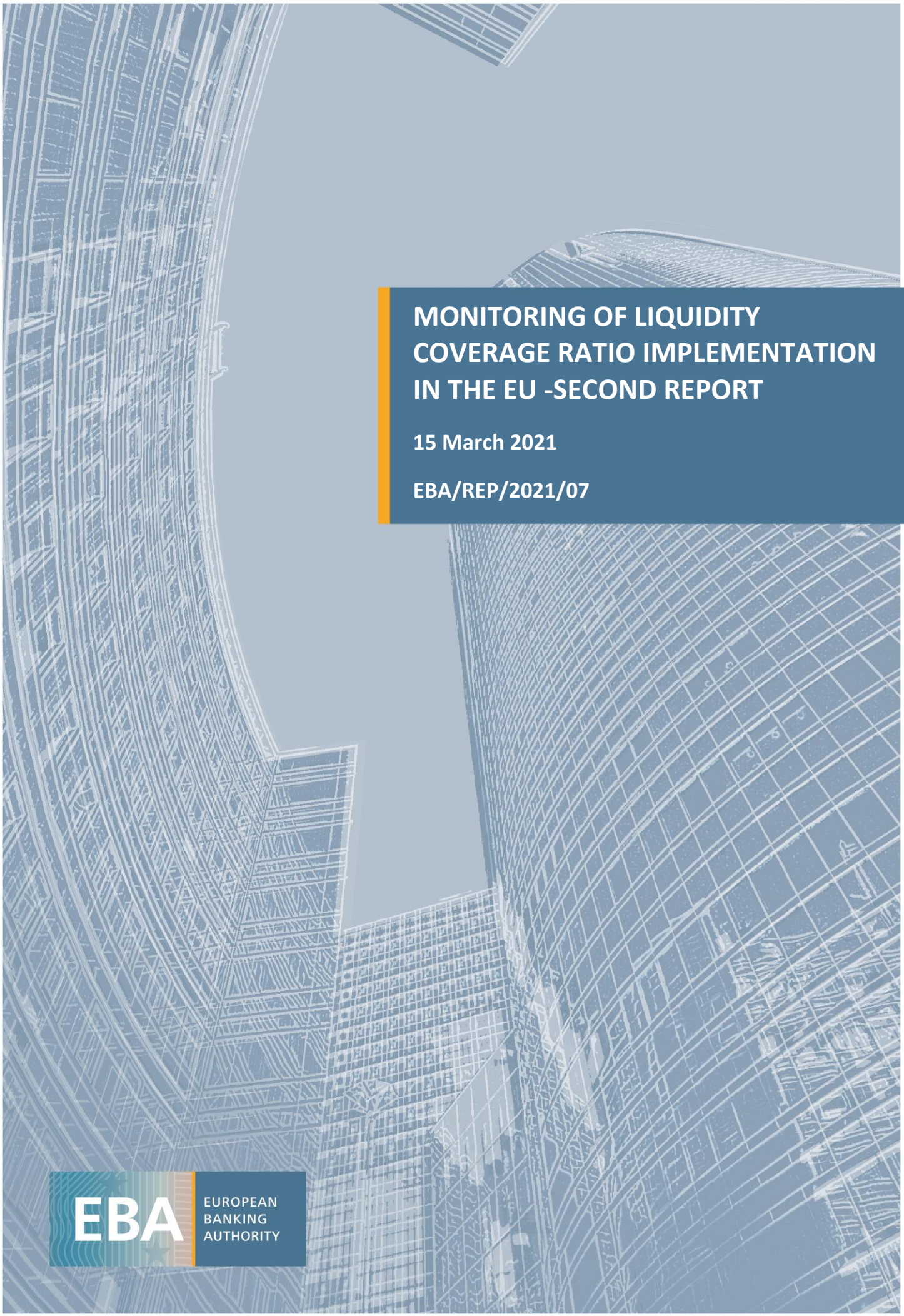

MONITORING OF LIQUIDITY COVERAGE RATIO IMPLEMENTATION IN THE EU -SECOND REPORT

15 March 2021

EBA/REP/2021/07

EBA EUROPEAN BANKING AUTHORITY

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Abbreviations

ASF	Available Stable Funding
CA	Competent Authority
COREP	Common reporting
CRR	Capital Requirements Regulation
DGS	Deposit Guarantee Scheme
DGSD	Directive on Deposits Guarantee Schemes
EBA	European Banking Authority
EC	European Commission
ECB	European Central Bank
ELA	Emergency Liquidity Assistance
EU	European Union
GL	Guidelines
HQLA	High quality liquid assets
ILAAP	Internal Liquidity Adequacy Assessment Process
ITS	Implementing Technical Standards
LCR	Liquidity coverage ratio
LCR DR	LCR Delegated Regulation
NSFR	Net Stable Funding Ratio
Q&A	Question and answer documents
RSF	Required Stable Funding
RTS	Regulatory Technical Standards
SFTs	Securities financing transactions
SREP	Supervisory Review and Evaluation Process
TLTRO	Targeted longer-term refinancing operations

1. Executive summary

1.1 Background

1. The liquidity coverage ratio (LCR) has been applicable in the European Union (EU) since 1 October 2015, and the LCR full implementation at a minimum of 100% became effective in January 2018, which put an end to any national provisions in the area of liquidity requirements (Article 412(5) of the Capital Requirements Regulation (CRR)[1]). Commission Delegated Regulation (EU) 2015/61 (LCR Delegated Regulation)[2] contains the specifications of the LCR. It was amended in July 2018 by Commission Delegated Regulation (EU) 2018/1620, which applied from April 2020. The LCR Delegated Regulation sets out a material number of national discretions to be exercised by competent authorities when implementing the LCR requirements, and envisages some leeway to credit institutions[3] in the assessment of some material LCR items.

2. In July 2019 the EBA published its first report on 'monitoring of liquidity coverage ratio implementation in the EU'[4].

3. This monitoring of the practical implementation of the LCR is framed in the European Banking Authority (EBA) monitoring duties, with a view to contributing to a consistent application of EU law and promoting common supervisory approaches and practices in this area.

4. The first report identified areas with material differences in implementation across jurisdictions and banks where further guidance was deemed useful for banks and supervisors in order to foster a common understanding and harmonisation of the application of the liquidity standard, while at the same time reducing some issues as regards the level playing field.

5. Specifically the report included guidance for: i) the identification of excess operational deposits, that would follow the treatment for non-operational deposits and; ii) the assessment of a material early withdrawable penalty in term retail deposits maturing beyond 30 days, that could allow them to be excluded from outflows. Furthermore, the report included guidance to clarify some products and services that could trigger additional outflows not specified in the LCR Delegated Regulation (LCR DR). The report also intended to draw supervisors' attention in their ongoing supervision as regards existing liquidity risks particularly related to the time dimension of the LCR (comparison between end-of-month LCR and intra-month LCR values) and to cases in which banks are swapping some retained own securities.

[1] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:176:0001:0337:EN:PDF

[2] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015R0061&from=EN

[3] This report refers to credit institutions and banks interchangeably.

[4] https://eba.europa.eu/sites/default/documents/files/documents/10180/2551996/67b34a0d-4e5f-4f46-82f3-48a9aa92e5e0/Monitoring%20of%20the%20LCR%20implementation%20in%20the%20EU%20-%20first%20report.pdf

6. The EBA explained in the report that it aimed to continue developing this monitoring exercise, with similar purposes, with new guidance to banks and supervisors on other areas of attention. The EBA clarified that further work was ongoing on the implementation of, particularly, Article 26 of the LCR DR, the LCR by significant currency and HQLA diversification. Furthermore, the monitoring effort was open to cover new aspects that might arise.

7. The policy guidance included in the report is not formally legally binding although the EBA expects that banks and competent authorities will follow it. It constitutes best practices to follow and focuses on aspects where diverse approaches have been observed in practice with a potential material impact.

8. This second report is a complement of the first report and pursues the same approach and objectives. The same methodology and the EBA sample of banks are used. It focuses on the assessment of the following topics for which guidance to banks and supervisors as well as messages to other market participants are provided. The EBA has observed for these items material differences in implementation which have a significant impact on the uniform application of the LCR, jeopardising robustness of the regulation and the level playing field. The report discusses in particular:

    - In a first section, the usage of liquidity buffers, guidance on unwinding mechanism waivers, recourse to central bank support and additional outflows from derivatives, in the context of a crisis, in particular in view of the COVID-19 pandemic;

    - In a second section, some specific practices or approaches for which guidance is provided to ensure a common understanding: the treatment of fiduciary deposits, LCR optimisation risk, interdependent inflows and outflows for LCR purposes, treatment of DGS deposits.

9. Finally, the last section of the report assesses the effects of past guidance, as issued in the first report. In this regard, the EBA has noticed that its previous guidance has positively influenced the behaviours of banks, which shows the usefulness of this guidance.

1.2 The EBA's observations and main conclusions

10. The EBA continues its work on monitoring the LCR implementation on a number of topics that have arisen for discussion, in some cases, or have raised the need to issue specific guidance, in others. Ultimately the target is to contribute to a common understanding of the Regulation in place and to ensure that banking practices do not alter the effectiveness of the regulations nor trigger level playing field issues.

1.2.1 - Liquidity discussions during a crisis period, including the COVID-19 context

11. The report provides a policy discussion on the management of liquidity buffers under stress. It builds on the regulatory expectation that the liquidity buffer in the LCR is designed to be used

to meet net outflows under stress. This is in order to avoid contagion risk and ensure liquidity injection into the economy and financial system. The report argues that the use of liquidity buffers should not be penalised by the reaction of external or internal agents. These discussions build on the observations raised by some supervisors on the reluctance of banks to use their buffers during the COVID-19 episodes. The report frames this in a context where, despite the influence of central bank support on the LCR levels, the liquidity risk profile overall should not be read differently from a supervisory policy perspective, except for some outliers. In particular, this item deals with the following aspects.

Usage of the LCR Liquidity buffer

12. The report explains that the liquidity buffer in the LCR Regulation is designed to be used under stress to meet net outflows and elaborates on why banks should not feel deterred from this. The report looks and analyses, from a policy perspective, the reasons observed by some supervisors for reluctance by banks to use their liquidity buffers. Special consideration is made to credit rating agencies assessment of LCR values and potential implications of downgrades to external funding access; market reaction to public disclosures of decreasing LCR values; supervisory scrutiny of reduced LCR values; activation of internal contingency plans due to lower LCR values; LCR related recovery triggers or optimisation of economic results.

Unwinding waivers

13. In accordance with paragraph 4 of Article 17 of the LCR DR competent authorities may waive banks from unwinding central bank SFTs or collateral swaps for the computation of HQLA caps. This is envisaged in the context of a systemic risk environment and subject to compliance with some conditions. Unwinding these transactions, particularly when the banks use the liquidity received, might reduce LCR values to an extent that it could even discourage banks from making recourse to central bank funding. This waiver aims to avoid unintended consequences when using central bank funding as a last resource and, in line with the previous discussions, to ensure that the liquidity received can be effectively used. Due to the high positive impact that the waiver has on LCR values, the report provides guidance on how to read the conditions required in the Regulation to ensure common understanding and a level playing field in the application of the waiver.

Central bank support

14. In clear connection with the unwinding waiver, the report provides a message to banks, supervisors and market participants, from a supervisory policy perspective, of how the LCR values can be read after the central bank liquidity injection. It also explains how central bank support has helped banks to maintain or even increase average LCR values. The report clarifies that, except for some outliers, the LCR values without such central bank support would still show a similar liquidity position and LCR liquidity risk profile. This is mainly due to the high liquidity buffers held by banks before March/April 2020.

Additional outflows from derivatives due to adverse market conditions

15. The report flags material additional outflows triggered by margin calls in derivatives in March/April 2020. The report highlights how, under the current Regulation in place (RTS on additional outflows[5]), the events in March/April will trigger direct implications in the quantification of outflows by banks during the following two years irrespective of the size of derivatives portfolios or market performance in the future. The EBA will monitor the impact of this provision in practice and act in due course if necessary.

1.2.2 - New implementation issues observed

Treatment of fiduciary deposits

16. The report assesses fiduciary deposits in the liquidity risk management of banks and provides guidance on the LCR treatment of inflows/outflows and on the NSFR treatment of RSF/ASF, to be applied by the fiduciary bank, final bank and original depositor. Generally, the report follows the treatment envisaged in Article 28(1) of the LCR DR and Articles 428l and 428ad CRR for brokered deposits (generally triggering a 40% outflow rate and 50% ASF in the final bank), in the LCR and NSFR respectively.

17. The report explains how, due to the complex and varied nature of these transactions, there is a risk of an uneven playing field across banks if the provisions setting the relevant rates are applied wrongly. Indeed, a wrong reading of the rules might involve applying outflow rates ranging from 5%, if fiduciary deposits are considered as stable retail deposits (95% ASF in the NSFR), to 100%, if the counterparty is considered as a financial customer (0% or 50% ASF in the NSFR if maturity is less than 6 months or one year) through to 20%/40% if it is considered a non-financial customer (50% ASF in the NSFR if maturity up to one year).

18. The treatment provided takes into account potential risks of arbitrage in practice to make interbank deposits benefit from the more favourable treatment of brokered deposits. Indeed, a deposit received from a deposit broker where the original depositor is a bank should be treated as an interbank deposit (100% outflow rate, in the LCR, or up to 50% ASF if below 1 year, in the NSFR) and not as a brokered deposit, irrespective of the form of the fiduciary.

LCR optimisation risks, concentration of outflows beyond 30 days

19. The report further elaborates on the LCR time dimension related issue flagged in the first report. The analysis reflects cases of potential LCR optimisation by concentrating outflows just beyond its 30-day time horizon. This mainly refers to the practice employed by some banks of adding a notice period for an early withdrawal of (otherwise longer-term) liabilities that last just beyond

[5] Commission Delegated Regulation (EU) 2017/208 of 31 October 2016 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for additional liquidity outflows corresponding to collateral needs resulting from the impact of an adverse market scenario on an institution's derivatives transactions.

the 30-day horizon, or the practice of renewing the maturities of liabilities with a greater than 30-day maturity period when these maturities approach 30 days.

20. The EBA (COREP-based) analysis estimates the impact of concentrations between 30 and 35 days, which in a number of credit institutions in the sample is comparatively high. These observations have been complemented with information collected from supervisors, covering the nature and characteristics of the outflows/inflows.

21. It appears that, while optimisation may not be widespread in a systematic manner, some banks may persistently engage in some degree of optimisation practices. The analysis explains the observed practices and warns of their associated risks, such as the effect of cliff risk associated with a notice period just beyond the 30-day horizon. In particular, if depositors make use of the notice period because of stress or any other reason, the LCR would drop materially after one or two days (when the remaining maturity of the funding enters the 30-day LCR horizon). It also provides guidance for the recognition of outflows.

Article 26 LCR DR on outflows with interdependent inflows

22. Article 26 LCR DR envisages the possibility for banks to net outflows with interdependent inflows, without the application of the inflow cap, subject to compliance with some conditions and to the approval of the relevant competent authority. The report explains the effects of the application of this treatment in the LCR, which leads in some cases to a full or predominant reduction of the requirement of a liquidity buffer in banks. It flags the importance of a common understanding on the conditions required for its application to ensure a level playing field across banks and EU jurisdictions ensuring equal opportunities to optimise resources as well as to avoid any risk to liquidity soundness in banks.

23. Based on both policy and legal views, the report provides guidance to banks and supervisors on how the conditions required for the above mentioned treatment should be read and shows how competent authorities might still grant, within the Pillar 1 requirement, the application of this inflow cap waiver in a partial manner if they wish to ensure a minimum LCR buffer is held. Flexibility is provided to supervisors within the Pillar 1 framework to calibrate the degree of reduction of the required liquidity buffer when the conditions of Article 26 are met and the use of this specific treatment has been approved.

DGS conditions for a 3% outflow rate in retail deposits

24. Paragraphs 4 and 5 of Article 24 of the LCR DR recognise the possibility for stable retail deposits to benefit from a 3% outflow rate, rather than the default 5% applicable to them, in cases where the deposits are covered by a DGS that meets specific conditions and subject to evidence of a less than 3% run-off rate. The application of this preferential 3% outflow rate is subject to authorisation by the relevant competent authority and prior approval of the European Commission. The European Commission shall ask for an Opinion from the EBA on whether the required conditions by the DGS have been met.

25. The report provides guidance in terms of a methodology on how the conditions required to be met by a DGS should be assessed in the LCR context. This is particularly the case of the assessment of whether the DGS has prefunded available financial means, access to additional funding or extraordinary contributions as well as the capacity to ensure repayment in seven working days. The methodology assesses both the legal framework and operational capability of the DGS to ensure compliance with these conditions. It builds on specific information that DGS will need to provide for such assessment. This guidance is a first step meant to ensure a common approach/methodology to be used in the assessment of the conditions for the EBA Opinion in each relevant case in order to avoid any level playing field issues.

26. Further work will be performed by the EBA in the near future on a methodology to assess the required evidence of a less than 3% run-off rate and ensure the harmonised application of this provision.

1.2.3 - Effects of EBA guidance provided in the first report

Treatment of excess operational deposits – Article 27 of the LCR DR

27. The report reviews the application of the guidance to identify excess operational deposits included in the first report. Data observations show some increase in the trend of deposits treated as non-operational after the first report. This is considered an expected result considering that in some cases no (sufficiently conservative) approach was used to identify these amounts.

28. Some supervisors have also confirmed that they have observed that banks treat excess operational deposits in accordance with EBA guidance. In addition, some CAs have used different ways of communication of the guidance. In some cases, CAs refer to the guidance in the course of their individual discussions with a bank in the context of an on-site inspection, the SREP or simply during their ordinary supervisory dialogue. In other cases, CAs have used a more general communication to banks, via letters or own guidance building on the EBA report.

Review of retail deposits excluded from outflows – Article 25(4) of the LCR DR.

29. The application of the guidance for the identification of a material early withdrawable penalty in the case of retail deposits beyond 30 days has been reviewed. COREP observations and input from supervisors show a decreasing amount of retail deposits excluded from outflows. This is consistent with the expectations based on the guidance provided.

30. CAs confirmed the EBA guidance to identify retail deposits excluded from outflows was being applied in practice. Here as well, some CAs confirmed similar bilaterals or general indications to their banks for the concrete application of the EBA guidance.

1.3 Feedback from the industry

31. The EBA organised an informal technical exchange in December 2020 with some EU professional associations that nominated specific banks for this purpose. The EBA Banking Stakeholder Group was also invited to participate in these discussions. Participants were invited to send additional written comments. Participants have generally welcomed the EBA's work on the new topics included, while no objection was raised on the proposed content, and flagged other items as potential areas of attention or investigation for the future.

32. The EBA will continue to hold exchanges on a regular basis with stakeholders while progressing with its monitoring work.

1.4 Next steps

33. The EBA will continue working on monitoring the implementation of the LCR in the EU and will subsequently extend it to the NSFR.

34. Some specific topics are already work in progress. For example, the EBA has started to work on a common understanding for a methodology to assess the required below 3% run-off evidence for the application of a 3% outflow rate in stable retail deposits (Article 24(5) of the LCR DR). The EBA will also work on the notifications to be received in application of Article 26(2) of the LCR DR on outflows with interdependent inflows in the context of the guidance included. The EBA will also monitor the application of the guidance on unwinding waivers. Other important topics are LCR by currencies subject to separate reporting (significant currencies) and HQLA diversification in the LCR, as already announced in the first report.

FIRST SECTION

Usage of liquidity buffers, unwinding mechanism waivers, recourse to central bank support and additional outflows from derivatives, in the context of a crisis, in particular in view of the COVID-19 pandemic

2. Liquidity discussions during a crisis period, including the COVID-19 context

35. In the context of the COVID-19 crisis episodes, the EBA has monitored some interconnected key elements in liquidity.

36. The usage of liquidity buffers under stress and the interaction with liquidity received from central banks' support is discussed here. The EBA differentiates the role of central bank support in the liquidity buffer in the context of normal (non-stressed) and stressed scenarios.

37. Under normal scenarios, banks are expected to hold a sufficient liquidity buffer composed of high-quality liquid assets, which are expected to be liquidated in private markets to cover any potential stressed net outflows that may arise. Here, the buffer is generally not expected to be built up mainly with central bank funding.

