to the calculation of the LCR. They will also need to devote management time to implement the changes, and ensure staff are adequately trained to manage liquidity risk reporting under the new regime. UK branches of third country firms will have to report the LCR of the firm or group they are legally part of.

9.46 To estimate the incremental compliance costs of the new regulatory reporting requirements, the PRA used information from a survey of firms asked to estimate the cost of COREP and FINREP.⁽³⁾

(1) *Ibid.* This assessment considers only the marginal benefits of liquidity above those benefits from the current United Kingdom and other elements of CRR and CRD IV eg capital regulation.
 (2) EBA (2013), 'Report on impact assessment for liquidity measures under Article 509(1) of the CRR', 20 December, page 35; www.eba.europa.eu/documents/10180/16145/EBA+BS+2013+415+Report+regarding+LCR+impact.pdf.
 (3) *FSA Consultation Paper CP09/13*, 'Strengthening liquidity standards 2: liquidity reporting', April 2009, pages 32-33; www.fsa.gov.uk/pubs/cp/cp09_13.pdf.

9.47 The PRA has extrapolated the above costs to the entire set of affected firms and across firm types and sizes (Table B). There are approximately 200 UK banks and building societies already reporting the LCR through COREP, for which the PRA has estimated that total ongoing costs will be £36 million, with a one-off cost of up to £46 million for updating the systems and filling the new regulatory returns. The nine investment firms already reporting the LCR are expected to incur an ongoing cost of £1 million and a one-off cost of £0.2 million. The PRA estimates that the 23 non-EEA groups or firms with a branch in the United Kingdom and already reporting COREP will incur ongoing costs of up to £4 million and a one-off cost of up to £9 million. And it estimates that the 42 groups or firms not reporting the LCR and with a branch in the United Kingdom will incur total ongoing costs of £8 million and one-off costs of £18 million.

Table B Costs to firms of reporting the LCR

	Total one-off costs (£ millions)	Total ongoing costs (£ millions)
Firms included in the scope of the CRR for liquidity reporting	46	36
<i>Banks</i>	40	31
<i>Building societies</i>	6	5
Additional firms required by the PRA to report the LCR	27.2	13
<i>Investment firms</i>	0.2	1
<i>Non-EEA groups or firms with a branch in the United Kingdom and where another entity reports already the LCR</i>	9	4
<i>Non-EEA groups or firms with a branch in the United Kingdom and where no other entity reports the LCR</i>	18	8
Total	73.2	49

9.48 The PRA does not expect the new regulation to significantly raise or reduce the costs of entering the UK banking sector. UK firms are already subject to liquidity regulation: new entrants already incur costs from setting up both a compliant liquidity risk management strategy and adequate reporting.

9.49 The PRA estimates that the additional compliance costs on smaller firms of the LCR reporting requirements will be proportionally lower than that of other larger firms because of the smaller scope of activities conducted by these firms.

5 Effects on competition

9.50 The PRA judges that, overall, there is no material impact on competition from the PRA's proposals.

9.51 The proposals in this CP allow for uniform treatment of all firms with regards to Pillar 1 requirements, thus meeting both PRA objectives. The proposed transition path for Pillar 2 requirements set out in Chapter 2 of this document reflects a bank-by-bank approach, and sets specific liquidity risk management requirements proportional to each firm's risk

profile. Nonetheless, the PRA will aim to ensure consistency in its application of the Pillar 2 regime.

9.52 The markets in which the population of affected firms operate cover products most closely associated with the credit intermediation process, including: deposit-taking, retail and wholesale lending, and interbank lending. However, the affected firms also operate in a number of other markets for similar or complementary products such as: venture capital/private equity, securitisation, repurchase agreements, securities lending and borrowing, over the counter derivatives and asset management. The PRA has not considered a strict definition of markets in this discussion. A more complete definition should consider products that perform very similar functions whether currently used for this purpose or not ('imperfect substitutes'), and consider those firms not currently in the market that could supply these products.

9.53 Non-banks are not captured under the scope of the regulation and are included in this empirical assessment. However banks compete successfully with non-banks in certain markets. Given the negligible private costs that the banking industry will incur when complying with the LCR in the United Kingdom, it is not expected that competition with non-banks will have any additional impact.

9.54 Non-UK firms will also need to comply with 100% LCR by 2018. However, their chosen transition paths may be different to that chosen by the United Kingdom. In the United States, firms are expected to be compliant with a 100% LCR (on the US definition) by 1 January 2017 — a faster transition path than that proposed by the PRA in this CP. Similarly, Belgium requires compliance with a 100% LCR level from 1 January 2015, and the Netherlands from October 2015. Germany on the other hand, is setting an LCR minimum of 60% in 2015. The variety of transition paths chosen by other countries, including other EU Member States, indicates that the United Kingdom is not an outlier and suggests that the effects of the PRA's transition path on competition with non-UK firms will be limited in aggregate.

9.55 The PRA is required to consider the competition impact on UK firms, compared to operating in jurisdictions which do not apply any form of liquidity regulation. However, all members of BCBS are implementing the LCR. The BCBS is currently reviewing members' progress with implementation through its Regulatory Consistency Assessment Program (RCAP).⁽¹⁾

9.56 Because the transition is binding on a subset of firms only, those firms might resort to strategies that affect their business models (for example, by reducing short-term

(1) BCBS, 'Basel III Consistency Assessment Programme (RCAP)', October 2013; www.bis.org/publ/bcbs264.pdf.

outflows and increasing short-term inflows). This could have unpredictable impacts on competition, but given the shortfalls are small any impact related to such a change is likely to be small too.

6 Impact on Shari'ah-compliant firms

9.57 Delegated Act Article 12(1)(f) allows firms which are unable to hold interest-bearing assets for reasons of religious observance to include non-interest bearing assets in their liquidity buffer, provided these assets meet certain criteria.

9.58 The PRA expects that firms that meet the current definition of Shari'ah-compliant will be eligible for this treatment. The categories of eligible assets and haircuts that apply to these firms under the Delegated Act are not significantly different from the current PRA liquidity regime for Shari'ah-compliant firms. As a result, the PRA does not expect any major cost increase or changes in the composition and liquidity of the HQLA buffer of Shari'ah-compliant firms from these changes.

Appendices

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- 1** **Draft supervisory statement — The PRA’s approach to supervising liquidity and funding risk**

 - 2** **Draft rules**
 - 2.A CRR Firms: Internal Liquidity Adequacy Assessment Instrument [Year]
 - 2.B CRR Firms: Liquidity Coverage Requirement — Transitional Provision Instrument [Year]
 - 2.C CRR Firms: Liquidity Coverage Requirement — UK-Designated Investment Firms Instrument [Year]
 - 2.D Non-CRR Firms: Liquidity Reporting Instrument [Year]
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 - 3** **Mapping of BIPRU 12 rules to the ILAA Part of the PRA Rulebook**

Draft supervisory statement — The PRA's approach to supervising liquidity and funding risk

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV⁽¹⁾ applies. The introduction of CRD IV and the recent consultation by the European Banking Authority (EBA) on new guidelines for the Supervisory Review and Evaluation Process under Directive 2013/36/EU Article 107(3)⁽²⁾ ('EBA SREP guidelines') have prompted the Prudential Regulation Authority (PRA) to review its approach to liquidity and funding risk. By clearly setting out its approach, the PRA enables firms to understand its expectations of them: this helps the PRA meet its safety and soundness objective. It also helps to ensure that the PRA's resources are used efficiently.

1.2 The European Commission delegated act to supplement EU Regulation (EU) No 575/2013 with regard to the liquidity coverage requirement for credit institutions ('Delegated Act') will apply from 1 October 2015.⁽³⁾ This legislation will be directly applicable in the United Kingdom.

1.3 This statement supplements the requirements in the Delegated Act, which specifies in detail the liquidity coverage requirement (LCR) provided for in Article 412 (1) of Regulation (EU) No 575/2013 (CRR). It provides further detail in relation to the high-level expectations outlined in the PRA's approach document.⁽⁴⁾ The supervisory statement sets out the PRA's expectations in relation to firms' management of their liquidity and funding risks. In particular, the supervisory statement explains the PRA's expectations in relation to the requirements contained in the Internal Liquidity Adequacy Assessment Part of the PRA Rulebook (ILAA rules).

1.4 The Delegated Act only applies to credit institutions. UK-designated investment firms must comply with the obligations laid down in the Delegated Act as they apply to credit institutions, by virtue of rule 2.1 of the UK-designated investment firms Part of the PRA Rulebook. They should read references in this statement to the Delegated Act accordingly.

1.5 The PRA is required under CRD IV to apply the Liquidity Supervisory Review and Evaluation Process (L-SREP) and any supervisory measures in accordance with the level of application of the requirements set out in CRD IV. Therefore, the ILAA rules, including the requirement to carry out an Internal Liquidity Adequacy Assessment Process (ILAAP), applies on an individual basis and on a consolidated basis where firms must comply with CRR Part 6 (Liquidity) on a consolidated basis. This enables the PRA to carry out an L-SREP and to apply supervisory measures at both individual and consolidated level where appropriate.

1.6 The PRA's approach is informed by the forthcoming EBA SREP guidelines. The PRA expects firms to have regard to the detail contained in Titles 8 and 9 of the EBA SREP guidelines to understand the PRA's expectations of them, in respect of liquidity and funding risk management. The rules should be read in conjunction with the supervisory statement and the EBA SREP guidelines, to gain a full understanding of the updated liquidity regime and of the PRA's expectations of firms.

1.7 This supervisory statement also sets out how the PRA will set individual liquidity guidance⁽⁵⁾ as part of the new regime and details transitional arrangements regarding Pillar 2 requirements. It also addresses the PRA's expectations of firms that fall below their quantitative individual liquidity guidance, and the treatment of collateral pre-positioned for use in the Bank of England's liquidity insurance facilities.

2 PRA expectations of firms' liquidity risk management

Overall liquidity adequacy

2.1 The PRA's approach to liquidity supervision is based on the principle that a firm must have adequate levels of liquidity resources and a prudent funding profile, and that it comprehensively manages and controls liquidity and funding risk. The firm itself is responsible for the effective management of its liquidity and funding risk. This overarching principle is set out in the overall liquidity adequacy rule (OLAR) in Chapter 2 of the ILAA rules, and supplemented by Chapter 3 of the ILAA rules on overall strategies, processes and systems.

2.2 For the purposes of OLAR, liquidity resources are not confined to the amount or value of a firm's marketable, or otherwise realisable, assets. Rather, in assessing the adequacy of those resources, a firm should have regard to the overall character of the liquidity resources available to it, which enable it to meet its liabilities as they fall due.

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- (1) CRD IV implements the international regulatory framework for banks known as Basel III in Europe. The legislation comprises two instruments: the Capital Requirements Regulation (575/2013) (CRR) and the Capital Requirements Directive (2013/36/EU)(CRD), jointly known as 'CRD IV'.
- (2) European Banking Authority, 'Guidelines for common procedures and methodologies review and evaluation process (SREP)', www.eba.europa.eu/documents/10180/748829/EBA-CP-2014-14+%28CP+on+draft+SREP+Guidelines%29.pdf. Please note that these are in the process of being finalised post-consultation. The EBA expects to issue the final version at the end of 2014.
- (3) European Commission: 'Commission Delegated Regulation (EU) [No.../.. of XXX] to supplement EU Regulation (EU) No 575/2013 with regard to liquidity coverage requirement for Credit Institutions', http://ec.europa.eu/internal_market/bank/docs/regcapital/acts/delegated/141010_delegated-act-liquidity-coverage_en.pdf.
- (4) *The Prudential Regulation Authority's approach to banking supervision*, June 2014; www.bankofengland.co.uk/publications/Documents/praaapproach/bankingappr1406.pdf.
- (5) Readers should note that when used with capital letters, or as the acronym 'ILG', the term 'Individual Liquidity Guidance' refers to the quantitative liquidity requirement set on firms under BIPRU 12. When used without capital letters, and fully spelt out, the term 'individual liquidity guidance' refers to the more general guidance given to firms, including qualitative elements.

