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June 4, 2015

Comments on Consultation Paper
Draft Guidelines on sound remuneration policies under Article 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013
issued by the European Banking Authority

Japanese Bankers Association

We, the Japanese Bankers Association (“JBA”), would like to express our gratitude for this opportunity to comment on the consultation paper: *Draft Guidelines on sound remuneration policies under Article 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013* issued on March 4, 2015 by the European Banking Authority (“EBA”).

We respectfully expect that the following comments will contribute to your further discussion.

<General Comment>

We recongnise the necessity of establishing guidelines to ensure financial institutions have sound remuneration policies.

It is however respectfully requested to consider that excessive regulations on remuneration would increase difficulty for financial institutions to attract and retain competent talent, and might undermine the quality of financial intermediary service.

Additionally, in applying the proposed guidelines to EU branches of foreign banks outside of the EU, we request to establish a regulatory framework in a manner that takes into account actual remuneration practice at the home jurisdiction.

Our comments on specific issues are discussed in the Specific Comments below.

<Specific Comments> (Our responses to the questions>

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

(Our response)

Definitions provided are clearly defined, and hence further definitions are not required. However, while the December FX rate for the prior year is required to be used,

we would request that this is amended to the FX rate for the month for the financial institution's relevant year end (e.g. March for a 31st March year-end).

Question 2 *Are the guidelines in chapter 5 appropriate and sufficiently clear?*

(Our response)

Guidelines relating to remuneration policies for all staff, including those deemed as Material Risk Takers ("MRT"), are sufficiently clear. However, the following is requested:

Paragraph 15 mentions conflicts of interest regarding compliance with insider trading rules. As Regulation on Market Abuse, which will be implemented, does not refer specifically to issues with regard to remuneration, in finalising the guidelines, it is requested to illustrate some concrete examples on how remuneration practices could lead to market abuse.

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

(Our response)

Guidelines regarding shareholders' involvement in setting higher ratios for variable remuneration are generally clear.

While, for subsidiaries, an approval is generally required to be obtained from the direct shareholder (for example, a (intermediate) holding company), the proposed guideline requires an approval from shareholders of listed parent company. As a result, this requirement would place an onerous burden on the listed parent company and its subsidiary companies to obtain the consent from shareholders of the listed parent company. It is therefore requested to amend to require obtaining an approval only from the direct shareholder (a (intermediate) holding company).

Question 4 *Are the guidelines regarding remuneration policies and group context appropriate and sufficiently clear?*

(Our response)

Paragraph 68 sets forth that "branches of credit institutions having their head

office in a third country are subject to the same requirements as applicable to institutions within Member States.” It is requested to specifically indicate which rules and guidance apply to third country branches.

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

(Our response)

Our understanding is that use of "neutralization," or de minimus threshold, for deferral, pay-out in instruments and clawback will no longer be permitted.

However, this change in the approach (i.e. not allowing the use of “neutralization”) for deferral and clawback would have a significant negative impact on expatriates from Japan who are deemed to be the MRTs. It is therefore requested to permit “neutralisations” through exemptions applied in the EU member states for the following reasons.

Since exemptions exist, currently, there are no expatriates from Japan who had been subject to the rules. Since however some expatriates may be deemed as the MRTs, they might be subject to bonus pay out in stock or deferred payments. Additionally, if the use of "neutralisation" is not permitted, the number of identified staff would significantly increase, giving rise to concerns of, for example, an increase in fixed cost of financial institutions since they would be forced to take actions such as an increase in the ratio of fixed pay to total remuneration in order to address bonus caps and other factors.

Moreover, rules on the pay out in stock, deferral arrangements and other elements

differ from those rules established in Non-EU member states, which would cause an unlevel playing field between those working within the EU and those outside of the EU. For example, since the de minimus threshold is currently applied in the UK (the individual's total remuneration of no more than £500,000, and the individual's variable remuneration of 33% or less against their total remuneration), even those deemed as an MRT might not be deemed to be identified staff. Other many European countries have similar exemptions. Additionally, as the term of expatriates is in most cases short, burden for managing these expatriates would increase. Further, the implementation of the proposed guideline would discourage senior individuals in control functions to take on roles within financial services compared to other industries, thereby reducing the size of talent pool available for these positions.

