



EBA/ITS/2014/02

28 March 2014

EBA FINAL draft implementing technical standards

On currencies with an extremely narrow definition of central bank eligibility under Article 416(5) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR)

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Abbreviations

BCBS	Basel Committee on Banking Supervision
BGN	Bulgarian Lev
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
ITS	Implementing Technical Standard
LCR	Liquidity Coverage Ratio
SFT	Secured Financing Transaction

1. Executive summary

Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR) sets out prudential requirements for liquidity.

The CRR contains specific mandates in a number of different articles for the EBA to develop draft regulatory or implementing technical standards (RTS and ITS) related to liquidity and liquidity reporting requirements. These standards will be part of the ‘single rule book’ enhancing regulatory harmonisation in the European Union.

Main features of the ITS

These final draft ITS have been drawn up pursuant to Article 416(5) of the CRR which mandates the EBA to list the currencies with an extremely narrow definition of central bank eligibility. For these currencies, Article 416(3)(d) of the CRR shall not apply, and subject to fulfilling the remaining conditions of Articles 416 and 417 of the CRR, institutions may report as liquid assets those that are not eligible collateral for standard liquidity operations of a central bank in a Member State or those that are held to meet liquidity outflows in the currency of a third country, of the central bank of that third country. This derogation ensures that institutions will be able to meet the liquidity requirements in currencies in which extremely narrow central bank eligibility exists by holding assets in the liquidity buffer that are not eligible at the relevant central bank, but are otherwise liquid.

In the final draft ITS, the list of currencies has been based on the assumption that an extremely narrow definition of central bank eligibility applies if only central government debt or debt issued by the central bank is eligible as collateral for standard liquidity operations at the central bank. This reflects the EBA’s view that central bank eligibility gives important support to the liquidity of assets, and that a central bank eligibility framework should be considered as extremely narrow only where the framework seems to have excluded any broader type of liquid asset class that meets the remaining requirements of Articles 416 and 417 of the CRR as eligible collateral. The EBA deems this situation to be likely where central bank eligibility is limited to central government debt or debt issued by the central bank.

Through a data-gathering exercise among Member States the EBA ascertained the asset classes that constitute central bank eligible assets for standard liquidity operations. The data show that during the financial crisis, central bank eligibility criteria were extended to include asset classes that were not eligible prior to the crisis. This varies widely, however, among EEA central banks. Within the EEA, the list of central bank eligible assets in the euro zone is among the widest, while central banks in countries such as the United Kingdom, Denmark, Norway and Sweden also allow a wide range of assets as collateral. On the other hand, other central banks such as those of the Czech Republic and Iceland have a quite narrow range of liquid assets that fulfil central bank

eligibility criteria. In Bulgaria, the central bank does not extend liquidity to institutions except in extreme circumstances pursuant to Article 33 of the Law on the Bulgarian National Bank.

Taking the extremely narrow definition of central bank eligibility as that limited to central government debt or debt issued by the central bank, and the information provided by Member States, there is just one currency falling into this category, namely the Bulgarian Lev.

Currencies outside the EEA were not included in the evaluation, because of, inter alia, constraints to data availability. In addition, the EBA considers it preferable to consider non-EEA currencies in the light of the assessments of the definition of central bank eligibility as performed by the relevant non-EEA jurisdiction itself.

To keep the ITS updated, the EBA will repeat its analysis whenever a change (or series of changes) occurs that is likely to have a major impact on the outcome. This implies that in the event of a decisive change in central bank eligibility, a review of the ITS for the relevant currency will be triggered.

The EBA assessed the responses received once the consultation had closed on 22 December 2013. This assessment led to the conclusion that no changes should be made to the version of the draft ITS on which the consultation had been based.

The EBA has submitted the draft to the European Commission.

2. Background and rationale

Background and regulatory approach followed in the final draft ITS

In January 2013, the Basel Committee on Banking Supervision (BCBS) published a revised text of its rules on the liquidity coverage ratio (LCR).¹ The LCR is intended to promote the short-term resilience of the liquidity risk profile of banks. It does this by ensuring that banks have an adequate stock of unencumbered high quality liquid assets (HQLA) that can be converted easily and immediately in private markets into cash to meet their liquidity needs for a 30-calendar-day liquidity stress scenario. The LCR should improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source, thus reducing the risk of spillover from the financial sector to the real economy.

