14 September 2012

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 BASEL, SWITZERLAND

Via email: baselcommittee@bis.org

Re: Request for comment on consultative document – monitoring indicators for intraday liquidity management

Ladies and gentlemen:

The Global Financial Markets Association[1] ("GFMA") appreciates the opportunity to provide comments on the Basel Committee on Banking Supervision's ("BCBS") consultative document regarding monitoring indicators for intraday liquidity management ("consultative document"). GFMA supports the BCBS's ongoing efforts to promote enhanced intraday liquidity risk management practices and supervisory tools originally outlined in Principal 8 of the BCBS's *Principles for Sound Liquidity Risk Management and Supervision* (September 2008).

In addition to responding to the five questions specifically raised in the consultation paper, GFMA wishes to highlight several items for the BCBS to consider. The following section highlights six practical concerns with the proposed framework and offers suggestions on how to ensure that the data collected helps the BCBS achieve its stated objectives.

Issues for Consideration

Our main concern is that the amount and nature of data proposed for monitoring in the consultative document significantly exceeds what banks are now providing, or what is contained in the proposed Basel III liquidity coverage ratio ("LCR") framework, the G-SIB common data template, the U.K. FSA's Individual Liquidity Adequacy Assessment, or other national and international reporting regimes. Moreover, the consultative document provides little clarity with regard to how supervisors expect to use the data collected. While the proposal states that "It should be noted that the

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[1] The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, visit http://www.gfma.org.

proposed indicators are for monitoring purposes only and do not represent the introduction of new standards around intraday liquidity management", we think it is realistic to expect that the introduction of metrics such as these could lead to supervisory expectations, if not standards, regarding intraday liquidity. For these reasons, we strongly encourage the BCBS to move slowly, with ample dialog and testing before making any final decisions about this framework. Specifically, we urge the BCBS to:

- <u>Provide more specific details on how supervisors plan to use the monitoring indicators, particularly in conjunction with qualitative risk management measures</u>. While the consultative document notes that the aim of the indicators is to "enable banking supervisors to monitor a bank's intraday liquidity risk management and its ability to meet payment and settlement obligations on a timely basis", the lack of concrete objectives makes it difficult for industry to comment on their appropriateness or fully address the questions posed by the BCBS. Moreover, it is important to acknowledge that effective intraday liquidity risk management involves both qualitative and quantitative measures and controls. While the stated purpose of the consultative document does not include qualitative risk management controls, one also must consider and evaluate the impact of effective governance, reporting, and risk communication. GFMA recommends that the BCBS provide additional information about the expected use of data collected through the monitoring exercise and highlight how supervisors will use quantitative and qualitative inputs when evaluating risk levels and liquidity risk management practices. As described in more detail below, the lack of clarity presents additional concerns should the indicators become standards and/or require public disclosure.

- <u>Consider the cost/benefit for enhanced reporting requirements prior to finalizing the framework</u>. Given the large amount of data requested from institutions and the equally significant burden on supervisors for analyzing the data, GFMA recommends that the BCBS evaluate the cost/benefit of collecting all of the indicators and with the granularity outlined in the consultative document. This is particularly important as the BCBS and national supervisors evaluate how they plan to use the data collected to better understand the intraday liquidity risk profiles of financial institutions.

  To that end, we believe that several indicators represent more of a test of institutions' liquidity monitoring systems than a measure of the intraday liquidity risk exposure. This oftentimes limits the utility of collecting the monitoring indicators. For example, indicator (vi) *intraday credit lines extended to financial institution customers* provides little insight into the risk position of a bank. Such credit lines are uncommitted and unadvised, meaning that borrowing institutions are unaware of the total amount of available credit. Therefore, there is virtually no risk if the lending bank were to limit or eliminate the intraday credit line in a period of stress. Indicator (vii) *timing of intraday payments* can be misleading, particularly when comparing the payment behavior across different jurisdictions. For example, the timing of payments in the U.S.'s Fedwire system generally is concentrated at the end of the day, while the U.K.'s CHAPS system shows a more even distribution of payments. This is due to throughput rules in the United Kingdom that require a certain percentage of average daily payments to be made throughout the day. Indicator (viii) *intraday throughput* presents issues for similar reasons.

Finally, we encourage the BCBS to evaluate alternative sources of data. Given the role that central banks play in maintaining and operating the payment systems in many jurisdictions, supervisors may find that such entities are able to provide helpful data without requesting the information from participating institutions.

- Avoid transitioning monitoring indicators into regulatory standards. While GFMA believes that collecting and reviewing certain intraday liquidity risk metrics could help supervisors evaluate trends in risk levels, there is a danger to developing formal – or even informal – quantitative limits. Doing so could have unintended consequences as participants may delay payments until later in the day so as to reduce the timing gap between cash outflows and inflows, thereby reducing their daily maximum liquidity requirements. This practice increases operational risk and systemic risk related to managing and participating in payment systems. Regulatory standards also could result in market expectations for the disclosure of metrics, which, when viewed without the appropriate context, could expose certain institutions to unnecessary or unjustified scrutiny.

- Create an industry working group to discuss the utility of monitoring metrics and resolve specific operational issues. GFMA recommends that the BCBS form an international industry advisory group comprised of direct and indirect payment and settlement system participants. This group can support the BCBS as it finalizes the intraday reporting framework and highlight specific implementation challenges. This forum could be particularly helpful when considering some of the key application issues outlined in the consultative document and, particularly, as institutions address the reporting harmonization and stress testing aspects of the reporting framework. It also could be a helpful venue to inform supervisors of institutions' governance and controls practices related to intraday liquidity risk. For example, effective controls mitigate risk and allow participants to delay or stop payments if they anticipate problems with a counterparty.

