THE
INVESTMENT
ASSOCIATION

IA response to EBA CP2020/26

Draft Guidelines on sound remuneration policies under Directive (EU) 2019/2034

About the Investment Association

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £7.7trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. 40% of this is for overseas customers. The UK asset management industry is the largest in Europe and the second largest globally.

Questions

1. Are the subject matter, scope and definitions appropriate and sufficiently clear?

The IA request that the disclosure requirements within the IFD/IFR package should only apply in respect of remuneration awarded under policies that are subject to the remuneration policy and governance requirements within the IFD/IFR package. Hence, the remuneration disclosure requirements should only apply to remuneration awarded in respect of performance years commencing after 31 December 2021. This will provide logical consistency between the remuneration policy / governance and the remuneration disclosure requirements within the IFD/IFR package.

Member firms would welcome guidance on disclosure times. Regulation (EU) 2019/2033 and Directive (EU) 2019/2034 together formed the IFD/IFR package, with the latter including remuneration disclosure requirements and the latter including remuneration policy and governance requirements for investment firms. Article 51 of Regulation (EU) 2019/2033 sets out those remuneration disclosure requirements. The draft guidelines do not include any guidance on the implementation timeline for those disclosure requirements.

Feedback in relation to section 3 on implementation

Under section 3, the date of application of the guidelines is specified in paragraph 10 as 26 June 2021 (subject to confirmation) while the transitional provisions set out in paragraph 11:

- require all firms in scope to make adjustments to their remuneration policies and policy documentation by 31 December 2021;
- require firms that need to seek shareholder approval of those remuneration policy changes to do so before 30 June 2022; and

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- require firms to apply the adjusted remuneration policies for performance years commencing after 31 December 2021.

IA member firms would find it helpful if the guidelines also made it clear that these transitional timelines apply to the remuneration requirements of Directive (EU) 2019/2034 itself, as well as these EBA guidelines. This would allow firms the time that is needed to amend their governance arrangements to meet the requirements of the Directive.

This could be achieved as follows:
"10. These guidelines, and the remuneration requirements of Directive 2019/34/EU to which they relate, apply from 26 June 2021 (TBC). … 11. Investment firms should implement any adjustments of their remuneration policies that are necessary to comply with these guidelines, and the remuneration requirements of Directive 2019/34/EU to which they relate, by 31.12.2021 and update the required documentation accordingly…."

Less substantive feedback that might increase the clarity of certain of the Definitions set out in section 2 on subject matter, scope and definitions.
The IA request that the following clarifications are considered:

- Paragraph 9 refers to "Directive 2019/34/EU". Paragraphs 7 and 8 refer to "Directive 2019/2034/EU". Should these references instead be to "Directive (EU) 2019/2034", being the Investment Firms Directive?
- The definition of ***Retention bonus*** could inadvertently capture deferred compensation grants, such as those granted in respect of the deferred element of an annual bonus award. The definition should be amended as follows: *"means variable remuneration awarded solely or principally on the condition that staff in the investment firm for a predefined period of time, and for the avoidance of doubt does not include awards granted as a deferral of variable remuneration earned by reference to performance already undertaken at the investment firm."*
- The definition of ***Identified staff*** could be clarified as follows: *"means staff whose professional activities have a material impact on the investment firm's individual or the group's risk profile or of the assets that it manages, in accordance with the criteria set out in Article 30(1) of Directive (EU) 2019/2034, the commission Delegated Regulation adopted under the empowerment within the last subparagraph of Article 30(4) of this Directive (RTS on identified staff) and, where appropriate to ensure a complete identification of staff ~~that~~ whose professional activities have a material impact on the risk profile, additional criteria defined by the investment firm."*
- The definition of ***Gender neutral*** remuneration policies could be clarified by referring to "gender diverse" or "gender non-binary" workers, rather than "diverse" workers.
- The definition of ***Clawback*** could be clarified as follows: *"means an arrangement under which the staff member has to return ownership to the investment firm of an amount of variable remuneration paid in the past or which as already vested ~~to the investment firm~~ under certain conditions."*

2. Is the section on gender neutral remuneration policies sufficiently clear?

The section is clear in the fact that investment firms should be operating a gender-neutral remuneration policy as part of an appropriate gender balance and representation, as applicable across the industry and within each member state. This clearly aligns with the requirements of equal pay legislation and the requirement for robust equal opportunity measures and practices where investment firms should already be adhering to this. In

addition, the non-exhaustive list of aspects to consider within paragraph 27 appears reasonable and not too prescriptive.