38. Under stress, the liquidity buffer can be used by banks and the LCR is built and calibrated with this exact purpose. According to the LCR-scenario, central bank funding would not be expected to replace the usage of the LCR buffer. However, in order to avoid unintended consequences, and only in exceptional circumstances which could go with systemic risk, the LCR DR envisages the possibility of applying exceptional measures. In this regard, banks might benefit from some preferential treatment in the LCR as regards central bank support, via a waiver of the 'unwind mechanism' in the context of the calculation of the caps on HQLA in the computation of the liquidity buffer. The unwind mechanism discounts the cash and other liquid assets (in and out) legs of up to 30 days SFTs to reflect an adjusted value of the liquid assets held by banks. The waiver here avoids a reduction of the LCR value particularly if the monies received from central banks are used and not reinvested in liquid assets.

39. Given the COVID-19 crisis, the intended EBA guidance to ensure a common understanding on how to apply the unwind mechanism waiver is now even more warranted in order to avoid any risks to the level playing field due to the impact that this mechanism has in the LCR values of banks. This guidance gains special relevance against the current background of material central bank support being injected into banks.

40. At the same time it has been observed that some banks are reluctant to make use of the buffers in the EU, even though these buffers are very large. The average LCR is 165% as of June 2020. The EBA also issues policy messages to banks and supervisors as regards the management and monitoring of the buffers and, in general, the LCR values.

41. Finally, the note acknowledges some issues surrounding the evolution of additional collateral outflows in derivatives in the crisis with the view of preparing for the EBA close monitoring in order to be ready to act if necessary in due course.

2.1 Usage of the buffer

2.1.1 Background

42. The fundamentals of the LCR Regulation allocate the marginal cost of liquidity/funding to banks. This is done by defining strict criteria regarding high-quality liquid assets that need to be held by banks to be used to handle net outflows under severe stress, both idiosyncratic and market wide. This encourages banks to adjust their liquidity risk profile and subsequently reduce the need for costly high-quality liquid assets. Ultimately, the intention is to prevent the private marginal costs of liquidity of banks from transforming into social marginal costs. This is flagged in Recital 1 of the LCR DR[6].

43. The definition of high-quality liquid assets and net outflows captures the specific targets of the LCR that seek to ensure that banks can meet their payment obligations under liquidity stress by using their liquidity buffer, while, more broadly, avoiding contagion effects to their counterparties and continuing to provide the real economy and the financial system with the necessary liquidity. Such outflows range from outflows due to payments to depositors, increased collateral or margin calls required in financial transactions or any funding facilities, among others.

44. However, despite these LCR objectives, input from some supervisors indicates that credit institutions experiencing a liquidity shortage or stress may tend to avoid using their liquidity buffers in order to maintain high LCR values. The EBA assumes that institutions may fear possible adverse effects of the use of the buffer in the event of market stigma if the LCR goes below 100%. The following specific concerns are raised:

    a. Credit rating impact: rating agencies require information on credit institutions' LCR values upon which, among others, they build their credit rating. Credit institutions would tend to prioritise keeping large amounts of liquidity buffers and high LCR values and avoid risks in accessing funding or increasing its cost.

    b. Public disclosures impact: in the same vein as above, institutions might be reluctant to disclose lower LCR values due to the reaction it could trigger from market participants. In this context, it is noted that the EBA Guidelines on LCR disclosures[7] require the publication of LCR values measured as the average of the previous 12 end month observations and referred to the end of each calendar quarter, differently from the Basel framework that requires LCR values to be disclosed as a simple average of daily observations over the previous quarter. This specific EU

[6] '… Ultimately many credit institutions became excessively dependent on liquidity provision by the central banks and had to be bailed out by the injection of massive amounts of funds from the public purse. Thus it became apparent that it was necessary to develop a detailed liquidity coverage requirement whose aim should be to avoid this risk by making credit institutions less dependent on short-term financing and central bank liquidity provision and more resilient to sudden liquidity shocks.'

[7] EBA/GL/2017/01- Guidelines on LCR disclosure to complement the disclosure of liquidity risk management under Article 435 of Regulation (EU) No 575/2013 (link).

approach was designed to seek a transparent mechanism for market participants while at the same time preserving a non-procyclical approach. However, banks might fear disclosure requirements other than the regulatory ones due to market expectations. This might be the case of disclosure requirements stemming from national corporate law requiring institutions to publicly disclose a breach of the general LCR minimum level of 100%. For instance, in relation to listed companies, a breach of the level of 100% may require an ad-hoc disclosure as such an event could have an impact on the share price.

c. Recovery trigger impact: The EBA GLs 'on the minimum list of qualitative and quantitative recovery plan indicators'[8] refer to liquidity indicators that should be included as recovery plan indicators. These indicators need to be set by each institution at the appropriate levels to initiate the escalation process, triggering the necessary actions in the recovery plan. The provision regarding the LCR is that the relevant indicator should be calibrated in a way that communication to senior management is ensured as soon as compliance with the LCR minimum requirement is at risk (paragraph 31 of the cited EBA Guidelines). Hence, liquidity risk managers in banks might have limited the use of their liquidity buffers to avoid any potential for LCR values to approach levels below 100% in order to circumvent any escalation process and recovery actions.

d. Supervisory scrutiny: Article 414 of the CRR envisages immediate notification to the competent authorities when there is a risk or expectation that LCR values could go below 100%. Competent authorities and institutions are then required to work together to design a proper plan to restore the LCR to adequate levels. Again, banks may have wished to avoid supervisory interactions by limiting the use of their buffers and subsequently ensuring high LCR values of above 100%.

e. Optimisation of economic results: Under a stress scenario, banks might prefer to use their less liquid assets as collateral in central bank repos and obtain funding at low cost. These monies would be used to pay for their outflows at a lower cost than would result from liquidating the liquid assets either via private repos or sale.

2.1.2 Best practices to encourage

45. A minimum level of 100% LCR is legally required under normal circumstances. However, the liquidity buffer in the LCR Regulation is designed to be used by credit institutions under stress to meet their net outflows even if this leads to a situation where their LCR values would fall below 100% (see Article 412(1) of the CRR in conjunction with Recital 3 and Article 4(3) of Delegated Regulation (EU) 2015/61). The Regulation allows banks' LCRs to fall below 100% under stress and requires them to issue a communication to the relevant competent authorities as well as to submit a restoration plan in due course. The Regulation does not distinguish

[8] EBA-GL-2015-02 (link).

between idiosyncratic and systemic stress situations. However, it may be inferred from the various provisions that a value of below 100% reflects an idiosyncratic situation given that various flexibilities, exemptions or waivers are embedded in the LCR in order to mitigate the impact of general stress. This would be a point to clarify as it helps to inform how much below 100% the LCR could be without creating a stigma upon one or the other bank.

46. In the short to medium term, regulatory LCR public disclosure should not be a big concern for the usability of the buffer, in particular in the case of market-wide stress where various institutions would disclose an LCR of less than 100%, thus reducing the stigma for individual institutions. Hence, it is not recommended to amend the regulatory LCR disclosures in the first instance (also considering the specific framework provided by EU rules, which should precisely address crisis circumstances).

47. Banks should avoid any reluctance to internally escalate any required communication of lower LCR values to ensure due control by senior management. These situations should be reflected and described in the relevant liquidity contingency plans of the institutions. Indeed, the liquidity policy of banks should clearly reflect and describe how liquidity risk should be managed under stress to steer towards targeted LCR levels as closely as possible. Liquidity indicators, such as LCR values, triggering escalation processes within the institutions and subsequent recovery actions should be considered part of the normal management of liquidity risk under stress. That said, the EBA is currently reflecting on a possible update of the Guidelines on the minimum list of qualitative and quantitative recovery plan indicators.

48. The fact that LCR values fall below 100% as a result of a proper use of the liquidity buffer under stress to ensure sufficient liquidity in the real economy and the financial system is contemplated in the Regulation. As such, this situation should not be necessarily perceived by supervisors as liquidity mismanagement. Indeed, this could be seen as the expected LCR management under stress. At the same time, a case-by-case assessment considering the specific circumstances and business model of the relevant institution is indispensable.

49. Credit rating agencies and market participants should not penalise banks in the course of their assessments if banks' LCR values fall below 100% under stress. As indicated, LCR values under stress do not necessarily reflect poor liquidity positions or liquidity mismanagement. Other liquidity related aspects should be considered in their holistic assessment (e.g. qualitative information provided in the liquidity disclosures related to liquidity management). The EBA will investigate further to determine whether a specific communication could be useful in this regard.

2.2 Unwinding waivers. Policy guidance

2.2.1 Background – LCR liquidity buffer and unwinding of securities financing transactions and collateral swaps

50. The LCR seeks to ensure that banks hold a sufficiently large liquidity buffer in order to face net outflows under potential severe liquidity stress situations, both idiosyncratic and market-wide. The LCR design reflects this underlying calibration.

51. The LCR liquidity buffer is calculated as:

    a. the current holdings of liquid assets, minus

    b. the excess liquid asset amount.

52. The excess liquid asset amount is the amount of liquid assets that is held in excess of the limits provided in the LCR DR. To recall, a maximum of 15% and 40% of the liquidity buffer may consist of Level 2B and Level 2 assets, respectively, and a minimum of 30% of the adjusted liquidity buffer has to be held in form of Level 1 assets (excluding extremely high quality covered bonds). However, the excess liquid asset amount is not only calculated based on the current holdings of liquid assets. In fact, for the purpose of the calculation of the excess liquid assets amount, the LCR DR envisages an approach to unwind repos, reverse repos and collateral swaps maturing in the following 30 days for the calculation of the caps in the liquidity buffer and subsequently for the determination of the liquidity buffer.

53. The unwind mechanism[9] was introduced to mitigate arbitrage in banks conducting very short-term SFTs and collateral swaps. Banks -particularly those with low liquidity resources- might carry out a temporary increase of their HQLA and LCR values around the reporting date by temporarily pledging assets of low liquidity value while receiving assets of a higher liquidity value. These practices would increase the amount of HQLA for some days but would not provide the bank with liquidity for the full LCR 30-day period. In the context of the calculation of the excess liquid asset amount, the LCR DR requires the liquidity buffer to be comprised of sustainably available liquid assets for at least 30 days. The unwind mechanism adjusts the collateral repayments for the quantifications of the different categories of HQLA before applying the liquidity buffer caps and calculating the excess amount that should be deducted, if any. However, if it is not reinvested in non-HQLA, the liquidity received in short-term SFTs and collateral swaps against less liquid assets will be reflected in the current holdings of liquid assets.

2.2.2 LCR liquidity buffer and unwinding of central bank securities financing transactions and collateral swaps- rationale and common understanding

54. Short-term central bank repos collateralised by non-HQLA allow banks' liquid assets to be increased by the cash received. This amount will be reflected in the current holdings of liquid assets. In the context of the calculation of the excess liquid asset amount, the unwind mechanism assumes that no roll-over of the transactions will happen and that, therefore, in a

[9] Article 17(2) of LCR Delegated Regulation. The EBA published in November 2020 the report on 'the unwind mechanism of the LCR under Article 17(5) of the LCR DR (EU) 2018/1620' on the technical suitability on the unwind mechanism as set out in the EU LCR DR.

matter of a few days the situation will revert to the original one with the bank paying back the cash collateral and receiving the non-HQLA collateral.

55. When a bank seeks to finance a material share of its buffer with cheap and very short-term central bank funding, collateralised by low quality liquid assets, the liquidity received (and potentially retained) would be neutralised by the unwind mechanism[10]. For the purposes of the computation of the available liquidity buffer in the following 30 days, in the context of the calculation of the excess liquid asset amount, the LCR rules 'discount' the repayment of the funding obtained in the very short term. This might, in some cases, materially or even fully reduce the amount of the LCR liquidity buffer available for the following 30 days.

2.2.3 Waiver

56. Recital 5 of the LCR amending Act and paragraph 4 of Article 17 of the LCR DR envisage the possibility that competent authorities may waive the unwind mechanism, on a case by case basis, of repos of up to 30-days, reverse repos and collateral swaps where the counterparty is a central bank and where at least one leg is a liquid asset; hence including repos or reverse repos collateralised by non-liquid assets. Prior consultation with the relevant central bank is required. These provisions envisage the conditions and safeguards that need to be met for its application. The note aims to provide supervisors and institutions with some guidance upon which to build the application of the unwinding waiver from a supervisory policy perspective.

57. The main conditions or assumptions for the waiver are the following (guidance is added to each as described below):

- Transactions with the ECB or the central bank of a Member State can be expected to be rolled over under conditions of severe stress.
- Exceptional circumstances exist which pose a systemic risk affecting the banking sector of one or more Member States.
- The implementation of the LCR should not hinder the effective transmission of monetary policy to the economy.
- The waiver should be subject to appropriate safeguards in order to avoid possible regulatory arbitrage opportunities or adverse incentives for credit institutions.
- The waiver can apply to all or part of the repos, reverse repos or collateral swaps.

[10] The European Regulation envisages the application of the unwind mechanism to all securities financing transactions and collateral swaps where at least one leg is a liquid assets including, therefore, repos or reverse repos collateralised by non-liquid assets. Basel only requires unwinding those transactions if both legs comprise liquid assets, thus not including repos or reverse repos collateralised by non-liquid assets. This probably responds to the fact that under stress repos collateralised by non-liquid assets are not common. This might be different in the EU where central bank repos have reached high volumes under stress.

In the consultation that the supervisor needs to make to the central banks before granting the waiver, the supervisor:

- ***is expected to gain some evidence from the central bank that the renewal of central bank transactions is reasonably expected in practice during a systemically stressed scenario;***

- ***should double check that its authorisation is not expected to have detrimental impacts on the implementation of monetary policy.***

During a normal scenario, in the absence of a systemic risk, the LCR unwinding waiver is not expected to be granted.

Supervisors should assess that recourse to central bank funding is indeed the only way for banks to obtain funding.

A waiver should not be granted if supervisors have reason to expect arbitrage from the relevant funding transactions (optimisation of resources without effective use for expected targets)

58. **Roll over of transactions with central banks under severe stress** are generally expected in the LCR. Indeed, these transactions do not trigger outflows in the LCR. Some clarifications are needed.

59. In the first instance, the LCR is based on liquidity driven from the private markets. Banks should not depend on central bank funding during normal times as the means to hold the necessary liquidity buffer for the purposes of meeting their outflows under future market-wide and idiosyncratic stress, i.e. the ordinary underlying LCR scenario.

60. However, during a systemically stressed scenario, where banks might have difficulty in accessing funding markets, the LCR DR seems to recognise that monies received and retained in the context of short-term central bank SFTs/collateral swaps could be allowed to be reflected as available for payment of other than central bank outflows during the 30 calendar day LCR period. These transactions would be expected to be rolled over and, therefore, would not be unwound. Recital 5 of the LCR amending Act, in this context, requires competent authorities to consult the relevant central bank. Therefore, from this dialogue the supervisor gains some evidence that the renewal of those transactions is reasonably expected in practice.

61. On the other hand, in a normal scenario, the LCR unwinding waiver is not expected to be granted as there are no exceptional circumstances that pose a systemic risk to the banking sector of one or more Member States, which is actually a pre-condition for granting this waiver. Only under severe stress might CAs/supervisors consider the possibility of the waiver.

62. **Exceptional circumstances exist which pose a systemic risk affecting the banking sector of one or more Member States**. Banks, benefitting from material central bank liquidity (e.g. ELAs) and

that reuse a significant part of it, but not for investing in HQLA, might see their LCR liquidity buffer heavily reduced or even fully eliminated when unwinding those central bank transactions.

63. CAs/supervisors should consider that not waiving relevant banks from unwinding could discourage them from having recourse to the central bank and deprive them from obtaining (and reusing) the necessary funding, which could trigger negative systemic consequences. These negative systemic consequences could, in particular, arise where during periods of stress banks favour compliance with the 100% LCR level, rather than making use of the flexibility of operating below it.

64. On the other hand CAs/supervisors should definitely consider that recourse to central bank funding is indeed the only way for banks to obtain funding, in particular when the minimum market conditions for issuance or funding banks in private markets are not met. This will support the exceptional case situation.

65. **Transmission of monetary policy to the economy.** Recital 5 of the LCR amending Act establishes that 'the implementation of Delegated Regulation (EU) 2015/61 should not hinder the effective transmission of monetary policy to the economy.'

66. In its mandatory consultation with the relevant central bank, in the context of a potential unwinding waiver, the CAs/supervisors should double check that its authorisation is not expected to have detrimental impacts on the implementation of monetary policy.'

67. **Arbitrage opportunities or the creation of adverse incentives in credit institutions.** Recital 5 of the LCR amending Act sets out that the use of the waiver should be subject to appropriate safeguards to avoid the triggering of arbitrage opportunities or the creation of adverse incentives in credit institutions.

68. CAs should assess whether there are reasons to expect arbitrage from the application of the waiver. In particular, waivers do not seem appropriate in the cases where supervisors understand that institutions have recourse to central bank funding to optimise funding costs only. Equally important is that waivers should be associated with cases where central bank funding is effectively used.

69. **Partial or full waiver**. Article 17(4) of the LCR DR establishes that the waiver can be granted partially, to one or more SFTs and collateral swaps, or in full, for all the transactions of this type conducted by the relevant bank.

70. When assessing whether an unwinding waiver should be authorised, CAs/supervisors should also make sure that the waiver is not used for the purposes of financing the LCR liquidity buffer itself but to avoid unintended effects of the unwind mechanism on short-term central bank SFTs. Recital 3 of the LCR DR indicates that during LCR stress periods '*a credit institution should be able to convert quickly its liquid assets into cash without recourse to central bank liquidity or public funds, which may result in its liquidity coverage ratio falling temporarily below the 100%*

level…' Central bank funding should not replace the usage of the existing buffers to meet LCR stressed net outflows.

71. In order to avoid the potential unintended effects described, supervisors and central banks should strive to operationalise the authorisation process of the unwinding waiver under a short timeframe.

2.3 Central bank support risks in LCR

72. The EBA looks at the interaction of central bank support and the LCR and long-term funding structure.

2.3.1 Recent evidence of central bank support in the COVID crisis

73. Particular attention has been paid to open market operations and especially the ECB TLTRO III tranches settled from March 2020[11] (those settled in March, June and September 2020, at the date of preparation of this report).

Euro operations

Ref.	Type	Settlement date	Maturity date	Days	Allotted amount	Outstanding amount
20200235	MRO	18/11/2020	25/11/2020	7	0.47 bn	0.47 bn
20200229	LTRO	05/11/2020	29/07/2021	266	0.75 bn	0.75 bn
20200225	LTRO	29/10/2020	28/01/2021	91	0.09 bn	0.09 bn
20200215	LTRO	08/10/2020	26/08/2021	322	1.01 bn	1.01 bn
20200211	LTRO	01/10/2020	17/12/2020	77	0.51 bn	0.51 bn
20200207	LTRO	30/09/2020	27/09/2023	1092	174.46 bn	174.46 bn
20200195	LTRO	03/09/2020	26/08/2021	357	0.79 bn	0.79 bn
20200190	LTRO	27/08/2020	26/11/2020	91	0.24 bn	0.24 bn
20200174	LTRO	06/08/2020	30/09/2021	420	5.68 bn	5.68 bn
20200131	LTRO	24/06/2020	28/06/2023	1099	1308.43 bn	1308.43 bn
20200136	LTRO	24/06/2020	30/09/2021	463	15.61 bn	15.61 bn
20200098	LTRO	21/05/2020	30/09/2021	497	0.85 bn	0.85 bn
20200029	LTRO	25/03/2020	29/03/2023	1099	114.98 bn	114.98 bn

74. Generally, banks should consider the impact of central bank funding in the price of liquidity for the purposes of the internal pricing of their products.

2.3.2 Possible LCR readings of central bank support

[11] https://www.ecb.europa.eu/mopo/implement/omo/html/top_history.en.html

75. The injection of liquidity solely via the TLTRO tranches in March, June and September comes to EUR 1.6 trillion. From a supervisory and policy perspective, it is interesting to establish how much of the LCR values correspond to liquidity received from the central bank and how the current values of the LCR reported by banks could be interpreted.

