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WITH SORAINEN AND RICHARD KEMMISH CONSULTING LIMITED

REPORT OF INTRODUCTION OF PAN-BALTIC COVERED BOND LEGAL AND REGULATORY FRAMEWORK

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1. INTRODUCTION

Creating pan-Baltic covered bonds market

The Ministries of Finance in Lithuania, Latvia and Estonia signed in November 2017 the Memorandum of Understanding with the intent to create a pan-Baltic covered bond framework. Accordingly, all three countries started working on developing a regional legal and regulatory framework for covered bonds. There are two main elements to this:

- ensuring to the greatest extent possible that the laws are similar in all three jurisdictions in all material ways. This includes the degree of credit protection that the structure provides for investors, identical asset eligibility rules and aligned administration and supervisory practices;
- ensuring that all three covered bond laws are able to easily use assets in all three countries. To the extent that asset transfer into a cover pool requires enabling rules to be passed, these rules should apply to all three covered bond frameworks.

In this spirit, it should be clear that each Baltic State will have its own covered bond law and secondary regulations, and so the pan-Baltic covered bonds issuance will be achieved on the basis of the overall framework. However, the law in each Baltic State should provide that an issue carried out in another country can use assets located in another Baltic State by applying any of the models – on balance sheet (OBS) or off balance sheet (SPV) and any local regulation may not restrict it. Moreover, the proper implementation of the pan-Baltic covered bond framework will ensure the possibility to pool the cover asset when the respective asset is recorded at a branch of a credit institution registered in another Member State or the European Economic Area country too.

A successful pan-Baltic covered bond framework should be one which both respects national specificities and achieves a high degree of harmonisation for all stakeholders. Thus, a close co-operation between all three Ministries of Finance is vital to ensure that the proposed legal and regulatory framework introduces functioning pan-Baltic covered bonds. Taking into account the aforementioned, the first draft Concept Paper (**Concept Paper**) for the introduction of the pan-Baltic covered bond legal and regulatory framework was prepared.

After a few rounds of the roundtable discussions and a close examination of the main obstacles which might limit the effective issuance of pan-Baltic covered bonds, all three Ministries of Finance have agreed on the need for a unified approach on a few specific topics to be addressed in the national laws.

The list of issues to be harmonised and the proposed wording of relevant issues/requirements are reflected in this Report (see Section 2). The list of issues which should be addressed on a pan-Baltic level was compiled taking into account the following:

- the legal framework should allow issuers to combine assets from all three jurisdictions in one cover pool and to issue covered bonds secured on this pool in a cost-effective way, but also allow for the bonds to be issued domestically, with assets from one country, if that is the wish of the issuer;
- investors should enjoy substantially the same level of protection in all three states to the extent which could be achieved by the covered bond framework in such a way that they should treat all three states as being the same risk category from the perspective of internal country credit limits.

However, all the recommendations proposed herein are subject to the final wording of the proposed Directive on the Issue of Covered Bonds and Covered Bond Public Supervision.

The purpose of this Report

The purpose of this report is to provide a summary of the work undertaken for the introduction of the pan-Baltic covered bond legal and regulatory framework. Subsequently, this paper introduces the proposals for legislation agreed among all three Ministries of Finance which should be implemented during the legislation process in Lithuania, Latvia and Estonia in order to introduce covered bonds on a pan-Baltic level.

Reasons for creating a Pan-Baltic covered bond market

Size

The residential mortgage markets in the Baltic States are, as shown in the below table, significantly smaller than the mortgage markets in the smallest countries which currently have a meaningful covered bond market. If combined the pan-Baltic mortgage market would be of a roughly comparable size to those in Hungary and Slovakia (which have, respectively €2.2bn and €4.2bn of covered bonds currently outstanding).

