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UNI Europa Finance reply to the consultation on draft regulatory technical standards on criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile under Article 90(2) of the proposed Capital Requirements Directive

Introduction

UNI Europa Finance welcomes the consultation on the criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile.

In April 2009, the predecessor of the EBA, the Committee of European Banking Supervisors (CEBS), published a first set of principles on remuneration policies and practices, followed by formal Guidelines by the end of 2010. A survey on the implementation of the Guidelines on Remuneration Policies performed by the EBA in April 2012 showed that material inconsistencies pertain and the discrepancies between the definitions of "identified staff" (staff that has material impact on risk taking) make comparisons between institutions difficult. The EBA also stated that if "the potential variable remuneration is greater than the fixed one, this could incentivise staff to take too much risk in order to assure a certain minimum pay level." In the BSG meeting of April 2012, UNI Europa Finance made a written statement in support of this initiative, it is important to address incentive schemes as they can work to destabilise the financial sector.

The final text of the CRD4 was published on 27 June, 2013 in the Official Journal. Several important changes had been made concerning remuneration policies, notably the introduction of a ratio of 1:1 between fixed and variable pay (with some flexibility to increase the ratio until 1:2 with shareholder approval). In Article 94.2.(ii) of CRD4, the EBA is requested to develop adequate standards to specify criteria to identify categories of staff whose activities have a material impact on risk taking.

General remarks

The categories of staff are described in Article 92.2.: "senior management, risk takers, staff engaged in control functions and any employee receiving remuneration that takes them into the same remuneration bracket as senior managers and risk takers whose professional activities have a material impact on their risk profile". The EBA has set out three types of criteria: internal, qualitative and quantitative. Given the diversity of the European banking sector, the exercise is not an easy one, as national differences, the particularities of smaller banks and SIFIs have to be taken into account at the same time.

Therefore, some criteria are based on percentages of key figures of the different institutions in order to be proportionate (i.e. credit risk exposure of 0.25% of common tier one). In this case, big institutions can engage huge risks, whereas smaller institutions must report their personnel for sums which are much smaller.

Others are in absolute terms (fixed remuneration of above 500 000 EUR and variable remuneration of above EUR 75 000).

In order to ensure an international level playing field, UNI Europa Finance welcomes the fact that the criteria shall be applicable both in EU and in subsidiaries established in third countries. Given the international nature of big banking groups, this is an important item to be added in order to ensure a harmonised identification of staff.

However, in general, the number of criteria in this proposal is presently too high: some criteria are likely to produce overlaps and catch employee categories that should not be included: for example Article 3.1.a-d relates to a more exclusive group than Article 3.1.e onwards where potentially not only senior management, but also middle management is included. This is even multiplied by Article 3.3, which includes potentially all staff in relation to risk functions.

UNI Europa Finance supports the idea of remuneration policies and practices that are consistent with and promote sound and effective risk management. Although for remuneration policies the absolute primacy of collective agreements must be respected.

Recital 69 in CRD4 reads: *The provisions on remuneration should be without prejudice to the full exercise of fundamental rights guaranteed by Article 153(5) of the TFEU, general principles of national contract and labour law, legislation regarding shareholders' rights and involvement and the general responsibilities of the management bodies of the institution concerned, as well as the rights, where applicable, of the social partners to conclude and enforce collective agreements, in accordance with national law and customs.*

It must thus be made clear that any legal provisions regarding remuneration do not apply to remuneration policies and provisions agreed in a collective agreement. An explicit reference to recital 69 should be included in the RTS.

As a basic principle, the possibility for collective bargaining should not be hampered by the inclusion of too vast a number of employees, including those in middle management functions which are not immediately concerned by risk taking.

Specific remarks¹

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

The qualitative criteria listed in Articles 3.1.e-j, combined with 3.3 and 3.2.b give leeway for too broad an interpretation of the list of employees in scope.

The functions listed in Article 3 of the draft RTS include support, expert and advisory functions, with staff in lower income brackets than staff in commercial or front office functions. However, it may be that the head of such a department is in the designated income brackets.

Although found at mid-management level, their remuneration, status and power within the institutions remain inferior to the one of senior management and their recommendations were often disregarded prior to the crisis. It should be ensured that including support functions in the list of identified personnel will not be used to dilute responsibility from the commercial risk takers in support and control functions. As an example: it should be avoided that control and support staff should be responsible for the actions of a rogue trader who manipulates market figures.

Recital 7 of the RTS specifies that functions providing infrastructure and internal support crucial to the operation of the business may be considered as identified staff. For market activities, these functions may include IT functions, which are very often outsourced to separate firms and located all over the world, i.e. in India, Morocco, etc. Including those outside firms in the RTS may prove difficult. A possibility would be to include relevant staff responsible for the outsourced project inside the institution in the scope of the criteria.

¹ Quotes from the Draft Technical Standards are in framed boxes.

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

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

When taking an example with real world figures out of the 30 biggest banks 0.25% of an institutions common tier 1 equity may involve the following amounts:.

- Example 1: Eur 50 Md * 0.25% = Eur 125 000 000
- Example 2: Eur 90 Md * 0.25% = Eur 225 000 000

For smaller or mid-sized institutions this could drop significantly:

- Example 3: Eur 16 Md* 0.25% = Eur 40 000 000

These amounts are quite common for a single transaction in the credit market.