76. Two estimates-based approaches have been followed for this analysis based on a sample of banks in September 2020, using as a starting point: i) the variation of non-level 1 sovereign collateralised repos as reported in the COREP maturity ladder between 2 and 5 years, and ii) the variation of central bank assets and withdrawable central bank reserves as reported in the LCR templates, as a contribution to LCR levels. Both approaches have shown that the average LCR reported, adjusted for central bank support, decreases by roughly 40 percentage points but remains substantially above the minimum (roughly 30 percentage points above the minimum of 100%).

77. Banks in the EU held strong enough liquidity buffers before the COVID-19 related crisis episodes. The liquidity injected by the central bank has reinforced their buffers. However, it should not lead generally to a different reading of the liquidity position of banks if compared with LCR values without central bank support. Supervisors are advised to remain observant of particular cases that might deserve special attention. Looking at the adjusted LCR, to neutralise the addition of central bank support, could help provide a true understanding of the idiosyncratic position of banks when it comes to liquidity stress.

2.3.3 Long-term funding

78. A similar estimates-based approach has been used to illustrate the implication of the TLTRO tranches in the funding structure of banks, again using the variation of repos maturing between 2 and 5 years as an estimation of the funding received, while the total funding is derived from the information reported as total outflows by time bucket in the maturity ladder. The long-term (3 year) TLTRO tranches represent on average 7% of the total funding maturing at over one year plus all retail deposits with maturities of less than one year. This percentage is 12% if only funding maturing at over one year is considered.

79. Supervisors should monitor particular cases where these percentages might be significantly higher. Dependency on central bank long-term funding could potentially trigger elevated refunding costs in a future scenario to maintain a potential long-term assets/funding structure. Monitoring the use of the funding received, particularly if reinvested in long-term assets, and the capacity to access private stable funding, in the absence of a renewal of central bank funding in the long term under normal scenarios, seems relevant in these cases.

2.4 Additional outflows from derivatives due to adverse market scenarios

80. Articles 423(3) of the CRR and 30(3) of the LCR DR, as well as relevant RTS on additional liquidity outflows[12], constitute the EU base Regulation on this point.

81. In the earlier weeks of the crisis (March-April 2020), and particularly in funding markets, margin calls increased drastically. This increase in collateral required in funding markets could trigger LCR implications for the following two years, with the risk of some procyclicality effects. The Regulation requires the computation of the relevant additional outflows due to collateral needs, if the derivatives transactions are material, and measured as such if the notional amount exceeds 10% of the net outflows at any time in the previous two years. Also, the relevant outflows in these cases are defined as the largest absolute net 30-day collateral flow realised during the previous 24 months.

82. This means that the episode affecting the markets in March/April could trigger material outflows under this item during the next 2 years, irrespective of the future volume of the derivatives portfolios in banks and of the future behaviour of the markets. The calibration responds to the behaviour of markets seen in times of crisis (with a time horizon across the previous 24 months) and based on the size of the portfolios at that time.

83. Between February and April 2020, the amounts reported as additional outflows increased on average by 24% (also 24% between February and September 2020). In some cases, these percentages are significantly higher for some banks. In other cases, unexpectedly, some banks seem not to report any increase. At this stage, supervisors and banks should be encouraged to monitor these amounts as established in the Regulation.

84. The EBA will closely monitor the implications of these additional outflows in banks' LCRs, particularly taking into account the trends in collateral required in these transactions in the markets and of the size of derivatives portfolios in banks over time. The EBA will assess potential procyclicality effects and will act as necessary in due course. On the one hand such exceptional picks may not be usefully taken on board in all their impact, and on the other hand markets may indeed navigate a quite uncertain period, which would warrant that the increased potential outflows are well reflected.

[12] Commission Delegated Regulation (EU) 2017/208 of 31 October 2016 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for additional liquidity outflows corresponding to collateral needs resulting from the impact of an adverse market scenario on an institution's derivatives transactions.

SECOND SECTION

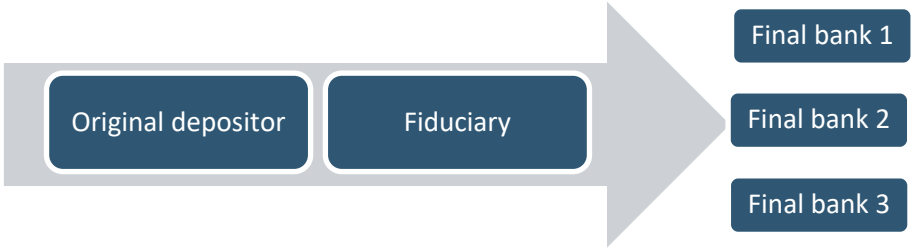
Specific practices or approaches for which guidance is provided: treatment of fiduciary deposits, LCR optimisation risk, interdependent inflows and outflows, treatment of DGS deposits

3. Fiduciary deposits

3.1 Background

85. Practices are observed where a legal entity, as a fiduciary, manages assets on behalf of third parties, including deposit placement activities.

86. Generally, fiduciary deposits could be represented as follows in a simplistic manner:



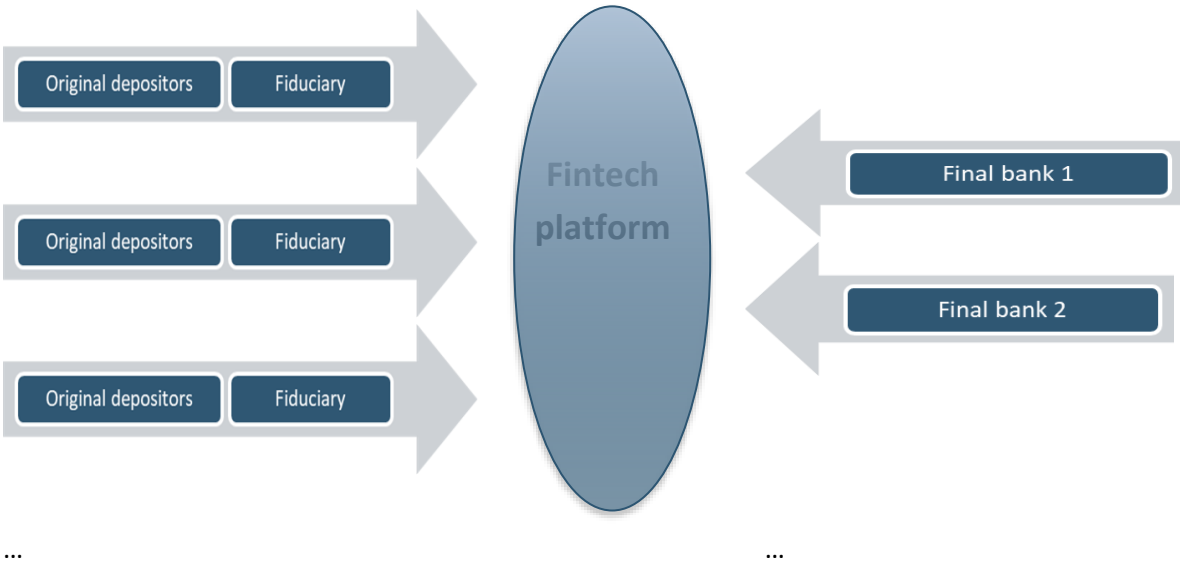
where the monies originally stem from the 'original depositor' and are deposited with a 'final bank' with the participation of (and via) a 'fiduciary'. Fiduciary deposits can be placed in various forms, e.g. in the form of term deposits or as money at call without a fixed maturity.

87. In practice, somewhat more sophisticated schemes can be observed where the final banks place deposit interest rate offers on an online platform of a Fintech and the original depositors place their monies with the final banks with the intervention of the fiduciary.

88. The platform provides high technology services to eventually connect the fiduciary and final banks to place the deposits. Fiduciary banks usually use their online banking units/subsidiaries to provide fiduciary deposits to the original depositor.

89. These platforms intend to provide final banks with access to deposit funding without the need to have an extensive infrastructure in each market. Simultaneously, they aim to provide the original depositors with market-leading interest rates from all over Europe without the need to switch/have multiple bank accounts across various final banks. Original depositors just have to open a centralised account in the fiduciaries (either with the institution itself or the account is opened with a predetermined partner institution of the fiduciary) that in turn have accounts[13] in the final banks, thus giving the original depositors access to a portfolio of deposit products. These schemes may vary considerably in relation to the underlying contractual arrangements as well as the legal rights and obligations of the parties involved.

[13] These are mostly pooled accounts opened on behalf of clients (client deposit accounts). These accounts are managed by the fiduciary (including withdrawals of funds) who are responsible for carrying out due diligence.



90. In the context of fiduciary deposits, institutions and supervisors have raised concerns on the applicable LCR treatment, particularly the relevant outflow rate, from the perspective of the final bank receiving these deposits.

91. This issue is material in two ways:

(i) the amount that these transactions could reach; and

(ii) the large difference in outflows rates that could be applied in the absence of clarity about the correct application of the legal framework. Indeed, a wrong reading of the rules could involve the application of outflow rates ranging from 5% (if fiduciary deposits are considered as stable retail deposits) to 100% if the counterparty is considered to be a financial customer, and 20%/40% if it is considered a non-financial customer.

92. Hence, a clarification of the treatment of these transactions seems necessary to avoid any incorrect interpretation of the regulation that would lead to an uneven playing field if banks follow very different approaches resulting in very different requirements.

93. Policy guidance is provided to clarify the LCR and also the treatment of NSFR from the perspective of all the parties involved in these transactions, i.e. the final banks and also the original depositors and fiduciaries.

3.2 Basics to be considered

94. There are different elements that should be considered regarding fiduciary deposits to understand the LCR inflow/outflow rates and NSFR ASF/RSF factors that should be applied by the institutions involved.

a. Original depositor:

95. The original depositor could be a non-financial customer, such as a natural person, a non-financial corporate, a PSE, a sovereign or a financial customer. However, in the case of an institution acting as the original depositor, the transaction is not expected to be a fiduciary deposit but an interbank deposit, from the perspective of both the fiduciary (where it is an institution subject to the LCR) as well as the final bank. This is because there is a reasonable assumption that the deposit will be ultimately managed by the original depositor rather than by the intermediary.

b. Fiduciary:

96. Fiduciaries are entities that provide asset management on behalf of another party. The Basel LCR standard refers to 'Fiduciary', in paragraph 40.42 of the consolidated framework, as '*a legal entity that is authorised to manage assets on behalf of a third party. Fiduciaries include asset management entities such as pension funds and other collective investment vehicles'*.

97. A fiduciary might be a financial customer or any specialised agent (non-financial customer or natural person).

c. Final bank:

98. This is always a credit institution and hence, a financial customer.

3.3 Legal basis

99. The LCR Delegated Regulation (LCR DR) and the CRR generally establish the applicable inflow/outflow rates (LCR) and ASF/RSF factors (NSFR) depending on the type of client/counterparty of the relevant transaction that a credit institution or an investment firm subject to the LCR and NSFR[14] (all these institutions are referred to as 'LCR institutions' and 'NSFR institutions' in this document) is involved in.

Generally, fiduciary deposits follow the regulated 'deposit broker structure'…

100. Neither the CRR nor the LCR DR contains an explicit definition of a 'fiduciary'. Yet, Article 411(4) of the CRR defines 'deposit broker' as 'a natural person or an undertaking that places deposits from third parties, including retail deposits and corporate deposits but excluding deposits from financial institutions, with credit institutions in exchange of a fee'. This legal definition of 'deposit broker' seems to generally target the economic notion of 'fiduciary deposits'. The CRR refers to deposits placed on behalf of third parties, in line with the Basel reference to deposits managed on behalf of third parties in the latter.

…However, not all fiduciary deposits are considered 'deposit broker' structures…

[14] Investment firms that are authorised to provide the investment services and activities listed in points (3) and (6) of Section A of Annex I to Directive 2014/65/EU are subject to the LCR DR and to the NSFR provisions in the CRR at an individual and consolidated level in accordance with Articles 6(4), 11(4) and 412(4a) of the CRR.

101. Article 411(4) of the CRR does not set any limit or restriction on the types of entities acting as deposit brokers. These, therefore, include natural persons and undertakings, either financial or non-financial. However, Article 411(4) excludes from the deposit broker structure deposits where the original depositor is a financial institution[15].

102. The treatment of the fiduciary deposit structures is described in points 3.4 (LCR) and 3.6 (NSFR).

…and not all deposits intermediated are considered as fiduciary deposits and accordingly as 'deposit broker' structures.

103. As highlighted in point 3.2, where the original depositor is an institution, the deposit is not expected to constitute a fiduciary deposit but an interbank deposit. Therefore, the structure of a deposit broker is not expected to occur in this case as is also confirmed by Q&A 2016_2642[16] on the definition of a deposit broker. The treatment of these structures is therefore addressed separately in points 3.5 (LCR) and 3.7 (NSFR).

104. Article 28 (1) of the LCR DR envisages the specific treatment of outflows resulting from deposits from customers that are deposit brokers (where the deposits can be withdrawn within 30 calendar days). Therefore, this provision, read together with Article 411 (4) of the CRR, sets out the outflow treatment of brokered deposits. The prescribed treatment is irrespective of whether the deposit broker is a financial or non-financial (retail or wholesale) customer and prevails over other general provisions on retail deposits or wholesale deposits (either financial or non-financial customers) in the LCR DR.

105. Articles 428l(b)(vi), 428ad(c)(vi) and 428am(b)(vi) of the CRR, on the NSFR, envisage specific treatment where the counterparty is a deposit broker. This treatment is irrespective of whether the deposit broker is a financial or non-financial (retail or wholesale) customer and prevails over other general provisions on retail deposits or wholesale deposits (either financial or non-financial customers) in the context of the NSFR in the CRR.

106. As a general rule, banks are required to identify their customers. Where the customer is opening an account on behalf of another party, banks are required to identify the beneficial owner of the account[17]. Therefore, banks are assumed to be in a position to identify a brokered deposit, including information on the original depositors.

[15] Article 4(1)(26) of the CRR defines a 'financial institution' as 'an undertaking other than an institution and other than a pure industrial holding company, the principal activity of which is to acquire holdings or to pursue one or more of the activities listed in points 2 to 12 and point 15 of Annex I to Directive 2013/36/EU, including a financial holding company, a mixed financial holding company, a payment institution as defined in point (4) of Article 4 of Directive (EU) 2015/2366 of the European Parliament and of the Council and an asset management company, but excluding insurance holding companies and mixed-activity insurance holding companies as defined, respectively, in points (f) and (g) of Article 212(1) of Directive 2009/138/EC'.

[16] Q&A 2016_2642 indicates that in the context of deposits from financials via a deposit broker '*the definition of deposit brokers should be restricted to a narrow interpretation*'.

[17] GL4.7 and GL 4.17, among others, in the draft revised EBA guidelines on money laundering and terrorist financing risk factors (link).

107. In accordance with the previous paragraphs and the legal provisions referred to, the following approaches should be applied in the context of brokered deposits received by credit institutions and for the purposes of determining the typology of the relevant fiduciaries in the context of the LCR and NSFR:

(i) **Fiduciary as a deposit broker.** This approach should apply in cases where the original depositor is not a financial institution pursuant to Article 411(4) of the CRR. As stated above, this would also not include cases where the original depositor is an institution as such structures would not be expected to fall into the category of fiduciary deposits.

(ii) **Fiduciary as a financial customer**. This approach should apply in cases where the original depositor is a financial institution. These cases are directly excluded from the 'deposit broker' structure pursuant to Article 411(4) of the CRR. Here, the fiduciary meets the definition of 'financial customer' set down in Article 411(1) of the CRR. In these cases, the fiduciary would either fall into the categories of entities listed in Article 411(1) or its main business would be included in the activities listed in Annex I to Directive 2013/36/EU (e.g. portfolio management and advice, money broking, trading for the account of customers, etc.) reserved for financial customers pursuant to Article 411(1) of the CRR. Again, as stated above, this would be the same approach as that established for cases where the original depositor is an institution, where these structures are expected to fall into the category of interbank deposits.

108. The report includes policy guidance to clarify:

- which specific inflow/outflow rates in the LCR should be applied in the context of fiduciary deposits by the fiduciary, the original depositor and the final bank;
- which specific inflow/outflow rates in the LCR should be applied in cases of deposits intermediated where the original depositor is an institution, in which case they should be treated as interbank deposits and not as fiduciary deposits;
- which specific RSF/ASF factors in the NSFR should be applied in the context of fiduciary deposits by the fiduciary, the original depositor and the final bank;
- which specific RSF/ASF factors in the NSFR should be applied in cases of deposits intermediated where the original depositor is an institution, in which case they should be treated as interbank deposits and not as fiduciary deposits.

3.4 Application of LCR inflow and outflow rates in the context of fiduciary deposits. Policy guidance

The report includes policy guidance to clarify which specific inflow/outflow rates in the LCR should be applied in the context of fiduciary deposits by the fiduciary, the original depositor and the final bank.

The final bank should apply Article 28(1) LCR DR (40%/20% outflow rate), without prejudice to potential specific liquidity requirements in the context of the SREP liquidity assessment, if the fiduciary is a deposit broker. If the fiduciary is a financial customer, then the final bank will apply Article 31a(1) (100% outflow rate).

The fiduciary will apply a 100% inflow rate pursuant to Article 32(2)(a) of the LCR DR unless the fiduciary manages the deposits but ultimately only acts on an explicit request from the original depositor, in which case the inflows would be contingent and cannot be recognised in the LCR. The fiduciary should recognise outflows, from the deposits intermediated and received from the original depositor, based on the type of counterparty/original depositor. Additional outflows should be recognised (Article 23 of the LCR DR) reflecting the contingent outflows stemming from the part of the deposits not repaid to the original depositor but reinvested in other deposits as part of the business of the fiduciary under stress (market-wide but also idiosyncratic).

The original depositor is not subject to the LCR since if it is an institution the deposit is not considered a fiduciary but an interbank deposit.

3.4.1 Application of LCR outflows rates by the final bank on fiduciary deposits received

109. The following approaches should be applied in the context of the LCR by credit institutions to establish the outflows from fiduciary deposits received:

- **Fiduciary as a deposit broker.** In this case, any deposit that can be withdrawn within 30 calendar days is considered to have been received from a deposit broker and, pursuant to Article 28(1) of the LCR DR, a 40% outflow rate (or 20% if the full amount is covered by a deposit guarantee scheme [DGS] in accordance with Directive 94/19/EC or Directive 2014/49/EU or an equivalent deposit guarantee scheme in a third country applies). Q&A 2017_3357 clarifies that a 20% rate applies only if the entire amount of the liabilities against each depositor, including deposits received via deposit brokers or directly, is fully covered by a DGS. For these purposes, the final bank should assess the amount covered by a DGS at the level of each original depositor, in accordance with Q&A 2015_2452.

- Furthermore, it should be noted that Article 27(6) of the LCR DR explicitly excludes brokered deposits from the treatment of operational deposits.

- In the particular case of fiduciary deposits where deposits are considered to have been received from a deposit broker, competent authorities may assess, as part of their SREP liquidity assessment of the final bank (as a credit institution), the materiality of the risks posed by those transactions to its liquidity, with particular consideration of the nature and degree of sophistication of the original depositor as well as the role of the fiduciary and the contractual arrangements of the structure that might trigger higher LCR outflows than the default values, and determine the need for setting institution-specific liquidity requirements[18], in the form of a higher minimum LCR value or by requiring a higher LCR liquidity buffer, to cover such risks in accordance with Articles 104(1)(k) and 105 of Directive 2013/36/EU, and as further specified in the EBA SREP Guidelines[19].

- **Fiduciary as a financial customer**. In these cases, the general outflow treatment for deposits from financial customers established in Article 31a(1) of the LCR DR (i.e. 100% outflow rate) applies with regard to the fiduciary deposits received.

3.4.2 Application of LCR inflow rates and outflow rates by the fiduciary (if a 'LCR institution') on the fiduciary deposits intermediated

110. If the fiduciary is an 'LCR institution', it should apply a 100% inflow rate on the amount of the deposits intermediated and placed with the final bank in accordance with Article 32(2)(a) of the LCR DR on inflows from financial customers.