	Residential mortgages outstanding
Estonia	€ 6.3bn
Latvia	€ 4.5bn
Lithuania	€ 6.1bn
Combined	**€16.9 bn**
For comparison..	
Hungary	€ 14.8bn
Slovakia	€ 19.7bn

Source: *European Mortgage Federation*

A lack of critical mass is clearly a problem to most capital markets instruments in the region, in particular to the extent that up-front costs have to be amortised over less proceeds. The problem is particularly acute in the case of covered bonds for three main reasons:

(i) **Costs:** the upfront costs of establishing a covered bond programme are significantly greater than those of establishing an unsecured bond programme. Material additional costs include more expensive legal and rating processes and the cost of establishing IT and operational procedures. Whereas the cost saving of a covered bond relative to other forms of term funding is material in terms of basis points, clearly the higher upfront costs imply a higher 'break-even' volume of issuance necessary for the product to be cost-effective.

(ii) **Investors:** investors typically view covered bonds as liquid products. The liquidity is largely determined by a certain minimum volume of bonds outstanding. The importance of liquidity and volumes outstanding is enshrined in many structural features of the market. In particular covered bond indices – against which investors are measured – typically only include bonds with at least 500mn outstanding. Furthermore, the prudential treatment of the bonds under EU law and for ECB repo operations is frequently size dependent. Some of the key 'cut-off' points are as shown in the below table.

Minimum size	
€1bn	• ECB liquidity category 2 for repo purposes
€500mn	• Eligible for tier 1 of bank liquidity ratio • Traditional cut-off for interbank market making • Many investor mandates • Eligibility for main covered bond indices
€250mn	• Eligible for tier 1 of bank liquidity ratio

Transactions smaller than this by smaller mortgage lenders are possible although they typical require a higher coupon to reflect the lack of liquidity. Furthermore they can only be effectively priced after larger transactions have been launched in the jurisdiction – for example by larger mortgage lenders – to provide pricing 'benchmarks'.

(iii) **Security efficiency:** Covered bonds typically use long maturity amortising assets to secure bullet maturity bonds. As such they inevitably create asset-liability mismatches which in the ordinary course of business are not a concern for investors – who rely on the issuer for the repayment of the bullet maturity bond.

However, post an issuer default, investors look to the cover pool for repayment of their bonds on their scheduled maturity date and, therefore possible asset-liability mismatches must be considered *ex ante*. The larger the covered bond programme the more bonds of acceptable size and different maturities can be issued, therefore the greater the 'natural' matching of asset and liability pay-down profiles. Larger programmes are therefore more security and cost efficient than smaller programmes.

Corporate structure of banks operating in the region

There is no 'standard' model of a pan-Baltic bank, i.e. banking group operating in the three Baltic states. Some banks operate in only one country, some in all three. Furthermore, some are based in one country and operate in the others via branches, some via subsidiaries. The degree to which treasury operations is centralised in one country varies. Finally, many are owned by non-Baltic bank parents. Any pan-Baltic covered bond framework must accommodate all of these banking models with as close as possible to equal treatment.

The diversity of corporate structures raises two important points:

(i) Covered bond regulators have a duty of care towards covered bond holders; general bank regulators have a duty of care towards all creditors of the bank. A bank which is regulated in one country (and for example operates in the others mainly via branches) but which issued covered bonds in another country would run significant risks of a conflict of interest between these two regulators. When the covered bonds and the banking group have the same regulator, these conflicts can be more easily managed.

(ii) Whilst access to the covered bond market is a net positive to the credit worthiness of the issuer, it also carries the small additional risk of greater encumbrance of liquid assets. However the benefit of access to stable, term funding in particular in a crisis scenario is much larger. If the costs and benefits of a covered bond programme were to fall in different jurisdictions (a bank based in country A is more stable due to the pledge of assets from country B) this would be inequitable.

Facilitating cross-border asset transfer

Most covered bond jurisdictions explicitly allow assets from other countries to be included in cover pools in their covered bond law. Most frequently this is restricted to EEA member states. Although allowed by law, only few jurisdictions have developed accompanying secondary regulations for assets other than those in their own country – for example specifying valuation methodologies for loans in other countries.