It would aim at a group of risk managers or the relevant credit committees with large delegations. The above mentioned staff may be easily identified (according to the delegation level they have, which should be easily available), but the choice is not necessarily relevant. Depending on the internal organisation and the internal delegation rule of the institution, it would include risk managers, senior management, possibly also middle management and in addition, in terms of Article 3.3, also employees that advise and sit on credit committees (see general remarks).

Neither would this criterion be appropriate for dealers, who typically work with limits set by the institution. The criterion respects the proportionality principle but may in some cases and combined with other criteria catch staff who is not necessarily a risk taker as such but only advising in risk functions.

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

- i. where the standardised approach is used, an own funds requirement for market risks of 0.25% or more of the institution’s Common Equity Tier 1 capital;
- ii. where an internal model based approach is used, 5% or more of the institution’s internal value-at-risk limit for trading book exposures at a 95th percentile, one-tailed confidence interval level; “

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

Market risks are usually valued according to VAR consumption. 5% of VAR consumption therefore seems like quite a high amount. However, as under Q2, it is possible that this catches employees in risk functions, who are middle management (e.g. senior risk analysts). Combined with Article 3.3.a, if this would also refer to people who merely advise the committee (e.g. a risk manager or credit analyst), it could be too broad.

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

- i. 75% of the fixed component of remuneration;
- ii. EUR 75 000;”

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

Having the difference in wage levels throughout the EU in mind, we are in favour of the threshold. In the case it catches employees who are not material risk takers, Article 4 permits an exemption for those persons falling under the criterion and who are not material risk takers.

The relative/percentage threshold of 75%, is below the threshold for a maximum variable remuneration given in the directive (unless shareholder approval for up to 200%). The threshold is valid if average variable remuneration is much lower (e.g. this is the case in French investment banks, where it is on average just above 30% for employees in the highest classifications, hors classe). In trading rooms, for identified staff, this can be much higher.

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

Even if a specific pay level per se does not equal risk-taking, the alternative to identify staff solely based on function may prove difficult. This is due to the great number of job titles, department names and functions in and across EU member states and banks.

The biggest advantage of the application of these criteria is its easiness. However they present several disadvantages: First, they may easily be avoided when companies may find ways around them (e.g. when the first restrictions were put in place under CRD3, banks increased the salaries of some categories of staff). Second, as payment levels differ widely in the EU², and these criteria may catch a great number of employees in some countries with proportionally large financial markets and almost none in others. Third, fixed thresholds are bound to be revised in the future, depending on the general development of pay structures. Then, if feasible, a focus should also be put on the function of staff, rather than solely focusing on pay.

Q4 c) What would be the number of staff members identified in addition to all other criteria within the RTS?

As said before, the combined criteria, especially with Article 3.3, may catch too vast a number of employees which are not necessarily risk takers. It is difficult to estimate the total number, but with a broad interpretation of articles 3.2.e-j and 3.3 it could roughly range between 5-25% of total staff.

Q4 d) What would be the additional costs of implementation for the above criterion if an institution applies Article 4 in order to exclude staff from the group of identified staff?

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

Q5 a) Can the above criterion be easily applied?

Application of the criterion may prove tricky. For the first one, it depends on the definition of senior management in an institution – this may be easily applicable if, for example senior management includes only the board of directors (but generally the definition is wider). In addition, the word “entity” may need a definition: is it meant to be a credit institution as such (e.g. a whole subsidiary) or a department, or a sub-division of a department?

The second one is even more difficult as there are a number of functions listed in article 2. For the second one, the human resources department needs statistics about remuneration levels sorted by department and function. A sorting by function can prove difficult as in many countries and businesses functions are defined in a granular fashion, which permanently changes and evolves.

² According to Eurostat, average gross annual earnings in the business economy ranged from EUR 4.668 to 60.002 in the EU countries in 2011, (full-time employees).

Article 3(2)b. has a huge multiplication effect and will include middle management who is not necessarily a risk taker as such.

Remuneration is a good reference which could potentially narrow down the range of people who are included in the functional criteria if these are too broad.

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

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

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“the staff member has been awarded total gross remuneration of EUR 500 000 or more in one of the two preceding financial years. “

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

It is possible that the criterion includes employees that are not material risk-takers (as spelled out under Q4b) but we believe it to be an objective criterion. As it refers to an absolute level it is also likely to be revised if salary structures evolve.

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

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

This criterion may have a weakness, very often, trading activities are done in subsidiaries of SIFIS and these subsidiaries do not have staff levels in the tens of thousands range.

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

- a. staff who are responsible for advising on or initiating such commitments or decisions;
- b. staff who are members of a committee which has authority to make such commitments or to take such decisions. “

This paragraph (Article 3.3 a and b) may potentially include a wider range of staff members including those who are insignificantly related to risk taking in the sense meant by CRD4. We believe that this criterion may be interpreted in such a broad way that it includes middle management, senior advisors and experts, in short, potentially between 5-25% of all staff in some banks.

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

Some important measures such as bonus clawback and deferral and the use of specific, equity-related instruments are already included in the directive. Additional criteria could include, inter alia: performance measures and compensation structures that include social and environmental criteria.

About UNI Europa Finance

UNI Europa Finance is the European-level trade union body for the finance sector. It represents 100 unions with 1.5 million workers in the banking and insurance industries. It is part of UNI Global Union and recognised by the European Union as a social partner. UNI Europa Finance is also part of UNI Europa, representing 7 million workers in the services and communication sectors. UNI Europa is member of the ETUC.