2.3 The LCR specified by the Delegated Act is distinct from, and does not replace, the concept of overall liquidity adequacy. The LCR applies to all firms in scope: it is a set of rules that apply to all firms and therefore could fail to capture firm-specific risks. The LCR also does not capture any of the qualitative arrangements that the PRA requires a firm to implement to ensure compliance with OLAR. It follows that a firm cannot rely solely on meeting the LCR in order to satisfy OLAR.

Internal Liquidity Adequacy Assessment Process

2.4 The ILAA rules include requirements on firms to identify, measure, manage and monitor liquidity and funding risk across different time horizons, consistent with the risk appetite established by the firm's management body. A firm must carry out an ILAAP in accordance with the ILAA rules, and the ILAAP should be proportionate to the nature, scale and complexity of the firm's activities, as set out in Chapter 13 of the ILAA rules. As part of the ILAAP, the firm should undertake a regular assessment of whether its liquidity resources are sufficient to cover the major sources of risk to the firm's ability to meet its liabilities as they fall due. Central to this process is an appropriate and clearly articulated risk appetite defining the duration and type of stress that the firm aims to survive. The ILAAP should be recorded in a document (ILAAP document). This should be updated annually by the firm, or more frequently if changes in the business, strategy, nature or scale of its activities or operational environment suggest that the current level of liquidity resources or the firm's funding profile is no longer adequate.

2.5 The PRA will take into account the criteria referred to in the forthcoming EBA SREP guidelines when reviewing a firm's ILAAP document and assessing a firm's compliance with OLAR. In particular, the PRA expects a firm to demonstrate in its ILAAP document that it complies with the requirements outlined in paragraphs 2.6 to 2.13 below.

Stress testing

2.6 Comprehensive, robust stress testing is a vital component of ensuring compliance with OLAR rule. The PRA expects firms to consider in their stress testing the impact of a range of severe but plausible stress scenarios on their cash flows, liquidity resources, profitability, solvency, asset encumbrance and survival horizon. Stress scenarios should be selected to reveal the vulnerabilities of the firm's funding, including for example, a vulnerability to previously liquid markets becoming unexpectedly illiquid. External stress testing scenarios should include a macroeconomic stress. The PRA expects the degree of conservatism of the scenarios and assumptions to be discussed in the ILAAP document.

2.7 In analysing the key risk drivers set out in Chapter 11 of the ILAA rules, the PRA expects firms to make appropriate assumptions, both quantitative and qualitative. In particular,

firms should include, where appropriate, the following assumptions, which are discussed in detail in the EBA SREP guidelines.

i. The run-off of retail funding

This includes an assessment of the response of different components of the retail book that share common features, eg guarantee cover, maturity, interest rate sensitivity, customer type, product type, deposit size, or the channel through which they were acquired.

ii. The reduction of secured and unsecured wholesale funding

This includes an assessment of the type and geographical location of the counterparty, the level of creditor seniority, the nature of the relationship the firm has with the counterparty, the type of underlying collateral (if applicable), and the speed of outflow. The risk of shortening tenors should also be assessed.

iii. The correlation, concentration and inadequate diversification between funding types

Firms should include an assessment that takes into account instrument type, markets, currency, liability term structure, counterparty and market access, as appropriate. Where diversification is sought, its effectiveness should be considered.

iv. Additional contingent off-balance sheet exposures

Firms should include, where appropriate, an assessment of derivative cash flows caused by maturity, exercise, repricing, margin calls, a change in the value of posted collateral, substitution and sleeper collateral, volatile market conditions or buy-out requests. Firms should also consider funding commitments (eg facilities, undrawn loans and mortgages, overdrafts and credit cards), guarantees and trade finance contracts, as well as facilities to support securitisation vehicles, including sponsored and third-party structures.

v. Funding tenors

Firms should consider vulnerabilities within the term structure due to external, internal or contractual events (eg where the funding provider has call options).

vi. The impact of a deterioration in the firm's credit rating

Firms should consider all types of contractual and behavioural outflows resulting from credit downgrades of varying magnitude, the types of collateral which may be required and the speed of outflow, to the extent appropriate.

vii. Foreign exchange (FX) convertibility and access to FX markets

Firms should calculate stressed outflows by individual currency and tenor where appropriate. This information must support an assessment of how the shortfalls can be funded in a stressed market with impaired access to FX markets and loss of convertibility.

viii. The ability to transfer liquidity across entities, sectors and countries

Firms should assess the implicit intragroup support required in stress, or a failure of a group entity to repay loans in a timely manner, where appropriate. This assessment should include considering existing legal, regulatory and operational limitations to potential transfers of liquidity and unencumbered assets among entities, business lines, countries and currencies.

ix. Estimates of future balance sheet growth

This should include considering how planned or forecast balance sheets may behave in stress and whether the firm's risk appetite⁽¹⁾ would be breached.

x. The impact on a firm's reputation or franchise

Firms should include an assessment of implicit liquidity requirements arising from a need to roll over assets, to extend or maintain other forms of liquidity support, or to permit premature termination of retail term or notice liabilities for reputational reasons or to protect the franchise, as appropriate. Firms should also bear in mind that responses to a liquidity stress cannot include actions that would significantly damage their franchise.

2.8 In addition, the PRA also expects firms to consider, where appropriate, the quantitative and qualitative assumptions for the following risk drivers, which are not explicitly addressed in the EBA SREP guidelines.

i. Intraday risk

Firms should assess intraday liquidity risk, that is, the risk of timing mismatches arising from direct and indirect membership in relevant payment or settlement systems. Firms should ensure that they have sufficient liquidity at all times to maintain normal payment activity if: incoming payments are delayed by several hours or until close to the end of the day; credit lines are withdrawn and require full collateralisation; or large individual customers default on their payments. The PRA assesses that intraday liquidity risk exposures are material for many firms and firms are expected to demonstrate robust analysis as outlined above.

ii. Marketable asset risk

Firms should include a consideration of how factors affecting their ability to liquidate assets or monetise those

through repurchase agreements may change in stress, where appropriate. This should include market access, haircuts, timelines, pricing, operational capacity or eligibility.

iii. Non-marketable asset risk

The PRA defines non-marketable assets as being those assets which cannot be monetised via repo or outright sale. They could be monetised, for example, via the securitisation market or as covered bonds. Firms should include an assessment of how factors affecting the liquidity of those assets (eg counterparty stress, whether market access is frequent and established, early amortisation triggers, or financing of warehoused assets) may change under stress.

iv. Internalisation risk

Internalisation risk occurs where firm or customer long positions are funded using the proceeds from customer short trades. When clients close out their short positions and these arrangements unwind, this may generate substantial liquidity outflows for a firm. Internalisation and netting efficiencies within synthetic prime brokerage also give rise to liquidity risk which should be measured and assessed as part of a firm's stress testing, where appropriate.

2.9 Consistent with Chapter 11 of the ILAA rules, the PRA expects the results of the stress testing exercise to be presented to the firm's management body on a regular basis.

Assessment of stress factors which are not specified in the Delegated Act

2.10 Firms are reminded of their obligation to comply with the specific requirements of Delegated Act Article 23 when completing their ILAAP. Article 23 requires firms to undertake their own regular assessment of the likelihood and potential volume of liquidity outflows during thirty calendar days, for all products or services which meet the following two conditions:

- the products or services are not referred to in Articles 27 to 31; and
- firms either offer or sponsor these products or services, or purchasers would consider these to be associated with the firm.

(1) The PRA expects firms to articulate for themselves the amount of risk they are willing to take across different business lines to achieve their strategic objectives. This **risk appetite** should be consistent with the PRA's objective, and the firm should pay appropriate attention to identifying, measuring and controlling risks, including those arising in unlikely but very severe scenarios. Please also see *The Prudential Regulation Authority's approach to banking supervision*, June 2014; www.bankofengland.co.uk/publications/Documents/prapproach/bankingappr1406.pdf.

Firms should refer to Article 23 of the Delegated Act for further details, including a non-exhaustive list of such products. The PRA will assess firms' individual assessments of such stress factors at least annually, reach a conclusion regarding appropriate methodologies, and report these conclusions to the EBA.

ILAAP governance

2.11 The PRA expects the ILAAP to be the responsibility of a firm's management body.⁽¹⁾ The ILAAP document must be approved by the management body and must meet the risk appetite approved by the management body and the firm's approach for measuring and managing liquidity and funding risk. The management body is also expected to ensure that the ILAAP is well integrated into management processes and the firm's decision-making culture.

Liquidity contingency plan

2.12 Chapter 12 of the ILAA rules sets out the requirements a firm needs to meet in relation to its liquidity contingency plan. In addition, the PRA already requires firms to prepare a recovery plan.⁽²⁾ To the extent that the broader recovery plan addresses the requirements for liquidity contingency plans, firms do not have to submit a separate liquidity contingency plan. However, regardless of whether this is addressed in the liquidity contingency plan, or in the broader recovery plan, firms' arrangements should reflect the specific requirements of good liquidity management, and must be cross-referenced, where appropriate, in the ILAAP document. In particular, these arrangements should be informed by the results of firms' liquidity stress testing. The PRA expects to review these arrangements as part of its review of firms' liquidity management.

Transfer pricing system

2.13 As part of its compliance with Chapter 6 of the ILAA rules, the PRA expects a firm to ensure that the costs, benefits and risks relating to liquidity are fully incorporated into firms' product pricing, performance measurement and incentives, and new product and transaction approval processes. All significant business lines should be included, whether on or off-balance sheet. Both stressed and business as usual costs should be assessed. The process should be transparent and understood by business line management, and regularly reviewed to ensure it remains appropriately calibrated.

3 The Liquidity Supervisory Review and Evaluation Process (L-SREP)

3.1 Building on previous liquidity reviews and ongoing supervisory activities, the PRA will carry out an L-SREP. This process will be consistent with the EBA SREP Guidelines. The outcome of the L-SREP informs the setting of a firm's individual liquidity guidance (see Section 4 below). In carrying

out the L-SREP, the PRA will undertake the following in a manner which is proportionate to the nature, scale and complexity of a firm's activities:

- review the arrangements, strategies, and processes implemented by a firm to comply with the liquidity standards laid down in the ILAA rules, CRR Part 6 (Liquidity) and the Delegated Act. This includes reviewing firms' COREP liquidity returns;
- evaluate the liquidity risk and funding risks to which the firm is or might be exposed;
- assess the risks that the firm poses to the financial system; and
- evaluate the further liquidity and funding risks revealed by stress testing.

Based on this assessment, the PRA will:

- quantify specific individual liquidity guidance;
- determine specific qualitative individual liquidity guidance; and
- determine firms' overall liquidity risk scoring.

The first two bullet points are addressed in Section 4 on setting individual liquidity guidance.

3.2 The quantitative assessment will review whether the firm has correctly identified its liquidity needs across appropriate time horizons in severe but plausible stresses in its ILAAP document, for all relevant risk drivers.

3.3 The qualitative assessment will review the governance arrangements of the firm, its risk management culture, and the ability of members of the management body to perform their duties. The degree of involvement of the management body will be taken into account, as will the appropriateness of the internal processes and systems underlying the ILAAP. The qualitative review also covers the firm's risk appetite, liquidity contingency plans and non-stressed funding plans, collateral management, the ability to monetise High Quality Liquid Assets (HQLAs) and wider liquidity in a timely fashion, intraday arrangements, market access and asset encumbrance.

3.4 The PRA may need to request further information and meet with the management body and other representatives of a firm, to evaluate fully the comprehensiveness of the ILAAP

(1) As defined in the PRA Handbook; <http://fshandbook.info/FS/html/PRA/Glossary>.
 (2) PRA Consultation Paper CP13/14, 'Implementing the Bank Recovery and Resolution Directive', July 2014, Annex C; www.bankofengland.co.uk/pradocuments/publications/cp/2014/cp1314.pdf.

and the adequacy of the governance arrangements around it. The management body should be able to demonstrate an understanding of the ILAAP consistent with its taking responsibility for it. And the management of the firm at appropriate levels should be prepared to discuss and defend all aspects of the ILAAP, covering both quantitative and qualitative components. Additionally, the PRA will consider the business model of the firm and the advocated rationale for the model, as well as the firm's expectations regarding the future market and economic environment and how they might affect its liquidity position and funding profile.

3.5 The PRA will review if a firm accurately and consistently complies with the obligations of the Delegated Act, including whether a firm is appropriately applying the outflow rates cited in the Delegated Act.

