COMMISSION OF THE EUROPEAN COMMUNITIES

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Proposal for a

EUROPEAN PARLIAMENT AND COUNCIL DIRECTIVE

AMENDING ARTICLE 12 OF DIRECTIVE 77/780/EEC ON THE COORDINATION OF LAWS, REGULATIONS AND ADMINISTRATIVE PROVISIONS RELATING TO THE TAKING UP AND PURSUIT OF THE BUSINESS OF CREDIT INSTITUTIONS,

ARTICLES 2, 6, 7, 8 AND ANNEXES II AND III OF DIRECTIVE 89/647/EEC ON A SOLVENCY RATIO FOR CREDIT INSTITUTIONS

AND

ARTICLE 2 AND ANNEX II OF DIRECTIVE 93/6/EEC ON THE CAPITAL ADEQUACY OF INVESTMENT FIRMS AND CREDIT INSTITUTIONS

(presented by the Commission)

EXPLANATORY MEMORANDUM

I. INTRODUCTION

The purpose of this proposal for a Directive is to amend Article 12 of Directive 77/780/EEC on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions, articles 2, 6, 7, 8 and annexes II and III of the Directive 89/647/EEC on a solvency ratio for credit institutions and article 2 and annex II of Directive 93/6/EEC on the capital adequacy of investment firms and credit institutions.

At recent meetings of the Banking Advisory Committee, it was deemed expedient to introduce a number of amendments to the above Directives, either to take account of recent developments (such as the creation of the European Investment Fund) or to remedy the shortcomings of those Directives (for example, the possibility of exchanging information with non-banking authorities of third countries, the weighting of no-risk assets included under prepayments and accrued income). Further amendments reflect refinements of the supervisory treatment of over-the-counter derivative instruments as regulated by another international forum of banking supervisors.

II. EXAMINATION OF THE ARTICLES IN THE PROPOSAL FOR A DIRECTIVE

Article 1: amendment to Article 12(3) of Directive 77/780/EEC

The purpose of this amendment is to allow the Member States to conclude agreements for the exchange of information with the non-banking supervisory authorities of third countries (i.e. the authorities vested with the public task of monitoring other financial institutions and insurance companies, and the authorities responsible for the supervision of financial markets) provided that the information disclosed is subject to guarantees of professional secrecy at least equivalent to those referred to in Article 12.

Article 2: amendment to Article 2(2) of Directive 89/647/EEC

The aim here is to treat churches and religious communities as regional government and local authority bodies in so far as national legislation confers on them the right to raise taxes.

Article 3: amendment to Article 6(1)(a)(8) and (c)(2) of Directive 89/647/EEC

The purpose of this article is to allow a zero weighting to be applied to asset items included under prepayments and accrued income where those assets are of a purely accounting nature, carry no risk and do not refer to counterparty. Article 6(1)(c)(2) as currently worded does not allow this more favourable weighting of these no-risk assets.

Article 4: amendment to Article 6(2) of Directive 89/647/EEC

The European Investment Fund provides for a 30% holding in its capital for financial institutions. Of this 30%, 80% need not be paid up immediately, and this percentage remains as a contingent liability for the members of the Fund.

In the light of the Fund's objectives, it is not appropriate to penalise private institutions' holdings in the Fund. Accordingly, it should be possible to apply a 20% rather than a 100% weighting to the portion of unpaid capital subscribed to the Fund.

Article 5: amendment to Article 6(3) of Directive 89/647/EEC

The purpose of this article is to determine the scope of application of the capital requirements for the credit risks inherent in off-balance-sheet contracts. Referring to the amended list in annex III the application is extended to all credit risk bearing off-balance-sheet contracts traded outside recognised exchanges (over-the-counter derivative instruments).

Article 6: amendment to Article 6(4) of Directive 89/647/EEC

Annex I to Directive 89/647/EEC, which deals with the classification of off-balance-sheet items, applies a 100% weighting to some of these items. In addition, Article 6(4) provides for weightings of 0% and 20% respectively where the exposure arising from off-balance-sheet transactions is fully secured by asset items recognised as collateral in paragraphs 1(a)(7) (Zone A central government or central bank securities) and (b)(11) (securities issued by the EIB or by multilateral development banks). It is therefore desirable to allow a more favourable weighting too where the exposure arising from off-balance-sheet transactions which are sureties or guarantees having the character of credit substitutes is secured by real collateral within the meaning of Article 6(1)(c)(1).

