GEDİK & ERAKSOY

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New Regulation on Liquidity Coverage Ratios

Speed read

The Banking Regulation and Supervision Agency (**BRSA**) continues to transpose the international regulatory capital standards recommended by the Basel Committee (known as the Basel III standards) into Turkish law. Recently, the BRSA has issued the Regulation on Liquidity Coverage Ratios (**Regulation**), published in the Official Gazette dated 21 March 2014 and numbered 28948. This Regulation seeks to ensure that a bank maintains an adequate level of high quality liquid assets (**HQLA**) on a consolidated and non-consolidated basis to meet the net cash flows. The Regulation entered into effect immediately with the provisions thereof becoming applicable as of 1 January 2014 (with the exception of certain provisions relating to minimum coverage ratio levels and the consequences of failing to maintain compliance, which will enter into effect on 1 January 2015).

The most essential change introduced by the Regulation is that the ratio of the HQLA stock to the net cash outflows cannot be lower than 100% in respect of total consolidated and non-consolidated liquidity and 80% in respect of total consolidated and non-consolidated foreign exchange liquidity. The Regulation further provides details as to the calculation of HQLA stock and the net cash outflows and inflows. The maximum number of noncompliance to these calculations and ratios banks are allowed to make in a given calendar year is also regulated under this Regulation and summarized below.

Highlights from the Regulation

Calculation of the Liquidity Coverage Ratios

Liquidity levels of banks are estimated by calculation of liquidity coverage ratio over the total consolidated and unconsolidated Turkish Lira and foreign exchange, and consolidated and unconsolidated foreign exchange. In line with the Basel III standards, liquidity coverage ratio has two components under the Regulation: (i) high quality liquid assets (**HQLA**), and, (ii) the net cash outflows. Liquidity coverage ratio is simply the ratio of HQLAs to the net cash outflows of a bank.

HQLAs

The Regulation provides guidance as to the characteristics what assets would constitute an HQLA for the purposes of calculation of the liquidity coverage ratio of a bank. Accordingly, an asset must bear the following properties to be classified as a HQLA: (i) must be easily and accurately valuated, (ii) must have an active and sizable market, (iii) must be reliable resource even during stressed periods, (iv) must be unencumbered (except for assets which are deposited with or pledged to the Central Bank of Turkish Republic or a public sector entity but have not been used to generate liquidity), (v) must be in Turkish Lira or in currencies announced by the Central Bank of Turkish Republic. HQLAs consist of first quality liquid assets, level 2A liquid assets and level 2B liquid assets and the Regulation further lists the type of assets which will be classified as a first or second quality asset.

Net Cash Outflows and Inflows

Similar to the provisions regarding HQLAs, properties of the net cash outflows and inflows are also indicated under the Regulation together with type of liabilities which will be taken into consideration in calculation of the net cash outflows and inflows.

Net cash outflows are defined as the total cash flows minus total cash inflows. Cash outflows are calculated by multiplying the outstanding balances of transactions and liabilities and off-balance sheet liabilities (as valuated by Turkish Accounting Standards) by the rates listed for such liability in the annexes of the Regulation. Similarly, cash inflows are calculated by multiplying the outstanding balances of transactions and assets and off-balance sheet assets (as valuated by Turkish Accounting Standards) by the rates listed for such assets in the annexes of the Regulation. The total cash inflows over 75% of the total cash outflows are not taken into consideration in calculation of the liquidity coverage ratio. Cash outflows are classified under the Regulation as: (i) unsecured liabilities, (ii) secured liabilities, (iii) liabilities arising from structured financial facilities, and (iv) off-balance sheet liabilities.

Liquidity Coverage Ratio Threshold

As indicated in the Speed Read section, ratio of the HQLA to the net cash outflows, calculated as described above, cannot be lower than 100% in respect of total consolidated and non-consolidated liquidity, and 80% in respect of total consolidated and non-consolidated foreign exchange liquidity.

Reporting Obligations

Banks are required to report their unconsolidated total and foreign currency liquidity coverage and their consolidated total and foreign currency liquidity coverage to the BRSA for the periods to be determined by the BRSA.

Noncompliance

Unconsolidated total and foreign currency liquidity coverage ratios cannot be noncompliant more than six times within a calendar year. This includes noncompliance which have already been remedied. With respect to consolidated total and foreign currency liquidity coverage, these cannot be noncompliant consecutively within a calendar year and such ratios cannot be noncompliant for more than two times within a calendar year, including the noncompliance that have already been remedied.

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