

The crisis of 2007–2009 and Basel 2.5

*Dr Alexander Ressos, TEP
Attorney-at-Law (Switzerland), Solicitor (Hong Kong),
Solicitor (England & Wales)*

The global financial crisis that began in the summer of 2007 with the turmoil in the US subprime mortgage market and reached its peak after the failure of Lehman Brothers in September 2008 was, among many other things, a failure of the Basel framework. Banks that reported comfortable capital ratios under the rules then in force had to be rescued by their governments. The losses they suffered in their trading books exceeded by far the capital that the value-at-risk models had required, while their Tier 1 capital contained hybrid instruments that proved unable to absorb losses in a going concern. Several institutions had financed long-term illiquid assets with short-term wholesale funding that evaporated within days.¹

The political response came from the Group of Twenty, whose leaders met for the first time in Washington in November 2008 and again in London in April 2009 and Pittsburgh in September 2009. They called for stronger capital standards, for measures against procyclicality, for a supplementary non-risk-based measure of leverage and for standards on liquidity. The Financial Stability Forum, which had been housed at the BIS since 1999, was converted into the Financial Stability Board in April 2009 and given the task of coordinating the reform agenda.² The Basel Committee became the main technical workshop of that agenda in the field of banking.

The first repairs concerned the trading book and securitisation. In July 2009, the Committee published a set of revisions that became known as Basel 2.5. It introduced a stressed value-at-risk requirement, calculated on data from a period of significant financial stress, in addition to the ordinary value-at-risk requirement. It also introduced an incremental risk charge for default and migration risk in the trading book and raised the capital charges for resecuritisation exposures. The capital requirements for trading activities of large banks increased substantially as a result.³

These measures were intended as a bridge. A fundamental review of the trading book followed in several consultative stages and resulted in a new

market risk framework in January 2016, revised in January 2019. It replaced value at risk with expected shortfall, tightened the boundary between trading book and banking book and made the approval of internal models depend on the performance of individual trading desks.⁴ Its implementation became one of the most delayed elements of the whole reform package, as later sections of this chapter show.

1 Notes

1. On the shortcomings of the pre-crisis framework, see Basel Committee, Strengthening the Resilience of the Banking Sector (consultative document, December 2009), introduction, and Financial Stability Forum, Report on Enhancing Market and Institutional Resilience (April 2008). To be verified. ↩
2. G20 Leaders' Statement, Pittsburgh Summit (24–25 September 2009), section on strengthening the international financial regulatory system. To be verified. On the FSB, see Part F, chapter IV. ↩
3. Basel Committee, Revisions to the Basel II Market Risk Framework and Enhancements to the Basel II Framework (both July 2009), together with Guidelines for Computing Capital for Incremental Risk in the Trading Book (July 2009). To be verified. ↩
4. Basel Committee, Minimum Capital Requirements for Market Risk (January 2016; revised January 2019), commonly known as the Fundamental Review of the Trading Book (FRTB). To be verified. ↩

For general information only. This article does not constitute legal or tax advice, does not replace advice on an individual case and creates no lawyer-client relationship. It reflects the legal position as of September 2026.

Online version: helveticaregister.com/basel-the-crisis-of-20072009-and-basel-2-5