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Relaxing of the liquidity coverage ratio under Basel III

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On January 6, 2013, the Basel Committee on Banking Supervision announced that it was relaxing the liquidity rules that will be applied to banks beginning in 2015. The Group of Central Bank Governors and Heads of Supervision ("**GHOS**"), the oversight body of the Basel Committee, then unanimously adopted the last changes made by the Basel Committee to the liquidity coverage ratio ("**LCR**"), which were presented in the version published in December 2010. This ratio is intended to enable banking institutions to withstand a severe crisis for a period of 30 days. The new rule will require banks to hold enough securities that can be easily be converted into cash, such as government or corporate bonds, to cover net cash outflows in case of serious funding difficulties for one month, in order to avoid a taxpayer-funded bailout.

Changes to the LCR are made at four levels:

a) revisions to the definition of high quality liquid assets ("HQLA") and net cash outflows by expanding the range of qualifying assets for these liquidity reserves to, among other things, equities and residential mortgage-backed securities ("RMBS");
b) a timetable for the gradual phase-in of the LCR standard;
c) reaffirmation of the usability of the stock of liquid assets in periods of stress, including during the transitional period; and d) approval for the Basel Committee to continue its work on the interaction between the LCR and the provision of facilities by central banks.

The full text of the LCR rules, incorporating the changes discussed here, was published on Monday, January 7, and is available on the website of the Bank for International Settlements.

The GHOS announced that the LCR would be subject to transitional provisions, which will follow those defined for the implementation of the Basel III capitalisation requirements. More specifically, the LCR will come into force, as planned, on January 1, 2015, but the minimum requirement will initially be fixed at 60%, thereafter increasing annually by 10 points to 100% on January 1, 2019. The banks are therefore being given four more years, as many of them had indicated that it was impossible to meet the original deadline of January 2015 for building these reserves while continuing their lending operations. The aim of this gradual approach is to ensure that the implementation of the LCR does not disturb the process for strengthening the banking systems or ongoing financing of economic activity, particularly in certain euro zone countries.

The Basel Committee can now turn its attention to improving the other component of the new global liquidity standard, the net stable funding ratio, still in the observation phase, which is scheduled for implementation in 2018.

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