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Final report

Draft Regulatory Technical Standards

on classes of instruments that adequately reflect the credit quality of the investment firm as a going concern and possible alternative arrangements that are appropriate to be used for the purposes of variable remuneration

Contents

1. Executive summary

Directive (EU) 2019/2034[1] (IFD) sets out requirements for the remuneration of staff whose professional activities have a material impact on the risk profile of the investment firm or of the assets that it manages (identified staff) that apply from 26 June 2021. Currently, such staff are subject to similar provisions under Directive 2013/36/EU[2] (CRD).

Article 32(1)(j) of the IFD provides that at least 50% of the variable remuneration consists of certain instruments, including (iii) Additional Tier 1 instruments or Tier 2 instruments or Other Instruments which can be fully converted to Common Equity Tier 1 instruments or written down, and that adequately reflect the credit quality of the investment firm as a going concern.

Article 32(1)(k) of the IFD provides that by way of derogation from point (j), where an investment firm does not issue any of the instruments referred to in that point, competent authorities may approve the use of alternative arrangements fulfilling the same objectives.

Article 32(8) of Directive (EU) 2019/2034 mandates the EBA, in consultation with ESMA, to develop draft regulatory technical standards to specify the instruments under point (j)(iii) of paragraph (1) of this Article and possible alternative arrangements for the pay out of variable remuneration.

The IFD refers to the requirements included in Regulation (EU) No 575/2013[3] (CRR) regarding AT 1 and Tier 2 instruments. The draft RTS introduce requirements for investment firms for AT 1, Tier 2 and Other Instruments used for the purposes of variable remuneration, to ensure that they appropriately reflect the credit quality of the investment firm, and define for Tier 2 and Other Instruments the write-down, write-up and conversion mechanisms. For AT 1 instruments, these mechanisms are defined by the CRR. The provisions in the RTS are aligned with Commission Delegated Regulation 527/2014[4] (Regulatory Technical Standards (RTS) on classes of instruments that are appropriate to be used for the purposes of variable remuneration under CRD) to ensure that, in particular, groups of credit institutions and investment firms are able to use a common set of instruments for remuneration purposes.

The draft RTS set out requirements to ensure that the credit quality of investment firms is reflected in the instruments and that these instruments are appropriate for the purposes of variable remuneration. The link to credit quality as a going concern is established by introducing uniform minimum trigger events for write-down and conversion of AT 1, Tier 2 and Other Instruments. To ensure that different

[1] Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and amending Directives 2002/87/EC, 2009/65/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU and 2014/65/EU

[2] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC

[3] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012

[4] COMMISSION DELEGATED REGULATION (EU) No 527/2014 of 12 March 2014 supplementing Directive (EU) No 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the classes of instruments that adequately reflect the credit quality of an institution as a going concern and are appropriate to be used for the purposes of variable remuneration

classes of instruments are appropriate for the purposes of variable remuneration, these instruments should provide appropriate incentives for staff to be prudent and long term oriented in their risk-taking.

The EBA has reviewed the draft RTS after three month of public consultation and has now submitted as mandated the draft RTS to the Commission for adoption.

2. Background and rationale

2.1 The nature of RTS under EU law

1. These draft RTS are produced in accordance with Article 10 of Regulation (EU) No 1093/2010 of 24 November 2010 (the EBA Regulation) as amended. Paragraph 4 of that same Article provides that the RTS shall be adopted by means of an EU Regulation or Decision.

2. In accordance with EU law, EU regulations are binding in their entirety and directly applicable in all Member States. This means that, on the date of their entry into force, EU Regulations become part of the national law of the Member States and that their implementation into national law is not only unnecessary but also prohibited by EU law, except insofar as this is expressly required by the regulations.

2.2 Legal basis and background

3. After the financial crisis, the EU co-legislator has put in place a legal framework under Directives 2010/76/EU and 2013/36/EU for identified staff, i.e. staff that have a material impact on the institution's risk profile. This framework aimed at ensuring that the variable remuneration of identified staff is aligned with the institution's risk profile in the longer-term and applied to credit institutions and investment firms.

4. Considering the differences between credit institutions and investment firms a specific remuneration framework for investment firms has been established for those firms that are subject to Directive (EU) 2019/2034[5] (IFD). Small and non-interconnected investment firms that meet all the conditions of Article 12(1) of Regulation (EU) 2019/2033 (IFR)[6] are not subject to the specific remuneration framework under the IFD, but have still to comply with the remuneration requirements of Directive 2014/65/EU[7] that sets out requirements on the remuneration of sales staff.

5. The IFD sets out a framework for remuneration policies for investment firms that has been construed as referring to the corresponding provisions in Directive 2013/36/EU[8]. The provisions

[5] Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and amending Directives 2002/87/EC, 2009/65/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU and 2014/65/EU

[6] Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) No 1093/2010, (EU) No 575/2013, (EU) No 600/2014 and (EU) No 806/2014

[7] DIRECTIVE 2014/65/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU

[8] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 as amended on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC Text with EEA relevance

should ensure that the remuneration of staff members who have a material impact on the investment firm's risk profile or on the assets that it manages is aligned with its risk profile.

6. While ensuring a level playing field, the IFD takes into account the differences between credit institutions and investment firms and offers some flexibility to investment firms in the way they use non-cash instruments when paying variable remuneration, as long as such instruments are effective in achieving the objective of aligning the interest 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. These conditions and the present draft RTS ensure that non-cash instruments are appropriate to be used for the purposes of variable remuneration.

7. Article 32(1)(j) of the IFD requires that at least 50% of 'the variable remuneration of staff members who have a material impact on the investment firm's risk profile or on the assets that it manages consists of any of the following instruments: (i) shares, or subject to the legal structure of the investment firm concerned, equivalent ownership interests; (ii) share-linked instruments, or subject to the legal structure of the investment firm concerned, equivalent non-cash instruments; (iii) additional Tier 1 instruments or Tier 2 instruments or Other Instruments which can be fully converted to Common Equity Tier 1 instruments or written down and that adequately reflect the credit quality of the investment firm as a going concern; (iv) non-cash instruments which reflect the instruments of the portfolios managed.

8. Article 32(1)(k) determines that by way of derogation from point (j), where an investment firm does not issue any of the instruments referred to in that point, national competent authorities may approve the use of alternative arrangements fulfilling the same objectives.

9. Article 32(3) of the IFD determines 'that Member States or their competent authorities may place restrictions on the types and designs of those instruments or prohibit the use of certain instruments for variable remuneration.'

10. Article 32(8) of the IFD sets out that the EBA, in consultation with ESMA, shall develop draft regulatory technical standards to specify the classes of instruments that satisfy the conditions set out in paragraph 1(j)(iii) as well as to specify possible alternative arrangements set out in paragraph 1(k).

11. The IFD allows investment firms to use a wide set of instruments for the pay out of variable remuneration. The purpose of the draft RTS is to specify a subset of those instruments, namely classes of additional Tier 1, Tier 2 and Other Instruments that are appropriate to be used for variable remuneration as well as to specify possible alternative arrangements for the pay out of variable remuneration where investment firms do not issue any of the instruments referred to in Article 32(1)(j) of the IFD.

12. The EBA has conducted an impact assessment of costs and benefits caused by the provisions contained in these draft RTS. The EBA came to the conclusion that the additional costs caused by these draft RTS are very limited, as the draft RTS are closely aligned with the existing

framework. The possibility for certain investment firms to use alternative arrangements is aimed at reducing the regulatory burden for those firms, which do not issue any of the instruments included in Article 32(1)(j) of the IFD. The setting up of alternative arrangements will trigger one off costs that are very limited as they do not require the issuance of any financial instruments.