111. Furthermore, to the extent that the original depositor can trigger deposit withdrawals within 30 calendar days, the fiduciary should recognise outflows, from the deposits intermediated and received from the original depositor, based on the type of counterparty/original depositor. The outflow rate that should be applied here would be the following: (i) 100% if the original depositor is a financial customer (pursuant to Article 31a(1) of the LCR DR); (ii) the relevant outflow rate for retail deposits (pursuant to Articles 24 and 25 of the LCR DR) if the original depositor is a retail depositor; or (iii) 40% (or 20%, if fully covered by

[18] In accordance with the terms established specifically in Articles 104(1)(k) and 105 of the CRD and paragraph 472 of the EBA SREP Guidelines ('*EBA GL on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing*', consolidated version from 19 July 2018.) and more generally in Titles 8 and 9 of the EBA SREP Guidelines, competent authorities may impose specific liquidity requirements. From those provisions it can be concluded that special liquidity requirements should: i) be institution-specific (and therefore they are not meant to be used for setting a supervisory policy), ii) be applied in a way that is proportionate to each institution's business model (and strategy), iii) take into account the institution's own assessment of liquidity risks (and its management of risks), and iv) be based on the SREP liquidity assessment (which goes beyond the minimum requirements set out in the LCR DR and gives the competent authorities a comprehensive view of an institution's liquidity risks). In this regard, competent authorities are empowered to adopt such specific liquidity requirements to cover those risks not covered or not adequately covered by Pillar 1. These specific liquidity requirements cannot undermine the Pillar 1 requirements –the LCR DR). Paragraph 485 of the EBA GL specifies that these requirements need to be formulated in the form of a higher minimum LCR, or covering a different survival period than in the LCR or via requiring a higher LCR liquidity buffer.

[19] Special observation of upcoming EBA GL on SREP should be made in the future in the formalisation of special liquidity requirements.

a DGS), if the original depositor is another non-financial customer (pursuant to Article 28(1) of the LCR DR).

112. For the purposes of establishing the LCR outflow rate by a fiduciary that is an 'LCR institution' with regard to deposits received from an original depositor that is a retail client, and where the fiduciary deposit is framed in a Fintech platform, it should be noted that conditions established in points b) and c) of paragraph 2 of Article 25 of the LCR DR should be considered to have been met. These deposits are expected to be internet-only accounts and to offer higher yields than the average rate of similar products as part of their normal functions. In accordance with paragraph 3 of this Article, the fiduciary needs to apply an outflow rate between 10% and 15% or, if any additional condition of paragraph 2 is met, between 15% and 20%. It should also be noted that, as indicated in the last subparagraph of paragraph 3 of Article 25 of the LCR DR, '*on a case by case basis, competent authorities may apply a higher outflow rate where justified by the specific circumstances of the credit institution*'.

113. The fiduciary should recognise additional outflows pursuant to Article 23 of the LCR DR. They reflect the contingent obligations/outflows that would arise under stress as part of the business of the fiduciary, for the amount withdrawn and not repaid to the original depositor but reinvested in other deposits on behalf of the original depositor. The inflows recognised by the fiduciary would be ultimately neutralised by the outflows to the original depositor and these additional outflows from the reinvestment of deposits withdrawn from the final bank.

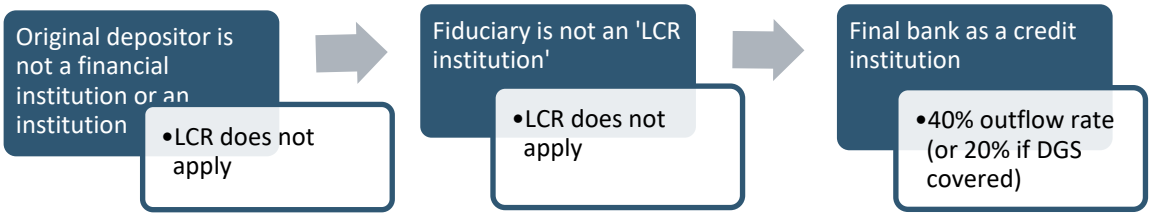
114. Particularly in those cases where the fiduciary manages the deposits but ultimately only acts upon explicit request from the original depositor (based on the contractual arrangements of the relevant fiduciary scheme), the fiduciary will not be able to recognise any inflows since they are dependent on the decision taken by the original depositor.

115. By derogation of the above, following the last subparagraph of Article 25(4) of the LCR DR, an outflow rate of 100% should be applied by the fiduciary if the fiduciary deposit, where the original depositor is a retail customer, has been cancelled with a residual maturity of less than 30 calendar days and where the payout has been agreed with another credit institution.

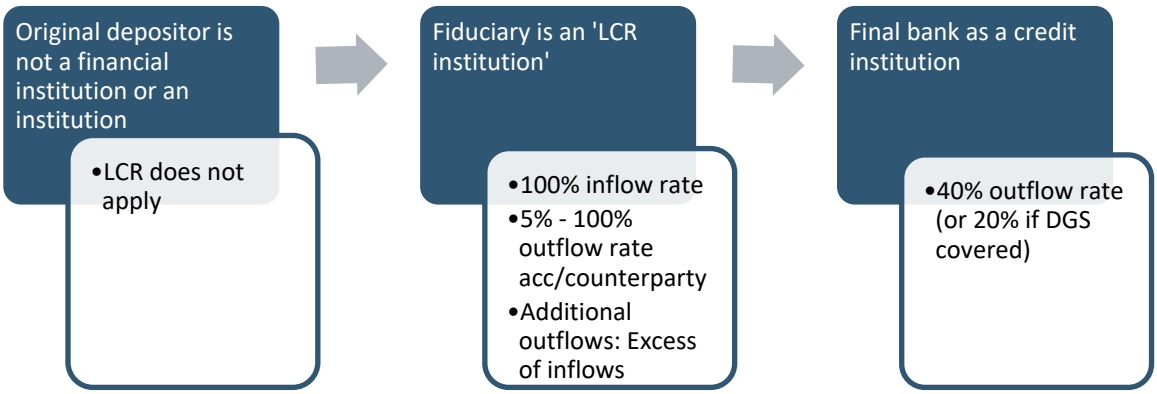
3.4.3 Summary

117. The following charts show the main types of fiduciary deposits as described in the previous paragraphs with the relevant inflow/outflow rates that should apply for any fiduciary deposits that could be withdrawn within 30 calendar days:

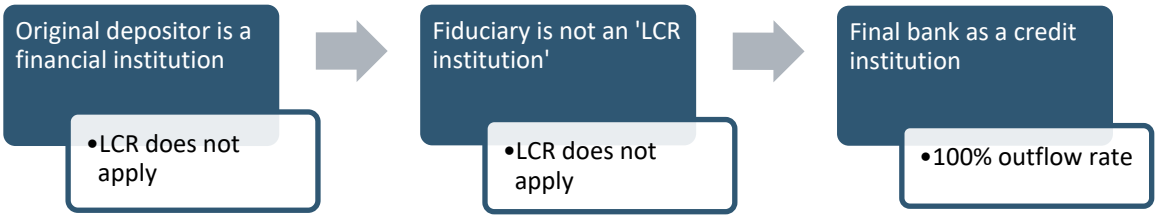
Case I – Deposit broker structure (Fiduciary is not an 'LCR institution')



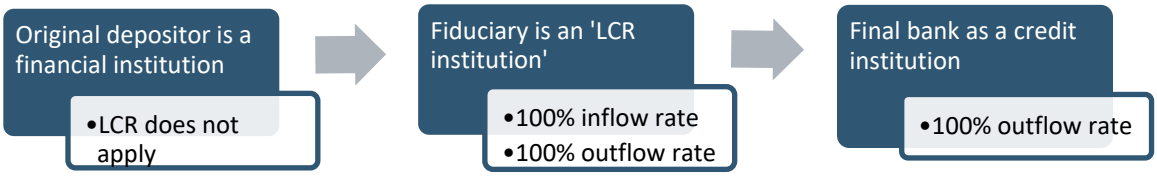
Case II – Deposit broker structure (Fiduciary is an 'LCR institution')[20]



Case III – Fiduciary as a financial customer (Fiduciary is not an 'LCR institution')



Case IV – Fiduciary as a financial customer (Fiduciary is an 'LCR institution')[8]



[20] The fiduciary would reflect no inflows for the case specified in paragraph 114.

3.5 Application of LCR inflow and outflow rates in the context of interbank deposits. Policy guidance

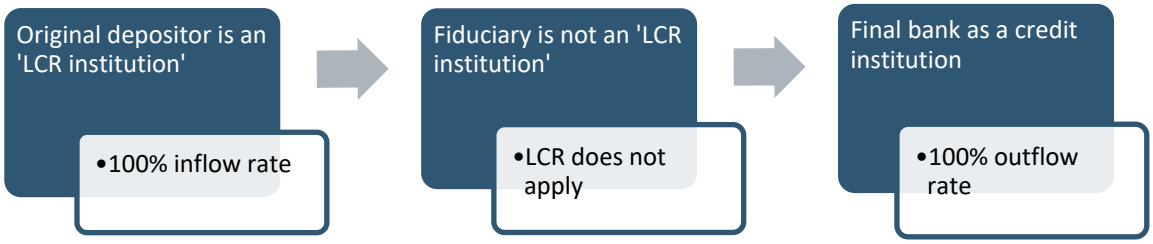
If the original depositor is an institution the deposit is not considered a fiduciary but an interbank deposit.

In this case, a 100% inflow/outflow rate should be applied by the original depositor and the final bank. If the intermediary is subject to the LCR then it will apply a 100% outflow rate and also a 100% inflow rate unless it only acts on an explicit request from the original depositor, in which case the inflows are contingent and cannot be recognised in the LCR.

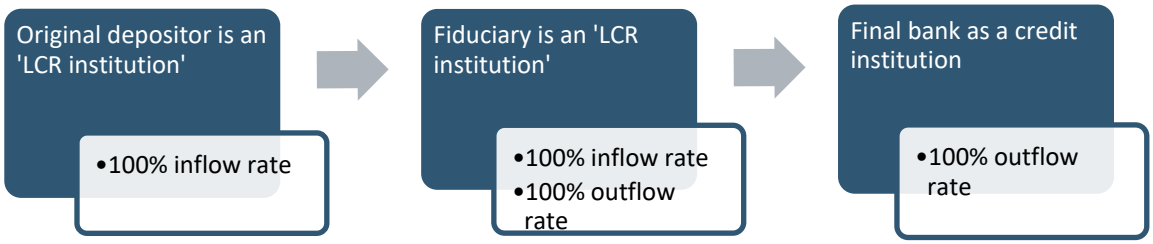
118. Where the original depositor is an institution, the deposit is expected to be an interbank deposit. Provided that deposits can be withdrawn within 30 calendar days, the final bank will apply a 100% outflow rate to this interbank deposit (Article 31a(1) of the LCR DR) and the original depositor, as an 'LCR institution', will apply a 100% inflow rate to this interbank deposit (Article 32(2)(a) of the LCR DR). If the intermediary is an 'LCR institution', a 100% inflow rate and outflow rate will apply in accordance with the same provisions.

119. Particularly, in those cases where the fiduciary manages the deposits but ultimately only acts on an explicit request from the original depositor (based on the contractual arrangements of the relevant fiduciary scheme), the fiduciary will not be able to recognise any inflows since they are dependent on the decision taken by the original depositor.

Case I – Interbank deposit (Intermediary is not an 'LCR institution')



Case II – Interbank deposit (Intermediary is an 'LCR institution')[21]



[21] The fiduciary would reflect no inflows in the case specified in paragraph 119.

3.6 Application of NSFR ASF and RSF factors in the context of fiduciary deposits. Policy guidance

The report includes policy guidance to clarify which specific RSF/ASF factors in the NSFR should be applied in the context of fiduciary deposits by the fiduciary, the original depositor and the final bank.

The final bank should apply a 50% ASF factor, without prejudice to potential specific liquidity requirements in the context of the SREP liquidity assessment, if the fiduciary is a deposit broker. If the fiduciary is a financial customer, then the final bank will apply will generally apply a 50% ASF factor if the residual maturity is between 6 and 12 months and 0% if below 6 months. In all cases a 100% ASF factor applies if the residual maturity is of one year or more.

The fiduciary should apply a 10%, 50% or 100% RSF factor (for the correlative three NSFR time buckets) unless the fiduciary manages the deposits but ultimately only acts on an explicit request from the original depositor, in which case the deposits will be considered not to have a stated maturity and a 100% RSF factor applies. The fiduciary should recognise ASF, from the deposits intermediated and received from the original depositor, based on the type of counterparty/original depositor and residual maturity. In addition, RSF should be recognised (Article 428p(10) of the CRR) reflecting the contingent obligation to reinvest in other deposits on behalf of the original depositor, the deposits that are withdrawn and not repaid to the original depositor.

The original depositor is not subject to NSFR since, if it is an institution, the deposit is not considered a fiduciary but an interbank deposit.

3.6.1 Application of NSFR ASF factors by the final bank on fiduciary deposits received

120. Fiduciary deposits received with a residual maturity of one year or more will receive a 100% ASF factor pursuant to Article 428o(e) of the CRR (and Article 428ap(e), in the simplified calculation of the NSFR). The final banks should apply the following available stable funding factors on fiduciary deposits received with a residual maturity of less than one year:

- **Fiduciary as a deposit broker.** In this case, the deposit received should be considered as a liability provided by a deposit broker following Article 428l(b)(vi) of the CRR (and Article 428am(b)(vi), in the simplified calculation of the NSFR) and a 50% ASF factor would apply. Competent authorities may assess, as part of their SREP liquidity assessment of the final bank (as a credit institution), the materiality of the risks posed by those transactions to its liquidity and determine the need for setting institution-specific liquidity requirements,

in the form of stricter NSFR requirements, to cover such risks in accordance with Articles 104(1)(k) and 105 of Directive 2013/36/EU, and as may be specified in the EBA SREP Guidelines.

- **Fiduciary as a financial customer**. In these cases, if the residual contractual maturity of the liability is at least six months but less than one year, the ASF factor for liabilities provided by financial customers is envisaged in Article 428l(c)(iii) of the CRR, i.e. a 50% ASF factor. If the residual contractual maturity of the liability is less than six months, the ASF factor in Article 428k(3)(c)(iii) of the CRR applies, i.e. a 0% ASF factor. In the case of simplified NSFR, Article 428al(3)(c)(iii) of the CRR, with a 0% ASF factor, applies if the residual contractual maturity is less than one year.

3.6.2 Application of NSFR RSF and ASF factors by the fiduciary (if a 'NSFR institution') on the fiduciary deposits intermediated

121. The fiduciary should apply a 10%, 50% or 100% RSF factor (for the correlative three NSFR time buckets) on the amount of the deposits intermediated and placed with the final bank in accordance with Articles 428v(a), 428ad(d)(iii) and 428ah(1)(b) of the CRR on RSF on monies due from transactions with financial customers.

122. Furthermore, it should recognise ASF, from the deposits intermediated and received from the original depositor, based on the type of counterparty/original depositor and residual maturity generally of 50% if the residual maturity is less than one year (Article 428l(b) of the CRR), unless the counterparty is retail (90% or 95%; Articles 428m and 428n of the CRR) or a financial customer with a residual maturity of less than six months (0% pursuant to Article 428k(3)(c)(iii) of the CRR). In the case of simplified NSFR, a 50% ASF applies if the residual maturity of the liability is less than one year (Article 428am(b) of the CRR), except if it stems from financial customers (0%, Article 428al(3)(c)(iii) of the CRR) or is retail (90%-95%; Articles 428an and 428ao of the CRR). 100% ASF applies if the residual maturity of the liability is of one year or more (Articles 428o(e) and 428ap(e) of the CRR).

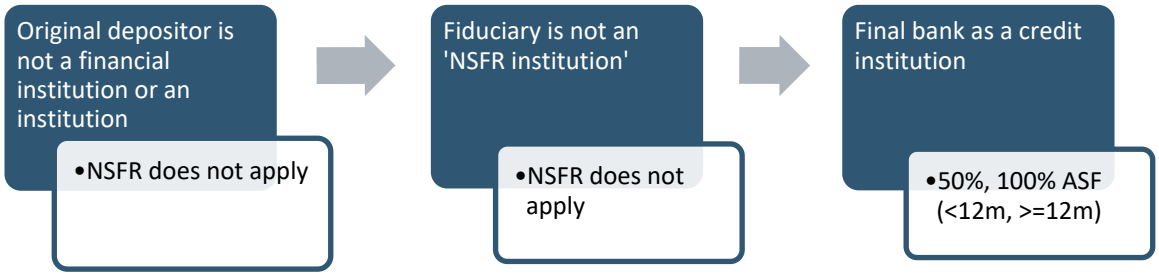
123. In accordance with paragraph 10 of Article 428p of the CRR, the fiduciary should also recognise the required stable funding on the arising contingent obligation to reinvest, in other deposits on behalf of the original depositor, the deposits that are withdrawn and not repaid to the original depositor. The required stable funding from this contingent obligation would reflect the excess of the available stable funding of the relevant deposit as detailed in paragraph 122 with respect to the required stable funding described in paragraph 121.

124. Particularly in those cases where the fiduciary manages the deposits but ultimately only acts on an explicit request from the original depositor (based on the contractual arrangements of the relevant fiduciary scheme), the deposits will be considered not to have a stated maturity. The CRR does not explicitly specify the treatment of assets that do not have a stated maturity. As such, these assets would fall under the residual category of other assets for which an RSF factor of 100% shall be applied in accordance with Article 428ah(1)(b) of the CRR and Article 428az(1)(b) of the CRR in the case of the simplified NSFR.

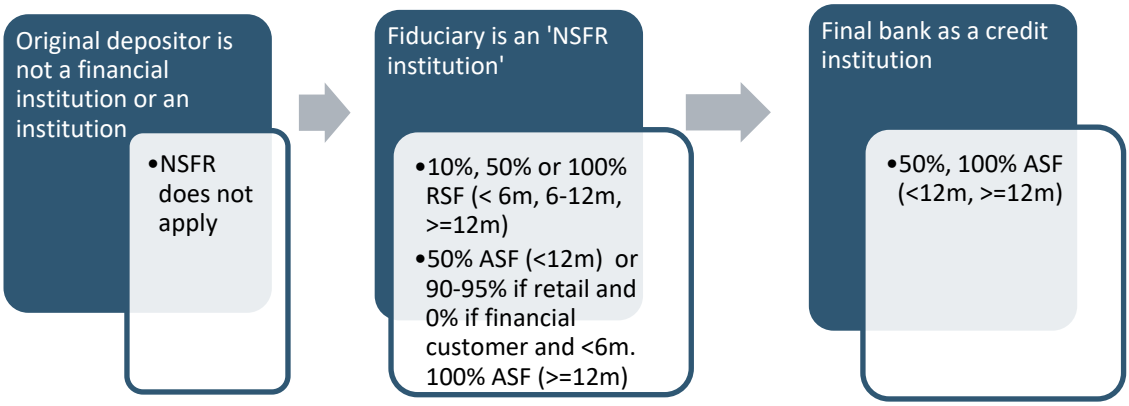
3.6.3 Summary

125. The following charts show the main fiduciary deposits as described in the previous paragraphs with the relevant ASF/RSF factors that should apply in the general NSFR:

Case I – deposit broker structure (Fiduciary is not an 'NSFR institution')

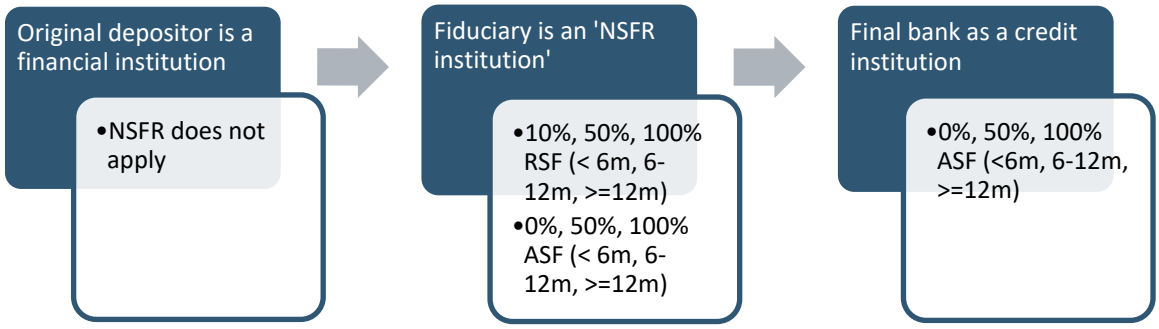


Case II – deposit broker structure (Fiduciary is an 'NSFR institution')[22]



Case III – Fiduciary as a financial customer (Fiduciary is not an 'NSFR institution')

Case IV – Fiduciary as a financial customer (Fiduciary is an 'NSFR institution')[9]



[22] The fiduciary would reflect a 100% RSF for the case specified in paragraph 124.

