EUROPEAN ASSOCIATION OF CO-OPERATIVE BANKS
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EACB Comments

Commission draft Delegated Regulation amending Delegated Regulation (EU) 2015/61 of 10 October 2014 (LCR delegated act)

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General comments

The members of the EACB welcome the opportunity to comment on the Commission draft text for the amendment of the Delegated Regulation (EU) 2015/61 of 10 October 2014, i.e. the LCR delegated act.

We truly appreciate that this exercise is done in a transparent manner and that the industry has the opportunity to submit feedback via a fully-fledged consultation.

Overall we see that most of the adjustments are of a targeted nature and aim to address a number of elements that needed alignment with the international standards. However, some of the proposed amendments do not reflect such spirit and introduce questionable novelties while others require clarifications.

In addition we would also call for amending the EBA LCR template only once the new delegated act is in force, and no longer than six months after, to avoid overlaps that may lead to uncertainty and undue reporting burden.

Specific technical aspects

Art. 3(8) and the use of the concept of connected clients

In terms of general concepts, we have serious doubts regarding the introduction of a credit risk notion such as the one of "group of connected clients".

We do not believe that 'connected clients' concept, as being currently developed based on credit risk concepts, is relevant for liquidity risk management. This is particularly the case when considering that connected client counterparties, whose financial health may be intrinsically linked owing to economic relationship, may not show the same behaviour regarding their investments (deposits or short-term investments withdrawals). Liquidity needs reliance on its own specific framework.

We believe that the notion of 'connected clients' for the definition of retail deposits in the Corrigendum should be removed.

Furthermore, 'retail deposits' definition in Part VI of the ongoing review of CRR related to Liquidity has also been modified in the same vein in article 411(2). To ensure a consistency of definitions and concepts between regulations, we believe that in ongoing negotiation this this notion should be removed as well.

Finally, the application of group of connected clients to retail and SME deposits seems conceptually far fetching.

Article 11 - Level 2A assets

The current wording of Article 11(1)(e)(iii) of the Delegated Regulation (EU) n°2015/61 is confusing. Indeed, "*time to maturit*y" suggests that the residual maturity of the security should be less than 10 years, whereas "*at the time of issuance*" refers to the initial maturity.

We believe that this point should be clarified, and we propose to delete the reference to the initial maturity as follows:

> "1*. Level 2A assets shall only include assets falling under one or more of the following categories and meeting in each case the eligibility criteria laid down herein: […]*
> *(e) corporate debt securities which meet all of the following requirements:*

[…]
(iii) the maximum time to maturity of the securities ~~at the time of issuance~~ is 10 years;"

<u>Art. 15(4) role of the external auditors in CIU calculations</u>

External auditors already have to validate the calculations regarding the NAV of the funds in the context of the overall balance sheet audit. It is unclear in which other sense the external auditor would have to assess the correctness of the calculations of the management company and in particular in the context of the LCR.

This aspect should be further clarified.

We believe that no additional audit procedure with short and burdensome timelines should be added for the LCR which is by definition a short term ratio.

For the sake of clarity, we propose the following amendment:

"*The correctness of the calculations market value of shares by the depository institution or the CIU management company shall be confirmed by an external auditor.*"

<u>Art. 32 repos and reverse repos</u>

We welcome the amendments to Art. 32 which introduce a symmetric treatment for the cash legs of repos and reverse repos. This element had been left outstanding in the previous version of the LCR delegated act, this alignment is very much appreciated.

<u>Art. 13 STS (simple, transparent and standardised) securitisations as liquid assets</u>

We appreciate the introduction of STS securitisations as liquid assets. However, we notice that work is needed on the framework for eligibility criteria.

The proposed Delegated Regulation in fact incorporates the requirements for STS securitisations provided under the newly enacted securitisation regulation, which creates a framework defining Simple, Transparent and Standardised securitisations (STS). In such new STS regulation, criteria are established for STS securitisation. However, such regulation does not mention the need for an actual STS label to get eligibility under the LCR ratio.