The IA do not support the wording of paragraph 26 as this requirement may not achieve the result of reaching gender neutrality. Although we support the spirit of ensuring compliance with this regulation, in order to recognise that different firms take a variety of approaches to ensure compliance with local country equal pay legislation, we suggest the removal of paragraph 26 because this might not be the specific approach adopted for some entities in certain jurisdictions.

What is not clear is the report that the EBA are mandated to issue on the application of gender pay neutral policies and how this may impact the current requirement of the IFD and other Directives.

The draft guidelines appear to be silent on promoting prescriptive gender-balanced remuneration committees, which is welcomed and ensures it is the responsibility of the investment firm to demonstrate their remuneration policy, practices and governance framework is gender neutral.

In paragraph 59 in terms of monitoring the gender pay gap as part of an analysis to ensure the remuneration policy is gender neutral, the consultation further outlines the need to document main reasons for material differences in average pay ratios. The IA is concerned that publishing gender pay gap reports for management bodies is highly confidential and conflicts with GDPR requirements, given likely very small sample sizes. We therefore request that this requirement is clarified as being for internal documentation only.

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3. Are the sections on the remuneration committee sufficiently clear?

The majority of the sections on remuneration committees are clear, however there are three that would benefit from further clarification.

Section 2.3, paragraph 48 specifies “The remuneration committee might be established at group level, including in situations where the consolidating institution is subject to Directive 2013/36/EU”. Member firms are supportive of this approach, which is reflected in the text of the Directive itself and is useful to allow firms to align their approach with different governance structures that might apply. However, the latter half of this sentence does not add any specific additional clarity and therefore it would be more clear to firms if the word were more simple: removing the specific situations, and leaving as: *“The remuneration committee might be established at group level.”*

Section 2.3.1, Paragraph 50 states “The remuneration committee must be gender balanced”. This statement is relatively unclear as to the definition of balanced, and in particular how this might apply to remuneration committees with an odd number of committee members. The IA propose to update the wording to specify *“the remuneration committee should be appropriately gender balanced”*. This change would enable firms to interpret and comply with the recommendation, which we support.

Section 2.3.1, Paragraph 51 states “The chair and the majority of members of the remuneration committee should qualify as independent (..) Where there are not a sufficient number of independent members, investment firms should implement other

measures to limit conflicts of interest in decisions on remuneration issues.”. The flexibility foreseen in this provision is welcome, but the IA would suggest clarifying the wording to state “*Where investment firms do not have any independent members of the management body in its supervisory function, or do not have sufficient number of such independent members, they should implement other measures that mitigate the risks of conflicts of interest and ensure that decisions are made with due consideration of these risks.”*

4. Are the guidelines on the application of the requirements in a group context sufficiently clear?

The IA suggest the proposed application of the requirements in a group context should be amended to reflect the less onerous approach under CRD V.

Paragraph 21 of the draft revised EBA Guidelines on sound remuneration policies under CRD states: “Subject to national discretion, subsidiaries for which other specific sectoral directives (e.g. MiFID, IFD, AIFMD and UCITS Directive) include a specific remuneration framework do not have to be included into the scope of applying the CRD requirements foreseen under Articles 92, 94 and 95 CRD on a ‘consolidated basis’ in accordance with Article 109 CRD. Staff members of subsidiaries that meet the conditions under Article 109(5)(a) CRD are subject to those requirements on an individual basis where the staff have been mandated to perform professional activities that have a direct material impact on the risk profile or the business of the institutions within the group.”

Whilst we appreciate that IFD does not have a specific provision on this, we think that the EBA has sufficient flexibility in interpreting how the remuneration rules in the IFD apply within groups to provide that a similar concept will apply under IFD. For example, the EBA could clarify in the guidelines that:

- If a subsidiary is subject to another EU remuneration regime, or would be if it were established in the EU, then it will not be necessary for that subsidiary to be included in the scope of the IFD remuneration requirements that apply to Material Risk Takers.
- The only exception to that would be for any individuals working for the subsidiary who are mandated to perform professional activities that have a direct material impact on the risk profile or business of the IFD firms within the consolidation group.

This change is important to ensure a proportionate approach within global groups. In particular, whilst the bonus cap does not apply under IFD, the application of the remuneration rules to anyone in the IFD consolidation group who earns over EUR 500,000 is onerous, especially as in practice it will catch entities within the consolidation group based outside the EU (for example in the US or Asia).

5. Are the guidelines regarding the application of waivers within section 4 sufficiently clear?

The EBA should clarify in its final Guidelines that the waiver can be obtained if the assets of the particular entity are below the relevant threshold (i.e. EUR 100 million or the increased threshold) and that it is not necessary for the assets of the consolidation group to be below EUR 100 million.

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6. Is section 9 on severance payments sufficiently clear?