- Adopt a measured approach to implementation. GFMA suggests that if the BCBS does proceed with an intraday reporting framework, it conduct an observation period first. An observation period would allow the BCBS 1) to understand if the data collected will serve the goals articulated by the BCBS; 2) uncover any ambiguities of standards or definitions, or inconsistencies of interpretation; and 3) to determine obstacles to collecting the data. An observation period would allow the reporting framework to go forward on a best-efforts basis and provide supervisors with significantly more information than currently exists on intraday liquidity risk profiles, while building in some flexibility to adjust the framework based on the observation period experience. This approach also would provide some relief to institutions that already have committed significant technical, operational, and business resources to addressing existing and emerging reporting requirements, such as the Basel III liquidity framework and the Financial Stability Board's common data template.

- Ensure confidentiality of data. GFMA urges the BCBS to establish a secure foundation for protecting the confidentiality of data to be shared among supervisors and authorities. Our members are concerned about confidentiality protections and information-sharing protocols. There needs to be strong governance over the use and disclosure of the data, with clear accountabilities to ensure confidentiality. We would like an opportunity to comment on the agreed arrangements.

Response to Questions Posed by the BCBS

(i) Do the proposed indicators adequately capture the intraday liquidity risk run by banks?

We believe that most of the proposed indicators provide a helpful picture of the intraday liquidity risk borne by direct and indirect payment and settlement systems participants, although such a picture could be provided with fewer indicators. As discussed in the above section, we believe that several of the indicators provide only incremental insight as to the intraday liquidity risk profile of institutions, particularly when evaluated against the level of effort required to develop reports and analyze the data. Notwithstanding the adequacy of the data collected, GFMA questions the statistical significance of the monitoring indicators, given that they are an average of daily data over a one month period.

Clarity on the definition of various indicators will help industry provide additional comments on their adequacy. For example, GFMA would appreciate further clarification regarding terms related to indicators (v) *value of customer payments made on behalf of financial institution customers* and (vi) *intraday credit lines extended to financial institution customers.* Do "financial institution customers" include non-bank clients, such as investment funds, insurance companies, or pension funds? Do "intraday credit lines" include lines of credit used to support business as usual clearing and settlement activities as well as backup/contingent liquidity facilities?

(ii) Are the stress scenarios identified in the paper comprehensive?

The stress scenarios are consistent with Principal 10 of BCBS's *Principles of Sound Liquidity Risk Management and Supervision* (September 2008). They address both idiosyncratic and systemic stress scenarios and consider the impact of external factors on an institution's ability to maintain adequate intraday liquidity. However, it also is important to consider whether the scenarios are consistent with other required stress testing firms have to undertake as part of international and national requirements, including their recovery and resolution planning. The GFMA would appreciate clarification as to how the proposed stress tests should align with those of Basel III's LCR and expectations regarding the application of liquidity buffers to intraday and inter-day business as usual and stress scenarios, the so called "double duty" issue. The treatment of liquidity buffers also applies to the calculation of indicator (ii) *available intraday liquidity*.

(iii) Is the proposed scope of application of indicators clear?

No. GFMA would appreciate further clarification on how the BCBS expects complex global institutions to consolidate reporting for subsidiaries that access payment and settlement systems in different ways in various jurisdictions and how disparate home and host supervisory requirements might affect reporting expectations. Inconsistent application presents additional operational challenges, particularly for institutions that use different systems in different regions and currencies or legal entities that are both direct and indirect participants (e.g., a German bank that self-clears euros, but relies on a correspondent for dollar clearing).

GFMA would appreciate additional information on how the intraday liquidity sources and uses may or may not be used in calculating the Basel III LCR. This is particularly important when allocating liquid assets to intraday and inter-day liquidity buffers. Should the proposed reporting exercise transition from monitoring to supervisory expectations, there could be a significant impact upon the LCR, especially if the intraday components are not more clearly defined.

Finally, we believe the BCBS should consider a materiality threshold for reporting indicators by currency. While paragraph 53 notes that "banks should also report the indicators at an individual currency level so that supervisors can monitor the extent to which firms are reliant on foreign exchange swap markets", we believe reporting should be limited to local currency and major currencies.

(iv) What, if any, implementation challenges would the proposed reporting requirements present to banks?

GFMA is concerned about the operational burden these reporting requirements present during both the development and production phases. Efforts to develop the report framework require staff and technical resources. Intangible costs include the opportunity cost of reallocating staff from other ongoing reporting initiatives. The use of an industry working group to identify unnecessary data elements or significant operational challenges can help to mitigate the cost of implementation, as would beginning any reporting with an observation period. These steps would also help ensure that supervisors have access to meaningful data.

In some cases, particularly for indirect participants, access to requested information may come from third parties such as correspondent banks. We urge the BCBS to consider such challenges when evaluating and finalizing the indicator reporting frequency and lag.

It also is important to consider the consistency of this reporting with other existing and emerging reporting requirements. Inconsistencies in definitions, reporting lags, etc. can have significant operational implications. To that end, it would be helpful if the BCBS could clarify paragraph 58, which notes that "banks are expected to report the monitoring indicators to their supervisor on a monthly basis in line with the proposed LCR reporting requirements." Does this mean that institutions must begin to provide the indicators to supervisors when the LCR is implemented in 2015 or simply that they should be reported with the same frequency as the LCR?

(v) Are the different monitoring and reporting requirements for direct and indirect payment and settlement system participants clear?

Yes, although please refer to our response to (iii) and (iv) for specific concerns regarding how the framework applies to direct and indirect market participants in the same holding company.

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The GFMA appreciates the opportunity to share our feedback on the consultative document. We welcome an ongoing dialogue with the BCBS as it continues to finalize the intraday liquidity risk reporting framework.

Sincerely,

Simon Lewis
CEO, GFMA