European
Banking
Federation

EBF_ 014354
03 June 2015

The European Banking Federation is the voice of the European banking sector, uniting 32 national banking associations in Europe that together represent some 4,500 banks - large and small, wholesale and retail, local and international - employing about 2.5 million people. EBF members represent banks that make available loans to the European economy in excess of €20 trillion and that securely handle more than 300 million payment transactions per day. Launched in 1960, the EBF is committed to creating a single market for financial services in the European Union and to supporting policies that foster economic growth. Website: www.ebf-fbe.eu

EBF comments on the EBA draft Guidelines on sound remuneration policies

General comments:

The EBF considers that the draft guidelines for most part are clear and precise. However, as set out below, several issues merit further consideration.

Notably, the European banks are concerned by the EBA's opinion, as confirmed by the Commission, requiring application of all remuneration related provisions of the CRD IV/CRR to all banks without consideration of *inter alia* their size and complexity. Considering that the main spirit of the corporate governance/remuneration related provisions of the CRD IV/CRR is curbing excessive and imprudent risk-taking, the aim supported by the European banks, it seems improper to remove the possibility of neutralisation of some provisions where the non-application of these do not pose any material risk. The members of the EBF consider that the approach taken by the EBA will incur disproportionately high costs, set an uneven playing field among institutions and poses the threat that institutions will refrain from variable remuneration in the future.

The aim of the CRD IV specific risk alignment remuneration requirements must be that the institution has a robust governance arrangement with remuneration policies and practices that are consistent with and promote a sound and effective risk management. Since no two institutions are identical (as acknowledged by the legislator in recital 66 of CRD IV) the CRD IV specific risk alignment remuneration requirements should be implemented and applied within each institution with regard to the size, internal organisation and the nature, scope and complexity of the institution's activities (i.e. based on a risk-based approach). In other words, when implementing and applying the CRD IV specific risk alignment remuneration requirements within institutions, institutions must be allowed to apply the proportionality principle as clearly set out in recital 66 and articles 92 and 94 of CRD IV. Although certain requirements may be deemed applicable by all institutions regardless of their risks, these requirements must only be applied in a manner that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities (cf. articles 92 and 94 of CRD IV). Further, these remuneration requirements must only be applied to the extent appropriate, or rather if appropriate (cf. articles 92 and 94 of CRD IV). As clearly indicated in recital 66 of CRD IV, the legislative intention is to allow the disapplication of disproportionate

European Banking Federation

remuneration requirements. It warrants noting that the proportionality principle as described herein applies to all remuneration requirements under the CRD IV and to all institutions without distinction. Having regard to the above, it seems too far-reaching to determine that all CRD IV specific risk alignment remuneration requirements must be applied in full and by all institutions. For example, variable remuneration below a threshold of EUR 100 000 could not be considered to give incentives to increase the institution´s risk profile, regardless of the institutions size, in the sense referred to here. Therefore, the application of the deferral requirements and requirement to award 50 per cent of the variable remuneration in shares/share-linked instruments should be 'neutralised'.

Having regard to the impact of the EBA´s guidelines on institutions, the general and fundamental principles of EU-law including the principle of proportionality cannot be disregarded.

As mentioned in the background text of the guidelines variable remuneration provides an incentive for staff members to pursue the goals and interests of the institutions and enables them to share in its success. Moreover, staff members' behaviour can be influenced by the use of well-designed variable remuneration schemes. In addition, variable remuneration enables institutions to lower salary costs in unfavourable market conditions. In the light of this it is important that the remuneration requirements are not too complex and burdensome so that they are difficult to apply. Although it is important to regulate variable remuneration, the requirements should not lead institutions to refrain from variable remuneration due to complicated rules as that would lead to the loss of all the benefits of variable remuneration.

Finally, the EBF believes that in many parts the Guidelines impose requirements instead of recommendations, where supposedly the nature of guidelines should be soft law.

Specific comments:

Note to EBA: in addition to answers given to the specific questions included in the EBA consultation paper the EBF also provides below its comments to the other parts of the paper.

Section 2. Scope:

The scope of the application is not clear enough and should be further explained, in particular it should be clarified that the remuneration regulations only apply in relation to members of staff that are deemed "employees" of the institution pursuant to national labour law.

Moreover, it should be clarified that the CRD IV specific risk alignment remuneration requirements, such as the cap on variable remuneration, do not apply in relation to captive AIFMs, captive UCITS asset managers, captive insurance providers or any other subsidiaries within institutions which are governed by specific sectorial legislation (cf. clarification with respect to setting up a remuneration policy in paragraph 39 of the guidelines).

It should also be noted that the legislative intention is to allow the disapplication of certain CRD IV specific risk alignment remuneration requirements. Particularly recital 66 of CRD IV should

be noted which states: *"/.../ it would not be proportionate to require certain types of investment firms to comply with all of those provisions [referring to the remuneration provisions of CRD IV]."*

In this context, as relates to captive AIFMs, UCITS asset managers and insurance providers, it should be noted that the European Parliament and Council did not deem it necessary to introduce a cap on variable remuneration in the AIFMD or UCITS Directive or Solvency Directive.

As relates to the suggested extension of the cap, it should also be considered that an extended application of the CRD IV would create an uneven playing-field between captive and non-captive businesses. This is contrary to the objectives of the remuneration regulations, spirit of the internal market and article 16 of the EBA founding regulation (1093/2010) according to which guidelines should ensure common, uniform and consistent application of EU Law.

In line with the above, the "*ESMA guidelines on sound remuneration policies under the AIFMD*" state that where an individual works for two separate entities of which one is covered by CRD IV and the other by AIFMD, remuneration for services provided for an AIFM should be governed solely by the AIFMD rules.

Having regard to the above, the suggested extension of the application of the CRD IV specific risk alignment remuneration requirements, such as the cap on variable remuneration, to captive AIFMs, UCITS asset managers and insurance providers, and other subsidiaries governed by specific sectorial legislation and any other non-consolidated subsidiaries should be rethought.

Moreover, further clarification is sought on whether Joint Ventures (JV) with companies not covered by these Guidelines are in scope? Are staff to be included if they are assigned to a non-banking JV or a JV which is not covered by these Guidelines especially if they are not paid by the JV (the home company continues to pay them upon instruction from the JV as the employee is on assignment from the home company)? This would discourage JVs with banks if such personnel were to come under the EBA remit.

Q 1: Are the definitions provided sufficiently clear; are additional definitions needed?

Section 3. Definitions:

It should be noted that the definition stated under letter "c." (variable remuneration) is not clear enough and too wide. Therefore, we suggest providing a more precise definition or at least a reference to Title III of the Guidelines, in which variable remuneration is categorised.

As relates to the definition of staff under letter "g", it should be clarified that the CRD IV remuneration requirements only apply in relation to staff members who are deemed "employees" of the relevant institution pursuant to applicable national labour law.

Section 4. Currency conversion:

The mentioned budget rates are a reasonable criteria for most of countries, but for high volatile/high inflation countries (such as: Argentina, Venezuela and Russia) this rate does not necessarily reflect the correct purchasing power of an executive receiving remuneration in local currency to buy assets in euros, for instance. This rule should allow adaptation in very specific cases to better reflect the countries current environment in order not to capture people in the quantitative criteria wrongly.

Moreover, we consider that the exchange rate to be used should be the annual average exchange rate of the year to which the remunerations relate (i.e. in 2014, the average exchange rate for fixed and variable remuneration during 2014, was used to determine the members of the identified staff for 2015).

Q 2: Are the guidelines in chapter 5 (remuneration policies for all staff, including identified staff) appropriate and sufficiently clear?

5. Remuneration policies for all staff

It should be clarified whether the reference to 'remuneration policy' throughout the EBA guidelines is a reference to general principles on remuneration or to a physical document titled remuneration policy. Currently the EBA seems to define 'remuneration policy' as both general principles and a physical document. In order to avoid uncertainties as to e.g. the institution's management body in its supervisory function's (in many member states being the board of directors) obligations pursuant to the guidelines, the EBA should consider re-visiting its references to 'remuneration policy'.

Considering that the institution's management body in its supervisory function is responsible for the adoption and maintenance of the remuneration policy (cf. paragraph 17 of the guidelines), the remuneration policy should not contain detailed regulation. Instead, the remuneration policy adopted by the institution's management body in its supervisory function should only contain the institution's overall principles for the institution's remuneration policy and practices.

Paragraph 8

The requirement to differentiate staff within the category of identified staff should be applied only if and to the extent variable remuneration is applied within the institution. Otherwise it is difficult to see the purpose of the requirement or how it would counter excessive risk taking.

