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Consultation response

EBA Remuneration Guidelines (EBA/CP/2015/03)

4 June 2015

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the **EBA's DRAFT GUIDELINES ON SOUND REMUNERATION POLICIES AND DISCLOSURES (EBA/CP/2015/03) (hereafter "the Guidelines")**. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

AFME is listed on the EU Register of Interest Representatives, registration number 65110063986-76.

I. Introductory comments

Before providing detailed responses to the individual questions raised in the consultation paper in Section 2, this first section briefly summarise AFME's key areas of concern where we feel the proposed Guidelines require change prior to their finalisation. This is followed by our views on general themes that are relevant to the Guidelines in their entirety, notably the impacts of removing proportionality, the need to strike a balance between the different elements of pay and the general level of prescriptiveness of the current text.

Key areas of concern

Our key areas of concern with the proposed Guidelines can be summarised as follows:

- *Maintaining the proportionality principle, as intended by the CRDIV* – proportionate application is key to ensuring that the impact of the CRD remuneration rules appropriately corresponds to the size and activities of an individual entity, and the extent to which an individual is taking material risk for the firm.
- *Factors for determining fixed pay* – for example, the requirement that there should be equivalence between similar roles should not be a precondition for remuneration categorisation. There are many reasons, unconnected to individual performance (e.g. different skills, experience levels, etc.), why the same or similar roles may have different levels of fixed pay, including different levels of allowances.
- *Long term incentive schemes* – these plans align individual's behaviour with the interests of shareholders by requiring the long term value creation of a company. Their valuation and inclusion in measurement of the ratio should be performed at grant rather than at vest, in line with current practice.
- *Indiscriminate treatment of severance payments* – there are different types of severance payments and those which are not related to past performance should not be included in variable remuneration for the purposes of the ratio.

- *Forfeiture/adjustments to fixed remuneration* – there are valid circumstances where firms may be required to reduce fixed remuneration (e.g. misconduct, an institution or business line is failing, material risk management failures, etc.). The forfeiture of fixed pay in such circumstances is consistent with prudent remuneration policies and with maintaining a sound capital base. It should not lead to a change in classification.
- *Prohibition for listed firms to use share linked instruments* - there is no economic justification for disallowing the use of such structures for listed firms while other types of firms are allowed to make use of them.
- *Non payment of dividends during vesting periods* – this would compromise the economic position of employees compared to other shareholders and reduce the value of awards
- *Retention periods* – we see no underlying rationale for extending the standard retention period to 1 year. Additionally, under the current drafting of the proposed Guidelines, the implications for senior managers would be disproportionate.
- *Shareholder approval requirements* – are unnecessary in the case of fully owned subsidiaries and, by requiring an unnecessary cascade to the ultimate parent of EU subsidiaries of non EU headquarters firms, the Guidelines have an extraterritorial impact.

Removal of proportionate application will have significant impacts and is unjustified

The revised Guidelines propose a significant extension to the scope of the CRD's remuneration related provisions whereby group wide policies and the requirements related to material risk takers would have to apply to subsidiaries that are not subject to the CRD. In addition, by removing the application of the principle of proportionality, the revised Guidelines will lead to a significant number of additional individuals being subject to the remuneration requirements of the CRD, regardless of whether it is appropriate to apply such strict deferral periods and payout structures to individuals who may only have very low levels of variable remuneration.

We question whether the scope extension and effective removal of the proportionality principle from the CRD's remuneration requirements are effectively within the EBA's mandate. In our view, the EBA's powers do not include the ability to modify the scope of the CRD nor to change the proportionality principle which has been enshrined into the Directive by the co-legislators. By including language suggesting that the remuneration principles only apply "to the extent appropriate", Article 92 of CRD clearly contemplates their neutralisation or partial neutralisation.

In relation to the quantitative principles, particularly those in Article 94 of CRD, the application of the proportionality principle would be rendered meaningless without full or partial neutralisation. There is also no basis to distinguish the principles in Article 92 and the principles in Article 94. Indeed, Article 94.1 states that the principles set out "shall apply in addition to, and under the same conditions as, those set out in Article 92(2)." Moreover, by removing the so-called neutralisations from the CEBS Remuneration Guidelines and modifying the application of the proportionality principle as proposed, the EBA is effectively creating binding, minimum standards that will apply indiscriminately and fail to reflect the nuances of firm specific situations.

We note further that this would represent a significant change compared to the current practices of the vast majority of National Competent Authorities who implement the proportionality principle in various ways (e.g. through the recognition of the immaterial nature of certain subsidiaries or specific treatment of businesses like investment management, enabling them to compete in a broader market place).