The BCBS has outlined in paragraph 26 of its revised rules text that HQLA, excluding certain level 2B assets, 'should ideally be eligible at central banks for intraday liquidity needs and overnight liquidity facilities', noting that in the past 'central banks have provided a further backstop to the supply of banking system liquidity under conditions of severe stress'. However as an exception, the BCBS notes that 'in jurisdictions where central bank eligibility is limited to an extremely narrow list of assets, a supervisor may allow unencumbered, non-central bank eligible assets [...]'. The CRR also seeks to provide for such circumstances in that Article 416(3)(d) of the CRR provides for institutions to report as liquid assets, subject to fulfilling the remaining conditions of Articles 416 and 417 of the CRR, those that are eligible collateral for standard liquidity operations of a central bank in a Member State or those that are held to meet liquidity outflows in the currency of a third country, of the central bank of that third country. Article 416(3) of the CRR, final sub-paragraph, outlines that this condition concerning central bank eligibility shall not apply in the case of liquid assets held to meet liquidity outflows in a currency in which there is an extremely narrow definition of central bank eligibility.

The final draft ITS have been drawn up pursuant to Article 416(5) of the CRR which mandates the EBA to list the currencies in which there is an extremely narrow definition of central bank eligibility. For these currencies, Article 416(3)(d) of the CRR shall not apply and subject to fulfilling the remaining conditions of Articles 416 and 417 of the CRR, institutions may report as liquid assets those that are not eligible collateral for standard liquidity operations of a central bank in a Member State or those that are held to meet liquidity outflows in the currency of a third country, of the central bank of that third country. This derogation ensures that institutions will be able to meet the liquidity requirements in currencies in which extremely narrow central bank eligibility exists by holding in the liquidity buffer assets that are not eligible at the relevant central bank, but are otherwise liquid.

¹ Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools - <http://www.bis.org/publ/bcbs238.htm>

In the final draft ITS, the list of currencies has been based on the assumption that an extremely narrow definition of central bank eligibility applies only if central government debt or debt issued by the central bank is eligible as collateral for standard liquidity operations at the central bank. This reflects the EBA's view that central bank eligibility gives important support to the liquidity of assets, and that central bank eligibility framework should be considered as extremely narrow only where the framework seems to have excluded any broader type of liquid asset class that meets the remaining requirements of Articles 416 and 417 of the CRR as eligible collateral. The EBA deems this situation to be likely where central bank eligibility is limited to central government debt or debt issued by the central bank.

The EBA completed a data-gathering exercise among Member States to ascertain the asset classes that constitute central bank eligible assets for standard liquidity operations and then to draw up in the ITS the list of currencies with narrow central bank eligibility. Data were collected on whether or not the eligibility for the standard central bank liquidity operations went beyond central government debt or debt issued by the central bank. For this assessment, it was not relevant whether institutions tended to choose only a more limited set of collateral; for example, if institutions did not pledge certain asset types because of large haircuts, then for the purposes of these ITS, the EBA still counted this asset class as included in the definition of central bank eligibility.

The data are shown in Table 1 and indicate that during the financial crisis, central bank eligibility criteria were extended to include asset classes that were not eligible before the crisis. This varies widely, however, among EU central banks. Within the European Union the list of central bank eligible assets in the euro zone is the widest, although central banks in countries such as the United Kingdom, Denmark, Norway and Sweden also allow a wide range of assets as collateral. Typically this includes covered bonds, debt instruments issued by corporate and asset-backed securities. On the other hand, other central banks such as those of the Czech Republic and Iceland have a quite narrow range of liquid assets that fulfil central bank eligibility criteria. In the Czech Republic, it is only supranational debt instruments and in Iceland it is only securities unconditionally guaranteed by the central government that are included in the definition of central bank eligibility in addition to central government debt or debt issued by the central bank. In Bulgaria, the central bank does not extend liquidity to institutions except in extreme circumstances pursuant to Article 33 of the Law on the Bulgarian National Bank, which states: 'Upon emergence of a liquidity risk that may affect the stability of the banking system, the Bulgarian National Bank may extend to a solvent bank leva-denominated credits with maturity no longer than three months, provided they are fully collateralised by gold, foreign currency or other such highly liquid assets.'