The vast majority of covered bond programmes do not use this functionality and restrict themselves, either by covenant or in practice to assets from one country. Of the covered bond programmes that do fund assets in more than one country a very high proportion fund ship, public sector or commercial mortgages in more than one state.

According to rating agency Fitch only 2 of the 125 covered bond programmes that they rate are backed by residential mortgages in more than 1 country. These are programmes from Danske Bank which combine Nordic region assets and from AXA which include a small proportion (10%) of French mortgages in a mainly Belgian cover pool. This was done by buying secured promissory notes from their French sister company. This is allowed under Belgian law for up to 10% of their portfolio. It is noteworthy that the two programmes which combine residential mortgages in different states do so between states that are widely considered to have highly correlated economies and thus credit risks.

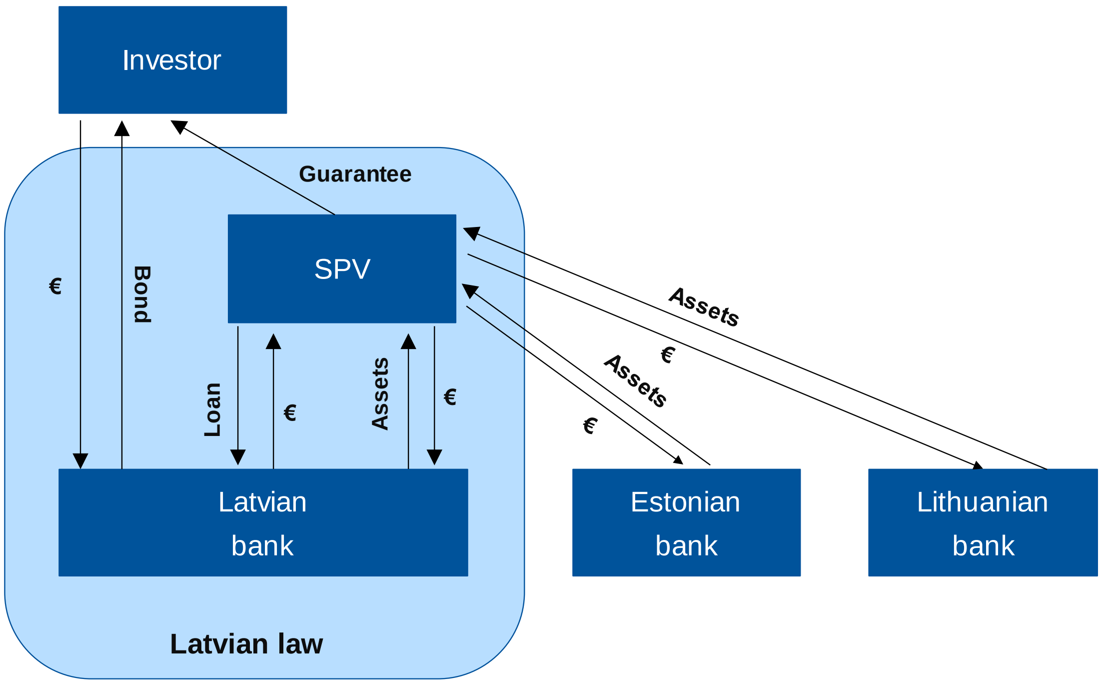
The European Commission in autumn 2015 undertook an open market consultation on the covered bond market. One of the topics that they questioned was the lack of cross-border cover pools and the impediments that existed to their formation. Market feedback, in particular from investors, was that there was opposition to the unrestricted combination of assets in cover pools from more than one jurisdiction unless those jurisdictions were considered to be of very similar credit quality.

Other models are used in the covered bond market to combine assets from more than one bank and could conceivably be amended to allow cross border pooling of assets. The most numerically prevalent model is that used in Spain where several banks issue bonds with the same terms on the same day. These bonds are then purchased by an entity which issues a bond to end investors secured on all of the individual bonds. We have rejected this model for the current project primarily as it would have required far higher upfront costs (an issuer present in all three countries would need to issue four bonds, one from each country and one from the SPV that combines them).