Paragraph 10

This paragraph requires that all institutions should comply with regard to the remuneration policy for all staff with the principles set out in Article 92 of CRD which includes, among others, in paragraph 2, letter c), that the institution's board of directors adopts and periodically reviews the general principles of the remuneration policy and is responsible for overseeing its implementation. According to CRD these principles are only stated for identified staff, therefore the board of directors should not be responsible for adopting the remuneration policy of all staff which gives excessive scope of responsibilities to the board.

European Banking Federation

<u>Paragraph 14</u>
Pursuant to corporate law of several member states, the management body in its supervisory function does not decide on the details of the business operations, such as detailed remuneration policy. It is therefore important to clarify that the remuneration policy adopted by the management body in its supervisory function does not contain detailed rules but rather general provisions.

The institutions should be allowed to delegate in accordance with national corporate law implementing rules to the appropriate level within the institution (e.g. to management and business support function level).

Furthermore, too many details in the remuneration policy may lead to too complex remuneration policies which may be difficult for staff members to understand. Too many details in the remuneration policy may therefore counter the intention to create transparent remuneration policies.

The EBA should also elaborate on the meaning of 'performance objectives' referred to in paragraph 14 and throughout the guidelines. Further, it is important to take account of other regulations e.g. the Shareholders' Rights Directive.

Q 3: Are the guidelines regarding the shareholders' involvement in setting higher ratios for variable remuneration sufficiently clear?

Section 6. Governance of remuneration:

<u>Paragraph 17</u>

As stated above in paragraph 10, the board of directors should not be responsible for the remuneration policy of the institution as a whole because this requirement would increase the scope of responsibilities established in CRD IV and could be considered excessive. It is not the board of directors´ responsibility to decide on single staff members´ remuneration. The board of directors should only be responsible for decision relating to senior executive management in accordance with national corporate governance structures.

Furthermore, and in light of the ongoing work on the revision of the Shareholders' Rights Directive, this paragraph should recognize and apply competences of shareholders with regard to approving remuneration policy of employees.

<u>Paragraph 23</u>
It is not the role of the remuneration policy to determine the role descriptions.

<u>Paragraph 25</u>
This paragraph requires that the board (where a remuneration committee has not been established) should oversee the remuneration of the senior officers in the independent control functions "including" the risk and compliance function. This exceeds the requirement in article 92.2 f) of the CRD IV, which only includes the senior officers, not all control functions.

Paragraph 28

It should be clarified that it is sufficient that the risk management function provides an analysis of the risk adjustment data to the remuneration committee and participates on an ad hoc basis, if and to the extent deemed necessary, in the remuneration committee meetings.

Paragraph 29

This paragraph requires the compliance function to analyse how the remuneration policy affects the institution's compliance with legislation, regulations, internal policies and risk culture. This added responsibility suggested by the EBA is neither in line with the requirements laid down in CRD IV (Article 92.2 d) nor practicably enforceable. It should suffice that the implementation of the remuneration policy is annually subject to central and independent internal review for compliance with policies and procedures for remuneration adopted by the management body in its supervisory function.

Paragraph 36

Sub-paragraph "a." could be problematic as it will require subsidiaries established outside of the EEA to adopt and apply a cap on variable remuneration. Such cap could be in breach or contradict local remuneration regulations. For instance in Russia, the Russian Central Bank requires variable remuneration to represent a minimum 40% of total remuneration. The Russian Central Bank´s approach is the opposite of the EU/EEA´s approach, and aims at ensuring that Russian banks maintain their cost base flexibility.

Paragraph 37

This paragraph requires that the institutions should notify to the competent authority at the latest five working days after notice to shareholders that an approval of the higher ratio will be sought. This requirement should consider national legislation which transposes CRD IV. Therefore, the number of working days needed to notify the competent authority regarding the recommendation made to shareholders of the proposed maximum ratio, should be kept under national legislation or in other case, extended. We consider that a reasonable number of days should be considered at the least thirty working days.

Paragraph 38

With regard to sub-paragraph "c.", the EBF considers that a statement from the institution to the competent authority confirming that the higher ratio does not conflict with the obligations under the CRD and the CRR, should be sufficient.

Paragraph 39

This paragraph requires that all significant institutions at individual, parent company and group level must establish a remuneration committee. It should, having regard to the proportionality principle, be sufficient to establish a remuneration committee on group-level. This particularly where the institution's business operations are organized on a pan-group basis along functional lines rather than by legal entity.

The requirement should also take into consideration existing national legislations, which sometimes goes counter to this obligation.

Paragraph 42
This paragraph requires that "[t]he chair and the majority of members of the remuneration committee should qualify as independent." This requirement goes beyond the requirement of Article 95.2 of the CRD IV, which is not appropriate.

Furthermore, while the paragraph clarifies that the 'independence' should be understood as set out in point 5.6 of the EBA guidelines on internal governance, it should also consider definitions of 'independence' contained in legislation implementing CRD IV into national legal orders.

Paragraph 44
With regard to sub-paragraph "a.", the remuneration committee is responsible for the oversight of the remuneration policy but should not be responsible for the review of each individual identified staff members´ compensation. The EBA´s suggested added responsibility goes far beyond what is set out in Article 95 (2) of CRD IV and if implemented would entail a substantially increased workload and would divert the remuneration committee´s time and attention from its main duties and responsibility.

Paragraph 49
This paragraph requires that a member of the risk committee should participate in the meetings of the remuneration committee and vice versa. Since the management body in its supervisory function (i.e., the members of the board of directors) is represented both in the risk committee and in the remuneration committee – the management body in its supervisory function is already represented in both committees and thus informed of the matters dealt with within those. Any co-ordination between these two committees can and should be dealt with by the management body in its supervisory function following national corporate governance procedures. This requirement is not proportionate to its aim.

The EBA should also elaborate on the responsibility of the member(s) of one committee that participate in the other committee's meetings. Is it the EBA's positon that e.g. a remuneration committee member should be responsible for all decisions made in relation to all such issues and questions that may be dealt with within the risk committee?

Paragraph 51
It should be possible for the institutions to engage an external auditor to review the compliance with the regulation.

Q 4: Are the guidelines regarding remuneration policies and group context appropriate and sufficiently clear?

7. Remuneration policies and group context

Paragraph 60
The EBF requests EBA to evaluate, in order to guarantee a fair competitiveness, the exclusion from the consolidation parameter of companies located in third countries in which banking institutions are not obliged to respect regulations similar to CRD IV.

European Banking Federation

Paragraph 63 (and 4)

According to this paragraph "*the consolidating institution must ensure that subsidiaries within the group which are not themselves subject to the CRD, apply the group-wide remuneration policies to all staff*" and that this "*also applies to specific requirements of CRD, which have not been included in other sectorial legislation (e.g. staff within entities that fall within the scope of the AIFMD and UCITS Directive and are part of a group have to comply with the limitation of the variable components of remuneration to 100 % (if applicable, up to 200 % with shareholders' approval) of the fixed components of remuneration if their professional activities have a material impact on the group's risk profile on a consolidated basis).*"

It should firstly be noted that the application of the CRD IV specific risk alignment remuneration requirements should be implemented and applied within each institution *in a manner* and *to the extent* that is *appropriate* to their size, internal organisation and the nature, scope and complexity of their activities (article 92 and 94 of CRD IV). It should secondly be noted that the legislative intention is to allow the disapplication of certain CRD IV specific risk alignment remuneration requirements (recital 66 of CRD IV states: "*/…/ it would not be proportionate to require certain types of investment firms to comply with all of those provisions [referring to the remuneration provisions of CRD IV]*"). It should thirdly be noted that the European Parliament and Council did not deem it necessary to introduce a cap on variable remuneration in the AIFMD or UCITS Directive or Solvency Directive.

Having regard to the CRD IV remuneration requirements only being applicable *to the extent appropriate*, it would not seem proportionate to require an AIFM or UCITS asset manager or insurance provider, which is not itself subject to CRD IV, to observe the CRD IV specific cap on variable remuneration merely due to being part of a consolidating group, as such AIFM and UCITS asset manager and insurance provider will have a competitive disadvantage (due to the application of the cap) compared to non-captive AIFMs and UCITS asset managers and insurance providers. The suggested extension of the cap to captive AIFMs and UCITS asset managers and insurance providers would create an uneven playing-field, contrary to the objectives of the remuneration regulations, spirit of the internal market and article 16 of the EBA founding regulation (1093/2010). EBA's suggested extension of the CRD IV specific risk alignment remuneration requirement is in direct conflict with the legislative intention (cf. recital 66 of CRD IV) and the principle of proportionality (cf. recital 66 and articles 92 and 94 of CRD IV, and article 16 of the EBA founding regulation (1093/2010)). The CRD IV specific risk alignment remuneration requirements, such as the cap on variable remuneration, should therefore not be applicable to any subsidiaries which are governed by specific sectorial legislation. The "*ESMA guidelines on sound remuneration policies under the AIFMD*", which are in line with the legislative intention and principle of proportionality, should prevail.

