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# Factbox - How ECB's Emergency Liquidity Assistance works

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FRANKFURT (Reuters) - The European Central Bank set Cyprus a Monday deadline to agree a bailout plan, threatening to cut off funding to the island's cash-strapped banks through Emergency Liquidity Assistance if a bailout programme is not agreed by then with the EU and the IMF.

An illuminated euro sign is seen in front of the headquarters of the European Central Bank (ECB) in the late evening in Frankfurt January 8, 2013. REUTERS/Kai Pfaffenbach

Below is a factbox explaining what euro zone central bank Emergency Liquidity Assistance (ELA) is and how it can be used.

Cyprus government bonds have not been accepted as collateral in the ECB's regular refinancing operations since June, which has left the country's banks short of ECB-eligible collateral.

ELA is effectively emergency loans given by euro zone national central banks to strapped commercial banks.

The loans are given at the discretion of the national central bank although they have to be approved by the ECB.

The ECB defines ELA as support given by central banks in “exceptional circumstances and on a case-by-case basis to temporarily illiquid institutions and markets”.

It adds that the national central banks may provide ELA “against adequate collateral” and only to “illiquid but solvent” credit institutions.

Any changes to the limits of ELA require a two-thirds majority in the ECB’s 23-member Governing Council. The Governing Council approves maximum ELA amounts for each individual bank.

A key justification for ELA provision is to “prevent or mitigate potential systemic effects as a result of contagion through other financial institutions or market infrastructures.”

ELA is subject to a ban on the ECB financing governments, which is set out in the central bank’s founding treaty.

ELA loans sit on the balance sheet of the national central bank and therefore that of the Eurosystem of Central Banks (the euro zone’s 17 national central banks plus the ECB), but not directly on the ECB’s own balance sheet.

It does appear in the ECB’s daily calculations of liquidity as part of the “autonomous factors” header.

Governments are ultimately responsible for any losses from ELA given by their central banks, as they underwrite them.

The exact details of ELA are not published but the average interest rate charged on it is estimated to be around 100 to 150 basis points above the ECB's overnight lending rate at the time. The overnight lending rate is currently 1.5 percent.

The collateral banks post when using ELA is typically of a lower average quality than is accepted by the ECB.

Despite the stipulation that the use of ELA should be temporary, Ireland used it to prop up its banks for months. After Ireland clinched a deal under which failed lender Anglo Irish's promissory notes were exchanged for government bonds, the ECB said Ireland ELA programme was

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