Letter

Title	Changes to the Guideline B-6 – Liquidity Principles
Category	Prudential Limits and Restrictions
Date	December 5, 2019
Sector	Banks Trust and Loan Companies

To: Banks, Bank Holding Companies, Federally Regulated Trust and Loan Companies

OSFI is releasing the final version of its *Guideline B-6 – Liquidity Principles* for implementation on January 1, 2020. Guideline B-6 sets out OSFI's expectations around the management of liquidity risk for banks, bank holding companies and federally regulated trust and loan companies. Together with the Liquidity Adequacy Requirements Guideline, which outlines a set of quantitative liquidity standards and metrics, it forms the framework under which OSFI assesses the liquidity adequacy of the institutions it supervises.

The changes incorporated to the guideline aim to ensure that it remains current and relevant as well as appropriate for the scale and complexity of institutions. In addition, as a result of OSFI's supervisory assessments, the updated guidance includes additional clarity on OSFI's expectations regarding institutions' liquidity risk management practices.

The appendix provides a summary of comments received from the public consultation and outlines OSFI's responses. We thank those who participated in the consultation process.

Questions concerning the guideline can be sent to Robert Bélanger, Senior Analyst, Capital Division, by email at robert.belanger@osfi-bsif.gc.ca.

Sincerely,

Ben Gully

Assistant Superintendent, Regulation Sector

Appendix: Summary of Public Consultation Comments Received and OSFI Responses

Comment/Question	OSFI Response
Principle 3 – Senior management should develop a strategy, policies and practices to manage liquidity risk in accordance with the risk tolerance and to ensure that the institution maintains sufficient liquidity. Senior management should continuously review information on the institution's liquidity developments and report, as appropriate, to the board of directors.	
Concerns were raised with the draft language where some stakeholders believed that OSFI was prescribing roles and responsibilities and / or a specific business model and reporting structure (e.g. parallel reporting requirements) for liquidity risk management and oversight.	OSFI's focus is on the independence of the oversight function, taking into account the size, nature, and complexity of an institution. More specifically, OSFI wants to ensure that, irrespective of the structure, an adequate separation of responsibilities in the risk management process is in place. OSFI has adjusted the final guidance to better reflect the acceptable range of practices regarding liquidity risk management structures.
Principle 5 – An institution should have a sound process for identifying, measuring, monitoring and controlling liquidity risk. This process should include a robust framework for comprehensively projecting cash flows arising from assets, liabilities and off-balance sheet items over an appropriate set of time horizons.	
Institutions are expected to have the capacity to measure their liquidity where they conduct business, both at branch and subsidiary levels. The language in the public consultation applied to all currencies which may be overly burdensome and not in line with the OSFI's risk-based, proportionate supervisory approach.	The final guidance applies to **material** currencies at the subsidiary / branch level in jurisdictions where deemed material by individual institutions.
Principle 6 – An institution should conduct stress tests on a regular basis for a variety of short-term and protracted institution-specific and market-wide stress scenarios (individually and in combination) to identify sources of potential liquidity strain and to ensure that current exposures remain in accordance with its established liquidity risk tolerance. An institution should use stress test outcomes to adjust its liquidity risk management strategies, policies, and positions and to develop effective contingency plans.	

Comment/Question	OSFI Response
Regarding the design of stress scenarios, the language in the public consultation referred to stressors being incorporated based on “unforeseen events”, a concept that may be difficult to quantify.	The final guidance removes the reference to “unforeseen events” and instead includes references to stressors based on “severe but plausible events”. This is more in line with the concept of plausibility that is intended in the liquidity rules.
Principle 8 (Other measures) – An institution should actively manage its collateral positions, differentiating between encumbered and unencumbered assets. An institution should monitor the legal entity and physical location where collateral is held and how it may be mobilised in a timely manner.	
Suggestions were provided to remove references to the LCR, NCCF and NSFR liquidity metrics so that the guideline focussed only on “principles” and not on quantitative measures.	OSFI remains principles based. The current guideline includes references to the new liquidity standards (that were introduced since the last update to Guideline B-6 in 2012) and related supervisory metrics. The revisions aim to continue to emphasize that Guideline B-6 and the Liquidity Adequacy Requirements (LAR) Guideline should be read in conjunction. In the event the LAR Guideline is updated, Guideline B-6 will be updated as required.
Principle 9 – An institution should have a formal contingency funding plan (CFP) that clearly sets out the strategies for addressing liquidity shortfalls in emergency situations. A CFP should outline policies to manage a range of stress environments, establish clear lines of responsibility, include clear invocation and escalation procedures and be regularly tested and updated to ensure that it is operationally robust.	
Respondents recommended replacing the early warning indicators (EWIs) listed with more broad categories. The intent and implementation of a EWI related to social medial was unclear for some stakeholders.	Examples of EWIs are included in the current guideline (as a footnote). Including EWIs is not a new concept, these are listed as examples and not intended to be an exhaustive list. OSFI understands that EWIs related to “social media activities” may involve judgement but that does not preclude institutions from developing a process to track and monitor their social media footprint.
The added prescriptiveness for options and actions for dealing with stress events is overly specific and seems burdensome without obvious benefit.	OSFI adjusted the language to provide a more flexible menu of options and approaches in the CFP for dealing with stress events.