



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Consultation Paper | CP13/17

Pillar 2 liquidity

July 2017



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Responses are requested by Friday 13 October 2017.

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1 Overview

1.1 This Consultation Paper (CP) sets out the Prudential Regulation Authority's (PRA's) proposals on a cashflow mismatch risk (CFMR) framework and other PRA methodologies for assessing firms' liquidity risk, under the Pillar 2 liquidity ('Pillar 2') framework.

1.2 This CP also proposes updates to Supervisory Statement (SS) 24/15¹ and SS34/15,² draft reporting rule changes, and a draft reporting template and instructions relating to CFMR.

1.3 This CP is relevant to UK banks, building societies and PRA-designated investment firms, referred to collectively as 'firms' in this CP.

1.4 The Pillar 2 framework is intended to complement the Pillar 1 regime by considering liquidity risks not captured, or not fully captured, under Pillar 1.³ Assessments under the Pillar 2 framework form part of the PRA's Liquidity Supervisory Review and Evaluation Process (L-SREP). In designing a Pillar 2 framework to assess and mitigate significant sources of liquidity risk, the PRA is seeking to ensure that firms have adequate liquidity, which contributes to the PRA's objective of promoting the safety and soundness of firms.

1.5 In CP21/16, the PRA outlined the objectives of the Pillar 2 framework, its scope, and planned future work. It proposed a Statement of Policy (SoP) on its approach to three Pillar 2 risks: intraday liquidity, debt buyback, and non-margined derivatives. It also made proposals on the level of application of Pillar 2 and the PRA's expectations relating to disclosure of Pillar 2.⁴ This CP builds on those proposals.

1.6 The draft SoP (Appendix 1) combines the proposals from this CP with those consulted on in CP21/16. Consequently, the PRA has renumbered the chapters in the draft SoP.

1.7 Additionally, this CP:

- (a) seeks early views on aspects of the calibration of overall liquidity requirements which will be consulted on in a third CP; and
- (b) outlines how feedback on CP21/16 was taken into account.⁵

Transitioning to the new regime

Timing of implementation

1.8 The entry into force of the proposed survival guidance under the granular Liquidity Coverage Requirement (LCR) stress will be linked to the implementation of the new PRA110 report proposed for 1 January 2019. This guidance can be found in paragraph 3.12 in the draft SS24/15 at Appendix 2.

1.9 The implementation of the new Pillar 2 methodologies is envisaged to commence in early 2018. The methodologies will be applied to each firm at the time of the next requirements setting process for that firm.

1 'The PRA's approach to supervising liquidity and funding risks – SS24/15 UPDATE', December 2016: www.bankofengland.co.uk/prapublications/ss/2016/ss2415update.aspx.

2 'Guidelines for completing regulatory reports – SS34/15 UPDATE', July 2017: www.bankofengland.co.uk/prapublications/ss/2017/ss3415update4.aspx.

3 Pillar 1 liquidity and funding requirements in force in the United Kingdom are limited to Commission Delegated Regulation (EU) 2015/61 of 10 October 2014 with regard to Liquidity Coverage Requirement (LCR) for Credit Institutions. It is still to be decided how and when a version of the Net Stable Funding Ratio (NSFR) will be implemented in the European Union as a Pillar 1 standard.

4 May 2016: www.bankofengland.co.uk/prapublications/cp/2016/cp2116.aspx.

5 The PRA published a statement of feedback received on CP21/16. October 2016: www.bankofengland.co.uk/pradocuments/publications/reports/prastatement181016.pdf.

1.10 However, the PRA recognises the importance of overall calibration of the regime. In order to analyse its Pillar 2 proposals fully, the PRA will set out proposals on calibration and their impact on the cost benefit analysis in a third CP in early 2018. The feedback requested in this CP on overall calibration will help to develop these proposals. It is not envisaged that the individual methodologies consulted on in the draft SoP will change as a result of the PRA's proposals on calibration.

1.11 The previous UK liquidity regime applied liquidity requirements at a percentage of the amount of risk quantified in the PRA's generic stress scenario: this was referred to as the glide path factor. The glide path factor was carried over from the previous UK liquidity regime into the new Pillar 2 regime. While the PRA considers overall calibration, it is not proposing to change the 'glide path factor' applied to existing Pillar 2 guidance. Therefore, the PRA expects that the revised methodologies will not lead to a material change in firms' liquidity held for Pillar 2 purposes.

Transition path

1.12 Once the PRA has created its proposals on overall calibration, it will determine if there is a need for a transition path. The exact shape and timing of any transition path will also be consulted on in the third CP.

CP Structure

1.13 This CP has the following structure:

- Chapter 2 outlines the proposals on which the PRA is seeking feedback;
- Chapter 3 details the cash flow mismatch reporting requirements;
- Chapter 4 details the PRA's statutory obligations;
- Chapter 5 details the PRA's updated thinking on its approach to overall calibration; and
- Chapter 6 details feedback on CP21/16 and resulting policy updates.

Responses and next steps

1.14 This consultation closes on Friday 13 October 2017. The PRA invites feedback on the proposals set out in this consultation. Please send any comments or enquiries to CP13_17@bankofengland.co.uk.

2 Proposals

Cashflow mismatch risk

2.1 The PRA is proposing to create a CFMR framework within the broader Pillar 2 framework to ensure an effective monitoring of a firm's liquidity risk profile in stress. Through the CFMR framework, the PRA intends to:

- (a) assess whether a firm has sufficient cash from monetisation of liquid assets and other inflows to cover outflows on a daily basis, under a defined stress scenario; and
- (b) monitor, with daily granularity, liquidity mismatches during longer lasting and more severe stress events.

2.2 The CFMR framework is covered by the proposals detailed in paragraph 2.5(a) to (d).

Other PRA methodologies for setting Pillar 2 guidance

2.3 There are significant sources of liquidity risk that are not captured, or not fully captured, in Pillar 1. Through setting out its methodologies for assessing these liquidity risks, the PRA is seeking to provide firms with transparency as to how supervisors will assess and mitigate liquidity risks under the Pillar 2 framework.

2.4 The PRA methodologies are covered by the proposals detailed in paragraph 2.5(e) to (i).

Proposals

2.5 The PRA seeks feedback on the following. The PRA proposes:

- (a) to assess CFMR on both a consolidated currency and single currency basis: see SoP paragraph 3.7 (Appendix 1);
- (b) that firms should survive throughout the granular LCR stress scenario on a consolidated currency basis: see SS24/15 paragraph 3.12 (Appendix 2);
- (c) to introduce a new liquidity reporting template (PRA110) to monitor CFMR: see Appendix 3;
- (d) to collect the new liquidity reporting template on a weekly basis with a one-day remittance period for large firms, and a monthly basis with a fifteen day remittance period for small firms: see paragraph 3.8 below;
- (e) to assess prime brokerage and matched book risks based on the LCR rates for secured transactions and supervisory judgement: see SoP paragraph 4.15;
- (f) to assess margined derivatives liquidity risks considering the firm's historical initial margin posted and received, with a stress uplift applied: see SoP paragraph 5.25;
- (g) to assess securities financing margin liquidity risks based on the firm's historical margin posted, with a stress uplift applied: see SoP paragraph 5.31;
- (h) to assess intragroup liquidity risk on a case-by-case basis, taking into account intragroup interconnectedness: see SoP paragraph 5.34; and
- (i) to assess liquidity systems and controls risks based on supervisory judgement of quantitative and qualitative issues: see SoP paragraph 5.37.

3 Cashflow mismatch risk reporting requirements and liquidity guidance

3.1 In CP21/16 the PRA anticipated that additional reporting requirements relating to CFMR would be required.¹

3.2 The monitoring of CFMR, as set out in the draft SoP, requires access to timely data on future daily profiles of inflows, outflows, and liquid assets, over different time horizons. In this CP the PRA sets out proposals to collect such data by introducing a new liquidity reporting template that is aligned to the LCR.

3.3 While recognising that this will require firms to transition to an updated reporting system, the PRA believes that firms themselves are already monitoring their day-by-day profile of liquid assets, inflows and outflows. Firms are currently reporting daily contractual cash flows through the FSA047 (based on the United Kingdom's previous Individual Liquidity Adequacy Standards (ILAS) liquidity regime's definition of liquid assets and cash flows).

3.4 The new liquidity reporting template, which will be named PRA110, will build on the EBA ML reporting template.² Appendix 4 sets out draft rules to introduce the collection of the PRA110. Appendix 3 contains the proposed PRA110 reporting template and associated reporting instructions. Appendix 5 sets out the proposed changes to SS34/14 to include PRA110.

3.5 PRA110 will:

(a) build on the EBA ML with additional columns to:

- i. distinguish claims and obligations without a contractual end date from overnight stocks;
- ii. provide daily buckets from day 8 to day 92.³ The PRA is of the view that a 90-day horizon is essential for properly monitoring firms' liquidity risks; and
- iii. let firms indicate the LCR weight associated with each PRA110 row. This weight will:
 - a. where the PRA110 row spans multiple rows from the LCR template: reflect the average of the relevant LCR weights based on the composition of data items combined in to the PRA110 row; or
 - b. where the PRA110 row is identical to a single row from the LCR template: mirror the LCR weight.

(b) build on the EBA ML with additional rows to enable the PRA to:

- i. implement the granular LCR stress and other CFMR stress scenarios and tools (as set out in the draft SoP);
- ii. implement the monetisation framework (as set out in the draft SoP);

1 The PRA also anticipated that additional reporting requirements relating to the monitoring of the proportion of high-quality liquid assets (HQLA) that firms hold at amortised cost would be required. The PRA is not making proposals on this at this time.

2 www.eba.europa.eu/regulation-and-policy/supervisory-reporting/implementing-technical-standards-on-supervisory-reporting.

3 Daily buckets extend to day 92 to accommodate months with 31 calendar days.

- iii. fill in material data gaps in the EBA ML compared to the FSA047 and FSA048 reports; and
 - iv. collect a limited amount of additional data which is not reported in the FSA047, FSA048, LCR or ML reports.
- (c) be reported on a consolidated currency and significant currency basis, as defined in CRR Article 415(2), to enable the PRA to monitor CFMR for significant currencies;¹ and
- (d) be reported on consolidated, sub-consolidated (where applicable), and solo or liquidity sub-group levels.

3.6 The PRA has balanced the accurate calculation of the granular LCR stress in its CFMR framework against the reporting burden placed on firms, when deciding which additional rows and columns are needed.

3.7 Appendix 3 contains a colour coded PRA110 template. This is included to help firms navigate the new template in relation to the changes noted in paragraph 3.5.

3.8 Large firms should report the PRA110 on a weekly basis with a one-day remittance period. To ensure the proposals are proportionate, smaller firms should report the PRA110 on a monthly basis with a fifteen-day remittance period. Firms should stand ready to increase reporting frequencies to daily for large firms and weekly for small firms, with a one-day remittance period. This is consistent with the current reporting frequencies of the FSA047 and FSA048 returns.

3.9 In defining a large firm for the purpose of reporting requirements the PRA will use the threshold that a firm has total assets of €30 billion or above, calculated in accordance with Council Directive 86/635/EEC. This is the key criteria used by the EBA to define large firms for reporting of the Additional Liquidity Monitoring Metrics which include the EBA ML.

3.10 The PRA110 is due to be implemented on 1 January 2019. The intended technical format for data exchange will be XBRL (eXtensible Business Reporting Language) with an associated XBRL taxonomy based on a DPM (Data Point Model). This will be an extension of the UK Banking Taxonomy (currently version 2.0.0). There will be a separate consultation in due course on technical aspects of the PRA110 template.

3.11 The proposed rule instrument in Appendix 4 makes proposals on the scope of firms required to report, the reporting frequency and remittance period of the PRA110.

Terminating the FSA047 and FSA048 returns

3.12 In June 2016 the PRA communicated its intention to maintain the FSA047 and FSA048 returns and to review this position in due course.² The PRA has reviewed this decision in light of the new proposals to introduce the PRA110.

