Response from the Italian Banking Association
to the EBA consultation document

Draft Regulatory Techincal Standards On criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile under Article 90(2) of the proposed Capital Requirements Directive

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Preliminary remarks

1. There is agreement with the aims expressed in the introduction to the consultation document i.e. the selection of a combined approach to identify the staff which have a material impact on the risk profile of institutions, in order to ensure appropriate harmonization and a level playing field among European countries, taking the risk profile of each institution into account.

2. We believe it is fundamental to use internal criteria which must be based on corporate risk assessment processes and must reflect the institution's risk profile, so as to ensure that, when identifying the most significant personnel, the level of risk and the business strategy of the company are held in due consideration.

3. Bearing in mind the need/appropriateness of identifying general criteria for all companies operating within Europe, we are of the opinion that it is essential to have **discretionary powers in the assessments based on the type of business** of the companies, or of the activities of specific organisational units or functions within the sphere of a single company so that the criteria identified in the consultation document are actually meaningful. Here we are, in particular, referring to the substantial differences existing between traditional activities, such as retail, on the one hand, and investment banking or asset management on the other.

4. The Capital Requirements Directive contains specific principles and criteria to which the banks must comply in order to ensure correct processing and implementation of remuneration frameworks, **in order to effectively manage any possible conflicts of interest**, to guarantee that the remuneration system takes appropriate account of the current and future risks, of the level of capitalization and the levels of liquidity of each intermediary. With the specific intention of achieving these objectives, in addition to the provisions contained in CRDIII, in CRDIV a number of new and more stringent provisions have been introduced for systems of remuneration of staff who have a material impact on the institution's risk profile, specifically intervening on variable remuneration and on the weight that it must have in comparison to the fixed component.

5. In order to clarify ABI's proposals contained in the responses to the consultation questions, it is appropriate to reflect on the expression “staff who take significant risks”: this, in particular, refers to staff members whose activities have or may have a material impact on the bank's risk profile. We are therefore talking about staff identified by the internal process of identifying risks in a company, whose remuneration system may be likely to lead to excessively risky conduct for the company.

Therefore we believe that the material risk takers cannot be identified exclusively on the basis of the level of their gross annual remuneration, regardless of the variable component.

6. Lastly, without providing specific answers to the consultation questions on costs of implementing the proposals, we believe that the impact analysis conducted by the EBA is thorough and that the most significant costs are those associated with technology, therefore those relating to training and changes to internal processes.

Response to the Consultation questions

Article 3 – Qualitative and quantitative criteria

(1) Staff shall be identified as having a material impact on an institution's risk profile if they meet one or more of the following criteria:

a. the staff member is a member of the management body;

b. the staff member is a member of the senior management;

c. the staff member is responsible and accountable to the management body for the activities of the internal risk control function, the compliance function or the internal audit function;

d. the staff member heads a business unit (within the meaning of Article 137(1)(3) of Regulation (EU) No xxxx/2013 [CRR]);

e. the staff member heads a function responsible for legal affairs, taxation, human resources, information technology, budgeting, economic;

Q1: Is the list of specific functions listed appropriate or should additional functions be added?

> We believe that the list of functions is appropriate and no additions are required. We do think, however, that it would be appropriate to point out that the qualitative criteria should be taken into consideration, provided that the remuneration framework of the person in question is such as to encourage the taking of risks (see quantitative criteria), or that the individual has been identified as a staff member whose activities have a material impact on the company's risk profile within the scope of the internal process of identification of company risks (see internal criteria).

f. the staff member has, individually or collectively with other staff members, authority to commit to credit risk exposures of a nominal amount per transaction which represents 0.25% of the institution's Common Equity Tier 1 capital;

Q2: Can the above criteria be easily applied and are the levels of staff identified and the provided threshold appropriate?

The criterion is not easy to apply due to the extremely diversified types of corporate organisation.

The company risk assessment models, in fact, are not all similar to the two types presented in the paper: there are very many others and not all intermediaries adopt them in the same way.

In addition, many banks are not currently equipped with the management tools to allow them to assess risk levels for each individual desk or individual person: more commonly their assessment ability stops with the highest levels, macro areas or divisions, with difficulty in assessing risks in a specified and detailed manner.