In our opinion, the cost/benefit case for making such a significant change is far from being proven. On the basis of a sample of our member firms, the removal of the proportionality principle would result in a 12 fold increase in the number of legal entities being affected, while the number of individuals that would be subject to remuneration requirements would more than triple compared to the current situation. Apart from the obvious additional administrative burden this will create for firms operating in Europe, it is entirely unclear that the new approach will contribute in any way to an increase in financial stability.

Moreover, we are concerned that these rules will impact competition, creating an un-level playing field between in-scope and out-of-scope firms, such as investment management businesses, operating in the same markets, both within the EU as well as in relation to third countries.

Lastly, we understand that the EBA could be supportive of the need for a proportionate application of the requirements but is constrained by a legal interpretation from the European Commission. However, it should be noted that legal opinions from a significant number of reputable legal firms question this interpretation. Given that there is ambiguity in the interpretation and that EBA has stated it would support changes to the primary legislation to make this issue clear, we are of the view that the pragmatic answer would be for EBA to leave the approach to proportionality unchanged until specific clarity is reached through possible future changes in primary legislation.

Balanced remuneration packages and the merits of variable pay

Under the CRD, the variable part of remuneration is subject to strict deferral and malus rules and a significant portion is awarded in shares rather than cash. As a result, variable remuneration is an extremely useful tool to guide staff behaviour and align risks with rewards. Variable pay is also an effective risk management tool as it provides firms with the flexibility to adapt their cost base in response to any downturn in business.

Placing too great restrictions on variable pay not only reduces its value to incentivise appropriate behaviour (employees have “less skin in the game”), it also limits firms’ flexibility to reduce pay in times of stress and has the unintended consequence of driving up fixed pay because firms need to remain competitive in global markets. With an increase in the fixed cost base being undesirable from a financial stability perspective, international regulators and standard setters have floated the concept of placing fixed pay at risk to address this concern. Under the proposed Guidelines, there may be an undesired effect where this at risk pay is considered variable in nature and thus subject to the same limitations that lead to an increase in fixed remuneration in the first place, potentially exacerbating the situation.

While ensuring that the principle and letter of the CRD is respected, we therefore encourage the EBA to retain a sufficient level of flexibility in their final Remuneration Guidelines to deliver on the ultimate policy objective of an appropriate alignment of risk and reward.

Complex and overly prescriptive nature of the Guidelines

While we welcome the EBA’s efforts to ensure consistent application of the remuneration requirements throughout the EU, we are concerned that this desire has led to the drafting of proposed Guidelines that are unnecessarily bureaucratic, in some places do not make sense, are contradictory to other rules, or conflict with national employment law. They also restrict

the ability of National Competent Authorities to apply the necessary flexibility they require to regulate the different types of organisations they deal with.

As a result, the proposed Guidelines will introduce unnecessary operational complexity. For example, by requiring the creation of remuneration committees at the level of each significant entity, the Guidelines fail to recognise the diversity of group structures and resulting governance practices. While remuneration governance solutions may differ in their practical application, many of these approaches are sound and robust. Therefore, provided that there is appropriate oversight of remuneration policy from the senior management of the institution, there is no reason to require the establishment of remuneration committees at local entity level. Other examples of this complexity include unnecessary shareholder approval requests in the case of fully owned subsidiaries and the extraterritorial reach of the proposals to the ultimate parent level of EU subsidiaries of non EU headquarters firms whereas approval of the immediate parent is sufficient.

By necessity we cannot point out all of these situations, but we have tried to provide examples throughout our response whenever possible. When considering the issuance of its final Guidelines, we would encourage the EBA to take into account the relative costs and benefits of its detailed proposals and adopt a more pragmatic approach wherever possible.

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II. Responses to the Consultation Questions

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

Definitions

In general the definitions are clear. There are however a number of points where further clarity or flexibility should be considered:

Routine employment packages (d): the wording "routine employment packages are..." does not make sense. We assume that the intention is to say "Routine employment packages include…." or some similar meaning.

Long term incentive plan (e): Definition (e) states part of an LTIP is "awarded at one point of time and under the same plan additional awards are made at future points in time subject to conditions". This definition is confusing in respect to the way in which LTIPs are typically structured and operate. Awards granted in respect of a performance cycle (typically three or five year periods) only occur on a single occasion at the start of the performance period. The achievement of pre-determined performance conditions over the performance period will determine the amount of the granted award that will vest. In other words, there is only one, initial granting of the award, with vesting subject to the completion of performance criteria.