In the proposed amendment regarding securitisation, existing LCR criteria which are similar to the STS are withdrawn, and instead securitisations have to be STS so that they can qualify as LCR level 2B assets. On the one hand, this direct incorporation by reference is positive, as it favours consistency across regulations (Solvency 2, LCR etc.). On the other hand, as a result of incorporation by reference, new criteria have been added that were not part of the LCR list of criteria until now while not providing any additional benefit for securitisations complying with such more demanding LCR requirements.

Furthermore, as the suggested list of criteria for LCR is broader, a number of transactions currently eligible to the LCR will not qualify any longer under the new regulation. This might have a negative effect on the market (secondary prices might be impacted – at least for the foreseeable future).

We suggest a more balanced approach, which would consist in:

- Including securitisations complying with STS requirements into level 2A assets;

- Maintaining the current parameters for level 2B securitisations (with some alignment with the STS criteria);
- Including a new asset class within securitisations, namely ABCP issued by programmes fully supported complying with European Money Market Funds requirements.

Several elements make the inclusion of ABCP programme issuances within eligible assets for the LCR very logical:

1) It is in line with the draft Commission Delegated Regulation that states pages 4 & 5 that "*the Commission will […] keep the [LCR regulation] up to date in light of market changes and will consider additional assets that may have become sufficiently liquid to merit inclusion in the liquidity buffer of a credit institution […].*"
2) It is also consistent and builds a holistic regulatory approach with the Money Market Fund Regulation (Regulation (EU) 2017/1131) which imposes to Money Market Fund to invest only in liquid assets, and includes ABCP programmes issuances within the set of liquid assets. It is well known now by market participants that fully supported ABCP programmes issuances are very close to short term covered bond. Like in covered bonds, investors of ABCP programmes have a dual recourse, and are secured firstly by liquidity lines from sponsoring banks which cover liquidity, credit and operational risks, and secondly by collaterals refinanced by ABCP programmes. These collaterals are securitisation positions funding real economy (predominantly, trade receivables, assets from automotive sector, consumer leases).
3) It is also in accordance with targets laid down in recital (10) of Commission LCR Delegated Regulation (EU) n°2015/61 of 10 October 2014 stating that "*a broader range of eligible sub categories of assets would increase diversification within the liquidity buffer and facilitate the financing of the real economy*". Indeed, inclusion of ABCP programmes within eligible subcategories of assets would increase diversification within the liquidity buffer and facilitate the financing of real economy, and would contribute to economic growth as it would send a positive signal to investors in relation to these assets.

   All these elements are in line with Capital Markets Union goals promoted by European Commission to facilitate the financing of real economy[1].

Finally, we consider that at least securitisations currently complying with LCR requirements should benefit from a grandfathering period, and continue to be LCR eligible without complying with new requirements during a transitory phase.

We propose the following amendment to Article 7, paragraph 3 of the draft LCR Delegated Regulation:

> "*3. The assets shall not have been issued by the credit institution itself, its parent undertaking, other than a public sector entity that is not a credit institution, its subsidiary or another subsidiary of its parent undertaking or by a securitisation special purpose entity with which the credit institution has close links.* ***For the purpose of this paragraph, ABCP programmes are not considered as***

[1] See also Moody's sector in depth report 'securitisation is a relevant source of funding for the European economy dated September 25, 2017 mentioning page 2: *'In 2016, the last partially supported European ABCP conduit was converted to full support, meaning that* *European ABCP investors benefit from a Covered Bond like dual recourse**. They are primarily exposed to the credit quality of the conduits' key counterparties (i.e. liquidity provider), with an additional claim over the securitised assets.*

securitisation special purpose entity with which the credit institution has close links or as a credit institution or subsidiary of credit institution;"

We ask for the deletion of Article 13, paragraph 1 of the draft Delegated Regulation:

~~"1. Exposures in the form of asset-backed securities referred to in Article 12(1)(a) shall qualify as level 2B securitisations where they satisfy the following conditions:~~

~~(a) they are permitted to use and are using the designation 'STS', or a designation that refers directly or indirectly to 'STS', in accordance with Regulation (EU) 2017/42 of the European Parliament and of the Council;~~*

~~(b) they meet the criteria laid down in paragraphs 2 to 13 of this Article."~~

Instead of deletion, we propose the following amendment to Article 13, paragraph 2, points (c), (d), (e), (f), (h), (i) and (j) of the LCR Delegated Regulation n°2015/61:

"(c) The title to the underlying exposures shall be acquired by the SSPE by means of a true sale or assignment or transfer with the same legal effect in a manner that is enforceable against the seller or any other third party. The transfer of the title to the SSPE shall not be subject to severe clawback provisions in the event of the seller's insolvency.

