Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland
baselcommittee@bis.org

Brussels, 14 September, 2012
VH/LD/B2/12-149

Consultative Document *"Monitoring Indicators for Intraday Liquidity Management"*

Ladies, Gentlemen,

The European Association of Co-operative Banks (EACB) welcomes the opportunity to comment on the Basel Committee on Banking Supervision Consultative Document on "*Monitoring Indicators for Intraday Liquidity Management".*

Please find our remarks on the following pages.

We will remain at your disposal,

Yours sincerely,

Hervé Guider
General Manager

Volker Heegemann
Head of Legal Department

EACB Comments on the BCBS Consultation on the Monitoring Indicators for Intraday Liquidity Management

Brussels, September 14, 2012

The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 28 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 4.000 locally operating banks and 63.000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 176 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 50 million members and 750.000 employees and have a total average market share of about 20%.

For further details, please visit www.eurocoopbanks.coop

EACB welcomes the opportunity to comment on the BCBS principles for monitoring the intra-day liquidity. We acknowledge the importance of effectively managing the intraday liquidity risk both for the timely payment & settlement of obligations and for the smooth functioning of payment and settlement systems.

We note that there is no deadline for implementation of the rules. EACB supports a sufficiently long implementation period due to the high implementation effort required for introducing new indicators.

PROPORTIONALITY AND LIMITED AMOUNT OF DATA

The paper mentions that although the indicators are aimed at internationally active banks, they have been designed to be applicable to all banks. In this context it is particularly important to co-operative banks that the rules will not apply indiscriminately to all banks without taking into consideration the proportionality principle. Appropriate proportionality rules and a suitable differentiated approach should be provided for. Currently there is no such provision in the consultative paper. Appropriate exemptions in connection with liquidity systems of co-operative banks could be provided. This can be the case for indirect participants (local co-operative banks) where a formal arrangement has been put in place with their central institutions (which act as a correspondent bank) that substantially reduces their intraday liquidity risk.

We note that the amount of data that banks will be asked to provide is relatively large - banks have to report on a monthly basis data for each payment and settlement system, for every (material) currency, both at the level of individual banks and on a consolidated level, under normal conditions and for different stress scenarios. It is important that the national supervisors are able to use the data in an efficient way. It is not evident how some of the metrics will be used to analyze intraday liquidity risk (e.g. value-weighted average time of settlements) and whether they provide a valued added from an informational point of view. Furthermore, it is debatable whether information on 95% quantile would be technically validated (there is a lack of statistically validated data on payment distributions and time intervals) and whether it would allow any conclusions that can be constructive. Moreover, it is important to remember that the reporting will be burdensome for banks (as setting up reporting systems can be costly) and supervisors as well (as coping with the amount of incoming monthly data requires resources from them as well). It is thus essential to strike the right balance useful reporting and cost.

In this regard EACB underlines that the intraday liquidity risk is already mitigated by the liquidity risk management rules under the BCBS “Principles for Sound Liquidity Management and Supervision” published in 2008. The time horizons of the liquidity overviews required under these principles offer a true and fair view of the short-term liquidity trends as daily maturity brackets are selected for at least the first 30 days. The liquidity reserves/ buffer required under the Principles for Sound Liquidity Management exceed the intraday liquidity need several times over and they can cover the intraday liquidity needs.

In practice, intraday liquidity risks translate into payments of damages as well as punitive interest rates or fees charged on the grounds of delayed payments. These are monitored and controlled by operational risk management; a *de facto* failure to pay falls under the remit of credit risk management.

Furthermore, separate reports at the level of individual banks and at the level of the group are redundant. Bank groups featuring a central body for liquidity management (and the cooperative banking networks' specific liquidity system) should be granted the right to limit their reporting to a consolidated view of the entire group.

Direct Participants vs. Correspondent Banks

We appreciate the BCBS differentiation between direct participants to payment systems and correspondent banks. Banks which use correspondent banks for managing their currency liquidity might have difficulties to report some of the indicators such as timing of intraday payments and intraday credit lines. Because of this, differences between direct participant in currency clearing systems and banks which are indirect by using correspondent banks should rightly be considered in reporting requirements of intraday liquidity for currencies.