Retention bonus (f): Almost all variable remuneration is conditional on the employee remaining in employment for a pre-defined period of time – e.g. until the end of the bonus year for short-term incentives and until the normal vesting date for longer term incentives. Retention bonuses are normally only those which are made outside the normal framework of short and long term variable remuneration in order, for example, to address a need to restructure part of a business, and it would be helpful if the definition could make this clear. Also, a restructuring activity that is critical to the institution (as agreed by National l Competent Authorities) may not lend itself to a time definition. Use of a time only definition may narrow the current scope of Competent Authorities to allow such payments in legitimate circumstances.

Staff (g): The definition is too broad and should end after the word "scope". Including "…and any other person acting on behalf of the institution and its subsidiaries" could bring into scope for example external legal advisors who act for an institution.

Lastly, we think that the EBA should also define the concept of "Group" in the context of these Guidelines.

Currency conversion proposals (§7)

Using a single fixed rate as defined in the Commission's financial programming and budget of the previous year lacks flexibility and will lead to unintended consequences:

a) An average exchange rate representing the previous performance year will be more representative than a point in time/year end rate.
b) For high inflation countries (e.g. Argentina, Venezuela) these rates may not necessarily reflect the correct purchasing power of an executive receiving local currency to buy assets in euros - adjustments should be made in these cases to better reflect the environment in these countries so that quantitative criteria do not capture people they are not intended to cover.

c) there should be an exclusion such that an employee should not be identified simply because of a movement in the exchange rate if their remuneration has not increased in their local currency.

Instead of using the rate suggested by the EBA, we instead suggest that the exchange rate used should be set by an institution (subject to approval by the Competent Authority) as it will relate much more closely to the way in which Remuneration costs are booked and expensed at an institution. Therefore, we believe that the current requirements contained in the "EBA Final 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 94(2) of [CRD IV]" should remain unchanged.

Q 2: Are the Guidelines in chapter 5 appropriate and sufficiently clear?

Yes, we support the principles outlined in this chapter.

Q 3: Are the Guidelines regarding the shareholders' involvement in setting higher ratios for variable remuneration sufficiently clear?

The Guidelines regarding shareholders' involvement are clear when applied at a consolidated level to a 'Group' level firm that is listed. However, it is unclear how the Guidelines would have to be applied at other levels in large groups where there are multiple organisational/shareholder levels.

For instance, in situations where a fully-owned subsidiary of an EU parent institution exists and is not itself listed on the open-market, authorisations received from shareholders of the EU parent institution should apply. To require the approval of intermediate shareholder levels in such cases would create unnecessary administrative burdens in groups with complex organisational structures with no additional benefit. It should therefore be clarified that shareholder decisions can be taken at the group level and cascaded down in these cases.

Moreover, if a staff member is identified as a Group level MRT, the Group policy should apply, i.e. the approval of the ratio at parent company level should be sufficient.

Paragraph 36.a will require the shareholders of non EEA entities to approve a maximum ratio which applies only because some staff are identified as MRTs at EU Group level. This could be problematic as these provisions do not exist in local regulations. In fact, some local regulations require a "minimum" variable remuneration component instead of a cap in relation to fixed pay. Russia for instance requires that variable remuneration must not be lower than 40% of the fixed salary. This creates a situation where EU firms have virtually no flexibility in setting the proportions of fixed versus variable pay in countries where their competitors do benefit from this flexibility. This is an example when linked to the elimination of the proportionality principle where the regulations will have significant unintended consequences (see our reply to Question 5 below).

We note further that non EEA entities will not need to inform their regulators about the shareholders' decision as this requirement is not recognised by local regulators.

The wording in § 36.b would seem to look up through the corporate ladder to require a vote of the shareholders of the ultimate parent of a non EEA headquartered entity. Article 94.1(g) of the CRDIV requires shareholders to approve a higher maximum level of the ratio. The Article refers to the *shareholders of the institution* and not the consolidated group. The requirement in § 36b of the draft EBA Guidelines to seek group level shareholder approval is an unjustified extension of the Directive and goes beyond legal advice received on corporate governance requirements. It is likely to cause extraterritorial regulatory difficulties. We do not believe it is right or appropriate to impose such a condition and would ask the EBA to modify the proposed language to clarify that it is the *immediate parent* only of the EEA subsidiary that will look at and decide upon the ratio question.

Q 4: Are the Guidelines regarding remuneration policies and group context appropriate and sufficiently clear?