Taking the extremely narrow definition of central bank eligibility as that limited to central government debt or debt issued by the central bank, and the information provided by Member States, there is just one currency falling into this category, namely the Bulgarian Lev.

Currencies outside the EEA were not included in the evaluation, because of, inter alia, limits on data availability. In addition, the EBA considers it preferable to consider non-EEA currencies in the light of the assessments of the definition of central bank eligibility as performed by the relevant non-EEA jurisdiction itself.

To keep the ITS updated, the EBA will repeat its analysis whenever a change (or series of changes) occurs that is likely to have a major impact on the outcome. This implies that in the event of a decisive change in central bank eligibility, a review of the ITS for the relevant currency will be triggered.

Table 1: Central bank eligible assets per country

Central bank eligible assets	Bulgaria	Croatia	Czech Republic	Denmark	Euro area	Hungary	Iceland	Latvia	Lithuania	Norway	Poland	Romania	Sweden	United Kingdom
Debt instruments issued by central banks	no (1)	yes	yes	yes	yes	yes	yes	no	no	yes	yes	yes	yes	yes
Central government debt instruments	no (1)	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes
Supranational debt instruments	no (1)	yes	yes	no	yes	yes	no	no	no	yes	yes (only EIB) (4)	yes	yes	yes
Securities unconditionally guaranteed by the central government	no (1)	yes	no	yes	yes	yes	yes	yes (3)	yes (6)	yes	no	no	yes	yes
Local and regional government debt instruments	no (1)	no	no	yes	yes	yes (2)	no	no	no	yes	yes (4)	no	yes	no
Covered bonds	no (1)	no	no	yes	yes	yes (2)	no	yes (3)	no	yes	yes (4)	no	yes	yes
Debt instruments issued by corporate and other issuers	no (1)	no	no	no	yes	yes (2)	no	yes (3)	no	yes	yes (4)	no	yes	yes
Credit institutions debt instruments (other than covered bonds)	no (1)	no	no	yes (8)	yes	yes (2)	no	yes (3)	no	no	no	no	no	no
Asset backed securities	no (1)	no	no	no	yes	no	no	no	no	yes (4)	no	no	yes (5)	yes
Credit claims	no (1)	no	no	yes	yes	no	no	no	yes	no	no	no	no	yes
Residential mortgage backed debt instruments (rmbs)	no (1)	no	no	no	yes	no	no	no	no	no	no	no	no	yes
Other assets	no (1)	no	no	yes (9)	yes	no	no	no	yes (7)	no	no	By decision of CB	no	no
(1) Subject to currency boards arrangements														
(2) Allowed in principle, but only few requirements meet the requirements														
(3) Allowed in principle, but not used in practice														
(4) Subject to conditions														
(5) Only until 31. December 2013														
(6) State guarantees														
(7) Includes credit institution warranties, and guarantees issued by procedure established by the Government and other asset by decision of the Central Bank														
(8) Only debt instruments issued in connection with mortgage-credit financing. Not uncollateralised senior debt in general														
(9) Only temporarily														

3. EBA final draft implementing technical standards on currencies with an extremely narrow definition of central bank eligibility under Article 416(5) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR)



Brussels, **XXX**
[...](2013) **XXX** draft

COMMISSION IMPLEMENTING REGULATION (EU) No .../..

of **XXX**

COMMISSION IMPLEMENTING REGULATION (EU) No .../...
laying down implementing technical standards with regard to currencies in which there
is an extremely narrow definition of central bank eligibility according to Regulation
(EU) No 575/2013 of the European Parliament and of the Council

COMMISSION IMPLEMENTING REGULATION (EU) No .../..