3.7 Application of NSFR ASF and RSF factors in the context of interbank deposits. Policy guidance

If the original depositor is an institution the deposit is not considered a fiduciary but an interbank deposit.

In this case, 10%, 50% or 100% RSF factors/0%, 50% and 100% ASF factors should generally be applied by the original depositor and the final bank respectively for the correlative three NSFR time buckets. If the intermediary is subject to the NSFR then the same RSF/ASF factors will apply unless it only acts on an explicit request of the original depositor in which case the deposits will be considered not to have a stated maturity and a 100% RSF factor applies.

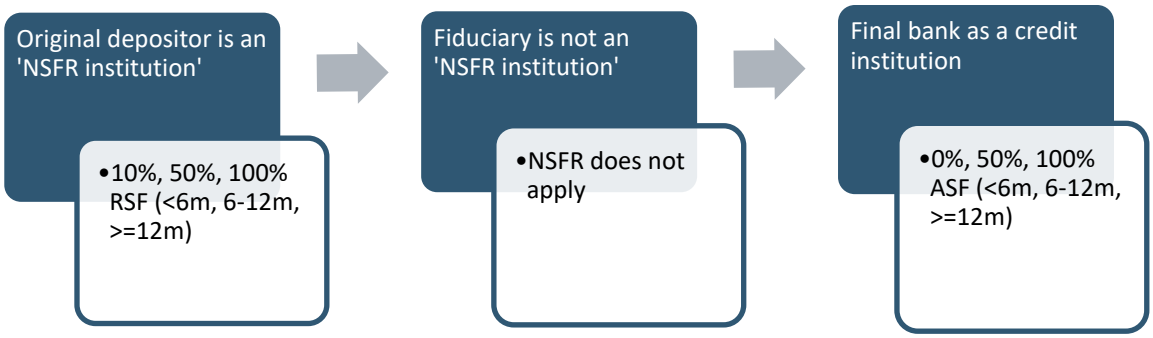
126. Where the original depositor is an institution, the deposit is expected to be an interbank deposit. The final bank will generally apply 0%, 50% and 100% ASF factors (pursuant to Articles 428k(3)(c)(iii), 428l(c)(iii) and 428o(e) of the CRR). The original depositor, as an 'NSFR institution', will generally trigger a 10%, 50% or 100% RSF factor (pursuant to Articles 428v(a), 428ad(d)(iii) and 428ah of the CRR). In both cases these factors apply for the correlative three NSFR time buckets. In the case of simplified NSFR, a 0% ASF applies if the residual maturity of the liability is less than one year (pursuant to Article 428al(3)(c)(iii) of the CRR) or 100% (pursuant to Article 428ap of the CRR) otherwise. Furthermore, a 50% or 100% RSF factor applies for those time buckets (pursuant to Articles 428aw and 428az of the CRR).

127. If the intermediary is an 'NSFR institution', those RSF and ASF factors will also apply. Particularly in those cases where the fiduciary manages the deposits but ultimately only acts on an explicit request from the original depositor (based on the contractual arrangements of the relevant fiduciary scheme), the deposits will be considered not to have a stated maturity. The CRR does not explicitly specify the treatment of assets that do not have a stated maturity. As such, these assets would fall under the residual category of other assets for which an RSF factor of 100% shall be applied in accordance with Article 428ah(1)(b) of the CRR and Article 428az(1)(b) of the CRR in the case of the simplified NSFR.

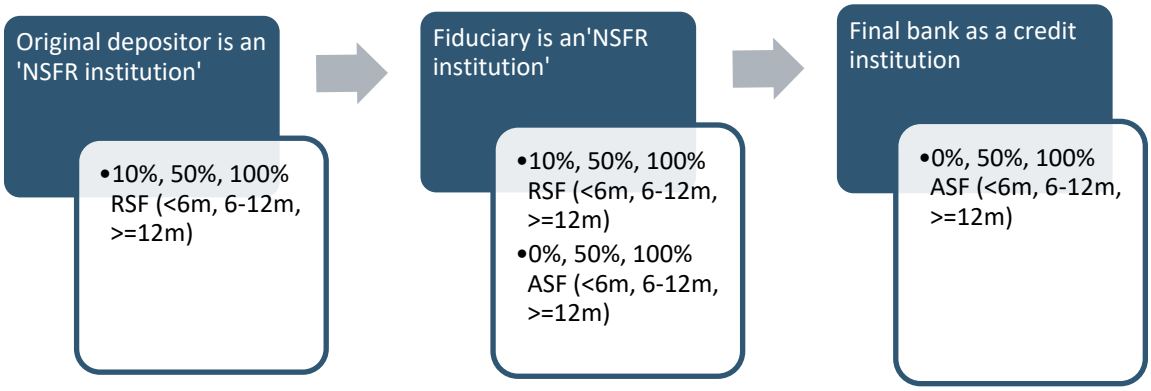
128. In the case of simplified NSFR, a 0% ASF applies if the residual maturity of the liability is less than one year (Article 428al(3)(c)(iii)) or 100% (Article 428ap) otherwise. Furthermore, a 50% or 100% RSF factor applies for those time buckets (Article 428aw and 428az).

129. The following charts show the main fiduciary deposits as described in the previous paragraphs with the relevant ASF/RSF factors that should apply in the general NSFR:

Case I – Interbank deposit (Intermediary is not an 'NSFR institution')



Case II – Interbank deposit (Intermediary is an 'NSFR institution')[23]



[23] The fiduciary would reflect a 100% RSF for the case specified in paragraph 127.

4. Monitoring of maturity concentrations

130. The EBA has performed an analysis on the implementation of the LCR and liquidity risks associated with the time dimension of the LCR. In particular, the EBA performed a quantitative data analysis regarding the 30-day horizon based on COREP data on a sample of banks, complemented by various qualitative analyses and observations reported by competent authorities on the basis of their experience of liquidity risk supervision.

131. In the quantitative analysis, to find possible cases of optimisation of the LCR horizon, the EBA calculated a theoretical 5-week proxy LCR, based on maturity ladder and LCR calculation templates in COREP. This methodology pays particular attention to the 30-day to 5-week (or 35 day) time bucket in the maturity ladder, where it can be observed if outflows are expected to be large compared to the outflows within the 30-day horizon. To obtain the weighted outflows (treating the outflows in the 30-day to 5-week bucket as if they were within the 30-day horizon) outflow and inflow factors were used, mapping the rows in the maturity ladder to the factors in the calculation of the LCR.

132. Based on this weighted calculation, the EBA was able to estimate a potential degree of optimisation of the LCR ratio. Complemented by additional information from supervisors, such as characteristics of the products involved (e.g. notice periods) and business model, the EBA was able to identify some practices that deserve further scrutiny.

4.1 Quantitative analysis (from January 2020 to June 2020)

133. Two approaches have been followed to calculate the 5-week proxy LCR in the EBA analysis. In particular, the first approach (the main approach), only uses the 30-day to 5-week time bucket from the maturity ladder and adds the outflows and inflows (after weighting) to the calculation of the LCR denominator. The second approach (the alternative approach), does not use the outflows and inflows reported by the banks but instead approximates both the 30-day LCR net outflows as well as the hypothetical 5-week net outflows based on the cumulated outflows and inflows (after weighting) reported in the maturity ladder.

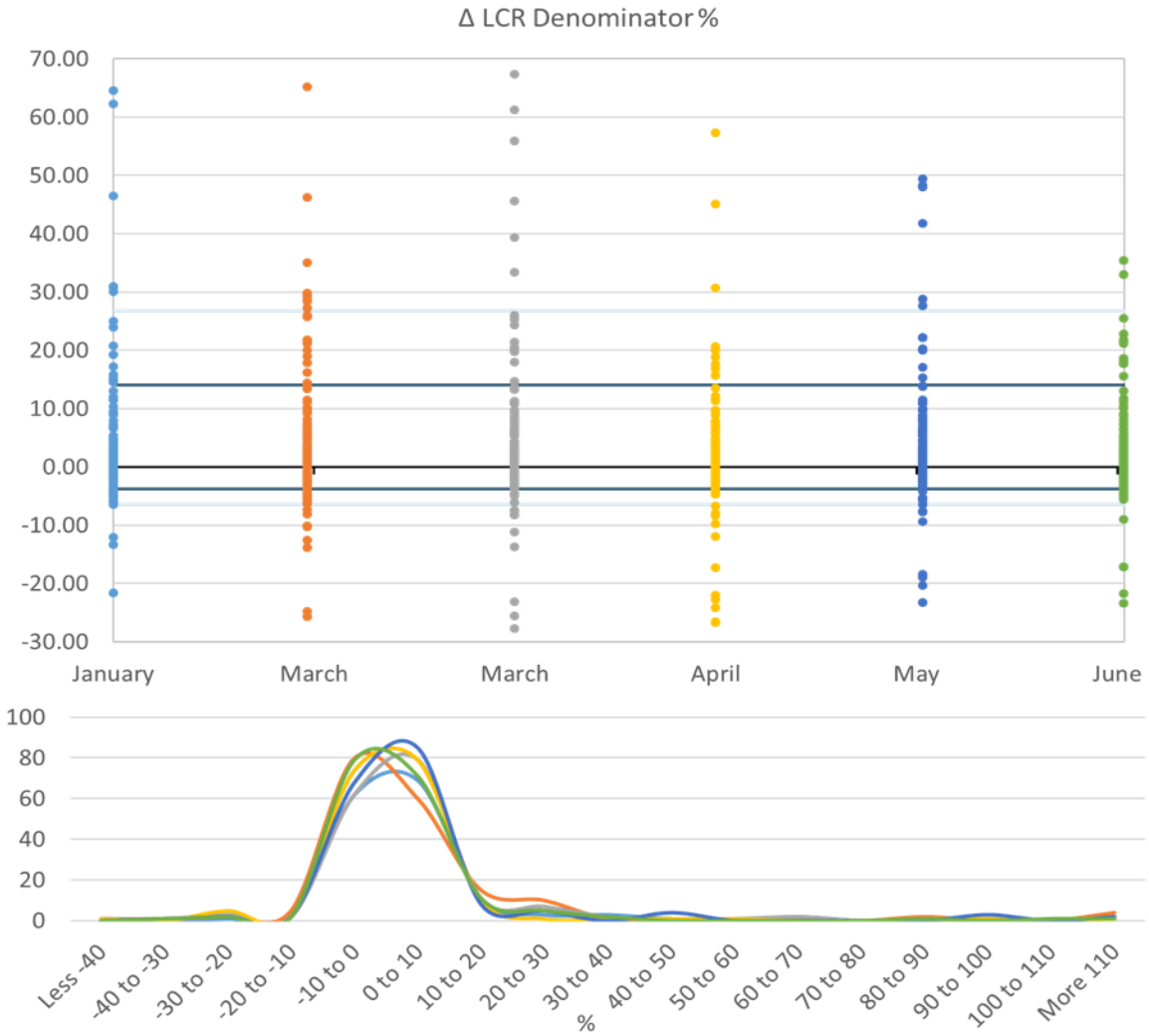
134. While these two approaches can provide helpful approximations, it is to be noted that a ‘precise’ estimation of a hypothetical 5-week LCR is not possible owing to some differences between the LCR and maturity ladder templates (with the latter having been developed with somewhat lower granularity). For example, it is not possible to perform the calculations of collateral swaps on the basis of the counterbalancing capacity section of the maturity ladder (in addition to collateral swaps, any changes in counterbalancing capacity can also be attributed partially to SFTs). To account for such effects/omissions, further examination by the supervisor appears necessary.

4.1.1 Observations based on the main approach

135. Based on the main approach, for the period of January 2020 to June 2020, an overall tendency can be observed of a 5-week LCR proxy that is mildly deteriorated compared to the official 30-day LCR. Specifically, for a monthly average of 56% of the sample, the LCR would deteriorate while, for a monthly average of 44% of the sample, the LCR would improve.

136. The impact on the LCR denominator appears to have a positively skewed distribution, with a subset of institutions that are positively affected and 'pull' the mean upward. The median impact on the LCR denominator ranges from a minimum of 0.07% - in April, to a maximum of 0.53% - in January, while the mean impact ranges from 2.71% - in April, to 9.75% - in February. Expressed as Δ LCR Denominator %: $\left(LCR\ denominator_{5weeks}/LCR\ denominator_{30days} - 1\right) * 100$, in the scattergram and density curves below (Figure 1), the impact for the entire sample is displayed. The 80% (in dark blue) and 90% (in light blue) intervals correspond to impacts on the LCR denominator of [-4.08% to +15.59%] and [-7.11% to +29.58%] respectively.

Figure 1: Distribution of the Δ LCR Denominator at the reporting date from January 2020 to June 2020.

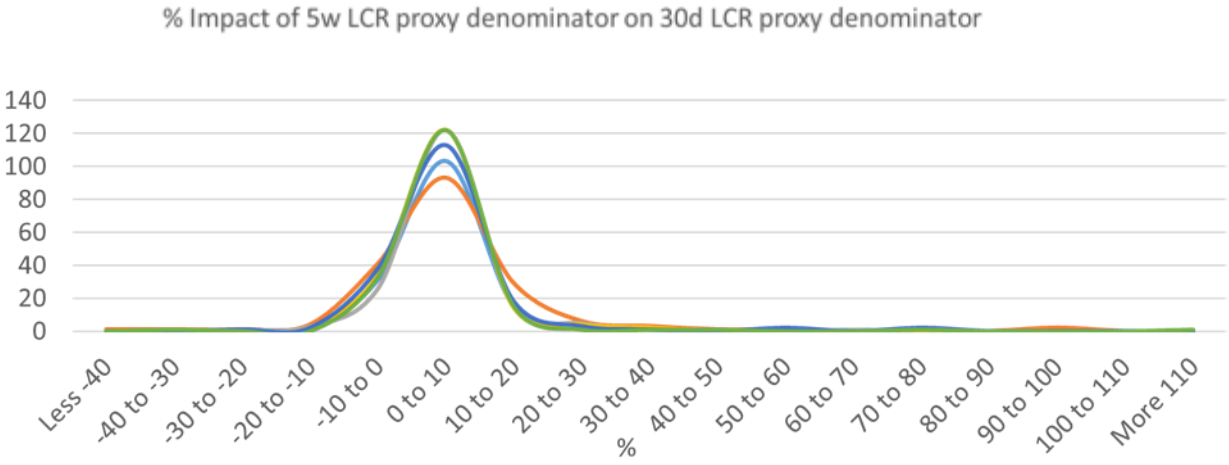


Note: The figure shows the distribution of the impact of the extension from 30 days to 5 weeks on the LCR denominator (Δ LCR Denominator) for the last six reporting dates available (from January 2020 to June 2020).

4.1.2 Observations based on the alternative approach

137. Similarly, the density curves on the basis of the alternative approach (Figure 2) show a mildly deteriorated 5-week LCR proxy compared to a 30-day horizon. For a monthly average of 79% of the sample there would be a positive impact on the LCR proxy denominator (i.e. a deterioration in the LCR proxy); while for a monthly average of 21% of the sample, there would be a negative impact on the LCR proxy denominator (i.e. an improvement in the LCR proxy).

Figure 2 Distribution of impact of the 5w LCR proxy denominator on 30d LCR proxy denominator from January 2020 to June 2020.



Note: The figure shows the distribution of the impact of the 5-week LCR proxy denominator on the 30-day LCR proxy denominator, for the last six reporting dates available (from January 2020 to June 2020).

4.1.3 Identification of possible outliers

138. To put the quantitative results into context for the purposes of the EBA's monitoring activities, qualitative information has been collected on credit institutions that have comparatively high concentrations in the 30-day to 5-week time bucket. To select a set of credit institutions for which concentration appears material a bucketing approach was used, as illustrated in Table 1, which provides the number of credit institutions that would experience an impact of more than 7.5 to 30 percent on the denominator when extending the horizon from 30 days to 5 weeks.

139. Additionally, the table provides information on the recurrence of exceedance of each threshold: whether it occurs for just one reference date or for up to all six reference dates. For example, 16 credit institutions (4+4+8 as shaded in grey) would exceed a 10% impact for at least four out of the six reference dates. In Table 2, the same information is provided in regard to the results from the alternative approach (based solely on the maturity ladder).

Table 1 Number of banks meeting threshold (main approach) from January 2020 to June 2020.

Months	7.50%	10.00%	12.50%	15.00%	20.00%	25.00%	30.00%
1	21	20	13	13	10	11	10
2	9	9	9	7	5	4	4
3	10	7	7	4	3	1	0
4	4	4	2	1	2	3	1
5	6	4	3	3	2	0	0
6	10	8	7	7	5	4	4

Note: Table 1 shows the number of banks that would meet the threshold specified in each column and whether this would occur just for one reference date or for up to all six reference dates (rows) according the main approach, for the last six reporting dates available (from January 2020 to June 2020).

Table 2 Number of banks meeting threshold (alternative approach) from January 2020 to June 2020.

Months	7.50%	10.00%	12.50%	15.00%	20.00%	25.00%	30.00%
1	36	25	15	15	7	7	5
2	17	15	14	8	8	5	3
3	7	6	5	6	1	2	1
4	8	6	3	2	1	1	1
5	9	5	2	2	2	0	1
6	10	5	5	2	1	1	0

Note: Table 2 shows the number of banks that would meet the threshold specified in each column and whether this would occur just for one reference date or for up to all six reference dates (rows) according the alternative approach, for the last six reporting dates available (from January 2020 to June 2020).

140. All considered, and without any inference about whether this does or does not constitute optimisation, 10% was selected as an impact level from which qualitative information was collected. To remove incidental observations, credit institutions were included only if they exceeded this threshold on four (or more) of the six reference dates (i.e. where the level of concentration appeared to exist more than half of the time).[24] Institutions were included where the level of concentration appeared to exist more than half of the time. This led to a selection of around 20 credit institutions.

141. The information collected on the selected credit institutions covered the nature and characteristics of the outflows/inflows (in addition to the information on the broad category available from the maturity ladder), such as the existence of notice periods or systematic roll-overs. This also included information on the type of customer/market behind the recurrent concentration, and any specific risks.

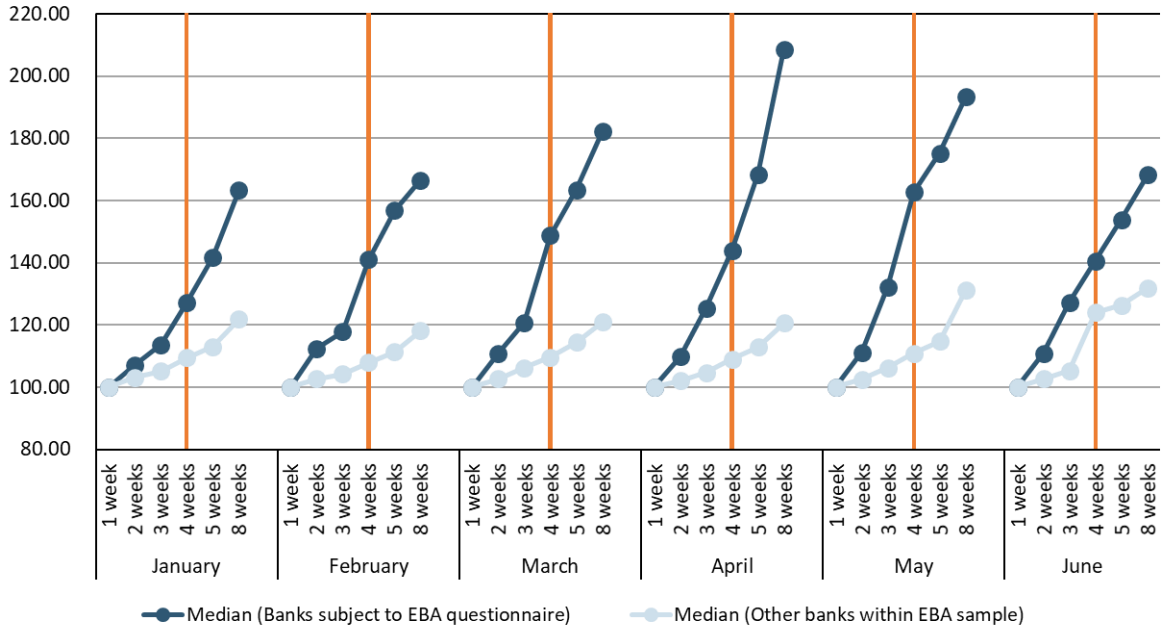
[24] To control for potential inaccuracies in the LCR proxy calculation of either the main and alternative approaches, the four out of six month exceedances could be in accordance with either the main approach or alternative approach.