The IA welcomes the guidance on severance pay and concurs with the EBA's view that firms should establish a framework for determining and approving severance pay within their organisation. We agree that such a framework should clearly set out the criteria used by the firm to determine severance pay amounts and ensure that it does not reward for failure or misconduct. However, we would suggest that the full detail of a firm's severance pay framework should remain confidential to the firm and for review by local regulators and supervisory bodies as appropriate, rather than needing to be replicated in full detail within the Remuneration policy itself, which could instead refer to the main principles – including in particular that severance pay should ensure there is no reward for failure or misconduct – and confirm existence of a more detailed framework. The IA request that the guidance clarify this point, as publication of the detailed severance pay framework could create disproportionate legal risks and employee relations complexity for member firms.

The IA also note that confirmation that notice pay is excluded is helpful. We would also suggest clarifying that any other standard payments related to notice periods are also excluded. For example, buyout of un-used vacation periods.

7. Are the provisions on performance criteria sufficiently clear, which other performance indicators, e.g. regarding the performance of business units or portfolios, are used to determine the variable remuneration of identified staff?

The IA note that the examples provided are broad enough to cover a wide range of performance indicators. The information on performance criteria in the CP is sufficiently clear. It is helpful that flexibility is given to individual firms to determine the relative importance of each level of the performance criteria, recognising the discrete differences between the structure and approach of each investment firm.

It is also clear that firms can adequately balance performance criteria by the role and responsibilities of the individual staff members and assess their individual and the firm's achievements against these clearly documented criteria during the accrual period. It should be relatively straightforward for firms to closely link risk and performance measures to the role and responsibilities of the identified staff member and the decisions that they have direct influence over, clearly documenting these. Financial criteria will be less relevant for certain roles (e.g. Head of HR) so the ability to balance such performance criteria with more relevant non-financial objectives is important.

The examples of quantitative performance measures are useful, as is the clarity of measures where additional risk adjustment is required. Firms will utilise these measure based on the structure of the firm and role of the individual they are being applied to. Firms are often cautious of including too many measures, as doing so makes each measure less meaningful, so firms are likely to focus on the most relevant and important measures. The assumption is that this will align with and be compliant with the requirements.

Stating that quantitative criteria should cover a period which is long enough to properly capture the risk taken by identified staff members, business units and the investment firm is helpful and allows flexibility between different identified staff members where the roles

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can differ relatively significantly. It would however be helpful to have greater clarity on whether one year is acceptable for certain non-investment related roles where multi-year performance is less appropriate and the risks relevant to the role (e.g. reputational and operational risk) can be assessed on an annual basis.

The list of qualitative measures is comprehensive. Additional measures that have increased in prevalence in investment firms in the recent years include collaboration (as an extension of teamwork), the integration of ESG criteria into investment processes and actively promoting all aspects of diversity & inclusion in the workplace.

8. Is the section on the pay out in instruments sufficiently clear?

The IA note that the requirements set out in paragraphs 258 to 266 are sufficiently clear. However, we would like to make the following comments with regards to the below paragraphs:

- Paragraph 243 should better reflect that the requirement is to have a balance between non-cash instruments and cash (as opposed to having a balance between equity, equity-linked instruments, other instruments and cash). As a result, we propose the following amendments: *"…investment firms should pay the variable remuneration partly upfront and partly deferred and in an appropriate balance between non-cash instruments (equity, equity-linked and other eligible instruments) and cash in accordance with Article 32 of Directive (EU) 2019/2033."*
- We propose the following amendment to paragraph 269: *"The ratio of variable remuneration that is paid out in instruments should be calculated as the quotient between the amount of variable remuneration awarded in instruments and the sum of the variable remuneration awarded in cash, instruments and in any other form ~~benefits~~."*
- In paragraph 274 we note the proposal to mirror the retention period set out in the EBA Guidelines on Sound Remuneration Policies under CRD. The IA do not support the minimum 12-month retention period. Paragraphs 270, 271 and 272 give firms the flexibility given to firms to determine the retention period that is appropriate to their risk profile and long-term interests. We believe that setting a minimum twelve-month retention period contradicts the flexibility given by these 3 paragraphs, and that in some scenarios a lower retention period (such as 6 months) may be more appropriate. We note that the ESMA Guidelines on Sound Remuneration Policies under UCITS and AIFMD do not mandate a minimum twelve-month retention period, and only require firms to make sure that the retention period is sufficient to align incentives with the longer-term interest of the firm, of the funds it manages, and of its investors. We also note that some national competent authorities recommended that a minimum 6-month retention period under UCITS and AIFMD. As a result of the above, we believe that it would be appropriate to remove paragraph 274, so that to be more aligned to UCITS and AIFMD rules – or alternatively to mandate a minimum six-month retention period, as opposed to twelve.

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