Financial institutions: capital requirements for the trading book and for re-securitisations; supervisory review of remuneration policies

2009/0099(COD) - 14/06/2010

The Committee on Economic and Monetary Affairs adopted the report drawn up by Arlene MCCARTHY (S&D, UK) on the proposal for a directive of the European Parliament and of the Council 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. It recommended that the European Parliament's position at first reading under the ordinary legislative procedure (formerly known as the codecision procedure) should be to amend the proposal as follows:

Remuneration policies: the report states that the Directive lays down core principles on remuneration policy. Those principles should be applied consistently by Member States in a manner and to the extent that is proportionate to the nature, scope, complexity and riskiness of the activities and the size and internal structure of the credit institution or investment firm concerned. The Directive should not preclude Member States from adopting additional measures taken in the context of financial support for specific banks.

The committee's amendments aim at the following:

- bonuses must be awarded on the basis of long term performance and not be guaranteed with no 'golden parachutes' that reward failure;
- in any event, the variable remuneration component must not exceed 50 % of the total remuneration of the individual concerned;
- firms must publicly disclose information on their remuneration policies and payments, including payments by business unit and to individual directors;
- in the case of credit institutions that are continuing to benefit from exceptional government intervention:· (i)remuneration must be strictly limited as a percentage of net revenues when it is inconsistent with the maintenance of a sound capital base and timely exit from government support, (ii) no variable remuneration must paid to the directors of that institution; (iii) the total remuneration of each director of that institution must not be in excess of EUR 500 000;
- the assessment of performance must be set in a multi-year framework over a period of at least three years in order to ensure that the assessment process is based on longer-term performance and the actual payment of performance-based components of remuneration must be spread over a period which takes account of the underlying business cycle of the firm and its business risks;
- in alignment with FSB principles, a substantial proportion of the variable remuneration component should be deferred over a sufficient period; the size of the deferred proportion and the length of the deferral period must be established in accordance with the business cycle, the nature of the business, its risks and the activities of the member of staff in question; remuneration payable under deferral arrangements must vest no faster than on a pro-rata basis; at least 40 % of the variable remuneration component must be deferred; in the case of a variable remuneration component of a particularly high amount at least 60 % of the amount must deferred and the deferral period must be no less than five years;
- furthermore, the variable remuneration, including the deferred portion, vests only if it is sustainable according to the financial situation of the credit institution as a whole, and justified according to the performance of the credit institution, the business unit and the individual concerned. In particular an individual's deferred portion will be reduced in proportion to the underperformance of the

institution, the business unit and the individual by means of malus or clawback against the deferred portion. Any malus or clawback must be reported to supervisors along with the identification of the individuals to whom it applies, taking into account the assessment of suitability for holding positions of senior management, risk-takers and control functions or being in that income bracket;
- payment of at least 50% of the deferred part of the bonus should be made in shares or share-linked instruments of the credit institution or investment firm.

Provisions to improve corporate governance, transparency and disclosure: the report aims to strengthen effective corporate governance and transparency. The amendments state that:

- credit institutions that are significant in terms of their size, internal organisation and the nature, the scope and the complexity of their activities shall establish a **remuneration committee**, which will be constituted in such a way as to enable it to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk, capital and liquidity;
- the Chair and the members of the remuneration Committee shall be members of the management body who do not perform any executive functions in the credit institution concerned. When preparing such decisions, the remuneration committee shall take into account the long-term interests of shareholders, investors and other stakeholders in the credit institution;
- firms must **publicly disclose information** on their remuneration policies and payments, including payments by business unit and to individual directors.

National and EU wide benchmarking: in order further to enhance transparency as regards the remuneration practices of credit institutions and investment firms, the competent authorities of Member States should collect information on remuneration to benchmark institutions in accordance with the categories of quantitative information that those institutions are required to disclose under the Directive. The competent authorities should provide the European Banking Authority (EBA) with such information to enable the EBA to conduct similar benchmarking at Union level. The EBA and national supervisors should promote a common international structure for disclosure of the number of individuals in pay brackets of EUR 1 million and above, including the business area involved and the main elements of salary, bonus, long-term award and pension contribution. All information collection and use must be in line with all relevant provisions of EU data protection legislation, including Directive 95/46/ECand Regulation (EC) No 45/2001.

Implementing Basel: the committee endorses Commission proposals implementing agreements at Basel, and proposes amendments in the following areas:

- it is necessary to reflect the further Basel decision to **exclude correlation trading from the new trading book requirements**. The Directive lays down limited exceptions for certain correlation trading activities, where banks may be allowed by their supervisor to calculate a comprehensive risk capital charge subject to strict minimum requirements. In such cases it might be appropriate to establish a floor to the capital requirement. Having regard to the fact that the Basel Committee on Banking Supervision is conducting an impact study on the capital charges for securitisation positions in the trading book, including those that would result from the specific treatment for correlation trading, the Commission should report to the European Parliament and the Council about any measures agreed at international level regarding the methodology and minimum levels and the Commission should be empowered to adopt delegated acts in accordance with Article 290 of the Treaty on the Functioning of the European Union for the purposes of setting such a floor;
- banks investing in re-securitisations are required under Directive 2006/48/EC to exercise due diligence also with regard to the underlying securitisations and the non-securitisation exposures ultimately underlying the former. For a better understanding of the effectiveness of those provisions for securitisations and re-securitisations, the Commission should comply with the tenth paragraph of Article 156 of Directive 2006/48/EC which provides for a Commission report on the expected

impact of Article 122a, and submit that report to the European Parliament and the Council, together with any appropriate proposal, by 31 December 2009. Pending such a review, additional requirements for 'highly complex' re-securitisation should not be covered in this Directive;

- the Commission should review the operation of Article 122a of Directive 2006/48/EC once it is implemented and assess what amendments are necessary, including whether it is adequate to ensure due diligence for securitisation, including re-securitisations.

Stronger Parliamentary Oversight: lastly, the report notes that the measures in the Directive are steps in the reform process in response to the financial crisis. In line with the conclusions of the G-20, the Financial Stability Board and the Basel Committee on Banking Supervision further reforms may be necessary, including the need to build counter-cyclical buffers, "dynamic provisioning", the rationale underlying the calculation of capital requirements in Directive 2006/48/EC and supplementary measures to risk-based requirements for credit institutions to help constrain the build-up of leverage in the banking system. In order to ensure appropriate democratic oversight of the process, the European Parliament and the Council must be involved in a timely and effective manner.

In this instance, the European Parliament or the Council have the period of three months from the date of notification to object to a delegated act. At the initiative of the European Parliament or the Council, this period can be prolonged by three months in significant areas of concern. The European Parliament and the Council may inform the other institutions of their intention not to raise objections. This early approval of delegated acts is particularly indicated when deadlines need to be met, for example to meet timetables set in the basic act for the Commission to adopt delegated acts.