(d) For the purpose of paragraph (c), any of the following shall constitute severe clawback provisions:

> ***(i) provisions which allow the liquidator of the seller to invalidate the sale of the underlying exposures solely on the basis that it was concluded within a certain period before the declaration of the seller's insolvency;***
>
> ***(ii) provisions where the SSPE can only prevent the invalidation referred to in point (i) if it can prove that it was not aware of the insolvency of the seller at the time of sale.***
>
> ***For the purpose of paragraph (c), clawback provisions in national insolvency laws that allow the liquidator or a court to invalidate the sale of underlying exposures in the case of fraudulent transfers, unfair prejudice to creditors or transfers intended to improperly favour particular creditors over others shall not constitute severe clawback provisions.***
>
> ***Where the seller is not the original lender, the true sale or assignment or transfer with the same legal effect of the underlying exposures to that seller, whether that true sale or assignment or transfer with the same legal effect is direct or through one or more intermediate steps, shall meet the requirements set out in paragraphs (c) and (d).***

(e) The transaction documentation shall clearly specify the processes and responsibilities necessary to ensure that a default by or an insolvency of the servicer does not result in a termination of servicing, such as a contractual provision which enables the replacement of the servicer in such cases.

(f) The transaction documentation shall clearly specify provisions that ensure the replacement of derivative counterparties, liquidity providers

and the account bank in the case of their default, insolvency, and other specified events, where applicable.

[…]

(h) The exposures underlying the securitisation position shall not include any securitisation position.

(i) The underlying exposures shall not include transferable securities, as defined in point (44) of Article 4(1) of Directive 2014/65/EU, other than corporate bonds that are not listed on a trading venue.

(j) The underlying exposures shall be transferred to the SSPE after selection without undue delay and shall not include, at the time of selection, exposures in default within the meaning of Article 178(1) of Regulation (EU) No 575/2013 or exposures to a credit-impaired debtor or guarantor, who, to the best of the originator's or original lender's knowledge:

> ***(i) has been declared insolvent or had a court grant his creditors a final non-appealable right of enforcement or material damages as a result of a missed payment within three years prior to the date of origination or has undergone a debt- restructuring process with regard to his non-performing exposures within three years prior to the date of transfer or assignment of the underlying exposures to the SSPE, except if:***
>
> ***- a restructured underlying exposure has not presented new arrears since the date of the restructuring, which must have taken place at least one year prior to the date of transfer or assignment of the underlying exposures to the SSPE; and***
>
> ***- the information provided by the originator, sponsor and SSPE in accordance with points transparency requirements of Regulation (EU) No 2017/2402 explicitly sets out the proportion of restructured underlying exposures, the time and details of the restructuring as well as their performance since the date of the restructuring;***
>
> ***(ii) was, at the time of origination, where applicable, on a public credit registry of persons with adverse credit history or, where there is no such public credit registry, another credit registry that is available to the originator or original lender; or***
>
> ***(iii) has a credit assessment or a credit score indicating that the risk of contractually agreed payments not being made is significantly higher than for comparable exposures held by the originator which are not securitised."***

In Article 13, paragraph 2, we support the deletion of point (k).