Remuneration payments to Japanese expatriates (including those deemed as the MRTs) are made in accordance with the remuneration policy established both in Japan and the UK. However, under the remuneration structure and culture in Japan, unlike those in Europe and the U.S., bonuses are rarely heavily linked to performance. (*See <Remuneration Structure and Culture in Japan> below for details.*) As such, an exemption, if permitted, is unlikely to promote excessive risk taking activities by Japanese banks, given their current business models.

Finally, we would like to emphasize that not being able to apply the de minimus threshold would result in the "one size fits all" approach to treatment of identified staff, thereby disregarding the impact the different roles have on the risk profile of the firm.

< Remuneration Structure and Culture in Japan>

In general, the remuneration policy for Japanese employees is structured by the Human Resources Division (HRD) in the bank's Head Office, which assumes a similar role and function as a remuneration committee. The HRD in Head Office is independent from business promotion functions.

The remuneration policy in Japan is based on seniority, capability for work and Job Grade, with adjustments made for Group, Divisional and individual performance. Salary levels are determined by the amount stipulated by the employee's Job Position and Job Grade (fixed remuneration).

Additionally, their bonus structure differs from a "pure" performance linked bonus but rather is composed of the following two elements: the first is based on their Rank/Level/Job size of each individual and does not vary substantially as it is built through their career in the bank. This element therefore does not incur a significant difference in the amount bonus across employees. The second part is the performance linked portion. This in general varies by only approximately 5%.

As such, the variable amount from performance linked bonus is small and performance linked bonus forms a small proportion of the overall bonus (for example, 1.5% = 30% x 5%). Hence, there is a significant difference between applying deferral, pay-out in instruments and clawback on a multi-million pound bonus versus the same on ten thousands of pond bonus.

<Impact on small-sized financial institutions>

Removing de minimus threshold would require applying the identified staff remuneration structure rules to remuneration of all delegated MRTs and junior MRTs (such as 40-60% deferral, 50% share linked, retention period, claw-back).

While these changes have no material implication on cost implication, it penalises smaller firms where relatively junior and low paid staff are subjected to the MRT criteria. If de minimus threshold were no longer allowed, there is a concern that the ability of small-sized financial institutions, including subsidiaries, to attract and retain this junior level of identified staff would be harmed.

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

(Our response)

Expatriates from the Head Office (HO) may be captured in accordance with the new guidelines.

The requirement in paragraph 107 sets forth that third country branches should inform their headquarters of the results of the identification process. It is requested to indicate regulators' expectations of this notification process.

We also request to clarify whether bank branches should obtain an approval from the HO.

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

(Our response)

The guidelines are sufficiently clear.

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

(Our response)

The guidelines are appropriate and sufficiently clear.

Question 9
Are the requirements regarding allowances appropriate and sufficiently clear?

(Our response)

The guidelines are appropriate and sufficiently clear.

Whilst we understand the intention to restrict the use of allowances such that they constitute fixed pay, these provisions are likely to have the effect of increasing base salaries. Having increased base salaries would increase the fixed costs of the financial institutions. From business management perspective, we believe it would be better to have allowances where there is the ability to be able to withdraw or reduce the allowances.

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

(Our response)

The guidelines are sufficiently clear.

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

(Our response)

The guidelines are sufficiently clear.

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

(Our response)

While the provisions regarding personal hedging with respect to downward adjustment in variable remuneration are clear, further guidance is required regarding currency hedging.

