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FSA proposals for new bank / investment firm liquidity reporting regime

In December 2008, the FSA published a consultation paper, CP08/22, in which it set out its proposals for overhaul of the bank/investment firm liquidity regime. This new regime is intended to apply to all banks, building societies and investment firms, including UK branches of certain EEA and non-EEA banks. The FSA is currently preparing a Feedback Statement in relation to responses it has received to that consultation paper. On 15 April, the FSA published a further consultation paper, CP09/13, on the specific issue of liquidity reporting, an issue which was initially addressed in Chapter 8 of CP08/22 where certain pre-consultation material on reporting was set out. In setting out its final proposals on liquidity reporting in CP09/13, the FSA has taken into account the responses it has received on Chapter 8 of CP08/22.

The proposed reporting regime represents a radical overhaul of liquidity reporting which will give the FSA access to a large amount of new data. The FSA will publish a Policy Statement in the third quarter of 2009, addressing all elements of the new regime, including reporting. The FSA proposes that the new reporting arrangements go live in the first quarter of 2010. This article sets out certain important aspects of these proposals as well as issues relating to their implementation.

The FSA found firms to be broadly supportive of its proposals and its objectives. In its most recent paper the FSA has sought to address some of the concerns raised, in particular delaying the introduction of the new rules, with the reporting regime now coming into force in the first quarter of 2010; extending the submission deadlines for liquidity reporting; and specifically recognising the need to maintain a strong qualitative element in assessing a firm's liquidity risk profile through discussions between firms and their FSA supervisors. The FSA has also sought to address concern expressed over its own capability to manage what is a significant new regulatory oversight responsibility.

The FSA's proposals are more advanced than those in other countries raising concerns that the UK could suffer competitive disadvantage from a higher compliance burden assuming the FSA introduced the new liquidity reporting proposals unilaterally. The FSA stresses it is continuing to work in major international fora to promote standardised quantitative liquidity reporting, but the ambitious timetable for the introduction of a new regime in the UK is clearly not going to be delayed by failure to make progress internationally. Commentators remain divided on whether, by taking a leading position, the UK will gain from providing a more stable regulatory environment or will suffer if more stringent liquidity requirements make London less attractive as a base for financial services.

The proposed reporting regime

The reporting requirements proposed in CP09/13 will apply to all ILAS ("Individual Liquidity Adequacy Standards") firms (all BIPRU banks, building societies and investment firms and UK branches of EEA and non-EEA banks). Limited licence and limited activity investment firms will fall outside the ILAS requirement of the new liquidity regime and will therefore not be subject to the proposed quantitative reporting requirements. Instead the FSA will monitor the compliance by such firms qualitatively through the annual Systems and Controls questionnaire.

There are two degrees of stringency depending on whether the firm is a standard ILAS firm or a simplified ILAS firm. The less stringent reporting requirements for 'simpler ILAS firms' apply to those that are eligible for and opt for the proposed standardised buffer ratio regime set out in CP08/22. ILAS firms eligible for the standardised buffer ratio regime are those which have no foreign currency exposures in assets or liabilities; whose wholesale funding is no more than 30% of total funding; and where the majority of a firm's assets are mortgages secured on residential property. Qualifying firms are expected primarily to be smaller building societies and mortgage banks.

Standard ILAS BIPRU firms will be required to:

- Submit Enhanced Mismatch Report Daily Flows up to three months ahead to analyse survival periods and spot potential liquidity squeezes early. Reporting would be weekly, stepping up to daily reporting in a liquidity crisis (FSA047).

All ILAS BIPRU firms will be required to:

- Submit an Enhanced Mismatch Report aiming to capture the ILAS risk drivers and contractual flows across the full maturity spectrum and to collect behavioural information from firms on a standardised basis. Reporting for Standard ILAS BIPRU firms on the full regime would be weekly, stepping up to daily reporting in a liquidity crisis (FSA048). Reporting for Simplified ILAS BIPRU firms would be monthly, again, stepping up to daily reporting in a liquidity crisis (FSA049).
- Report on a monthly basis a more granular analysis of firms' marketable asset holdings (FSA050).
- Report on a monthly basis the firm's borrowings from unsecured wholesale funders (excluding primary issuance) by counterparty class, to identify concentrations on a firm- and market-wide basis (FSA051).
- Report on a weekly basis the firm's daily transaction prices and transacted volumes for wholesale unsecured liabilities by product, tenor (where appropriate) and currency, giving insight into system-wide financial stability (FSA052).
- Report on a quarterly basis the firm's retail and corporate funding profiles and the stickiness of various retail deposits, showing changing retail funding profiles (FSA053).
- Provide a monthly analysis of the foreign exchange exposures on the firm's balance sheet (FSA054).

The new reports replace the FSA's existing liquidity reporting requirements FSA010, FSA012 and FSA013 in their entirety and almost all of FSA011. In response to industry feedback, the FSA is also considering discontinuing FSA044.

Waivers and modifications

In addition to the less stringent regime for Simplified ILAS firms, there are also three types of waiver/modification packages available under the proposed regime:

- Whole-firm liquidity waivers replace the current Global Liquidity Concession (GLC) framework for UK branches of overseas banks and waive all of BIPRU 12.

