Proposal for a Regulation of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms (COM (2011) 452 final).

Proposal for a Directive of the European Parliament and of the Council on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms and amending Directive 2002/87/EC (COM(2011) 453 final).

FINAL DOCUMENT APPROVED BY THE COMMITTEE
(Doc. XVIII, no. 55)

The Finance Committee of Italy's Chamber of Deputies,

having jointly examined the Proposal for a Regulation of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms (COM (2011) 452) and the Proposal for a Directive of the European Parliament and of the Council on the access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms and amending Directive 2002/87/EC (COM(2011) 453 final);

having regard to the recommendation adopted by the European Banking Authority (EBA) on 9 December to the effect that banks should form, on an exceptional and temporary basis, an additional reserve of capital before the end of June 2012;

taking into account the hearings held by the Finance Committee as part of its fact-finding investigation of the aforementioned proposals;

Whereas:

the financial crisis that began in 2007 is significantly impacting both the financial markets and the real economy: specifically, Italy faces pressure from the sovereign debt market and the prospect of an excessively low rate of growth; it has entered a new recessionary phase, and failed to recover the level of national income that it enjoyed before the onset of the crisis;

the current state of considerable instability has several causes rooted both in the real and in the financial economy, the latter of which has also been greatly influenced by banking supervision policies adopted at an international level;

specifically, past use of financial leverage and the consequent recourse to borrowing has been excessive; the use of low-quality assets was also characterised by excess, and resulted in the use of capital instruments that then proved inadequate to the task of absorbing losses; excesses also surrounded the ready availability of liquidity, which was too long regarded as being limitless and cost-free; excessive use was made of complex financial instruments which proved to be “toxic”, and were unfamiliar to and went undetected by the oversight authorities themselves; and, finally, excess also marked the manner in which supervisory policies were framed without any distinction being drawn between the diverse business models of financial intermediaries and without allowing for the differences in the size and the particular areas of operation of the latter;

over the past three years, monetary, supervisory and political authorities have been striving to counter these excesses with a series of broad-ranging regulatory measures, and have set themselves the long-term goal of creating conditions conducive to the lasting stability of intermediaries and the financial markets. The proposals under examination are intended as a step in the direction of this goal; the chief objectives are to improve the quality of bank capital, impose controls on the management of liquidity, lower the debt-equity ratio of banks, obtain more accurate measurements of the value of budget items that carry market risk, and base the relevant regulations on the principle of proportionality;

the recent regulatory reform of the financial system of the United States engendered a debate also in Europe on the need for financial regulations that are more closely attuned both to the specific business models of different banks and to the relative importance of the banks, as measured by size and the extent of their interconnectedness with other financial intermediaries;

European laws enacting the terms of the Basel III Accord provide for a general tightening of the capital adequacy requirements of banks. While higher capitalisation is undoubtedly needed to restore confidence in the solvency of banks, unless properly calibrated, the result might be to raise costs and aggravate the difficulties of obtaining credit for the industrial sector and, especially, for small and medium-sized enterprises (SMEs).

the Annual Growth Survey 2012 presented by the European Commission on 23 November 2011 (COM (2011) 815 final), urges the restoration of "normal lending to the economy", to which end it expressly recommends "that banks strengthen their capital ratios primarily by increasing their capital positions, and not by unduly restricting lending to the real economy", and calls for “prudential rules to be reviewed to ensure that they do not unduly penalise lending to SMEs";

although the proposals under examination are intended to be introduced over a lengthy transition period and will not become fully effective until 2019, the announcement that new rules were imminent caused investors and counterparties to pressurise the banks into adopting the reforms ahead of schedule and into building up their capital and liquid reserves in spite of the current parlous state of the market and the economy;

the magnitude of the additional capital buffer that the EBA is demanding of the Italian banks that participated in the recapitalisation exercise promoted by the EBA itself on 26 October 2011 has been largely determined by a deliberate choice, which is not grounded on any European legislation, to mark to market all the government securities in the possession of the banks;