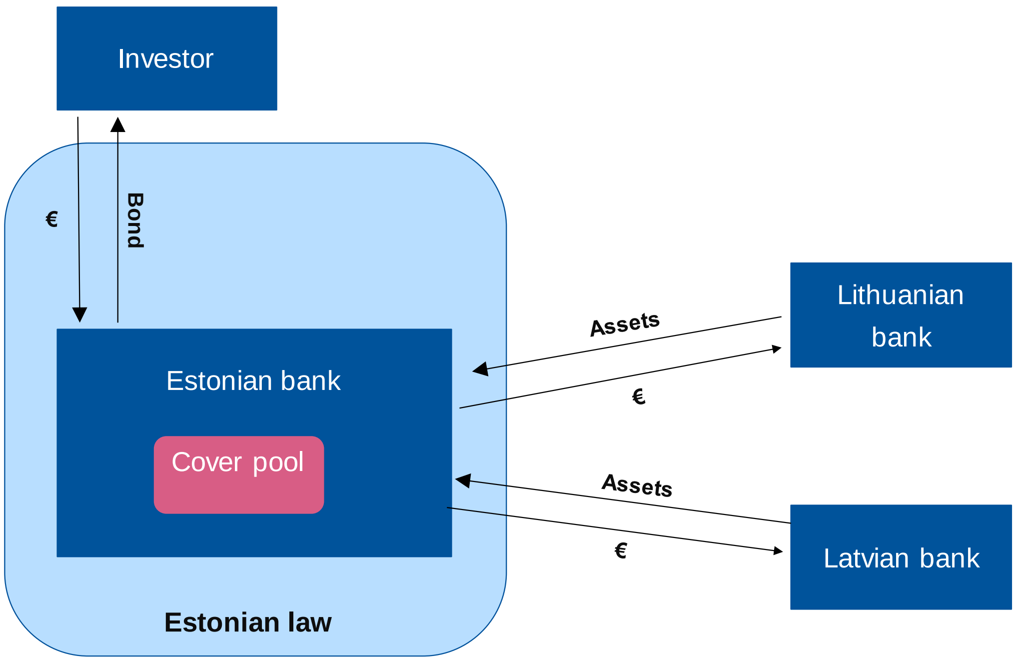
The above considerations further confirm the necessity for the three Baltic States to harmonize the covered bond regulation in the material aspects.

Pan-Baltic issuance of covered bonds

We propose the following pan-Baltic covered bonds issuance structure (assuming an issuer in Latvia or Lithuania):



And the following structure (assuming an issuer in Estonia):



Some of the implications of these structures are:

i) Each state will have its own covered bond law and secondary regulations. In each country the law should allow assets to be included in the cover pool from all three states and assets to be transferred into the cover pool in other countries.

ii) Certain laws and regulations should be identical to the greatest possible extent.

Status of legislation

At the moment of issue of this Report, the following is the status of covered bond legislation in the three states:

- Estonia – the Estonian Ministry of Finance published a draft Law on Covered Bonds for initial public consultation in March 2018, which was submitted to the Parliament in November 2018. The law was adopted by the Parliament in February 2019. The law is based on work undertaken before the launch of the pan-Baltic framework initiative. The pan-Baltic covered bond aspects will be implemented by a separate amendment to the present Law on Covered Bonds.
- Latvia – the Concept Paper was finalised in February 2019 and published on Ministry of Finance website. The initial draft law will be presented to stakeholders by the end of summer 2019. Afterwards the consultation with the stakeholders will begin. The pan-Baltic covered bond aspects will be implemented by the present draft Law.
- Lithuania – the draft Law on Securitisation and Covered Bonds has been drafted and presented for public consultation on the 19th of July, 2018. Currently the draft law is being adjusted according to the remarks received from the market. The pan-Baltic covered bond aspects will be implemented by the present draft Law on Securitisation and Covered Bonds.

