Guernsey Financial Services Commission

BASEL III: LIQUIDITY

FEEDBACK ON THE CONSULTATION PAPER ISSUED BY THE GUERNSEY FINANCIAL SERVICES COMMISSION

March 2017

This feedback paper reports on input received by the Guernsey Financial Services Commission on the Consultation Paper issued in November 2016 and consequent related changes.

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1: Executive Summary

1.1 Background

This paper details and responds to the feedback received on the Consultation Paper ("CP").

The CP outlined proposals to amend the minimum regulatory liquidity requirements that apply to licensed deposit takers that are incorporated in Guernsey.

The substantive changes proposed were as follows:

- Establishment of a new minimum regulatory liquidity requirement for Guernsey incorporated banks consistent with the Basel Committee's Basel III Liquidity Coverage Ratio standard;
- Establishment of a new regulatory liquidity reporting requirement for Guernsey incorporated banks consistent with the Basel Committee's Basel III Net Stable Funding Ratio standard; and
- The transition of the current maturity mis-match minimum liquidity standard to a regulatory reporting requirement for all banks.

1.2 Feedback received

The CP was issued publicly. Responses to the CP were received from six Guernsey licensed banks.

The Commission is grateful to the respondents for taking the time to consider and comment on the proposals. Fuller consideration of these comments is in section 2.

1.3 Proposals

As a result of the predominantly positive feedback received the Commission has made no material revisions to the proposals contained in the CP. However some minor changes were made and these are reflected in the revised versions of reporting guidance and reporting forms provided to banks and to be published on the Commission's website.

1.4 Next steps

The revised regime will come into effect on 31 July 2017.

2: Summary of Feedback and Commission Response

2.1 Structure of this section

Very few issues were identified with the majority of respondents indicating their agreement and confirming understanding of the proposals. Where an issue has been raised a summary of the responses received and the Commission's responses to the matters raised are set out below.

2.2 Liquidity Coverage Ratio ("LCR")

One bank sought clarification of the definition of Personal Investment Company ("PIC") (which includes trusts) and the underlying eligibility criteria, under Appendix 3 of the proposed Guidance to completing the LCR module of Form LCR.

Another bank questioned whether there would be a requirement to submit the LCR on an individual currency basis.

Commission response

A revision has been made to Appendix 3 in the final policy (both LCR and LMR guidance) to enhance clarity. The proposed definition of PIC remains unchanged but the eligibility criteria has been be simplified. It was previously proposed that in order to qualify for the 40% outflow assumption that a PIC would be required to meet the following criteria:

- Deposits must either (1) be held on a designated account (not pooled) and not be managed through a brokerage arrangement or (2) be placed by the PIC itself;
- The adjustment should only be applied to deposits where the choice of the bank is not actively managed in order to achieve an investment return. Banks will be expected to assess against criteria they establish and document in their LMPs. Deposits representing long-term investments, which must include all deposits placed with an original maturity exceeding three months, may not be adjusted; and
- Where the deposit is held on a designated account, the deposit mandate must either (1) not require the deposits to be moved in the event of a downgrade below a certain level or (2) in the case that it does require this, the bank must be more than three notches above that level.

It was noted that the proposed additional criteria introduce a degree of complexity and subjectivity in interpretation which could lead to inconsistent application and that these criteria are not a feature of the European LCR regime for the treatment of PIC deposits (the source of the PIC definition used), and therefore would present a higher standard in comparison. The decision was made therefore to apply a simpler approach. These criteria have been removed from Appendix 3 in the final policy. For the avoidance of doubt, this change means that all PIC deposits will be eligible for a 40% outflow.

There is no requirement to submit the LCR by significant currency. Banks should address material exposure to foreign currency as part of their internal liquidity management policy.

2.3 Liquidity Mismatch Ratio ("LMR")

One bank sought to confirm whether the LMR approach could be used by banks that currently place no reliance on group bank inflows but might do so in the future.

One bank stated that it would be preferable to allow up-streaming to parent companies as HQLA, regardless of whether these are part of a formal liquidity group.

Commission response

Where an existing bank plans to change its business model to one of significant up-streaming to its parent group an application to use the LMR may be made (along with any associated application for an appropriate up-streaming limit under the Commission's Guidance Note on Up Streaming).

The LMR permits a greater reliance on qualifying group inflows than under the stricter definition of the LCR. The definition of "qualifying group inflows" includes the criterion that the counterparty and the local bank are part of a group that is subject to the LCR on a consolidated basis. This criterion provides assurance to the Commission, as a host supervisor, that the group, the source of substantial liquidity to the local bank, is subject to appropriate liquidity standards on a consolidated basis. The Commission is not minded to revise this criterion.

2.4 Alignment with European Union rules

One bank indicated a preference for closer alignment with the liquidity requirements under the relevant EU Delegated Act.

Commission response

While the Commission recognises that alignment with EU liquidity reporting rules may reduce the reporting burden for certain banks which are subsidiaries of EU domiciled groups, there are other important considerations which must be taken into account. The liquidity framework developed for Guernsey seeks to meet the international standards set by the Basel Committee (the jurisdiction hosts banks with parents both in and outside of the EU) while at the **same** time recognising the particular business models adopted locally and adapting the framework appropriately. Simple adoption of the EU Delegated Act would not permit necessary adaptation e.g. use of the LMR approach.

2.5 Timing

One bank sought an implementation date of six months following publication of the final rules to provide sufficient time to implement with appropriate rigour.

Commission response

To provide sufficient time to prepare for the change to the liquidity regime the implementation date will be set as 31 July 2017.

3: Implementation Timeline

The revised regime will come into effect on 31 July 2017. Banks incorporated in Guernsey will therefore be required to submit a first return under the new framework for information as at 31 July 2017 by the deadline of 28 August 2017 via the online submissions portal.

It should also be noted that for all banks the Quarter 3 2017 BSL/2 reporting should be made using the applicable revised BSL/2 reporting form. The inputs to this form remain unchanged but references to the replaced minimum regulatory liquidity requirements (i.e. behavioural adjustment in the case of subsidiary banks and the -20% mismatch threshold in the case of branches) have been removed.