Moreover, certain risks are not even considered in the consultation proposal, such as those regarding collateral or counterparty (predominant within the scope of managing derivative products or, for example, securities lending) or operating risks. In some companies there are desks that are outside the perimeter of risk takers identified as such, since they work mainly on counterparty risk and on certain non-standard derivatives where the prevalent risk is one of legality or reputation.

All the afore-mentioned risks, however, are taken into consideration by companies in their internal risk assessment process, based on the type of activity that they perform.

This having been said, we believe that the numerical approach runs the risk of becoming bridled in specific procedures, that are sometimes difficult to quantify in detail and cannot be quantified equally among all the banks, and of leaving out, on the other hand, elements that are not always numerically definable, but with considerable effects on risks.

The impact of the provisions under examination will be negligible in many cases, since risk taking is often delegated solely to Committees.

Moreover, it would also be necessary to clarify the concept of having the “authority to commit”, as this could refer to individuals who have deliberative powers and to those whose task it is to propose business opportunities (front office areas) or to assess the related risks (risk management).

g. in relation to an institution to which the derogation for small trading book business under Article 89(1) of Regulation (EU) No xxxx/2013 [CRR] does not apply, the staff member has, individually or collectively with other staff members, authority to commit to transactions on the trading book which in aggregate represent one of the following:

i. where the standardised approach is used, an own funds requirement for market risks of 0.25% or more of the institution’s Common Equity Tier 1 capital;

ii. where an internal model based approach is used, 5% or more of the institution’s internal value-at-risk limit for trading book exposures at a 95th percentile, one-tailed confidence interval level;

Q3: Can the above criteria be easily applied and are the levels of staff identified and the provided thresholds appropriate?

The criterion is not easy to apply and the reasons for this are those expressed in our response to Q2.

h. the staff member has managerial responsibility for a group of staff members who have individual authorities to commit the institution to transactions, and the sum of those authorities equals or exceeds a threshold set out in point (f) or in point (g);

i. the staff member has managerial reponsibility for a staff member whose professional activities have or may have a material impact on the institution’s risk profile according to the internal risk identification process in Article 2;

j. the staff member has, individually or collectively with other staff members, the authority to take, approve or veto decisions on the introduction of new products, material processes, or material systems.

(2) Staff shall be identified as having a material impact on an institution’s risk profile if they meet one or more of the following criteria, subject to Article (4):

a. the staff member could, in accordance with the institution’s remuneration policy, be awarded variable remuneration that exceeds both of the following amounts:

i. 75% of the fixed component of remuneration;

ii. EUR 75 000;

Q4 a) Is this criterion appropriate to identify risk takers?

We believe that the proposed criterion is capable of identifying staff with a significant impact on an institution's risk profile.

Q4 b) Are the thresholds set in the criterion appropriate?

We believe that the proposed threshold should be raised.

Therefore, our proposal is that the variable remuneration should be above both the following figures:

75% of fixed remuneration;

€.100.000

b. the staff member has been awarded total gross remuneration in one of the two preceding financial years which is equal to or greater than the lowest total remuneration that was awarded in that year to a member of staff who performs professional activities for the same entity and who either is a member of senior management or meets one of the criteria in paragraph (1) or one of the internal crietria referred to in Article 2;

Q5 a) Can the above criterion be easily applied?

The proposed criterion is not easy to apply when reference is made to two financial years. Our proposal, therefore, is to introduce the reference **to just one financial year.** In addition to facilitating implementation, this method would avoid continuous changes in the perimeter of the so-called *risk takers*.

In addition, we believe that the proposed criterion needs to be used together with the quantitative criterion relating to the incidence of variable remuneration.

Therefore, our proposal is to modify the criterion as follows:

b. **Staff members whose variable remuneration exceeds 75% of the fixed remuneration and who were awarded a total gross remuneration during the preceding financial year** which is equal to or above the lowest total remuneration assigned in that year to an employee who performs professional activities for the same entity and who is either a member of the senior management or meets one of the qualitative criteria identified in paragraph (1) or one of the internal criteria referred to in Art. 2.

Q5 b) Would it be more appropriate to use remuneration which potentially could be awarded as a basis for this criterion?

In order to identify staff members who have a material impact on an institution's risk profile due to the remuneration framework, we believe it is correct to refer to the variable remuneration which could potentially be awarded (the so-called target value).

In those cases, however, where the procedure does not envisage reference to a target variable remuneration or does not identify the value of the bonus opportunity in advance - as happens, for example, but not solely, with investment banking - it would be necessary then to identify the staff members who have a material impact on the institution's risk profile taking account of the remuneration values of the previous year.