Article 7: amendment to Articles 7(1) and (2) and 8(1) of Directive 89/647/EEC

Article 7(1) provides that, under certain conditions, a zero weighting may be applied to claims on regional governments and local authorities and to claims guaranteed directly by those regional governments and local authorities. Nonetheless, Article 8(1) provides for a 20% weighting to be applied to claims secured by collateral in the form of securities issued by regional governments or local authorities. It is more appropriate to broaden the scope of Article 7(1) to cases where the guarantee is collateral in the form of securities issued by those regional governments or local authorities. This will enable the competent authorities to treat guarantees given by their own regional governments or local authorities and collateral in the form of securities issued by such governments or authorities in the same way.

Article 8: amendments to annex II to Directive 89/647/EEC

The purpose of this article is to introduce in annex II the technical provisions necessary for a refined and more stringent supervisory treatment of over-the-counter derivative instruments. The amendments to annex II

- oblige institutions with trading activities beyond a given threshold to use the more accurate "mark to market" approach when calculating the capital requirements for the current credit risks;
- expand the matrix of percentages to be applied when calculating the capital requirements for the potential future credit risks and
- afford to competent authorities the possibility of recognising risk reducing effects of contractual netting agreements on the potential future credit risks inherent in over-the-counter derivative instruments included in the contractual netting.

Article 9: amendments to annex III to Directive 89/647/EEC

The purpose of this article is to enlarge the list of covered derivative instruments in annex III. In particular, a third category of high risk derivative instruments is added under Nr. 3 and a provision indicating the non-exhaustive character of the list is added under Nr. 3 d).

Article 10 and 11: amendments to article 2 and annex II of Directive 93/6/EEC

The purpose of these articles is to adjust the references made in Directive 93/6/EEC to amended provisions of Directive 89/647/EEC in order to guarantee a consistent supervisory treatment of the over-the-counter derivative instruments of credit institutions and investment firms falling under Directive 93/6/EEC.

Articles 12, 13 and 14

These articles call on the Member States to take the measures necessary to comply with the Directive, to make explicit reference to it in the provisions adopted and to notify those provisions to the Commission.

PROPOSAL FOR A EUROPEAN PARLIAMENT AND COUNCIL DIRECTIVE AMENDING ARTICLE 12 OF DIRECTIVE 77/780/EEC ON THE COORDINATION OF LAWS, REGULATIONS AND ADMINISTRATIVE PROVISIONS RELATING TO THE TAKING UP AND PURSUIT OF THE BUSINESS OF CREDIT INSTITUTIONS,

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AND

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The European Parliament and the Council of the European Union,

Having regard to the Treaty establishing the European Community, and in particular the first and third sentences of Article 57(2) thereof,

Having regard to the proposal from the Commission,[1]

Having regard to the opinion of the Economic and Social Committee,[2]

Acting in accordance with the procedure referred to in Article 189B of the Treaty,[3]

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1 OJ No C ..., ...

2 OJ No C ..., ...

3 Opinion of the European Parliament of ... (OJ No C...., ...), common position of the Council of .... (OJ No C...., ...) and decision of the European Parliament of ... (OJ No C ...., ...).

Whereas Article 12(1) of Council Directive 77/780/EEC[4] provides that the competent authorities are bound by the obligation of professional secrecy; whereas Article 12(2) allows the competent authorities of the Member States to exchange information in accordance with the directives applicable to credit institutions, any information thus exchanged being covered by professional secrecy; whereas Article 12(5) provides for the exchange of information within a Member State, or between Member States, between competent authorities and other types of authorities or bodies defined in the same paragraph, any information thus exchanged being subject to professional secrecy;

Whereas Article 12(3) allows Member States to conclude cooperation agreements, providing for exchanges of information, with the competent authorities of third countries only if the information disclosed is subject to guarantees of professional secrecy at least equivalent to those referred to in Article 12;