In Article 13, paragraph 2, point (g) of the draft Delegated Regulation, we believe that the following amendment should be introduced:

"(g) the securitisation position is backed by a pool of underlying exposures and those underlying exposures either all belong to only one of the following subcategories or else they consist of a combination of residential loans referred to in point (i) and residential loans referred to in point

[…]

(vi) an ABCP issued by an ABCP programme which: (i) is fully supported by a regulated credit institution that covers all liquidity, credit and material dilution risks, as well as ongoing transaction costs and ongoing programme-wide costs related to the ABCP, if necessary to guarantee the investor the full payment of any amount under the ABCP; (ii) is not a re-securitisation and the exposures underlying the securitisation at the level of each ABCP transaction do not include any securitisation position; (iii) does not include a synthetic securitisation as defined in point (11) of Article 242 of Regulation (EU) No 575/2013. Requirements set out in paragraph 2, points (c) to (f) and (h) to (j) and in paragraph (3) to (6) apply securitisation positions underlying the ABCP programme;"

Next to the deletion of paragraphs 7 to 9 of Article 13 of the Delegated Regulation n°2015/61, we ask for the following amendments to paragraphs 3 to 6:

"(3) The repayment of the holders of the securitisation positions shall not have been structured to depend predominantly on the sale of assets securing the underlying exposures. This shall not prevent such assets from being subsequently rolled-over or refinanced.

The repayment of the holders of the securitisation positions whose underlying exposures are secured by assets the value of which is guaranteed or fully mitigated by a repurchase obligation by the seller of the assets securing the underlying exposures or by another third party shall not be considered to depend on the sale of assets securing those underlying exposures.

(4) (a) Where an enforcement or an acceleration notice has been delivered:

> ***(i) no amount of cash shall be trapped in the SSPE beyond what is necessary to ensure the operational functioning of the SSPE or the orderly repayment of investors in accordance with the contractual terms of the securitisation, unless exceptional circumstances require that an amount be trapped to be used, in the best interests of investors, for expenses in order to avoid the deterioration in the credit quality of the underlying exposures;***
>
> ***(ii) principal receipts from the underlying exposures shall be passed to investors via sequential amortisation of the securitisation positions, as determined by the seniority of the securitisation position;***
>
> ***(iii) repayment of the securitisation positions shall not be reversed with regard to their seniority; and***
>
> ***(iv) no provisions shall require automatic liquidation of the underlying exposures at market value.***

(b) Transactions which feature non-sequential priority of payments shall include triggers relating to the performance of the underlying exposures resulting in the priority of payments reverting to sequential payments in order of seniority. Such performance-related triggers shall include at least the deterioration in the credit quality of the underlying exposures below a predetermined threshold.

(c) The transaction documentation shall include appropriate early amortisation provisions or triggers for termination of the revolving period where the securitisation is a revolving securitisation, including at least the following:

> ***(i) a deterioration in the credit quality of the underlying exposures to or below a predetermined threshold;***
>
> ***(ii) the occurrence of an insolvency-related event with regard to the originator or the servicer;***
>
> ***(iii) the value of the underlying exposures held by the SSPE falls below a predetermined threshold (early amortisation event); and***
>
> ***(iv) a failure to generate sufficient new underlying exposures that meet the predetermined credit quality (trigger for termination of the revolving period).***

(5) The debtors shall, at the time of transfer of the exposures, have made at least one payment, except in the case of revolving securitisations backed by exposures payable in a single instalment or having a maturity of less than one year, including without limitation monthly payments on revolving credits.

(6) In the case of securitisations where the underlying exposures are residential loans, the pool of loans shall not include any loan that was marketed and underwritten on the premise that the loan applicant or, where applicable, intermediaries were made aware that the information provided might not be verified by the lender."

We also suggest the introduction of the following paragraph 13b:

"13b. Exposures in the form of asset-backed securities referred to in Article 12(1)(a) shall qualify as level 2A securitisations where they satisfy the following conditions:

> ***(a) they are permitted to use and are using the designation 'STS', or a designation that refers directly or indirectly to 'STS', in accordance with Regulation (EU) 2017/42 of the European Parliament and of the Council*;***
>
> ***(b) they meet the criteria laid down in paragraphs 2 to 13 of this Article."***

In Article 13, paragraph 14 the following amendment should be made:

"(14) The market value of level 2B securitisations shall be subject to the following minimum haircuts:

*(a) 25 % for securitisations backed by the subcategories of assets referred to in points (g)(i), (ii), ~~and~~ (iv) **and (vi)** of paragraph 2;*

(b) 35 % for securitisations backed by the subcategories of assets referred to in points (g)(iii) and (v) of paragraph 2."