3.6 The PRA will assess what requirements, beyond that of meeting the LCR, should be requested of firms as part of the L-SREP. It may provide further clarification on its quantitative assessment framework, including for Pillar 2, once the EBA SREP guidelines have been finalised and the PRA has had an opportunity to assess them. The EBA SREP guidelines also ask competent authorities to design generic scenarios and assumptions and incorporate these into a stress model. This stress model will be driven off the data supplied in the Common Reporting (COREP) LCR reporting templates and additional liquidity monitoring metrics (AMMs), but additional data may be necessary.

3.7 On the basis of the L-SREP, the PRA will determine whether the arrangements, strategies, processes and mechanisms implemented by a firm and the liquidity it holds provide sound management and adequate coverage of its risks.

4 Setting individual liquidity guidance

4.1 Following the L-SREP, the PRA will give individual liquidity guidance, advising a firm of the amount and quality of HQLAs which the PRA considers are appropriate, having regard to the liquidity risk profile of the firm. In giving individual liquidity guidance, the PRA will also advise the firm of what it considers to be a prudent funding profile for the firm. Compliance with individual liquidity guidance does not necessarily imply compliance with OLAR.

4.2 The type of liquid assets that a firm will be allowed to hold to satisfy the PRA's individual liquidity guidance will be no wider than defined in the Delegated Act. Quantitative guidance will extend beyond the liquidity buffer the firm is required to maintain under the LCR and will cover liquidity risks to which the firm is exposed to but which are not captured by the LCR (Pillar 2 quantitative requirements). Qualitative guidance will include actions required to mitigate

those risks identified as inconsistent with the PRA's objectives. Where appropriate, the PRA may also set specific guidance on pre-positioning collateral at the Bank of England.

4.3 Typically, individual liquidity guidance given to firms will cover the following areas:

- whether the quantity of HQLAs held is sufficient;
- whether the quality of HQLAs held is appropriate;
- whether the firm's funding profile is appropriate; and
- any further qualitative arrangements the firm should undertake to mitigate its liquidity risk.

4.4 The PRA is adopting an interim Pillar 2 approach based on firms' existing Individual Liquidity Guidance (ILG) add-ons. Where current ILG add-ons relate to risks not captured by the LCR, the PRA will continue to apply them at the same absolute amounts as previously, and until the firm's next L-SREP can be undertaken. Where a firm needs more clarity on its interim Pillar 2 add-ons, it should contact its PRA supervisor in a timely manner.

4.5 The PRA proposes that, in due course, Pillar 2 add-ons be set separately at both the individual and consolidated levels, consistent with the level of application of the LCR. Initially however, the interim ILG add-ons carried over will apply at both the individual and consolidated levels. This approach will apply until the firm's next L-SREP can be undertaken.

4.6 The type of HQLAs held to meet interim ILG add-ons should be no wider than defined in the Delegated Act and follow the same composition by asset level as set out in the Delegated Act. Nonetheless, the quality of HQLAs should be appropriate to mitigate firm-specific risks⁽¹⁾ and be consistent with OLAR.

4.7 Delegated Act Article 23 requires competent authorities to determine outflow rates for those products or services which are not addressed by the Delegated Act and for which the likelihood and potential volume of liquidity flows are material. The PRA will adopt an interim approach to define material liquidity flows for LCR reporting and determine appropriate outflow rates for these products or services.

4.8 The PRA will review its proposed quantitative assessment framework, including its interim Pillar 2 approach, at a later date. This review will consider the PRA's approach to trapped liquidity between and within different group entities and elements set out in the Delegated Act which require the PRA to take specific actions.

(1) For example, where the PRA advises a firm of an amount of HQLAs which the PRA considers appropriate to mitigate intraday liquidity risk, the PRA expects the firm to be able to liquidate these HQLAs on an intraday basis, as required.

5 Managing the HQLA buffer

5.1 Firms are expected to integrate fully the operational requirements set out in Delegated Act Article 8 in their liquidity and funding risk management when managing their buffer of HQLAs. An important aim of these requirements is to maintain a firm's ability to convert HQLAs into cash within a short timeframe.

5.2 As part of giving individual liquidity guidance, the PRA will set out its expectations of a firm's compliance with these operational requirements and the PRA may also ask a firm to take specific actions, where appropriate. The PRA's approach to evaluating how a firm manages its liquidity buffer will be adapted to each firm's size, complexity, business model and risk management practices.

5.3 The PRA expects firms to consider the cumulative stressed low point of their cash flows both within the 30-day horizon and within the context of survival days along the potentially longer horizon of their own risk appetite. Daily granularity is necessary for this analysis.

5.4 The PRA expects firms to focus particularly, but not solely, on the following principles in paragraphs 5.5 to 5.13.

Ability to monetise

5.5 Firms are reminded of their obligation to have in place appropriate internal investment policies and procedures to control and monitor the composition of their HQLA buffer. This also includes having appropriate internal limits and controls to ensure that their ability to monetise HQLAs in stress is not limited in any way.

5.6 In particular, while accounting classifications remain decisions for firms, where firms hold HQLAs in the held-to-maturity portfolio, they should be able to demonstrate that this does not create barriers to their ability to monetise these assets.

5.7 The PRA may ask a firm to review its policies and procedures to ensure that it retains full ability to monetise its HQLA buffer (note this will not cover those assets exempt by Delegated Act Article 8(4) from the requirement to be monetised periodically). In so doing, the PRA will take a proportionate approach to assessing the evidence, based on the firm's business model.

Diversification of assets

5.8 Firms are reminded of their obligation to have in place appropriate internal limits and controls to ensure that they appropriately diversify their HQLA buffer. This should be sufficient to demonstrate that their ability to monetise HQLAs in a short time frame without significant loss of value is not compromised by exposure to a common risk factor. In

addition, the PRA expects larger firms to take into account the absolute size of their HQLA holdings and to be able to monetise these without compromising on either speed of disposal or price and the impact of their actions on the wider market and on financial stability.

5.9 Firms should have due regard to their own business model when determining the appropriate level of diversification in their buffer. In particular, they should consider whether a particular asset holding exposes them to wrong-way risk.⁽¹⁾ Conversely, they should also consider whether their choice of assets is appropriate given their ability to manage properly the risk in that asset, and to access the relevant repo or sale market.

5.10 In accordance with Delegated Act Article 8(1), the PRA may set requirements on a firm to enforce increased diversification of the HQLA buffer, or conversely to restrict holdings of particular asset classes. This may include requirements on a firm's liquidity management practices or investment policies. Under CRD Article 103, the PRA may also restrict holdings of particular asset classes if it observes that this exposes several firms to a common set of risk factors.

Consistent currency denomination

5.11 Currency conversion is an additional step between monetising HQLA and using HQLA to meet specific outflows. Therefore, the PRA will also review whether the currency denomination of assets is an obstacle to firms using their assets when meeting outflows in a specific currency in stress.

5.12 The PRA reminds firms that Delegated Act Article 8(6) gives the PRA, as the competent authority, the option to restrict currency mismatches by setting limits on the proportion of net liquidity outflows in a currency that can be met by holding HQLA not denominated in that currency. The PRA may apply this discretion through a range of firm-specific measures, including setting LCRs by currency on significant currencies (therefore including the reporting currency).

Transferability of funds

5.13 In assessing the stress tests carried out by firms under Chapter 11 of the ILAA rules, the PRA will review whether a firm places appropriate emphasis on the risk that, in severely stressed circumstances, liquidity might not be freely transferred between and within group entities, across national borders, as well as between currencies. Consistent with Chapter 8 of the ILAA rules, the PRA will expect firms to demonstrate that there are no legal or practical impediments to the actual flow of liquidity across the firm and, as appropriate, across the group.

(1) Wrong-way risk is the risk that occurs when exposure to a counterparty is adversely correlated with the credit quality of that counterparty.

Eligibility of non-interest bearing assets, including sukuk⁽¹⁾

5.14 Delegated Act Article 12(1)(f) allows firms to include non-interest bearing assets in their liquidity buffer, provided these assets meet certain criteria, and if these firms are unable for reasons of religious observance to hold interest-bearing assets, in accordance with their statutes of incorporation. The PRA expects that this provision will apply to firms whose entire operations are structured and conducted in accordance with Islamic commercial jurisprudence and its investment principles. However, firms should satisfy themselves that their assets are eligible for inclusion in their HQLA buffers.

5.15 These firms may also benefit from the derogation available under Delegated Act Article 12 which allows competent authorities not to apply two specific criteria that determine the eligibility of corporate debt securities for inclusion in a firm's Level 2B HQLA buffer: these two criteria are the minimum issue size and maximum time to maturity. The PRA expects that a number of sukuk will meet the conditions that allow the PRA to exercise this discretion. Firms that consider they would be eligible to benefit from these derogations should apply to the PRA for a permission.

5.16 Delegated Act Article 7 requires firms to assess whether a trading venue provides for an active and sizable market, in order to confirm that assets that are not listed on recognised exchanges are tradable via outright sale. In particular, firms are required to take into account the minimum criteria specified in Delegated Act Article 7(6)(a) and (b) when making this assessment. The PRA acknowledges that firms will need to exercise judgement in deciding whether these criteria are met in relation to specific assets, including sukuk. It is the responsibility of firms to satisfy themselves that their assets are eligible for inclusion in their HQLA buffers. Firms should contact their PRA supervisor if, after completing their assessment, they are still unsure whether their assets meet the requirement stated in the Delegated Act.

5.17 When considering the option of restricting currency mismatches under Delegated Act Article 8, the PRA will take into account all relevant considerations: this will include considerations relevant to firms that, for reasons of religious observance, are unable to hold interest-bearing assets.

6 PRA's expectations of firms that fall below the level of quantitative individual liquidity guidance

6.1 A firm may use its HQLA buffer to cover its net liquidity outflows during stress periods, as set out in Delegated Act Article 4, thereby falling below the applicable LCR. For the avoidance of doubt, this means that the firm will have already fallen below the level of assets required to meet any

additional quantitative liquidity guidance that the PRA has given the firm. Liquidity buffers can and should be used in times of stress: a firm can fall below the level of HQLAs it is required to hold under the LCR and still meet the Threshold Conditions as defined in the PRA's approach document.⁽²⁾ The introduction of the LCR will not lead to a change in that approach.

6.2 If a firm's liquidity buffer falls, or is expected to fall, below the level advised in the individual liquidity guidance, or if a firm's funding profile ceases or is expected to cease to conform to that advised in the individual liquidity guidance, a firm is expected to notify the PRA immediately. It should then agree a plan with the PRA setting out the timely restoration of compliance with the advised guidance. The plan should include actions documented in the firm's liquidity contingency plan. Firms are reminded of their obligations in CRR Article 414 to notify the PRA immediately where it does not, or expects not to, meet the applicable LCR.

6.3 Upon receipt of the firm's plan, the PRA will judge how rapidly it expects the firm to rebuild its liquidity buffer. In exercising its judgement, the PRA will take into account both current and forecast macroeconomic and financial conditions. The PRA's response will also be proportionate to the drivers, magnitude, duration and frequency of the firm's shortfall. It will take into account the amount of pre-positioned collateral at the Bank of England, or the amount available for drawing at other central banks to which the firm has access.

7 Role of collateral pre-positioned for use in the Bank of England's liquidity insurance facilities

7.1 The Bank of England announced a number of changes to its liquidity insurance facilities in October 2013.⁽³⁾ These changes are designed to increase the availability and flexibility of liquidity insurance, by providing liquidity at longer maturities, against a wider range of collateral, at a lower cost and with greater predictability of access. The certainty with which a firm can expect to be able to access the Bank of England's facilities has been reinforced through a presumption that all firms that meet Threshold Conditions may sign up for the Sterling Monetary Framework and have full access to use the Bank of England's facilities.

(1) Certificates of equal value representing an undivided interest in the ownership of specified assets or investments acquired or to be acquired and that comply with Islamic commercial jurisprudence and its investment principles, but excluding shares.
 (2) Firms have to be able to meet their liabilities on an ongoing basis with sufficient confidence, including in stressed circumstances, consistent with their safety and soundness, Bank of England, *The Prudential Regulation Authority's approach to banking supervision*, June 2014; www.bankofengland.co.uk/publications/Documents/prapproach/bankingappr1406.pdf.
 (3) Bank of England (2013), 'Liquidity Insurance at the Bank of England: developments in the Sterling Monetary Framework', October; www.bankofengland.co.uk/markets/Documents/money/publications/liquidityinsurance.pdf.