3.13 The PRA proposes to terminate the reporting requirement of the FSA047 and FSA048 returns at the same time that the PRA110 is implemented. This will apply to UK banks, building societies and PRA-designated investment firms. The PRA intends to have a period of overlap between the EBA ML, which is due to be implemented in March 2018, and FSA047 and FSA048 returns. The PRA considers that there is a strong prudential case for maintaining the FSA047 and FSA048 returns until the implementation of the PRA110, as the data will be needed to help ensure the PRA has adequate sight of liquidity and funding positions during

1 CRR Article 415(2) requires firms to report on a single currency basis, any currency which exceeds 5% of aggregate liabilities.
 2 CRD firms – Reporting Requirements, June 2016: www.bankofengland.co.uk/pr/Pages/regulatorydata/formscrdfirms.aspx.

the transition to the PRA110. In case of any delay in the implementation of the PRA110, the PRA will delay the termination of the FSA047 and FSA048 returns.

3.14 The PRA intends to run a testing phase on a voluntary basis with a subset of firms. These firms will report PRA110 at the same time as they report FSA047 and FSA048 ahead of the implementation of PRA110 on 1 January 2019. This would enable the PRA to deal with any potential reporting issues ahead of the formal implementation of PRA110 and termination of the FSA047 and FSA048 returns.

Liquidity guidance

3.15 The entry into force of the proposed 30-day survival guidance under the granular LCR stress will be linked to the implementation of the PRA110 report proposed for 1 January 2019. This guidance can be found in paragraph 3.12 in the draft SS24/15 (see Appendix 2).

3.16 The PRA welcomes feedback on the proportionality aspects of the proposed approach to CFMR reporting requirements.

4 The PRA's statutory obligations

4.1 Before making any rules, the Financial Services and Markets Act 2000 (FSMA)¹ requires the PRA to publish a draft of the proposed rules accompanied by:

- (i) a cost-benefit analysis;
- (ii) a statement as to whether the impact of the proposed rules will be significantly different for mutuals than for other persons;²
- (iii) an explanation of the PRA's reasons for believing that making the proposed rules is compatible with the PRA's duty to act in a way that advances its general objective,³ and secondary competition objective;⁴ and
- (iv) an explanation of the PRA's reasons for believing that making the proposed rules are compatible with its duty to have regard to the regulatory principles.⁵

4.2 The PRA is also required by the Equalities Act 2010⁶ to have due regard to the need to eliminate discrimination and to promote equality of opportunity in carrying out its policies, services and functions.

4.3 The PRA should also have regard to aspects of the government's economic policy as recommended by HM Treasury.

Cost benefit analysis

4.4 The proposals included in this consultation paper fall into two areas: (i) a set of methodologies for assessing Pillar 2 liquidity risks on a consistent basis; and (ii) reporting requirements for CFMR. These are discussed in more detail below. The cost benefit analysis below considers the impact from these proposals that are envisaged to commence in early-2018. Any costs and benefits associated with future changes to the overall calibration will be assessed in the third CP. The cost benefit analysis takes into account the proportionate application of Pillar 2 methodologies and how this facilitates effective competition.

A set of methodologies for assessing liquidity risks not captured by LCR

4.5 PRA supervisors currently apply methodologies similar to those in the draft SoP in setting liquidity guidance on a firm-by-firm basis, through the use of add-ons to the liquid asset buffer. Therefore, the PRA expects that the revised methodologies will not lead to a material change in firms' liquidity held for Pillar 2 purposes. As a result, the PRA does not expect the use of the revised methodologies to change the costs and benefits compared to the existing liquidity framework.

4.6 By presenting its proposed methodologies for consultation, the PRA is seeking to operate in an open and transparent manner. The revised methodologies will ensure a consistent application of Pillar 2 guidance and will allow firms to understand how the PRA has formed this Pillar 2 guidance. This increase in transparency is a benefit of the revised methodologies.

1 Section 138J of FSMA.

2 Section 138K of FSMA.

3 Section 2B of FSMA.

4 Section 2H(1) of FSMA.

5 Sections 2H(2) and 3B of FSMA.

6 Section 149.

Reporting requirements for monitoring cashflow mismatch risk

4.7 In the interest of minimising burdens on firms, the new liquidity reporting template will build on the European Banking Authority (EBA) Maturity Ladder (ML) reporting template, and consolidate existing PRA reports where there is overlap in the data. In particular, firms are currently required to provide cashflow mismatch data as part of the regulatory reports FSA047 and FSA048. For this reason, there are immaterial incremental ongoing costs for firms to provide the cashflow mismatch data above and beyond that experienced to provide the FSA047 and FSA048 or CRR regulatory reports.

Transitional costs from reporting requirements for cashflow mismatch risk

4.8 The proposals will require firms to transition to an updated reporting system and to provide additional breakdowns. The PRA estimates that the total costs will be £41 million.¹ The PRA asks firms to provide feedback to this consultation with their assessment of these costs.

Proportionate application of Pillar 2 methodologies

4.9 The draft SoP is designed to ensure a proportionate approach to setting Pillar 2 add-ons. This approach considers: each firm's business model; objective judgements about how the firm approaches its liquidity risk management; the materiality of the risk compared to Pillar 1 risks; and the size of the burden, particularly on smaller firms. Through this approach no firm or group of firms should face a disproportionate cost imposed on it relative to other firms posing similar or greater liquidity risk.

The PRA's objectives

4.10 The PRA has a statutory objective to promote the safety and soundness of banks, building societies, credit unions, insurers and PRA-designated investment firms. The proposals in this CP are intended to further that objective by ensuring that the PRA has an appropriate regime for assessing and mitigating firms' liquidity risk and ensuring that firms have adequate liquidity. Where appropriate, the framework also enables the PRA to mitigate liquidity risks in ways other than firms holding liquid assets, for example by requiring firms to limit the liquidity risks they are running. In both cases, these actions contribute to the PRA's objective of promoting the safety and soundness of firms.

4.11 When discharging its general function in a way that advances its primary objectives, the PRA has, as a secondary objective, a duty to facilitate effective competition in the markets for services provided by PRA-authorized persons. The Pillar 2 framework provides methodologies for assessing and mitigating risks in a consistent manner across all firms. This contributes to the PRA's secondary objective. The methodologies enhance effective competition by ensuring that firms' liquidity risk is accurately assessed when calculating the PRA's Individual Liquidity Guidance (ILG), thereby preventing firms with greater liquidity risk from gaining an undue competitive advantage.

Regulatory principles

4.12 In developing the proposals in this CP, the PRA has had regard to the regulatory principles.² One principle is of particular relevance. The PRA, when developing the proposals outlined in the CP, has taken care to ensure that a burden or restriction which is imposed on a person, or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction. Paragraph 1.6 of the SoP details some of the ways in which the PRA will be proportionate under the Pillar 2 framework.

1 CP27/14 'CRD IV: Liquidity', November 2014 discussed the methodology for the firm-by-firm cost estimation of regulatory reporting. It estimated the one-off and ongoing costs for the introduction of the LCR reporting to be £73.2 million. Available at: www.bankofengland.co.uk/pr/Pages/publications/cp/2014/cp2714.aspx.

2 See section 3B FSMA.

HM Treasury recommendation letter

4.13 In March 2017, HM Treasury made recommendations to the Prudential Regulation Committee (PRC) about aspects of the government's economic policy to which the PRC should have regard when considering how to advance the objectives of the PRA and apply the regulatory principles set out in FSMA.¹ The PRA has considered the implications of the proposals in this CP for each of these aspects and considers that the following aspects of economic policy are relevant.

Competitiveness

4.14 The Government wishes to ensure that the United Kingdom remains an attractive domicile for internationally active financial institutions, and that London retains its position as the leading international financial centre. The Government considers that achieving this aim in a manner that is consistent with robust institutions and a resilient system will support its aims for sustainable economic growth.

4.15 The PRA considers that the proposals contained in this CP do not put at risk this economic policy aim. This is because the proposals aim at maintaining or enhancing the quality of supervision applied to the firms in scope.

Better outcome for consumers

4.16 The Government wants to see financial services work in the best interests of consumers and businesses they serve. This is supported by improved competition in financial services and the securing of an appropriate degree of protection for consumers.

4.17 The PRA considers that the proposals contained in this CP do not put at risk this economic policy aim. The proposed methodologies will be applied with supervisory discretion, taking into account business models and the materiality of Pillar 2 risks. The supervisor will also consider whether any Pillar 2 measures would have a disproportionate impact on a particular type of firm, including whether it results in a relatively bigger burden on smaller firms.

Impact on mutuals

4.18 In the PRA's opinion, the impact on mutuals from the proposed methodologies and reporting requirements is expected to be no different from the impact on other firms. This is also because the methodologies will be applied by supervisors in a way that is proportionate to each firm's business model and the risk that it poses to the PRA's safety and soundness objectives.

Equality and diversity

4.19 The PRA has performed an assessment of the policy proposals and does not consider that the proposals give rise to equality and diversity implications.

¹ Information about the Prudential Regulation Committee and the recommendations from HM Treasury are available on the Bank's website at www.bankofengland.co.uk/about/Pages/people/prapeople.aspx.

5 The PRA's approach to overall calibration

Calibrating overall liquidity requirements

5.1 In CP21/16, the PRA outlined its intention to make an assessment of the most appropriate calibration of the liquidity regime overall. In setting overall liquidity requirements it will be necessary to undertake an assessment of the economic impact of the proposals as part of a cost benefit exercise.

5.2 The PRA will consult on overall calibration in a third CP. In the meantime, the PRA will implement its new individual risk methodologies at the current glide path factor. The PRA may propose to adjust this once it has formed a view of the appropriate calibration of the Pillar 2 regime in the third CP.

Areas for the PRA to consider

5.3 The PRA welcomes respondents' views on overall calibration.

5.4 By way of reminder, below is an update on the areas the PRA stated it would consider in CP21/16:

- (a) the likelihood of each risk crystallising. This is integrated into the Pillar 2 framework as supervisors have the flexibility not to set requirements for risks they think are very unlikely to crystallise for a given firm;
- (b) the likely correlation between each liquidity risk identified. The PRA has considered correlation when designing its individual risk methodologies and generally has found that liquidity risks are strongly correlated, irrespective of whether they are captured in the Pillar 1 or Pillar 2 framework. This is a broad topic and the PRA is continuing to consider this issue; and
- (c) costs imposed on firms from changing the liquid asset eligibility rules for Pillar 2. At present, the PRA requires firms to meet interim Pillar 2 requirements with assets that meet the eligibility criteria detailed in the LCR. Any change to this would have an impact on the overall cost of the regime and would therefore be included in the assessment of the impact of the new regime. The PRA intends to consider this jointly with its final calibration proposal in a third CP.

5.5 In addition to work outlined in paragraph 5.4, the PRA is also analysing the macroeconomic effects of the aggregate liquidity requirements from different calibrations of its regime. This analysis broadly follows the framework set out in the Bank's Financial Stability Paper No. 35.¹ This considered aggregate capital requirements by assessing the benefits of higher capital from a reduced likelihood and cost of financial crises against the potential costs. The potential costs are mainly related to the possibility that higher bank capital requirements might lead to higher bank lending rates which dampen investment activity and, in turn, potential output.

5.6 The PRA intends to analyse further overall calibration before making final proposals in a third CP. This will take into account the macroeconomic exercise referred to in paragraph 5.5.

5.7 The PRA welcomes feedback on any of the areas detailed in paragraph 5.4. Firms will have an additional opportunity to provide feedback after the PRA makes overall calibration proposals in the third CP.

1 'Measuring the macroeconomic costs and benefits of higher UK bank capital requirements', December 2015: www.bankofengland.co.uk/financialstability/Pages/fpc/fspapers/fs_paper35.aspx.