In summary, the EBF considers that a system of equivalence should be introduced – whereby captive AIFMs or UCITS asset managers which apply the remuneration provisions set out in AIFMD or UCITS V in relation to identified staff under CRD IV, will not be required to also apply the remuneration provisions set out in CRD IV in relation to such staff members. It is the EBF's firm opinion that the AIFMD and UCITS V remuneration regulations are equally as effective as the CRD IV remuneration regulations. There are therefore no reasonable grounds for requiring captive AIFMs or UCITS asset managers to also apply the remuneration provisions contained in

CRD IV in relation to such identified staff. An introduction of a system of equivalence would ensure a level playing field between captive and non-captive AIFMs and UCITS managers.

The EBA should confirm that the term 'institution' used throughout the guidelines only refers to institutions that are directly subject to CRD IV; confirm that the identification of identified staff on solo level only aims at identifying staff members who can materially impact the risk levels on a consolidated basis; confirm that the CRD IV specific risk alignment remuneration requirements apply only in relation to members of staff who are identified as having a material impact on the consolidated basis; confirm that the requirement to apply the CRD IV specific risk alignment remuneration requirements does not apply in relation to variable remuneration awarded for work performed for subsidiaries within institutions which are governed by specific sectorial legislation or any other subsidiaries on a non-consolidated basis.

Q 5: All respondents are welcome to provide their comments on the chapter on proportionality, with particular reference to the change of the approach on 'neutralisations' that was required following the interpretation of the wording of the CRD. In particular institutions that used 'neutralisations' under the previous guidelines for the whole institution or identified staff receiving only a low amount of variable remuneration are asked to provide an estimate of the implementation costs in absolute and relative terms and to point to impediments resulting from their nature, including their legal form, if they were required to apply, for the variable remuneration of identified staff: a) deferral arrangements, b) the pay out in instruments and, c) malus (with respect to the deferred variable remuneration). In addition those institutions are welcome to explain the anticipated changes to the remuneration policy which will need to be made to comply with all requirements. Wherever possible the estimated impact and costs should be quantified, supported by a short explanation of the methodology applied for their estimation and provided separately for the three listed aspects.

Section 8. Proportionality:

General comments on the application of the proportionality principle:

Comparing the remuneration principles set out within CRD III and CRD IV, no substantial changes to the wording are to be found. It could be even argued that CRD IV emphasises the meaning of the proportionality principle more than CRD III. Moreover, within both directives the principle of proportionality is laid down as a core principle forming the basis for the application of the remuneration rules. This is understood and applied in such a way by National Competent Authorities in most of the EU Members States. Accordingly there is no apparent reason for a change in the application approach of proportionality.

Recital 66 of CRD IV states that "*The provisions of this Directive on remuneration should reflect differences between different types of institutions in a proportionate manner, taking into account their size, internal organisation and the nature, scope and complexity of their activities. In particular it would not be proportionate to require certain types of investment firms to comply with all of those principles.*" The clear legislative intention is thus to allow institutions to apply the CRD IV remuneration requirements in a proportionate manner. It is also acknowledged that institutions may dis-apply certain CRD IV remuneration requirements to the extent these are disproportionate. The legislator has not expressed any limitation as to the application of the

proportionality principle, not to any particular remuneration requirements nor to any particular type of institution.

Article 92(2) of CRD IV states that "/…/ *institutions comply with the following principles in a manner and to the extent that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities* /…/". Article 94 of CRD IV "*shall apply in addition to, and under the same conditions as, those set out in Article 92(2*)". This shows that the remuneration requirements are not meant to be implemented in the same way within all institutions. Instead, the remuneration requirements shall be implemented *having regard to* the institution's size, internal organisation and the nature, scope and complexity of its activities. Further, and although all remuneration requirements are applicable, these must only be applied *in a manner* and *to the extent* that is *appropriate.*

The change in approach of EBA to the application of the principle of proportionality is not supported by the legislative intention or wording of CRD IV. Furthermore, the EBA's change in approach would lead to disproportionately high implementation costs and administrative burdens without any benefits. As an example, requiring institutions to defer any and all variable remuneration exceeding EUR 0 does not achieve the objectives of the remuneration regulations but would only lead to a weakened incentive as well as a disproportionate administrative burden. Such interpretation of the CRD IV is not risk driven and does not serve its purpose.

The approach currently chosen by Scandinavian and other EU supervisors is to implement thresholds for the application of the deferral requirement and requirement to award variable remuneration in shares/share-linked instruments. Such thresholds have been set at levels where the variable remuneration is deemed to create an incentive for excessive risk taking and currently range between EUR 15.000 to EUR 100.000, depending on the country. We are of the opinion that it would be beneficial to apply one threshold throughout the EU/EEA, e.g. a threshold of EUR 100 000.

Many institutions currently make use of the possibility to neutralise some of the specific risk alignment requirements in line with national implementation, which does not lead to a circumvention of the CRD IV. Therefore, the possibility of 'neutralisation' of the CRD IV specific risk alignment remuneration requirements should be maintained for all institutions.

The requirements for variable remuneration regarding material risk takers are too complicated and difficult for small institutions that do not have resources for very sophisticated remuneration systems and people dedicated to the issue. On the flip side, the implementation of sophisticated remuneration systems and the full application of the CRD IV provisions would lead to significant costs and will also have consequences on the structure of the remuneration schemes.

Some of the small and less complex institutions that are not limited companies have relied on the regulation in place ("neutralisation") and have not prepared for requirements to pay variable remuneration with instruments. Since they have no shares to use, they would be obligated to rely only on fixed remuneration. This would add costs of the institution. Also in a

bigger picture if the banks cannot compensate their employees properly, it encourages the employees to transfer to other business areas.

It should also be taken into account that in many, in particular, small institutions employees may be owners of the company. In these situations the concept of material risk taker gets easily “too wide” due to low salaries of the owners (who typically count on dividends and growing value of the business, not on salaries). If the neutralisation is taken away from this kind of institutions, they cannot use variable remuneration at all.

If only fixed remuneration can be used, the costs cannot be reduced in an unfavourable market situation. This is specifically difficult for the smaller institutions. Also, if the institution cannot use variable remuneration, it cannot affect the behaviour of its employees by use of remuneration and the good influence of variable remuneration is in full lost.

The EBA has indicated that it understands the implications of its current interpretation of CRD IV and suggests advising the Commission to amend CRD IV so as to allow the application of the proportionality principle (to which reference is clearly made in recital 66 and articles 92 and 94 of CRD IV). Although such clarification in an amended CRD would be helpful, such potential future amended CRD is of little or no comfort for institutions which in the ‘transitional period’ are forced to apply the CRD IV as interpreted by the EBA. **Therefore it would be imperial, that EBA re- interpret the regulatory framework**.

Answer to EBA’s specific questions:

1. Assuming that all institutions have to implement deferral arrangements and pay out of variable remuneration in instruments for all identified staff, how many institutions and how many identified staff would be affected within your member organisations?

<u>Belgium</u>

One bank in Belgium informed us that in case it would need to implement deferral schemes and pay out in instruments for all identified staff, this would mean that for 460 people deferral schemes and instruments have to implemented, whereas now this has been done for 119 people. This is an increase of nearly 400% just for the provisions related to deferral schemes and pay out in instruments.

<u>Finland</u>

In Finland all the banks (and investment companies that are in scope) have used the relief of the threshold EUR 50.000. The meaning of the threshold is specifically important to small savings and cooperative banks who have no natural instrument to use in remuneration, but also bigger limited companies find this threshold very important. In the smaller banks the threshold has made it possible to keep all material risk takers out of the deferral arrangements due to their low variable remuneration awards. For these banks the removal of the thresholds would in practice block the possibility to use variable remuneration in whole. Also in middle-sized banks the percentage of material risk takers may rise up to 900 %, and according to one estimation the removal of the threshold would increase tenfold the costs of the administrative work in such a bank.