2.3 Regulatory approach within the RTS

13. The EBA has taken the existing remuneration framework established under Directive 2013/36/EU and Commission Delegated Regulation 527/2014[9] into account when developing the draft RTS. The existing framework takes into account market practices for own funds instruments and aims to ensure that already existing types of instruments can be used when they meet certain additional conditions that ensure that such issuances are appropriate for the purpose of variable remuneration.

14. Regarding the classes of additional Tier 1 (AT 1), Tier 2 and Other Instruments that are appropriate to be used for variable remuneration, the Commission has already adopted the aforementioned Delegated Regulation specifying the classes of such instruments that meet the conditions of Article 94(1)(l)(ii) of Directive 2013/36/EU.

15. The conditions for such instruments under the IFD are equal to the conditions set out in Directive 2013/36/EU and therefore the classes of instruments that satisfy the conditions under Article 32(1)(j)(iii) of the IFD should be equivalent to the classes of instruments specified in Commission Delegated Regulation 527/2014, but should also take into account the need for increased flexibility of investment firms. This additional flexibility has to a large extent already been provided for in paragraphs 4 and 5 of the same Article that allows limitations in the application of the requirement to pay out variable remuneration to certain investment firms and staff. Moreover, investment firms that do not issue instruments are allowed to use alternative arrangements to pay out variable remuneration.

16. Variable remuneration awarded in instruments is intended to promote sound and effective risk management and should not encourage risk-taking that exceeds the level of tolerated risk within the investment firm. Receiving a part of the variable remuneration in instruments or via alternative arrangements should provide incentives for staff to act in the long-term interest of the investment firm.

17. The price or value of instruments awarded as variable remuneration should reflect changes in the credit quality of the firm, in particular if it deteriorates, to ensure that instruments awarded to staff participate in potential losses that have an adverse effect on credit quality as a going concern. This link provides incentives for prudent and long term oriented risk-taking. Credit quality may be measured by different means, e.g. using a rating, spreads or capital ratios.

[9] COMMISSION DELEGATED REGULATION (EU) No 527/2014 of 12 March 2014 supplementing Directive (EU) No 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the classes of instruments that adequately reflect the credit quality of an institution as a going concern and are appropriate to be used for the purposes of variable remuneration

18. The qualification that the instrument shall reflect the credit quality of the investment firm as a going concern makes it necessary to introduce measures that ensure that the value of the instruments is not reduced only at the time when an investment firm is resolved or at the point of non-viability. Therefore, the trigger level for investment firms at which write-off or conversion takes place is set above the regulatory minimum requirements to ensure that the instruments are suitable for the purposes of variable remuneration.

19. To ensure that a reliable measure exists for all investment firms without creating costs for additional rating processes and to ensure a close alignment with the framework applicable to credit institutions, including on a consolidated basis, the CET 1 capital ratio was chosen as an indicator for the credit quality as a going concern and the same trigger level has been set.

20. The IFD provisions for variable remuneration require deferral and retention periods and state, among other requirements, that variable remuneration is not paid through vehicles or methods that facilitate non-compliance with the requirements. Consequently, the conditions of instruments need to ensure a sufficiently long maturity to account for deferral and retention periods and to be at market rates to avoid situations in which overly high distributions jeopardise the ability of investment firms to strengthen their capital bases or that would circumvent limits set for the variable components of remuneration in the investment firm's remuneration policy or weaken the risk alignment. This is achieved by a cap on the distributions or through the requirement to issue significant parts of any issuance to other investors. To ensure a level playing field, the requirements of the draft RTS have been aligned with the framework applicable to credit institutions.

21. Where an investment firm does not issue any of the instruments referred to in Article 32(1)(j), national competent authorities may approve the use of alternative arrangements fulfilling the same objectives. The draft RTS specify possible alternative arrangements that should ensure that the variable remuneration received by staff members who have a material impact on the investment firm's risk profile or on the assets that it manages is aligned with its risk profile.

22. To achieve this objective it is necessary to create conditions that ensure that the value of the variable remuneration received under alternative arrangements is reduced when risks cause an adverse effect on the performance of the investment firm or managed assets, or that such arrangements could be converted into CET1 capital. Such arrangements should allow the deferral and retention of variable remuneration received, so that compliance with other requirements for variable remuneration is ensured.

3. Draft regulatory technical standards

COMMISSION DELEGATED REGULATION (EU) No …/..

of [date]

on classes of instruments that adequately reflect the credit quality of the investment firm as a going concern and possible alternative arrangements that are appropriate to be used for the purposes of variable remuneration

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and amending Directives 2002/87/EC, 2009/65/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU and 2014/65/EU, and in particular Article 32 (8) thereof,

Whereas:

(1) Directive (EU) 2019/2034 regarding the governance and remuneration provisions applicable to investment firms has been construed as referring to the corresponding provisions in Directive 2013/36/EU to ensure that governance and remuneration provisions applicable to investment firms benefit from the well established meaning of these concepts under Directive 2013/36/EU. Against this background, and also with a view to ensure a level playing field between credit insitutions and investment firms, this Regulation should be inspired by and as far as possible aligned with Commission Delegated Regulatiuon 527/2014 that specifies the classes of instruments that are appropriate to be used under Directive 2013/36/EU. This Regulation should also provide appropriate flexibility to investment firms regarding the use of different types of non-cash instruments or of alternative arrangements when paying variable remuneration as long as such instruments are effective in achieving the objective of aligning the interest 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.

(2) Investment firms have been subject to Commission Delegated Regulation 527/2014 that specifies the additional Tier 1, Tier 2 and Other Instruments, of which the substancial portion of variable remuneration to be paid out in instruments under Article 94(1)(l) of Directive 2013/36/EU should consist. Those instruments are included also in point (j)(iii)

of Article 32(1)of Directive (EU) 2019/2034. Investment firms should be able to continue to use those instruments that comply with Commission Delegated Regulation 527/2014 under the present Commission Delegated Regulation.

(3) Variable remuneration awarded in instruments should promote sound and effective risk management and should not encourage risk-taking that exceeds the level of risk appetite of the investment firm. Therefore, classes of instruments which can be used for the purposes of variable remuneration should align the interests of staff with the longer-term interests of the investment firm, its shareholders, creditors, clients and other stakeholders by providing incentives for staff to act in the longer-term interest of the investment firm.

(4) Directive (EU) 2019/2034 allows investment firms to use a wide set of instruments for the pay out of variable remuneration. In order to ensure that there is a strong link to the credit quality of an investment firm as a going concern, additional Tier 1, Tier 2 and Other Instruments used for the purposes of variable remuneration should contain appropriate trigger events for write down or conversion which reduce the value of the instruments in situations where the credit quality of the investment firm as a going concern has deteriorated. The trigger events used for remuneration purposes should not change the level of subordination of the instruments and therefore should not lead to a disqualification of Additional Tier 1 or Tier 2 instruments as own funds instruments.

(5) While the conditions which apply to Additional Tier 1 and Tier 2 instruments are specified in Article 9 of Regulation (EU) 2019/2033[10] in conjunction with Chapter 3 and 4 of Title 1 of Part Two of Regulation (EU) No 575/2013, the Other Instruments referred to in point (j)(iii) of Article 32(1) of Directive (EU) 2019/2034, which can be fully converted to Common Equity Tier 1 instruments or written down, are not subject to specific conditions pursuant to that Regulation as they are not classified as own funds instruments for prudential purposes. Specific requirements should therefore be set for different classes of instruments to ensure that they are appropriate to be used for the purposes of variable remuneration, taking account of the different nature of the instruments. The use of instruments for the purposes of variable remuneration should not in itself prevent instruments from qualifying as own funds of an investment firm as long as the conditions laid down in Regulation (EU) 2019/2033 are met. Nor should such use in itself be understood as providing an incentive to redeem the instrument, as after deferral and retention periods staff members are, in general, able to receive liquid funds by other means than redemption.