6 CP21/16 feedback and policy updates

Feedback from CP21/16

6.1 In October 2016 the PRA published a statement on feedback received during the consultation period for CP21/16 'Pillar 2 liquidity'.¹ The feedback received led to a number of methodological changes and clarifications. One example of a methodological update is the stress uplift applied to intraday liquidity assessments. The stress uplift reference point has been revised downwards to reflect concerns among respondents to CP21/16 that there is a potential double counting of liquidity risks between the methodologies for assessing intraday and the LCR. However, it should be noted that these methodological changes and clarifications have not required changes to the proposed SoP text that was consulted on in CP21/16, and subsequently included in the SoP appended to this CP.

6.2 A full overview of the feedback received from CP21/16 and from this consultation, along with an explanation of any policy updates, will be published following this consultation period.

CP21/16 updates

6.3 One important aspect of the SoP that has been updated since CP21/16 is the use of the word 'guidance'. In CP21/16, the PRA referred to 'Pillar 2 requirements' in a number of places. This has been updated throughout the draft SoP where appropriate to 'Pillar 2 guidance' to reflect the PRA's approach to communicating its view of a firm's liquidity need.

6.4 The PRA, through communicating its view of a firm's liquidity need as guidance, aims to provide the flexibility needed for a firm to draw down their liquid asset buffer in times of stress, in line with the PRA's expectations detailed in SS24/15.² Further, the communication of the PRA's assessment of a firm's liquidity need as guidance is consistent with the PRA's stated expectation in SS24/15 that a firm is not expected to hold excess liquid assets above the higher of ILG or their own assessment of overall liquidity adequacy, as appropriate, to avoid falling below this level.

6.5 Additionally, three paragraphs in the SoP consulted on in CP21/16 have been moved into a proposed amendment to SS24/15. These paragraphs relate to disclosure and intraday liquidity. The paragraphs in the SoP are clearly marked using strikethrough text.

6.6 Finally, the definition of securities financing margin risk has been updated since the publication of CP21/16. The updated definition can be found in the draft SoP.

Pillar 2 risks not covered in this CP

6.7 In CP21/16 the PRA stated that it would consult on its proposed framework and methodologies for assessing and mitigating risks associated with settlement failure and funding concentrations. Given the relative materiality of the two risks compared to other Pillar 2 risks, the PRA will not be making proposals in this CP on these risks. However, it should be noted that the PRA considers settlement failure risk and funding concentration risk to be potentially material Pillar 2 risks for some firms. As such a firm's supervisor may assess and provide liquidity guidance on either or both of these risks when undertaking supervisory reviews.

1 www.bankofengland.co.uk/pradocuments/publications/reports/prastatement181016.pdf.

2 'The PRA's approach to supervising liquidity and funding risks', December 2016: www.bankofengland.co.uk/pradocuments/publications/ss/2016/ss2415update.aspx.

Risks to be considered under the LCR

6.8 Underwriting risk was highlighted for assessment under Pillar 2 in CP21/16. Following further analysis the PRA has deemed that liquidity risks associated with underwriting activities are adequately covered in the LCR. Underwriting risk pertains to the risk that firms may find themselves unable to on-sell part of a new issue. In such cases, the firm retains the unsold portion on their own balance sheet, and must fund the position. Firms should therefore report additional outflows in respect of outstanding commitments on the reporting date and potential commitments arising within 30 days which are linked to underwriting activities under LCR Delegated Act Article 23.

Updates to SS24/15

6.9 Further to the changes outlined in paragraph 6.5, SS24/15 has been updated to introduce:

- (a) additional expectations on firms' stress testing of their ability to transfer liquidity across entities, sectors and countries;
- (b) an expectation on firms to compute a monetisation profile of their liquid asset buffer;
- (c) proposed Pillar 2 guidance that a firm survives for 30-days under the granular LCR stress when the firm's monetisation profile is taken into account; and
- (d) removes outdated text relating to 'ILG during the transition' and 'transition to L-SREP process'.

Updates to SS34/15

6.10 The proposed update to SS34/15:

- (a) provides an end-date for the reporting of FSA047 and FSA048 reporting; and
- (b) introduces links to the PRA110 data item and reporting instructions.

Appendices

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| 1 | Draft Statement of Policy - Pillar 2 Liquidity |
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| 2 | Proposed revisions to SS24/15 'The PRA's approach to supervising liquidity and funding risks' |
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| 3 | Draft reporting template and instructions |
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| 4 | Draft PRA RULEBOOK: CRR FIRMS: REGULATORY REPORTING PRA110 AMENDMENT INSTRUMENT |
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| 5 | Proposed revisions to SS34/15 'Guidelines for completing regulatory reports' |
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Appendix 1: Draft Statement of Policy – Pillar 2 liquidity

The draft SoP combines the proposals from CP13/17 with those consulted on in CP21/16. Consequently, the PRA has renumbered the chapters in the draft SoP. New text is underlined and deleted text is struck through.

1 Introduction

1.1 This statement of policy is relevant to all UK banks, building societies and PRA-designated investment firms.

- Chapter 2 details the PRA's approach to the level of application of Pillar 2 guidance.
- Chapter 3 details the PRA's approach to assessing cashflow mismatch risk.
- Chapter 4 details the PRA's approach to assessing franchise viability risks.
- Chapter 5 details the PRA's approach to assessing other Pillar 2 liquidity risks.

1.2 The Pillar 2 framework covers risks not captured, or not fully captured, in Pillar 1.

1.3 In publishing its approach to Pillar 2, the PRA seeks to help firms understand how it assesses liquidity risks, thereby encouraging them to develop better approaches to reduce or manage these risks.

1.4 The PRA reminds firms that, in line with the Overall Liquidity Adequacy Rule, it is incumbent on them to undertake their own assessment of liquidity risks, including Pillar 2 risks, and to take appropriate measures to reduce or manage these risks.

1.5 The supervisor's overall judgement about how the firm approaches its liquidity risk management will influence the supervisor's decision on how conservative or specific to be in providing individual guidance to firms.

1.6 The Pillar 2 approach applies in a way that is proportionate to each firm's business model and to the risk that the firm poses to the PRA's safety and soundness objective and the Bank of England's financial stability objective. In particular, if a supervisor judges the firm's Pillar 2 risks to be relatively immaterial compared to its Pillar 1 risks, the supervisor may choose not to apply Pillar 2 requirements. If, having reviewed the firm's Individual Liquidity Adequacy Assessment Process (ILAAP) document, a supervisor judges that the risks to the PRA's safety and soundness objective and the Bank of England's financial stability objective from a particular firm are immaterial, the supervisor can also choose not to review the firm for Pillar 2 risks. A supervisor's assessment will involve consideration as to whether any Pillar 2 measures would have a disproportionate impact on a particular type of firm, including whether it results in a relatively bigger burden on smaller firms.

1.7 If appropriate, supervisors may impose other requirements for risks not previously identified in Pillar 1 or Pillar 2.

2 Level of application and disclosure of Pillar 2 guidance

Level of application

2.1 Pillar 2 requirements apply at individual (or sub-group) and consolidated levels. In general, the level of application for setting guidance for a firm under Pillar 2 will be aligned to the Pillar 1 approach. Consolidated guidance will consist of the sum of individual guidance, plus any consolidated level risk. The PRA may consider some netting of solo liquidity guidance to a limited extent, where appropriate.

Disclosure of Pillar 2 requirements

2.2 ~~In line with legal requirements, firms report all eligible high quality liquid assets (HQLA) within their publically disclosed liquidity coverage ratios (LCRs). This includes HQLA held for Pillar 1 requirements, Pillar 2 guidance, and any eligible 'surplus' above that. However, firms should be clear to investors that the HQLA they report in their LCRs is to cover both Pillar 1 and Pillar 2 risks.~~

2.3 ~~The PRA expects firms not to disclose publically their total individual liquidity guidance ('ILG', composed of Pillar 1 requirements and Pillar 2 requirements). Disclosure of the ILG may lead to an expectation, from both firms and markets, that firms should hold a further buffer of liquid assets, above their level of ILG. The PRA has no such expectation, as outlined in Supervisory Statement (SS) 24/15: 'The PRA does not expect firms to hold higher liquid asset buffers than the amount advised in their ILG or as required to meet their assessment of overall liquidity adequacy, as appropriate.'¹ Therefore, the PRA expects that firms will not provide any further details on their Pillar 2 requirements unless disclosure is required by law, and that firms will notify the PRA in advance of any proposed disclosure announcement.~~

3 Cashflow mismatch risk

3.1 This chapter provides a definition of cashflow mismatch risk (CFMR) and then outlines the PRA's approach to assessing and calibrating the risk under Pillar 2.

Definition of CFMR

3.2 CFMR is the risk that a firm has insufficient liquidity from liquid assets and other liquidity inflows to cover liquidity outflows on a daily basis.

3.3 The Liquidity Coverage Requirement (LCR) is a measure of a firm's cumulative liquidity position at the end of a 30-day period. It does not assess whether, if a firm experiences a significant outflow on a given day of the LCR stress, the firm has sufficient inflows and cash, including from monetised liquid assets, to cover the outflow on that day.

3.4 It is therefore possible that a firm meets its LCR, yet is not able to survive the stress scenario captured in the LCR itself: a firm's net cumulative outflow position in stress may exceed available liquidity before the 30-day mark.

3.5 The PRA's CFMR framework focuses on the following sources of risk:

- (a) 'Low point risk': Under the LCR firms need to hold sufficient high-quality liquid assets (HQLA) to cover their cumulative liquidity needs over 30 calendar days. If a firm experiences a peak liquidity need within the 30-day window that is greater than its requirement on day 30, the firm is exposed to the additional net outflow (the difference between the peak and end-month requirement). But it does not necessarily hold sufficient HQLA to cover these additional outflows on that day.

¹ Supervisory Statement (SS) 24/15 'The PRA's approach to supervising liquidity and funding risks', June 2015; www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss2415.aspx.

- (b) HQLA monetisation risks: Firms may not be able to monetise sufficient non-cash HQLA to cover cumulative net outflows under the LCR stress on a daily basis. There are likely limitations to the speed with which cash can be raised in the repo market or through outright sales, linked to market depth, the number of a firm's regular counterparties, individual turnover, settlement times etc.
- (c) 'Cliff risk': The LCR focuses on a 30 calendar day horizon. Firms may 'window-dress' their LCRs by pushing maturity mismatches just beyond the 30-day horizon.
- (d) FX mismatch risks: Firms typically assume that currencies are fungible given the depth of liquidity in the spot FX and FX swap markets, particularly in reserve currencies. However, firms may not be able to access FX markets as normal in times of stress.

CFMR stress scenarios and tools

3.6 CFMR can be assessed under different stress scenarios and monitored over a range of horizons. The PRA's CFMR framework is composed of a set of stress scenarios and tools of different severity and duration. These scenarios represent distinct lenses through which the PRA assesses if firms are running excessive maturity mismatches or have not adequately considered limits to monetisation. The ultimate goal of the framework is to:

- (a) ensure that, throughout the LCR stress and 30-day horizon, firms have sufficient liquidity to cover their liquidity needs on a daily basis; and
- (b) enable the PRA to monitor, with daily granularity, liquidity mismatches which will occur during longer lasting and more severe stress events.

3.7 The stress scenarios and tools described below are those which the PRA tests on an ongoing basis for all firms. This does not preclude the temporary use of targeted stress scenarios, for example, to test firms' resilience to specific, foreseeable, future stress events. Table 1 at the end of this chapter details, for each stress scenario or stress tool, whether the PRA will monitor or set guidance at the point of introduction of the CFMR framework, and whether this is at the consolidated currency and/or single currency level.

LCR AND BENCHMARK STRESSES

A. Granular LCR stress scenario (30-day horizon)

3.8 To assess 'low-point' risk under the stress scenario embedded in the LCR, the PRA computes firms' liquidity inflows and outflows throughout the LCR stress scenario, with daily granularity. The LCR makes behavioural assumptions about the percentage of funding that will be lost (eg retail deposits, repos) during a forward 30-day period. On the asset side, the LCR focuses on projected inflows over the same 30-day period and assigns rates according to how likely the creditor is to demand an extension of funding (eg unsecured lending to non-financials) or for the asset to roll-over (eg reverse repos).

