



Council of the  
European Union

**Brussels, 2 February 2016  
(OR. en)**

**5759/16**

**EF 16  
ECOFIN 65  
DELECT 11**

**COVER NOTE**

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From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
date of receipt:	26 January 2016
To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union

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No. Cion doc.:	C(2016) 270 final
Subject:	COMMISSION DELEGATED REGULATION (EU) No .../.. of 26.1.2016 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards specifying the conditions for the application of the derogations concerning currencies with constraints on the availability of liquid assets

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Delegations will find attached document C(2016) 270 final.

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Encl.: C(2016) 270 final



Brussels, 26.1.2016  
C(2016) 270 final

**COMMISSION DELEGATED REGULATION (EU) No .../..**

**of 26.1.2016**

**supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards specifying the conditions for the application of the derogations concerning currencies with constraints on the availability of liquid assets**

(Text with EEA relevance)

## EXPLANATORY MEMORANDUM

### **1. CONTEXT OF THE DELEGATED ACT**

Article 419(5) of Regulation (EU) No 575/2013 ('the Regulation') empowers the Commission to adopt, following submission of draft standards by the European Banking Authority (EBA), and in accordance with Articles 10 to 14 of Regulation (EU) No 1093/2010, delegated acts specifying the derogations referred to in Article 419(2) of the Regulation concerning currencies with constraints on the availability of liquid assets, including the conditions of their application.

These derogations provide that the denomination of liquid assets may be inconsistent with the distribution by currency of net outflows, and/or liquid assets may be substituted by credit lines from the central bank. The derogations are intended to address the inherent difficulties that institutions would face in meeting their liquidity coverage requirement in such currencies where it is not possible to reduce, by sound liquidity management, the resultant need for liquid assets and given the holdings of those assets by other market participants.

In accordance with Article 10(1) of Regulation (EU) No 1093/2010 establishing the EBA, the Commission shall decide within three months of receipt of the draft standards whether to endorse the drafts submitted. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in those Articles.

### **2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT.**

In accordance with the third subparagraph of Article 10(1) of Regulation (EU) No 1093/2010, the EBA has carried out a public consultation on the draft technical standards submitted to the Commission in accordance with Article 423(3) of Regulation (EU) No 575/2013. A consultation paper was published on 22 October 2013 on the EBA internet site, and the consultation closed on 22 December 2013. Moreover, the EBA invited the EBA's Banking Stakeholder Group set up in accordance with Article 37 of Regulation (EU) No 1093/2010 to provide advice on them.

Together with the draft technical standards, the EBA has submitted an explanation on how the outcome of these consultations has been taken into account in the development of the final draft technical standards submitted to the Commission.

As specifically requested by the Commission, only the draft technical standard and explanatory memorandum are submitted to the Commission for adoption. All relevant accompanying information – notably the background and rationale of the draft technical standards, the impact assessment and the feedback on the public consultation – is included in the full version of the technical standards, which was approved by the EBA's Board of Supervisors and will be published on the EBA's public website: <http://www.eba.europa.eu/regulation-and-policy/liquidity-risk/draft-technical-standards-ts-on-currencies-with-constraints-on-the-availability-of-liquid-assets>.

### **3. LEGAL ELEMENTS OF THE DELEGATED ACT**

The provisions of these draft standards set out the derogations, and the conditions for their application, which have been specified with the following overarching objectives in mind. First, the application of a derogation should not be advantageous to the extent that, while it corrects for a disproportionate impact, it would lead to an uneven playing field between institutions. Second, the application of a derogation should not lead to undue risks for an institution. Third, the use of a derogation should be limited, and – in accordance with Article 419(3) of the Regulation – inversely proportional to the availability of the relevant assets.

Article 2 requires as a condition of using a derogation that an institution notify its competent authority of the proposed use, or a material change in use.

Article 3 sets out conditions which must be met for an institution to be considered to have justified needs for liquid assets in the relevant currency.