This comment should be taken into consideration in all cases where reference is made to potentially awarded remuneration.

Q5 c): What would be the difference in implementation costs if the potentially awarded remuneration would be used as a basis?

On the basis of what was said in response to question Q5 b), we are not talking about additional costs but about an intervention on the policies of non-presumable remuneration, taking account of the management differences in the companies in the sector.

c. the staff member has been awarded total gross remuneration of EUR 500.000 or more in one of the two preceding financial years.

Q6: Can the above criterion be easily applied and are the threshold and the levels of staff identified appropriate?

The proposed criterion is not easy to apply when reference is made to two financial years. Our proposal, therefore, is to introduce the reference **to just one financial year.** In addition to facilitating implementation, this method would avoid continuous changes in the perimeter of the so-called *risk takers*.

In order to identify staff members who have a material impact on an institution's risk profile due to the remuneration framework, we believe it is correct to refer to the variable remuneration which could potentially be awarded (the so-called target value).

In those cases, however, where the procedure does not envisage reference to a target remuneration - not identified in advance as happens, for example, but not solely, with investment banking - it would be necessary then to identify the staff members who have a material impact on the institution's risk profile taking account of the remuneration values of the previous year.

In addition, we believe that the proposed criterion needs to be used together with the quantitative criterion relating to the incidence of variable remuneration.

Therefore, our proposal is to modify the criterion as follows:

c. **Staff members whose variable remuneration exceeds 75% of the fixed remuneration and who were awarded** a total gross remuneration of €500,000 or more **during the preceding financial year.**

d. the staff member is within the 0.3% of staff who received the highest total gross remuneration in either the most recent financial year or in the preceding financial year

Q7: Can the above criteria be easily applied and are the levels of staff identified appropriate?

We agree with the identification of a fixed ratio between the number of most significant staff and the overall staff numbers in an institution, and consider in general that the proposed value is appropriate (0.3% of employees).

Furthermore, in line with the suggestion - commented on in the preliminary remarks - to differentiate these criteria based on the companies' type of business, we believe that the aforesaid **value needs to be halved at least, when referring to banks of a strongly retail nature.**

We are of this opinion since, in order to take the same risks and achieve equivalent economic results, these banks are forced to address a much broader customer base (spread over a much wider area of the country) compared to investment banks, therefore requiring much higher numbers of staff, thereby significantly reducing their influence on the overall risk profile of the company.

Consequently, the application of the same percentage ratio to the two categories of companies represented above would lead, in the case of retail banks, to the inclusion among the most significant members of staff, those resources: i) with negligible impact on the overall level of risk for the company and ii) with considerably more modest levels of remuneration and with much less aggressive forms of remuneration compared to those found amongst staff in investment banks just outside the aforesaid threshold of 0.3%

We also feel that for the proposed criterion it is necessary to refer **to just the previous financial year.** In addition to facilitating implementation, this method would avoid continuous changes in the perimeter of the so-called *risk takers.*

In order to identify staff members who have a material impact on an institution's risk profile due to the remuneration framework, we believe it is correct to refer to the variable remuneration which could potentially be awarded (the so-called target value).

In those cases, however, where the procedure does not envisage reference to a target remuneration - not identified in advance as happens with investment banking - it would be necessary then to identify the staff members who have a material impact on the institution's risk profile taking account of the remuneration values of the previous year.

In addition, we believe that the proposed criterion needs to be used together with the quantitative criterion relating to the incidence of variable remuneration.

Therefore, our proposal is to modify the criterion as follows:

d. **Staff members whose variable remuneration exceeds 75% of the fixed remuneration** and who are included within 0.3% (this percentage is reduced to 0.15% for retail banks) of staff who are potentially awarded the highest total gross remuneration or have received the highest total gross remuneration **during the most recent financial year.**

(3) In paragraph (1), a reference to staff members having, individually or collectively with other staff members, authority to commit to transactions or exposures or to take, approve or veto a decision includes both of the following categories of staff:

a. staff who are responsible for advising on or initiating such commitments or decisions;

b. staff who are members of a committee which has authority to make such commitments or to take such decisions.

Q8: Are there additional criteria which should be used to identify staff having a material impact on the institutions risk profile?

We do not feel that there are additional useful criteria in the identification of staff with a material impact on an institution's risk profile.