3.9 To obtain projected daily liquidity flows under the LCR stress, the PRA applies the prescribed LCR inflow or outflow rate to:

- (a) contractual cash flows that reach maturity during a forward 30-day horizon; and
- (b) claims and obligations without a contractual end date but which may be called during the same horizon.

3.10 The PRA prescribes assumptions about the intra-month distribution of the latter.

3.11 In respect of claims and obligations without a contractual end date, the PRA assumes that:

- (a) The LCR-prescribed liquidity inflows and outflows from wholesale transactions and retail funding occur on day one of stress.
- (b) Liquidity outflows from off-balance sheet transactions without a defined maturity date occur either on day one of the granular LCR stress (eg outflows corresponding to collateral needs from derivatives transactions) or are uniformly distributed across the 30-days horizon (eg mortgage loans that have been agreed but not yet drawn down).

3.12 Daily available liquidity from cash, central bank-reserves and monetising non-cash HQLA are used to complete the calculation of net liquidity profiles under the granular LCR stress. See 'Approach to modelling the monetisation of High Quality Liquid Assets (HQLA)' section in paragraphs 3.21 and 3.22 for more information. Through the granular LCR stress therefore the PRA covers both 'low-point' and HQLA monetisation risks.

B. Benchmark retail and wholesale stress scenarios (90-day horizon)

3.13 The PRA will also monitor a 90-day horizon. To have visibility over cliff risks under a severe yet plausible stress, the PRA extends the respective LCR inflow and outflow rates to contractual flows scheduled between days 31-90 (months two and three of stress).

3.14 The benchmark retail stress applies the LCR stress inflow and outflow rates to retail claims and obligations contractually maturing within days 1 to 90. Liquidity flows from claims and obligations without a contractual end date should be assumed to materialise only once, as per LCR stress, within days 1 to 30 of the stress period; the timing of these liquidity flows should follow the assumptions described in paragraph 3.11.

3.15 The benchmark wholesale stress applies the LCR stress inflow and outflow rates to wholesale claims and obligations contractually maturing within days 1 to 90. Liquidity flows from claims and obligations without a contractual end date should be assumed to materialise only once, as per LCR stress, within days 1 to 30 of the stress period; the timing of these liquidity flows should follow the assumptions described in paragraph 3.11.

3.16 The benchmark retail and wholesale stress scenarios are considered both separately and jointly, as a combined benchmark stress scenario. The daily available liquidity derived from the firm's monetisation of HQLA profile will be used to complete the calculation of net liquidity profiles under the benchmark stress scenarios.¹

ENHANCED STRESS TOOLS

3.17 The PRA uses two additional stress tools, as sensitivity checks, to monitor firms' resilience to very severe stress events.

C. Enhanced retail stress (90-day horizon)

3.18 The PRA assesses firms' vulnerability to an acute retail run by amplifying outflow rates on uninsured deposits to the maximum withdrawal rate observed during the financial crisis.

D. Enhanced wholesale stress (90-day horizon)

3.19 The PRA further assesses firms' reliance on wholesale markets and their vulnerability to a market shutdown through an enhanced wholesale stress. This assumes a complete closure of secured and unsecured wholesale markets for 90 days, with all claims and obligations running off at the earliest possible date (according to contractual rights).

¹ The first 30 days of the combined benchmark scenario is equivalent to the granular LCR stress scenario.

Foreign currency mismatches in the CFMR framework

3.20 The PRA monitors the granular LCR and combined benchmark stress scenarios, and enhanced wholesale stress tool, on a single currency basis. In the scenarios and tools monitored at the single currency level, the PRA does not differentiate between outflow rates for domestic currencies and non-domestic currencies.

Approach to modelling the monetisation of high-quality liquid assets (HQLA)

3.21 The PRA includes in its assessment, assumptions provided by firms on the limitations they are likely to face in monetising non-cash HQLA. Firms will assess, at least annually, the speed with which they expect to be able to monetise different types of non-cash HQLA, on a daily basis, via repo markets and outright sales, in times of stress. Firms will not include public liquidity insurance as a monetisation channel in this assessment. This enables the PRA to monitor firms' resilience to different stresses using self-insurance alone. Firms will use their assessments to report the resulting monetisation profiles in PRA110 [PRA will insert link when policy and templates finalised].

3.22 These profiles will be computed and reported on a consolidated currency level as well as in each significant currency.¹

Monitoring tools, metrics and limits

3.23 The PRA applies the CFMR stress assumptions to the contractual flows and 'open maturity' columns from the PRA110 report to compute daily projected inflows, outflows and net outflows under each scenario. The LCR inflow cap does not apply to the daily projected flows. The PRA incorporates reported monetisation profiles to compute daily available liquidity, and accounts for projected liquidity needs associated with remaining Pillar 2 risks (which could crystallise at the same time as other risks captured in the CFMR scenarios). The PRA then calculates the following standard monitoring metrics on a consolidated currency basis:

- a) survival days under the combined benchmark stress,² as the distance (in number of days) to the future point in time when a firm's cumulative net cash outflows become larger than its available liquidity;
- b) net liquidity position (the difference between available liquidity and cumulative net outflows) on expected day of default under the combined benchmark stress; and
- c) peak cumulative net outflows and worst net liquidity position under the granular LCR stress within 30 days, and under each of the benchmark stresses within 90 days; peak cumulative net outflows under the enhanced stress tools.

3.24 The PRA assumes that projected liquidity needs associated to all Pillar 2 risks, with the exception of L-SYSC risk, will materialise on day 1 of stress when computing metrics (a) and (b) above. The projected liquidity needs associated with L-SYSC risk should be accounted for on day 30.

3.25 The PRA will monitor firms' worst net liquidity position under the granular LCR stress and enhanced wholesale stress tool on a single currency basis within a 15-calendar-day horizon. The PRA will also monitor firms' survival days under the granular LCR stress in each significant currency.

¹ The PRA does not expect this to create an additional burden: firms would anyway need to consider limits by each security type (e.g. gilts, treasuries) to design consolidated currency profiles.

² This is equivalent to the granular LCR stress during the first 30 days.

Table 1: Stress scenarios and tools: monitoring and guidance, on a consolidated and single currency basis¹

Stress scenarios and stress tools		Consolidated currency		Single currency		
		Monitoring only	Setting guidance	Monitoring only	Setting guidance	
Stress scenario	Granular LCR		✓	✓	✓	
	Benchmark	Retail	✓		✓	
		Wholesale	✓			
Stress tool	Enhanced Retail		✓			
	Enhanced Wholesale		✓		✓	

4 Franchise viability: debt buyback, early termination of non-margined derivatives and prime brokerage and matched books

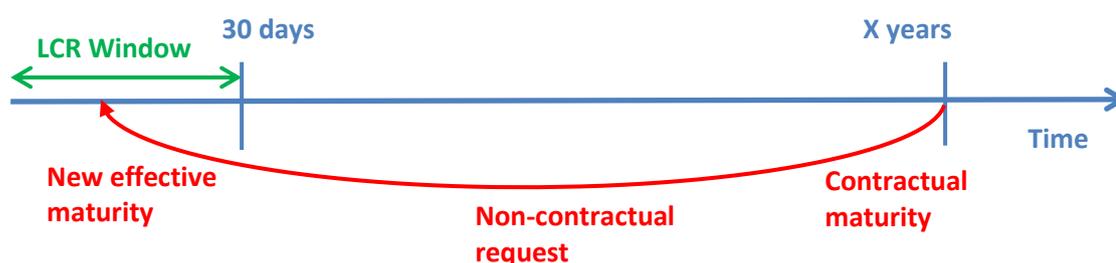
4.1 Several risks fall within the franchise viability category: this chapter focuses on two specific types of franchise viability risk which will be assessed under Pillar 2. The first part provides a general definition of franchise viability liquidity risk. The second part outlines the PRA's approach to assessing debt buyback risk under Pillar 2. The final part outlines the PRA's approach to assessing the risk of early termination of non-margined derivatives under Pillar 2.

Definition of franchise viability risk

4.2 Franchise viability risk arises when a firm takes actions, despite having no legal obligation to do so, in order to preserve its reputation, and where these actions cause unforeseen liquidity outflows. Failing to take these actions may damage the firm's franchise, which could impede access to wholesale markets or cause significant outflows. The associated outflows are uncertain before the event, as there is no associated contractual obligation.

4.3 Franchise viability risk is an open-ended category. It includes risks from prime brokerage, matched books, debt buyback, early termination of non-margined derivatives and settlement failure risk. Chart 1 depicts a counterparty non-contractual request and the impact this may have on maturity.

Chart 1: Effect of a counterparty non-contractual request on maturity



¹ The PRA will monitor the wholesale benchmark and combined benchmark stress scenarios.

Debt buyback risk

4.4 Debt buyback risk arises when firms are asked, by holders of their paper, to buy back debt immediately, transforming a longer-dated contractual maturity into a new, short-dated effective maturity, as shown in Chart 1. Firms may accept buyback requests, despite having no legal obligation to do so, for reputational reasons and to show that a functioning two-way secondary market exists for their debt. Outflows that were previously forecast to occur over the medium to long term have therefore been brought forward.

4.5 If a firm were to refuse such a request, it may signal that it was experiencing a liquidity stress. This could cause liquidity outflows and/or damage future access to capital markets. However, if a firm accepts a buyback request, it must ensure it has liquidity readily available to fulfil that request.

4.6 As early buyback of debt is not a contractual obligation, this risk is not captured in the ~~Liquidity Coverage Requirement (LCR)~~: only outflows from debt contractually maturing within 30 days are captured in the LCR.

4.7 When assessing liquidity risk arising from debt buyback risk, based on the firm's percentage of outstanding debt the supervisor may:

- a) consider outstanding debt with maturities beyond a 30-day horizon. This assessment will take into account the need for banks to maintain levels of debt eligible for minimum requirement for own funds and eligible liabilities (MREL) in a stress;¹ and
- b) take into account activity in the secondary debt market. Firms that are market makers in their secondary debt market may experience a greater frequency of buyback requests.

4.8 The PRA's approach relies on firms' systems and processes recording instances of buybacks, including the circumstances in which they arise.

Risk from early termination of non-margined derivatives

4.9 Non-margined derivative transactions incur neither initial nor variation margin: changes in the mark-to-market value of the derivative are not reserved for upfront or day by day. As a result, negative mark-to-market fluctuations in value may result in unexpected liquidity outflows for a firm if the derivatives contracts were to be terminated early.²

4.10 A firm's derivative counterparty may, at any time, request early termination of the transaction. Such requests may occur for a number of reasons, but will likely occur when the counterparty is 'in the money' on the transaction: conversely, that means the firm is out of the money at the point of early termination, and, for non-margined trades, it will therefore incur an unexpected liquidity outflow if it accepts the request.

4.11 A firm may still accept such requests, despite having no legal obligation to do so, as rejection could suggest it does not have enough liquidity to compensate its 'in the money' counterparty. Such a perception could result in the firm being locked out of wholesale funding markets.

4.12 Payments at the contractual maturity date of the derivative are accounted for in the LCR. Liquidity risk from early termination is not included, because there is no contractual obligation to accept a request for early termination. Therefore if the contractual maturity date falls outside the LCR stress horizon, and an early termination request is accepted, the resulting

1 CP44/15 'The minimum requirement for own funds and eligible liabilities (MREL) – buffers and Threshold Conditions', December 2015, www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp4415.aspx.

2 While the materiality of the non-margined derivative market has declined as a result of the move to greater margining and central clearing, the PRA considers that non-margined derivatives can be a material liquidity risk for some firms.

outflow will not be included in the LCR. As with debt buyback risk, early terminations of non-margined derivatives result in an original maturity date contractually outside the 30-day horizon of the LCR being transformed into an effective maturity date that falls within that 30-day window (see Chart 1).

4.13 When assessing liquidity risk arising from non-margined derivatives, based on the firm's percentage of outstanding exposure, the supervisor may:

- a) choose either peak or average exposure;
- b) identify a historical time period which, allows the supervisor to 'look through' unusual events regarding frequency of early termination requests; and
- c) take into account the following factors as a guide for setting the size of the add-on:
 - i. exposure, as a proportion of total balance sheet, to non-margined derivatives; and
 - ii. exposure to derivatives with more volatile mark-to-market valuations. On average, greater mark-to-market volatility will cause greater liquidity outflows from early termination, for a given frequency of early terminations and a given exposure.