of XXX

COMMISSION IMPLEMENTING REGULATION (EU) No .../...
laying down implementing technical standards with regard to currencies in which
there is an extremely narrow definition of central bank eligibility according to
Regulation (EU) No 575/2013 of the European Parliament and of the Council

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,
Having regard to Regulation (EU) No 575/2013 of 26 June 2013 of the European
Parliament and of the Council on prudential requirements for credit institutions and
investment firms and amending Regulation (EU) No 648/2012¹, and in particular Article
416(5) thereof,

Whereas:

- (1) The Basel Committee on Banking Supervision has developed international standards regarding the liquidity coverage ratio and liquidity risk monitoring tools², which in particular establish that the requirement for liquid assets to be eligible as collateral in central bank credit operations does not need to apply to currencies with an extremely narrow definition of central bank eligibility.
- (2) The list of currencies with an extremely narrow definition of central bank eligibility should be limited to those currencies where central bank eligibility is confined to central government debt and debt issued by the central bank and so does not extend to any other assets which comprise liquid assets in accordance with the remaining requirements of Articles 416 and 417 CRR.
- (3) The assessment should be based on the best available data that can be supplied by competent authorities to the European Supervisory Authority (European Banking Authority) (EBA) on central bank eligibility in a given currency.
- (4) This Regulation is based on the draft implementing technical standards submitted by EBA to the Commission.
- (5) EBA has conducted open public consultations on the draft implementing technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010,

¹ OJ L 176, 27.6.2013, p. 1.

² Basel Committee on Banking Supervision, Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools, January 2013.

HAS ADOPTED THIS REGULATION:

Article 1

Currencies with extremely narrow central bank eligibility

The currencies which meet the conditions referred to in the third subparagraph of Article 416(3) of Regulation (EU) No 575/2013 are listed in the Annex.

Article 2

Final Provisions

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Commission
The President

On behalf of the President
[Position]

Annex

- Bulgarian lev (BGN)

4. Accompanying documents

4.1 Cost-benefit analysis / impact assessment

Introduction

1. Article 15(1) of the EBA Regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council) provides that when any draft implementing technical standards developed by the EBA are submitted to the European Commission for adoption, they shall be accompanied by an analysis of ‘the potential related costs and benefits’. This analysis should provide an overview of the findings regarding the problem to be dealt with, the solutions proposed and the potential impact of these options.

2. This note outlines the assessment of the impact of the draft ITS concerning currencies with an extremely narrow definition of central bank eligibility under Article 416(5) of the CRR.

Problem definition

Issues addressed by the European Commission (EC) regarding liquidity management

3. In its impact assessment of the CRD IV framework, the European Commission noted that the existing liquidity risk management approaches and supervisory regimes inadequately captured risks inherent in the underlying market practices and trends. These shortcomings contributed to the failure of several institutions and greatly undermined the financial health of many others, threatening financial stability and requiring unprecedented levels of central bank liquidity and government support.

4. The CRR proposes two minimum standards for funding liquidity to address this issue. One of these requirements is the liquidity coverage requirement, which is intended to ensure that an institution has enough high quality liquid assets to survive an acute stress scenario lasting for 30 days. This requirement will help achieve the general objectives of CRD IV, as well as the following two specific objectives:

- ▶ enhancing adequacy of capital and liquidity requirements
- ▶ enhancing bank risk management

5. To meet the liquidity coverage requirement, institutions must hold a stock of high quality liquid assets (HQLA) to cover the total net cash outflows over a 30-day period. These assets should be liquid during a time of stress and be eligible for central bank refinancing operations. However, in some jurisdictions where there are insufficient HQLA available, the CRR allows

institutions to use derogations to meet the requirements of the liquidity coverage requirement in line with what has been incorporated in the Basel III framework.

Issues addressed by the technical standards

6. The CRR mandates the EBA to develop draft implementing technical standards to list the currencies with an extremely narrow definition of central bank eligibility. For those currencies, the requirement in Article 416(3)(d) of the CRR, that liquid assets held by institutions should be eligible collateral for standard central bank liquidity operations, does not have to be met.