(6) Other Instruments should not be limited to financial instruments as defined in point 15 of Article 4(1) of Regulation (EU) No 2019/2033 and allow for the use of other contractual arrangements between staff members and investment firms to reduce the administrative burden for the creation of such instruments. To ensure that Other Instruments reflect the credit quality of an investment firm as a going concern, appropriate requirements should ensure that such instruments are written down or converted before an investment firm fails to meet its own funds requirements.

(7) When instruments used for the purposes of variable remuneration are called, redeemed, repurchased or converted, in general such transactions should not increase the value of

[10] Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) No 1093/2010, (EU) No 575/2013, (EU) No 600/2014 and (EU) No 806/2014

the remuneration awarded by paying out amounts that are higher than the value of the instrument or by converting into instruments which have a higher value than the instrument initially awarded. The replacement of instruments at the same value should ensure that remuneration is not paid through vehicles or methods that facilitate non-compliance with Directive (EU) 2019/2034 or Regulation (EU) 2019/2033.

(8) When awarding variable remuneration and when instruments used for variable remuneration are redeemed, called, repurchased or converted, those transactions should be based on values that have been established in accordance with the applicable accounting standard at the point of time of the transaction to ensure that the correct amount of variable remuneration is awarded and not unduly altered when the instrument is redeemed, called, repurchased or converted.

(9) Article 54 of Regulation (EU) No 575/2013 sets out the write-down and conversion mechanisms for Additional Tier 1 instruments. Additionally, point (j)(iii) of Article 32(1) of Directive (EU) 2019/2034 requires that Other Instruments can be fully converted into Common Equity Tier 1 instruments or written down. As the economic outcome of a conversion or write-down of Other Instruments is the same as for Additional Tier 1 instruments, write-down or conversion mechanisms for Other Instruments should take into account the mechanisms that apply to Additional Tier 1 instruments, with adaptations to take account of the fact that Other Instruments do not qualify as own fund instruments from a prudential perspective. Tier 2 instruments are not subject to regulatory requirements regarding write-down and conversion under Regulation (EU) No 575/2013. To ensure that the value of all such instruments, when used for variable remuneration, is reduced when the credit quality of the investment firm deteriorates, the situations in which a write-down or conversion of the instrument is necessary should be specified. The write down, write up and conversion mechanisms for Tier 2 and Other Instruments should be specified to ensure consistent application.

(10) Distributions arising from instruments can take various forms. They can be variable or fixed and can be paid periodically or at the final maturity of an instrument. In order to promote sound and effective risk management no distributions should be paid to staff during deferral periods. Staff members should only receive the distributions in respect of periods which follow the vesting of the instrument, after which staff becomes the legal owner of the instrument. Therefore, only instruments with distributions which are paid periodically to the owner of the instrument are appropriate for use as variable remuneration; zero coupon bonds or instruments which retain earnings should not count towards the portion of remuneration which must consist of any of the instruments referred to in point (j) of Article 32(1) of Directive (EU) 2019/2034. This is because staff would benefit during the deferral period from increasing values, which can be understood as equivalent to receiving distributions.

(11) Very high distributions can reduce the long-term incentive for prudent risk-taking as they effectively increase the variable part of the remuneration. In particular, distributions should not be paid out at intervals of longer than one year, as this would lead to distributions effectively accumulating during deferral periods and being paid out once the variable remuneration vests. Accumulation of distributions would circumvent the principle in paragraph 3 of Article 32 that remuneration payable under deferral arrangements vests no faster than on a pro rata basis. Point (b) of Article 32(2) of

Directive (EU) 2019/2034 requires that variable remuneration shall not be paid through financial vehicles or methods that facilitate the non-compliance with this Directive or Regulation (EU) 2019/2033. Therefore, distributions made after the instrument has vested should not exceed market rates for such instruments issued by other investment firms or institutions of comparable credit quality. This should be ensured by requiring instruments used for variable remuneration, or the instruments to which they are linked, to be issued mainly to other investors, or by requiring such instruments to be subject to a cap on distributions.

(12) Deferral and retention requirements which apply to awards of variable remuneration pursuant to point (l) of Article 32(1) and Article 32(3) of Directive (EU) 2019/2034 have to be met at all relevant times, including when instruments used for variable remuneration are called, redeemed, repurchased or converted. In such situations, instruments should therefore be replaced with Additional Tier 1, Tier 2 and Other Instruments which reflect the credit quality of the investment firm as a going concern, have features equivalent to those of the instrument initially awarded, and are of the same value, taking into account any amounts which have been written down. Where instruments other than Additional Tier 1 instruments have a fixed maturity date, minimum requirements should be set for the remaining maturity of such instruments when they are awarded in order to ensure that they are consistent with requirements regarding the deferral and retention periods for variable remuneration.

(13) Directive (EU) 2019/2034 does not limit the classes of instruments that can be used for variable remuneration to a specific class of financial instruments. It should be possible to use synthetic instruments or contracts between staff members and investment firms which are linked to Additional Tier 1 and Tier 2 instruments which can be fully converted or written down. This allows for the introduction of specific conditions in the terms of such instruments which apply only to instruments awarded to staff, without the need to impose such conditions on other investors.

(14) In a group context, issuances may be managed centrally within a parent undertaking; this should include situations where the parent undertaking is subject to Directive 2013/36/EU or Directive 2019/2034. Investment firms within a group may not always issue instruments which are appropriate to be used for the purpose of variable remuneration themselves. Regulation (EU) 2019/2034 in conjunction with Regulation (EU) No 575/2013 enables Additional Tier 1 and Tier 2 instruments issued through an entity within the scope of consolidation to form part of an investment firm´s own funds subject to certain conditions. Therefore, it should also be possible to use such instruments for the purpose of variable remuneration, provided that there is a clear link between the credit quality of the investment firm using these instruments for the purpose of variable remuneration and the credit quality of the issuer of the instrument. Such a link can usually be assumed to be the case between a parent undertaking and a subsidiary. Instruments other than Additional Tier 1 and Tier 2 instruments which are not issued directly by an investment firm should also be capable of being used for variable remuneration, subject to equivalent conditions. Instruments which are linked to reference instruments issued by parent undertakings in third countries and which are otherwise equivalent to Additional Tier 1 or Tier 2 instruments should be eligible to be used for the purposes of variable remuneration if the trigger event refers to the investment firm using such a synthetic instrument.

(15) Investment firms that do not issue any of the instruments listed under point (j) Article 32(1) of Directive (EU) 2019/2034, should be able to use alternative arrangements, subject to the approval of the competent authority. Such alternative arrangements should meet the same objectives as the award of eligible instruments. The alternative arrangement should ensure that the variable remuneration awarded is subject to implicit risk adjustments, i.e. changes of its value in cases there is an adverse effect on the performance of an investment firmor managed assets. Where the investment firm is subject to the requirement to defer variable remuneration under point (l) of this Article, the alternative arrangements should also be consistent with the requirement to defer variable remuneration, the application of malus or claw back and the application of retention periods to variable remuneration paid in instruments.

(16) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority (EBA) to the European Commission.