Article 4 specifies the derogation in point (a) of Article 419(2) of the Regulation. In particular it requires institutions to maintain effective systems which enable use of the derogation to be monitored and controlled, and requires a general additional 8% haircut to be applied to foreign currency liquid assets held to meet domestic currency net outflows to adjust for currency risk. This additional haircut can be lower in the case of a mutually supported currency peg and higher in the case of a currency which is not actively traded in global foreign exchange markets.

Articles 5 and 6 specify the derogation in point (b) of Article 419(2) of the Regulation. In particular it requires that the associated fee to be paid by institutions to the central bank offset the higher yield earned on the assets kept to secure the credit lines and, where applicable, also incorporate a charge which reflects the amount drawn down.

Article 7 ensures that the use of a derogation is inversely proportional to the availability of the relevant assets by limiting the total use of the derogations by institutions to the percentage specified in implementing technical standards containing a list of currencies with constraints on liquid assets adopted pursuant to Article 419(4) of the Regulation. This constitutes an approach to limiting the use of derogations which is sensitive to the actual shortage identified for that currency.

# COMMISSION DELEGATED REGULATION (EU) No .../..

of 26.1.2016

## supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards specifying the conditions for the application of the derogations concerning currencies with constraints on the availability of liquid assets

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012<sup>1</sup>, and in particular Article 419(5) thereof,

Whereas:

- (1) The Basel Committee on Banking Supervision has established international standards regarding the liquidity coverage ratio and liquidity risk monitoring tools<sup>2</sup> (BCBS standards).
- (2) In order to ensure effective oversight and application of the derogations provided for in Article 419(2) of Regulation (EU) No 575/2013 and effective monitoring of institutions' compliance with the requirements applicable to those derogations, in line with the BCBS standards, institutions should notify competent authorities when they intend to apply those derogations or when they intend to make a material change to the application of those derogations.
- (3) The BCBS standards establish guiding principles for supervisors in jurisdictions with insufficient high quality liquid assets. In line with Principle 3 of those guiding principles for supervisors, before applying any derogation, in order to demonstrate justified needs, institutions should take reasonable steps, to the extent practicable, to ensure that high quality liquid assets are used and reduce their overall level of liquidity risk to improve compliance with the liquidity coverage requirement.
- (4) In line with Principles 1 and 4 of the guiding principles for supervisors set out in the BCBS standards, it is necessary to ensure that institutions do not apply the derogations

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<sup>1</sup> OJ L 176, 27.6.2013, p. 1.

<sup>2</sup> Basel Committee on Banking Supervision, *Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools*, January 2013

as an economic choice that maximises their profits through the selection of alternative high quality liquid assets based primarily on yield considerations. In line with those principles it is also necessary to establish a mechanism for limiting the use of the derogations in order to mitigate risks of non-performance of the alternative assets. Taking into account the BCBS standards it is also necessary to provide for appropriate haircuts for the purposes of the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013 and to establish rules on the fee for the purposes of the derogation provided for in Article 419(2)(b) of that Regulation. In particular, as regards the derogation provided for in Article 419(2)(b) of Regulation (EU) No 575/2013, in order to ensure that the price paid by an institution for a central bank credit line is fair, the fee should be composed of two elements. The first should offset the higher yield earned on the assets kept to secure the credit line in order to ensure that the pricing reflects benefits which accrue independently of the amount currently drawn. The second should reflect the amount of the credit line drawn down.

- (5) In line with Principle 2 of the guiding principles for supervisors set out in the BCBS standards, the use of the derogations should be limited for all institutions with exposures in the relevant currency. Pursuant to Article 419(3) of Regulation (EU) No 575/2013, the derogations applied are to be inversely proportional to the availability of the relevant assets. For those reasons, the use of the derogations should be limited to a percentage of a credit institution's net liquidity outflows in the relevant currency which corresponds to the relevant shortage in liquid assets in that currency.
- (6) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority (EBA) to the Commission.
- (7) EBA has conducted open public consultations on the draft regulatory 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 of the European Parliament and of the Council<sup>3</sup>.
- (8) In accordance with the procedure in Article 15 of Regulation (EU) No 1093/2010, the Commission has endorsed with amendments the draft regulatory standard submitted by EBA after having sent the draft regulatory standard back to EBA explaining the reasons for the amendments. The EBA provided a formal opinion supporting those amendments,

