EBA/Op/2014/10

15 October 2014

Opinion of the European Banking Authority on the application of Directive 2013/36/EU (Capital Requirements Directive) regarding the principles on remuneration policies of credit institutions and investment firms and the use of allowances

Introduction and legal basis

1. The EBA is monitoring closely the developments of remuneration practices within the EU and is mandated with several tasks in this area. Appropriate remuneration policies are an important tool for aligning the incentives for staff with the risk strategy and profile of the institutions. Inappropriate remuneration policies were identified as one underlying factor of the financial crisis.

2. Following the adoption of Directive 2013/36/EU[1] (Capital Requirements Directive or CRD) a number of institutions across the EU have recently changed their remuneration policies and introduced 'role-based allowances', which they treat as part of the fixed remuneration paid to staff. The introduction of such allowances has led to a widening of the scope for granting variable remuneration, alongside an increase in the supposedly fixed remuneration.

3. As part of its market monitoring and assessment tasks, and in response to a request made by the European Commission on 12 February 2014, the EBA has launched an investigation into the nature of these allowances and their consistency with CRD IV provisions. For that purpose, the EBA has collected information from all competent authorities in order to analyse the types and use of these allowances.

4. The EBA has analysed the responses provided by the competent authorities using also the disclosed institutions' remuneration reports and other information that is publicly available. The EBA findings are presented in this Opinion and in the annexed report and will be taken into account when updating the guidelines on remuneration policies and practices.

[1] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

5. This Opinion is addressed to the European Commission and the competent authorities, as defined in Article 4 (1) (40) of Regulation (EU) No 575/2013[1].

6. The EBA competence to deliver this Opinion is based on Articles 29(1)(a) and 34(1) of Regulation (EU) No 1093/2010, as amended, given that institutions' remuneration policies and practices relate to the EBA's area of competence.

General comments

7. In accordance with the CRD, the institutions' remuneration policy has to be consistent with, and promote, sound and effective risk management and should not encourage risk-taking that exceeds the level of tolerated risk of the institution.

8. To this end, the remuneration policy has to make a clear distinction between 'fixed' and 'variable' remuneration. Fixed remuneration should reflect primarily relevant professional experience and organisational responsibility as set out in an employee's job description. In turn, variable remuneration should comprise all components linked to performance or, in exceptional cases, other contractual elements that do not form part of routine employment packages.

9. Such a distinction is strictly linked to the limitation set out in Article 94(1)(g) of the CRD (bonus cap), i.e. that the variable component shall not exceed 100% of the fixed component of the total remuneration (200% with shareholders' approval).

10. Institutions have introduced role-based allowances linked to the position and organisational responsibility of staff. 'Allowances' are additional payments or benefits paid in addition to the traditional fixed remuneration (basic salary) and the directly performance-related variable remuneration (bonus). Institutions tend to consider all allowances and, in particular, role-based allowances, as fixed remuneration, and argue that they are not based on performance.

11. Although 'role-based allowances' are not related explicitly to performance, some common characteristics include the fact that they are not part of the basic salary and are not pensionable, are initially granted for a limited period of time, can be reduced, suspended or cancelled by institutions on a fully discretionary basis, or are based on other contractual conditions which do not form part of routine employment packages.

12. Without the role-based allowances, or if such allowances were effectively considered as variable remuneration, the EBA's understanding is that the respective remuneration policies would not comply with the limit on the variable remuneration to 100% of the fixed component of remuneration (200% with shareholders' approval).

[1] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27. 6.2013, p. 1).

13. The EBA's opinion is that in order to achieve the result prescribed by the CRD, i.e. in order to qualify as fixed remuneration, the conditions for their granting and the amount of the role-based allowances should be predetermined, transparent to staff, permanent, i.e. maintained over time and tied to the specific role and organisational responsibilities, not provide incentives to take risks and, without prejudice to national law, be non-revocable.

14. Therefore, the EBA is of the view that 'role-based allowances' which are not predetermined, are not transparent to staff, are not permanent, provide incentives to take risks or, without prejudice to national law, are revocable, should not be considered as fixed remuneration but should be classified as variable in line with the letter and purpose of the CRD. The amount paid is not fixed, is not permanent, i.e. maintained over time for the specific role and organisational responsibilities, can be understood as being indirectly performance-related given that its review depends on cost and benefit considerations, is neither set out in a pre-defined objective manner nor is transparent to staff and therefore does not promote sound and effective risk management, and is based on other contractual conditions which do not form part of routine employment packages.

15. Where competent authorities are aware of the use of the role-based allowances referred to in paragraph 14 they should use all necessary supervisory measures to ensure that by 31 December 2014 institutions' remuneration policies are updated to reflect the findings of this Opinion that such allowances should be classified as variable remuneration and that payments of such allowances are not causing institutions to contravene the bonus cap and other CRD requirements.

Specific comments

Specific comments are set out in the Annex to the report.