7.2 The terms of the Bank of England's liquidity insurance facilities are set to ensure counterparties have the incentive to manage their liquidity primarily through private markets in normal times. Consistent with this, for limited liquidity shocks, it is appropriate for firms to draw initially on their holdings of HQLAs. For larger or more severe liquidity outflows, the Bank of England expects firms to consider using the Discount Window Facility or other liquidity insurance facilities alongside, rather than after, using a significant proportion of their liquidity buffer. As noted in the PRA's approach document, the PRA expects firms to have credible options in their recovery plans for restoring their HQLAs following firm-specific or market-wide stress.

7.3 A firm can count assets pre-positioned at the Bank of England to meet the PRA's quantitative liquidity guidance, if these assets are eligible for inclusion in the HQLA buffer under the Delegated Act. If pre-positioned assets are not eligible for inclusion in the HQLA buffer, they cannot be used to meet the PRA's quantitative liquidity guidance.

7.4 The PRA continues to expect firms to have robust levels of pre-positioning. However, the PRA also acknowledges the need for flexibility for firms to be able to use these assets to access market funding. The PRA may set explicit requirements of firms for pre-positioning where appropriate, and may provide additional guidance to firms in stress.

7.5 Assets pre-positioned at the Bank of England may be of varying quality, and some of these assets may have been monetised. The Bank of England previously stated that it will let firms know what proportion of their Level A, B and C assets have been encumbered,⁽¹⁾ but it will not specify which quality of asset has been monetised first. For reporting purposes, firms with pre-positioned assets that have been partially monetised can assume that assets are encumbered in order of increasing liquidity.

(1) Bank of England (2010), 'Extending eligible collateral in the Discount Window Facility and information transparency for asset-backed securitisations', March, page 5; www.bankofengland.co.uk/markets/Documents/money/publications/condocmar10.pdf.

**PRA RULEBOOK: CRR FIRMS: INTERNAL LIQUIDITY ADEQUACY ASSESSMENT
INSTRUMENT [YEAR]**

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (1) section 137G (the PRA’s general rules); and
 - (2) section 137T (general supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook: CRR Firms: Internal Liquidity Adequacy Assessment Instrument [YEAR]

- D. The PRA makes the rules in the Annex to this instrument.

Commencement

- E. This instrument comes into force on [Date].

Citation

- F. This instrument may be cited as the PRA Rulebook: CRR Firms: Internal Liquidity Adequacy Assessment Instrument [YEAR].

By order of the Board of the Prudential Regulation Authority

[DATE]

Annex

In this Annex, the text is all new and is not underlined.

Part

INTERNAL LIQUIDITY ADEQUACY ASSESSMENT

Chapter content

- 1. APPLICATION AND DEFINITIONS**
- 2. OVERALL LIQUIDITY ADEQUACY RULE**
- 3. OVERALL STRATEGIES, PROCESSES AND SYSTEMS**
- 4. LIQUIDITY RISK APPETITE AND FUNDING RISK APPETITE**
- 5. INTRA-DAY MANAGEMENT OF LIQUIDITY**
- 6. TRANSFER PRICING SYSTEM**
- 7. MANAGEMENT OF COLLATERAL**
- 8. MANAGING LIQUIDITY ACROSS LEGAL ENTITIES, BUSINESS LINES, COUNTRIES AND CURRENCIES**
- 9. FUNDING DIVERSIFICATION AND MARKET ACCESS**
- 10. MANAGEMENT OF ASSET ENCUMBRANCE**
- 11. STRESS TESTING**
- 12. LIQUIDITY CONTINGENCY PLAN**
- 13. INTERNAL LIQUIDITY ADEQUACY ASSESSMENT PROCESS**
- 14. APPLICATION OF THIS PART ON AN INDIVIDUAL BASIS AND A CONSOLIDATED BASIS**
- 15. TRANSITIONAL PROVISION**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to a *CRR firm*.

1.2 In this Part, the following definitions shall apply:

consolidation group

means the undertakings included in the scope of consolidation pursuant to Articles 18(1), 19(1), 19(3) and 23 of the *CRR*.

EEA parent institution

means a *parent institution in an EEA State* which is not a *subsidiary* of another *institution* authorised in an *EEA State* or of a *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

EEA parent financial holding company

means a *parent financial holding company in an EEA State* which is not a *subsidiary* of an *institution* authorised in any *EEA State* or of another *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

EEA parent mixed financial holding company

means a *parent mixed financial holding company in an EEA State* which is not a *subsidiary* of an *institution* authorised in any *EEA State* or of another *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

funding risk

means the risk that a *firm* does not have stable sources of funding in the medium and long term to enable it to meet its financial obligations, such as payments or collateral calls, as they fall due, either at all or only at excessive cost.

Internal Liquidity Adequacy Assessment Process (ILAAP)

means the process for the identification, measurement, management and monitoring of liquidity implemented by the *firm* in accordance with 3 - 13.

liquidity contingency plan

a plan for dealing with liquidity crises as required by 12.1.

liquidity risk

means the risk that a *firm*, although solvent, does not have available sufficient financial resources to enable it to meet its obligations as they fall due.

overall liquidity adequacy rule

means the rule in 2.1.

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 OVERALL LIQUIDITY ADEQUACY RULE

- 2.1 A *firm* must at all times maintain liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due.
- 2.2 For the purposes of the *overall liquidity adequacy rule*:
- (1) a *firm* also must ensure that:
 - (a) its liquidity resources contain an adequate buffer of high quality, unencumbered assets; and
 - (b) it maintains a prudent funding profile;
 - (2) a *firm* may not include liquidity resources that may be made available through emergency liquidity assistance from a central bank.

3 OVERALL STRATEGIES, PROCESSES AND SYSTEMS

- 3.1 As part of the *overall liquidity adequacy rule*, a *firm* must have in place robust strategies, policies, processes and systems that enable it to identify, measure, manage and monitor *liquidity risk* and *funding risk* over an appropriate set of time horizons, including intra-day, so as to ensure that it maintains adequate levels of liquidity buffers and an appropriate funding profile. These strategies, policies, processes and systems must be tailored to business lines, currencies, *branches* and legal entities and must include adequate allocation mechanisms of liquidity costs, benefits and risks.

[Note: Art. 86(1) of the CRD]

- 3.2 The strategies, policies, processes and systems referred to in 3.1 must be proportionate to the complexity, risk profile and scope of operation of the *firm*, and the *liquidity risk* appetite and *funding risk* appetite set by the *firm's management body* in accordance with Chapter 4 (Liquidity risk appetite and funding risk appetite), and must reflect the *firm's* importance in each country in which it carries on business.

[Note: Art. 86(2) (part) of the CRD]

- 3.3 A *firm* must, taking into account the nature, scale and complexity of its activities, have *liquidity risk* profiles and *funding risk* profiles that are consistent with and not in excess of those necessary for a well-functioning and robust system.

[Note: Art. 86(3) of the CRD]

- 3.4 A *firm* must put in place risk management policies to define its approach to asset encumbrance, as well as procedures and controls that ensure that the risks associated with collateral management and asset encumbrance are adequately identified, monitored and managed.
- 3.5 A *firm* must ensure that its systems and processes enable it, at the request of the *PRA*, to:
- (1) report the items referred to in Title II and Title III of Part Six of the *CRR* at least daily; and

- (2) produce and transmit to the *PRA* any data and information necessary for the purpose of monitoring the *firm's* compliance with this Part.

4 LIQUIDITY RISK APPETITE AND FUNDING RISK APPETITE

- 4.1 A *firm* must ensure that:
 - (1) its *management body* establishes the *firm's liquidity risk* appetite and *funding risk* appetite and that this is appropriately documented;
 - (2) its *liquidity risk* appetite and *funding risk* appetite is appropriate for its business strategy and reflects its financial condition and funding capacity; and
 - (3) its *liquidity risk* appetite and *funding risk* appetite is communicated to all relevant business lines.

[Note: Art. 86(2) (part) of the CRD]

5 INTRA-DAY MANAGEMENT OF LIQUIDITY

- 5.1 A *firm* must actively manage its intra-day liquidity positions and any related risks so that it is able to meet its payment and settlement obligations on a timely basis.
- 5.2 For the purposes of 5.1, a *firm* must ensure that its intra-day liquidity management arrangements enable it:
 - (1) to meet its payment and settlement obligations on a timely basis under both normal financial conditions and under the stresses required by 11.3;
 - (2) to identify and prioritise the most time-critical payment and settlement obligations; and
 - (3) in relation to the markets in which it is active and the currencies in which it has significant positions, to measure, monitor and deal with intra-day *liquidity risk*. A *firm* must in particular be able to:
 - (a) measure expected daily gross liquidity inflows and outflows, anticipate the intra-day timing of these flows where possible, and forecast the range of potential net funding shortfalls that might arise at different points during the day; and
 - (b) manage the timing of its liquidity outflows such that priority is given to the *firm's* most time-critical payment obligations.

6 TRANSFER PRICING SYSTEM

- 6.1 A *firm* must implement an adequate transfer pricing system to ensure that it accurately quantifies liquidity costs, benefits and risk in relation to all significant business activities.

7 MANAGEMENT OF COLLATERAL

- 7.1 A *firm* must actively manage collateral positions.
- 7.2 A *firm* must distinguish between pledged and unencumbered assets that are available at all times, in particular during emergency situations. A *firm* must also take into account the legal entity in which assets reside, the country where assets are legally recorded either in a register or in an account as well as their eligibility and must monitor how assets can be mobilised in a timely manner.

[Note: Art. 86(5) of the CRD]

8 MANAGING LIQUIDITY ACROSS LEGAL ENTITIES, BUSINESS LINES, COUNTRIES AND CURRENCIES

- 8.1 A *firm* must actively manage its *liquidity risk* exposures and related funding needs and take into account:
- (1) existing legal, regulatory and operational limitations to potential transfers of liquidity and unencumbered assets amongst entities, both within and outside the *EEA*; and
- [Note: Art. 86(6) of the CRD]**
- (2) any other constraints on the transferability of liquidity and unencumbered assets across business lines, countries and currencies.

9 FUNDING DIVERSIFICATION AND MARKET ACCESS

- 9.1 A *firm* must ensure that it has access to funding which is adequately diversified, both as to source and tenor.
- 9.2 A *firm* must develop methodologies for the identification, measurement, management and monitoring of funding positions. Those methodologies must include the current and projected material cash-flows in and arising from assets, liabilities, off-balance-sheet items, including contingent liabilities and the possible impact of reputational risk.

[Note: Art. 86(4) of the CRD]

10 MANAGEMENT OF ASSET ENCUMBRANCE

- 10.1 A *firm* must actively manage its asset encumbrance position.
- 10.2 For the purpose of 10.1 a *firm* must ensure that:
- (1) its risk management policies take into account:
 - (a) the *firm*'s business model;
 - (b) the countries in which it operates;
 - (c) the specificities of the funding markets; and

- (d) the macroeconomic situation; and
 - (2) its *management body* receives timely information on:
 - (a) the current and expected level and types of asset encumbrance and related sources of encumbrance, such as secured funding or other transactions;
 - (b) the amount, expected level and credit quality of unencumbered assets that are capable of being encumbered, specifying the volume of assets available for encumbrance; and
 - (c) the expected amount, level and types of additional encumbrance that may result from stress scenarios.
- 10.3 For the purpose of this Chapter a *firm* must treat an asset as encumbered if it is subject to any form of arrangement to secure, collateralise or credit enhance any transaction.

11 STRESS TESTING

- 11.1 A *firm* must consider different *liquidity risk* mitigation tools, including a system of limits and liquidity buffers in order to be able to withstand a range of different stress events and an adequately diversified funding structure and access to funding sources. It must review those arrangements regularly.

[Note: Art. 86(7) of the CRD]

- 11.2 A *firm* must consider alternative scenarios on liquidity positions and on risk mitigants and must review the assumptions underlying decisions concerning the funding position at least annually. For these purposes, alternative scenarios must address, in particular, off-balance sheet items and other contingent liabilities, including those of *securitisation special purpose entities* or other special purpose entities, as referred to in the *CRR* in relation to which the *firm* acts as *sponsor* or provides material liquidity support.