4.14 The PRA's approach relies on firms' systems and processes recording instances of early termination requests, including the circumstances in which they arise.

Prime brokerage and matched book liquidity risk

4.15 This section provides a definition of prime brokerage and matched book liquidity risk, and outlines the PRA's approach to assessing and calibrating the risk under Pillar 2.

4.16 Prime brokerage services allow investors, usually hedge funds, access to securities lending, leveraged trade executions, and cash management, among other things. Prime brokers (PB) act as intermediaries to facilitate investor positions, but do not generally assume the risk of the transactions. They do this by sourcing funding for the transactions and, where possible, the maturity of this funding will be matched to the maturity of the client transaction.

4.17 The two main liquidity risks within prime brokerage relate to franchise risk and internalisation (whereby a PB can internally net opposite positions on the same asset). Both risks, if either were to materialise, would require the firm to cover or re-fund customer positions. In a stress situation, firms may find accessing usual sources of funding for these positions difficult and therefore liquidity is required to cover these risks.

4.18 **Franchise risk:** PBs often offer their service to maintain a franchise value with their clients in addition to the revenues generated directly by the business activity. As such, the PB may roll over funding transactions at a customer's request even in circumstances where doing so might be detrimental to the firm's liquidity position. This could leave the PB in a position where either the customer transaction is not fully covered, and so will need to be funded further by the PB, or the maturities of the matched transactions no longer align.

4.19 **Internalisation:** If a PB has two clients that are taking opposite positions on the same asset (one long, the other short), the PB may internally net these amounts to avoid having to fund the positions elsewhere: a client short position is therefore funding a client long position. Liquidity risk arises if one client wishes to withdraw from their transaction: the PB will either need to find additional funding or will need to purchase or borrow the asset to match the remaining transaction.

4.20 Risks posed by franchise risk and internalisation are different:

- (a) Franchise risk is dependent on how likely (willing) a PB is to roll over the transaction of a client in order to protect its franchise, and the amount that is likely to be rolled over.
- (b) Internalisation risk crystallises when a customer withdraws their position, giving rise to a funding requirement for the remaining customer position, where previously the positions had matched each other.

Synthetic prime brokerage

4.21 Where synthetic structures, using derivatives, are used to mimic the effects of cash prime brokerage transactions the PRA assesses them to derive the underlying economics of the transactions and aligns the assessment with that of cash transactions. This is because synthetic structures generate similar risks to cash transactions.

4.22 The LCR in some cases captures these types of risks, including liquidity risks arising from deposits from prime brokerage customers. But for most liquidity risks within prime brokerage and matched books, the LCR either does not capture, or does not fully capture the risks posed by franchise risk and internalisation.

Methodology for assessing liquidity risks arising from prime brokerage and matched books

4.23 The PRA assesses firms on a case-by-case basis, using a supervisory approach described below, alongside firms' own assessment. The PRA keeps its approach general to allow flexibility for changing business practices. This ensures the general principles apply for all similar cases and accounts for differences in businesses.

4.24 The PRA expects, as part of its L-SREP process that firms will undertake an assessment of their prime brokerage clients to determine the likely liquidity risks that could arise for franchise reasons, in a stress. This will inform the supervisor's judgement.

4.25 An initial add-on is calculated using the inflow rate that has been applied for secured funding transactions under the LCR. If the transactions are internally netted and conducted synthetically, the PRA will seek to assess these transactions consistently with the LCR rates. This ensures a consistent treatment of prime brokerage business across the LCR and Pillar 2.

4.26 The supervisor then applies judgement through the use of appropriate firm level information or data to adjust the initial add-on calculation. This takes into account a number of factors including the firm's governance and risk management, concentration of funding counterparties, and the firm's own franchise client assessment.

Consideration of inflow cap

4.27 Certain business models such as cash prime brokerage and matched books can lead to large gross inflows and outflows, which means the LCR inflow cap is more likely to apply. This is likely to affect firms specialising in PB activities much more than firms who undertake this as a smaller part of their overall diversified activities.

4.28 In determining any liquidity guidance issued for cash prime brokerage or matched books, the PRA takes into consideration 'capped out' inflows, and may in limited circumstances allow a firm to use capped out inflows under the LCR in lieu of a liquidity add-on. Any liquidity guidance issued will be dynamic in that, if capped out inflows are not sufficient to cover the entire guidance specified by the PRA, additional HQLA equal to the value of the difference between capped out inflows and the total add-on will be required.

5 Other liquidity risks

Intraday liquidity

5.1 This ~~chapter~~ section provides a definition of intraday liquidity risk, then outlines the PRA's approach to assessing and calibrating intraday liquidity risk under Pillar 2.

5.2 The PRA defines intraday liquidity risk as 'the risk that a firm is unable to meet its daily settlement obligations, for example, as a result of timing mismatches arising from direct and indirect membership of relevant payments or securities settlements systems'.¹

5.3 The PRA considers that all firms connected to payment or securities settlement systems, either directly or indirectly, are exposed to intraday liquidity risk.

5.4 This chapter addresses intraday liquidity risk within two main types of system: payment systems and securities settlement systems, covering both gross and net settlement. There are two ways in which a firm can connect to these systems: directly or indirectly. A 'direct participant' is directly connected to the system and is responsible to the settlement agent (or to all other participants) for the settlement of its own payments, those of its customers and those of indirect participants on whose behalf it is settling. An 'indirect participant' requires the services of a direct participant to perform activities on its behalf (eg input of transfer orders, settlement).²

Double duty

5.5 Mitigating the risk of double duty is a primary reason for including a calibration of intraday liquidity risk in a firm's liquid asset buffer. Double duty is the use of a liquid asset buffer held for wider liquidity resilience, to support also payments and securities settlement activities intraday, where intraday liquidity risk is not included as a risk in the calibration of the liquid asset buffer.

5.6 While double duty can reduce the cost of participation in payment and securities settlement systems through lower liquid asset holdings, it carries risks. Conceptually, there is a significant risk associated with using the same assets for two separate purposes: when the assets are used for one purpose they are not available for another purpose. In practice this manifests itself in two ways:

- a) Balance sheet resilience risk: if a firm's liquid asset buffer is serving the purpose of providing intraday liquidity then it cannot be as effective as a buffer against a run on liabilities.
- b) Intraday liquidity risk: if a firm suffers a prolonged balance sheet liquidity stress, this uses up the firm's liquid asset buffer meaning that the bank has insufficient funds available to operate effectively in payments and securities settlement systems.³

5.7 For these reasons, the PRA mitigates the risks associated with double duty by calibrating liquid asset buffers to include intraday liquidity risk as a separate risk.

Overall assessment of intraday liquidity risk

5.8 Where an add-on is applied to mitigate intraday liquidity risk, it will be determined by considering at least:

1 SS24/15 'The PRA's approach to supervising liquidity and funding risks', June 2015, paragraph 2.23; www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss2415.aspx.

2 Committee on Payment and Settlement Systems (2003), 'A glossary of terms used in payments and settlement systems'; http://www.bis.org/cpmi/glossary_030301.pdf.

3 For an example of the dangers associated with double duty, see Ball et al. (2010), 'Intraday liquidity: risk and regulation', Bank of England Financial Stability Paper No. 11 June 2011, Box 2; www.bankofengland.co.uk/financialstability/Documents/fpc/fspapers/fs_paper11.pdf.

- a) the firm's mean maximum net debits;
- b) the firm's stress testing framework;
- c) the relevant characteristics of the firm; and
- d) the markets the firm operates in.

5.9 The PRA considers that the mean average of maximum net debits, combined with a stress uplift, is the most appropriate measure to assess intraday liquidity risk. The remainder of this chapter explains this approach in more detail.

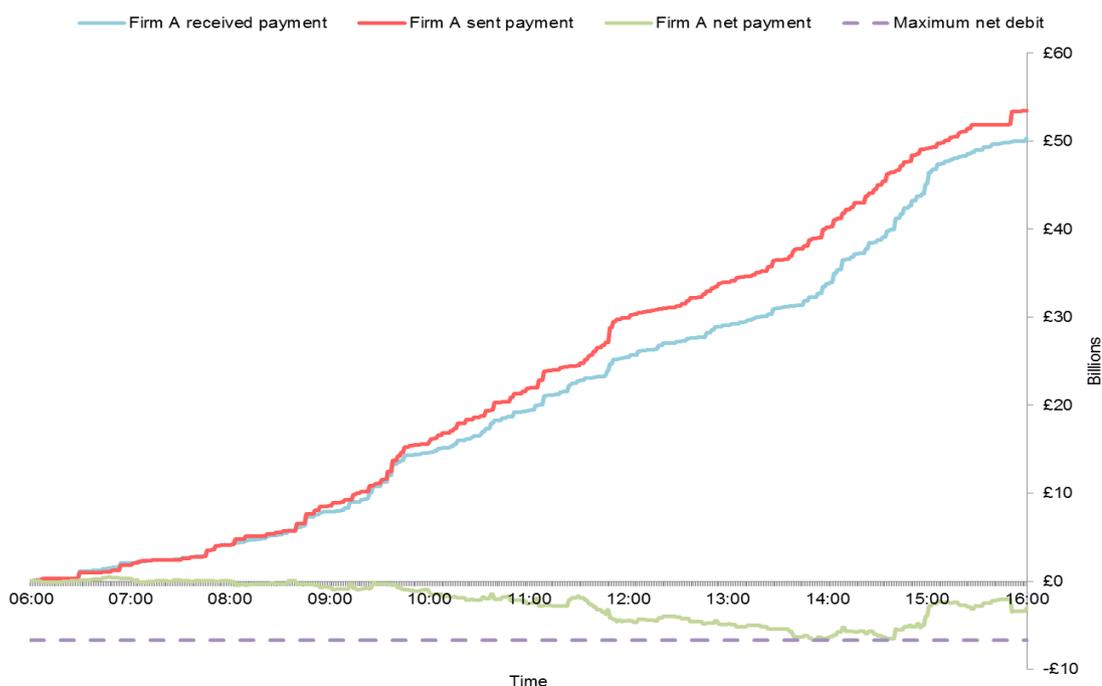
Maximum net debit

5.10 The maximum net debit is a measure of the intraday liquidity need of a firm on any given day. It is calculated as the point at which the value of payments sent by a firm most exceeds the value received by that firm, for a given payment or securities settlement system. Chart 2 shows how Firm A's payment profile and intraday liquidity needs can evolve in a single system over the course of a day.

5.11 The PRA favours the mean average maximum net debit measure, combined with a stress uplift. An alternative approach to sizing intraday liquidity risk is to simply estimate the peak maximum net debit. But this is often driven by one-off, anticipated events, for which liquidity has been set aside, and therefore does not always provide a true reflection of a firm's intraday liquidity risk on an ongoing basis.

5.12 The mean average maximum net debit is assessed for a firm on a system by system basis. The PRA recognises that some firms may be able to create liquidity efficiencies across the systems they operate in. However, for the purposes of considering intraday liquidity risk, the PRA does not consider these efficiencies to be accurately quantifiable on a systematic basis. Nonetheless, where a firm can demonstrate these efficiencies the PRA will give them due consideration during the Liquidity Supervisory Review and Evaluation Process (L-SREP) assessment.

Chart 2: Example of an intraday real time gross settlement payment profile, for a single firm



5.13 A firm should not assume that a reduction in the maximum net debit profile will necessarily lead to a reduction in the PRA's assessment of intraday liquidity risk.