For banks which are direct participants in a payment and settlement system the required data (in euro) is already readily available in these payment and settlement systems. The data could be directly gathered by the central banks.

A more detailed illustration for indirect participants or for banks offering payment transactions as a service for other market participants, of the Basel Committee's expectation would be helpful. This might come in the form of an example similar to the one presented in Annex 1or publication of a reporting template which is already populated with data.

Effects of Applying the Rules

EACB agrees that in order to ensure the ability to carry out payments at any moment during the day, every bank should have an active management of intraday liquidity. To this end, the ratios proposed in the consultative document can support the internal control and management of intraday liquidity. However, this may depend on the respective bank's individual situation and it should be left to the banks'discretion which ratios or combinations of ratios they wish to monitor in their internal liquidity risk management.

In general, Basel Committee should take into consideration the behavioural changes that could arise as a consequence of applying the new rules. In this way it can estimate what is the effect of these metrics on the banks' practices to handle payments. Most likely, the requirement of calculating the "largest net cumulative outflow" on a daily basis will have a clear impact on banks' intraday payment behaviour. Banks will endeavour to keep this figure as low as possible. Hence, this provision would create incentives to hold back own payments as far as possible.

Moreover, if limits on the different metrics would be applied, this would undermine the stable and balanced intraday transactions and promote disequilibria at various points during the day. High volume deals would probably only be feasible if carried out in several tranches so that payments can be made at different hours of the day.

ADDITIONAL CLARIFICATION NEEDED

The template in its current form seems to be only for information purposes and it does not contain all relevant information for possible cost estimation. In addition, the implementation of the proposed monitoring process would entail considerable effort from a technical, financial and human resources perspective while sometimes it might not be feasible and have low added value. Below we noted some of the aspects that have an impact on the cost and value added of the monitoring regime proposed.

- There is no information about when the final template is planned to be released;
- The planned stress assumptions can lead to duplication or misunderstandings with the liquidity coverage ratio assumptions;
- An accurate representation of what stress factors must be applied to the intraday cash flows is missing;
- Internalised payments (i.e. internal payments that are settled across a bank's books) should be shown separately but it is not clear what the intraday liquidity risk of such "internalised payments" is. This extension of the regulatory scope would create wrong management incentives and would trigger results that would lack comparability.
- The template provides for the determination of cumulative intraday liquidity inflows and outflows "at any point in the day" and the highs and lows of liquidity within each hour of the working day. To determine this, it must be assumed that a real-time monitoring must be applied, and not only a monitoring for random times. It is worth noting that a real-time monitoring is hardly possible both from a technical and operational perspective. This type of monitoring would lead to significant amounts of data and would require significant resources and investments in IT operations, payments infrastructure, treasury, risk management;
- There is not sufficient differentiation between the different payments systems to which the bank belongs to. Many banks are direct participants in EUR payments via Target 2, in foreign currency, however, an indirect participant. For an indirect participant it is virtually impossible to collect data on the implementation of payments and payment volumes in real time. These banks only know the time of sending a payment order but not yet the time of execution by the designated correspondent bank. The suggested rules are therefore not appropriate for all banks' business models.
- Information on currencies where the payments are handled through a correspondent bank is hardly feasible to gather in practice. The exact execution times of incoming and outgoing payments are unknown for nostro accounts. Furthermore, the aspect of the time zones needs to be taken into account.

There are a few technical aspects which should be defined in more detail:

➢ ***Metrics:***

More details for fulfilling the requested reports are needed:

o "Payments sent / payments received": payments might be either bank transfers (meaning that money will be transferred from Bank A to Bank B) or collections (meaning that money will be transferred from Bank B to Bank A) resulting in different payment flows for the same transactions. We are assuming that payment flows are more relevant than transaction flows. Are only payments relevant for filling the template?