4.1.4 Graphic representation of proxy denominator for banks subject to questionnaire

142. To provide further background on the maturity concentrations of the selected banks, Figure 3 graphically indicates the concentration in all time buckets up to and including 2 months for the roughly 20 credit institutions selected compared to the rest of the sample. Starting with a proxy LCR denominator in week 1 at an index of 100, the median of the subsequent cumulative net (weighted) outflows (i.e. proxies of the LCR denominator) is provided, which allows for a quick overview between the different time buckets, with a particular interest in the concentration beyond the 30-day horizon compared to the net outflow proxy just beforehand.

143. Figure 3 shows that there is a clear difference between the two paths displayed. In particular, there is a concentration for the identified credit institutions in the 30-day to 5-week bucket (sometimes larger than that of the 3 weeks spanning the 5-week to 8-week bucket), right after the 30-day LCR horizon (vertical lines), which is absent in the rest of the sample.

Figure 3 Evolution of the LCR proxy denominator from 1 to 8 weeks.



Notes: Figure 3 shows the evolution (on a median value) of the LCR proxy denominator from 1 to 8 weeks for the banks subject to specific thresholds compared with the rest of the EBA sample. The data refers to the last six reporting dates available (from January 2020 to June 2020).

4.2 Preliminary observations

144. Building on the combination of quantitative and qualitative information collected, preliminary observations could be made. It appears that, **while optimisation may not be widespread in a systematic manner, some banks may persistently engage in some degree of optimisation practices**.

145. There appear to be some differences in the size of the concentrations highlighted. In some cases, the size of the concentrations appears to be 30% or 40% (if scaled against the LCR denominator) while in others it is closer to 10%. Almost none of these cases, to the EBA's knowledge, involves banks that would be close to/below an LCR of 100% if these amounts were counted as maturing within the 30-day horizon.

146. Regarding the type of products that produce larger of concentrations, the EBA typically observes the use of (non-operational) deposits with a 31- or 32-day notice period that are marketed to institutional clients. These clients tend to be non-financial corporates, other (non-bank) financials, and other counterparties (e.g. semi-governmental/official sector). In other cases, particularly when there is an intra-group setting, the counterparty of the notice period deposit is another (subsidiary or parent) bank. Lastly, cases exist where the practice takes the form of collateral swaps (e.g. in the form of a combination of a repo and an exactly mirrored reverse repo transaction).[25]

147. There are several risks that can result from a product with a notice period. First, the notice period clauses may not actually hold in all cases, leading to a possibility of withdrawal within the 30 calendar day period, which should be captured in the LCR.

148. Second, there is the cliff risk to meeting the LCR, or more broadly the risk that the informational value of the LCR ratio (e.g. to supervisors) is undermined. Particularly, a bank may have a comparatively high LCR ratio if it attracts a lot of funding with a 31- or 32-day notice period. However, if depositors make use of the notice period because of stress or any other reason, the LCR would drop materially after one or two days (when the remaining maturity of the funding enters the 30-day LCR horizon).

149. Third, the risks are heightened if the funding subject to the notice period is highly concentrated in one or a few counterparties (observed in one of the banks), and/or if the product attracts a certain type of customer with homogeneous behaviour (equally leading to concentration).

150. Another practice that could equally be a source of cliff risk, but which is not based on a notice period, is that of rolling-over/renegotiating funding before a 30-day residual maturity is reached. In some cases, credit institutions renegotiate funding of, for example 3 or 6 months, and agree with their funding provider (often intragroup) to redeem/roll-over before reaching a residual maturity of 30 days. Sometimes, the intragroup funding provider is located in a different country. Clearly, attracting funding with a medium-term maturity can improve the funding profile of a bank. However, if a credit institution systematically pushes the roll-over of funding just outside the 30-day horizon, then the LCR ratio would not reveal the material (cliff) risks if the maturity of a large part of the funding expired.

[25] Specifically in this regard, it was highlighted that cases have been observed where banks reciprocally invest in retained own issuances with, for instance, a 31-day notice period. In addition to the risks described in this note, they are subject to further risks such as those regarding the marketability of the assets. This aspect should receive heightened scrutiny as detailed in section 2.5 of the first EBA monitoring report on the LCR.

151. From the qualitative information provided it appears that in specific circumstances concentration in the (beyond 30-day) bucket of the maturity ladder does not necessarily imply optimisation of the LCR. Specifically, this is the case of FX transactions under the condition that they are considered on a net basis in the LCR. Alternatively, as suggested by responses, sometimes the concentration is not material enough to create any concern. However, no further specific circumstances were clearly highlighted that could mitigate the existence of the risks resulting from optimisation practices/concentration.

4.3 Policy guidance

The report proposes measures to mitigate cliff risks due to concentration of outflows beyond 30 days. In particular, banks should:

- ***Assess the need to compute outflows from liabilities maturing beyond 30 calendar days or with a notice period of over 30 calendar days where a potential withdrawal could happen within the following 30 calendar days. This is expected to be the case if there is an early withdrawal clause, informal agreements or if there are any expectations that the liability could be repaid, even for reputational reasons.***

- ***Monitor their exposures to cliff risks and in particular where there is concentration with a small number of counterparties or intragroup. Detailed information should be provided in the ILAAP/SREP liquidity assessment process which could trigger specific liquidity requirements if the concentration of outflows is specifically linked to LCR optimisation practices.***

152. It is important that banks actively monitor and stand ready to explain their exposure to cliff risks based on the maturity ladder or other information. In addition to demonstrating an in-depth understanding of the risks, banks should assess the need to reduce the concentration and hold a buffer on top of the 100%.

153. To provide some structure to the necessary assessment, the following could be taken into account:

a) In the case of term deposits (or other type of funding) maturing just beyond 30 calendar days or with a notice period of over 30 calendar days, credit institutions should assess the need to compute outflows in the LCR. The presence of an early withdrawal clause, according to which a funding provider could potentially withdraw its funding within the 30-day tenor or notice period, shall be considered to trigger outflows when calculating the LCR in accordance with point (b) of Article 22(2) of the LCR DR[26]. Also, in the absence of such a

[26] Credit institutions refer to Article 25(4) for cases of retail deposits that can be excluded from outflows where there is a material penalty for early withdrawal and to the EBA guidance on this specific item provided in section 2.2 of the LCR monitoring report.

clause, any expectation by the provider of the funding that the credit institution would repay the liability during the next 30 calendar days, for example due to reputational reasons or informal agreements, should lead to a computation of outflows in the LCR in accordance with Article 27, 28 and 31a of the LCR DR.

b) If the concentration is just beyond the 30-day horizon, credit institutions need to assess how large the concentration is compared to products maturing in the other time buckets and its potential impact on the LCR should these concentrations be included in the LCR calculation. This can be based on the maturity ladder, as highlighted in the EBA analysis, taking into account the applicable outflow rate as would be the case if the maturities were to fall within the LCR horizon.

c) Credit institutions should generally avoid and provide detailed justification in the event of projected outflows that accelerate just after the 30-day horizon when compared to the previous days and weeks, as well as a recurring pattern at each reporting reference date.

d) In addition, a maturity concentration should be viewed as more material or more risky if it is associated with a large name concentration in the relevant time bucket, or if the concentration in the time bucket is associated with a certain type of customer/product with homogeneous behaviour (equally leading to a concentration),[27] or subject to contagion/network fragility.[28]

e) Credit institutions should duly assess intragroup maturity concentrations (in the form of either notice periods or funding that is negotiated before the residual maturity enters the LCR horizon) even though they may be considered to be less risky.

154. Within the ILAAP/SREP process, it is to be expected that institutions are able to explain their funding patterns, and to ensure that concentrations of liquidity outflows just beyond the LCR time horizon are adequately captured in the institutions' risk identification process and corresponding stress tests. Within this context institutions should highlight to their supervisor any risks posed by time bucket concentrations. In addition, credit institutions need to explain the underlying reasons for the build-up of the concentration. Also as a part of the dialogue, institutions should be able to explain why a product with a 31-day notice period could not partially be replaced by, for example, 60-day or 90-day notice periods.

155. Competent authorities should assess, as part of their SREP liquidity assessment, the materiality of liquidity risks and determine the need for setting institution-specific liquidity requirements to cover such risks in accordance with Articles 104(1)(k) and 105 of Directive 2013/36/EU, and as further specified in the EBA SREP Guidelines. When the assessment indicates that the risks posed by these concentrations to an institution's liquidity profile are not

[27] For example, if a bank is dependent on a specific customer base, such as non-financial corporates, then a concentration just beyond the 30-day horizon would be higher than for a bank that sources its funding from multiple client types.

[28] For example, in the case where banks reciprocally invest in retained own issuances, which appears to be a scheme that is subject to the cooperation of many players.

based on well-grounded liquidity risk management, but assessed as being material and/or driven by LCR optimisation purposes, section 9.4 and 9.5 of the EBA SREP Guidelines provide approaches for the articulation of specific quantitative liquidity requirements. Particularly, the following measures appear relevant:

a) Require an LCR higher than the regulatory minimum, of such a size that shortcomings identified (the risk arising from the maturity concentration) are sufficiently mitigated (e.g. commensurate to the LCR inflation caused by the maturity concentration);

b) Require a minimum survival period of such a length that identified shortcomings are sufficiently mitigated; the survival period can be set either directly, as a requirement, or indirectly, by setting a cap on the amount of outflows over the relevant time buckets considered (e.g. the 30-day to 5-week time bucket); competent authorities may require different types of liquid assets (e.g. assets eligible for central banks), to cover risks not (adequately) covered by the LCR;

c) Require a minimum total amount of liquid assets or counterbalancing capacity, either as a minimum total amount or as a minimum amount in excess of the applicable regulatory minimum, of such a size that the risk arising from the maturity concentration is sufficiently mitigated.

5. Article 26 LCR DR – Outflows with interdependent inflows

5.1 Background

156. The liquidity coverage ratio (LCR) is a prudential requirement that aims to ensure that banks will have sufficient liquid resources to meet their outflows under severe idiosyncratic and market-wide stress during a 30-day time horizon.

157. The LCR Delegated Regulation (LCR DR)[29] provides the details of the calculation of the outflows and inflows as well as the liquidity buffer. The liquidity gap in the LCR, the stressed net outflows (outflows – inflows) during the following 30 days, represents the liquidity risk in the LCR that needs to be covered at all times by the liquidity buffer.

158. By default, total LCR inflows are capped at 75% of total outflows (the inflow cap). Therefore, banks always need to hold a liquidity buffer at least amounting to 25% of outflows. In line with the LCR objective to cover liquidity stress situations, this safety valve is introduced to cover situations where expected inflows might not be available in time, or ever, to pay outflows.

159. Against this backdrop, the netting of outflows and inflows considered interdependent for the calculation of the liquidity buffer requirements, an exemption to the inflow cap provided for in Article 33(2)(c) in conjunction with Article 26 of the LCR DR, is subject to certain conditions and requires prior approval of the relevant competent authority. Interdependent inflows may therefore be exempted by competent authorities from the inflow cap, meaning that credit institutions would not need to hold any liquidity buffer for the part of outflows netted by interdependent inflows on account of the fact that they would not trigger any liquidity risk.

160. Compliance with the conditions established in Article 26 of the LCR DR ensures the absence of liquidity risk in interdependent outflows and inflows and, hence, the inflows would be sufficient themselves in these cases to pay the outflows without the need to hold any liquidity buffer.

161. It should be noted that the application of Article 26 of the LCR DR, in cases where all/most of the outflows and inflows would be treated as interdependent, would lead to a situation in which the whole credit institution is exempted (or nearly exempted) from holding a liquidity buffer, meaning that the ability to pay outflows (also during stress periods) would rely solely or mostly on the inflows.

[29] Commission Delegated Regulation (EU) 2015/61 of 10 October 2014 to supplement Regulation (EU) No 575/2013 of the European Parliament and the Council with regard to liquidity coverage requirement for Credit Institutions

162. Article 425(1) of the CRR, Article 33(2)(c) and Recital (16) of the LCR DR place these exemptions in the context of specialised business models under the principle of proportionality, including, for example, credit institutions specialised in pass-through mortgage lending, institutions passing through promotional loans, in every case subject to certain criteria to be fulfilled and to the prior approval of the competent authorities. However, Article 26 of the LCR DR does not specify the type of credit institutions, business models or transactions in relation to which it can be applied, other than what follows from the strict conditions established therein.

163. As Recital (16) of the LCR DR states, the application of these exemptions, including Article 26 of the LCR DR, should be available at both individual (interdependent individual inflows and outflows) and consolidated level (interdependent consolidated inflows and outflows). It should be noted that, when a subsidiary applies Article 26 of the LCR DR at an individual level and calculates its liquidity outflows net of interdependent inflows, it will contribute to the consolidated LCR with its amount of individual outflows, as calculated net of interdependent inflows, and other individual inflows it may have.

5.1.1 Robustness and level playing field issues

164. Due to the material exemption from EU directly applicable and uniform liquidity requirements that the use of Article 26 of the LCR DR entails, it is key to ensure that the conditions required for it are well understood and applied in a common, uniform and consistent manner. This should avoid the application of Article 26 of the LCR DR jeopardising the sound liquidity position of a credit institution and the level playing field across credit institutions and EU jurisdictions.

165. In this context, it is also to be noted that generally in the EU the liquidity buffer of credit institutions represents more than 15% of their total assets. As a result of the application of Article 26 of the LCR DR, credit institutions would have the opportunity to optimise the yield of this significant share of assets by investing them in assets other than low yielding liquid assets.

166. The EBA understands from exchanges with banks that a detailed list of products benefiting from the treatment of Article 26 would be welcome. Nevertheless, this is not possible. The eligibility of a transaction to benefit from Article 26 depends on its particular characteristics and arrangements and their compliance with the conditions required in Article 26. Competent authorities need to assess whether these transactions with their own characteristics and arrangements fulfil the conditions required therein. However, a precise policy guidance is included here to ensure a sufficiently robust and consistent treatment across EU institutions and jurisdictions.

5.2 Conditions envisaged in Article 26 of the LCR DR on ‘Outflows with interdependent inflows’ – Policy guidance

167. Article 26 of the LCR DR sets out that '*Subject to prior approval of the competent authority, credit institutions may calculate the liquidity outflow net of an interdependent inflow which meets all the following conditions:'*

5.2.1 Condition (a): 'the interdependent inflow is directly linked to the outflow and is not considered in the calculation of liquidity inflows in Chapter 3'

Inflows directly linked to outflows, in the context of outflows with interdependent inflows as envisaged in Article 26 of the LCR DR, are specific inflows that have to be used for the payment of specific outflows within a 30 calendar day period. Outflows may then be calculated net of the interdependent inflows. In the case of a pass-through lending business model, interdependent inflows need to be passed through to pay the relevant outflows within 30 calendar days, the LCR time horizon. Interdependent inflows that are passed-through cannot be reinvested to be used beyond the 30 calendar day period for the payment of the relevant outflows.

In the case of some specific pass-through financing transactions, the CRR and the LCR DR refer specifically to certain inflows that may be approved by the competent authority to be treated as interdependent inflows, subject to meeting all the conditions provided for in Article 26 of the LCR DR:

- ***Regarding pass-through mortgage lending funded by bonds (e.g. securitisations or covered bonds pursuant to Articles 425(1) of the CRR and 33(2)(c) in conjunction with 26 of the LCR DR):***
    - ***Inflows from monies due from mortgage borrowers that the credit institution will pass through in the form of outflows to the bond investors that fund the mortgages (covered bond or securitisation investors).***
    - ***Inflows from the bond investors (covered bond or securitisation investors) that the credit institution will pass through in the form of outflows to the mortgage borrowers or existing bond investors when the mortgages are originated or refinanced.***
- ***Regarding pass-through promotional lending, pursuant to Articles 425(1) of the CRR and 33(2)(c) in conjunction with 26 and 31(9) of the LCR DR, inflows from promotional loans stemming from the promotional bank that the credit institution acting as an intermediary will pass through in the form of outflows to the final borrower (a non- financial customer).***
- ***Regarding pass-through funding from multilateral development banks or public sector entities, pursuant to Article 33(2)(c) of the LCR DR in conjunction with Article 26 of the LCR DR, inflows stemming from loans from multilateral development banks or public sector entities that the credit institution will pass through to the final borrower.***

168. Condition (a) of Article 26 of the LCR DR requires that the interdependent inflow is '*directly linked*' to the outflow. The requirement of direct linkage implies that an '*immediate or straight*' connection needs to exist between the inflow and the outflow, without any '*intermediate transaction or bridge activity'* between both monetary flows. Expectedly, the interdependent inflows would be immediately passed through or used to pay to the relevant recipients of the outflows. Article 26 envisages that the relevant liquidity outflows are calculated net of the inflows that are interdependent to them[30]. In any case, technically, there could be up to 30 calendar days between the relevant interdependent inflows and outflows. Accordingly, interdependent inflows cannot be reinvested to be used beyond 30 calendar days for the payment of the relevant outflows[31]. Interdependent inflows are computed in the LCR when the relevant outflows arise and as a lower value of them. As referred to in the last part of condition (a) of Article 26 of the LCR DR, the interdependent inflows cannot be considered separately in the calculation of the liquidity inflows.

169. Although Article 26 of the LCR DR does not specify the type of credit institutions, business models or transactions in relation to which it can be applied, some provisions in the CRR and the LCR DR outline examples of some concrete pass-through financing transactions whose relevant inflows can be exempted from the inflows cap and/or considered interdependent in the context of Article 26 of the LCR DR, subject in every case to compliance with all the conditions established in that Article 26 and prior approval of the competent authority:

- Following point (c) of paragraph 2 of Article 33 of the LCR DR (which also encompasses the inflows referred to in Article 26 of the LCR DR):
    - Inflows from loans related to mortgage lending that the credit institution has passed through;
    - Inflows from promotional loans that the credit institution acting as intermediary has passed through;
    - Inflows from loans from a multilateral development bank or a public sector entity that the credit institution has passed through.

[30] Furthermore, the implementing technical standards on LCR reporting, as per 'Commission Implementing Regulation (EU) 2020/429 of 14 February 2020 amending Implementing Regulation (EU) No 680/2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council', establish that 'subject to prior approval of the competent authority within each category of outflows, the amount of each item reported in Column 010 of template C 73.00 of Annex XXIV shall be netted by subtracting the relevant amount of interdependent inflow in accordance with Article 26'.

[31] Within the match funded covered bonds business model, interest and amortization from mortgages may be placed in high quality liquid assets for more than 30 days before being passed on to the covered bonds investors. Likewise, proceeds from the issuance of covered bonds may be placed in high quality liquid assets for more than 30 days before being paid out to loan takers to finance a property. These high quality liquid assets are encumbered and cannot be used for other purposes until being passed on to bond investors/loan takers. The forthcoming LCR corrigendum envisages that these assets shall, for the purpose of calculating the LCR, be considered unencumbered.

- Following Article 425(1) of the CRR on the basis of which the inflow cap exemptions under 33(2)(c) are specified[32] (and therefore, the possibility to net the interdependent inflows and outflows referred to in Article 26 of the LCR DR):
    - In the context of mortgage lending funded by some eligible covered bonds:
        - Inflows from the mortgage borrowers funded by those covered bonds;
        - Inflows from those covered bond investors to fund the mortgage loans.
    - Inflows from promotional loans that the institution has passed through.