(17) The EBA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010[11]. The Banking Stakeholder Group has not submitted an opinion.

HAS ADOPTED THIS REGULATION:

Article 1

Classes of instruments that adequately reflect the credit quality of an investment firm as a going concern and are appropriate to be used for the purposes of variable remuneration

1. The following shall be the classes of instruments that satisfy the conditions laid down in point (j)(iii) of Article 32(1) of Directive (EU) 2019/2034:

(a) classes of Additional Tier 1 instruments where those classes fulfil the conditions referred to in paragraph 2 and Article 2, and comply with Article 5(9) and point (c) of Article 5(13);

(b) classes of Tier 2 instruments where those classes fulfil the conditions referred to in paragraph 2 and Article 3, and comply with Article 5;

(c) classes of instruments which can be fully converted to Common Equity Tier 1 instruments or written down and which are neither Additional Tier 1 instruments nor Tier 2 instruments ('Other Instruments') in the cases referred to in Article 4 where those classes fulfil the conditions referred to in paragraph 2 and comply with Article 5.

[11] Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2020, p. 12)

2. The classes of instruments referred to in paragraph 1 shall fulfil the following conditions:

(a) instruments shall not be secured or subject to a guarantee that enhances the seniority of the claims of the holder;

(b) where the provisions governing an instrument allow its conversion, that instrument shall only be used for the purposes of awarding variable remuneration where the rate or range of conversion is set at a level that ensures that the value of the instrument into which the instrument initially awarded is converted is not higher than the value of the instrument initially awarded at the time it was awarded as variable remuneration;

(c) the provisions governing convertible instruments which are used for the sole purpose of variable remuneration shall ensure that the value of the instrument into which the instrument initially awarded is converted is not higher than the value, at the time of that conversion, of the instrument initially awarded;

(d) the provisions governing the instrument shall provide that any distributions are paid on at least an annual basis and are paid to the holder of the instrument;

(e) instruments shall be priced at their value at the time the instrument is awarded, in accordance with the applicable accounting standard. The valuation shall be subject to independent review;

(f) the provisions governing the instruments issued for the sole purpose of variable remuneration shall require a valuation to be carried out in accordance with the applicable accounting standard in the event that the instrument is redeemed, called, repurchased or converted.

Article 2

Conditions for classes of Additional Tier 1 instruments

Classes of Additional Tier 1 instruments shall comply with the following conditions:

(a) the provisions governing the instrument shall specify a trigger event for the purpose of point (e)(iii) of Article 9(2) of Regulation (EU) No 2019/2033;

(b) the trigger event referred to in point (a) occurs when the Common Equity Tier 1 capital ratio of the investment firm issuing the instrument falls below either of the following:

(i) 7% of the product of 12.5 multiplied by the own funds requirements calculated under Article 11(1) of Regulation (EU) 2019/2033;

(ii) a level higher than specified in (i), where determined by the investment firm or institution issuing the instrument and specified in the provisions governing the instrument;

(c) one of the following requirements is met:

(i) the instruments are issued for the sole purpose of being awarded as variable remuneration and the provisions governing the instrument ensure that any distributions are paid at a rate which is consistent with market rates for similar instruments issued by the investment firm or by investment firms or institutions of comparable credit quality and which in any case is, at the time the remuneration is awarded, no higher than 8 percentage points above the annual average rate of change for the Union published by the Commission (Eurostat) in its Harmonised Indices of Consumer Prices published pursuant to Article 11 of Council Regulation (EC) No 2494/95 (1). Where the instruments are awarded to staff members who perform the predominant part of their professional activities outside the Union and the instruments are denominated in a currency issued by a third country, investment firms may use a similar independently-calculated index of consumer prices produced in respect of that third country;

(ii) at the time of the award of the instruments as variable remuneration, at least 60% of the instruments in issuance were issued other than as an award of variable remuneration and are not held by one of the following or by any undertaking that has close links with one of the following: the investment firm or its subsidiaries, the parent undertaking of the investment firm or its subsidiaries, the parent financial holding company or its subsidiaries, the mixed activity holding company or its subsidiaries or the mixed financial holding company and its subsidiaries.

Article 3

Conditions for classes of Tier 2 instruments

Classes of Tier 2 instruments shall comply with the following conditions:

(a) at the time of the award of the instruments as variable remuneration, the remaining period before maturity of the instruments shall be equal to or exceed the sum of the deferral periods and retention periods that apply to variable remuneration in respect of the award of those instruments;

(b) the provisions governing the instrument provide that, upon the occurrence of a trigger event the principal amount of the instruments shall be written down on a permanent or temporary basis or the instrument shall be converted to Common Equity Tier 1 instruments;

(c) the trigger event referred to in point (b) occurs where the Common Equity Tier 1 capital ratio of the investment firm issuing the instrument falls below either of the following:

(i) 7% of the product of 12.5 multiplied by the own funds requirements calculated under Article 11(1) of Regulation (EU) 2019/2034;

(ii) a level higher than specified under (i), where determined by the investment firm or institution issuing the instrument and specified in the provisions governing the instrument;

(d) one of the requirements in point (c) of Article 2 is met.

Article 4

Conditions for classes of Other Instruments

1. Under the conditions laid down in point (c) of Article 1(1), Other Instruments satisfy the conditions laid down in point (j)(iii) of Article 32(1) of Directive (EU) 2019/2034 in each of the following cases:

(a) the Other Instruments fulfil the conditions referred to in paragraph 2;

(b) the Other Instruments are linked to an Additional Tier 1 instrument or Tier 2 instrument and fulfil the conditions referred to in paragraph 3;

(c) the Other Instruments are linked to an instrument which would be an Additional Tier 1 instrument or Tier 2 instrument but for the fact that it is issued by a parent undertaking of the investment firm which is outside the scope of consolidation pursuant to Chapter 2 of Title II of Part One of Regulation (EU) No 575/2013 and the Other Instruments fulfil the conditions in paragraph 4.

2. The conditions referred to in point (a) of paragraph 1 are the following:

(a) the Other Instruments shall be issued directly or through an institution or financial institution included in the consolidation scope pursuant to Chapter 2 of Title II of Part One of Regulation (EU) No 575/2013 or Article 7 of Regulation (EU) 2019/2034, provided that a change to the credit quality of the issuer of the instrument can reasonably be expected to lead to a similar change to the credit quality of the investment firm using the Other Instruments for the purpose of variable remuneration;

(b) the provisions governing the Other Instruments do not give the holder the right to accelerate the scheduled payment of distributions or principal other than in the case of the insolvency or liquidation of the institution or investment firm issuing the instrument;

(c) at the time of the award of the Other Instruments as variable remuneration the remaining period before maturity of the Other Instruments is equal to or exceeds the sum of the deferral periods and retention periods that apply in respect of the award of those instruments;

(d) the provisions governing the instrument provide that, upon the occurrence of a trigger event, the principal amount of the instruments shall be written down on a permanent or temporary basis or the instrument shall be converted to Common Equity Tier 1 instruments;

(e) the trigger event referred to in point (d) occurs when the Common Equity Tier 1 capital ratio of the institution or investment firm issuing the instrument falls below either of the following:

(i) in the case of an investment firm issuing the instrument, 7% of the product of 12.5 multiplied by the own funds requirements calculated under Article 11(1) of Regulation (EU) 2019/2034;

(ii) in the case of an institution issuing the instrument, 7% of the Common Equity Tier 1 capital ratio of the institution issuing the instrument;

(iii) a level higher than specified under (i) or (ii), where determined by the investment firm or institution issuing the instrument and specified in the provisions governing the instrument;

(f) one of the requirements in point (c) of Article 2 is met.