Whereas Article 12 does not allow Member States to conclude cooperation agreements, providing for exchanges of information, with the non-banking supervisory authorities of third countries; whereas, on grounds of consistency, it should be possible to conclude cooperation agreements with the non-banking supervisory authorities of third countries as defined in the first indent of Article 12(5) of Directive 77/780/EEC, provided that the information disclosed is subject to guarantees of professional secrecy at least equivalent to those referred to in Article 12;

Whereas Directive 89/647/EEC on a solvency ratio for credit institutions[5] weights assets and off-balance-sheet items according to their degree of credit risk;

Whereas churches and religious communities which, constituted in the form of a legal person under public law, raise taxes in accordance with the laws conferring such a right on them represent a credit risk similar to that of regional governments and local authorities; whereas, accordingly, it is consistent to afford the competent authorities the possibility of treating claims on churches and religious communities, including non-profit-making bodies and undertakings controlled by them, in the same way as claims on regional governments and local authorities where these churches and religious communities raise taxes;

Whereas Article 6(1)(c)(2) of Directive 89/647/EEC lays down, with regard to prepayments and accrued income, that "these assets shall be subject to the weighting corresponding to the counterparty where a credit institution is able to determine it in accordance with Directive 86/635/EEC. Otherwise, where it is unable to determine the counterparty, it shall apply a flat-rate weighting of 50%";

Whereas this treatment is inappropriate where the asset items shown under prepayments and accrued income are of a purely accounting nature, carry no risk and do not have a counterparty, and consequently are simply the expression in accounting terms of a

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4 OJ No L 322, 17.12.1977, p. 30.
Last amended by Directive 96/13/EC (OJ No L 66, 16.03.96, p. 15).

5 OJ No L 386, 30.12.1989 p. 14. Directive last amended by Directive 96/10/EC (OJ No L 85, 3.4.1996, p. 17).

liability; whereas, in view of the absence of risk, these assets should have a weighting of 0% under prepayments and accrued income;

Whereas Commission Directive 94/7/EC adapting Council Directive 89/647/EEC on a solvency ratio for credit institutions as regards the technical definition of "multilateral development banks"[6] included the European Investment Fund in that definition; whereas the Fund constitutes a new and unique structure of cooperation in Europe in order to contribute to the strengthening of the internal market, the promotion of economic recovery in Europe and the furthering of economic and social cohesion;

Whereas, under Article 6(1)(d)(7) of Directive 89/647/EEC, a weighting of 100% should be applied to the unpaid portion of capital subscribed to the European Investment Fund by credit institutions;

Whereas the capital of the European Investment Fund reserved for subscription by financial institutions is limited to 30%, of which 20% would be paid up at the outset in four annual payments of 5% each; whereas, accordingly, 80% would not be paid up, remaining a contingent liability on the members of the Fund; whereas, having regard to the European Council's stated objective when creating the Fund of encouraging commercial banks to participate, such participation should not be penalised and whereas, accordingly, it would be more appropriate to apply a 20% weighting to the unpaid portion of subscribed capital;

Whereas Annex I to Directive 89/647/EEC, which deals with the classification of off-balance-sheet items, classifies certain items as full risk and, accordingly, applies a 100% weighting; whereas Article 6(4) of that Directive lays down that "Where off-balance-sheet items carry explicit guarantees, they shall be weighted as if they had been incurred on behalf of the guarantor rather than the counterparty. Where the potential exposure arising from off-balance-sheet transactions is fully and completely secured, to the satisfaction of the competent authorities, by any of the asset items recognised as collateral in paragraph 1(a)(7) or (b)(11), weightings of 0% or 20% shall apply, depending on the collateral in question.";

Whereas account should also be taken of the case where the guarantee is secured by real collateral within the meaning of Article 6(1)(c)(1) in respect of off-balance-sheet items which are sureties or guarantees having the character of credit substitutes;

Whereas, under points 2, 4 and 7 of Article 6(1)(a) of Directive 89/647/EEC, a zero weighting is applied to assets constituting claims on Zone A central governments and central banks or explicitly guaranteed by them and to assets secured by collateral in the form of Zone A central government or central bank securities; whereas, under Article 7(1) of that Directive, the Member States may, under certain conditions, apply a zero weighting to assets constituting claims on their own regional governments and local authorities and to claims on third parties and off-balance-sheet items held on behalf of third parties and secured by those regional governments or local authorities;

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6 OJ No L 89, 6.4.1994, p. 17.