170. It is to be noted that none of these concrete pass-through transactions envisage any intermediate transaction or bridge activity. Rather, Article 425(1) of the CRR directly links the inflows from the mortgage borrowers or covered bond investors funding the mortgages to the outflows to those investors or mortgage borrowers respectively in the cited transactions. This essential aspect set out in the CRR is enshrined and further specified in Article 26 of the LCR DR when referring to outflows with interdependent inflows ('*the interdependent inflow is directly linked to the outflow*'). This is also in line with the description of characteristics of a pass-through financing structure as provided in the 2015 EBA NSFR report[33].

171. Interdependent inflows and outflows in the context of Article 26 LCR DR can only occur within a 30 calendar day period. By ensuring that interdependent inflows are passed through within a short period of time, of up to 30 calendar days, in the form of outflows, the co-legislators mitigate the liquidity risk.

5.2.2 Condition (b): 'the interdependent inflow is required pursuant to a legal, regulatory or contractual commitment;'

Either in the applicable legislative or regulatory provisions or in the contractual provisions governing the transaction, the right of the credit institution to receive the interdependent inflow as well as a description thereof and of the relevant outflow that is dependent on the inflow must be specified.

[32] The LCR DR is a delegated act that supplements (not amends) the CRR, specifying in detail the general liquidity coverage requirement set out in Article 412(1) of the CRR, and in particular the detail liquidity requirements for the purpose of the application, amongst others, of Article 425 of the CRR (see Article 460(1) of the CRR).

[33] The 2015 EBA NSFR report refers to pass-through financing. Before entering into the treatment of these activities in the NSFR, the report explains what pass-through financing is. In page 128 it explains how '*A strict definition of the pass-through financing principle implies that payments on an asset or a pool of assets are passed directly on to investors in a security, the holders of which have the right to receive these payments. This could, for example, be in the form of a mortgage-backed security (MBS), where interest and principal payments from a pool of borrowers are passed through to the holders of the MBS, thereby making up the running payments from the security to the investor. Pass-through financing can also be in the form of a covered bond where the payments from the cover pool are passed through to the covered bond investor. It must be emphasised, however, that not all covered bond funding is a pass-through structure. Regular banks use covered bond funding, where the assets in the cover pool typically change over time and the running payments are not necessarily passed through the bank from the cover pool to the investor. This type of arrangement is not a pass-through structure.*'

172. Credit institutions applying Article 26 of the LCR DR have therefore to be legally entitled to receive the interdependent inflows either because this legal right is established in a legislative or regulatory act or in contractual commitments.

173. These binding legal, regulatory or contractual commitments must therefore govern the credit institution's right to receive the interdependent inflow as well as its interdependence with the credit institution's obligation to pay the relevant outflow. Pursuant to this and Article 32(1) of the LCR DR, no contingent inflows can be considered as inflows and therefore as interdependent inflows to be netted with outflows. In that regard, and for the purpose of this provision, an inflow is not contingent where contractual arrangements are in place that ensure that the associated outflow will not be paid if the inflows are not received beforehand.

5.2.3 Condition (c): '(c) the interdependent inflow meets one of the following conditions:

(i) it arises compulsorily before the outflow;

(ii) it is received within 10 days and is guaranteed by the central government of a Member State'

Unless condition (c) (ii) of Article 26 of the LCR DR is met, it must be ensured that the interdependent inflow is not only legally required to be received by the credit institution but is also effectively received before the relevant outflow occurs. Therefore, the credit institution should not be obliged to pay the relevant outflow on the maturity date if the interdependent inflow has not been received beforehand.

This condition should not be considered to be met in those transactions where the contractual maturity date of the interdependent inflow is earlier than the contractual maturity date of the relevant outflow, but the credit institution is still obliged to pay the outflow on the maturity date irrespective of whether or not the inflow is effectively received on its maturity date.

174. Condition (c) envisages that the interdependent inflow needs to be effectively received by the credit institution before the outflow (point (i)) or, alternatively, up to 10 days after the outflow occurs provided that it is guaranteed by the central government of a Member State (point (ii)) [34].

175. By applying Article 26 of the LCR DR, interdependent inflows are netted with the outflows, no inflow cap applies and no liquidity buffer is required for those outflows. Their payment relies only on the effectiveness of the reception of those interdependent inflows. The denominator of

[34] It would be illogical to interpret that condition (c)(i) of Article 26 of the LCR DR can be met both without ensuring that the inflow is effectively received before the outflow and without the additional guarantee of the central government required under condition (c)(ii). It is precisely this latter guarantee which allows a delay in the inflows being received and only up to 10 days. Otherwise, condition (c)(ii) would lose its '*effet utile*' and be redundant.

the LCR (net outflows) for the part related to outflows and interdependent inflows is zero, meaning that there is no liquidity risk in those transactions.

176. The inflow cap seeks to ensure that only inflows that will be ultimately available in time to pay outflows are computed in the LCR. It covers, at an aggregated level, a situation of timing mismatch between expected inflows and outflows such that the expected inflows are received after the outflows, if ever, and where, therefore, the inflows cannot be used to pay the outflows in time. The co-legislators first in the CRR and, subsequently, the Commission in the LCR DR, ensure this by capping the LCR inflows at 75% of the outflows and simultaneously by ensuring a minimum liquidity buffer of 25% of the outflows. Those timing mismatch situations between inflows and outflows can respond to cases where potential losses or arrears of expected inflows maturing before the outflows can make the inflows be received ultimately after the outflows if ever (in case of unexpected losses of the counterparty) and to cases where the expected inflows mature after the outflows[35]. Indeed, these situations are not unlikely under a LCR severe stress scenario[36].

177. With this condition (c) of Article 26 of the LCR DR, it is ensured that Article 26 will only be applied in those transactions where there is no need to apply an inflow cap, where the inflows can themselves, without any buffer, cover the relevant outflows, meaning that the risk of interdependent inflows not being received in time, or ever, is eliminated. That is why in the transactions under Article 26 of the LCR DR the inflows have to be received compulsorily before the outflows, meaning that in these transactions the outflows have to be paid by the credit institution only if it has received the inflows beforehand[37].

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[35] On 20 December 2013 the EBA published the Report on impact assessment for liquidity measures under Article 509(1) of the CRR (20 December 2013), on the calibration of the LCR, where it states that '*The inflow cap, as introduced in the Basel rules text, aims at ensuring that banks hold a minimum of HQLA in relation to their outflows, and has the following rationale: • To increase banks' resilience against unexpected loss of contractual inflows due to liquidity/solvency problems of the counterparty. • To reduce contagion risk by curbing the room for 'domino effects' in stress situations, thus contributing to stabilising money markets and EU banks' access to funding sources. • To account for maturity mismatches between inflows and outflows within the 30-day stress horizon, i.e. liquid assets may cover cash outflows in case the inflows materialise later than the outflows…'*

On 10 October 2014 (the same date the LCR DA was adopted by the Commission), the Commission published an FAQ where it refers to the meaning of the inflow cap and indicates that it is '*to reflect possible timing differences between outflows and inflows to allow for possible loss of inflows from some counterparties'*.

Recital (16) of the LCR DR states that 'In order to prevent credit institutions from relying solely on anticipated inflows to meet their liquidity coverage ratio and also to ensure a minimum level of liquid assets holdings, the amount of inflows that can offset outflows should be capped at 75% of total expected outflows… However, taking into account the existence of specialised business models, certain exemptions to this cap, either full or partial should be permitted…Those exemptions should be available at both the individual and consolidated level, but only where certain criteria are fulfilled'. Indeed, this recital generally envisages the need to apply the inflow cap to ensure a minimum liquidity buffer due to the possibility that the anticipated inflows might not be available in time, or ever. It recognises exceptional cases where the inflow cap might not be necessary and the bank would not require a minimum liquidity buffer. The recital establishes that in these cases certain criteria should be fulfilled that would ensure the absence of liquidity risk. This is related to Article 26 and the required conditions set down therein for its application.

[36] The LCR incorporates two general mechanisms to generally cover at an aggregated level both expected losses of inflows (Article 32(1) of the LCR DR does not allow the recognition of inflows where the credit institution expects losses on them) and also unexpected losses of inflows (Article 33(1) of the LCR DR envisages an inflow cap as explained for these purposes).

[37] In Denmark within the match funded covered bond model the service of a mortgage is done by paying interest and amortization quarterly/monthly to the mortgage credit institute, which places the received amounts in a cover pool in form of liquid assets until being passed on to the investors of the specific covered bond on an annual basis. The

178. This is consistent with condition (a) where '*the interdependent inflow is directly linked to the outflows'*. This reinforces the idea that one leg cannot happen without the other. The outflow should not happen without the inflow to which it should be linked. Outflows should only happen if the inflows are received effectively.

179. This condition should not be considered to be met in those transactions where it is only established that the contractual maturity of the inflows needs to be prior to that of the outflows and where the credit institution is still obliged to pay the outflows on time irrespective of whether or not the interdependent inflows are effectively received on the maturity date. It is clear that in such transactions it would not be ensured that the inflows will be received before the outflows, as required under condition (c)(i) of Article 26 of the LCR DR. In cases of potential unexpected arrears or non-payment of the inflows, the credit institution would still need to pay the outflow on time and would have not received the inflows. The credit institution would be exposed to a large liquidity risk if it were to apply Article 26 of the LCR DR without ensuring that the inflows would be received before the outflows since it would need to pay outflows without having received the inflows and without holding any liquidity buffer.

180. For this condition to be met it needs to be ensured that the interdependent inflows will be received before the relevant outflows are paid. For example, the legal framework or contractual arrangements of the relevant transactions might establish that the outflows will only be paid if the interdependent inflows have been received beforehand; or they might envisage automatic triggers that would extend the maturity of the specific relevant outflow if the interdependent inflow to which it is linked has not been received beforehand.

181. The LCR DR envisages, however, that for transactions where the central government of a Member State guarantees that the credit institution will receive the inflows no later than 10 days after the outflows are paid, the liquidity risk is sufficiently mitigated, and Article 26 of the LCR DR can apply. The regulation assumes that there is certainty that the central government will make the inflows available to the credit institution within those 10 days.

5.3 Interaction with specific liquidity requirements in Article 105 of the CRDV

182. As indicated, the application of Article 26 of the LCR DR, approved by a competent authority, could result in some cases in the requirement for a minimum liquidity buffer in a credit institution being reduced in full or mostly. In these cases, the denominator of the LCR, the net outflows, is very much reduced or approaches zero, meaning that the liquidity risk inherent

payment of interest and amortization in installments reduce the liquidity risk of the mortgage institute to those installments not yet paid in. Within the match funded covered bond model the terms and conditions of a mortgage are usually settled when signing the mortgage deed. This is done by selling spot the covered bonds needed to finance the mortgage and placing the proceeds in a cover pool in form of liquid assets until the due date of the mortgage, or by selling the bonds forward with a due date corresponding to that of the underlying mortgage. Refinancing of existing mortgages and ARMs are done in a similar manner. Refinancing of ARMs are done on auction more than 30 days prior to the due date to reduce the risk of failing auctions. In extreme scenarios where the ARMs can only be sold at an interest rate exceeding the present rate by more than 5%-points, the existing ARMs are automatically extended by one year.

to the LCR is negligible in the bank. This is because the inflows by themselves are sufficient to cover the payment of the outflows.

183. It might still happen that, despite the assumed absence of LCR related liquidity risk, the supervisor would see risks associated with the extent to which the application of Article 26 has reduced (or fully removed in some cases) the required amount of the total liquidity buffer in a credit institution and the supervisor would rather ensure a minimum liquidity buffer for prudential reasons.

184. In these cases, it should be taken into account that the application of Article 26 is ultimately subject to the competent authority's approval.

185. In addition to this, the LCR DR provides competent authorities with sufficient flexibility to calibrate the degree of reduction of the required liquidity buffer in the LCR, as a Pillar 1 requirement, when the conditions of Article 26 are met and its approval has been granted.

186. The first subparagraph of Article 33(2) of the LCR DR recognises that the inflow cap waiver, including the case of interdependent inflows (subject to compliance with Article 26 conditions and prior approval by the CA, as referred to in Article 33(2)(c)), may be applied partially, and still a minimum LCR buffer might be required on the amount of outflows.

187. Importantly, the application of institution-specific liquidity requirements in the context of supervisory measures (so called Pillar 2 measures), as envisaged in Articles 104(1)(k) and 105 of the CRD, to ensure a minimum liquidity buffer where Article 26 is approved, should not be used. Pillar 2 measures cannot replace the aforementioned specific approach envisaged for these cases in the Pillar 1 requirement framework under EU Regulation.

188. Furthermore, a specific liquidity requirement aimed at ensuring a minimum amount of the liquidity buffer in these cases would not be consistent with paragraph 463 of Title 9 ('SREP liquidity assessment') of the EBA SREP Guidelines[38]. Indeed, the application of a specific liquidity requirement, pursuant to paragraph 463[39], assumes that the credit institution is not covering the liquidity risk it is exposed to, which would contradict the objective pursued by Article 26, i.e. to treat situations where the credit institution is basically not exposed to liquidity risk and therefore is not required to hold a liquidity buffer. Overall, the liquidity risks already covered by the LCR should be precisely covered by a proper application of the provisions of the LCR DR (such as Article 26 of the LCR DR), not by setting alternative specific liquidity requirements.

[38] EBA/GL/2014/13 on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing – Consolidated version published on 19 July 2018.

[39] Paragraph 463 of the EBA SREP Guidelines states that 'competent authorities should determine through the SREP liquidity assessment whether the liquidity held by the institution provides appropriate coverage of the risks to liquidity and funding assessed in accordance with Title 8. Competent authorities should also determine through the SREP liquidity assessment whether it is necessary to set specific liquidity requirements to cover risks to liquidity and funding to which an institution is or might be exposed.'

189. It should also be noted that the LCR full application at a minimum of 100% became effective in January 2018, which put an end to any national provisions in the area of liquidity requirements (Article 412(5) of the CRR).

6. DGS conditions for a 3% outflow rate in retail deposits

6.1 Background

6.1.1 EU Legal basis

190. Paragraphs 4 and 5 of Article 24 of the LCR Delegated Regulation (LCR DR) envisage the application of a 3% outflow rate on stable retail deposits covered by a deposit guarantee scheme (DGS)[40] from 1 January 2019 (instead of the usual 5%) if authorised by the relevant competent authority after having obtained prior approval from the Commission which must assess, after having sought the opinion of the EBA, whether certain conditions[41] are complied with by the relevant DGS.

191. Specifically, Article 24(4) and (5) of the LCR DR sets out that the following conditions need to be met:

- The retail deposits should be stable retail deposits as per Article 24(1) of the LCR DR.
- The amount on which to apply a 3% outflow rate cannot exceed EUR 100 000 per depositor (first subparagraph of Article 24(4) of the LCR DR).
- Existence of a reasoned justification/evidence that the run-off rates would be below 3% during any LCR stress period (Article 24(5) of the LCR DR).
- The amount of the retail deposits to apply a 3% outflow rate has to be covered by a DGS in accordance with Directive 2014/49/EU that meets the following criteria:
  - Criterion a) in Article 24(4) of the LCR DR. The DGS needs to be prefunded, i.e. '*The DGS has available financial means raised ex ante by contributions made by members at least annually*';
  - Criterion b) in Article 24(4) of the LCR DR. The DGS needs to have ready access to additional funding, i.e. '*The DGS has adequate means of ensuring ready access to additional funding in the event of a large call on its reserves, including access to extraordinary contributions from member credit*

[40] The possibility of applying a 3% outflow rate is envisaged in paragraph 40.11 of the Basel consolidated framework as regards the LCR.

[41] This note refers only to the assessment process of the DGS criteria envisaged in Article 24(4) of the LCR DR and does not contemplate the assessment process of evidence of a less than 3% run-off rate in the relevant stable retail deposits.

institutions and adequate alternative funding arrangements to obtain short-term funding from public or private third parties', and;

- Criterion c) in Article 24(4) of the LCR DR> The DGS needs to meet a maximum 7 day repayment period, i.e. '*The deposit guarantee scheme ensures a seven working day repayment period from the date of application of the 3% outflow rate.*'

192. After having obtained prior approval from the Commission, competent authorities have the possibility to authorise credit institutions to apply a 3% outflow rate.

193. Upon request of banks to apply a 3% outflow rate, the required evidence of a less than 3% run-off rate for stable retail deposits under stress will be assessed. The EBA will work in 2021 on a common methodology for the assessment of this evidence.

194. The competent authority will present a reasoned notification, including the evidence of a less than 3% run-off rate and relevant information[42] on the required DGS conditions, to the European Commission.

195. Article 24 (5) of the LCR DR establishes that competent authorities may authorise credit institutions to apply a 3% outflow rate provided that the Commission previously approves that the relevant DGS meets the required criteria (a), (b) and (c) in Article 24(4) of the LCR DR[43], for which the Commission shall seek the opinion of the EBA on the conformity of the relevant DGS with those criteria.

196. Article 24(5) establishes that '*The reasoned notification shall be submitted to the Commission at least three months prior to the date from which authorisation is requested.'* In order to enable the EBA to express a properly informed view on the subject matter of the envisaged consultation, competent authorities are asked to consider submitting the reasoned notification to the Commission sufficiently in advance from the date from which the authorisation is requested.

197. This note contains the harmonised methodology to be used by the EBA in the exercise of its mandate for the assessment of conformity by the DGS with the criteria (a), (b) and (c) required in Article 24 (4) of the LCR DR and for the specific purposes of this provision in the LCR DR. The use of a harmonised methodology will ensure a level playing field across institutions and jurisdictions in the EU.

[42] This information is detailed in this note as part of the methodology to be used in the assessment of the DGS conditions.

[43] Nevertheless, even if those criteria are fulfilled, the Commission may not approve the competent authority's request to grant authorisation if there exist overriding grounds for withholding approval having regard to the functioning of the internal market for retail deposits.

6.2 Methodology. Policy guidance

The report includes a list of necessary information to be provided to the EBA by the relevant DGS designated authority (assisted by the relevant DGS where the two are different) in the form of three questionnaires.

It also includes the methodology that the EBA will follow to assess that information for the elaboration of its Opinion to the Commission on the compliance of the relevant DGS with the conditions established in Article 24(4) LCR DR.

It also refers to other available information to be used in this assessment without prejudice to any further interaction with the DGS designated authority (and if necessary, the DGS where the two are different), and where relevant with the relevant competent authority, in order to obtain any clarification or additional information.

198. The EBA will evaluate the following information:

(i) National legislation where the transposition of Directive 2014/49/EU on deposit guarantee schemes (DGSD) is made and any other implementing national regulations, administrative provisions or DGS by-laws, with indication of the relevant Articles or provisions on the matter.

(ii) Responses to Questionnaire 1, on criteria (a) of Article 24(4) of the LCR DR, based on Article 10 of the DGSD. Annex 1 of this item contains this questionnaire, as well as the methodology to be used by the EBA in the assessment of this questionnaire.

(iii) Responses to Questionnaire 2, on criteria (b) of Article 24(4) of the LCR DR, based on Article 10 of the DGSD. Annex 2 of this item contains this questionnaire as well as the methodology to be used by the EBA in the assessment of this questionnaire.

(iv) Responses to Questionnaire 3 on criteria (c) of Article 24(4) of the LCR DR, based on Article 8 of the DGSD. Annex 3 of this item contains this questionnaire as well as the methodology to be used by the EBA in the assessment of this questionnaire.

The information referred to under point (i) above[44] and the responses to the questionnaires 1 to 3[45] will be prepared and filled in, respectively, by the relevant DGS designated authority (assisted by the relevant DGS where the two are different) and are expected to be included by

[44] In case of several DGSs supervised by one single DGS designated authority, this information should be tailored (e.g. DGS by-laws) to the specific characteristics of the relevant DGS.

[45] In case of several DGSs supervised by one single DGS designated authority, there should be as many questionnaires as existing DGSs.

the competent authority in the reasoned notification to the Commission when requesting the approval referred to by Article 24(5) of the LCR DR, and communicated to the EBA.

199. In addition to this, the EBA will consider the following information available for the assessment of criteria (a) or Article 24(4) of the LCR DR:

(i) Frequency of contributions (Article 10(1) of the DGSD). This information is necessary to assess if the contributions are made at least annually.

(ii) The minimum target level of the amount of available financial means with respect to covered deposits (Articles 10(2) and 10(6) of the DGSD). This information is necessary to understand whether the applicable target level is the default 0.8% or if it has been reduced. This information is published on the EBA website.