- Whole-firm liquidity modifications permit branches to rely on the availability of liquidity resources from elsewhere in the firm for the purpose of meeting the overall liquidity adequacy rule.
- Intra-group liquidity modifications are relevant to firms that are part of a UK or international group and permit them to rely on liquidity support from elsewhere in the group for the purpose of meeting the overall liquidity adequacy rule.

The proposed conditions for granting a waiver or modification are outlined in BIPRU 12.8 set out in CP08/22.

Frequency of reporting and reporting deadlines

The frequency of reporting of key liquidity data items has been set to weekly or monthly under 'business-as-usual' conditions, but firms will be expected to have the capability to report these items on a daily basis under crisis conditions. The FSA is proposing to test this capability by periodically requesting daily reporting over a set time period, for example two weeks, as part of the normal supervisory relationship.

The FSA has also extended the reporting deadlines originally set out in CP08/22. Under the new proposals, during 'business-as-usual', the FSA is proposing to require firms to submit weekly data by end-of-day Monday for the previous week. Monthly and quarterly data will have to be submitted within three business days after the end of the reporting period. Annual submissions should be made within five business days of year end.

During periods of firm-specific or market crisis, the FSA is proposing that much of the data should be reported on a daily basis with a reporting deadline at the end of the business day immediately following the business day to which the data relate. The FSA note that supervisors will still expect to receive, on specific request, key data at the end of the day for that same day during periods of crisis.

Currency reporting

The FSA has amended its original proposal in CP08/22 for currency reporting and in response to industry feedback is proposing a more proportionate and risk-based approach requiring ILAS firms to submit a consolidated sterling report (FSA047 and FSA048). Reporting on any additional material currencies will now be agreed with firms bilaterally as part of the ILAS assessments but the FSA considers that it would not expect a firm to be asked to complete this data item in more than three material currencies in addition to the consolidated sterling report.

Legal entity basis for reporting

In line with indications given in CP08/22, the FSA is proposing that each individual ILAS firm will report separately, where applicable, on a solo basis and on a UK consolidation group and Defined Liquidity Group ("DLG") basis if a UK firm is a member of such a group. The reporting requirements on a UK consolidation group and DLG basis apply to UK firms only.

A DLG exists where a firm has an intra-group liquidity modification permitted by the FSA under the proposed regulations in which case the DLG includes each entity on whose liquidity support the firm is permitted to rely for the purpose of meeting the overall liquidity adequacy rule.

A DLG is defined where a firm does not have an intra-group liquidity modification under the regulations in which case the DLG includes each entity which is a member of the firm's group and (i) provides or is committed to provide material support to the firm against liquidity risk; (ii) the firm provides or is committed to provide material support to that entity against liquidity risk; or (iii) that entity has reasonable grounds to believe that the firm would supply such support, and vice versa.

The composition of a firm's DLG will be agreed between the firm and its supervisors to reflect accurately how liquidity is managed across the firm and wider group.

The FSA may also ask firms to submit solo returns from non UK regulated entities if they are relevant from a liquidity management perspective.

Compliance costs

In CP09/13 the FSA published the results of a survey of firms' expectations of compliance costs. The survey found that, for example, UK banks were expecting to incur a one-off cost of just under £3.3m with annual ongoing costs of around £950,000 during business as usual rising to in excess of £1.1m during times of crisis. Full-scope investment firms surveyed by the FSA were expecting compliance costs to be roughly double those expected by UK banks.

Implementation timetable and next steps

Consultation on CP08/22 closed on 4 March 2009 and the FSA deadline for responses to the latest paper, CP09/13, is 15 July 2009. The FSA intends to publish a final consultation paper in the second quarter of this year which will contain the transitional rules for the detailed switch on of the new regime. A Policy Statement covering all aspects of the new regime, including reporting, will be published in the third quarter of 2009 with the new rules and guidance coming into effect from the fourth quarter.

The FSA is planning to phase in the new reporting requirements with reporting of key data items – FSA047 (Daily Flows), FSA048 (EMR-Standard), FSA049 (EMR-Simplified) and FSA052 (Pricing data) – commencing from the first quarter of 2010. The FSA has not yet set a date for the subsequent collection of other data items.

The extended timetable set out in the April consultation paper is still challenging and will require detailed planning, significant investment in IT and staff training. Firms will need to ensure that their compliance officers and other relevant specialists are aware of the implications of the FSA's proposed liquidity risk management regime.

For more information on the topics covered in this issue, please contact:

Barnabas W.B. Reynolds
London
+44.20.7655.5528
barney.reynolds@shearman.com

Thomas Donegan
London
+44.20.7655.5566
thomas.donegan@shearman.com

Azad Ali
London
+44.20.7655.5659
azad.ali@shearman.com

James Brilliant
London
+44.20.7655.5612
james.brilliant@shearman.com

Aatif Ahmad
London
+44.20.7655.5120
aatif.ahmad@shearman.com

Katerina Rainwood
London
+44.20.7655 5156
Katerina.rainwood@shearman.com