3. The conditions referred to in point (b) of paragraph 1 are the following:

(a) the Other Instruments fulfil the conditions in points (a) to (e) of paragraph 2;

(b) the Other Instruments are linked to an Additional Tier 1 or Tier 2 instrument issued through an entity included within the scope of consolidation pursuant to Chapter 2 of Title II of Part One of Regulation (EU) No 575/2013 or Article 7 of Regulation (EU) 2019/2034 (the 'reference instrument');

(c) the reference instrument fulfils the conditions of points (c) and (f) of paragraph 2 at the time that the instrument is awarded as variable remuneration;

(d) the value of an Other Instrument is linked to the reference instrument such that it is at no time more than the value of the reference instrument;

(e) the value of any distributions paid after the Other Instrument has vested is linked to the reference instrument such that distributions paid are at no time more than the value of any distributions paid under the reference instrument;

(f) the provisions governing the Other Instruments provide that if the reference instrument is called, converted, repurchased or redeemed within the deferral or retention period the Other Instruments shall be linked to an equivalent reference instrument which fulfils the conditions in this Article such that the total value of the Other Instruments does not increase.

4. The conditions referred to in point (c) of paragraph 1 are the following:

(a) the competent authorities have determined for the purpose of Article 55 of Directive (EU) 2019/2034 or Article 127 of Directive 2013/36/EU that the investment firm or institution that issues the instrument to which the Other Instruments are linked is subject to consolidated supervision by a third-country supervisory authority which is equivalent to that governed by the principles set out in that Directive and the requirements of Chapter 2 of Title II of Part One of Regulation (EU) No 575/2013;

(b) the Other Instruments fulfil the conditions referred to in points (a) and points (c) to (f) of paragraph 3.

Article 5

Write-down, write-up and conversion procedures

1. For the purpose of point (b) of Article 3 and point (d) of Article 4(2) the provisions governing Tier 2 instruments and Other Instruments shall comply with the procedures and timing laid down in paragraphs 2 to 14 for calculating the Common Equity Tier 1 capital ratio and the amounts to be written down, written up or converted. The provisions governing Additional Tier 1 instruments shall comply with the procedures laid down in paragraph 9 and point (c) of paragraph 13 in respect of amounts to be written down, written up or converted.

2. Where the provisions governing Tier 2 and Other Instruments require the instruments to be converted into Common Equity Tier 1 instruments upon the occurrence of a trigger event, those provisions shall specify either of the following:

(a) the rate of that conversion and a limit on the permitted amount of conversion;

(b) a range within which the instruments will convert into Common Equity Tier 1 instruments.

3. Where the provisions governing the instruments provide that their principal amount shall be written down upon the occurrence of a trigger event, the write-down shall permanently or temporarily reduce all the following:

(a) the claim of the holder of the instrument in the insolvency or liquidation of the institution or investment firm issuing the instrument;

(b) the amount to be paid in the event of the call or redemption of the instrument;

(c) the distributions made on the instrument.

4. Any distributions payable after a write-down shall be based on the reduced amount of the principal.

5. Write-down or conversion of the instruments shall, under the applicable accounting framework, generate items that qualify as Common Equity Tier 1 items.

6. Where the investment firm or institution issuing the instrument has established that the Common Equity Tier 1 ratio has fallen below the level that activates conversion or write-down of the instrument, the management body or any other relevant body of the investment firm or

institution issuing the instrument shall be required to determine without delay that a trigger event has occurred and there shall be an irrevocable obligation to write down or convert the instrument.

7. The aggregate amount of instruments that are required to be written down or converted upon the occurrence of a trigger event shall be no less than the lower of the following:

(a) the amount required to fully restore the Common Equity Tier 1 ratio of the investment firm or institution issuing the instrument to the percentage set as the trigger event in the provisions governing the instrument;

(b) the full principal amount of the instrument.

8. Where a trigger event occurs:

(a) the investment firm shall inform the staff members who have been awarded the instruments as variable remuneration and the persons who continue to hold such instruments;

(b) the investment firm or institution issuing the instrument shall write down the principal amount of the instruments, or convert the instruments into Common Equity Tier 1 instruments as soon as possible and within a maximum period of one month in accordance with the requirements laid down in this Article.

9. Where Additional Tier 1 instruments, Tier 2 instruments and Other Instruments include an identical trigger level, the principal amount shall be written down or converted on a pro rata basis to all holders of such instruments which are used for the purposes of variable remuneration.

10. The amount of the instrument to be written down or converted shall be subject to independent review. That review shall be completed as soon as possible and shall not create impediments to write down or convert the instrument.

11. An investment firm or institution issuing instruments that convert to Common Equity Tier 1 on the occurrence of a trigger event shall be required to ensure that its authorised share capital is at all times sufficient to convert all such convertible instruments into shares if a trigger event occurs. The investment firm or institution shall be required to maintain at all times the necessary prior authorisation to issue the Common Equity Tier 1 instruments into which such instruments would convert upon the occurrence of a trigger event.

12. An investment firm or institution issuing instruments that convert to Common Equity Tier 1 on the occurrence of a trigger event shall be required to ensure that there are no procedural impediments to that conversion by virtue of its incorporation or statutes or contractual arrangements.

13. In order for the write-down of an instrument to be considered temporary, all of the following conditions shall be met:

(a) write-ups shall be based on profits after the issuer of the instrument has taken a formal decision confirming the final profits;

(b) any write-up of the instrument or payment of coupons on the reduced amount of the principal shall be operated at the full discretion of the investment firm or institution issuing the instrument subject to the constraints arising from points (c), (d) and (e) and the investment firm or institution shall not be obliged to operate or accelerate a write-up under specific circumstances;

(c) a write-up shall be operated on a pro rata basis among Additional Tier 1 instruments, Tier 2 instruments and Other Instruments used for the purpose of variable remuneration that have been subject to a write-down;

(d) the maximum amount to be attributed to the sum of the write-up of Tier 2 and Other Instruments together with the payment of coupons on the reduced amount of the principal shall be equal to the profit of the investment firm or institution issuing the instrument multiplied by the amount obtained by dividing the amount determined in point (i) by the amount determined in point (ii):

(i) the sum of the nominal amount of all Tier 2 instruments and Other Instruments of the investment firm before write-down that have been subject to a write-down;

(ii) the sum of own funds and of the nominal amount of Other Instruments used for the purpose of variable remuneration of the investment firm;

(e) the sum of any write-up amounts and payments of coupons on the reduced amount of the principal shall be treated as a payment that results in a reduction of Common Equity Tier 1 and shall:

(i) be consistent with the maintenance of a sound capital base of an investment firm and, if applicable,

(ii) its timely exit from extraordinary public financial support and shall be limited to a portion of net revenue when the investment firm benefits from extraordinary public financial support.

14. For the purposes of point (d) of paragraph 13, the calculation shall be made at the moment when the write-up is operated.