Whereas Article 8(1) of Directive 89/647/EEC lays down that the Member States may apply a weighting of 20% to asset items which are secured, to the satisfaction of the competent authorities, by collateral in the form of securities issued by Zone A regional governments or local authorities; whereas collateral in the form of securities issued by regional governments or local authorities of the Member States should be regarded as being guaranteed by those regional governments and local authorities within the meaning of Article 7(1) with a view to allowing the competent authorities to apply a zero weighting to assets and off-balance-sheet items secured by such collateral, again subject to the conditions laid down in that paragraph;

Whereas Annex II to Council Directive 89/647/EEC lays down the treatment of off-balance-sheet items commonly referred to as over-the-counter derivative instruments concerning interest and foreign exchange rates in the context of the calculation of credit institutions' capital requirements;

Whereas Articles 5, 8, 9, 10, 11 as well as Annex 1 and 2 of this Directive are in accordance with the work of another international forum of banking supervisors on a refined and in some aspects more stringent supervisory treatment of the credit risks inherent in over-the-counter derivative instruments, in particular the extension of compulsory capital cover to over-the-counter derivative instruments concerning underlyings other than interest and foreign exchange rates and the possibility of taking into account the risk reducing effects of contractual netting agreements recognised by competent authorities when calculating the capital requirements for the potential future credit risks inherent in over-the-counter derivative instruments;

Whereas for internationally active credit institutions and groups of credit institutions in a wide range of countries, which compete with Community credit institutions, the rules adopted on the wider international level will result in a refined supervisory treatment of over-the-counter derivative instruments; whereas this refinement results in a more appropriate compulsory capital cover taking into account the risk reducing effects of supervisorily recognised contractual netting agreements on the potential future credit risks;

Whereas for Community credit institutions a similar refinement of the supervisory treatment of over-the-counter derivative instruments including the possibility of taking into account the risk reducing effects of supervisory recognised contractual netting agreements on the potential future credit risks can only be achieved by an amendment of Directive 89/647/EEC;

Whereas to ensure a level playing field between credit institutions and investments firms competing in the Community consistency in the supervisory treatment of their respective activities in the area of over-the-counter derivative instruments is necessary and can only be achieved by adaptations of the Council Directive 93/6/EEC[7];

Whereas adoption of this Directive constitutes the most appropriate means of attaining the desired objectives; whereas this Directive is limited to the minimum necessary to

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[7] OJ No L 141, 11.6.1993 p. 1-26.

attain these objectives and does not go beyond what is needed for this purpose;

Whereas this Directive concerns the European Economic Area (EEA) and whereas the procedure under Article 99 of the Treaty on the European Economic Area has been complied with;

Whereas adoption of this Directive has been the subject of consultations with the Banking Advisory Committee, which was set up by Council Directive 77/780/EEC,

HAVE ADOPTED THIS DIRECTIVE:

TITLE I - AMENDMENTS TO DIRECTIVE 77/780/EEC

Article 1
Amendment to Article 12

Article 12(3) of Directive 77/780/EEC is replaced by the following:

"3. Member States may conclude cooperation agreements, providing for exchange of information, with the competent authorities of third countries or with the non-banking supervisory authorities of third countries as defined in the first indent of paragraph 5 only if the information disclosed is subject to guarantees of professional secrecy at least equivalent to those referred to in this Article."

TITLE II - AMENDMENTS TO DIRECTIVE 89/647/EEC

Article 2
Amendment to Article 2

The following subparagraph is added to Article 2(2):

"The competent authorities may also include within the concept of regional governments and local authorities churches and religious communities constituted in the form of a legal person under public law, including non-profit-making bodies and undertakings controlled by them, in so far as they are empowered to raise taxes in accordance with legislation conferring on them the right to do so."

Article 3
New point 8 in Article 6(1)(a) and amendments to Article 6(1)(c)(2)

1. The following point 8 is added to Article 6(1)(a):

"8. asset items included under prepayments and accrued income that are of a purely accounting nature, carry no risk and have no counterparty;".