2. SPECIFIC TOPICS TO BE ADDRESSED IN THE NATIONAL LAWS OF ESTONIA, LATVIA AND LITHUANIA

A: CROSS-BORDER TRANSFER OF ASSETS

Cross border asset transfer aspects			
No	**Issue**	**Required rules in Estonia/Lithuania/Latvia***	**Primary law**
Asset transfer recognition			
1.	**The right to transfer asset to SPV/bank**	Regulation should enable a bank to transfer assets to a non-licenced SPV/bank established in a member state of the EEA other than the home state of the issuer, given that the transferred asset can be used as cover asset according to the covered bond law applicable to the issuer and receiving entity. Ring-fencing principle should be recognised by all countries, particularly the assets' country of origin. The bank transferor will legally separate or 'ring-fence' the assets to be included into cover pool from other parts of the bank according to the issuer's law.	Yes
2.	**Third parties' consent**	An assignment of claims to a SPV/bank is valid disregarding whether the initial transaction limits or prohibits such transfer.	Yes
3.	**Notification about assignment of claims**	The borrowers and pledgors (if it is not the same person) may be notified about the assignment of claims to the SPV/bank before assignment or afterwards, but in any case not later than before issuer's insolvency. The notification may be performed via collective public notification (public notification in the national newspapers or mass media websites and on the website of the originator).	
4.	**"True sale" principle**	"True sale" principle should be applicable and ensured in relation to assets to be transferred to SPV/bank of another EEA country too[1].	Yes
5.	**Banking secrecy**	Explicit exemption from banking secrecy rules for a transaction itself – transfer of assets to SPV/bank. A bank/SPV shall provide the information which is considered a secret of a bank to cover pool monitor, auditors, special administrator, servicer and other parties, which should receive it with the aim to ensure proper administration of the cover pool. However, SPV/bank which owns the cover pool has an obligation to follow transferor's national banking secrecy regulation, i.e. regime continues to be applicable in respect of information disclosure to any third party regardless of the fact that the Cover Pool is owned by the SPV/bank.	Yes

* Currently in Latvia there is ongoing discussion which model, SPV or On-Balance Sheet model, to choose. At this stage the Concept Paper for Latvia proposes SPV model; however, approval from stakeholders (especially, Latvian banks) is still pending.

[1] For legal purposes, the term 'true sale' is used to describe a process of assets transfer by a seller to the SPV that removes and isolates the assets from the seller so that the seller and its creditors will be unable to recover the asset or challenge the validity of the transfer in the case of insolvency proceedings (in legal presumption, bankruptcy remote). The 'true sale' element means that the assets are transferred by the seller to the SPV and, as a result of which, the SPV becomes entitled to the cash flows that are generated by the assets (including those resulting from a subsequent sale of the assets). The legal arrangements should ensure that, in the event of insolvency of the seller, the cash flows remain the property of the SPV and, therefore, that the seller's creditors cannot challenge the validity of the transfer. This is typically achieved through an effective legal transfer of the assets or a perfected security interest created over such assets.

