ACI DEUTSCHLAND e.V.
THE FINANCIAL MARKETS ASSOCIATION

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ACI-Germany comments on CEBS Guidelines on Liquidity Cost Benefit Allocation (CP 36)

We the ALM Expert Group of the ACI-Germany appreciate the opportunity to comment the guidelines on liquidity cost benefit allocation. It is our strong belief that the proposed guidelines will support prudent liquidity management and are likely to improve the understanding of liquidity mechanisms as a whole. In general the guidelines refer to best practices within individual principles of risk alignment. Nevertheless some parts of the guidelines appear to miss practicability in order to manage liquidity under acceptable rules.

As an association of market practitioners we'd like to address those parts which are difficult to handle or are not applicable for reaching the intended goals. We would recommend to clarify or to adjust those parts in the final document..
Please refer to the appendix or to the ACI-Germany website "ACI-Germany.de" for more details on our association and our ALM Expert Group.

General remarks

1. There is a need to adjust liquidity regulations
Liquidity is certainly an aspect which was neglected by some market participants. The dimension of the recent crisis and its impact on liquidity was definitely underestimated by all parties involved. Therefore, it is necessary to improve the international regulations on liquidity by the supervisors. But before focusing on any possible aspect of liquidity which may cause shortfalls, one has to acknowledge that the crisis had many reasons, most of them are outside the regulation on liquidity. Nevertheless, the request for transparency

of calculating liquidity costs will force some market participants to incentivize liquidity providers as well as to improve the acceptance of liquidity charges by liquidity users.

2. One-size-fits-all versus principle-based regulation

As with all regulatory changes the one-size-fits-all rule should be avoided by all means. With business models substantially differing across the banking industry, the proposed 'one-size-fits-all' approach to liquidity cost benefit allocation does not address institution, market and country-specific liquidity risks and could expose individual banks to greater risk if implemented.

3. Tough time schedule reduces the quality of the necessary changes to technical systems

The given timeframe for the implementation into national regulations of the guidelines on liquidity cost benefit allocation seems rather tight. We expect that most institutions have to have a look at their loan and debt programs in order to fulfill the requirements technically. Similar IT-projects in the past have taken at least 12-24 months for implementation, not counting the budgeting and preparation time. With respect to the ongoing regulatory changes we would like to suggest an implementation schedule in line with the requirements for the "Liquidity Coverage & Net Stable Funding Ratio" until end of 2012. Even the proposal of phased implementation will overburden those banks which obviously will have a need to implement necessary changes of internal processes and / or technical system upgrades.

Special remarks:

<u>Guideline 2</u>

No. 7: Controlling and monitoring of the transformation of liquidity costs to users and the benefits to providers should be organized within the banks regular controlling process and being supervised within the agreed governance structure. To avoid misinterpretations the wording should be more specified.

No. 9: It should be made clear that liquidity planning will only be part of the overall balance sheet structure plan, as capital is the other major driving force of business development.
Additionally off-balance sheet activities should be included, as in many cases off-balance sheet activities are hidden liquidity drivers.

No. 10: We appreciate that personnel working in the internal pricing area now are being able to remain in a profit center while not being set profit targets. This will enable banks to continue to keep and hire the most qualified persons for one of the most important business functions within the refinancing departments.

No. 11: Even if it's clear that the business unit being responsible for liquidity management should have visibility over the entire organization's balance sheet it should be avoided to define that department as "Central Treasury". In many institutions Treasury may have a different function or is not directly responsible for liquidity. We suggest to change the wording into more general business titles, i.e. management function, steering function or risk control function.

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Additionally we suppose that all off-balance sheet activities should be made visible for the central liquidity management as well.

Guideline 3

The described transaction level should be limited for customer businesses. In financial market units it might be more appropriate to calculate costs on a portfolio or strategy level. The “treasury function” should be specified as “liquidity management function”.

Guideline 4

No. 15: We support the request to reward deposit gatherers but only as long as this liquidity is needed within the liquidity funding plan.

No. 16: As far as liquidity risk management is concerned, the market liquidity risk of a trading portfolio should only be reflected within the expected holding period. This period, which should be back tested, determines the funding costs of this particular strategy or portfolio. The inherent liquidity risk of a loss due to price changes should in this case not be covered by haircuts since it is already covered by the addressed capital for market or credit risk.

Guideline 5

No: 24: We understand that funding costs including the calculation of transfer pricing have to be part of the New Product Process, please specify.

No. 25: We don’t understand this part and kindly ask for further explanation. If it’s meant to calculate transfer pricing every time a new product is added we kindly request to remove the respective guideline. Liquidity transfer pricing should not be subjected to financial engineering activities.

Appendix:

Background information on the ACI Germany

The ACI Germany is an association of practitioners working in several areas of financial markets. The above comments have been made by the Expert Group “Asset Liability Management”.

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Liquidity is one of the key aspects in the day-to-day business of our members and liquidity has been a constant issue during many (including the most recent) meetings of the aforementioned working group. There is a common understanding of the basic principles of the management of liquidity risk. We believe in a principles-based approach rather than in a "one-size-fits-all" model. The recent market developments have once again shown that liquidity risk is heavily dependent on the business model, type of customers, products and markets in which an institute operates. Within our working group we have a heterogeneous background, representing all three pillars of the German banking sector with a variety of business models, which has driven our comments to the issue as well.

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