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Financial services: Council agrees a general approach on strengthened capital requirements and remuneration policies in the banking sector

The Council agreed on a general approach[1], pending the European Parliament's opinion in first reading, on a draft directive[2] aimed at:

– strengthening disclosure and capital requirements for the trading book and re-securitisation instruments in the banking sector; and

– preventing remuneration policies that generate unacceptable levels of risk.

It requested the presidency to pursue negotiations with the Parliament on the basis of its general approach, with a view to adopting the directive in first reading.

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1 The decision was taken without discussion at a meeting of the Economic and Financial Affairs Council.

2 Draft directive amending directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies.

P R E S S

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It is widely recognised that weaknesses in the regulatory framework on capital requirements for the banking sector and in the risk management of financial institutions contributed to the crisis in global financial markets.

As regards the capital requirements framework, the draft directive, in line with the approach envisaged by the Basel Committee on Banking Supervision[1], sets higher and reinforced capital requirements for certain assets that banks hold in the trading book and for re-securitisation instruments. Such investments entail higher risks on account of their complexity and their sensitivity to losses.

The draft directive also enhances disclosure requirements, in line with internationally agreed standards, in several areas such as securitisation exposures in the trading book and sponsorship of off-balance-sheet vehicles.

As concerns risk management, the draft directive introduces a requirement that the remuneration policies of financial institutions be subject to supervisory oversight. There is no such requirement under the current supervisory framework, and as a result, supervisory authorities have generally not focused on the implications of remuneration policies for the risk management of financial institutions.

With regard to the supervision of remuneration policies, the draft directive:

– imposes a binding obligation on credit institutions and investment firms to have remuneration policies and practices that are consistent with and promote sound and effective risk management;

– brings remuneration policies within the scope of supervisory review, so that supervisors may require firms to take measures to rectify any problems that they may identify;

– ensures that supervisors may also impose penalties, including fines, against firms that fail to comply with the obligation.

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1 The Basel Committee provides a forum for regular cooperation on banking supervisory matters. In recent years, it has developed into a standard-setting body for all aspects of banking supervision, now comprising 28 member countries (http://www.bis.org/bcbs/).