2. The following is added to Article 6(1)(c)(2) after the words "flat-rate weighting of 50%":

"...subject to the provisions of point (a)(8) of this paragraph;".

Article 4
Amendment to Article 6(2)

The following is added to the end of Article 6(2):

"The portion of unpaid capital subscribed to the European Investment Fund may be weighted at 20%."

Article 5
Amendment to Article 6(3)

Article 6(3) of the Directive 89/647/EEC is replaced by the following:

"3. The methods set out in Annex II shall be applied to the off-balance-sheet items listed in Annex III. They do not apply to contracts traded on recognised exchanges where they are subject to daily margin requirements and to foreign exchange contracts (except contracts concerning gold) with an original maturity of fourteen calendar days or less.

Article 6
Amendment to Article 6(4)

The following subparagraph is added to Article 6(4):

"The Member States may apply a 50% weighting to off-balance-sheet items which are sureties or guarantees having the character of credit substitutes and which are fully guaranteed, to the satisfaction of the competent authorities, by mortgages meeting the conditions set out in paragraph 1 (c)(1), subject to the guarantor having a direct right to such collateral."

Article 7

Amendments to Articles 7(1) and (2) and 8(1)

1. The following is added at the end of Article 7(1):

"... or secured, to the satisfaction of the competent authorities concerned, by collateral in the form of securities issued by those regional governments or local authorities."

2. The following is added at the end of Article 7(2):

"..., including collateral in the form of securities."

3. Article 8(1) of Directive 89/647/EEC is replaced by the following:

"The Member States may apply a weighting of 20% to asset items which are secured, to the satisfaction of the competent authorities concerned, by collateral in the form of securities issued by Zone A regional governments or local authorities other than those of the Member States, by deposits placed with Zone A credit institutions other than the lending institution, or by certificates of deposit or similar instruments issued by those credit institutions."

Article 8
Amendment to Annex II

Annex II to Directive 89/647/EEC shall be amended as laid down in Annex 1 hereto.

Article 9
Amendment to Annex III

Annex III to Directive 89/647/EEC is replaced by the Annex 2 hereto.

TITLE III - AMENDMENTS TO DIRECTIVE 93/6/EEC

Article 10
Amendment to Article 2 (10)

Article 2(10) of Directive 93/6/EEC is replaced by the following:

"10. over-the-counter (OTC) derivative instruments shall mean the off-balance-sheet items to which according to Article 6(3) of Directive 89/647/EEC the methods set out in Annex II of the said Directive shall be applied."

Article 11
Amendment to Annex II

Annex II, point 5. to Directive 93/6/EEC is replaced by the following:

"5. In order to calculate the capital requirement on their OTC derivative instruments, institutions shall apply Annex II to Directive 89/647/EEC.

The risk weightings to be applied to the relevant counter-parties shall be determined in accordance with Article 2 (9) of this Directive."

Article 12

1. Member States shall bring into force the laws, regulations and administrative provisions necessary for them to comply with this Directive by 31st December 1997. They shall forthwith inform the Commission thereof.

2. The provisions adopted pursuant to this paragraph shall contain a reference to this Directive or shall be accompanied by such reference at the time of their official publication. The procedure for such reference shall be adopted by the Member States.

3. Member States shall communicate to the Commission the texts of the main laws, regulations and administrative provisions which they adopt in the field covered by this Directive.

Article 13

This Directive shall enter into force on the date of its publication in the Official Journal of the European Communities.

Article 14

This Directive is addressed to the Member States.

Done at Brussels,

For the European Parliament	For the Council
The President	The President

1. The heading of Annex II to Directive 89/647/EEC shall be replaced by the following:

   "ANNEX II"

2. Annex II, point 1 to Directive 89/647/EEC shall be replaced by the following text:

   "1. Choice of the method

   To measure the credit risks associated with the contracts listed in Annex III point 1 and 2 credit institutions may choose, subject to the consent of the competent authorities, one of the methods set out below. Credit institutions which have to comply with Article 6 (1) of the Directive 93/6/EEC have to use method 1 set out below. To measure the credit risks associated with the contracts listed in Annex III point 3. all credit institutions have to use method 1 set out below."