(iii) The current level of the available financial means of the DGS with respect to the amount of the covered deposits and the evolution of these elements (Article 10(2) of the DGSD). This is to understand the DGS's current financial position and its path towards the required minimum target level of 0.8% (or the lower target level as per Article 10(6) of the DGSD) in 2024. This information is published on the EBA website.

(iv) Disbursements made by the DGS with respect to covered deposits up to date and if they have triggered any extension of the deadline to meet the minimum target level as per Article 10 of the DGSD. This is to understand the plan to compliance with the 0.8% (Article 10(2) of the DGSD). This information is partially published on the EBA website.

200. The EBA will engage with the relevant DGS designated authority (and if necessary, the DGS where the two are different), and where necessary with the relevant competent authority, in order to obtain any clarification or additional information (such as documents, records, stress test results or audit reports) that might be needed in the course of the technical assessment. The EBA will discuss with the DGS designated authority (and if necessary, the DGS where the two are different) and the relevant competent authority the reasons for which some conditions might not be considered to be met, if any, and, if that is the case, potential actions to be taken that can ensure compliance.

201. Finally, the EBA will provide its Opinion on the conformity of the relevant DGS with the conditions set out in Article 24(4)(a), (b) and (c) to the European Commission as envisaged in paragraph 5 of Article 24 of the LCR DR.

Annex 1 – criterion (a) of Article 24(4) LCR DR

Questionnaire 1 to be filled in by the DGS designated authority (assisted by the relevant DGS, where the two are different)

Questionnaire 1 on DGS criteria 1 of Article 24(4)LCR DR '*(a) the deposit guarantee scheme has available financial means, as referred to in Article 10 of Directive 2014/49/EU, raised ex ante by contributions made by members at least annually;*'		
Relevant paragraph of Article 10 of Directive 2014/49/EU on Financing of DGSs	**Question**	**DGS designated authority's answer**
1 – Do you consider that the DGS meets the requirement in the Delegated Regulation on LCR to have '*available financial means, as referred to in Article 10 of Directive 2014/49/EU, raised ex ante by contributions made by members at least annually*'? [Yes/No]. To further justify your reply to this question, please provide answers to the remaining questions in this form.		
1	2 – Please describe the systems the DGS has in place to determine its potential liabilities (i.e. covered deposits).	
2	3 – Please provide the latest readily available information of the amount of the available financial means expressed as a percentage of the amount of the covered deposits, with indication of its reference date.	
3	4 – If a DGS uses payment commitments, please provide the latest readily available information of the share of payment commitments in the total amount of the available financial means, with indication of its reference date.	

7	5 – Please describe how the available financial means of the DGS are invested and explain how it is ensured that they are invested in a low risk and sufficiently diversified manner.	

Assessment methodology to be used by the EBA

Questionnaire 1 on DGS criteria 1 of Article 24(4) LCR DR *'(a) the deposit guarantee scheme has available financial means, as referred to in Article 10 of Directive 2014/49/EU, raised ex ante by contributions made by members at least annually;'*		
Relevant paragraph of Article 10 of Directive 2014/49/EU on Financing of DGSs	**Question**	**Methodology**
1 – Do you consider that the DGS meets the requirement in the Delegated Regulation on LCR to have '*available financial means, as referred to in Article 10 of Directive 2014/49/EU, raised ex ante by contributions made by members at least annually*'? [Yes/No]. To further justify your reply to this question, please provide answers to the remaining questions in this form.		The DGS self-assessment will be taken into account but it is not enough in itself for an EBA assessment of compliance. The EBA's assessment might potentially lead to a different conclusion. The EBA will assess the rest of the information in this questionnaire and any clarification or additional information obtained from the DGS designated authorities to raise its opinion on the compliance with this condition.
1	2 – Please describe the systems the DGS has in place to determine its potential liabilities (i.e. covered deposits)	The methodology will build on the existence of specific rules[46] implemented by the DGS regarding the process to assess its potential liabilities (e.g. it will be assessed if this information is reported regularly to the DGS by member institutions, if it is reported under the institutions' responsibility and if it is, in any case, reviewed by the DGS). The existence of any procedure, aimed at ensuring that banks provide accurate information at a depositor level, will be taken into account (e.g. it will be considered if

[46] Formal documents signed and approved by the Governing/Management Bodies of the DGS that are in place and whose application is subject to internal and external control.

		institutions are subject to some internal or external control on the determination of the covered deposits such as supervision, audit or stress test).
1, 2, 4 and 6	3 – Please provide the latest readily available information of the amount of the available financial means expressed as a percentage of the amount of the covered deposits, with indication of its reference date. Please specify the mandatory contributions to other schemes envisaged in paragraph 4 of Article 10, where applicable, that are considered in the available financial means as a percentage of the amount of the covered deposits.	The EBA will verify if the DGS is prefunded and if the available financial means meet the required target levels as per the DGSD considering phase in arrangements or any derogations in place.
3	4 – If a DGS uses payment commitments, please provide the latest readily available information of the share of payment commitments in the total amount of the available financial means, with indication of its reference date.	The EBA will verify that the total share of payment commitments does not exceed 30% of the total amount of available financial means.
7	5 – Please describe how the available financial means of the DGS are invested and explain how it is ensured that they are invested in a low risk and sufficiently diversified manner.	The EBA will assess the existence of specific rules[5] or guidelines aimed at ensuring low risk and diversified available financial means.

Annex 2 – criterion (b) of Article 24(4) LCR DR

Questionnaire 2 to be filled in by the DGS designated authority (assisted by the relevant DGS, where the two are different)

Questionnaire 2 on DGS criteria 2 of Article 24(4) LCR DR '*(b) the deposit guarantee scheme has adequate means of ensuring ready access to additional funding in the event of a large call on its reserves, including access to extraordinary contributions from member credit institutions and adequate alternative funding arrangements to obtain short-term funding from public or private third parties;*'		
Relevant paragraph of Article 10 of Directive 2014/49/EU on Financing of DGSs	**Question**	**DGS designated authority's answer**
1 - Do you consider that the DGS meets the requirement in the Delegated Regulation on LCR to have '*adequate means of ensuring ready access to additional funding in the event of a large call on its reserves, including access to extraordinary contributions from member credit institutions and adequate alternative funding arrangements to obtain short-term funding from public or private third parties*'? [Yes/No] To further justify your reply to this question, please provide answers to the remaining questions in this form.		
8	2 – Please explain if the DGS has a specific framework in place to be able to raise extraordinary contributions promptly from its members. If so: i) does the framework envisage any timelines for raising such contributions and, ii) is there any specific maximum amount [other than the 0.5 percent of covered deposits per calendar year referred to in Article 10.8 of Directive 2014/49/EU] for these cases? Where applicable, please provide answers referred to the results of the stress tests based on the EBA Guidelines on stress testing of DGSs including whether some member institutions' extraordinary contributions may be deferred in whole or in part on the grounds that the payments would jeopardise their liquidity or solvency position.	
9	3 – Please explain if there are alternative funding arrangements in place to obtain short-term funding, and if yes, (i) what they are, ii) what is the maximum amount that can be accessed using this alternative funding arrangement, iii) what is the envisaged time for the funds from the alternative	

	funding arrangement to be made available to the DGS, and iv) if there is any guarantee in place to receive that amount in a timely manner [potentially with a reference to any stress tests performed by the DGS].	

Assessment methodology to be used by the EBA

Questionnaire 2 on DGS criteria 2 of Article 24(4) LCR DR *'(b) the deposit guarantee scheme has adequate means of ensuring ready access to additional funding in the event of a large call on its reserves, including access to extraordinary contributions from member credit institutions and adequate alternative funding arrangements to obtain short-term funding from public or private third parties;'*		
Relevant paragraph of Article 10 of Directive 2014/49/EU on Financing of DGSs	**Question**	**Methodology**
1 - Do you consider that the DGS meets the requirement in the Delegated Regulation on LCR to have '*adequate means of ensuring ready access to additional funding in the event of a large call on its reserves, including access to extraordinary contributions from member credit institutions and adequate alternative funding arrangements to obtain short-term funding from public or private third parties*'? [Yes/No] To further justify your reply to this question, please provide answers to the remaining questions in this form.		The DGS self-assessment will be taken into account but it is not enough in itself for an EBA assessment of compliance. The EBA's assessment might potentially lead to a different conclusion. The EBA will assess the information in this questionnaire and any clarification or additional information obtained from the DGS designated authorities to raise its opinion on the compliance with this condition and will take into account the available financial means the DGS has at its disposal.
8	2 – Please explain if the DGS has a specific framework in place to be able to raise extraordinary contributions promptly from its members. If so: i) does the framework envisage any timelines for raising such contributions and, ii) is there any specific maximum amount [other than the 0.5 percent of covered deposits per calendar year referred to in Article 10.8 of Directive 2014/49/EU] for these cases? Where applicable, please provide answers referred to the results of the stress tests	The EBA will assess answers to these questions because, if there is no framework in place as regards the timeline or the amount to be received, it might be questionable under which premises it can be considered that ready access to extraordinary contributions is ensured. The results of a stress test, that the DGS might be subject to, will be specially considered, including whether any member

	based on the EBA Guidelines on stress testing of DGSs including if some member institutions' extraordinary contributions may be deferred in whole or in part on the grounds that the payments would jeopardise their liquidity or solvency position.	institutions' extraordinary contributions may be deferred in whole or in part on the grounds that the payments would jeopardise their liquidity or solvency position. If the DGS is subject to an audit exercise on these aspects, the results would also be particularly taken into account.
9	3 – Please explain if there are alternative funding arrangements in place to obtain short-term funding, and if yes, (i) what they are, ii) what is the maximum amount that can be accessed using this alternative funding arrangement, iii) what is the envisaged time for the funds from the alternative funding arrangement to be made available to the DGS, and iv) if there is any guarantee in place to receive that amount in a timely manner [potentially with a reference to any stress tests performed by the DGS].	The EBA will assess answers to these questions because, if there is no framework in place as regards the timeline or the amount to be received, it might be questionable under which premises it can be considered that ready access to alternative funding arrangements is ensured. The results of an audit exercise or a stress test that the DGS might be subject to, will also be considered.

Annex 3 – criterion (c) of Article 24(4) LCR DR

Questionnaire 3 to be filled in by the DGS designated authority (assisted by the relevant DGS, where the two are different)

Questionnaire 3 on DGS criteria 3 of Article 24(4) LCR DR *'(c) the deposit guarantee scheme ensures a seven working day repayment period as referred to in Article 8(1) of Directive 2014/49/EU from the date of application of the 3% outflow rate.'*		
Relevant paragraph of Article 8 of Directive 2014/49/EU on Financing of DGSs	**Question**	**DGS designated authority's answer**
1 - Do you consider that the DGS meets the requirement in the Delegated Regulation on LCR to '*ensure a seven working day repayment period as referred to in Article 8(1) of Directive 2014/49/EU from the date of application of the 3% outflow rate*'? [Yes/No] To further justify your reply to this question, please provide answers to the remaining questions in this form.		
1	2 – Is the DGS legally required to make the repayable amount available within seven working days? Please attach copy of the relevant legal document.	
1	3 – Is the DGS operationally capable of making the repayable amount available within seven working days (e.g. based on recent real-life cases, or the results of the DGS stress tests)? Please explain.	

Assessment methodology to be used by the EBA

Questionnaire 3 on DGS criteria 3 of Article 24(4) LCR DR *'(c) the deposit guarantee scheme ensures a seven working day repayment period as referred to in Article 8(1) of Directive 2014/49/EU from the date of application of the 3% outflow rate.'*		
Relevant paragraph of Article 8 of Directive 2014/49/EU on Financing of DGSs	**Question**	**Methodology**
1 - Do you consider that the DGS meets the requirement in the Delegated Regulation on LCR to '*ensure a seven working day repayment period as referred to in Article 8(1) of Directive 2014/49/EU from the date of application of the 3% outflow rate'*? [Yes/No] To further justify your reply to this question, please provide answers to the remaining questions in this form.		The DGS self-assessment will be taken into account but it is not enough in itself for an EBA assessment of compliance. The EBA's assessment might potentially lead to a different conclusion. The EBA will assess the rest of the information in this questionnaire and any clarification or additional information obtained from the DGS designated authorities to raise its opinion on the compliance with this condition.
1	2 – Is the DGS already legally required to make the repayable amount available within seven working days? Please attach copy of the relevant legal provision or document.	The methodology will assess if this repayment period has been transposed into the national rules without any transitional period. If the transitional period has been used, it will be assessed whether there is a formal, unambiguous, legally binding and enforceable commitment made by the relevant DGS, confirmed by its DGS designated authority, if different, where it commits to make the repayable amount available within seven working days or refuses to make use of the transitional period.
1	3 – Is the DGS operationally capable of making the repayable amount available within seven working days (e.g. based on recent	The EBA will assess if the results of the stress tests or any recent real-life cases can demonstrate the capability of repayment in seven working days.

	real-life cases, or the results of the DGS stress tests)? Please explain.	

THIRD SECTION

Review of the effects of past guidance: Non-operational deposits and excess operational deposits, retail deposits excluded from outflows

7. Non-operational deposits and excess operational deposits - Review

202. The first EBA report on monitoring the LCR implementation in the EU, from July 2019, provided policy guidance on the treatment of operational wholesale deposits received (Article 27 of the LCR DR). Specifically, the report provided policy guidance in the form of a couple of possible prudent approaches and good practices for estimating the 'excess operational deposits' within the operational deposits, which need to be treated as non-operational. The report also provided some examples of specific transactions that should fall under operational deposits and others that should not.

203. This section monitors the practical implementation of the practices suggested in the first report.

7.1 Observations

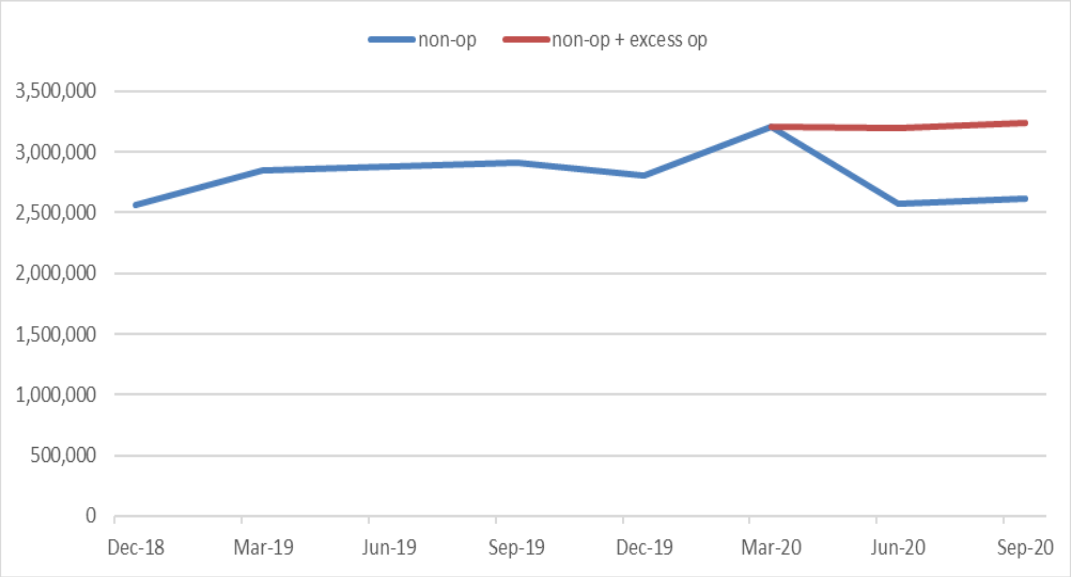
204.

205. Figure 4 Evolution of non-operational deposits and excess operational deposits (€M)

206. shows aggregated figures for all the banks in the EBA sample of the evolution of non-operational deposits reported. In parallel to this, the figures reported in September 2020 on non-operational deposits and excess operational deposits[47] are shown together.

Figure 4 Evolution of non-operational deposits and excess operational deposits (€M)

[47] The part of the operational deposit that is not necessary for the provision of operational services and that subsequently will not receive the preferential outflow treatment envisaged for operational deposits



207. Clearly, the amount of non-operational deposits reported decreases from April 2020. This is due to the segregation of the amount of excess operational deposits following the update of the ITS on LCR reporting applicable since April 2020. The amount of excess operational deposits was reported within non-operational deposits until March 2020.

208. Competent authorities and banks have generally confirmed the implementation of the EBA guidance in the assessment of the amount of excess operational deposits.

209. Looking at the evolution of deposits subject to the treatment of non-operational deposits (non-operational deposits per se plus excess of operational deposits) the trend seems to experience a slight increase, particularly from December 2019.

210. The slightly increasing trend of non-operational deposits, particularly from December 2019, seems to confirm the expectations around the application of the guidance published in the first report, where it also acknowledged the lack of a harmonised approach in the identification of excess operational deposits or even the absence of recognition.

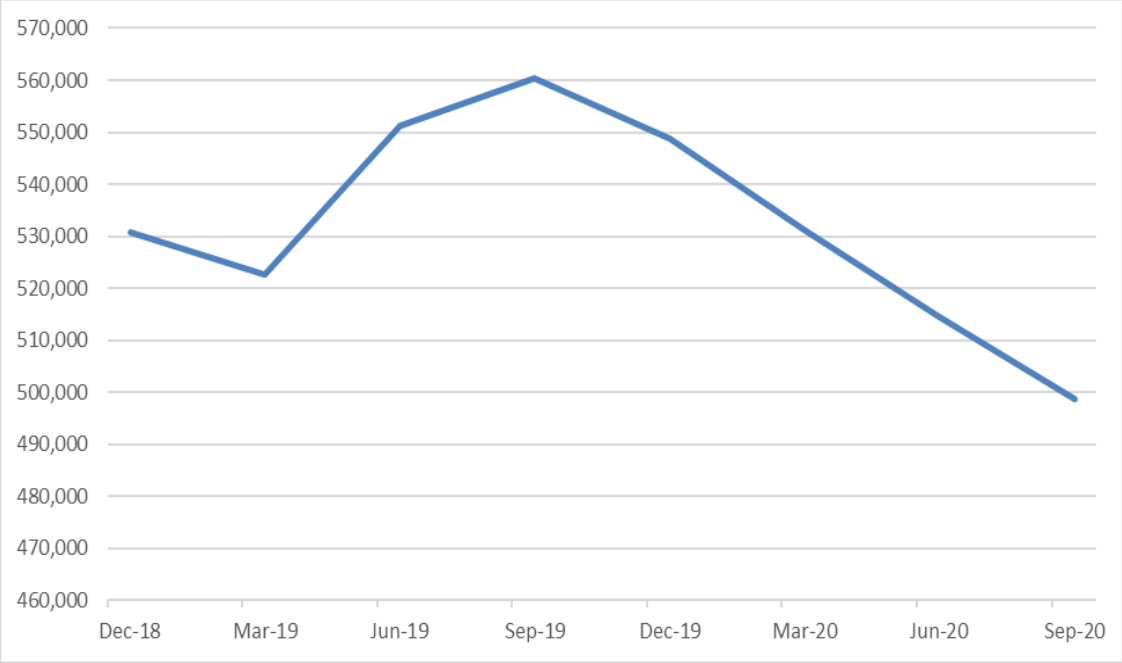
8. Retail deposits excluded from outflows - Review

8.1 Observations

211. The first EBA report on monitoring the LCR implementation in the EU, from July 2019, provided guidance for the identification of a material early withdrawal penalty in retail deposits maturing beyond 30 days that would allow them to be exempted from outflows.

212. Figure 5 reflects the evolution of exempted retail deposits reported from December 2018 to September 2020 with aggregated figures for all the banks in the EBA sample. These figures should capture potential changes in the approach followed for their identification due to the policy guidance of the July 2019 EBA report and better-quality data with the amendments in the ITS on LCR reporting from April 2020.

Figure 5 Evolution of exempted retail deposits (€M)



213. From September 2019 there has been a decreasing trend in the amounts reported.

214. The policy guidance provided to identify early withdrawal penalties was considered to be prudent and more conservative than the approaches previously followed in practice in many cases. From this perspective, a reduction of the amounts reported under exempted retail deposits is consistent with the application of the guidance. Again, competent authorities and banks have generally confirmed the use of the EBA guidance for the identification of a material early withdrawal penalty.

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