6.	**Consumer rights, mortgage borrowers' rights**	The consumers and mortgage borrowers be entitled to the same level of protection regardless the fact that the claims were pooled and transferred to SPV/bank in other jurisdiction. Respective transferor's national consumer protection regulation, mortgage credit regulation continues to be applicable regardless of the fact that the Cover Pool is owned by the SPV/bank in other jurisdiction.	Yes
7.	**Set-off**	The borrowers' set-off rights and right to raise counterclaims against the cover pool/SPV should be limited. The borrower may set up all such defences which the borrower had against the original creditor at the time of assignment of the claim. The borrowers may not set-off the claims they have against the original creditor if the borrower's claim falls due later than the assignment of the Cover Pool to the SPV/bank and the borrower has been notified about Cover Pool transfer to the SPV/bank. Alternatively, an over-collateralisation model which will adequately account for set-off risk (e.g. through stress testing) could be implemented as well.	Yes
Authorisation			
8.	**Authorisation requirements**	No licencing requirements (no banking, no consumer credit provider, no payment institution or any other licence is required) for SPV. Bank secrecy, consumer rights regulation continues to apply regardless of the fact that cover pool is owned by the SPV. Note: this is based on the fact that the SPV will sub-contract the servicing of the assets to an entity that has all necessary licenses, authorisations and approvals in place. This will presumably be a condition of the transfer.	Yes
Other conflicts of law aspects			
9.	**The third-party effects of an assignment of claims**	The third-party effects[2] of an assignment of claims shall be governed by the law of the country in which the assignor has its habitual residence at the material time. However, the assignor (the bank) and the assignee (SPV/bank) may choose the law applicable to the assigned claim as the law applicable to the third-party effects of an assignment of claims. The choice of law shall be made expressly in the assignment contract or by a separate agreement. The substantive and formal validity of the act whereby the choice of law was made shall be governed by the chosen law. However, the present recommendation is subject to the final wording of the Proposal for a Regulation of the European Parliament and of the Council on the Law Applicable to the Third-Party Effects of Assignments of Claims.	Yes
Security			

[2] The law applicable to the third-party effects of assignment of claims pursuant to the present proposal shall govern, in particular: (a) the requirements to ensure the effectiveness of the assignment against third parties other than the debtor, such as registration or publication formalities; (b) the priority of the rights of the assignee over the rights of another assignee of the same claim; (c) the priority of the rights of the assignee over the rights of the assignor's creditors; (d) the priority of the rights of the assignee over the rights of the beneficiary of a transfer of contract in respect of the same claim; (e) the priority of the rights of the assignee over the rights of the beneficiary of a novation of contract against the debtor in respect of the equivalent claim.

10.	**Simplified security transfer registration**	The following principles should be ensured in the law: - mortgages or pledges attached to the claims follow the assigned claims by the law; - the change of creditor/mortgagee in the mortgage/pledge sheets can be made by one-off notarial (where notary is involved in filling re-registration applications) or digitally signed (where applicable) unilateral statement by the acquirer of the mortgage (e.g. SPV) or by the transferor as it is performed in corporate merger or spilt scenarios or other simplified procedure on security re-registration needs to be introduced (to avoid complex, lengthy and expensive security re-registration that might be the case if usual security re-registration procedure is used). - the records on change of the creditor/mortgagee could be made through one-off entry at any time later in the Hypothec Registry/land registers/pledge registers when there is a need for the acquirer of the mortgage (for example, the insolvency of the issuer).	Yes
Insolvency			
11.	**Unsecured creditors' claims**	Neither issuer's/assignors' bankruptcy administrator nor issuer's/assignors' creditors have a right to challenge the assets transfer to SPV/issuer pre or post insolvency. Neither bankruptcy administrator nor creditors other than covered bond holders or relevant creditors shall have the discretionary right to decide on further continuance of issuer's arrangements related to covered bonds and asset backed securities. Neither bankruptcy administrator nor creditors of the issuer/bank assignor shall have any right to review and challenge the agreements (including asset transfer agreements under "true-sale" principle) and issue documentation related to cover pool, covered bonds and asset backed securities (including submission of *Actio Pauliana*). Upon issuer's/bank's (which has transferred asset to cover pool) insolvency, resolution or restructuring the cover pool shall not be subject to issuer's/bank's (which has transferred asset to cover pool) creditor's arrangements of any kind.	Yes
Tax issues			
12.	**Transfer of asset to SPV/bank**	Transfer of asset (claims) should be made on a commercial basis (par book value). Loss which assignor could suffer because of the transfer of the asset (claims), when the assignor gets less than the amount of transferred asset (claims), as well as loss, which could be suffered by the assignee (SPV) when the assignee gets less than it has paid for the transferred asset (claims), is recognized as deductibles for CIT purposes [(Lithuania) and does not lead to CIT liability (Latvia and Estonia)]. In practice this should never occur as all transfers are at par value. The assignment of the claims to SPV is not subject to VAT.	