3. Table 1 is replaced by the following table:

"TABLE 1[(a) (b)]

Residual maturity[(c)]	Interest-rate contracts	Contracts concerning foreign-exchange rates and gold	Contracts concerning equities	Contracts concerning precious metals except gold	Contracts concerning commodities other than precious metals
One year or less	0 %	1 %	6 %	7 %	10 %
Over one year to five years	0,5 %	5 %	8 %	7 %	12 %
Over five years	1,5 %	7,5 %	10 %	8 %	15 %

(a) Contracts which do not fall within one of the five categories indicated in this table shall be treated as contracts concerning commodities other than precious metals.

(b) For contracts with multiple exchanges of principal, the percentages have to be multiplied by the number of remaining payments still to be made according to the contract.

(c) For contracts that are structured to settle outstanding exposure following specified payment dates and where the terms are reset such that the market value of the contract is zero on these specified dates, the residual maturity would be equal to the time until the next reset date. In the case of interest rate contracts that meet these criteria and have a remaining maturity of over one year, the percentage shall be no lower than 0,5%."

4. In Table 2 the heading in the first row third column is replaced by:

"Contracts concerning foreign-exchanged rates and gold"

5. At the end of point 2. the following paragraph is inserted:

"For both methods the supervisory authorities have to ensure that the notional amount to be taken into account is an appropriate yardstick for the risk inherent in the contract. Where, for instance, the contract provides for a multiplication of cash flows, the notional amount has to be adjusted in order to take into account the effects of the multiplication on the risk structure of that contract."

6. At the end of point 3. (b) the following paragraph is inserted:

"The competent authorities may recognise as risk reducing contractual netting agreements covering foreign exchange contracts with an original maturity of fourteen calendar days or less, written options or similar off-balance-sheet items to which this Annex does not apply because they bear only a negligible or no credit risk. If, depending on the positive or negative market value of these contracts, their inclusion in an other netting agreement can result in an increase or decrease of the capital requirements, competent authorities must oblige their credit institution to use a consistent treatment."

7. The first paragraph and the first indent of the second paragraph of point 3. (c) (ii) is replaced by the following:

"(ii) Other netting agreements

In application of **Method 1** in Step (a) the current replacement cost for the contracts included in a netting agreement may be obtained by taking account of the actual hypothetical net replacement cost which results from the agreement; in the case that netting leads to a net obligation for the credit institution calculating the net replacement cost, the current replacement cost is calculated as "0";

In Step (b) the figure for potential credit exposure for all contracts included in a netting agreement may be reduced according to the following equation:

$$PCE_{red} = 0{,}4 * PCE_{gross} + 0{,}6 * NGR * PCE_{gross}$$

where:

- PCE_{red} = the reduced figure for potential future credit exposure for all contracts with a given counterparty included in a legally valid bilateral netting agreement

- PCE_{gross} = the sum of the figures for potential future credit exposures for all contracts with a given counterparty that are included in a legally valid bilateral netting agreement and that are calculated by multiplying their notional principal amounts by the percentages set out in table 1

- NGR = "Net-to-gross ratio": at the discretion of the supervisory authorities either:

  (i) separate calculation: the quotient of the net replacement cost for all contracts included in a legally valid bilateral netting agreement with a given counterparty (numerator) and the gross replacement cost for all contracts included in a legally valid bilateral netting agreement with that counterparty (denominator) or

  (ii) aggregate calculation: the quotient of the sum of the net replacement cost calculated on a bilateral basis for all counterparties taking into account the contracts included in legally valid netting agreements (numerator) and the gross replacement cost for all contracts included in legally valid netting agreements (denominator)"

  If Member States permit credit institutions a choice of methods, the method chosen is to be used consistently.

For the calculation of the potential future credit exposure according to the above formula perfectly matching contracts included in the netting agreement may be taken into account as a single contract with a notional principal equivalent to the net receipts. Perfectly matching contracts are forward foreign exchange contracts or similar contracts in which notional principal is equivalent to cash flows if the cash flows fall due on the same value date and fully or partly in the same currency.

In the application of Method 2, in Step (a)

- perfectly matching contracts included in the netting agreement may be taken into account as a single contract with a notional principal equivalent to the net receipts; the notional principal amounts are multiplied by the percentages given in Table 2.