European Banking Federation

Luxembourg

Luxembourg is the Europe's largest Investment fund centre and the world's second largest after the United States of America. As of 28 February 2015 (Source: Commission de Surveillance du Secteur Financier), Luxembourg domiciled Investment funds represented more than EUR 3.4 billion in assets under Management. These factual elements emphasize one of the specificities of the Luxembourg Banking Sector where a significant part of credit Institutions are providing services to collective investment vehicles and act as, highly specialized, service providers in that field. In general, the core business of credit Institutions involved in the Investment fund industry is to provide fund administration and depositary/custody services to such collective investment vehicles. These activities, by nature, do not involve excessive risk taking, but rather focus on safekeeping the assets and administering these vehicles, frequently upon exact directions received from clients. Equally, majority of individuals who are servicing Investment funds essentially have fairly limited impact on operational results of the credit Institution. The regulatory environment in which such credit Institutions operate is already highly regulated, embedding strong client protection clauses which discourage risk taking behaviour that could ultimately have adverse consequences on investors and/or the financial system as a whole. The application of remuneration requirements without regard to proportionality principles through a "one-size fits all approach" which would not consider the risk profile, risk appetite and strategy of the credit Institutions and the materiality of the impact the professional activities of each of its staff members poses from a prudential risk perspective, would increase operational costs in a manner which may not be proportionate to the interest to be protected. This observation is of particular relevance for the subdivision of the banking business having as core activity the servicing of Investment funds where rather conservative and stable level of variable remuneration illustrates its uniqueness and the limited influence of the variable component of the remuneration on the respective risk profile of these Institutions

With the above in mind the Luxembourg supervisory authority confirmed the percentage of eligible credit institutions and investment firms to the principle of proportionality in the past year to be as follows:

1. Credit institutions (excluding branches of Community origin)
   ELIGIBLE for the application of the proportionality principle: 64%
   NON- ELIGIBLE: 36%
2. Investment firms
   ELIGIBLE for the application of the proportionality principle: 71%
   NON- ELIGIBLE: 29%

The change in approach to the application of the principle of proportionality would be very significant based on these numbers.

France

One bank informed the EBF that should the CRDIV provisions on remuneration in terms of deferral and payment in instruments apply to all entities, whatever their nature, complexity of activities and location, and to all staff, whatever their level of

remuneration, in addition to the 770 persons already identified (555 at Group level and 215 in 7 EEE countries on a solo basis), 6.000 to 10.000 staff would be affected:

- 3.000 to 4.000 employees in more than 130 consolidated subsidiaries
- 3.000 to 6.000 executive officers in about 3.000 non-consolidated subsidiaries without staff

2. Please quantify, if possible separately, the cost impact in absolute and relative (compared to the institutions' profits) terms for institutions that do not apply yet the CRD remuneration provisions on:
   a. deferral (excluding the setting up for a framework to apply malus);
   b. deferral (including the setting up for a framework to apply malus);
   c. pay out of variable remuneration in instruments;
   d. the setting up of criteria and arrangements for the application of clawback;
   e. deferral and pay out of variable remuneration in instruments for discretionary pension benefits that may be awarded.

Answer: We believe the EBA misses a point in cost impact; the burdensome CRD remuneration provisions force the institutions to employ additional staff for the administration. This cost is left out of the EBA question. Generally an estimation of implementation costs is only possible with high effort but there is no doubt that the costs will be very significant and in no efficient relation to the amount of variable payment especially within small and less complex institutions.

For subsidiaries which are notified internally as subsidiaries falling under the CRD requirements, additional cost will arise, if they have to identify risk takers at a lower level than the members of the management body of these subsidiaries. These additional costs cannot be quantified so far.

Point 2b

This would significantly increase the operational cost and it would have a detrimental influence on the retention of staff and attracting of new staff. The lowest total variable remuneration of an identified staff member is sometimes very low (there are examples of around 1.200 EUR per performance year). It would not make any sense to defer such person's variable remuneration for 3 years. The incentive tool will be lost in relation to such staff members.

Point 2c

The complexity and costs of implementation of deferral schemes and payment of variable remuneration in instruments rather than cash indexed on instruments would be very high, especially if it had to apply to a very large population based in several countries (see question 1. above). These costs would be of different nature:

Governance and external formalities: depending of the nature of shares distributed (ordinary shares through capital increase or buybacks programs; free shares), need for the parent company which grants shares:

- to obtain the authorization from its ordinary or extraordinary general meeting of shareholders

- to manage various formalities vis-à-vis the markets control authorities and the public in several countries
- to make sure from a legal point of view that the transfer of instruments issued by the parent company to subsidiaries is possible in each country

Internal communication towards identified staff: establishment of contractual documentation on deferred variable remuneration and deployment of individual notification process on a much larger basis increasing the administrative burden.

Accounting and tax constraints:
- re-invoicing of the charge corresponding to the amount of variable remuneration paid in instruments is complex to put in place in all affected subsidiaries
- follow-up on an individual basis of the tax obligations of all beneficiaries of instruments is complicated, especially when taking into account the geographical moves of the employees

IT and HR costs and operational complexity:
- costs linked to the evolution of IT remuneration tools to integrate functionalities for deferral and pay-out in instruments on variable part
- costs related to the increase of HR staff worldwide to manage the application of deferral and pay-out in instruments to a much wider MRTs population
- costs linked to (i) the enlargement of the service contract with the securities intermediary in charge of the management of the distribution of shares and (ii) the opening of deposit accounts for all identified staff, with potentially some restrictions in some countries
- costs related to the management of the withholding of social charges and income taxes on the employees bank accounts for the parts of variable remuneration paid in instruments (cash not always available to fund these charges and taxes)

One bank informed the EBF that at this stage it is difficult to provide an exhaustive and precise estimate of costs. The sole costs linked to the evolution of IT tools would amount to circa 2 M€.

Another bank informed the EBF that if it were obliged to install the pay out in instruments for all identified staff, this would double its cost at least.

An estimation of another bank sets the extra costs at 1.5 million EUR, not taking into account the operational cost.

Point 2d

This would significantly increase the operational costs and it would have a detrimental effect on the retention of staff and make it more difficult to attract new staff.

Furthermore, please note that clawbacks cannot be applied under labour law of some of the EU member states.

Point 2e

In some countries, for instance Belgium, it is not possible to award discretionary pension benefits.

3. Do you anticipate any indirect impact of the application of those provisions, for instance changes in the remuneration structure, the risk profile of institutions, the risk assumption by staff or the ability to attract new staff?

Answer: The direct impact of the CRD remuneration provisions can be seen in at least the following areas:

A) The main risk identified is the non-compliance risk, as the regulatory constraints on banks would be reinforced, whereas they do not necessarily have the material means to put in place the structures or controls required to monitor the application of such constraints in the absence of adapted IT tools.

B) In many jurisdictions, variable remuneration forms an important remuneration component across various business sectors. The inevitable consequence of the EBA´s draft guidelines is a shift towards fixed remuneration in the financial sector. Compared to other non-regulated sectors in which variable remuneration can be freely offered, awarded and paid, the financial sector will become less attractive to new staff, especially where there is a shortage of qualified personnel (HR, auditors, compliance and IT).

These less attractive profiles are more of an issue for smaller banks that already start with a handicap in recruiting staff due to the fact that they can offer less career opportunities and financial remuneration. When the financial sector becomes less attractive to work in, small banks might encounter recruiting problems faster than larger banks – however, high performing and highly qualified HR, internal audit and IT professionals are likely to choose a career within more fruitful business sectors.

C) The tension between the CRD rules and the guidelines of CEBS/EBA also exists inside each country. In implementing new legislation a certain balance was achieved to allow proportionality as long as the variable remuneration was limited (threshold). For instance Belgian banking legislation 2014 allowed explicitly that banks' remuneration policy could take into account their size, internal organisation, nature and complexity of activities. Thus the general principles were legally seen as "principles" by the Belgian legislator and that the CRD III remuneration provisions under the control of the National Bank - could be implemented in a way that was adapted to the reality of banks.

D) Not all banks have tradable shares, for instance in the Netherlands banks have shares that are owned by Dutch public sector institutions. These banks often have tradable bonds, but due to internal rules employees are not allowed to trade in bonds of their organization since it is considered not to be manageable. Creating new non-financial instruments would, if possible at all, place a huge financial and operational burden on these banks.

Moreover, this is an issue for banks with a cooperative structure, or where large parts of the shares are held by a few families, or a holding structure. Even when the shareholders of these banks would be open for this kind of participation, including listed companies, the costs to implement that - with the only reason to allow a variable remuneration - are prohibitive.