		Note: market price is assumed to be par value = current carrying value of mortgage therefore no taxable gain or loss would be recognised on transfer).	
13.	**Withholding on interest**	The issuer should not have an obligation to withhold the tax on covered bonds interest.	
14.	**Tax advantage for mortgages (natural persons)**	Tax treatment of borrowers should not change when claims are transferred to SPV.	

B) ISSUES TO BE ADDRESSED IN ALL THREE COVERED BOND LAWS TO MAKE THEM COMPATIBLE AND STANDARDISED

No	Issue	Agreed solution to be incorporated in each legislation	To be addressed in Primary law	To be addressed in Secondary law
Recognition				
1.	**Cover Pool** **Inclusion of non-EEA assets in cover pool**	If the issuer wants to title the issue as “Residential Mortgage Covered Bonds”, this pool has to be designated to residential mortgages from European Economic Area (EEA) only.	Yes	
Assets				
2.	**Treatment of arrears**	Assets in arrears cannot be added to the cover pool. Treatment of arrears in coverage calculation. Residential Mortgage Covered Bonds – for mortgages with 90 day+ arrears, value is reduced for the purposes of coverage calculation to 0.4, if the mortgage has an LTV in excess of 50%, or 0.7 otherwise. For mortgages with 180 day+ arrears, zero value is given in coverage calculations. Those principles should also be applied to commercial mortgages and other mortgages (commercial or residential mortgages outside MS or EEA).	Yes	
3.	**Designation of mixed cover pools**	Pools need to be designated as specific asset or mixed. If there is a mixed asset pool, there should be no material change in risk profile associated with the designation of asset (including jurisdiction of asset) throughout the lifetime of the covered bond. Material change is subject to secondary legislation.	Yes	
4.	**Substitute assets**	Primary assets must be at least 80% of the required amount of the cover pool. Primary assets defined as assets not included in CRR article 129 (1) a, b and c. Primary assets plus article c assets must be at least 85% of the required amount of the cover pool.	Yes	

5.	**LTV ratios**	70% residential and 60% commercial LTV for coverage calculations. Market value basis for collateral. Annual indexation of market value should be allowed, i.e. the ratio is adjusted based on annual indexation. Methodology is left to the discretion of the banks, which has to be approved by the FSA. The secondary legislation should ensure common requirements for methodology.	Yes	
Over-collateralisation				
6.	**Over-collateralisation in cover pool**	Mandatory, voluntary and operational in excess of that required by law, supervisory order or contract over-collateralisation assets are protected the same way as mandatory over-collateralisation assets. There cannot be any possibility that a claim for payment, seizure or other restraint on disposition can be made against a cover asset or cover pool for reasons not related to covered bonds in any jurisdiction. Minimum over-collateralisation requirement – at least 105 per cent of the nominal amount of the covered bonds outstanding (principle liabilities towards bondholders are considered), derivatives are not included. The FSA has a right to impose a higher level of over-collateralisation before the issuance of the programme or during the lifetime of the bonds (it is not limited to covered bond portfolio separation event). For the purpose of over-collateralisation calculations, all eligible assets can be considered.	Yes	
Disclosure				
7.	**Disclosure requirements for the issuer**	Regular publication of cover pool details – quarterly reports latest in 1 month at quarter end, yearly report in 3 months at year end. Scope of disclosure as per CRR Article 129(7) which may be modified by Directive (Article 14).	Yes	
Stress testing				
8.	**Frequency**	At least once a quarter.	Yes	
9.	**Variables to be stressed**	The stress tests shall relate to at least: 1) the interest rate risk; 2) the currency risk; 3) the credit risk; 4) the liquidity risk; 5) set-off risk; 6) commingling risks;		Yes