7. These ITS list the currencies for which the EBA identified that an extremely narrow definition of central bank eligibility may excessively constrain the amount of liquid assets available to meet the liquidity coverage requirement.

Methodology used and results

8. The EBA collected qualitative data on eligible collateral used in standard central bank liquidity operations. The analysis shows that the list of central bank eligible assets is wide in most currencies. The list often includes different types of assets beyond central government and central bank debt. The only currency for which the definition of central bank eligible assets is deemed extremely narrow is the Bulgarian Lev (BGN).

Impact

Costs

9. The EBA identified only one currency for which an extremely narrow definition of central bank eligibility applies. The number of institutions operating in this currency is small and the total assets that they hold represents only a small share of the total assets held by the banking sector in the EEA. The risk of creating an uneven playing field for the application of the liquidity coverage requirement is, therefore, not significant.

Benefits

10. These ITS will ensure that currencies with insufficient liquid assets due to an extremely narrow definition of central bank eligibility are identified using one and the same methodology. It will also ensure that institutions operating in these currencies may, if appropriate, use the derogation to meet their liquidity coverage requirements without impeding the liquidity of the financial markets in which they operate.

4.2 Feedback on the public consultation

The EBA publicly consulted on the draft proposal contained in this paper.

The consultation period lasted two months and ended on 22 December 2013. Ten responses were received, of which six were published on the EBA website.

This paper presents a summary of the key points and other comments arising from the consultation, the analysis and discussion triggered by these comments.

In many cases, several industry bodies made similar comments or the same body repeated its comments in the response to different questions. In such cases, the comments, and EBA analysis, are included in the section of this paper that the EBA considers the most appropriate.

No changes to the draft ITS have been made as a result of the responses received during the public consultation.

Summary of key issues and the EBA's response

General comments

Respondents generally welcomed the opportunity to comment on the EBA's proposal. Some respondents requested a slight broadening of the 'extremely narrow definition of central bank eligibility'.

The EBA response

The EBA remains of the view that extremely narrow central bank eligibility only applies where eligibility is limited to central government debt or debt issued by the central bank. This reflects the EBA's view that central bank eligibility gives important support to the liquidity of assets, and that the central bank eligibility framework should be considered as extremely narrow only where the framework seems to have excluded any broader type of liquid asset class. There seem to be no compelling reasons to widen the 'extremely narrow definition of central bank eligibility'.

Summary of responses to the consultation and the EBA’s analysis

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
General comments			
	Some respondents requested a slight broadening of the ‘extremely narrow definition of central bank eligibility’.	The EBA remains of the view that extremely narrow central bank eligibility only applies in those cases where eligibility is limited to central government debt or debt issued by the central bank. This reflects the EBA’s view that central bank eligibility gives important support to the liquidity of assets, and that the central bank eligibility framework should be considered as extremely narrow only where the framework seems to have excluded any broader type of liquid asset class.	No amendments made
Responses to questions in Consultation Paper EBA/CP/2013/37			
Question 1. Do you agree with the general approach and its results?	Three respondents argue that the CZK and RON should also be classified as currencies with an extremely narrow definition of central bank eligibility due to their strict eligibility criteria. The respondents propose that the ‘extremely narrow definition of central bank eligibility’ should be widened to include supranational debt, which would lead to the CZK and RON being classified as currencies with extremely narrow central bank eligibility. This would however not substantially change the original definition of ‘extremely narrow central bank eligibility’, as the proportion of most banks’ counter balancing capacity (CBC) that consists of supranational debt would not be	The EBA remains of the view that extremely narrow central bank eligibility only applies in those cases where eligibility is limited to central government debt or debt issued by the central bank. This reflects the EBA’s view that central bank eligibility gives important support to the liquidity of assets, and that the central bank eligibility framework should be considered as extremely narrow only where the framework seems to have excluded any broader type of liquid asset class.	No amendments made

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	material.		
<p>Question 2.</p> <p>Do you agree with the above analysis of the cost and benefit impact of the proposals?</p>	No responses.	No comments.	No amendments made.