In addition, small banking subsidiaries of wider non-banking groups which are currently subject to group-wide remuneration policies, practices and related resources will encounter particular difficulties in implementing policy requirements that are inconsistent with the non-banking group.

In practice: many banks will have to abolish variable remuneration (in fact some banks already have decided to cease the use of variable remuneration and to only pay fixed remuneration). The variable remuneration will become a part of the fixed remuneration to maintain a remuneration level that is comparable to the total remuneration offered on the financial market. This will inevitably have negative consequences on the bank´s possibility of maintaining flexibility in connection with a potential future market downturn and will counter the objectives of CRD IV.

4. Which legal or other impediments exist for the use of instruments for the pay out of variable remuneration and what would be the simplest non-cash instrument that could be used for that purpose?

There exist legal/regulatory impediments to use instruments in some big countries:

- Russia where the local markets control authority does not authorize Russian people to hold shares which are not listed on the Russian stock exchange
- The US where maximum 5 M$ of all remuneration paid to the whole staff employed locally can be attributed in shares issued by a parent company not listed on the US stock exchange. This cap, which includes all types of remuneration in shares (profit-sharing; company savings plan; employee share ownership; free shares; variable remuneration), can be quickly exceeded.

There could be also other major obstacles in several countries:

- In terms of governance, the grant of shares to identified staff could be refused by the general meeting of shareholders, who have to provide their authorization on such operation, or capped at a lower amount than that required
- Due to tax risks, the payment in instruments would not be possible in countries, where the corresponding charge is not tax deductible
- For confidentiality reasons, in countries where a very limited number of employees are identified, it would not be possible to implement payment in instruments, since the re-invoicing of corresponding variable remuneration amounts would not be feasible

For savings and cooperative banks that have no natural instruments to use, the costs for buying some kind of regime from a third party is expected to be very high compared to the sums used in remuneration (and the fact that this would be required by

legislation would raise the prices even further). According to one estimation the costs for this kind of arrangement could add total salary costs for 10-20 %. The EBA should consider that any increase in cost, will affect the end consumer.

The EBF considers that the most efficient instruments without any legal impediments are share linked instruments and that it should be possible for all institutions (whether or not listed) to choose to use these instruments instead of shares. See Q16 of the consultation for the impediments.

5. Do you foresee an impact on the competition between small non-complex institutions and large complex institutions, if the small and complex institutions would have to apply the same remuneration principles?

Yes, attracting new staff in the financial industry today is much more difficult due to the application of the CRD IV remuneration provisions. Therefore, we would appreciate the creation of a more level playing field for all competitors, not merely in the financial sector. From the EBF's point of view this situation needs to be improved as soon as possible as the fluctuation in this areas rises since other industries are currently not subject to any regulation.

It will become more difficult for institutions to attract highly qualified staff members and to stimulate those staff members. Variable remuneration constitutes a means to reward high performing staff members, not to incentivise staff members to take excessive risks.

6. If specific exemptions were suggested, which remuneration provisions should be within the scope of exemption and which criteria for their non-application should be set? What should be the level of application of such exemptions (i.e. the whole institution, certain identified staff, e.g. based on their variable remuneration)?

Answer: The CRD IV remuneration provisions are complex and a simplification of the provisions is needed. The existing provisions force institutions to identify a disproportionately large number of staff as identified staff and then to rule them out due to not having a material impact on the institution's risks. Therefore, we strongly ask for the following specific exemptions or neutralization possibilities:

- neutralization of subsidiaries, which are non-CRD institutions and which do not offer any essential services for the consolidating institution (the same shall apply for subsidiaries which are not in the consolidating situation)
- general neutralization of subsidiaries with total assets below EUR 15 billion
- no application of deferral, awards in shares or share-linked instruments and retention for identified staff if the annual variable remuneration does not exceed an amount of 100,000 EUR (= general exemption limit for identified staff within certain member states).

The above suggested exemption or neutralization possibilities would enable smaller banks to remain competitive and larger banks to retain identified staff with small

variable remuneration awards, whilst enabling to capture all identified staff and thus fulfilling the objectives of CRD IV.

Q 6: Are the guidelines on the identification of staff appropriate and sufficiently clear?

Section 9. The identification process:

Paragraph 83

It is coherent to include all subsidiaries for the identification of MRTs on a consolidated basis, but if every single subsidiary within a banking group had to perform the identification of MRTs on a solo basis, this would lead to a tremendous amount of work and be a very heavy operational burden. Therefore, It should be clarified that the identification process only apply to institutions directly subject to CRD IV and not to subsidiaries governed by specific sectorial legislation or other subsidiaries on a non-consolidated basis, as clarified with respect to setting up a remuneration policy in paragraph 39 of the guidelines. The identification of identified staff within non-CRD entities should only aim at identifying staff members who can materially impact the risk levels on a consolidated level.

For instance, if the identification process was extended to all subsidiaries within one of the member institutions, this would lead to identify more than 10 times today's regulated population, almost all coming from retail banking or specialized finance activities with quite low levels of variable remuneration, which does not seem relevant:

- The new draft guidelines introduce new requirements on top of CRDIV rules which go far beyond the rules applicable until now to European Institutions (which themselves go far beyond the FSB principles applied everywhere outside Europe, except for EEA Banks).
- Given their activity, these employees would not have any significant impact on the risk profile. The cancellation of the proportionality principle seems thus in contradiction with the objective of CRDIV to target the staff members who can have a material impact on risks.
- It also comes in contradiction with the proportionality thresholds that have been set by most national regulators/legislators (generally size of total balance sheet).
- It would create high competitive distortion in geographies (countries outside EEE) or businesses (automotive leasing, insurance) which are not subject to CRD. Additionally, some of the investment banking businesses are in branches and would therefore not be impacted by such provisions.
- It would represent a very heavy operational burden.

Since the core objective of the CRD IV remuneration requirements is the counteraction of variable remuneration systems which might encourage an excessive risk taking amongst eligible staff members, the obligation to identify identified staff should only apply where variable remuneration is applied. Institutions in which variable remuneration schemes are not applied, the application of the principle of proportionality should entail an alleviation of the administrative burden for the institutions.

Paragraph 86

The EBA states that: "where institutions use multi-year accrual periods, they should consider the variable remuneration accrued for the preceding period, even if the award will be made only at the end of the performance period." However, splitting multiyear accrual periods into annual accrual periods may not be practicably possible (e.g. where the multiyear performance is subject to average financial criteria or conditions at the end of each vesting period).

Paragraph 93

In terms of delays, presenting all exemption requests might be problematic when reorganizations occur and are effective only end of the first semester of the year. EBA should envisage possible derogations in such contexts.

Globally, the governance for the identification of staff and the exemption process is very heavy and if both the management body and the supervisory board (Art 92. A1 and 97) have to approve the list of identified staff as well as the list of exemptions, the calendar for submitting these requests to the supervisor will be very difficult to respect.

Moreover, the request for prior approval under article 4 (5) of the RTS on identified staff should be made each year. This seems very illogical. The approval should be valid until change of position or in case of significant salary increase – the reasons for applying for an exemption remaining the same and the EBA`s suggested requirement only giving rise to an unnecessary and disproportionate administration burden. In any event, an application every second year should suffice.

Paragraph 97

Regarding this paragraph it is important that the requirements are, or will be, coordinated with the forthcoming revision of the Shareholders´ Right Directive. If the said directive will require that the shareholders shall decide on the remuneration policy, the requirements in the guidelines will be too far-reaching. A remuneration policy is a living document which is or can be updated one or more times per year. It would not be proportionate to require shareholders to meet several times per year to adopt minor detail changes in an institution's remuneration policy.

Q 7: Are the guidelines regarding the capital base appropriate and sufficiently clear?

No comments

Q 8: Are the requirements regarding categories of remuneration appropriate and sufficiently clear?

Section 11. Categories of remuneration:

Paragraph 117

Not even basic fixed salary complies with all the conditions under article 117. Indeed fixed salary can be reviewed upwards even if the staff member does not change position, and the amount is not only changed via collective bargaining. Many jurisdictions apply individual wage

setting and have annual salary reviews in connection with which the individual employee´s performance over the past year will be of a decisive impact. Moreover in some jurisdictions, fixed salary can be reduced upon the employer's sole decision, even if there is no change in the role or responsibilities of the staff member. Based on the EBA´s suggested criteria all remuneration including "fixed base salary" will be deemed "variable" for the purpose of the EBA guidelines. This is hardly the intention.