Moreover, we recommend the introduction of a paragraph 14a in Article 13:

"(14a) The market value of level 2A securitisations shall be subject a 15% minimum haircut."

Art. 16 Deposits and other funding in cooperative networks and institutional protection schemes

We believe that the amendment introduced in Art. 16 clarifies appropriately what was previously cross referenced with Art. 27, i.e. that deposits considered as liquid by the local banks of the cooperative group/network cannot be considered as operational and thus stable by the central body and vice versa.

In this context, we draw attention to the fact that the EBA LCR template shall be amended on the basis of the revised wording of Art. 16(1). It must be borne in mind how the (liability-sided) liquidity reserve shall be disclosed in the future (e.g. among 'non-operational deposits').

Art. 17 Composition of the liquidity buffer by asset level

We welcome the introduction of the new paragraph 4. Nevertheless, there is no reason to restrict the waiver-option on Member States where systemic risks affecting the banking sector are materialising. Some of the sovereign and central bank programs for the middle asset class would also be responsible for negative LCR effects once coming to an end. Art. 17 (4) lit. b should be deleted.

Article 23

In our view, outflows on items listed in Article 23, other than Trade Finance, are already taken into account via Article 31 (notably with the introduction of Art. 31A(2) of the corrigendum) and for some items via the inflow reduction on monies due from non-financial customers (Art. 32(3)(a)):

- ✓ Outflows on undrawn loans and advances to wholesale counterparties (art.23(b)), and on mortgage loans that have been agreed but not yet drawn down; (23(c)).
- ✓ credit cards (art.23(d)) and overdrafts (art.23(e)); planned derivatives payables (art 23(g))

Regarding uncommitted funding facilities (Art.23(a)), we believe that no outflow should be taken for the LCR calculation. Indeed, they represent revocable commitments that the institution can (by definition) terminate at anytime. This is confirmed by the fact that those elements are neither recorded in accountancy, nor taken into account for the calculation of Risk weighted assets in Solvency.

Article 28(7)

Article 30(5) provides that "*If the credit institution holds a short position (1) that is covered by an unsecured security borrowing, the credit institution shall add an additional outflow corresponding to 100% of the market value of the securities or other assets sold short unless the terms upon which the credit institution has borrowed them require their return only after 30 calendar days (2)*".

- ✓ Unlike the current LCR delegated act, where it was clearly stated that short positions concerned by this paragraph were to be deliverd within 30 days, the delivery date of these operations is not specified in the corrigendum, leading us to believe that this article applies to all the short positions covered by an unsecured

securities borrowing, whatever their delivery dates are.

- ✓ Article 28(7) states that unsecured securities borrowings maturing within 30 days shall give rise to an outflow of 100%.

The application of these two articles could lead to a double-counting of outflows when a short position is covered by an unsecured securities borrowing maturing within 30 days, whereas it is not the case in the Basel Framework, where no double counting is possible:

BCBS 328.147: "*In the case of a bank's short positions, if the short position is being covered by an unsecured security borrowing, the bank should assume the unsecured security borrowing of collateral from financial market participants would run-off in full, leading to a 100% outflow of either cash* ***or*** *HQLA to secure the borrowing, or cash to close out the short position by buying back the security.*"

For the sake of clarity, as recital (7) precises that the treatment of short positions was clarified to align it to international standards, and in accordance with the principle of not double-counting liquidity inflows or outflows, we propose the following amendment to Article 28(7):

"*Assets borrowed on an unsecured basis and maturing within 30 calendar days shall be assumed to run off in full, leading to a 100% outflow of liquid assets, unless the credit institution owns the assets borrowed and the assets borrowed do not form part of the credit institution's liquidity buffer.* ***This shall not lead to any double counting of outflows when the unsecured security borrowing covers a short position;***"

Art. 4 The liquidity coverage ratio

The new paragraph (5)(b) "for items denominated in the reporting currency where the aggregate amount of liabilities denominated in currencies other than the reporting currency equals or exceeds 5% of the credit institution's total liabilities, excluding regulatory capital and off-balance sheet items, in the reporting currency." provides in certain cases (e.g. for many institutions supervised by NCAs) for a new but unnecessary reporting burden with no use for supervisory purposes.