BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

PRA statement on feedback received during the consultation period for CP21/16 'Pillar 2 liquidity'

On 12 May 2016 the Prudential Regulation Authority (PRA) published Consultation Paper (CP) 21/16 'Pillar 2 liquidity'.[1] The consultation closed on 12 August 2016; in total the PRA received 11 responses. This statement summarises the feedback received on the draft statement of policy, but does not provide final policy proposals. As noted in CP21/16, the PRA will publish a second consultation paper covering a range of risks outlined in CP21/16 (mid-2017 on current plans). This second consultation paper will include a cost benefit analysis on the entire proposed Pillar 2 framework. Until all Pillar 2 framework proposals are finalised, a cost benefit analysis cannot be completed, and therefore finalised proposals cannot be put forward. The feedback received on CP21/16 will feed into a cost benefit analysis and final PRA policy proposals published in the second consultation paper.

Level of application

Some respondents suggested that Pillar 2 requirements should be set at the lowest relevant level of application. If consolidated requirements are set, respondents asked that high quality liquid assets (HQLA) held against add-ons at lower levels of application and which are considered trapped, be taken into account when sizing the consolidated requirement.

Disclosure of Pillar 2 requirements

Respondents broadly agreed with the proposed approach to disclosure of Pillar 2 requirements.

Franchise viability: debt buyback risk

Most respondents welcomed the PRA's approach to assessing debt buyback risk, in particular the proposal to take account of the need to maintain debt eligible for minimum requirement for own funds and eligible liabilities (MREL). Some respondents noted that they have a clear policy not to buy back debt, even in a stress, and questioned whether the PRA should set add-ons in light of this. One respondent requested that the PRA take account of the reduced likelihood of a subsidiary buying back debt issued by a parent legal entity.

Franchise viability: early termination of non-margined derivatives

Some respondents questioned the need to set add-ons for potential early termination of non-margined derivatives given the declining materiality of the risk with the move to margining and central clearing of derivatives. One respondent requested additional clarity on how the PRA measures exposure to non-margined derivatives.

Intraday liquidity

Respondents had mixed views on the proposed use of the mean of daily maximum net debits to size intraday liquidity needs. Some respondents were concerned that this approach could lead to double counting of liquidity risks captured by the Liquidity Coverage Requirement (LCR), for instance where clients pre-fund payments.[2] Other respondents thought that the burden of producing data to support analysis of the maximum net debit was too high given their size and business model. Alternative methods of calculation were suggested by respondents.

Outline of future work

Respondents were supportive of the PRA's intention to consult on cash flow mismatch risk. While few respondents commented on the PRA's plan to undertake an assessment of the most appropriate calibration of the liquidity regime overall, those that did were supportive. The PRA will consult in due course on these items, as well as whether and, and if so how, to address foreign currency liquidity and funding risks within the proposed framework.

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1 www.bankofengland.co.uk/pra/Pages/publications/cp/2016/cp2116.aspx.
2 European Commission Delegated Regulation (EU) 2015/61.