several analyses carried out in the course of the Finance Committee's fact-finding work discovered that there were significant misalignments among the banks of different countries regarding the risk-weighting of assets, and that the misalignments did not appear to be ascribable either to the structural situation of the countries or to differences in product specialisation;

it is essential to make sure that the Basel III Accord is applied as faithfully as possible, and that the parties involved adopt a single rulebook that will guarantee a level playing field for all European banks, especially for those with significant international operations. Any margins of flexibility that exist at a national level must not be permitted to prejudice the uniformity of the regulatory framework, with particular regard to capital ratios and the risk weighting of assets;

with regard to the above, work must continue on regulating rating agencies, which are pursuing objectives that do not necessarily correspond to the public good and many aspects of whose operations are marred by conflicts of interest and a lack of transparency in several organisational and management processes;

so that the introduction of tighter capital requirements does not simply result in regulatory arbitrage in favour of the “shadow-banking” system (hedge and private equity funds), the legislative proposals here under consideration should be accompanied by the adoption of stricter rules also for the shadow-banking system, including oversight mechanisms and measures to enforce capital requirements;

noting that this document, along with the opinion of the Committee on European Union Policies, must be transmitted to the European Parliament, the Council and the European Commission as part of the informal political dialogue,

CALLS ON THE GOVERNMENT

to take action at the relevant decision-making meetings of the EU in furtherance of the following:

a) the adoption of rules that are coherent with the current cyclical phase of the European and Italian economy, so that the introduction of regulatory capital requirements will act as a catalyst for long-term market stability rather than as a brake preventing banks from supporting businesses and households. The manner of application and the timing of the proposals must be such as to avoid undesirable pro-cyclical effects;

b) the sponsoring and advancement of an EU-wide debate that seeks to define the clearest possible line of demarcation between traditional and investment banking, in order to make sure that the European legislation transposing the Basel III Accord includes regulatory incentives for those banking activities that serve to support the real economy. The legislation should also be framed to conform with the principle of proportionality, according to which the importance of banks is measured by their size, scope of operation and the effective support they provide to the real economy. With reference to the foregoing, consideration should be given to the possibility of allowing capital adequacy requirements to vary according to the type of bank or investment company. The specific nature, size, business model and risk propensity of the banks should be taken into account, and, in particular, banks with a significant systemic relevance need to be distinguished from others;

c) with particular reference to capital ratios, steps should be taken to ensure that the list of instruments eligible for inclusion as top-grade capital (Tier 1 common equity) is fully harmonised and that the relevant EBA list is both binding and comprehensive, so that all banks operating in the Single Market enjoy full equality of treatment;

d) again with regard to the question of regulatory capital, support should be given to proposals for amendments that would ensure that the tax credits of Italian banks arising from the deduction of loan-loss provisions from the net income for the year are not excluded from capital, but are, rather, included as risk-weighted assets;

e) with reference to the rules on liquidity, uniform criteria need to be set down for determining which assets may be included in the liquidity buffers that banks are required to maintain. Otherwise, uncertainty on this point, coupled with the permitted use of internal weighting models by the banks themselves, might bring about a situation of unfair competition in the area of liquidity management, which would undermine the entire regulatory function of the proposals;

f) the leverage ratio should be binding and uniform for all banks, and not a mere instrument of supervision imposed on them as part of the second pillar. This will therefore require an amendment of the text of the proposal so that regulators are given an essential tool to deal with what was one of the major causes of the financial crisis;

g) as regards the measures contained in the proposal for a regulation that oblige financial and credit intermediaries to disclose comprehensive information about their leverage ratio to the market, uniform rules need to be set out for the calculation of the ratio, with particular reference to the configuration of Tier 1 capital, to prevent the parties concerned from using whatever method of calculation happens to be most favourable for them, as this would prejudice the possibility of making meaningful comparisons;