"ANNEX III
TYPES OF OFF-BALANCE-SHEET ITEMS

1. Interest-rate contracts

a) Single-currency interest rate swaps,
b) Basis swaps,
c) Forward-rate agreements,
d) Interest-rate futures,
e) Interest-rate options purchased,
f) Other contracts of a similar nature.

2. Foreign-exchange contracts and contracts concerning gold

a) Cross-currency interest-rate swaps,
b) Forward foreign-exchange contracts,
c) Currency futures,
d) Currency options purchased,
e) Other contracts of a similar nature,
f) Contracts concerning gold of a nature similar to a) to e).

3. Contracts of a nature similar to those in points 1 (a) to (e) and 2 (a) to (d) concerning other reference items or indices concerning:

a) Equities,
b) Precious metals except gold,
c) Commodities other than precious metals,
d) Other contracts of a similar nature."

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a) Cross-currency interest-rate swaps,
b) Forward foreign-exchange contracts,
c) Currency futures,
d) Currency options purchased,
e) Other contracts of a similar nature,
f) Contracts concerning gold of a nature similar to a) to e).

3. Contracts of a nature similar to those in points 1 (a) to (e) and 2 (a) to (d) concerning other reference items or indices concerning:

a) Equities,
b) Precious metals except gold,
c) Commodities other than precious metals,
d) Other contracts of a similar nature."

IMPACT ON COMPETITIVENESS AND EMPLOYMENT

I. What is the main justification for the measure?

The purpose of the proposed Directive is to update a number of provisions (for example, that concerning the European Investment Fund) and to reduce the weighting applied to specific assets where the risk involved does not correspond to the current weighting. Furthermore the proposed Directive aims at introducing a refined and more stringent supervisory treatment of over-the-counter derivative instruments, thus, aligning the EU-legislation to measures adopted by another international forum of banking supervisors in the wider context of G 10-countries.

II. Characteristics of the enterprises concerned

The proposed Directive concerns credit institutions and investment firms in the European Union.

III. What are the obligations imposed directly on enterprises?

The proposal imposes new obligations only for over-the-counter derivative instruments of credit institutions and investment firms. These instruments will be subject to a refined and more stringent supervisory treatment requiring a capital cover better reflecting the existing credit risks. However, the total amount of compulsory capital cover will not necessarily be higher than under the current legislation. The proposed Directive affords Member States the possibility to recognise risk reducing effects of contractual netting on the potential future credit risks inherent in the netted over-the-counter derivative instruments. If Member States choose to do so an increase of compulsory capital cover resulting from the more stringent treatment is likely to be balanced by a decrease resulting from risk reducing effects of the recognised netting.

IV. What obligations are likely to be imposed on enterprises through local authorities?

None.

V. Are there any special measures for SMEs? If so, what type of measures are they?

None.

VI. What is the likely effect on:

(a) the competitiveness of enterprises?

(b) employment?

(a) Some of the provisions of the proposed Directive grant more favourable treatment to a number of asset items constituting claims as compared with the solvency ratio. In so far as capital requirements are lower for the same balance sheet, it may be hoped that the capital thus released will increase the amount of credit available for enterprises.

For over-the-counter derivative instruments the proposed Directive introduces a refined and more stringent supervisory treatment. However, a detrimental impact on the competitiveness of Community institutions is not likely. The proposed measures are closely in line with regulations by another international forum of banking supervisors in the wider context of G 10 countries. Even where comparable provisions might not apply, e.g. for third-country investment firms, there is no evidence of competitive disadvantages. As already mentioned, an increase of compulsory capital cover resulting from the more stringent treatment is likely to be balanced by a decrease resulting from the supervisory recognition of risk reducing effects of contractual netting on the potential future credit risks. Furthermore, an advanced legal framework with a sound supervisory system in place contributes to the strength and, thus, to the competitiveness of financial institutions.

(b) The effects on employment are limited to the consequences of the increase in credits that the proposed measures may produce.

VII. Have the two sides of industry been consulted? What are their views?

No. The proposed measures affect only the prudential legislation governing credit institutions, and in a manner largely favourable to the latter.

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