[Note: Art. 86(8) of the CRD]

- 11.3 A *firm* must:
- (1) conduct on a regular basis appropriate stress tests so as to:
 - (a) identify sources of potential liquidity strain;
 - (b) ensure that current liquidity exposures continue to conform to the *liquidity risk* and *funding risk* appetite established by that *firm's management body*; and
 - (c) identify the effects on that *firm's* assumptions about pricing; and
 - (2) analyse on a regular basis the separate and combined impact of possible future liquidity stresses on its:
 - (a) cash flows;
 - (b) liquidity position;
 - (c) profitability; and

(d) solvency.

11.4 A *firm* must consider the potential impact of institution-specific, market-wide and combined alternative scenarios. Different time periods and varying degrees of stressed conditions must be considered.

[Note: Art. 86(9) of the CRD]

11.5 In carrying out the liquidity stress tests required by 11.3, a *firm* must make appropriate assumptions around the major sources of risk, including the major sources of risk in each of the following categories where they are relevant to the *firm* given the nature and scale of its business:

- (1) retail *funding risk*;
- (2) wholesale secured and unsecured *funding risk*;
- (3) risks arising from the correlation between funding markets and lack of diversification between funding types;
- (4) off-balance sheet *funding risk*;
- (5) risks arising from the *firm's* funding tenors;
- (6) risks associated with a deterioration of a *firm's* credit rating;
- (7) cross currency *funding risk*;
- (8) risk that liquidity resources cannot be transferred across entities, sectors and countries;
- (9) *funding risks* resulting from estimates of future balance sheet growth;
- (10) franchise risk;
- (11) intra-day risk;
- (12) marketable assets funding risk;
- (13) non-marketable assets risk; and
- (14) internalisation risk.

11.6 A *firm* must ensure that its *management body* reviews regularly the stresses and scenarios tested to ensure that their nature and severity remain appropriate and relevant to the *firm*.

11.7 A *firm* must ensure that the results of its stress tests are:

- (1) reviewed by its *senior management*;
- (2) reported to that *firm's management body*, specifically highlighting any vulnerabilities identified and proposing appropriate remedial action;
- (3) reflected in the processes, strategies and systems established in accordance with 3.1;
- (4) used to develop effective *liquidity contingency plans*;

- (5) integrated into that *firm's* business planning process and day-to-day risk management; and
 - (6) taken into account when setting internal limits for the management of that *firm's liquidity risk* exposure.
- 11.8 A *firm* must report the results of its liquidity stress tests to the *PRA* in a timely manner.

12 LIQUIDITY CONTINGENCY PLAN

- 12.1 A *firm* must adjust its strategies, internal policies and limits on *liquidity risk* and *funding risk* and develop an effective *liquidity contingency plan*, taking into account the outcome of the alternative scenarios referred to in 11.2.

[Note: Art. 86(10) of the CRD]

- 12.2 The *liquidity contingency plan* must include strategies to address the contingent encumbrance resulting from relevant stress events including downgrades in the firm's credit rating, devaluation of pledged assets and increases in margin requirements.
- 12.3 The *liquidity contingency plan* must also set out adequate strategies and proper implementation measures in order to address possible liquidity shortfalls, including in relation to *branches* established in another *EEA State*. Those plans must be tested at least annually, updated on the basis of the outcome of the alternative scenarios set out in 11.2, and be reported to and approved by the *firm's senior management*, so that internal policies and processes can be adjusted accordingly.

[Note: Art. 86(11) (part) of the CRD]

- 12.4 A *firm* must take the necessary operational steps in advance to ensure that *liquidity contingency plans* can be implemented immediately, including holding collateral immediately available for central bank funding. This includes holding collateral where necessary in the currency of another *EEA State* or currency of a *third country* to which the *firm* has exposures, and where operationally necessary within the territory of an *EEA State* or *third country* to whose currency it is exposed.

[Note: Art. 86(11) (part) of the CRD]

13 INTERNAL LIQUIDITY ADEQUACY ASSESSMENT PROCESS

- 13.1 A *firm* must ensure that:
- (1) it regularly, but at least annually, reviews its *ILAAP*;
 - (2) carries out an internal assessment of the adequacy of its liquidity in accordance with its *ILAAP*;
 - (3) the assessment in (2) is proportionate to the nature, scale and complexity of its activities and includes an assessment of:
 - (a) the adequacy of its liquidity resources to cover the risks identified in accordance with this Part;

- (b) the methodologies and assumptions applied for risk measurement and liquidity management;
 - (c) the results of the stress tests required by 11.3; and
 - (d) the *firm's* compliance with this Part;
- (4) its *ILAAP* identifies those of the measures set out in its *liquidity contingency plans* that it would implement.
- 13.2 A *firm* must maintain a record of its *ILAAP* for at least three years.
- 13.3 A *firm* must ensure that its *management body* approves the *firm's* *ILAAP*.

14 APPLICATION OF THIS PART ON AN INDIVIDUAL BASIS AND A CONSOLIDATED BASIS

- 14.1 This Part applies to a *firm* on an individual basis whether or not it also applies to the *firm* on a *consolidated basis* or a *sub-consolidated basis*.

[Note: Art 109(1) of the CRD]

- 14.2 Where a *firm* is a member of a *consolidation group*, the *firm* must ensure that the arrangements, processes and mechanisms at the level of the *consolidation group* of which it is a member comply with the obligations set out in 3 to 13 on a *consolidated basis* (or a *sub-consolidated basis*).
- 14.3 Compliance with 14.2 must enable the *consolidation group* to have arrangements, processes and mechanisms that are consistent and well integrated and that any data relevant to the purpose of supervision can be produced.

[Note: Art 109(2) (part) of the CRD]

- 14.4 A *UK bank* or *building society* which is an *EEA parent institution* must comply with this Part on the basis of its *consolidated situation*.
- 14.5 A *UK designated investment firm* which is an *EEA parent institution* must comply with this Part on the basis of its *consolidated situation* if the *firm* is an *investment firm* that is authorised to provide the investment services and activities listed in points (3) and (6) of Section A of Annex I to Directive 2004/39/EC.
- 14.6 A *UK bank* or *building society* controlled by an *EEA parent financial holding company* or by an *EEA parent mixed financial holding company* must comply with this Part on the basis of the *consolidated situation* of that holding company if the *PRA* is responsible for supervision of the *UK bank* or *building society* on a *consolidated basis* under Article 111 of the *CRD*.
- 14.7 A *UK designated investment firm* controlled by an *EEA parent financial holding company* or by an *EEA parent mixed financial holding company* must comply with this Part on the basis of the *consolidated situation* of that holding company if:
- (1) the *firm* is an *investment firm* that is authorised to provide the investment services and activities listed in points (3) and (6) of Section A of Annex I to Directive 2004/39/EC;

- (2) there is no *subsidiary* of the holding company which is a *credit institution* that is supervised under the *CRD*; and
- (3) the *PRA* is responsible for the supervision of the *UK designated investment firm* on a *consolidated basis* under Article 111 of the *CRD*.

14.8 If this Part applies to a *firm* on a *consolidated basis*, the *firm* must carry out consolidation to the extent and in the manner prescribed in Articles 18(1), 19(1), 19(3), 23 and 24 of the *CRR*.

15 TRANSITIONAL PROVISION

15.1 In 1.2 and 14.4 to 14.7:

- (1) any reference to *EEA* is to be read as a reference to *EU*; and
- (2) any reference to *EEA State* is to be read as a reference to *Member State*.

**PRA RULEBOOK: CRR FIRMS: LIQUIDITY COVERAGE REQUIREMENT –
TRANSITIONAL PROVISION INSTRUMENT [YEAR]**

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (1) section 137G (the PRA’s general rules); and
 - (2) section 137T (general supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

**PRA Rulebook: CRR Firms: Liquidity Coverage Requirement Ratio – Transitional Provision
Instrument [YEAR]**

- D. The PRA makes the rules in the Annex to this instrument.

Commencement

- E. This instrument comes into force on 1 October 2015.

Citation

- F. This instrument may be cited as the PRA Rulebook: CRR Firms: Liquidity Coverage Requirement Ratio – Transitional Provision Instrument [YEAR]

By order of the Board of the Prudential Regulation Authority

[DATE]

Annex

In this Annex, the text is all new and is not underlined.

Part

**LIQUIDITY COVERAGE REQUIREMENT –
TRANSITIONAL PROVISION**

Chapter content

- 1. APPLICATION AND DEFINITIONS**
- 2. TRANSITIONAL PROVISIONS**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to:

- (1) a *UK bank*; or
- (2) a *building society*.

1.2 In this Part, the following definitions shall apply:

liquidity coverage ratio

means the ratio calculated in accordance with Article 4 of the Commission Delegated Regulation (EU) No [number]¹.

2 TRANSITIONAL PROVISION

2.1 The applicable *liquidity coverage ratio* for the purpose of Article 412(5) *CRR* shall be:

- (1) 80% as from 1 October 2015;
- (2) 90% as from 1 January 2017; and
- (3) 100% as from 1 January 2018.

¹ Replace with Official Journal number of Commission Delegated Regulation made under article 460 of the CRR.

PRA RULEBOOK: CRR FIRMS: LIQUIDITY COVERAGE REQUIREMENT – UK DESIGNATED INVESTMENT FIRMS INSTRUMENT [YEAR]

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (1) section 137G (the PRA’s general rules); and
 - (2) section 137T (general supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook: CRR Firms: Liquidity Coverage Requirement – UK Designated Investment Firms Instrument [YEAR]

- D. The PRA makes the rules in the Annex to this instrument.

Commencement

- E. This instrument comes into force on [Date].

Citation

- F. This instrument may be cited as the PRA Rulebook: CRR Firms: Liquidity Coverage Requirement – UK Designated Investment Firms Instrument [Year].

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex

In this Annex, the text is all new and is not underlined.

Part

LIQUIDITY COVERAGE REQUIREMENT – UK DESIGNATED INVESTMENT FIRMS

Chapter content

- 1. APPLICATION AND DEFINITIONS**
- 2. LIQUIDITY COVERAGE REQUIREMENT**
- 3. COMPLIANCE WITH LIQUIDITY REPORTING**
- 4. APPLICATION OF THIS PART ON AN INDIVIDUAL BASIS AND A CONSOLIDATED BASIS**
- 5. TRANSITIONAL PROVISIONS**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to a *UK designated investment firm*.

1.2 In this Part, the following definitions shall apply:

COREP Regulation

means the Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and the Council, as amended by [Commission Implementing Regulation on additional liquidity monitoring metrics]¹.

Delegated Regulation

means Commission Delegated Regulation (EU) [number]².

EEA parent institution

means a *parent institution in an EEA State* which is not a *subsidiary* of another *institution* authorised in an *EEA State* or of a *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

EEA parent financial holding company

means a *parent financial holding company in an EEA State* which is not a *subsidiary* of an *institution* authorised in any *EEA State* or of another *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

EEA parent mixed financial holding company

means a *parent mixed financial holding company* in an *EEA State* which is not a *subsidiary* of an *institution* authorised in any *EEA State* or of another *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

liquidity coverage ratio

means the ratio calculated in accordance with Article 4 of the *Delegated Regulation*.

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 LIQUIDITY COVERAGE REQUIREMENT

2.1 (1) For the purpose of complying with Article 412 (1) of the *CRR*, a *firm* must comply with the obligations set out in the *Delegated Regulation* as they apply to a *credit institution* supervised under the *CRD*, subject to the modifications in (2).

¹ Replace with ITS to be adopted by the Commission in accordance with CRR Art 415(3)(b).

² Replace with Official Journal number of Commission Delegated Regulation made under article 460 of the CRR

- (2) For the purposes of (1):
 - (a) the provisions in Article 2(3) of the *Delegated Regulation* do not apply where Article 12 of the *CRR* applies;
 - (b) the provisions in Article 2(3)(d) and Article 37 of the *Delegated Regulation* do not apply; and
 - (c) any reference to *competent authority* means a reference to the *PRA*.