h) European legislation transposing Basel III should also include regulatory measures to encourage the supply of credit to SMEs by reducing lending costs. Specifically, there is a need for measures that can effectively counter the negative impact that higher capital requirements might have on lending to SMEs if the new capital adequacy rules were to be applied indiscriminately;

i) a corrective coefficient needs to be added to the formula for calculating the value of risk-weighted assets relating to non-profit organisations (NPOs) and social cooperatives so that the mandatory capital coverage for loans to these entities may be maintained at the level required by current regulations, even after the introduction of the new rules;

l) with reference to leasing, non-bank leasing companies should be exempted from the liquidity requirements given that their activities, which do not include the collection of deposits, do not appear to present any risk in this area;

m) in cases where a loan is backed by a credit consortium providing collective guarantees, it needs to be clear that the criterion for calculating the capital requirement related to the value of the provision that the consortium is required to set aside may not result in a value greater than the capital saving that the bank has obtained thanks to the intervention of the consortium;

n) those legislative proposals that, the absence of international agreements notwithstanding, would introduce the risk weighting of government securities for regulatory capital purposes into European law need to be opposed on the grounds that they would result in the imposition of an unjustified extra capital requirement on banks that hold government bonds and, consequently, render those bonds less attractive to the market;

o) action should be taken to ensure that the agenda of the next European Council includes a reconsideration of the need for and the size of the additional capital buffers against sovereign risk required by the EBA recapitalisation exercise, as recommended also by the EBA itself on 8 December 2011;

p) in any event, European and national authorities should be encouraged to act so that the measures taken by European banks to address any capital shortfalls revealed by the EBA exercise will be spread out over time, thereby avoiding unwanted pro-cyclical effects and synchronising the measures with the economic cycle;

q) the European Union must act to ensure the simultaneous enforcement in all major countries participating in the global financial system of basically similar capital requirements and prudential rules;

r) European institutions should be encouraged to take an urgent look at the need to fine-tune the regulatory framework establishing the European supervisory authorities not only in order to secure the effective independence of the same in the specific technical areas for which they are responsible, but also in order to prevent decisions with a significant impact on the economic policies of Member States and on the lives of citizens from being immediately forced into effect by the behaviour of markets, without first being subjected to the necessary evaluation of the political bodies that Europe's citizens have democratically elected;

s) a rapid comparison needs to be made of the supervisory policies adopted in Member States in order to reduce competitive misalignments of a purely regulatory nature and avoid any delay in the application of the EBA's peer review system, scheduled to begin in 2014. By means of appropriate procedures, the peer review will effectively ensure that the policies adopted by each national regulator are transparent and comparable;

t) in particular, a provision needs to be introduced making it mandatory for the EBA to prepare an annual report on the convergence of secondary legislation on banking supervision in which any significant discrepancies are highlighted and the corrective actions under way are outlined;

u) consideration should be given to the possibility of allowing national regulators to introduce specific countercyclical "discount factors", including on a temporary basis, that are configured with reference to the particular circumstances of the country and do not generate unfair advantages or distort the competitive context;

v) with reference to banking governance, consideration should be given to the possibility of extending the exemption to the general regulation - whereby, in calculating the maximum number of executive posts that may be held by a single person, positions held within a group are counted as a single office - to those held in institutions-based protection systems; greater "diversity" should be guaranteed within the governing bodies of banks, in relation not only to gender but also to the level of professional qualification, in view of the fact that a large part of the decisions taken by banks are increasingly technical in content. Bank board members should therefore be endowed with proven technical knowledge of the various matters they deliberate, so that their decisions may be responsible, adequate and informed;

z) it is necessary to speed up the process begun by the Financial Stability Forum in 2008 and formally adopted by the G-20 in Seoul in 2010 for the review of financial regulations with a view to eliminating any automatic linkage between ratings issued by an external credit assessment agency (ECAI) and consequences in terms of regulation. Greater speed is also needed in the adoption of regulations that will impose stronger governance and transparency constraints on ECAIs and subject them to greater supervisory scrutiny in regard to market manipulation.