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<sup>3</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

HAS ADOPTED THIS REGULATION:

*Article 1*  
*Subject matter*

This Regulation specifies the conditions for the application of the derogations referred to in Article 419(2) of Regulation (EU) No 575/2013 concerning currencies with constraints on the availability of liquid assets.

*Article 2*  
*Notification of the derogation*

1. A credit institution shall notify the competent authority that it intends to apply one or both of the derogations provided for in Article 419(2) of Regulation (EU) No 575/2013. The notification shall be provided in writing 30 days prior to the date of the first application of the derogation.

Where an institution intends to make any material change in its application of the derogation(s) as notified in accordance with the first subparagraph, it shall notify the competent authority thereof 30 days prior to the date of the first application of such change.

In exceptional circumstances where, due to sudden market developments, idiosyncratic events or other factors outside the control of the institution, it is not possible to notify the competent authorities of a material change 30 days prior to its first application, institutions shall provide a preliminary notification to competent authorities prior to the application of a material change. The preliminary notification shall provide a description of the nature of the material change together with an indication of the extent to which the intended derogation may be applied, expressed as a percentage of the liquid assets required to be held by an institution to meet its liquidity coverage requirement. The preliminary notification shall be completed by a notification in accordance with the second subparagraph within 30 days of the first application of any derogation.

Institutions shall notify competent authorities annually whether they intend to continue applying the derogation notified in accordance with the first subparagraph.

2. The notification referred to in the first subparagraph of paragraph 1 shall specify the following information:
  - (a) whether the notification relates to the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013 or the derogation provided for in Article 419(2)(b) of that Regulation, or both;
  - (b) confirmation of compliance with the conditions set out in Article 419(3) of Regulation (EU) No 575/2013 and the requirements of Article 3 of this Regulation;

- (c) if the notification relates to the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013, confirmation of compliance with the requirements of Article 4 of this Regulation;
- (d) if the notification relates to the derogation provided for in Article 419(2)(b) of Regulation (EU) No 575/2013, confirmation of compliance with the requirements of Articles 5 and 6 of this Regulation;
- (e) an estimate of the institution's future application of the derogation(s) in terms of the derogation to be applied, expressed as a percentage, and its variation over time together with a comparison between the institution's liquidity position if it applies the derogation(s) provided for in Article 419(2) of Regulation (EU) No 575/2013 and its liquidity position if it does not apply the derogation(s) provided for in that Article.

*Article 3*  
*Assessment of justified needs*

An institution shall be deemed to have justified needs for liquid assets for the purposes of Article 419(3) of Regulation (EU) No 575/2013 only where the following conditions are met:

- (a) it has reduced, by sound liquidity management, the need for liquid assets in the full range of business conducted by the institution;
- (a) its holdings of liquid assets are consistent with the availability of those assets in the relevant currency.

*Article 4*  
*Application of the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013*

1. An institution shall take all reasonable steps to fulfil the liquidity coverage requirement set out in Article 412 of Regulation (EU) No 575/2013 before applying the derogation provided for in Article 419(2)(a) of that Regulation.
2. An institution shall ensure that it is at all times able to operationally identify the liquid assets used to meet foreign currency liquidity coverage requirements and the liquid assets held as a result of the application of the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013.
3. An institution shall ensure that its foreign exchange risk management framework meets the following conditions:
  - (a) currency mismatches resulting from the use of the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013 are adequately measured, monitored, controlled and justified;
  - (b) liquid assets inconsistent with the distribution by currency of liquidity outflows after the deduction of inflows can be liquidated in the currency of the Member State of the relevant competent authority whenever necessary;



- (c) historical evidence relating to stress periods supports the conclusion that the institution is able to promptly liquidate the assets referred to in point (b).
4. An institution which uses liquid assets in a currency other than the currency of the Member State of the relevant competent authority to cover liquidity needs in the latter currency shall apply a haircut of 8% to the value of those assets in addition to any haircut applied in accordance with Article 418 of Regulation (EU) No 575/2013.