3 COMPLIANCE WITH LIQUIDITY REPORTING

- 3.1 In accordance with Article 6(4) and Article 11(3) of the *CRR*, a *firm* is exempt from complying with the obligations laid down in Title II and Title III of Part Six of the *CRR* on an individual basis and on a *consolidated basis*.
- 3.2 (1) A firm must comply with the reporting requirements laid down in Articles 2, 3, 15³, 16, 16(b) and 18 of the *COREP Regulation* as they apply to a *credit institution* supervised under the *CRD*.
- (2) For these purposes of (1), the words “according to Article 415 of Regulation (EU) No 575/2013” in Articles 15, 16 and 16b of the *COREP Regulation* are construed as references to the obligations set out in (1).

4 APPLICATION OF THIS PART ON AN INDIVIDUAL BASIS AND A CONSOLIDATED BASIS

- 4.1 This Part applies to a *firm* on an individual basis whether or not it also applies to the *firm* on a *consolidated basis*.
- 4.2 A *firm* which is an *EEA parent institution* must comply with this Part on the basis of its *consolidated situation* if the *firm* is an *investment firm* that is authorised to provide the investment services and activities listed in points (3) and (6) of Section A of Annex I to Directive 2004/39/EC.
- 4.3 A *firm* controlled by an *EEA parent financial holding company* or by an *EEA parent mixed financial holding company* must comply with this Part on the basis of the *consolidated situation* of that holding company if:
 - (1) the *firm* is an *investment firm* that is authorised to provide the investment services and activities listed in points (3) and (6) of Section A of Annex I to Directive 2004/39/EC;
 - (2) there is no *subsidiary* of the holding company which is a *credit institution* that is supervised under the *CRD*; and
 - (3) the *PRA* is responsible for the supervision of the *UK designated investment firm* on a *consolidated basis* under Article 111 of the *CRD*.

³ Replace with reference to the updated Liquidity Coverage Templates under the *COREP Regulation*.

- 4.4 If this Part applies to a *firm* on a *consolidated basis*, the *firm* must carry out consolidation to the extent and in the manner prescribed in Articles 18(1), 19(1), 19(3) 23 and 24 of the *CRR*.

5 TRANSITIONAL PROVISIONS

- 5.1 The applicable *liquidity coverage ratio* for the purpose of Article 38 (2) of the *Delegated Regulation* shall be:
- (1) 80% as from 1 October 2015;
 - (2) 90% as from 1 January 2017; and
 - (3) 100% as from 1 January 2018.
- 5.2 In 1.2, 4.2 and 4.3:
- (1) any reference to *EEA* is to be read as a reference to *EU*; and
 - (2) any reference to *EEA State* is to be read as a reference to *Member State*.

PRA RULEBOOK: NON-CRR FIRMS: LIQUIDITY REPORTING INSTRUMENT [YEAR]

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (1) section 137G (the PRA’s general rules); and
 - (2) section 137T (general supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook: Non-CRR Firms: Liquidity Reporting Instrument [YEAR]

- D. The PRA makes the rules in the Annex to this instrument.

Commencement

- E. This instrument comes into force on 1 April 2016.

Citation

- F. This instrument may be cited as the PRA Rulebook: Non-CRR Firms: Liquidity Reporting Instrument [YEAR].

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex

In this Annex, the text is all new and is not underlined.

Part

LIQUIDITY REPORTING

Chapter content

- 1. APPLICATION**
- 2. COMPLIANCE WITH CRR LIQUIDITY REPORTING**
- 3. SYSTEMS, PROCESSES AND MECHANISMS**
- 4. TRANSITIONAL PROVISION**

Links

1 APPLICATION

- 1.1 This Part applies to every *third country firm* that is a *bank* or a *designated investment firm*.

2 COMPLIANCE WITH CRR LIQUIDITY REPORTING

- 2.1 A *firm* must comply with the reporting requirements laid down in Titles II and III of Part 6 of the *CRR* on an individual basis as they apply to a *credit institution* supervised under the *CRD*, subject to the modifications in 2.2.
- 2.2 The modifications referred to in 2.1 are that the provisions in Article 16b (1) (b) and (c) of the Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and the Council, as amended by [Commission Implementing Regulation on additional liquidity monitoring metrics]¹, do not apply.

3 SYSTEMS, PROCESSES AND MECHANISMS

- 3.1 A *firm* must put in place systems, processes and mechanisms that enable it, at the request of the *PRA*, to report:
- (1) report the items referred to in the reporting requirements in 2.1 at least daily; and
 - (2) produce and transmit to the *PRA* any data and information necessary for the purpose of liquidity supervision.

4 TRANSITIONAL PROVISION

- 4.1 In 1.1 the reference to *third country firm* is to be read as a reference to a *firm* which has its registered office (or, if it has no registered office, its head office) outside the *European Union*.

¹ Replace with Implementing Technical Standards to be adopted by the Commission in accordance with CRR Art 415(3)(b).

LIQUIDITY STANDARDS CONSEQUENTIALS INSTRUMENT [YEAR]

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (The PRA’s general rules); and
 - (2) section 137T (General supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Commencement

- D. Annex A to Annex D and Annex F to this instrument come into force on 1 October 2015.
- E. Annex E to this instrument shall come into force on the date specified by a subsequent PRA Board Instrument.

Amendments to the Handbook

- F. The modules of the *PRA Handbook* of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary of definitions	Annex A
Senior Management Arrangements, Systems and Controls sourcebook (SYSC)	Annex B
Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)	Annex C
Supervision manual (SUP)	Annex D
Supervision manual (SUP)	Annex E

Amendments to the Rulebook

- G. The PRA Rulebook: Fundamental Rules is amended in accordance with Annex F to this instrument.

Citation

- H. This instrument may be cited as the Liquidity Standards Consequential Instrument [YEAR].

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text. Insert the following new definitions and amendments in the appropriate alphabetical order.

ILAS BIPRU firm (A) In the PRA Handbook:
~~a firm falling into BIPRU 12.1.1R, but excluding a firm that is:~~

- (a) ~~an exempt full scope BIPRU investment firm; or a UK bank; or~~
- (b) ~~a BIPRU limited licence firm; or a building society; or~~
- (c) ~~a BIPRU limited activity firm; or a UK designated investment firm; or~~
- (d) ~~an exempt BIPRU commodities firm.~~ a third country reporting firm that has a branch in the United Kingdom.

...

intra-group liquidity modification a modification to the *overall liquidity adequacy rule* of the kind described in *BIPRU 12.8.7G* as in effect on 30 September 2015 granted to a firm and in effect on that date.

...

low frequency liquidity reporting firm any of the following:

- (a) a *simplified ILAS BIPRU firm*; or
- (b) a *standard ILAS BIPRU firm* whose most recent *annual report and accounts* show balance sheet assets of less than £5 billion (or its equivalent in foreign currency translated into sterling at the balance sheet date); or
- (c) a *standard ILAS BIPRU firm* that meets the following conditions:
 - (i) it does not have any *annual report and accounts* and it has been too recently established to be required to have produced any;

- (ii) it has submitted a projected balance sheet to the *FCA* or *PRA* (as the case may be) as part of an application for a *Part 4A* permission or a variation of one; and
- (iii) the most recent such balance sheet shows that the *firm* will meet the size condition in (b) in all periods covered by that projection.

In respect of ~~an incoming EEA firm or~~ a third country BIPRU reporting firm that is also a *standard ILAS BIPRU firm* and which reports on the basis of its *branch* operation in the *United Kingdom*, if the balance sheet assets attributable to the *UK branch* can be determined from the firm's most recent *annual report and accounts* (or, if applicable, the projected balance sheet) or any *data item* submitted by the *firm*, then paragraphs (b) and (c) apply at the level of the *branch* rather than of the *firm*.

...

overall liquidity adequacy rule

BIPRU 12.2.1R as in effect on 30 September 2015.

...

simplified ILAS

the approach to the calculation of the liquid assets buffer of a *simplified ILAS BIPRU firm* described in *BIPRU 12.6* as in effect on 30 September 2015.

...

simplified ILAS BIPRU firm

an *ILAS BIPRU firm* that, in accordance with the procedures in *BIPRU 12 (Liquidity)* as in effect on 30 September 2015, is ~~was~~ using the *simplified ILAS* on that date.

...

third country reporting firm

one of the following:

- (1) an overseas firm that:
 - (a) is a bank;
 - (b) is not an EEA firm; and
 - (c) has its head office outside the EEA; or
- (2) an EEA bank that has its registered office (or if it has no registered office, its head office) outside the EU.

...

*whole-firm liquidity
modification*

a modification to the *overall liquidity adequacy rule* of the kind described in *BIPRU 12.8.22G* as in effect on 30 September 2015 granted to a *firm* and in effect on that date.

Annex B

**Amendments to the Senior Management Arrangements, Systems and Controls
sourcebook (SYSC)**

In this Annex, underlining indicates new text and striking through indicates deleted text.

12.1 Application

...

CRR firms and non-CRR firms that are parent financial holding companies in a Member State

12.1.13 R If this *rule* applies under SYSC 12.1.14R to a *firm*, the *firm* must:

- (1) ...
- (2) ensure that the risk management processes and internal control mechanisms at the level of any *consolidation group* or non-*EEA sub-group* of which it is a member comply with the obligations set out in the following provisions on a consolidated (or sub-consolidated) basis:
 - (a) ...
 - ...
 - (e) ~~BIPRU 12.3.4 R, BIPRU 12.3.5 R, BIPRU 12.3.7A R, BIPRU 12.3.8 R, BIPRU 12.3.22A R, BIPRU 12.3.22B R, BIPRU 12.3.27 R, BIPRU 12.4.2 R, BIPRU 12.4.1 R, BIPRU 12.4.5A R, BIPRU 12.4.10 R, BIPRU 12.4.11 R and BIPRU 12.4.11A R; [deleted]~~
 - (f) ...

...

Annex C

Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)

The entirety of part 2 of the Annex to Prudential sourcebook for Banks, Building Societies and Investment Firms (Liquidity Standards) Amendments Instrument 2013 is revoked.

BIPRU 12, BIPRU Schedule 3 and BIPRU Schedule 6 are deleted in their entirety.

Annex D

Amendments to the Supervisory manual (SUP)

The entirety of part 5 of the Annex of the Capital Requirements Regulation (Reporting) Amendment Instrument 2013 is revoked.

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

16.12 Integrated Regulatory Reporting

...

16.12.4A G ~~RAG 1 includes an incoming EEA firm exercising a BCD right through a UK branch.~~[deleted]

Group liquidity reporting

16.12.4B G ~~Reporting at group level for liquidity purposes by firms falling within BIPRU 12 (Liquidity) is by reference to defined liquidity groups. Guidance about the different types of defined liquidity groups and related material is set out in SUP 16 Annex 26 (Guidance on designated liquidity groups in SUP 16.12).~~[deleted]

Regulated Activity Group 1

SUP 16.12.5R is deleted in its entirety. This text is not shown.