Paragraph 118

According to the currently applicable CEBS guidelines, ancillary payments which "*are part of a general, non-discretionary, institution-wide policy and pose no incentive effects in terms of risk assumption*" can be waived under the definition of variable remuneration for the purposes of the CRD III specific requirements on variable remuneration (such as performance conditions and deferral).

EBA, however; splits all remuneration into either fixed or variable remuneration. There is, according to the EBA, no such remuneration as 'ancillary payments'. In paragraph 118, the EBA introduces an additional criteria in order to define 'ancillary payments' as fixed remuneration, namely that these 'ancillary payments' do "*not depend on performance*". It should be clarified whether or not this additional criteria presented relates to individual performance, and thus aims at preventing unwanted risk behaviour, or aims at capturing all forms of performance including *for example* RAROCAR, RAROC or ROE on institution/group level, and thus merely aims at punishing employees within the CRD IV institutions.

An institution-wide profit sharing scheme which is generally applicable, non-discretionary and thus part of routine employment packages, and which for example is based on the institution's/group's RAROCAR or ROE and thus poses no incentive effects in terms of risk assumption – should continue to be excluded from the CRD IV specific risk alignment remuneration requirements, and thus be defined as 'fixed remuneration'.

Regarding mandatory severance payments for termination of an employment contract under national law should be excluded from this guidelines, but if such argument is not convenient, we would suggest to consider them as fixed remuneration because they comply with the conditions set up in paragraph 117: they are predetermined, permanent, not discretionary, transparent to staff, non-revocable, cannot be suspended or cancelled by the institution and do not provide incentives for risk assumption.

Paragraph 120

The modification of the integration modalities of the long term incentives is very problematic:

- It would not be possible to be sure to respect the ratio as the variable remuneration is decided in February and paid in March while the LTIs' value is based on the share price end of March.
- As it would lead to uncertainty for the respect of the ratio, these type of instruments might be abandoned. This would be in contradiction with the regulation which highly recommends long term remuneration. Therefore, and in the context of the cap, long term incentive plans should be valued at grant.

Q 9: Are the requirements regarding allowances appropriate and sufficiently clear?

12.1 Allowances

The EBA should clarify the meaning of "comparable situation". Does "comparable situation" within the guidelines have the same meaning as in *for instance* discrimination legislation?

It should be noted that a "role based allowance" is individual and depends on the staff member's underlying employment agreement and base salary. The "role based allowance" is awarded in exchange of the employee performing certain duties within or in addition to the ones described in the employment contract or for taking on additional responsibilities. "Role based allowance" is also commonly used in member states or institutions with defined benefit pension systems as an increase in base salary is very costly due to payment of past service costs.

It should also be noted that role based allowances are used throughout the European labour market and that these have been applied long before the CRD remuneration regulations entered into force. Role based allowances are thus not new remuneration components designed to avoid the application of CRD IV remuneration requirements. Furthermore role based allowances do not provide an incentive to risk taking.

Paragraph 124

The requirements in paragraph 124, sections (a) and (b), are appropriate but not the requirement in section (c) which requires that "*any other staff member fulfilling the same role or having the same organisational responsibility and who is in a comparable situation would be entitled to a comparable allowance*" as this will limit the flexibility in agreeing individual remuneration packages as well as limit the possibility for changing the remuneration structure within institutions. As the current practice shows not all employees with the same role have the same fixed income. The amount of the fixed income (and therefore also the amount for the allowances) depends on seniority, responsibilities, experience etc.

Q 10: Are the requirements on the retention bonus appropriate a sufficiently clear?

Section 12.2. Retention bonuses:

To the extent 'retention bonuses' are not performance related – for example only subject to that employees stay within the institution within a specific period – they should be considered as fixed remuneration.

The EBF further supports the use of retention bonuses – which are performance related – in connection with restructurings, in wind downs and change of control, as well as in connection with other situations in which the institutions can provide a rationale for its legitimate interest in not only retaining relevant staff members but also ensuring that these staff members perform satisfactorily during this time.

Paragraph 126

Retention bonuses are qualified as variable pay and as relates to identified staff subject to the same deferral periods and criteria of variable remuneration. As retention payments are generally in place to be paid at the end of a project or a wind down situation, it does not make sense to obligate a deferral in these situations. On the contrary, in some cases this would increase the risk of the identified staff resigning from the institution.

Paragraph 127

Since retention bonuses are awarded in specific situations such as restructurings and wind down scenarios, it would not be appropriate to require all provisions regarding pay out and ex post risk alignment to have to be complied with (as relates to identified staff). The EBA should clarify the status of schemes agreed before these rules came into force.

Section 12.3. Discretionary pension benefits:

The EBF considers that the EBA should provide clarification of what constitutes discretionary pension benefits. It should in this context be noted that not all legal system allow retention periods on pension benefits.

Section 13.1 Guaranteed variable remuneration

Paragraph 137

The EBA should confirm that "*awarded /…/ before the first performance period starts*" includes agreements entered into with the staff members before they commence their employments. The EBA should also confirm that such awards can vest pro rata.

Paragraph 139

It should be clarified that buy-outs are excluded from the ratio between variable and fixed remuneration, as they were already considered variable compensation in the previous institution.

Q 11: Are the provisions regarding severance payments appropriate and sufficiently clear?

Section 13.2. Severance pay

The EBA should clarify whether or not post-employment non-competition compensation is deemed to be included by the definition of severance payment as well as other post-employment compensation based on national labour law practices.

The EBA should also elaborate on how to risk-adjust severance payments that are made under a full and final settlement agreement in exchange of the staff member´s waiver of any and all claims against the institution.

In most member states, the unilateral dismissal of an employee requires just cause. What constitutes just cause is often set out in mandatory statute and ultimately decided by the tribunals or courts on a case-by-case basis. The starting point thus being that it is fairly difficult for institutions to dismiss staff members and that institutions will be at risk of having claims

raised against them when executing dismissals (this, regardless of the underlying reasons for the dismissals). In many member states, tribunals or courts may re-instate unjustly dismissed staff members or order the institution to pay the staff member damages. Such damages can be substantial. Add to that, full salary and benefits during the legal proceedings. Consequently, institutions will have an incentive to enter into full and final settlement agreements under which staff members are paid severance in exchange of their waiver of any and all claims against the institution.

In certain member states institutions entering into settlements would risk being in breach of the CRD IV remuneration requirements. As an example, the worst case cost pursuant to the Swedish Employment Protection Act in connection with an unjust termination with notice amounts to (1) full salary and benefits during the notice period (up to 12 months), and (2) full salary and benefits throughout the legal proceedings (which can take up to two (2) years in the first instance and thereafter be appealed), and (3) up to 32 months' base salary in financial damages, and (4) general damages of approximately SEK100,000. Add to that, (5) legal costs. Generally parties reach a full and final settlement at the notice payment and 50 per cent of the financial damages. An employer who enters into a full and final settlement will significantly reduce its costs. Nevertheless, where the employer is a CRD institution and where the settlement entails the payment of a severance above the cap on variable remuneration, the institution would be in breach of the CRD IV remuneration requirements.

Furthermore, if severance is included in the calculation of the variable remuneration cap, and where the staff member participates in a variable remuneration scheme under which the staff member is eligible for a variable remuneration equal to 100 per cent of the staff member's fixed remuneration – the institute would be prevented from awarding said variable remuneration at which the institution would be at risk of having legal proceedings initiated against it for breach of contract.

Many member states also exempt certain senior managerial employees from the protection of mandatory employment legislation. Thereby entitling employers to terminate senior managers at will. However, instead of enjoying mandatory employment law protection such senior managers will often be entitled to *inter alia* contractual severance pay. Such severance payments are often subject to good/bad leaver provisions and thus not intended to reward failure but rather to provide a level of protection in case of termination. Contractual severance payments are commonly used within all industries. The amount of severance paid generally range between three (3) to twelve (12) months' salary. If institutions within the financial sector are prevented from offering similar contractual severance payments, the financial sector will not be competing for the most talented employees on the same terms as non-regulated industries. It should also be noted that there are limitations as to the amount of severance payable *for instance* in corporate governance codes applicable to listed companies.