Where the liquid assets are denominated in a currency that is not actively traded in global foreign exchange markets, the additional haircut shall be the higher of 8% and the largest monthly exchange rate movement between both currencies in the 10 years prior to the relevant reporting reference date.

Where the currency of the Member State of the relevant competent authority is formally pegged to another currency under a mechanism in which the central banks of both currencies are bound to support the currency peg, the institution may apply a haircut equal to the width of the exchange rate band.

#### *Article 5*

#### *Application of the derogation provided for in Article 419(2)(b) of Regulation (EU) No 575/2013*

1. An institution shall take all reasonable steps to fulfil the liquidity coverage requirement set out in Article 412 of Regulation (EU) No 575/2013 before applying the derogation provided for in Article 419(2)(b) of that Regulation.
2. An institution shall obtain from the central bank in respect of the currency with constraints on the availability of liquid assets a credit line which complies with the following conditions:
  - (a) the credit line specifies that the institution has a legally binding entitlement to access the credit facilities and that entitlement is set out in a written agreement;
  - (b) following the decision to provide a credit line, access to the credit facilities is not subject to a credit decision by the central bank;
  - (c) the credit facilities can be drawn on by the institution without delay and no later than one day after giving notice to the central bank;
  - (d) the credit line is at all times available for a period exceeding the 30 day period of the liquidity coverage requirement specified in Article 412(1) of Regulation (EU) No 575/2013.
3. An institution shall fully post collateral at the central bank, which, after being subject to any haircut applied by the central bank, shall at all times be equal to or greater than the maximum amount that may be drawn on the credit line.

*Article 6*  
*Fee payable for the granting of a credit line*

1. An institution shall pay a fee established by the central bank. The fee shall be made up of two components for the credit line referred to in Article 5(2) of this Regulation and shall ensure that there is no economic advantage or disadvantage arising from the application of the derogation provided for in Article 419(2)(b) of Regulation (EU) No 575/2013, when compared to institutions which do not apply the derogation.
2. The fee to be paid by an institution for the credit line shall be the sum of the following components:
  - (a) an amount which is based on the amount of the credit line drawn down;
  - (b) an amount which approximates the difference between the following:
    - (i) the yield on the assets used to secure the credit line;
    - (ii) the yield on a representative portfolio of assets of the type provided for in points (a) to (d) of Article 416(1) of Regulation (EU) No 575/2013.

The amount referred to in point (b) of the first subparagraph may be adjusted to take into account any material differences in credit risk between the sets of assets referred to in that point.

*Article 7*  
*Limitation on the use of derogations*

1. When applying the derogations provided for in Article 419(2) of Regulation (EU) No 575/2013, institutions shall not exceed the relevant percentage set in respect of a currency by the implementing technical standards adopted pursuant to Article 419(4) of Regulation (EU) No 575/2013.
2. For the purposes of paragraph 1, when applying the derogations provided for in Article 419(2) of Regulation (EU) No 575/2013 the institutions shall calculate the percentage as the percentage that X represents of Y where:
  - (a) “X” is the sum of the value of all liquid assets to which the derogation provided for in Article 419(2)(a) of Regulation (EU) No 575/2013 applies, after application of any haircuts and the maximum amount that may be drawn on a credit line to which the derogation provided for in Article 419(2)(b) of Regulation (EU) No 575/2013 applies;
  - (b) “Y” is the amount of liquid assets required to be held by an institution to meet its liquidity coverage requirement pursuant to Article 412 of Regulation (EU) No 575/2013.

*Article 8*  
*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, 26.1.2016

*For the Commission*  
*The President*  
*Jean-Claude JUNCKER*