European Banking Federation

Secretary General

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Email

Mr Arnoud VOSSEN
Secretary General
CEBS

Cp36@c-ebs.org

Brussels, 11 June 2010

Subject : ***EBF Comments on the proposed CEBS's Guidelines on Liquidity Cost Benefit Allocation (CP36)***

Dear Mr Vossen,

The European Banking Federation fully supports the basic rationale underlying the Consultation Paper, i.e. that sufficient awareness needs to be created across the various business lines within each bank about the internal (direct and indirect) cost of liquidity and, in particular, that banks should, in general, be in a position to allocate cost of liquidity to each transaction/product with some allowance for pool pricing where appropriate.

We note that the outcome which the Consultation Paper wishes to achieve corresponds with a recommendation made by the Basel Committee in its 2008 document entitled "Principles for Sound Liquidity Risk Management and Supervision" (see, in particular, Principle 4).

Obviously, liquidity allocation mechanisms which banks have developed (or are in the process of developing differ as each individual bank needs to cope with a different risk appetite, business model and/or strategy. Imposing a strict methodology to be observed by each individual bank would, therefore, not be helpful. We, therefore, welcome the principles-based approach which the Paper proposes adopting as well as the emphasis which it puts on the principle of proportionality.

In general, we believe the main components of the allocation mechanism as detailed in the paper to be appropriate. We agree that CEBS issue broad guidelines rather than producing a detailed and prescriptive paper. We welcome, therefore each individual bank being required to enter into a dialogue with its supervisor on the soundness and completeness f the methodology which it has established to measure its internal liquidity costs.

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In general, we support the proposed principle that the allocation system should have an appropriate level of granularity and, more particularly, that banks should endeavour to allocate an internal price to each transaction/product. The clarification that was made at the CEBS hearing of 1 June 2010 that pool pricing may be an acceptable approach to determine the cost of liquidity in some particular instances (e.g. concerning deposits or trading book transactions) was, however, useful.

One basic critical comment that needs to made, however, concerns the somewhat ambiguous wording which the Consultation Paper uses (on page 9, paragraph 24) where it elaborates on the link between the bank's internal cost allocation mechanism and external pricing. Clearly, it cannot be denied that, in general, sound management requires banks to take into account the cost of liquidity when determining the price of a product which they charge to their clients. However, there may be sound commercial strategy considerations explaining why banks may prefer deviating from this basic principle (e.g. the comprehensive client relationship; competitive reasons), and we were pleased to take away from the CEBS hearing that the proposed guidelines do not intend to interfere which commercial choices made by the bank.

Finally, we concur with the view that supervisory practices would need to be harmonised across EU Member States over time. Undertaking a study on how the EU supervisory community will have implemented the guidelines one year after the implementation date would indeed be an appropriate way forward to pave the ground for further harmonisation.

Yours faithfully,

Guido RAVOET