Article 6

Alternative arrangements

Alternative arrangements that may be used by investment firms for the pay out of variable remuneration under point (k) of Article 32(1) of Directive (EU) 2019/2034 subject to the approval of the competent authority shall comply with all of the following conditions:

(a) the alternative arrangement contributes to the alignment of the variable remuneration with the long-term interests of the investment firm, its creditors and clients;

(b) the alternative arrangement is subject to a retention policy designed to align the incentives of the individual with the longer-term interests of the investment firm, its creditors and clients, the retention period shall be at least six months;

(c) the amount received under an alternative arrangement and the applicable conditions are well documented and transparent to the staff member receiving variable remuneration under such an arrangement;

(d) for amounts received under deferral and retention arrangements the alternative arrangement ensures that staff cannot access, transfer or redeem the deferred part of variable remuneration during such periods;

(e) the alternative arrangement does not foresee the increase of the value of the variable remuneration received during deferral periods by interest payments or other similar arrangements other than by arrangements that fulfil the conditions under point (f);

(f) 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) where deferral and retention have to be applied, 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 under (i) of point (f) 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 under (i) of point (f) is based on the credit quality of the investment firm, the percentage of value change should be limited to the percentage of the annual total gross revenue in relation to the investment firms total own funds;

(g) the alternative arrangement does not hinder the application of point (m) of Article 32(1) of Directive (EU) 2019/2034.

Article 7

Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union. It shall apply from […]. This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Commission
The President

[For the Commission
On behalf of the President

[Position]

4. Accompanying documents

4.1 Cost-benefit analysis / impact assessment

1. Article 10(1) of the EBA Regulation provides that before any draft regulatory technical standards developed by the EBA are submitted to the Commission for adoption the EBA should analyse 'the potential related costs and benefits'. This analysis is to provide an overview of the findings regarding the problem to be dealt with, the solutions proposed and the potential impact of these options.

A. Problem identification

1. Commission Delegated Regulation (EU) No 527/2014 of 12 March 2014 supplementing Directive (EU) No 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the classes of instruments that adequately reflect the credit quality of an institution as a going concern and are appropriate to be used for the purposes of variable remuneration has been applicable to investment firms and credit institutions.
2. A specific framework on remuneration requirements has been created for certain investment firms in the IFD. Investment firms to which those provisions apply must use the instruments specified in point (j) of Article 32(1) of the IFD or alternative arrangements in point (k) of Article 32(1) of the IFD for the pay out of a part of the variable remuneration to staff whose professional activities have a material impact on the risk profile of the investment firm or of the assets that it manages.
3. The draft RTS have been mandated under the requirement laid down in Article 32(8) of the IFD that requires that the EBA, in consultation with ESMA, shall develop draft regulatory technical standards to specify the classes of instruments that satisfy the conditions set out in point (j)(iii) of paragraph 1 and to specify possible alternative arrangements set out in point (k) of paragraph 1.

B. Policy objectives

4. The present draft RTS should, in line with the mandate in Article 32(8) of the IFD, specify the additional Tier 1 instruments or Tier 2 instruments or Other Instruments which can be fully converted to Common Equity Tier 1 instruments or written down, and that adequately reflect the credit quality of the investment firm as a going concern and where an investment firm does not issue any of the instruments referred to in point (j)(iii) of Article (32(1) of the IFD, the alternative arrangements fulfilling the same objectives that may be approved by competent

authorities in derogation of point (j) of Article (32)(1) of the IFD where an investment firm does not issue any of the instruments referred to in that point.

5. The specified instruments and alternative arrangements should ensure, together with other remuneration requirements, that the variable remuneration of staff whose professional activities have a material impact on the risk profile of the investment firm or of the assets that it manages is aligned with the risk profile of the investment firm or the assets its manages.

6. The RTS should not lead, within the restrictions set by the IFD, to instruments or alternative arrangements that are overly burdensome to create and use for the purpose of variable remuneration and respect the principle of proportionality.

C. Baseline scenario

7. The baseline scenario for the present impact assessment is set by points (j) and (k) of Article 31 (1) of the IFD and Commission Delegated Regulation (EU) No 527/2014 of 12 March 2014 supplementing Directive (EU) No 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the classes of instruments that adequately reflect the credit quality of an institution as a going concern and are appropriate to be used for the purposes of variable remuneration that is currently applicable to investment firms.

D. Options considered

Option 1 - Conditions for instruments under point j(iii) of Article 31 (i) of the IFD

Option A: Maintaining the provisions in the current RTS No 527/2014 of 12 March 2014.

8. No material change to the current framework would ensure that investment firms that currently use such instruments will be able to do so also in the future and therefore no additional implementation costs would be created. In particular, the possibility of using instruments under certain conditions that are issued by parent undertakings limits the costs.

Option B: Setting a different framework for such instruments.

9. Given that the framework in existence has been applied since 2014, any material deviation from existing provisions would create an additional burden for investment firms in creating instruments. Setting softer conditions, e.g. with regard to the level of the trigger event, would lead to an un-level playing field between investment firms and credit institutions and would lead to challenges if instruments issued by the parent undertaking would be used for the pay out of variable remuneration. With regard to other conditions, e.g. for the definition of write down or conversion, the IFD refers to CRD provisions and therefore no material differentiation of instruments compared to the instruments defined under Commission Delegated Regulation (EU) No 527/2014 of 12 March 2014 was possible.

Option A has been retained

Option 2 – Conditions for alternative arrangements

10. Alternative arrangements require the approval of the competent authorities and the approval is subject to the condition that an investment firm does not issue any of the instruments referred to in point (j) of Article 31(1) of the IFD.

Option A: Setting conditions for alternative arrangements that ensure that they meet the same objectives 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).

11. Given the limitation that alternative arrangements can only be approved for investment firms that do not issue any of the instruments under point (j) of Article 31 of the IFD, any requirement to create another specific financial instrument would lead to an additional implementation burden. Considering the nature, size and complexity of investment firms that are subject to the specific remuneration framework under the IFD this could create material costs. Also, requiring specific forms of deferred cash to be held on frozen accounts might be more burdensome than other possible alternative arrangements. Given that so far no alternative arrangements have been observed, a high level of flexibility would ensure that the implementation costs and burdens are kept low. The regulatory objectives will be achieved by defining the conditions that have to be met in order to ensure that the alternative arrangement is appropriate for the use of paying out variable remuneration of identified staff. The conditions set should ensure that other requirements such as deferral or malus can be applied, when the institution is not benefitting from the waiver under Article 32(4) of the IFD.

Option B: Specifying other financial instruments that ensure that the alternative arrangement would meet the same objectives as the pay out of variable remuneration in instruments.

12. As explained above, requiring specific financial instruments would increase the implementation burden without necessarily improving the alignment of variable remuneration with risks.

Option A has been retained

E. Overall impact of the draft RTS

13. Considering that investment firms that are subject to the IFD have several instruments available for the pay out of variable remuneration to identified staff and the available waivers that may be implemented by Member States and given that the existing framework for the use of Additional Tier 1 instruments or Tier 2 instruments or Other Instruments which can be fully converted to Common Equity Tier 1 instruments or written down and that adequately reflect the credit quality of the investment firm as a going concern has been retained and that the requirements for alternative arrangements have been kept as flexible as possible to ensure the objectives set in IFD, the draft RTS would create only a minor cost impact for investment firms

that use such instruments or arrangements for the pay out of variable remuneration for identified staff.

4.2 Summary of responses to the consultation and the EBA's analysis

Altogether the EBA received 15 responses. Eleven of these have been published and four responses were submitted confidentially.

Given the fact that most investment firms are currently subject to a similar framework under Directive 2013/36/EU, the comments received were limited. In particular, respondents suggested that a more proportionate framework for the award of variable remuneration in instruments should be applied. Most comments concerned the provisions on alternative arrangements. Overall, it was felt that the provisions relating to alternative arrangements were too prescriptive.

The IFD already allows for a high level of flexibility and leaves it to investment firms to establish which of the eligible instruments they use for the award of variable remuneration. The instruments specified in the RTS are only a subset of the wide range of eligible instruments defined in Article 32(1)(j) of the IFD. Moreover, the specific IFD provisions on remuneration do not apply to small and not interconnected investment firms. The IFD also contains waivers for the requirement to pay out variable remuneration for smaller investment firms. Article 6 on alternative arrangements has been reviewed in order to provide more clarity on its application.

