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30 April 2014

By email & by post

Mr He Guangbei
Chairman
The Hong Kong Association of Banks
Room 525, 5/F
Prince's Building
Central
Hong Kong

Dear Mr He,

Consultation on Returns for Reporting of Liquidity Maintenance Ratio and Liquidity Monitoring Tools

I am writing to consult the Association on the reporting requirements for (i) the Liquidity Maintenance Ratio (LMR) [1], a modified version of the existing Liquidity Ratio under the Banking Ordinance, and (ii) certain liquidity monitoring tools introduced by the Basel Committee on Banking Supervision (BCBS) in the document *Basel III: Liquidity Coverage Ratio and liquidity risk monitoring tools* in January 2013 (referred to as the "2013 BCBS LCR Document" in this letter).

As part of the implementation of the Basel III Liquidity Coverage Ratio (LCR) and the LMR in Hong Kong from 1 January 2015, the HKMA is revising the existing return relating to Liquidity Position of an Authorized Institution [MA(BS)1E] (Return of Liquidity Position) for the purpose of requiring authorized institutions (AIs) to report their liquidity positions in respect of the LCR or LMR [2] and other associated supplementary information for supervisory monitoring purposes. In addition, a new return [MA(BS)23] (Return on Liquidity Monitoring Tools) is being developed to implement the liquidity monitoring tools introduced in the 2013 BCBS LCR Document. The HKMA considers that these tools will facilitate supervision of AIs' liquidity risk management and thereby enable the HKMA to promote sound and prudent practices.

[1] This ratio was formerly referred to as the Modified Liquidity Ratio or MLR in the HKMA's liquidity consultation documents issued in 2012 and 2013.

[2] Under the two-tiered approach adopted by the HKMA, AIs designated by the Monetary Authority as category 1 institutions under the Banking (Liquidity) Rules (under development) will be subject to the LCR and other AIs not designated as such (i.e. category 2 institutions) will be subject to the LMR.

Please find enclosed the draft templates and accompanying completion instructions for the two returns:

(i) Revised Return of Liquidity Position [MA(BS)1E] for the reporting of the LMR by category 2 institutions and for the reporting of other supplementary information by all AIs. Additional sections of the Return for the reporting of the LCR by category 1 institutions will be issued for consultation in the coming weeks, once remaining technical issues involved in the calculation of the LCR have been resolved[3]; and

(ii) New Return on Liquidity Monitoring Tools [MA(BS)23] for the reporting of three liquidity monitoring tools in relation to (a) concentration of funding sources; (b) unencumbered assets available for secured borrowing; and (c) committed facilities.

The 2013 BCBS LCR Document also contains two further monitoring tools relating to maturity mismatch profile and LCR by significant currency. Reporting requirements relating to maturity mismatch profile will be issued for consultation after incorporating any consequential changes arising from the finalisation of revisions to the Basel III Net Stable Funding Ratio by the BCBS later this year. The requirements for reporting on LCR by significant currency will be issued for consultation together with those relating to the reporting of the LCR minimum standard.

Except for LCR by significant currency (which should be reported by category 1 institutions only), reporting in relation to all of the other monitoring tools in the new Return on Monitoring Tools should be made by all AIs. This is because the main objective of these tools is to facilitate supervision of individual AIs' liquidity risk profiles, and hence they should be generally applicable to all AIs.

In order to alleviate the reporting burden, the HKMA has where appropriate reduced, or refined, the scope of the supplementary information to be reported under the revised Return of Liquidity Position. Moreover, the HKMA proposes to allow AIs a longer timeline, relative to that for the revised Return of Liquidity Position, for submission of the new Return on Liquidity Monitoring Tools (as provided in paragraph 2 of the Completion Instructions).

Under the new liquidity regime, the revised Return of Liquidity Position, covering the reporting of the LCR and LMR and other supplementary information, will take effect from 1 January 2015[4], in line with the BCBS timetable for implementing the LCR. The HKMA

[3] The remaining technical issues associated with the calculation of the LCR mainly relate to (i) the calculation of haircuts on high quality liquid assets denominated in foreign currencies if a category 1 institution has a need to use such assets to cover its Hong Kong dollar liquidity needs under the second option of the Alternative Liquidity Approaches provided in the 2013 BCBS LCR Document; and (ii) the calculation of LCR by significant currency as a liquidity monitoring tool. These issues involve various complexities, such as whether (and if yes, how) the 40% ceiling on Level 2A and Level 2B assets, the 15% ceiling on Level 2A assets, and the 75% ceiling on total expected cash inflows should be applied at the currency-specific level.

[4] This means that the first submission of the revised Return by AIs will cover their LCR or LMR positions for the month ending on 31 January 2015.

also intends to implement the new Return on Liquidity Monitoring Tools at the same time, so as to further enhance the effectiveness of liquidity risk supervision and monitoring under the new regime. The HKMA may consider allowing individual AIs a grace period (say, six months) for reporting in relation to the liquidity monitoring tools, if they can provide reasonable justification that more time is needed for them to put in place necessary data and reporting systems.

For the purposes of preparing for the launch of these two Returns, the HKMA plans to conduct monthly test runs following completion of this consultation, tentatively starting from the reporting period of September 2014. The HKMA will distribute a set of Excel templates to AIs together with information regarding arrangements for the test runs nearer the time.

<u>The HKMA would strongly encourage members of the Association which are potential category 2 institutions to make a precise assessment of their current LMR position using the draft LMR reporting template</u>. This is in anticipation of the fact that, unlike the LCR, there will <u>not</u> be any phase-in period for implementation of the LMR. Should there be any identified liquidity shortfall under the LMR, the AI concerned should take prompt remedial actions in the remaining part of this year in order to be able to comply with the 25% minimum LMR requirement from January 2015.

I would be grateful if the Association could circulate this letter and the enclosures to its members, and forward any comments on the two Returns by 30 May 2014.

If there are any questions on this letter and its enclosures, please feel free to contact Ms Rita Yeung (2878-1388) or Mr Thomas Wong (2878-1219).

I am writing in similar terms to the DTC Association.

Yours sincerely,

Karen Kemp
Executive Director (Banking Policy)

Encl.

c.c. FSTB (Attn: Mr Jackie Liu)