

**BVI<sup>1</sup> Position on the EBA's Consultation Paper (EBA/CP/2020/08) on a Draft Regulatory Technical Standard on classes of instruments that adequately reflect the credit quality of investment firms as a going concern and possible alternative arrangements that are appropriate to be used for the purposes of variable remuneration**

We take the opportunity to present our views on the third [consultation](#) paper of the EBA related to **remuneration** and the Draft Regulatory Technical Standard (Draft RTS) on **classes of instruments**. Our members providing portfolio management services do not regularly issue equity instruments as variable remuneration to their employees. We therefore limit our response to the proposals on alternative instruments (Article 6 of the Draft RTS) as follows:

**Question 3:** *Are the provisions in Article 6 appropriate and sufficiently clear?*

*Where respondents are of the view that the draft RTS should define a set of specific arrangements rather than providing conditions that such arrangements should meet, comments are most helpful, when they clearly describe the alternative arrangements that investment firms desire to use to ensure that variable remuneration is aligned with the long-term interest of the investment firm and its risk profile.*

In general, the purpose of the IFD is to offer some flexibility to investment firms in the way they use non-cash instruments to pay variable remuneration, provided that such instruments are effective in achieving the objective of aligning the interests of staff with the interest of various stakeholders, such as shareholders, creditors and clients, and contribute to the alignment of variable remuneration with the risk profile of the investment firm (cf. Recital 24 of the IFD). **In this regard, a principle-based approach should be adopted to enable competent authorities to assess the specificities of markets and diverse legal structures of investment firms.** We therefore support the selection of Option A in setting conditions for alternative arrangements that ensure they meet the same objective as the pay out of variable remuneration in instruments without specifying in detail the form such an arrangement should take (e.g. financial instruments or deferred cash on frozen accounts).

We also welcome the general assumption made by the EBA in its impact assessment that the RTS should not lead to alternative arrangements that are overly burdensome to create and use for the purpose of variable remuneration and respect the principle of proportionality. In our view, the Draft RTS largely reflects that approach.

**However, we see a need for improvement related to the proposed alternative arrangements based on the performance of the managed assets or the investment firm.** In our view, the proposed reference to percentage dependencies on the performance of portfolios or the investment firm's total own funds are too rigidly. This applies even more as the revenues of investment firms in the form

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<sup>1</sup> BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Asset Managers act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's 114 members manage assets more than 3 trillion euros for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 23%, Germany represents the largest fund market in the EU. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit [www.bvi.de/en](http://www.bvi.de/en).



of fees, commissions or other revenues in relation to the provision of different investment services are highly volatile. Limiting the performance-based variable remuneration to the percentage of value change of the managed assets or to the percentage of value of net revenue in relation to the investment firms total own funds would affect the investment firm's ability to reduce remuneration at times of reduced revenues, leading in turn to risks to the investment firm's ability to withstand times of economic downturn or reduced revenues.

**We therefore propose to delete the criteria linked to the percentage of value change of the managed assets or to the percentage of value of net revenue in relation to the investment firm's total own funds in Article 6(g)(iv) and (v) of the Draft RTS as follows:**

'(g) where the alternative arrangement allows for predetermined changes of the value received as variable remuneration during deferral and retention periods, based on the performance of the investment firm or the managed assets; the following conditions shall be met:

- (i) the change of the value is based on predefined performance indicators that are based on the credit quality of the institution or the performance of the managed assets;
- (ii) value changes should at least be calculated annually and at the end of the retention period;
- (iii) the rate of possible positive and negative value changes should equally be based on the level of positive or negative credit quality changes or performance measured;
- ~~(iv) where the value change is based on the performance of assets managed, the percentage of value change should be limited to the percentage of value change of the managed assets;~~
- ~~(v) where the value change is based on the credit quality of the investment firm, the percentage of value change should be limited to the percentage of net revenue in relation to the investment firms total own funds;~~

As an alternative approach, EBA could follow the guidance provided by ESMA in its remuneration guidelines under the UCITS Directive and AIFMD which also deal with performance-based remuneration. For example, ESMA states in its guidelines on sound remuneration policies under the UCITS Directive:

*'103. Performance-related remuneration should include parameters linked to the risks and performance of the UCITS concerned and of the business unit of the management company in addition to the risks and performance of the individual activities. Thus, the amount of variable remuneration a staff member is eligible for should be determined by his/her individual performance, the performance of his/her business line or the UCITS concerned and the performance of the management company. The relative importance of each level of the performance criteria should be determined beforehand and adequately balanced to take into account the position or responsibilities held by the staff member.'*

In addition, we request the EBA to clarify that **instruments issued by an entity within a group** as defined in Article 2(12) of Directive 2002/87/EU (as amended) should be recognised as alternative instruments.

**Question 4:** Do respondents agree with the findings of the impact assessment?

*Where respondents have identified additional costs or burdens created by the draft RTS, it would be most helpful if respondents could specify and, where possible, quantify separately the costs for the implementation of the provision and the costs for the ongoing application of the provisions.*

We would like to draw EBAs attention to the fact that the implementation of the pay-out processes in instruments or alternative arrangements will increase the administrative burden for investment firms



which are currently not covered by the remuneration requirements of the CRD, such as the pay-out process. In addition, the lack of proportionality (both on the identification of Material Risk Takers and on application of the pay-out regime) may also lead to an unlevel playing field across the financial industry (e.g. banks and AIF/UCITS Management Companies). This applies for our members who provide portfolio management services. We see the following impact:

- Adjusting the content of the remuneration policies (such as changing the scope of the remuneration policy regarding to the pay-out process)
- Implementation of a pay-out process for parts of the variable remuneration (such as deferral arrangements, pay-out in instruments, application of malus) including software adaption for the pay-out process and adjusting the accounting systems (such as implementation of different payment methods and new employees' accounts, monitoring of the deferral arrangements, initiation of subsequent payments)
- In cases where a pay-out process is partially in place, changing the implemented processes for salary payments of the identified staff (such as changing the calculation process for the deferred part of the bonus and the timeline of the deferred period)
- Adjusting the employment contracts of the identified staff, including conduct of negotiations with the employees
- Informing – where applicable - the workers' council ("Betriebsrat") and requiring the consent of the workers' council (including complying with the requirements of the Equal Treatment Law); in practice, there are open questions what happens if the workers' council fails to give its approval under employment legislation or collective agreements (e.g. consent for malus agreements).
- Clarification of legal issues by internal/external lawyers
- Hiring external service providers for the implementation of the new (complex) requirements.

We therefore refer to our answer to question 3 and request the EBA to adopt a more principle-based approach.

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