The feedback table below contains a summary of the responses received, limited to responses received that concern the draft RTS on instruments.

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
General comments			
Mandatory use of instruments	Several respondents asked to consider the burden and to reduce the likelihood that firms would be forced to issue instruments to be used purely to pay out variable remuneration.	The use of instruments for the purposes of variable remuneration is a requirement under the IFD (at least 50% of the variable remuneration), unless waivers are applied in accordance with Article 32(4) of the IFD. Different types of instruments are available, as set out in point (j) of this Article. The RTS does not contain a requirement to use a specific instrument, it allows, under certain conditions, the use of already issued instruments.	Article 6 clarified
Use of different types of instruments and alternative arrangements Article 6	Several respondents noted that a number of the provisions of Article 6 are drafted relatively prescriptively, asked for more flexibility and suggested that different types of instruments should be allowed in order to reflect the diverse legal structures of investment firms, such as shares (or equivalent ownership interests) and share-linked instruments (or equivalent non-cash instruments) and other arrangements that effectively allow aligning the interests of staff with other stakeholders' longer-term interests, and help to align variable remuneration with the risk profile of the firm. One of them pointed out that the current provisions are too narrow because they presuppose the issuance of an equity-like instrument for remuneration purposes, which could be too burdensome especially for small firms.	Article 32(1)(j) of Directive (EU) 2019/2034 (IFD) provides for several types of instruments that can be used for the pay out of variable remuneration. The use of alternative arrangements can only be approved in accordance with Article 32(1)(k) of the IFD where investment firms do not issue any of the other eligible instruments. If there are other instruments issued, investment firms cannot use alternative arrangements. For many investment firms it might not be necessary to pay out any variable remuneration in instruments or under alternative arrangements, if the benefit from the waivers set down in Article 32(4) of the IFD is implemented under national law. The criteria listed in this RTS allow competent authorities to assess whether the alternative arrangements implemented	Article 6 clarified

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
		by firms are appropriate and ensure a harmonised application of requirements.	
Implementation date	Many respondents suggested that it would be better to provide an option for firms to apply this RTS from the start of the accounting period/year-end, following the date of adoption of the IFR/IFD, in order mitigate the administrative burden of having to divide an administrative year in half for remuneration purposes, especially for performance-linked remuneration structures.	The provisions of the IFD should apply from 26 June 2021, including the requirement to pay out variable remuneration in instruments. The same principle applied under Directive 2013/36/EU (CRD), but the IFD provides for more flexibility in this regard. Currently, the same 'other instruments' are available to investment firms. The award of variable remuneration occurs after the end of the performance period under the legal framework applicable at that time. The EBA's mandate is limited to developing draft regulatory technical standards to specify the classes of instruments that satisfy the conditions set out in point (j)(iii) of paragraph 1 and to specify possible alternative arrangements set out in point (k) of paragraph 1. The entry into force will be determined by the publication of the RTS in the Official Journal.	No change
Responses to questions in Consultation Paper EBA/CP/2020/08			
Question 1			
Dividends on awarded instruments	A few respondents commented on the point that dividends or interest must not be paid on deferred remuneration in the form of instruments (recital 10). This could create a potentially significant	Investment firms should not pay out to staff any interest or dividend on instruments which have been awarded as variable remuneration during deferral periods as the staff members only become the legal owners of the instrument	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	misalignment of interest with shareholders, investors or other stakeholders. The respondent suggested amendments of both the EBA's Guidelines on the CRD IV remuneration requirements, the CRD V regime, and IFD on this point.	after vesting. For the same reason, interest and dividends payable during the deferral period should not be paid to staff after the deferral period ends. If the investment firm held the instrument during the deferral period, these payments should be treated as received and owned by the investment firm.	
Award in instruments	Another respondent stated that under Article 32(1)(j)(iv) of the IFD, which states that at least 50% of variable remuneration can consist of 'non-cash instruments which reflect the instruments of the portfolios managed', firms are allowed to use existing fund deferral arrangements as provided for under the UCITS Directive. The overlap in the staff identified under multiple regimes (e.g. UCITS and the new prudential regime for investment firms) requires the ability to use the same instruments to award remuneration under deferral arrangements. This respondent further suggested that, where an investment firm has unquoted shares but the parent does have quoted shares, the latter could be used as instruments for variable remuneration.	Investment firms, unless they are small and not interconnected, have to comply with IFD remuneration requirements. Similar remuneration requirements also apply under the UCITS Directive and AIFMD. Therefore, there is a level playing field for all such firms. The RTS only covers the mandate given to the EBA and does not set conditions for the use of shares, share linked instruments or non-cash instruments which reflect the instruments of the portfolios managed. Where investment firms are stock companies, it should be possible to use shares or share-linked instruments rather than using AT-1, Tier 2 or other instruments. The same applies for non-cash instruments which reflect the instruments of the portfolios managed. Regulation (EU) 2019/2034 in conjunction with Regulation (EU) No 575/2013 enables Additional Tier 1 and Tier 2 instruments issued through an entity within the scope of consolidation to form part of an investment firm´s own	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
		funds subject to certain conditions. Therefore, it should also be possible to use such AT-1 and Tier-2 instruments for the purpose of variable remuneration, provided that there is a clear link between the credit quality of the investment firm using these instruments for the purpose of variable remuneration and the credit quality of the issuer of the instrument.	
Article 1 Classes of instruments that adequately reflect the credit quality of an institution as a going concern and are appropriate to be used for the purposes of variable remuneration	One respondent asked whether the review under Article 1 point 2(e) is intended to be annual, in line with variable remuneration being awarded, such a frequency would be too burdensome. The respondent suggested the introduction of a *de minimis* threshold based on total assets.	The review should be done every time there is a new award of variable of remuneration partly paid out in such instruments. This is necessary to ensure that the intended value of remuneration is awarded. Current remuneration practices show that in most cases different instruments (e.g. share linked instruments) are used for remuneration awards. Where AT-1 or Tier-2 instruments are awarded, in many cases a market price is available.	No change
Article 4 Conditions for classes of Other Instruments	One respondent argued Article 4 point 2(a) is too burdensome for unlisted firms with total assets of over EUR 100 million for three reasons: 1) a credit rating for the underlying firms issuing the instruments and a requirement for them to be independently assessed; 2) triggering event provisions (paragraph 2	The IFD requires the EBA to develop draft RTS to ensure that instruments are appropriate to be used for the purposes of variable remuneration, that they can be fully converted or written down and in each case adequately reflect the credit quality of the investment firm as a going concern.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	of Article 4); and 3) periodic independent review required under point (e) of paragraph 2 of Article 1. This respondent also proposed to create a threshold of total assets at a higher level for the application of these conditions, so that the conditions apply in a proportionate manner. Finally, this respondent also noted that a significant number of investment firms currently do not have and do not need a credit rating, other than for the purposes of this regulation, raising cost-benefit issues.	The threshold is established in the IFD. Article 32(5) allows Member States to increase the threshold under certain conditions. It must also be considered that investment firms may additionally use other instruments for awarding variable remuneration. The draft RTS does not require that a credit rating be provided by a rating agency. As explained in the consultation paper, the draft RTS uses the term 'credit quality', which may be measured by different means, e.g. using a rating, spreads or capital ratios.	
Question 2			
Redemption period	One respondent suggested that, according to Articles 52 and 63 of the CRR, one of the conditions that needs to be met for instruments to be regarded as good capital from a Tier 1 or Tier 2 perspective is a redemption period of no less than 5 years. Allowing small investment firms a 3-year deferral of variable remuneration, for instruments held, would breach this condition unless the deferral is extended to 5 years. The respondent suggested avoiding such a mismatch so that a 3-year redemption is applied.	The EBA is not empowered to change the provisions regarding the redemption period for AT1 or AT2 instruments and their eligibility as own funds instruments. It is possible to use such instruments also for the award of variable remuneration with a deferral period of less than 5 years. Staff could, after the vesting and retention periods, sell the instruments received.	No change
Question 3			