Moreover, according to common practice and settled case law in certain EU members states, notably in Spain, preretirement agreements by virtue of which a staff member ceases to be actively employed by the institution until his retirement, and during a certain period of time the institution pays that staff member an annual compensation and often additional benefits, imply the early termination of an employment contract. This type of agreements are commonly carried out in the banking sector to avoid collective restructuring proceedings and layoffs,

ensuring that no traumatic measures are undertaken by the institution if there is a need to downsize the staff. The conditions of preretirement agreements are agreed collectively with trade unions, after negotiation and consultation proceedings. We believe that the EBA should clearly exclude this type of compensation from the guidelines as it is not "per se" a variable remuneration or a severance pay due to an early termination of the contract because the parties involved are still governed by a preretirement agreement with different obligations in force. Alternatively, these compensations should be considered as fixed remuneration because they are predetermined, permanent, not discretionary, non-revocable, cannot be reduced, suspended or cancelled by the institution, do not depend on performance and do not provide incentives for risk assumption.

Having regard to the above, the EBA should clarify that the EBA remuneration guidelines as relates to severance in particular is without prejudice to national employment law practices. The EBA should also clarify that severance payments made in accordance with local labour law practices are deemed as fixed remuneration for the purpose of CRD IV. The requirement to obtain legal opinions as to any full and final settlements entered into should be removed.

The EBA should also clarify that any new requirements pursuant to the EBA guidelines do not apply retroactively in relation to existing contracts and agreements. Institutions should not be obliged to re-negotiate any employment contracts or agreements entered into with its current staff members.

Paragraph 144

We would appreciate greater clarity around this statement and examples on what types of payments are meant to be included under severance.

Paragraph 148

The amount of severance payments is based on local legislation and case law it is therefore not possible to determine the maximum amount that can be awarded as severance pay. Moreover, this is impossible for group-wide policies, since every national labour law should then be included. This makes the policy extremely long and cluttered.

Q 12: Are the provisions on personal hedging and circumvention appropriate and sufficiently clear?

Section 13.3 Personal hedging:

Paragraph 159

This paragraph states that an employee's "*mere declaration of self-commitment /…/ that he or she will refrain from concluding personal hedging strategies or insurances for the purpose of undermining the risk alignment effects is not sufficient to comply with the hedging prohibition. Institutions human resources or internal control functions should perform at least spot-check inspections of the compliance with this declaration. Random checks should, in all cases, include the internal custodianship accounts of identified staff. Furthermore, notification of any custodial accounts outside the institution should also be made mandatory.*"

Individual staff members, as well as other individuals, are subject to banking privacy. It is consequently not possible for an institution to check the accuracy of information provided by a staff member or to access any staff member's accounts without the individual staff member's consent. Nor are individual staff members bound to abide by the EBA guidelines. It will consequently not be possible for institutions to verify the accuracy of the information provided by individual staff members, other than where the staff member is deemed an insider trader.

The EBA should avoid including requirements in the EBA guidelines which cannot be practically complied with.

Having regard to the above, an individual employee's self-commitment should be considered sufficient.

Section 14. Remuneration of specific functions:

Paragraph 168
The EBA should clarify whether the prohibition against paying variable remuneration to members of the management board in its supervisory function also encompasses variable remuneration awarded staff members, who are members of said board, for work performed in their employment (e.g. employee representatives).

It should be further clarified that, where a person undertaking an "identified staff" role, including the role of Director, is employed by another group entity in a third (non-EU) country, and is not remunerated for the Director role but rather for a non-EU group role, the CRD requirements should not be considered applicable on that staff members remuneration.

Q 13: Are the requirements on remuneration policies in section 15 appropriate and sufficiently clear?

Section 15. Remuneration policy

Paragraph 174
We do not see the reason why the pay-out of the fixed remuneration in another way than cash should be reasoned and approved. In various countries the payment in non-cash (e.g. lease cars, gym membership and lunch vouchers) is a common practice throughout various business sectors.

Paragraph 181
It is not clear what is meant with the formulation 'in a sufficiently granular way'.

Q 13: Are the requirements on the risk alignment process appropriate and sufficiently clear?

Section 16. Risk alignment process

Paragraph 188

It should be clarified what "at all stages" relates to as well as whether or not the absolute and relative criteria should be applied on all levels (individual, business unit and/or institution. Also refer to the comments made under paragraph 198 below.

Paragraph 189

The paragraph includes too many detailed requirements. The institutions should be allowed to implement the risk alignment process in a practical way, having regard to the proportionality principle. Also refer to the comments made under paragraph 198 below.

Paragraph 198

This paragraph states that institutions should set and document both, quantitative and qualitative, including financial and non-financial performance criteria for not only individuals, but also for business units and the institution. This statement should be read in conjunction with paragraph 188, which states that "*Within the risk alignment process an appropriate combination of quantitative and qualitative criteria in the form of absolute and relative criteria should be used at all stages to ensure that all risks, performance and necessary risk adjustments are reflected. Absolute performance measures should be set by the institution on the basis of its own strategy, including its risk profile and risk appetite. Relative performance measures should be set to compare performance with peers, either 'internal' peers (i.e. within the organisation) or 'external' (i.e. similar institutions). Quantitative and qualitative criteria and the applied processes should be transparent and as much as possible pre-defined. Both quantitative and qualitative criteria may partly rely on judgment.*"

The EBA guidelines are "guidelines" and should not regulate in detail how institutions should implement CRD IV. Instead, institutions should be allowed to implement the remuneration requirements, including the performance targets for variable remuneration with regard to the institution's business strategy and goals. An institution should not be required to design artificial performance targets and criteria which do not aim to achieve the institution's business strategies or goals solely for the purposes of complying with the remuneration requirements. Such requirement would not be in line with the proportionality principle as set out in recital 66 and articles 92 and 94 of CRD IV. Qualitative and quantitative performance criteria should not be required on all levels (individual, business unit and institution), but rather on the levels where appropriate considering the internal organization, business unit and individual position/role concerned. Most importantly, Institutions should not be required to apply relative criteria, as relative criteria may encourage excessive risk taking – there being an incentive to outperform peers. Also, it is very difficult, next to impossible, to establish trustworthy external relative criteria. The handling and evaluation of external data is also cumbersome and risks postponing the performance assessment - thereby jeopardising the requirements on disclosure as relates to respect of disclosure deadlines.

Paragraph 206

Criteria used for internal control functions' should be allowed to be based on the objectives of the institution (vs. relevant business unit), as for instance stated in the Finnish Credit Institution Law.

The EBA should also elaborate on the rationale for requiring institutions to set a lower ratio between variable and fixed remuneration components for control functions.

Paragraph 208
Some banks do not see the need for establishing bonus pools as they only award higher amounts of variable remuneration to identified staff. It should therefore be up to each institution to decide whether or not to establish bonus pools having regard to amongst other its internal organisation policy.

Paragraph 209
We would appreciate it if the EBA could clarify whether the requirement to award remuneration after the end of the accrual period applies for all staff or only identified staff? For instance does this preclude the awarding of extraordinary variable remuneration to non-identified staff at the completion of projects in the middle of a performance year?

Paragraph 219
It is not clear how to calculate the bonus pool based on the bottom-up approach. The EBA is therefore requested to further elaborate on this. For instance does this require the calculation of the maximum ratio for every individual and count everything together? Does this only apply for identified staff or all staff?

Q 15: Are the provisions on deferral appropriate and sufficiently clear?

Section 17.2. Deferral period and proportion of deferred remuneration:

Paragraph 236
This paragraph requires significant institutions to apply deferral periods for at least five years. This is an excess of the requirement according to CRD IV (article 94.1.m) where a period of three to five years is stated. The deferral period should be aligned with the nature of the business, its risks and the activities of the relevant identified staff. Further, a requirement to defer variable remuneration over a period of five years regardless of the size of the variable remuneration will dilute the payment too much.

Paragraph 238
It is not clear what the EBA means by a "particular high amount". The EBA´s draft guidelines as well as the RTS on risk takers, contain many clear thresholds. Such thresholds ensure a coherent application of the regulations across the EU/EEA member states and also for banking groups having operations in several jurisdictions. We would therefore appreciate it if the EBA could also set a clear threshold for what constitute a particularly high amount.

Q 16: Are the provisions on the award of variable remuneration in instruments appropriate and sufficiently clear? Listed institutions are asked to provide an estimate of the impact and costs that would be created due to the requirement that under Article 94(1)(l)(i) CRD only shares (and no share linked instruments) should be used in parallel, where possible, to instruments as set out

in the RTS on instruments. Wherever possible the estimated impact and costs should be quantified and supported by a short explanation of the methodology applied for their estimation.

Section 17.4. Award of variable remuneration in instruments:

Paragraph 248(a)
According to this paragraph "*The availability of instruments under Art 94(l)(i) of the CRD depends on the legal form of an institution: a. Shares, for institutions in the legal form of a stock corporation; /…/; listed stock corporations must not use share linked instruments in line with the above mentioned article.*"

Furthermore, it should be noted that the wording in relation to award of variable remuneration in shares in CRD IV is identical to that of CRD III.