~~The PRA expects all direct participants in payment and securities settlement systems to be able to calculate their maximum net debit position for each respective system in which they participate in. The PRA encourages indirect participants that are currently unable to calculate their maximum net debit position to engage with their correspondent bank(s), with the aim of improving the granularity and timeliness of payment settlement data to enable them to do this. While the PRA will be proportionate in its expectations on the ability of indirect participants to be able to do this for all markets, the PRA reminds firms of the expectations set out in Principle 8 of the Basel Principles for Sound Liquidity Risk Management and Supervision.~~

Alternative methodologies for sizing intraday liquidity add-ons

5.14 The methodologies used by the PRA are based on the maximum net debit position of a firm as a first best option, but where a firm is unable to calculate its maximum net debit, the PRA can employ a range of other methodologies.

5.15 An important proxy methodology is to estimate the level of liquidity recycling. Liquidity recycling is the ratio between value of payments sent and liquidity usage. For example, in a single system on a given day, if a firm has liquidity usage of £1 million and a gross outflow of £10 million, the firm would have a liquidity recycling factor of 10.

Secured, disclosed intraday credit facilities in securities settlement systems

5.16 An alternative to the maximum net debit approach for assessing intraday liquidity risk is used when the following criteria are met:

- a) the securities settlement venue provides a secured and disclosed intraday credit facility to the direct participant; and
- b) the direct participant in that system secures their intraday credit line by holding a pool of assets of value equivalent to the haircut value of the underlying security being settled.

5.17 When both criteria are met, the PRA assesses the intraday liquidity risk to be at least equivalent to the sum of the haircut value of settled trades and a stress uplift.

Assessing risks in stress

5.18 As outlined in paragraph 5.9, a stress uplift is applied to the assessment of intraday liquidity risk.

Stress scenarios

5.19 The following, based on the stress scenarios detailed in Basel Committee on Banking Supervision (BCBS) Monitoring tools for intraday liquidity management,¹ are ways in which an intraday stress may manifest:

- a) a credit or liquidity shock affecting the firm directly, reducing counterparties' willingness to make payments to it in a timely fashion;
- b) an operational, credit or liquidity shock affecting the ability of a major counterparty in the payment system to make payments to the settlement firm as expected;
- c) a credit or liquidity shock affecting a major customer or group of customers of the settlement firm, preventing them from receiving payments as expected; and

1 BCBS (2013), 'Monitoring tools for intraday liquidity management'; <http://www.bis.org/publ/bcbs248.pdf>.

d) market conditions change which mean that a given pool of assets generates less intraday liquidity.

5.20 Scenarios (i) to (iii) capture the risk of a change in the payment profile of a firm which can in turn affect the maximum net debit position, while scenario (iv) affects the ability of the firm to fund its intraday liquidity position. These stresses are applicable to both direct and indirect participants. For more detail on the manifestations of these stress scenarios, see BCBS Monitoring tools for intraday liquidity management.

5.21 A significant impact of stress (i) on a firm that uses correspondent banking services may be the withdrawal of intraday credit line(s) by its correspondent bank(s). This may require the firm to prefund or collateralise its intraday credit line(s).

Stress uplift

5.22 The stress uplift reference point is based on historical evidence gathered during stressed conditions of the type described above, and for both market stress and idiosyncratic stresses.

5.23 The stress uplift will be subject to supervisory judgement. Factors taken into account will include, but are not limited to, the sophistication of the firm's intraday liquidity management systems, how the firm connects to the respective payment and securities settlement systems it uses, and the business model of the firm.

5.24 The PRA expects firms to consider the risk of haircut and collateral eligibility changes in their assessment of intraday liquidity risk.

Margined derivatives

5.25 This section provides a definition of the liquidity risks arising from margined derivatives then outlines the PRA's approach to assessing and calibrating the risk under Pillar 2.

5.26 The PRA considers that liquidity risk arising from initial margin on derivatives contracts is not captured in the LCR. However, liquidity risk arising from variation margin on derivatives contracts is captured within the LCR. Therefore, the Pillar 2 assessment of liquidity risk arising from derivatives contracts will cover initial margin only.

Methodology for assessing liquidity risks arising from initial margin on derivatives contracts

Initial margin posted

5.27 During stress, counterparties may, for a number of reasons, increase a firm's initial margin requirements. This represents a contingent liquidity risk.

5.28 When calculating a firm's liquidity need arising from initial margin posted, the PRA takes into consideration the historical average of initial margin posted to counterparties, and applies a stress uplift to this figure.

Loss of initial margin as a source of funding

5.29 The loss of initial margin received due to the counterparty requesting a trade termination, novation, or segregation represents a contingent liquidity risk to the extent that collateral is no longer available to the firm to use as a source of funding. Firms generally have the contractual right to refuse these requests but may grant requests due to franchise reasons. As such, the PRA will in general treat risks arising from the loss of IM received as a funding source, consistently with the PRA's approach to other franchise risks.

5.30 When assessing liquidity risk arising from loss of initial margin as a source of funding, the supervisor takes into consideration historical evidence of trade termination, novation or segregation.

Securities financing margin

5.31 This section provides a definition of the liquidity risks arising from securities financing initial margin requirements (SFMR) and outlines the PRA's approach to assessing and calibrating the risk under Pillar 2.

5.32 SFMR is the risk of additional outflows relating to margin requirements on securities transactions, both over-the-counter (OTC) and centrally cleared repo transactions. The PRA will assess:

- (a) firm-related margin calls due to the perceived higher probability of default of the firm by the repo counterparty; and
- (b) collateral-related margin calls due to a fall in the price of the collateral or haircut widening due to perceived higher risk of the collateral.

5.33 When assessing the liquidity risk arising from SFMR, the PRA takes into consideration the firm's own historical average initial margin data and applies a stress uplift. The stress uplift will be informed by supervisory judgement, the firm's own assessment, peer comparison, and risk management approaches of relevant clearing houses.

Intragroup Liquidity

5.34 Intragroup liquidity risk may manifest in the following situations:

- (a) where entities within the same group are strongly interconnected and reliant on each other, there is a risk that intragroup support may become unavailable in stress; and
- (b) liquidity may not flow freely within one group or one single legal entity, between an overseas branch and headquarters because of legal, contractual, regulatory or operational limitations resulting in liquidity being trapped in business as usual circumstances or becoming trapped under stress.

5.35 The PRA addresses intragroup liquidity risk on a case-by-case basis, taking into consideration the degree of intragroup interconnectedness. This includes group entities' degree of willingness and ability to support one another in both business-as-usual and stress situations.

5.36 In respect of trapped liquidity, following LCR Article 7(2), assets which are subject to any legal, contractual, regulatory or other restriction preventing the firm from disposing of those assets cannot qualify as liquid assets. Some assets are not subject to any such restriction in business as usual circumstances but may become trapped under stress, for any contingent restriction that a third country may set. Such assets are not excluded from the LCR. Therefore, as part of the Pillar 2 assessment of intragroup liquidity risk, the PRA considers the risk of contingent trapped liquidity.

Liquidity systems and controls

5.37 This section provides a definition of liquidity systems and controls (L-SYSC) risks and then outlines the PRA's approach to assessing and calibrating the risk under Pillar 2.

5.38 L-SYSC risks can be both quantitative and qualitative in nature. Quantitative risks typically include mismeasuring or misreporting, inappropriate assumptions or imprudent calibrations. Qualitative risks can include a lack of reportable metrics, poorly articulated risk appetites and poor quality ILAAPs. Risks stemming from inadequate liquidity systems and controls are not currently captured under Pillar 1.

5.39 Such quantitative and qualitative issues can demonstrate poor liquidity risk management and give rise to additional liquidity risks. Where such concerns are noted, the PRA typically

informs a firm of these and requests remediation. The PRA may also impose additional liquidity guidance under Pillar 2, until such time as L-SYSC risks have been addressed. This liquidity guidance is generally calibrated in the form of a scalar applied to the total of a firm's LCR net outflows and other Pillar 2 liquidity guidance.

5.40 L-SYSC risks and poor liquidity risk management are typically idiosyncratic, and supervisory analysis and judgement are crucial in assessing the level of risk posed and the appropriate mitigant. To ensure consistency, L-SYSC scalars are therefore also informed by internal peer review.

5.41 The purpose of any additional liquidity guidance stemming from L-SYSC concerns should not be confused or conflated with the existing Risk Management and Governance ('RM&G') capital scalar framework set out in the PRA's statement of policy on methodologies for setting Pillar 2 capital.¹ As set out in that statement, a RM&G scalar is considered only when the PRA assesses a firm's overall risk management and governance to be significantly weak. As outlined, any L-SYSC scalar would only be considered to specifically reflect inadequate liquidity systems and controls.

5.42 However, there could be circumstances in which a firm has both poor overall risk management and governance, and inadequate liquidity systems and controls. In such a scenario, both a RM&G scalar and an L-SYSC scalar could be both proportionate and appropriate.

1 'The PRA's methodologies for setting Pillar 2 capital', February 2017:
www.bankofengland.co.uk/pr/Pages/publications/sop/2017/p2methodologiesupdate.aspx.

Appendix 2: Proposed revisions to SS24/15 ‘The PRA’s approach to supervising liquidity and funding risks’

In this appendix, new text is underlined and deleted text is struck through.

Extract

...

2.17 The LCR is distinct from and does not replace the concept of overall liquidity adequacy. The LCR is a set of rules applying 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 the OLAR. It follows that a firm cannot rely solely on meeting the LCR and/or LCR and Pillar 2 guidance in order to satisfy the OLAR.

2.19 The PRA expects, in line with paragraph 3.12A, firms to consider the lowest point of cumulative stressed net cashflows both within the 30-day LCR horizon and within the context of survival days along the horizon of their own risk appetite. Daily granularity is necessary for this analysis.

2.20 (viii) The ability to transfer liquidity across entities, sectors and countries

Firms should assess the intragroup support assumed available in stress, or the impact of 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 amongst entities, business lines, countries and currencies. Firms should detail information on their approach for measuring and managing intragroup liquidity risk and develop their own assessment of the risk of contingent trapped liquidity, on an individual, sub-consolidated (where applicable) and consolidated level. Firms should consider the likely implications of these risks in their stress scenarios and discuss the degree of conservatism and assumptions applied.

2.24A All direct participants in payment and securities settlement systems should be able to calculate their maximum net debit position for each respective system in which they participate. Indirect participants that are currently unable to calculate their maximum net debit position are encouraged to engage with their correspondent bank(s), with the aim of improving the granularity and timeliness of payment settlement data to enable them to do this. The PRA will be proportionate in its expectations on the ability of indirect participants to be able to do this for all markets.

Cashflow mismatch risk (CFMR) monetisation assumptions

2.29A From the date of first PRA110 reporting, the PRA expects firms to assess, at least annually in their ILAAP, the speed with which they expect to be able to monetise different types of non-cash HQLA, on a daily basis, through repo markets and outright sales in times of stress. Firms should take into account relevant factors such as market depth, number of regular counterparties, individual turnover, settlement times, and the need to roll short-term repo transactions etc. Firms should provide evidence of the data used for their assessments in their ILAAPs. Firms should not include public liquidity insurance as a non-cash HQLA monetisation channel in this assessment. This enables the PRA to monitor firms’ resilience to different stresses using self-insurance alone.

2.29B Firms should use their assessments to apply daily monetisation limits to their stock of different types of non-cash HQLA available at the reporting date, in the CFMR framework. The monetisation profiles should be computed on a consolidated currency level as well as in each significant currency. Firms will report the resulting monetisation profiles in PRA110[PRA will insert link when policy and template finalised].

Consistent currency denomination Currency mismatch (see also risk driver vii)

2.33

ILG during the transition

~~[Deleted.]3.12 The PRA is adopting an interim Pillar 2 approach based on the add-ons in a firms' existing ILG. Where add-ons as at 30 September 2015 relate to risks not captured by the LCR, the PRA will continue to apply them at the same absolute amounts as previously. This covers all add-ons except those relating to prime brokerage and margined derivatives.~~

~~[Deleted.]3.13 Until the firm's first L-SREP is undertaken, the add-ons carried over apply on an individual level. If the firm must comply with Part Six (Liquidity) of the CRR on a consolidated level, then the add-ons will also apply at the consolidated level.~~

Pillar 2 guidance

3.12A From the date of first PRA110 reporting, the PRA sets liquidity guidance on the basis that firms should survive throughout the granular LCR stress scenario of the CFMR framework, when combined with the reported monetisation profile, on a consolidated currency basis. To clarify, no guidance is being set on the other CFMR stress scenarios at this time.¹

3.13A Mismatches under the CFMR scenarios are taken into account when assessing compliance with the Overall Liquidity Adequacy Rule.

