AFME and its members continue to follow the evolution of CRDIV with great interest. We believe that the industry and regulatory community share the common objective of ensuring that regulatory capital and liquidity frameworks identify and ensure sufficient resources to support risk while enabling continued support to economic recovery. With the continuation of the Level 2 process, AFME and its members welcome very much the opportunity to continue to present some of our thinking in the important areas that remain.

AFME priorities across the respective areas are summarised as follows.

**Liquidity**

- **Operational Requirements for the Holding of Liquid Assets:** The EBA report to the Commission clarifies that – in line with Basel III – assets used for hedging or other trading strategies can count towards the liquid asset buffer, so long as they are readily available to the treasury function when needed (e.g. if the liquid assets can be sold without breaching internal risk limits or can be monetised through repo).

  We continue to believe that firms should be able to include assets in the liquid assets buffer that they can indicate that their Treasury or other central function can monetise throughout the 30 day stress period without directly conflicting with a stated business or risk management strategy. The BCBS text offers a helpful example in this respect in that the sale of an asset which is being used as a hedge should not result in an open position that breaches risk limits. We note that the main aim of the CRR in this area is to ensure that ‘liquid assets are subject to appropriate internal arrangements to ensure that they are available to the treasury when needed’. We believe, therefore, that the reference to the use of liquid assets in ‘other on-going operations, including: (i) hedging or other trading strategies provides an example of when an asset might not be readily available. However, if an asset happens to serve as a hedge but is readily available, it should be eligible for inclusion in the buffer. This is consistent with Basel III.

- **Operational Deposits:** We have been encouraged that the CRDIV Level 1 text provides for the inclusion in this category of deposits that have to be maintained by the depositor in established operational relationships that are wider than those generated for clearing, custody and cash management purposes. This is set out under CRR Article 422(3)(c). We are, nevertheless, concerned that the EBA is still suggesting that banks should be able to present evidence that the client is unable to withdraw amounts legally due over a 30 day horizon without compromising its operational functioning. We continue to consider that requiring banks to provide such evidence might lead to significant variances of interpretation across banks and prove difficult to obtain in practical terms as customers may not wish to disclose these types of dependencies for competitive/pricing reasons and owing to the costs of any attempt to try to obtain this information from the very large number of corporate customers banks are likely to have in this category. We consider also that the definition of wider established relationships may not reflect the operational nor economic requirements of the customer, for instance through the exclusion of balances in excess of the average 5-day rolling cumulative net-cash outflow over the preceding 90 days.
We would suggest instead that a straight-forward approach is developed under which the EBA might set-out a list of products and services that could be considered usual in the context of an established operational relationship. Conditions around the classification of operational deposits might then include criteria such as:

- the interest payable/other income does not provide an economic incentive to the customer to leave excess funds in the accounts;
- the exclusion of term deposits; and,
- the maintenance by the customer of an active contractual relationship with the institution for a minimum duration.

Such an approach would mitigate also the risk of level playing field issues arising in the identification of operational deposits.

• **Definition of Liquid Assets:** AFME and its members view the recommendations in the EBA’s report to the Commission in this area as a positive step forward and in particular we welcome the inclusion of RMBS and equities meeting the necessary criteria as assets eligible for inclusion in the liquid assets buffer; although further clarification is needed on the definition of equities for inclusion. While the EBA recommended including exchange traded equities, further clarity is still needed, hence we would recommend the inclusion of constituent equities in primary international indices.

In addition, we would continue to stress that as well as high quality RMBS, securitisations backed by other ‘real economy’ assets such as credit cards, consumer loans, SME and auto loans have also performed well, and should also be considered for inclusion in the buffer.

We have noted also the recent change to the BCBS standards which will allow supervisors to include the undrawn value of contractual committed liquidity facilities provided by a central bank as Level 2B liquid assets. AFME and its members continue to recommend the inclusion of committed liquidity facilities from central banks as high quality liquid assets to reflect the BCBS agreement that central banks may be the most reliable source of liquidity available to banks in times of stress. We would, however, suggest that pricing conditions should be determined by national central banks to avoid potential conflicts with the implementation of monetary policy.

• **Trade Finance:** We continue to work on the assumption that the treatment under the CRR remains unchanged and that a 100% inflow factor for trade finance assets maturing the next 30 days will apply. This is important to the continuing ability of banks to finance trade and its associated ‘real economy’ activity.

**Capital**

• **Look-through approach:** A look-through approach, whereby institutions have to look-through an exposure to determine the underlying exposures, has been proposed in a number of instances, and yet is very problematic from a practical perspective. Such an approach is not general practice for all institutions in different Member States and so would impose additional burdens. The approach is burdensome and costly for small firms and large, for which implementing a look through approach is almost impossible, particularly for trading book exposures where very little net exposure will exist. Given the difficulties with the look-through approach we strongly believe that alternative approaches need to be viable from a practical perspective (e.g., recognizing the difficulties obtaining information from external sources like investment funds) and from a capital perspective (e.g., not requiring full capital deduction, which
is likely to be wholly out of proportion to the regulatory objective). The look-through approach has been proposed by various authorities for determining indirect exposures to financial sector entities (for the purposes of capital deductions), for large exposures, and for determining capital requirements for bank investments in funds.

Leverage Ratio

- We highlight the fact that a number of material interpretation issues in the final January 2014 text of the new Basel leverage rules need to be resolved. AFME is working actively with its members to identify these issues in a comprehensive way. In this context, AFME, together with its global umbrella organisation GFMA, is activating the FAQs process to get these clarifications, which will be important in order to ensure that the rules are interpreted correctly without unintentional adverse impacts on the markets and to facilitate consistent implementation. Therefore, we recommend that the EC moves forward with incorporating the changes into the CRR via a delegated act only once the interpretation issues are clarified by the Basel Committee.

CVA

- The EBA are tasked under CRR to produce by end 2014:
  1. a review on the application of CVA charges to non-financial counterparties established in a third country, which are currently exempt from CVA (Art 382), on the back of which an RTS will be developed with ESMA; and,
  2. a more comprehensive report to EC on the operation of the CVA requirements in Europe, on the back of which EC is empowered, via a delegated act, to amend Title VI in the CRR (Art 456).

- **AFME continues to believe that the overall Basel III calibration of the CVA capital charge is flawed.** EU policymakers also came to the same conclusion and allowed specific exemptions for certain counterparties. While the US has not implemented similar exemptions, it has clarified that non-credit risk hedges (market risk or exposure hedges) of CVA are not meant to be included in market risk capital, and should instead be risk-weighted as banking book exposures - Basel III and CRD4 are silent in this regard. Clearly, there are unintended consequences when some jurisdictions make what they consider to be appropriate adjustments or clarifications to the standards, but others do not.

- **AFME believes the right place to make changes to the CVA framework is at the Basel level.** To avoid regulatory divergence, the BCBS should be willing to make adjustments when widespread concerns are producing different solutions. These may be at both a principle and a technical level and both can have material effects in terms of the outcomes. We therefore urge EU and international policymakers to encourage and work with the BCBS to reconsider the CVA framework as soon as possible, perhaps through the trading book review as already proposed, with a view to promoting a consistent and prudent approach that does not negatively impact financial stability or the real economy. **Until such time, no further changes to the current European framework should be made.**