		7) and other risks as indicated by the supervisory authority.		
10.	**Process to arrive at stress level**	To be agreed by FSAs jointly with regard to existing stress tests for banks in each country, mutatis mutandis.		Could be covered in the agreement between FSAs
Derivatives				
11.	**Derivatives in cover pool**	For the purpose of risk mitigation only.	Yes	
12.	**Cap on exposures, eligibility criteria for counterparties**	The eligibility criteria for the counterparties should be defined in the secondary legislation. If there is a need, specific limits on the amount of derivative contracts in the cover pool and other rules for covered pool derivative contract should be defined in the secondary legislation too.	Yes	Yes
13.	**Eligibility criteria for counterparties**	The following eligibility criteria for the counterparties should be defined (at least): CQS2. Derivatives should be documented with a requirement that if the counterparty becomes ineligible (is downgraded) they must immediately collateralise their exposure and must use best efforts to find a replacement counterparty at their own expense.		Yes
Maturity extension				
14.	**Maturity extension conditions**	Maturity extensions should be primarily determined by the issue documents. Nothing in the legislation should prevent a maturity extension structure including no statutory imposition of acceleration in insolvency. If the maturity extension meets certain criteria then the principal payment can be considered to occur at the legal final maturity, not the expected maturity for the purposes of the calculation of the required liquidity buffer. The maturity extension criteria should be objective financial triggers and cannot be something over which the issuer has control. Maturity extension conditions should be aligned with final text of the Directive.	Yes	
Liquidity rules				
15.	**Flows covered by liquidity assets**	Net liquidity outflows under the covered bond programme must be covered by liquidity assets	Yes	

		over the next 180 days[3] (subject to comments above with regard to principal payments under qualifying maturity extension provisions).		
16.	**Eligible assets for the liquidity buffer**	Assets qualifying for LCR calculation purposes plus exposures to CQS1 credit institutions.	Yes	
		Cover pool monitor		
17.	**Who can be a cover pool monitor**	An auditor who meets all of the criteria necessary to be an external auditor of the issuer but who is not the issuer's current auditor. There are no licencing requirements for cover pool monitor in addition to general licencing requirements for auditors. It is appointed by the issuer. The FSA has a right at any time to request replacement of the monitor for objective reasons.	Yes	
18.	**Reporting**	Yearly report in 3 months. In case of material breach the cover pool monitor has to immediately report to the issuer's FSA and the issuer.	Yes	
		Insolvency of issuer		
19.	**Bonds acceleration in case of issuer insolvency**	Neither issuer's insolvency nor asset transferor's insolvency does accelerate the obligations related to the covered bonds.	Yes	
20.	**Status of residual claim of the covered bond holders against the insolvency estate**	The residual claim of the covered bond holders against the issuer's insolvency estate (in the case there is an event of default under the issue documents and cover pool assets are insufficient) rank *pari passu* with the claim of the issuer's ordinary unsecured creditors.	Yes	

[3] To calculate the minimum level of the liquidity buffer, the difference between the payments to be made in order to meet all the liabilities arising from the covered bonds and derivative instruments entered in the cover register, on the one hand, and the cash flow to be received from the cover pool, on the other hand, shall be calculated on a daily basis for each of the following 180 days (hereinafter referred to as the daily difference). Thereafter the sum of the accumulated daily differences shall be calculated for each of the following 180 days, and the highest negative result shall be covered by cover assets.

3. NEXT STEPS

Feedback from stakeholders

Prior to starting to amend and/or draft the national laws, feedback regarding the proposed unified approach from national supervision authorities, commercial banks and other stakeholders will be sought.

Implementation into national laws

Given that the initiative to develop the covered bonds framework in Estonia, Latvia and Lithuania originated from the Ministries of Finance, it would be expected that the legislative proposals (necessary amendments to the covered bond law and other related laws) should be prepared by the respective Ministry of Finance in each country. The amendments to the secondary legislation should be coordinated by the respective Ministry of Finance in each country too.

We consider that there should be an agreed timeline of implementation. The amendments to the laws and secondary legislation should come into force in all countries (Estonia, Latvia and Lithuania) simultaneously as close as possible.

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