- o Payment systems: Is it required to use a final Real Time Gross Settlement System like TARGET 2? Are clearing systems which are doing their settlement across these systems are only “correspondence banking relationships” relevant? This issue is important as automatic executing systems (which are doing “batch” payments / executing to fixed times) might distort the hourly statistic as requested in the template: e.g. payments will be executed at 9 a.m, at 12a.m and at 5p.m, for the rest no payments might be observed
- o There should be a clarification that positive liquidity positions or negative positions will only have to be established for those points in time which also saw intraday payments (in correspondence to “any point during the day”). Alternatively, it should be possible to use at least hourly time buckets for cumulating the payments.
- o Clarifying the measurement of "largest five financial institutions" – will this result in a fixed set of counterparts or the counterparty will be changing according to daily business volume
- o Clarification of measurement unit (e.g. “EUR Mio.”) within the Excel template, at least for the major currencies and major systems
- o Clarification about currencies which need to be reported - it be in terms of materiality compared to total balance sheet, the “largest five” for example
- o More detailed information of the reporting scope is required. Should sectoral banks also be included?
- o The available own sources of liquidity (especially securities) should be broken down further on the basis of the time required for turning them into liquidity. For instance securities which are already deposited at the central bank can be converted into liquidity faster than securities which may be ECB eligible and available but which, for instance, are kept in a custody account abroad.
- o There should be a clarification of the “the start of a business day” for internationally active banks in cases where an aggregation through the payment system would be possible.
- o The term "time critical payment obligation" should be defined more precisely. Due to the fact that there will generally be a so-called cut-off-time for payments which will always have to be respected, generally speaking, all payments tend to be “time critical”.
- o In order to ensure that it will be construed in a consistent manner amongst banks themselves, also the term "correspondent bank“ should be defined in greater detail, specifically because central institutions in co-operative systems in many cases function as ‘correspondent bank’ for the operations of the local institutions.
- o It is ambiguous whether the average time of a bank’s daily payment settlements as the value-weighted average time of settlement is calculated taking into account inflows and outflows at the same time. In our view, this ratio makes no sense if the formula is supposed to include both liquidity flows. A simplification could be added if payments are aggregated to full hours (for instance all payments between 8.00 a.m. and 9.00 a.m. aggregated to 9.00 a.m. or all payments between 8.30 and 9.30 aggregated to 9.00). Another simplification could be to use a two hour interval (for the timing of intra-day payments as well as for the daily maximum liquidity requirement). It is unclear how the lowest intraday liquidity available shall be calculated. To our understanding, paragraph 21 explains that when calculating the available intraday liquidity banks will have to determine as well the lowest amount of available intraday liquidity during the day (lowest total liquidity). On the other hand,

the reporting template suggests a different calculation method: the lowest available intraday liquidity results from adding the lowest amount of the aforementioned intraday liquidity items (3a, 3b, 3d, and 3f). This calculation method might lead to a situation where the determined lowest available liquidity will be lower than the actual lowest intraday liquidity available calculated as suggested in article 21.

- Annex 2 should include for the calculation of available intraday liquidity all items referred to in paragraph 12.

➢ ***Identifying of stress scenarios***

Paragraphs 33 to 39 are general statements about the required stress scenarios. As the definition of that is similar, but not equal to "Basel 3" / LCR, more detailed explanation of the stress scenarios is required to avoid misunderstanding and unwanted interpretation of the scenarios.

In general, there is not enough consideration of the individual business models of the banks (e.g. an investment bank will have a complete different intraday liquidity management / risk management as a corporate or a retail bank). Therefore, a detailed explanation on how the information collected through the template will be interpreted would be highly appreciated. This should also take into consideration a distinction due to the different business models of banks.

➢ ***Reporting frequency***

Paragraph 58 states that a monthly data delivery is required. Given the fact that within the template also hourly indications are requested, it might be misinterpreted how often reporting has to be done.

In addition:

- Are the maximum values within the respective month requested?
- Is it required to send each month several templates, one for each day?