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Carried interest	One respondent was concerned that some remuneration arrangements, in particular carried interest arrangements, while invariably designed to contribute to the alignment of variable remuneration with the risk profile of the firm, would not be considered acceptable under the new regulation because of the number and prescriptiveness of the provisions in the draft Article 6, and requested a shorter, more principles-based, set of criteria.	Carried interest within the meaning of Article 4(1)(d) of Directive 2011/61/EU is considered to be remuneration and is subject to the IFD remuneration requirements including the pay out in instruments. During deferral periods, staff do not own the instrument and therefore do not receive interest payments. Interest payments during such periods would also reduce the risk alignment and contradict the principle that variable remuneration should not vest faster than on a pro rata basis. In any case, alternative arrangements can only be approved if no other instruments listed under point (j) of Article 32(1) of the IFD are issued.	No change
Article 6 Alternative arrangements	One respondent considered that the conditions set out in draft Article 6 are too narrow, because they assume the issuance of an equity-like instrument, in that they contemplate deferral and retention of the amounts of variable remuneration received (which is duplicative of the independent requirement in Article 32(1)(l) of the IFD), and specify a minimum retention period of at least six months. Article 6 assumes that value will be measured annually, prohibits growth in value, and prohibits the transfer of the part of variable remuneration paid in instruments. Consequently, the respondent suggested removing Articles 6(b), 6(d), 6(e), 6(f) and 6(g)(ii)(iv) and (v).	Article 6 does not require an equity like instrument. On the contrary, if another eligible instrument would be issued, no alternative arrangements can be approved by the competent authority. An alternative arrangement should in the same way lead to a risk alignment of the variable remuneration as an award in instruments. Therefore, similar conditions need to be applied, e.g. to deferred cash that is kept on a specific account and can only be paid out after a fictive retention period has passed after vesting.	Article 6 clarified

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Article 6 Alternative arrangements	One respondent considered it would be useful to provide concrete examples of alternative arrangements where an investment firm does not issue any of the listed instruments in Article 32(1) and does not manage assets. For instance, they asked about the possibility of using an instrument that is partially indexed to the financial result of the parent company.	The mandated RTS will, after adoption, be directly applicable, examples cannot be provided in the RTS. Please refer to the above for one example of an alternative arrangement.	No change
Article 6 Alternative arrangements	One respondent suggested that the EBA could grant national competent authorities the right to provide blanket consent for the use of alternative arrangements where the variable remuneration reflects the performance of assets managed by the firm without the firm being required to obtain individual approval for such arrangements from their national competent authorities.	The RTS only sets out the conditions for such alternative arrangements, but not the process in which they can be approved. A general approval of certain arrangements by competent authorities would be possible, if the national law allows for this. As explained in recital 15 and set out in point (k) of Article 32(1) of the IFD, such arrangements can only be used by investment firms that do not issue any of the instruments listed under point (j) of Article 32(1) of the IFD.	No change
Article 6(a)	One respondent suggested adding '…to the alignment of the variable remuneration with the risk profile of the investment firm <u>and/or its clients</u>.'	The comment has been accommodated and the text has been aligned with Article 32(3) of the IFD. '… longer-term interests of the investment firm, its creditors and clients.'	Article 6 amended
Article 6 (b)	One respondent pointed out that deferrals do not apply for every investment firm and there are exemptions set down in the IFD/IFR based on thresholds, and therefore this cannot be a criterion applying for every firm.	The IFD establishes that the remuneration practices and, in particular, the variable remuneration should be aligned with the risk profile of the investment firm or the assets it manages. Point (b) of Article 6 has been amended.	Article 6 amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	Another respondent considered that is was not necessary for Article 6 to reference the operation of deferral and retention, as this is a matter covered by the IFD itself, and these references in the RTS would appear to risk further restricting the degree of flexibility that is intended to be afforded by the concept of alternative instruments.	Where waivers are applied, investment firms will likely benefit from both, a waiver of the deferral requirement and a waiver of the requirement of paying variable remuneration in instruments. However, there are situations where an investment firm is subject to the deferral requirement but has not issued any of the instruments under point (j) of Article 32(1) of the IFD.	
Article 6 (e)	One respondent requested more guidance on the scenarios where a retention period longer than 6 months would be expected to be used and how long it would be likely to be considered appropriate in these circumstances, favouring an approach whereby firms are able to establish their own longer retention periods based on their individual circumstances, risk horizon and the way in which their compensation is calculated.	An alternative arrangement should in the same way as instruments under point (j) of Article 32(1) IFD lead to an alignment with the longer-term interests of the investment firm, its creditors and clients. The 6-month period is a minimum period. Depending on the business cycle, longer deferral or retention periods than the minimum periods may be appropriate for some identified staff or in general. The EBA is due to issue guidelines on remuneration policies under the IFD that provide further clarity on the application of remuneration requirements.	No change
Article 6(g)	Several respondents considered items (iv) and (v) of this article too prescriptive, and some directly requested their removal. They see a need for improvement related to the proposed alternative arrangements based on the performance of the managed assets or the investment firm. They considered that limiting the performance-based variable remuneration to the percentage of value change of the managed assets or to the percentage of	The provisions allow investment firms to define approaches within the alternative arrangements that allow them to change the value of remuneration. This is equivalent to price changes of instruments awarded. Such approaches are not mandatory but contribute to the risk alignment of variable remuneration that must be achieved. However, where such approaches are applied, certain conditions must be met. Such conditions do not limit the requirement regarding the application of malus or claw-back.	Article 6 has been clarified

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	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.		
Article 6(g)	Two respondents considered Article 6(g)(i) to be too restrictive and that because of the different types of investment firms the definition of 'credit quality' is inappropriate and should be replaced by 'risk profile' in Articles 6(g)(i) and 6(g)(v) as in Article 6 (a). Another option suggested was to create a new paragraph (vi) to add criteria based on the financial result, or directly removing item (i).	The wording of the RTS is consistent with the wording used under the IFD. As explained above, credit quality can be measured using different approaches. The approach taken allows for a high level of flexibility.	The provisions have been clarified
Question 4			
Impact assessment	Several respondents pointed out that the implementation of new provisions relating to instruments are likely to significantly increase the administrative burden for investment firms which are currently not covered by the remuneration requirements of the CRD, and the administrative resource requirements for multiple disciplines as consequence of new requirements such as additional requirements for deferral administration systems, separated allocation processes during year-end	Currently, investment firms are subject to the CRD and the corresponding RTS on instruments. New requirements are only added to the RTS with regard to alternative arrangements. The remuneration requirements under the IFD apply to investment firms unless they are small and not interconnected in accordance with Article 25 of Directive (EU) 2019/2034.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	compensation cycles and extensive internal communication activities.	The legislator has already assessed the impact of the IFD on investment firms. It should be mentioned that the legislator has also established several waivers under specific conditions in accordance with Article 32 (4) of the IFD to reduce the regulatory burden.	