Pillar 2 asset eligibility

3.14 The type of HQLAs held to meet Pillar 2 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. The quality of HQLAs should be appropriate to mitigate firm-specific risks² and be consistent with the OLAR.

~~[Deleted.]3.15 In due course, the PRA will review its Pillar 2 approach. The Pillar 2 approach will be proportionate to each firm's business model, which includes taking into account the implications of structural reform as required by the Financial Services (Banking Reform) Act 2013).~~

Transition to the L-SREP process

~~[Deleted.]3.16 The PRA will follow the L-SREP process, as outlined in the EBA SREP Guidelines and this supervisory statement, at the latest from October 2015. There is a considerable overlap in the content of the Supervisory Liquidity Review Process under BIPRU 12 and the new L-SREP processes.~~

~~[Deleted.]3.17 Firms reviewed prior to October 2016 may be assessed on the basis of the existing ILAA document if no annual or out-of-cycle reviews have been completed in the intervening period. In the event that the ILAA document does not provide all the detail~~

¹ The PRA is not setting liquidity guidance on firms to meet the CFMR stress scenarios on a single currency basis at this time.

² 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.

~~required of an ILAAP document, the PRA may request additional information as part of the review.~~

6.2 The PRA considers that for firms with a balance sheet total above £5 billion it is appropriate to submit the following returns on a daily basis during times of stress in accordance with of CRR Article 414:

- Liquidity Coverage Requirements (C 72.00–C 76.00); and
- ~~Maturity template (C 66.00);~~
- Rollover of funding (C 70.00).

The PRA also considers that during times of stress, it is appropriate for firms with:

- total assets above €30 billion to submit the PRA110 on a daily basis; and
- total assets below €30 billion to submit the PRA110 on a weekly basis.

6.3 Therefore, the PRA expects those firms to have systems and processes in place that enable them to report these returns as set out in paragraph 6.2. The PRA recognises that firms may require time to develop systems and processes and will be proportionate in its expectations; ~~taking into account that the PRA will still be collecting the FSA047 and FSA048 returns and will be able to require these on a daily basis if necessary.~~

7 Disclosure of Pillar 2 guidance

7.1 In line with legal requirements, firms report all eligible HQLA within their publically disclosed liquidity coverage ratios (LCRs). This includes HQLA held for Pillar 1 requirements, Pillar 2 guidance, and any eligible 'surplus' above that. However, firms should be clear to investors that the HQLA they report in their LCRs is to cover both Pillar 1 and Pillar 2 risks.

7.2 The PRA expects firms not to disclose publically their total ILG. Disclosure of ILG may lead to an expectation, from both firms and markets, that firms should hold a further buffer of liquid assets, above their level of ILG. The PRA has no such expectation, as outlined in paragraph 4.1. Therefore, the PRA expects that firms will not provide any further details on their Pillar 2 guidance unless disclosure is required by law, and that firms will notify the PRA in advance of any proposed disclosure announcement.

Appendix 3: Draft reporting template and instructions

Name		Item
PRA110	Cash flow mismatch	Available at www.bankofengland.co.uk/pr/Pages/publications/cp/2017/cp1317.aspx
PRA110 Colour coded	Cash flow mismatch	Available at www.bankofengland.co.uk/pr/Pages/publications/cp/2017/cp1317.aspx
Instructions		Available at www.bankofengland.co.uk/pr/Pages/publications/cp/2017/cp1317.aspx

Appendix 4: Draft PRA RULEBOOK: CRR FIRMS: REGULATORY REPORTING PRA110 AMENDMENT INSTRUMENT

PRA RULEBOOK: CRR FIRMS: REGULATORY REPORTING PRA110 AMENDMENT INSTRUMENT [2017]

Powers exercised

- 1 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”):
 - 2 [section 137G (The PRA’s general rules)];
 - 3 [section 137T (General supplementary powers)]; and
- 4 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

- 5 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: Regulatory Reporting PRA110 Amendment Instrument [2017]

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

Commencement

- 7 This instrument comes into force on [1 January 2019].

Citation

- 8 This instrument may be cited as the PRA Rulebook: CRR Firms: Regulatory Reporting PRA110 Amendment Instrument [2017].

By order of the Prudential Regulation Committee

[DATE]

Annex

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

Part

REGULATORY REPORTING

1 APPLICATIONS AND DEFINITIONS

...

1.2 In this Part, the following definitions shall apply:

...

~~intra-group liquidity modification~~

~~means a modification to the overall liquidity adequacy rule of the kind described in BIPRU 12.8.7G in the PRA Handbook as in effect on 30 September 2015 granted to a firm and in effect on that date.~~

...

lead regulated firm

means a *firm* which is the subject of the financial supervision requirements of an *overseas regulator* in accordance with an agreement between the *PRA* and that regulator relating to the financial supervision of *firms* whose head office is within the country of that regulator.

~~This definition is not related to the defined term 'UK lead regulated firm'.~~

...

reporting level

means (in relation to a *data item*) the basis on which that *data item* is prepared (being either: (1) an individual basis; or (2) the basis of a group) and, if it is prepared on the basis of a group, the type of group (such as a ~~UK DLG by modification or a non-UK DLG by modification (firm-level)~~ domestic liquidity sub-group).

...

~~whole-firm liquidity modification~~

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

...

7 REGULATED ACTIVITY GROUP 1

7.1 The applicable data items referred to in the table in 6.1 are set out according to firm type in the table below:

RAG 1	Prudential category of firm, applicable data items and reporting format (1)						
	<i>UK bank other than a ring-fenced body</i>	<i>Ring-fenced body</i>	<i>Building society</i>	<i>Non-EEA bank</i>	<i>EEA bank that has permission to accept deposits and that has its registered office (or, if it has no registered office, its head office) outside the EU</i>	[deleted.]	<i>Dormant account fund operator (12)</i>
Description of data item							
...							
[Deleted.] Daily Flows	[Deleted.] FSA047 ((13), (16) and (18))	[Deleted.] FSA047 ((13), (16) and (18))	[Deleted.] FSA047 ((13), (16) and (18))	-	[Deleted.] FSA047 ((13), (15), (16) and (18))	-	-
[Deleted.] Enhanced Mismatch Report	[Deleted.] FSA048 ((13), (16) and (18))	[Deleted.] FSA048 ((13), (16) and (18))	[Deleted.] FSA048 ((13), (16) and (18))	-	[Deleted.] FSA048 ((13), (15), (16) and (18))	-	-
...							
Cash Flow Mismatch	PRA110 (13) (18) (26)	PRA110 (13) (18) (22) (26)	PRA110 (13) (18) (26)	=	PRA110 (13) (18) (26)	=	=

...

(13) A firm must complete this item separately on each of the following bases that are applicable.

- It must complete it on an individual basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the firm alone.
- [Deleted.] If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group.
- If it is a *group liquidity reporting firm* in a *UK DLG by modification* part of a *domestic liquidity sub-group*, it must complete the item on the basis of that group and (a) does not apply.
- [Deleted.] If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.

...

(16) [Deleted.] (a) This item must be reported in the reporting currency.

- If any *data element* 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.
 - In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency).
- However if:
- the reporting frequency is (whether under a rule or under a *waiver*) quarterly or less than quarterly; or

- (ii) the only *material currency* is the reporting currency, then (c) does not apply.
- (d) If there are more than three *material currencies* for this *data item*, (c) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure:
 - (i) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*.
 - (ii) Take the three largest figures from the resulting list of amounts.
- (e) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question.
- (f) The reporting currency for this *data item* is whichever of the following currencies the *firm* 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).

...

(18) Unless otherwise stated in the relevant modification, any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) a *domestic liquidity sub-group permission* do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification*, or variation part *permission* of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun.

...

(26) This *data item* must be reported in the single reporting currency and any significant reporting currency as determined in accordance with paragraphs (1) and (2) of Article 415 of the *CRR*.

...

7.2

The applicable reporting frequencies for submission of *data items* and periods referred to in 7.1 are set out in the table below according to *firm* type. Reporting frequencies are calculated from a *firm's* *accounting reference date*, unless indicated otherwise.

RAG 1				
<i>Data item</i>	<i>UK banks and building societies</i> (on an unconsolidated or individual consolidated basis) (9)	[deleted.]	<i>UK banks and building societies</i> (on a <i>UK consolidation group, defined liquidity group domestic liquidity sub-group</i> or <i>sub-consolidation group basis</i>, as applicable)	Other members of RAG 1
...				
[Deleted.] FSA047	[Deleted.] Daily, weekly, monthly or quarterly ((2), (3) and (6))	-	[Deleted.] Daily, weekly, monthly or quarterly ((2), (5) and (6))	[Deleted.] Daily, weekly, monthly or quarterly ((2), (4) and (6))
[Deleted.] FSA048	[Deleted.] Daily, weekly, monthly or quarterly	-	[Deleted.] Daily, weekly, monthly or quarterly ((2), (5) and (6))	[Deleted.] Daily, weekly, monthly or quarterly

	((2), (3) and (6))			((2),(4) and (6))
...				
<u>PRA110</u>	<u>Daily, weekly or monthly (2) (6) (12)</u>	-	<u>Daily, weekly or monthly (2) (6) (12)</u>	<u>Daily, weekly or monthly (2) (6) (12)</u>

...

(3) ~~[Deleted.]~~ If the report is on an individual basis (and the *firm* is a *UK firm*) the reporting frequency is as follows:

- (a) if the *firm* does not have an *intra-group liquidity modification* the frequency is:
 - (i) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and
 - (ii) monthly if the *firm* is a *low frequency liquidity reporting firm*;
- (b) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is:
 - (i) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and
 - (ii) monthly if the *firm* is a *low frequency liquidity reporting firm*;
- (c) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.

(4) ~~[Deleted.]~~ (a) If the report is on an individual basis (and the *firm* is not a *UK firm*) the reporting frequency is as follows:

- (i) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and
 - (ii) monthly if the *firm* is a *low frequency liquidity reporting firm*.
- (b) ~~–~~

(5) ~~[Deleted.]~~ (a) If the report is by reference to the *firm's DLG by default* the reporting frequency is:

- (i) weekly if the *group liquidity standard frequency reporting conditions* are met;
- (ii) monthly if the *group liquidity low frequency reporting conditions* are met.

 (b) If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:

- (i) weekly if the *group liquidity standard frequency reporting conditions* are met;
- (ii) monthly if the *group liquidity low frequency reporting conditions* are met.

 (c) If the report is by reference to the *firm's non-UK DLG by modification* the reporting frequency is quarterly.

(6) (a) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress or market liquidity stress firm-specific liquidity stress or market liquidity stress* in relation to the *firm, branch* or group in question.

(b) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress or market liquidity stress firm-specific liquidity stress or market liquidity stress* in relation to the *firm, branch* or group in question.

(c) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (a) or (b) even if there is no *firm-specific liquidity stress or market liquidity stress firm-specific liquidity stress or market liquidity stress* and none is expected.

...

(12) The reporting frequency is as follows:

- (i) weekly if the *firm* has total assets, calculated in accordance with Council Directive 86/635/EEC, equal or greater than EUR 30 billion on either an individual basis or *UK consolidation group* basis. This requirement stops applying if the *total assets* of the *firm* on both an individual basis and *UK consolidation group* basis reduce to less than EUR 30 billion for at least four consecutive weekly reporting periods, in which case the *firm* is required to start reporting this *data item* monthly after the end of last consecutive reporting period; and
- (ii) monthly if the *firm* has total assets, calculated in accordance with Council Directive 86/635/EEC, of less than EUR 30 billion on both an individual basis and *UK consolidation group* basis. This requirements stops applying if during any monthly reporting period the *total assets* of the *firm*, on either an individual basis or *UK consolidation group* basis, become equal to or

greater than EUR 30 billion, in which case the *firm* is required to start reporting this *data item* weekly after the end of that reporting period.