The rules on some financial institutions' identified staff deferral plan state that the currency for the purpose of the deferral plan shall be in Yen. As such, the deferred Share Price Linked (SPL) amount is treated as follows: Sterling amount is converted to Yen, linked to the banking group's share price and converted back to Sterling for payment. Deferred variable remuneration for identified staff is therefore subject to currency fluctuation and identified staff may want to transfer FX risk through hedging. Consequently, further guidance is sought on the use of currency hedging within the scope of Capital Requirements Directive ("CRD").

Guidelines regarding circumvention are sufficiently clear.

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

(Our response)

The guidelines are sufficiently clear.

Question 14
Are the requirements on the risk alignment process appropriate and sufficiently clear?

(Our response)

The guidelines are not clear.

The examples given in paragraph 206 are for financial institutions that fall within the scope of CRD. It is requested to provide guidance on how remuneration for control staff should be set in third country branches.

Question 15
Are the provisions on deferral appropriate and sufficiently clear?

(Our response)

The provisions are not clear.

When setting rules on remuneration, an appropriate balance should be sought between limiting excessive remuneration and retaining high quality staff. We see little benefit in increasing minimum deferral requirements for senior managers from the current 3 years to 5 years, particularly within support and control functions in the context of limiting excessive remuneration. On the other hand, the increase in deferral could decrease the attractiveness of senior positions in the financial services industry compared to positions with similar levels of responsibility in other sectors and jurisdictions which are not subject to such rules. Additionally, 5 years may not necessarily align to all banks' practice.

Therefore, it is recommended that the 5 years could be utilised as a minimum unless a firm can demonstrate to the relevant regulator that their risk time horizon is less than 5 years, in which case a minimum of 3 years may be applied.

Question 16
Are the provisions on the award of variable remuneration in instruments appropriate and sufficiently clear? Listed institutions are asked to provide an estimate of the impact and costs that would be created due to the requirement that under Article 94(1)(l)(i) CRD only shares (and no share linked instruments) should be used in parallel, where possible, to instruments as set out in the RTS on instruments. Wherever possible the estimated impact and costs should be quantified and supported by a short explanation of the methodology applied for their estimation.

(Our response)

The provisions are not clear.

Paragraph 248 sets forth the award of variable remuneration in shares. Further clarity is required for third country institutions which are in the legal form of a stock corporation and which are not listed in European Union stock exchange markets but other countries.

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

(Our response)

The guidelines are sufficiently clear.

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

(Our response)

The guidelines are sufficiently clear.

Question 19
Are the requirements in Title V (institutions that benefit from government support) sufficiently clear and appropriate?

(Our response)

The guidelines are sufficiently clear.

Question 20
Are the requirements in Title VI (disclosures by institutions and internal transparency) appropriate and sufficiently clear?

(Our response)

The guidelines are sufficiently clear.

Question 21
Do institutions, considering the baseline scenario, agree with the impact assessment and its conclusions?

(Our response)

We agree with the impact assessment and its conclusion.

<Our other requests>

・Markets in Financial Instruments Directive 2 (MiFID2) and remuneration policy (Paragraph 20)

Paragraph 20 refers to conflicts of interests arising from remuneration practices. MIFID2 includes specific rules on how firms should address conflicts of interest (Article 23). It would be useful to have some guidance on whether the MiFID2 regime on conflicts would also apply to remuneration or whether this should be seen as a different "class".

・Compliance function (Paragraph 29)

We do not consider that the proposed guidelines place enough emphasis on the role of the compliance function in ensuring integrity and identifying breaches of rules and standards. The compliance function (which is considered a risk function in many financial institutions) should have a role similar to that assigned to the risk function. In other words, the compliance function should be capable of informing on and assisting in setting performance measures so that any conduct risks are sufficiently covered in the remuneration policy. In addition, any relevant compliance findings should be taken into account by the remuneration committee.

・Guaranteed variable remuneration (Paragraph 135)

The proposed guidelines refer to a sound and strong capital base. As third country branches are not subject to CRD and generally do not hold capital, we would request guidance on how third country firms should approach this assessment.