16.12.5A R The applicable *data items* and forms or reports referred to in SUP 16.12.4R are set out according to *firm type* in the table below:

Description of data item	Prudential category of firm, applicable data items and reporting format (Note 1)						
	<u>UK bank</u>	<u>Building society</u>	<u>Non-EEA bank</u>	<u>EEA bank that has its registered office (or, if it has no registered office, its head office) outside the EU that has permission to accept deposits, other than one with permission for cross border services</u>	[deleted]	<u>Credit union</u>	<u>Dormant account fund operator (note 15)</u>

				only			
<u>Annual report and accounts</u>	<u>No standard format</u>		<u>No standard format, but in English</u>				<u>No standard format</u>
<u>Annual report and accounts of the mixed-activity holding company (note 9)</u>	<u>No standard format</u>						
<u>Solvency statement (note 10)</u>	<u>No standard format</u>						
<u>Balance sheet</u>	<u>FSA001 (note 2)</u>	<u>FSA001 (note 2)</u>				<u>CQ; CY</u>	
<u>Income statement</u>	<u>FSA002 (note 2)</u>	<u>FSA002 (note 2)</u>	<u>FSA002</u>			<u>CQ; CY</u>	
<u>Capital adequacy</u>						<u>CQ; CY</u>	
	[deleted]	[deleted]					
<u>Market risk</u>	<u>FSA005 (notes 2, 4)</u>	<u>FSA005 (notes 2, 4)</u>					
<u>Market risk - supplementary</u>	<u>FSA006 (note 5)</u>						
<u>Large exposures</u>						<u>CQ; CY</u>	
<u>Exposures between core UK group and non-core large exposures group</u>	<u>FSA018 (note 12)</u>	<u>FSA018 (note 12)</u>					
<u>Liquidity (other than stock)</u>		<u>FSA011</u>				<u>CQ; CY</u>	
<u>Forecast data</u>	<u>FSA014 (note 11)</u>	<u>FSA014 (note 11)</u>					
<u>Solo consolidation data</u>	<u>FSA016 (note 7)</u>	<u>FSA016 (note 7)</u>					
<u>Interest rate gap report</u>	<u>FSA017</u>	<u>FSA017</u>					

<u>Sectoral information, including arrears and impairment</u>	<u>FSA015 (Note 2)</u>	<u>FSA015 (Note 2)</u>				
<u>IRB portfolio risk</u>	<u>FSA045 (note 13)</u>	<u>FSA045 (note 13)</u>				
<u>Daily Flows</u>	<u>FSA047 (Notes 16, 20 and 22)</u>	<u>FSA047 (Notes 16, 20 and 22)</u>	<u>FSA047 (Notes 16, 18, 20 and 22)</u>	<u>FSA047 (Notes 16, 18, 20 and 22)</u>		
<u>Enhanced Mismatch Report</u>	<u>FSA048 (Notes 16, 20 and 22)</u>	<u>FSA048 (Notes 16, 20 and 22)</u>	<u>FSA048 (Notes 16, 18, 20 and 22)</u>	<u>FSA048 (Notes 16, 18, 20 and 22)</u>		
<u>Funding Concentration</u>	<u>FSA051 (Notes 17, 21 and 22)</u>	<u>FSA051 (Notes 17, 21 and 22)</u>	<u>FSA051 (Notes 17, 19, 21 and 22)</u>	<u>FSA051 (Notes 17, 19, 21 and 22)</u>		
<u>Retail and corporate funding</u>	<u>FSA053 (Notes 17, 21 and 22)</u>	<u>FSA053 (Notes 17, 21 and 22)</u>	<u>FSA053 (Notes 17, 19, 21 and 22)</u>	<u>FSA053 (Notes 17, 19, 21 and 22)</u>		
<u>Note 1</u>	<u>When submitting the completed <i>data item</i> required, a <i>firm</i> must use the format of the <i>data item</i> set out in SUP 16 Annex 24R, except for credit union reports that are in SUP 16 Annex 14R. Guidance notes for completion of the data items are contained in SUP 16 Annex 25G (or Annex 15G for credit unions).</u>					
<u>Note 2</u>	<u><i>Firms</i> that are members of a <i>UK consolidation group</i> are also required to submit this data item on a <i>UK consolidation group</i> basis. <i>Firms'</i> attention is drawn to SUP 16.3.25G regarding a single submission for all <i>firms</i> in the <i>group</i>.</u>					
<u>Note 3</u>	<u>[deleted]</u>					
<u>Note 4</u>	<u>For <i>PRA-authorised persons</i> lines 62 to 64 only are applicable. These lines apply to a <i>firm</i> that applies add-ons to their market risk capital calculation under the RNIV framework. For further guidance on how to complete the form <i>PRA-authorised persons</i> may refer to SUP 16.12.25A R.</u>					
<u>Note 5</u>	<u>Only applicable to <i>firms</i> with a <i>VaR model permission</i>.</u>					
<u>Note 6</u>	<u>[deleted]</u>					
<u>Note 7</u>	<u>Only applicable to a <i>firm</i> that has a <i>solo consolidation waiver</i>.</u>					
<u>Note 8</u>	<u>[deleted]</u>					
<u>Note 9</u>	<u>[deleted]</u>					
<u>Note 10</u>	<u>[deleted]</u>					
<u>Note 11</u>	<u>Members of a <i>UK consolidation group</i> should only submit this <i>data item</i> at the <i>UK consolidation group</i> level.</u>					
<u>Note 12</u>	<u>Only applicable to a <i>firm</i> that has both a <i>core UK group</i> and a <i>non-core large exposures group</i>.</u>					
<u>Note 13</u>	<u>Only applicable to <i>firms</i> that have an <i>IRB permission</i>.</u>					
<u>Note 14</u>	<u>[deleted]</u>					

Note 15	Only applies to a <i>dormant account fund operator</i> that does not fall into any of the other prudential categories in this table.
Note 16	<p><u>A firm must complete this item separately on each of the following bases that are applicable.</u></p> <p>(1) It must complete it on a solo basis (including on the basis of the <i>firm's UK branch</i>). Therefore even if it has a <i>solo consolidation waiver</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it is a <i>group liquidity reporting firm</i> in a <i>DLG by default</i> and is a <i>UK lead regulated firm</i>, it must complete the item on the basis of that group.</p> <p>(3) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that group and (1) does not apply.</p> <p>(4) If it is a <i>group liquidity reporting firm</i> in a <i>non-UK DLG by modification</i>, it must complete the item on the basis of that group.</p>
Note 17	<p><u>A firm must complete this item separately on each of the following bases that are applicable.</u></p> <p>(1) It must complete it on a solo basis (including on the basis of the <i>firm's UK branch</i>) unless it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>. Therefore even if it has a <i>solo consolidation waiver</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that group.</p>
Note 18	<p>(1) If the <i>firm</i> has a <i>whole-firm liquidity modification</i>, it must complete this item on the basis of the whole <i>firm</i> (or at any other <i>reporting level</i> the <i>whole-firm liquidity modification</i> may have required) and not just its <i>UK branch</i>.</p> <p>(2) Otherwise the <i>firm</i> must complete this item by reference to the activities of its branch operation in the <i>United Kingdom</i> in accordance with SUP 16.12.3R (1)(a)(iv).</p>
Note 19	<p>(1) If the <i>firm</i> has a <i>whole-firm liquidity modification</i> there is no obligation to report this item.</p> <p>(2) Otherwise the <i>firm</i> must complete this item by reference to the activities of its branch operation in the <i>United Kingdom</i> in accordance with SUP 16.12.3R (1)(a)(iv).</p>
Note 20	<p>(1) This item must be reported in the reporting currency.</p> <p>(2) If any <i>data element</i> is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency.</p> <p>(3) In addition, all <i>material currencies</i> (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if:</p> <p>(a) the reporting frequency is (whether under a <i>rule</i> or under a <i>waiver</i>) quarterly or less than quarterly; or</p> <p>(b) the only <i>material currency</i> is the reporting currency;</p> <p>(3) does not apply.</p> <p>(4) If there are more than three <i>material currencies</i> for this <i>data item</i>, (3) only applies to the three largest in amount. A <i>firm</i> must identify the largest in amount in accordance with the following procedure.</p> <p>(a) For each currency, take the largest of the asset or liability figure as referred to in the definition of <i>material currency</i>.</p> <p>(b) Take the three largest figures from the resulting list of amounts.</p> <p>(5) The date as at which the calculations for the purposes of the definition of <i>material currency</i> are carried out is the last day of the reporting period in question.</p> <p>(6) The reporting currency for this <i>data item</i> is whichever of the following currencies the <i>firm</i> chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).</p>
Note 21	Note 20 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that <i>material currencies</i> must not be recorded separately.
Note 22	Any changes to reporting requirements caused by a <i>firm</i> receiving an <i>intra-group liquidity modification</i> or a <i>whole-firm liquidity modification</i> (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the <i>data item</i> in question if the <i>firm</i> receives that <i>intra-group liquidity modification</i> , <i>whole-firm liquidity modification</i> or variation part of the way through such a period. If the change is that the <i>firm</i> does not have to report a particular <i>data item</i> or does not have to report it at a particular <i>reporting level</i> , the <i>firm</i> must nevertheless report that item or at that <i>reporting level</i> for any reporting period that has already begun. This paragraph is subject to anything that the <i>intra-group liquidity modification</i> or a <i>whole-firm liquidity modification</i> says to the contrary.
Note 23	Only applicable to <i>firms</i> that hold <i>securitisation positions</i> in the <i>trading book</i> and/ or are the <i>originator</i> or <i>sponsor</i> of <i>securitisations</i> held in the <i>trading book</i> .
Note 24	[deleted]

...

16.12.11B R The applicable *data items* referred to in SUP 16.12.4R for UK designated investment firms are set out below:

Description of <i>data item</i>	Applicable <i>data items</i> (Note 1)
...	
Daily flows	FSA047 (Notes 10, 13; and 15 and 16)
Enhanced Mismatch Report	FSA048 (Notes 10, 13; and 15 and 16)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 11, 14, 15 and 16)
Funding Concentration	FSA051 (Notes 11, 14; and 15 and 16)
Pricing data	FSA052 (Notes 11, 15, 16 and 17)
Retail and corporate funding	FSA053 (Notes 11, 14; and 15 and 16)
Currency Analysis	FSA054 (Notes 11, 14, 15 and 16)
Systems and Controls Questionnaire	FSA055 (Notes 12 and 16)
...	
Note 10	<p>A <i>firm</i> must complete this item separately on each of the following bases (if applicable).</p> <p>(1) It must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it is a <i>group liquidity reporting firm</i> in a <i>DLG by default</i> and is a <i>UK lead regulated firm</i>, it must complete the item on the basis of that group.</p> <p>(3) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that group <u>and (1) does not apply</u>.</p> <p>(4) If it is a <i>group liquidity reporting firm</i> in a <i>non-UK DLG by modification</i>, it must complete the item on the basis of that group.</p>
...	

Note 12	If it is a <i>non-ILAS BIPRU firm</i> , it must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone. [deleted]
...	
Note 16	FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an <i>ILAS BIPRU firm</i> . An <i>ILAS BIPRU firm</i> does not need to complete FSA055. A <i>non-ILAS BIPRU firm</i> must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054. [deleted]
Note 17	This <i>data item</i> must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported. [deleted]
...	

...

Regulated Activity Group 4

16.12.15B R The applicable *data items* referred to in SUP 16.12.4R for *UK designated investment firms* are set out below:

Description of <i>data item</i>	Applicable data items (Note 1)
...	
Daily Flows	FSA047 (Notes 7,10, and 12 and 13)
Enhanced Mismatch Report	FSA048 (Notes 7,10, and 12 and 13)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 8, 11, 12 and 13)
Funding Concentration	FSA051 (Notes 8, 11, and 12 and 13)
Pricing data	FSA052 (Notes 8, 12, 13 and 14)

Retail and corporate funding	FSA053 (Notes 8, 11, and 12 and 13)
Currency Analysis	FSA054 (Notes 8, 11, 12 and 13)
Pricing data	FSA052 (Notes 8, 12, 13 and 14)
Systems and Control Questionnaire	FSA055 (Notes 9 and 13)
...	
Note 7	<p>A <i>firm</i> must complete this item separately on each of the following bases (if applicable).</p> <p>(1) It must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it is a <i>group liquidity reporting firm</i> in a <i>DLG by default</i> and is a <i>UK lead regulated firm</i>, it must complete the item on the basis of that group.</p> <p>(3) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that group and (1) does not apply.</p> <p>(4) If it is a <i>group liquidity reporting firm</i> in a <i>non-UK DLG by modification</i>, it must complete the item on the basis of that group.</p>
Note 9	<p>If it is a <i>non-ILAS BIPRU firm</i>, it must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.[deleted]</p>
...	
Note 13	<p>FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an <i>ILAS BIPRU firm</i>. An <i>ILAS BIPRU firm</i> does not need to complete FSA055. A <i>non-ILAS BIPRU firm</i> must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.[deleted]</p>
Note 14	<p>This <i>data item</i> must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.[deleted]</p>

...	
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...