...

7.3

The applicable due dates for submission referred to in the table in 6.1 are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in 7.2, unless indicated otherwise.

RAG 1						
Data item	Daily	Weekly	Monthly	Quarterly	Half yearly	Annually
...						
[Deleted.]FSA047	[Deleted.]22.00 hours (London time) on the <i>business day</i> immediately following the last day of the reporting period for the item in question	[Deleted.]22.00 hours (London time) on the <i>business day</i> immediately following the last day of the reporting period for the item in question	[Deleted.]15 <i>business days</i>	[Deleted.]15 <i>business days</i> or one month (5)	-	-
[Deleted.]FSA048	[Deleted.]22.00 hours (London time) on the <i>business day</i> immediately following the last day of the reporting period for the item in question	[Deleted.]22.00 hours (London time) on the <i>business day</i> immediately following the last day of the reporting period for the item in question	[Deleted.]15 <i>business days</i>	[Deleted.]15 <i>business days</i> or one month (5)	-	-
...						
PRA110	22.00 hours (London time) on the <i>business day</i> immediately following the last day of the reporting period for the item in question	22.00 hours (London time) on the <i>business day</i> immediately following the last day of the reporting period for the item in question	15 <i>business days</i>	-	-	-

...

(5) [Deleted.] It is one *month* if the report relates to a ~~non-UK DLG by modification.~~

...

9 REGULATED ACTIVITY GROUP 3

...

9.2

The applicable *data items* referred to in the table in 6.1 for a *UK designated investment firm* are set out in the table below:

RAG 3	
Description of data item	Applicable data items (1)
...	
[Deleted.] Daily flows	[Deleted.] FSA047 ((9), (11) and (13))
[Deleted.] Enhanced Mismatch Report	[Deleted.] FSA048 ((9), (11) and (13))
...	
Cash Flow Mismatch	PRA110 (9)(13)(19)

...

- (9) A firm must complete this item separately on each of the following bases that are applicable.
- (a) It must complete it on an individual basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the firm alone.
 - (b) ~~[Deleted.] If it is a group liquidity reporting firm in a DLG by default and is a UK lead regulated firm, it must complete the item on the basis of that group.~~
 - (c) If it is a ~~group liquidity reporting firm in a UK DLG by modification~~ part of a *domestic liquidity sub-group*, it must complete the item on the basis of that group and (a) does not apply.
 - (d) ~~[Deleted.] If it is a group liquidity reporting firm in a non-UK DLG by modification, it must complete the item on the basis of that group.~~

...

- (11) ~~[Deleted.] (a) This item must be reported in the reporting currency.~~
- ~~(b) If any data element 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.~~
 - ~~(c) In addition, all material currencies (which may include the reporting currency) must each be recorded separately (translated into the reporting currency).~~
 - However if:
 - (i) the reporting frequency is (whether under a rule or under a waiver) quarterly or less than quarterly; or
 - (ii) the only material currency is the reporting currency,
 - then (c) does not apply.
 - ~~(d) If there are more than three material currencies for this data item, (c) only applies to the three largest in amount. A firm must identify the largest in amount in accordance with the following procedure.~~
 - (i) For each currency, take the largest of the asset or liability figure as referred to in the definition of material currency.
 - (ii) Take the three largest figures from the resulting list of amounts.
 - ~~(e) The date as at which the calculations for the purposes of the definition of material currency are carried out is the last day of the reporting period in question.~~
 - ~~(f) The reporting currency for this data item is whichever of the following currencies the firm 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).~~

...

- (13) Unless otherwise stated in the relevant modification, any changes to reporting requirements caused by a firm receiving an *intra-group liquidity modification* (or a variation to one) a *domestic*

liquidity sub-group permission do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that ~~*intra-group liquidity modification, or variation part permission*~~ of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun.

...

(19) This *data item* must be reported in the single reporting currency and any significant reporting currency as determined in accordance with paragraphs (1) and (2) of Article 415 of the *CRR*.

...

9.3

The applicable reporting frequencies for submission of *data items* and periods referred to in 9.2 are set out in the table below. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.

RAG 3	
Data item	Reporting frequency
...	...
[FSA047]	Daily, weekly, monthly or quarterly ((1), (2) and (3))
[FSA048]	Daily, weekly, monthly or quarterly ((1), (2) and (3))
...	...
PRA110	Daily, weekly or monthly (1) (3) (8)

(1) Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular:

- (a) A week means the period beginning on Saturday and ending on Friday.
- (b) A month begins on the first day of the calendar month and ends on the last day of that month.
- (c) Quarters end on 31 March, 30 June, 30 September and 31 December.
- (d) Daily means each *business day*.

All periods are calculated by reference to London time.

Any changes to reporting requirements caused by a *firm* receiving an ~~*intra-group liquidity modification (or a variation to one)*~~ a *domestic liquidity sub-group permission* do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that ~~*intra-group liquidity modification, or variation part permission*~~ of the way through such a period, ~~unless the *intra-group liquidity modification* says otherwise.~~

(2) ~~[Deleted.] If the report is on an individual basis the reporting frequency is as follows:~~

- ~~(a) if the *firm* does not have an *intra-group liquidity modification* the frequency is:

 - ~~(i) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~
 - ~~(ii) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~~~
- ~~(b) if the *firm* is a *group liquidity reporting firm* in a *non-UK-DLG by modification (firm level)* the frequency is:

 - ~~(i) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~
 - ~~(ii) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~~~
- ~~(c) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK-DLG by modification*.~~

(3) (a) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress or market liquidity stress firm-specific liquidity stress or market liquidity stress* in relation to the *firm, branch* or group in question.

(b) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress or market liquidity stress firm-specific liquidity stress or market liquidity stress* in relation to the *firm, branch* or group in question.

(c) A firm must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (a) or (b) even if there is no firm-specific liquidity stress or market liquidity stress ~~firm-specific liquidity stress or market liquidity stress~~ and none is expected.

...

(8) The reporting frequency is as follows:

- (i) weekly if the firm has total assets, calculated in accordance with Council Directive 86/635/EEC, equal or greater than EUR 30 billion on either an individual basis or UK consolidation group basis. This requirement stops applying if the total assets of the firm on both an individual basis and UK consolidation group basis reduce to less than EUR 30 billion for at least four consecutive weekly reporting periods, in which case the firm is required to start reporting this data item monthly after the end of last consecutive reporting period; and
- (ii) monthly if the firm has total assets, calculated in accordance with Council Directive 86/635/EEC, of less than EUR 30 billion on both an individual basis and UK consolidation group basis. This requirements stops applying if during any monthly reporting period the total assets of the firm, on either an individual basis or UK consolidation group basis, become equal to or greater than EUR 30 billion, in which case the firm is required to start reporting this data item weekly after the end of that reporting period.

...

9.4

The applicable due dates for submission referred to in the table in 6.1 are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in 9.3, unless indicated otherwise.

RAG 3						
Data item	Daily	Weekly	Monthly	Quarterly	Half yearly	Annually
[Deleted.]FSA047	[Deleted.]22.00 hours (London time) on the business day immediately following the last day of the reporting period for the item in question	[Deleted.]22.00 hours (London time) on the business day immediately following the last day of the reporting period for the item in question	[Deleted.]15 business days	[Deleted.]15 business days or one month (3)	-	-
[Deleted.]FSA048	[Deleted.]22.00 hours (London time) on the business day immediately following the last day of the reporting period for the item in question	[Deleted.]22.00 hours (London time) on the business day immediately following the last day of the reporting period for the item in question	[Deleted.]15 business days	[Deleted.]15 business days or one month (3)	-	-
...						
PRA110	22.00 hours (London time) on the business day immediately following the last day of the	22.00 hours (London time) on the business day immediately following the last day of the	15 business days			

	reporting period for the item in question	reporting period for the item in question				
--	---	---	--	--	--	--

...

(3) ~~[Deleted.] It is one month if the report relates to a non-UK DLG by modification.~~

16 DATA ITEMS AND OTHER FORMS

...

16.15 ~~[Deleted.] FSA047 can be found here.~~

16.16

~~[Deleted.] FSA048 can be found here.~~

...

16.44

PRA110 can be found here.

...

[DELETED.] ANNEX 1

Liquidity definitions

defined liquidity group

DLG by default

DLG by modification (firm level)

firm-specific liquidity stress

group liquidity low frequency reporting conditions

group liquidity reporting firm

group liquidity standard frequency reporting conditions

low frequency liquidity reporting firm

market liquidity stress

material currencies

non-UK DLG by modification

non-UK DLG by modification (DLG level)

non-UK DLG by modification (firm level)

~~overall liquidity adequacy rule~~

~~standard frequency liquidity reporting firm~~

~~UK DLG by modification~~

~~UK lead regulated firm~~

Appendix 5: Proposed revisions to SS34/15 'Guidelines for completing regulatory reports'

In this appendix, new text is underlined and deleted text is struck through.

There may be other changes to SS34/15 made prior to the PRA finalising policy¹. The final updates for this policy will take any intermediate updates into account.

Extract

...

1 Overview

1.1 This statement is addressed to all firms regulated by the Prudential Regulation Authority (PRA) who are required to submit supervisory reports under the Regulatory Reporting, Close Links and Change in Control Parts of the PRA Rulebook.¹ Its purpose is to set out the PRA's expectations for how firms should complete the data items and returns required by those Parts.

...

- Appendix 11 takes effect from 1 January 2019.

...

1.4 The guidance on completing data items is set out in the following series of appendices:

Appendix	Data items	Description
<u>11</u>	<u>PRA 110</u>	<u>Instructions for completing PRA110</u>

...

2 Integrated regulatory reporting

...

2.2 In the example of a UK bank that is not a FINREP firm or a ring-fenced body, and that does not apply International Financial Reporting Standard 9 (IFRS9), in Regulatory Activity Group (RAG) 1 that also carries on activities in RAG 5, overlaying the RAG 1 reporting requirements (Regulatory Reporting 7.1) with the requirements for a RAG 5 firm (Regulatory Reporting 11.2) gives the following:

RAG 1 requirements (7.1)	RAG 5 requirements (11.2)
Annual report and accounts	Annual report and accounts
Annual report and accounts of the mixed-activity holding company	
Solvency statement	
Balance sheet	Balance Sheet

¹ Consultation CP6/17

Income statement / Statement of profit or loss	Income statement
Statement of Comprehensive income	
Market risk	
Market risk - supplementary	
Exposures between core UK group and non-core large exposures group	
Forecast data	
Solo consolidation data	
Interest rate gap report	
Sectoral information, including arrears and impairment	
IRB portfolio risk	
Daily Flows <u>(Until 31 December 2018)</u>	
Enhanced Mismatch Report <u>(Until 31 December 2018)</u>	
Cash flow mismatch <u>(from 1 January 2019)</u>	
Memorandum items	
	Lending - Business flow and rates
	Residential Lending to individuals - New business profile
	Lending - Arrears analysis
	Mortgage administration - Business profile
	Mortgage Administration - Arrears analysis
	Analysis of loans to customers
	Provisions analysis
	Fees and levies
	Sale and Rent back

...

Appendix 1

Name		Data item	Instructions
FSA047 <u>(Until 31 December 2018)</u>	Daily flows	www.bankofengland.co.uk/pradocuments/crdiv/fsa047jan2016.pdf	www.bankofengland.co.uk/pradocuments/crdiv/fsa047instructionsjan2016.pdf
FSA048 <u>(Until 31 December 2018)</u>	Enhanced mismatched report	www.bankofengland.co.uk/pradocuments/crdiv/fsa048jan2016.pdf	www.bankofengland.co.uk/pradocuments/crdiv/fsa048instructionsjan2016.pdf

Appendix 11 - Guidelines for completing data item PRA110 (in force from 1 January 2019)

Name		Data item	Instructions
PRA 110	Cash flow mismatch	[Insert link]	[Insert link]