According to article 94.1(l) of CRD IV "*/…/ a substantial portion, and in any event at least 50 %, of any variable remuneration shall consist of a balance of the following: shares or equivalent ownership interests, subject to the legal structure of the institution concerned or share- linked instruments or equivalent non-cash instruments, in the case of a non-listed institution; /…/*". Based on this wording in isolation, it can be argued that only non-listed stock corporations are entitled to use share-linked and non-cash instruments. However, the wording can also be read as allowing listed stock corporations to also award share-linked instruments, but not equivalent non-cash instruments. This latter reading is how CEBS interpreted the identical wording included in Annex I of CRD III (refer to paragraphs 124 and 125 of CEBS guidelines on sound remuneration practices). CEBS reading and interpretation was based on recital (7) of CRD III ("*/…/ To align incentives further, a substantial portion of variable remuneration of all staff members covered by those requirements should consist of shares, share-linked instruments of the credit institution or investment firm, subject to the legal structure of the credit institution or investment firm concerned or, in the case of a non-listed credit institution or investment firm, other equivalent non-cash instruments /…/*") and recital (9) of CRD III ("*/…/ Moreover, a substantial portion of the variable remuneration component should consist of shares, share-linked instruments of the credit institution or investment firm, subject to the legal structure of the credit institution or investment firm concerned or, in the case of a non-listed credit institution or investment firm, other equivalent non-cash instruments /…/*"). It should be noted that CRD IV does not contain any wording which supports a change in application or interpretation of the principle on award in shares or share-linked instruments. The wording of CRD IV should therefore be given the same interpretation as the identical wording in CRD III.

Having regard to the above, the underlying reason for requiring institutions to award part of the variable remuneration as shares or share-linked instruments is to encourage long term incentives. Such long term incentives can be achieved by using share-linked instruments. Considering this – and the fact that implementing a share based remuneration scheme is very cumbersome (*inter alia* requiring another financial company to support the issue of the shares, conversion from C-shares to ordinary shares, internal processes to monitor the holding of shares, complicated accounting rules, etc. as further elaborated on below) and requires qualified majority, in some member states up to 9/10 majority, at the annual general meeting – there is no objectively justifiable reason to exclude listed stock corporations from using share-linked instruments instead of shares.

European Banking Federation

It should in this context be noted that the proportionality principle as expressed in recital 66 and articles 92 and 94 of CRD IV applies in relation to all CRD IV remuneration requirements without distinction. All institutions, regardless of their legal form, should therefore be entitled to use share-linked instruments.

Implementing a share based remuneration scheme is very cumbersome:

- From an operational standpoint (IT; HR; governance; accounting and tax; external and internal communication), the distribution of shares is very complicated and costly.
- In some countries there are even legal/regulatory impediments to use instruments (if the company is not listed in the country, the employees cannot receive shares: Russia, US).
- There could be also other major obstacles in several countries:
  - In terms of governance, the grant of shares to identified staff could be refused by the general meeting of shareholders, who have to provide their authorization on such operation, or capped at a lower amount than that required.
  - Since the shares are issued at Group level, the charge corresponding to the amount of variable remuneration paid in such shares should be re-invoiced to each entity. In some countries, where the corresponding charge is not tax deductible, the payment in shares would not be possible, due to tax risks.
  - For confidentiality reasons, in countries where a very limited number of employees are identified, it would not possible to implement payment in instruments, since the re-invoicing of corresponding variable remuneration amounts is not feasible.

The use of e.g. share linked instruments is easier and less costly to put in place, whereas it contributes in the same way as an award in shares in terms of risk alignment.

Paragraph 255

The EBA should elaborate on the reasons for introducing a prohibition on paying interest and dividends on deferred amounts.

It should be noted that shares in institutions where dividends are not paid increase in value. Shares in institutions in which dividends are paid do not experience the same increase in value. The EBA allows retained shares and instruments to be adjusted for dividends in the retention period. Consequently, the EBA should allow employees in institutions where dividends are paid to adjust shares or share-linked instruments at the end of the deferral period.

Introducing a prohibition against paying out dividends will give senior management a strong incentive to suggest capital preservation as opposed to payment of dividends. This may seem in line with the objectives of the CRD IV, however; this will give rise to a negative influence on free dividend policy, create a conflict of interest in the corporate governance structure and lead to buy-back of shares in order to enhance the value of shares at end of deferral. A prohibition on payment of interest or dividends on deferred amounts will also significantly lower the perceived value of deferred amounts amongst staff identified as identified staff and thereby put an pressure on the fixed remuneration.

Neither interest rates nor dividends are decided based on individual performance or unwanted risk behaviour. The reason for introducing this prohibition therefore seems purely punitive. This is not at least the case if the company pays extraordinary dividends.

Furthermore, according to company law in some Member States, it is not possible to separate dividends from the shares.

Q 17: Are the requirements regarding the retention policy appropriate and sufficiently clear?

Section 17.6. Retention policy

Paragraph 263

In the guidelines the minimum retention period is set at 12 months. Most locally implemented regulations currently require a minimum 6 month retention period. A 6 month retention period fully aligns incentives with prudent risk management without giving rise to unwanted negative tax consequences.

Retaining shares over a period of 12 months will give rise to unnecessary negative tax implication which are not proportionate to the aim and which in fact may counter the objectives of the remuneration regulations. Such negative effects could be avoided if identified staff were allowed to divest part of their retained shares in order to cover any taxes levied before the end of the retention periods. This practice has been previously approved by the EBA and should therefore not give rise to any objections.

An alternative to a pro-longed retention period could be to postpone the vesting of the shares (in effect pro-longing the deferral period), thereby avoiding negative tax consequences. There does not seem to be any particular reason why such alternative could not be allowed. This particularly considering that a pro-longed vesting allows institutions to apply malus provisions and forfeit shares/share-linked instruments (a right which in many cases cannot be exercised during the retention period due to national labour and contract law provisions).

If the sole reason for requiring a twelve (12) month retention period is to place staff members at risk of negative tax consequences, the requirement cannot be said to be proportionate to the aim of the remuneration regulations.

We propose that the EBA should introduce a minimum 6 month retention period which can be adapted and extended for some specific populations or instalments, up to each institution.

Paragraph 264

Clarity on the understanding of “large (including significant) and complex institutions” is sought. It is unclear to whom this applies. The EU financial regime already has a clear specification of Significant and Less Significant institutions under the SSM. It would be more helpful to be consistent with this.

Moreover, sub-paragraph “a.” is not clear. Can you please clarify?

Q 18: Are the requirements on the ex post risk adjustments appropriate and sufficiently clear?

Section 17.7. Ex post risk adjustment; malus and clawback

Paragraph 271
In some cases malus (e.g. Poland) and/or claw back is prohibited by national law. How should this be dealt with? If you do have to apply claw back, is this then only the net amount the individual has received or the amount including taxes?

Q 19: Are the requirements in Title V sufficiently clear and appropriate?

No comments

Q 20: Are the requirements in Title VI appropriate and sufficiently clear?

Section 19. Requirements on disclosure

We agree with the EBA's guidelines concerning the requirements on disclosures. Guidelines allow appropriate cross-references to other information and/or disclosures and take into account the size of the institution and the nature, scope and complexity of its activities. All these will reduce administrative burden of institutions.

Paragraph 309
Only the parts of the remuneration policy which are applicable to all staff should be shared. In relation to parts applicable only to a limited number of employees the disclosure should be limited to the persons in scope.

Section 26. Date of application

Institutions should be given reasonable time to incorporate the new remuneration requirements in their organisations and get the necessary approval by the shareholders without having to call an extraordinary meeting. We believe that the undertakings should comply with the new provisions effective from the remuneration policy for 2017 (which will be presented in 2017, when the 2016 Financial Statements are to be approved).

Furthermore, it should be clarified that the new remuneration requirements do not apply retroactively. Not in relation to existing and binding contracts. Not mid-year in relation to variable remuneration which members of staff are in the midst of accruing.

Title VII – Requirements for competent authorities – Remuneration policies

Paragraph 312
The EBF supports more transparency between supervisors and institutions. Such transparency should apply also in relation to other aspects of the remuneration guidelines.

European Banking Federation

Annex 1

The mapping table would be more readable if another column is inserted with reference to the paragraph of the guidelines.

Blazej Blasikiewicz
b.blasikiewicz@ebf-fbe.eu