Regulated Activity Group 7

16.12.22C R The applicable *data items* referred to in SUP 16.12.4R for UK designated investment firms are set out in the table below:

Description of <i>data item</i>	Applicable <i>data item</i> (Note 1)
...	
Daily Flows	FSA047 (Notes 6, 9, and 11 and 12)
Enhanced Mismatch Report	FSA048 (Notes 6, 9, and 11 and 12)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 7, 10, 11 and 12)
Funding Concentration	FSA051 (Notes 7, 10, and 11 and 12)
Pricing Data	FSA052 (Note 7, 10, 12 and 13)
Retail and corporate funding	FSA053 (Notes 7, 10, and 11 and 12)
Currency Analysis	FSA054 (Notes 7, 10, 11 and 12)
Systems and Controls Questionnaire	FSA055 (Notes 8 and 12)
...	
Note 6	<p>A <i>firm</i> must complete this item separately on each of the following bases (if applicable).</p> <p>(1) It must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it is a <i>group liquidity reporting firm</i> in a <i>DLG by default</i> and is a <i>UK lead regulated firm</i>, it must complete the item on the basis of that group.</p> <p>(3) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that group <u>and (1) does not apply</u>.</p> <p>(4) If it is a <i>group liquidity reporting firm</i> in a <i>non-UK DLG by modification</i>, it must complete the item on the basis of that group</p>

Note 8	If it is a <i>non-ILAS BIPRU firm</i> , it must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone. [deleted]
...	
Note 12	FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an <i>ILAS BIPRU firm</i> . An <i>ILAS BIPRU firm</i> does not need to complete FSA055. A <i>non-ILAS BIPRU firm</i> must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054. [deleted]
Note 13	This <i>data item</i> must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported. [deleted]
...	

...

Regulated Activity Group 8

16.12.25C R The applicable *data items* referred to in SUP 16.12.4R are set out in the table below:

Description of <i>data item</i>	Applicable <i>data item</i> (Note 1)
...	
Daily flows	FSA047 (Notes 9, 12, and 14 and 15)
Enhanced Mismatch Report	FSA048 (Notes 9, 12, 14 and 15)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 10, 13, 14 and 15)
Funding Concentration	FSA051 (Notes 10, 13, and 14 and 15)
Pricing data	FSA052 (Notes 10, 14, 15 and 16)
Retail and corporate funding	FSA053 (Notes 10, 13, and 14 and)

	15)
Currency Analysis	FSA054 (Notes 10, 13, 14 and 15)
Systems and Controls Questionnaire	FSA055(Notes 11 and 15)
Note 9	<p>A <i>firm</i> must complete this item separately on each of the following bases (if applicable).</p> <p>(1) It must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it a <i>group liquidity reporting firm</i> in a <i>DLG by default</i> and is a <i>UK lead regulated firm</i>, it must complete the item on the basis of that group.</p> <p>(3) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that group and (1) does not apply.</p> <p>(4) If it is a <i>group liquidity reporting firm</i> in a <i>non-UK DLG by modification</i>, it must complete the item on the basis of that group.</p>
...	
Note 11	<p>If it is a <i>non-ILAS BIPRU firm</i>, it must complete it on a solo basis. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone. [deleted]</p>
...	
Note 15	<p>FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an <i>ILAS BIPRU firm</i>. An <i>ILAS BIPRU firm</i> does not need to complete FSA055. A <i>non-ILAS BIPRU firm</i> must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054. [deleted]</p>
Note 16	<p>This <i>data item</i> must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported. [deleted]</p>
...	

...

16

Annex Guidance on designated liquidity groups in SUP 16.12

26

The entirety of SUP 16 Annex 26 (Guidance on designated liquidity groups in SUP 16.12) is deleted. The deleted text is not shown.

Annex E

Amendments to the Supervisory manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

16.12 Integrated Regulatory Reporting

...

Regulated Activity Group 1

SUP 16.12.5R is deleted in its entirety. This text is not shown.

16.12.5A R The applicable *data items* and forms or reports referred to in SUP 16.12.4R are set out according to *firm* type in the table below:

...

Description of data item	Prudential category of <i>firm</i> , applicable <i>data items</i> and reporting format (Note 1)						
	<i>UK bank</i>	<i>Building society</i>	<i>Non-EEA bank</i>	<i>EEA bank that has its registered office (or, if it has no registered office, its head office) outside the EU that has permission to accept deposits, other than one with permission for cross border services only</i>	[deleted]	<i>Credit union</i>	<i>Dormant account fund operator (note 15)</i>
...							
Daily Flows	FSA047 (Notes 16, 20 and 22)	FSA047 (Notes 16, 20 and 22)	FSA047 (Notes 16, 18, 20 and 22)	FSA047 (Notes 16, 18, 20 and 22)			
Enhanced Mismatch Report	FSA048 (Notes 16, 20 and 22)	FSA048 (Notes 16, 20 and 22)	FSA048 (Notes 16, 18, 20 and 22)	FSA048 (Notes 16, 18, 20 and 22)			
...							
Note 17	<p>A <i>firm</i> must complete this item separately on each of the following bases that are applicable.</p> <p>(1) It must complete it on a solo basis (including on the basis of the <i>firm's UK branch</i>) unless it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>. Therefore even if it has a <i>solo consolidation waiver</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone.</p> <p>(2) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that</p>						

	group and (1) does not apply. [deleted]
...	
Note 21	Note 20 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that <i>material currencies</i> must not be recorded separately. [deleted]

...

16.12.11B R The applicable *data items* referred to in SUP 16.12.4R for UK designated investment firms are set out below:

Description of <i>data item</i>	Applicable <i>data items</i> (Note 1)
...	
Funding Concentration	FSA051 (Notes 11, 14 and 15)
...	
Retail and corporate funding	FSA053 (Notes 11, 14 and 15)
...	
Note 11	A <i>firm</i> must complete this item separately on each of the following bases that are applicable: (1) It must complete it on a solo basis unless it is a <i>group liquidity reporting firm</i> in a UK DLG by modification. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm</i> alone. (2) If it is a <i>group liquidity reporting firm</i> in a UK DLG by modification, it must complete the item on the basis of that group. [deleted]
...	
Note 14	Note 13 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that <i>material currencies</i> must not be recorded separately. [deleted]
...	

...

Regulated Activity Group 4

16.12.15B R The applicable *data items* referred to in SUP 16.12.4R for UK designated investment firms are set out below:

Description of <i>data item</i>	Applicable <i>data items</i> (Note 1)
...	

Funding Concentration	FSA051 (Notes 8, 11 and 12)
...	
Retail and corporate funding	FSA053 (Notes 8, 11 and 12)
...	
Note 8	<p><i>A firm must complete this item separately on each of the following bases that are applicable.</i></p> <p><i>(1) It must complete it on a solo basis unless it is a group liquidity reporting firm in a UK DLG by modification. Therefore even if it has an individual consolidation permission it must complete the item on an unconsolidated basis by reference to the firm alone.</i></p> <p><i>(2) If it is a group liquidity reporting firm in a UK DLG by modification, it must complete the item on the basis of that group.</i>[deleted]</p>
...	
Note 11	Note 10 applies, except that paragraphs (3), (4), and (5) do not apply, meaning that <i>material currencies</i> must not be recorded separately.[deleted]
...	

...

Regulated Activity Group 7

16.12.22C R The applicable *data items* referred to in SUP 16.12.4R for UK designated investment firms are set out in the table below:

Description of <i>data item</i>	Applicable <i>data item</i> (Note 1)
...	
Funding Concentration	FSA051 (Notes 7, 10 and 11)
Retail and corporate funding	FSA053 (Notes 7, 10 and 11)
...	
Note 7	<p><i>A firm must complete this item separately on each of the following bases that are applicable.</i></p> <p><i>(1) It must complete it on a solo basis unless it is a group liquidity reporting firm in a UK DLG by modification. Therefore even if it has an individual consolidation permission it must complete the item on an unconsolidated basis by reference to the</i></p>

	<i>firm alone.</i> (2) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that <i>group</i>. [deleted]
...	
Note 10	Note 9 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that <i>material currencies</i> must not be recorded separately.[deleted]
...	

...

Regulated Activity Group 8

16.12.25C R The applicable *data items* referred to in SUP 16.12.4R are set out in the table below:

Description of <i>data item</i>	Applicable <i>data item</i> (Note 1)
...	
Funding Concentration	FSA051 (Notes 10, 13 and 14)
...	
Retail and corporate funding	FSA053 (Notes 10, 13 and 14)
...	
Note 10	A <i>firm</i> must complete this item separately on each of the following bases that are applicable. (1) It must complete it on a solo basis unless it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>. Therefore even if it has an <i>individual consolidation permission</i> it must complete the item on an unconsolidated basis by reference to the <i>firm alone</i>. (2) If it is a <i>group liquidity reporting firm</i> in a <i>UK DLG by modification</i>, it must complete the item on the basis of that <i>group</i>. [deleted]
...	
Note 13	Note 24 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that <i>material currencies</i> must not be recorded separately.[deleted]
...	

Annex F**Amendments to the Fundamental Rules**

In this Annex new text is underlined and deleted text is struck through.

3 RESTRICTIONS

3.1 The *Fundamental Rules* apply to every *firm*, except that:

- (1) ...
- (2) for an *incoming EEA firm* that is a *credit institution* without a *top-up permission*, Fundamental Rule 4 ~~applies only in relation to the liquidity of a branch established in the UK~~ does not apply; and
- (3) ...

Mapping of BIPRU 12 rules to the ILAA Part of the PRA Rulebook

BIPRU 12	ILAA Part of the PRA rulebook	Deleted
12.1 Application		
12.1.1 R	-	yes
12.1.2 R	-	yes
12.1.7 R	-	yes
12.2 Adequacy of liquidity resources		
12.2.1 R	2.1 and 2.2(2)	no
12.2.3 R	-	yes
12.2.8 R	2.2	no
12.2.11 R	-	yes
12.3 Liquidity risk management		
12.3.4 R	3.1	
12.3.5 R	3.2	no
12.3.5A R	3.4	no
12.3.6 E	-	yes
12.3.7A R	3.3	no
12.3.8 R	4.1	no
12.3.8A R	-	yes
12.3.10 R	-	yes
12.3.11 R	-	yes
12.3.12A R	-	yes
12.3.15A R	6.1	no
12.3.17 R	5.1	no
12.3.19A R	5.2(1)	no
12.3.21 E	5.2(2) and 5.2(3)	no
12.3.22 R	7.1	no
12.3.22A R	7.2	no
12.3.22B R	8.1(1)	no
12.3.23 R	-	yes
12.3.25A E	-	yes
12.3.26 R	-	yes
12.3.27 R	9.2	no
12.3.29 R	9.1	no
12.3.30 R	-	yes
12.3.32 E	-	yes
12.3.33 R	10.1	no
12.3.34 R	10.2	no

BIPRU 12	ILAA Part of the PRA rulebook	Deleted
12.4 Stress testing and contingency funding		
12.4.-2 R	11.1	no
12.4.-1 R	11.2	no
12.4.1A R	11.3	no
12.4.2 R	11.6	no
12.4.5A R	11.4	no
12.4.8 E	11.7	no
12.4.9 R	11.8	no
12.4.10 R	12.1	no
12.4.11 R	12.3	no
12.4.11A R	12.4	no
12.4.13A R	-	yes
12.4.14A E	-	yes
12.5 Individual Liquidity Adequacy Standards		
12.5.1 R	-	yes
12.5.2 R	-	yes
12.5.4 R	13.1 and 13.2	no
12.5.6 R	-	yes
12.5.8 R	-	yes
12.5.9 R	-	yes
12.5.11 R	-	yes
12.5.12 R	-	yes
12.5.13 R	13.1.(3)	no
12.5.14 R	11.5	no
12.5.15 R	-	yes
12.5.16 R	-	yes
12.5.19 R	-	yes
12.5.20 R	-	yes
12.5.21 R	-	yes
12.5.26 R	-	yes

BIPRU 12	ILAA Part of the PRA rulebook	Deleted
12.5.29 R	-	yes
12.5.31 R	-	yes
12.5.33 R	-	yes
12.5.34 R	-	yes
12.5.36 R	-	yes
12.5.38 R	-	yes
12.5.40 R	-	yes
12.5.41 R	-	yes
12.5.42 R	-	yes
12.5.43 R	-	yes
12.5.44 R	-	yes
12.5.52 R	-	yes
12.5.56 R	-	yes
12.5.62 R	-	yes
12.5.63 R	-	yes
12.5.67 R	-	yes
12.5.72 R	-	yes
12.5.75 R	-	yes
12.6 Simplified ILAS	-	yes
12.7 Liquid assets buffer	-	yes
12.8 Cross-border and intra-group management of liquidity		
12.9 Individual liquidity guidance and regulatory intervention points	-	yes
Annex 1 Mapping of credit assessments of ECAs to credit quality steps	-	yes