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Office of the Comptroller of the Currency
U.S. Department of the Treasury

OCC BULLETIN 2013-35

Subject: Liquidity Coverage Ratio
Date: November 29, 2013

To: Chief Executive Officers of All National Banks and Federal Savings Associations, Federal Branches and Agencies, Department and Division Heads, All Examining Personnel, and Other Interested Parties

Transmittal - See OCC 2014-51.

Description: Notice of Proposed Rulemaking

Summary

The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation (collectively, the agencies) have issued a notice of proposed rulemaking that would implement a quantitative liquidity requirement consistent with the liquidity coverage ratio (LCR) established by the Basel Committee on Banking Supervision (BCBS). The proposal would apply to internationally active banking organizations—generally, those with $250 billion or more in total consolidated assets or $10 billion or more in on-balance-sheet foreign exposure; to systemically important nonbank financial institutions; and to any consolidated bank or savings association subsidiary of one of these companies that, at the bank level, has total consolidated assets of $10 billion or more. (The proposal refers to these institutions collectively as "covered companies.") The proposal would not apply to bank holding companies or savings and loan holding companies with substantial insurance operations; to nonbank, systemically important financial institutions with substantial insurance operations; to “bridge banks” that may be utilized in the course of bank resolutions; or to federal branches and agencies. The proposed LCR, which is designed to strengthen the liquidity risk management of banks and savings associations, would require covered companies to maintain a standard level of high-quality liquid assets (HQLA). The comment period for the proposed rule ends January 31, 2014.

Highlights

Liquidity Coverage Ratio

- The proposal would create a quantitative liquidity standard, the LCR, for covered companies. The LCR is the ratio of a company’s HQLA to its projected net cash outflows over a 30-day period. A company would have to calculate and maintain an LCR equal to or greater than 1.0 on each business day. Thus, a company would be required to hold such HQLA on each business day in an amount equal to or greater than its projected cash outflows minus its projected inflows over a 30-day period of significant stress.
- The numerator of the proposed LCR would be composed of HQLA. Assets that would qualify as HQLA would be unencumbered by liens and other restrictions on transferability and could be converted into cash easily and quickly, with little or no loss of value, during a period of liquidity stress. Central bank reserves, government and government-sponsored enterprise securities, and corporate debt securities may qualify as such assets. The proposed rule defines three categories of HQLA—level 1, level 2A, and level 2B liquid assets—and sets forth qualifying criteria and compositional limitations for an asset’s inclusion in the HQLA amount.
- The denominator of the proposed LCR would be a company’s projected net cash outflows, defined as the highest daily amount of cumulative net cash outflows within a 30-day stress period. The proposal explains items that would be included in a covered company’s projected cash outflow and inflow amounts and specifies respective outflow and inflow rates, which reflect aspects of a short-

term stress scenario, that would have to be applied to a firm's funding sources, obligations, and assets.

Supervisory Response

- The proposed rule would establish a supervisory response when a covered company's LCR falls below 1.0. A covered company would be required to notify its primary federal supervisor on any business day that its LCR is less than 1.0. If its LCR is below 1.0 for three consecutive business days, the company would be required to submit a plan to remediate the shortfall.

Transition and Timing

- The transition period for the proposed LCR would be accelerated compared with the transition set forth in the BCBS liquidity framework. The proposed rule would require covered companies to comply with the minimum LCR standard as follows: 80 percent by January 1, 2015; 90 percent by January 1, 2016; and 100 percent by January 1, 2017, and thereafter. The agencies are proposing an accelerated transition period for covered companies to build on the strong liquidity positions these companies have achieved since the recent financial crisis, thereby providing greater stability to the firms and the financial system.

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Note for Community Banks

The proposed rule would not apply to community banks.

Background

Recognizing the need for banking organizations to improve their liquidity risk management and control their liquidity risk exposures, the BCBS established quantitative standards for liquidity in the Basel III liquidity framework in 2010[1] and updated the standards in 2013.[2] The framework introduced the Basel III LCR, which established the first international quantitative liquidity standard with the primary objective of promoting the short-term resilience of internationally active banking organizations. Beginning in January 2015, under the Basel III LCR, internationally active banking organizations would be required to start holding sufficient HQLA to meet their liquidity needs during a 30-day stress scenario.

Since the financial crisis, the agencies have worked to establish a more rigorous supervisory and regulatory framework for U.S. banking organizations that would incorporate and build on the BCBS liquidity standards. The proposed rule would further enhance current supervisory efforts aimed at identifying, measuring, and managing liquidity risk by implementing a minimum quantitative liquidity requirement in the form of an LCR. The agencies are proposing a minimum LCR that would be consistent with the Basel III LCR, with modifications to reflect characteristics and risks specific to aspects of the U.S. market and the U.S. regulatory framework. The proposed rule is more stringent in several areas than the Basel III LCR, including the range of assets that would qualify as HQLA, the assumed rate of outflows for certain types of funding, and the proposed transition timeline.

Further Information

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Related Link:

- Federal Register, "Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring" (PDF)

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[1] See "Basel III: International Framework for Liquidity Risk Measurement, Standards and Monitoring" (December 2010), available at http://www.bis.org/publ/bcbs188.pdf [http://www.bis.org/publ/bcbs188.pdf].

[2] See "Basel III: The Liquidity Coverage Ratio and Liquidity Risk Monitoring Tools" (January 2013), available at http://www.bis.org/publ/bcbs238.pdf [http://www.bis.org/publ/bcbs238.pdf].