No, there are a number of areas of concern

Overall, in relation to this topic (as well as others throughout the Guidelines), it is important to note that regulations and practice in certain local jurisdictions render the suggested approach unworkable. To the extent the rules are in conflict with national requirements, we presume to follow those national requirements first while striving to uphold the general principles of these Guidelines.

<u>Remuneration Committees</u>

The requirements for remuneration committees in Section 6.4 and in particular in §39 envision multiple remuneration committees at parent and subsidiary levels (significant institutions at an individual level) within an institution. We believe the decision on whether to have a single remuneration committee or multiple committees should ultimately be a matter for each institution in conjunction with its supervisor, based on its internal organisation and complexity.

Remuneration is typically the responsibility of a global remuneration committee that sets the firm's policies and approach to remuneration across the firm on a global business line/divisional basis but not by individual legal entity. Individual group structures will result in a fragmented approach to remuneration and will make remuneration governance extremely complicated.

We note that there is a danger that if the Guidelines do not clarify how subsidiary remuneration committees are expected to interact with consolidated parent remuneration committees under group-wide remuneration governance hierarchy, subsidiary remuneration committees could end up asserting their autonomy over remuneration policy which could jeopardise the requirement to implement a group-wide remuneration policy. We also wish to point out that regional responsibility or an oversight function for remuneration does not have to be through the creation of board-level remuneration committees within each legal entity and encourage the EBA to examine alternative options.

Further consideration also needs to be given to the EU operations of non-EU headquartered firms where the above concerns are particularly acute due to potentially conflicting regulatory requirements and governance.

In light of the above concerns surrounding the practical organisation of remuneration committees at individual legal entity level, AFME strongly recommends that the EBA retain a more flexible approach whereby Competent Authorities evaluate the appropriateness of a specific group structure on the basis of common Guidelines.

The Appendix set outs more detailed examples of where the Guidelines regarding remuneration committees are not practicable.

Remuneration policies and group context

We strongly disagree with the wording in §63 which results in the application of the requirements to non-CRD entities which could include asset managers, insurance companies, automotive leasing firms and non EEA subsidiaries. Application of the requirements on a solo basis to these entities would create unlevel playing fields in these businesses or geographies where entities that are not part of an EU banking group will not have to apply the same rules. This is another area where, viewed in light of the changes to the proportionality principle, will have significant cost impacts (see our response to question 5).

We also consider the requirements in §64 regarding seconded staff to be too onerous and likely to discourage exchanges of this nature. There should be a proportionate definition for when an employee is subject to remuneration provisions: "a few weeks" will have a disproportionate impact and cause a barrier in the workforce, preventing firms from benefitting from the skills and experience of staff in this context. We recommend that a commercial approach for a minimum time until an employee is subject to the rules (e.g. 6 months) be provided for.

Q 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.

We note that, upon advice of the European Commission, the EBAs' preliminary analysis of the remuneration principles set out in Article 92 to 94 of the CRDIV is that the Directive does not provide for any explicit provision that allows the possibility to 'neutralise' some of those principles. However, we do not see any basis for this analysis. While there are textual changes between CRDIII and CRDIV, the substance of the Directive in this area is unchanged. Further, in discussions with legal advisors our members have been told that there appears to be no sound legal basis for the change in interpretation, contrary to the view EBA has indicated it has received from the Commission. Rather than repeat any legal arguments here we understand that a number of the largest legal practices will be responding separately to the consultation.

The EBA's own position on proportionality outlined in the proportionality workshop of October 2013 (after the publication of the CRDIV) continued to recognise the importance of proportionality to disapply certain provisions and to allow neutralisations, and we would strongly encourage the EBA, as it did in the CEBS Guidelines, to accommodate the proportionality and subsidiarity principles as intended by the Directive.

National Competent Authorities have indeed implemented the existing Guidelines and other remuneration requirements in a manner that is proportionate to the nature, scope and complexity of institutions' activities. In practice, this proportionality has been exercised on both an entity level and an individual level, allowing Competent Authorities to exercise flexibility and judgement in relation to the institutions they supervise.

In France and Germany, for instance, thresholds are set by reference to the size of an institution (balance sheet total). In the UK, a three-tiered model is applied, reflecting the flexibility provided by the CRDIV in terms of size, internal organisation and nature, scope and complexity of institutions' activities. Under this model, the most significant institutions are allocated a Level 1 status and therefore have to meet the provisions of CRD IV to the fullest extent. However, Level 3 institutions, which are not considered significant under the above definition, are able to disapply some of the rules with respect to the structure of remuneration.

At the individual level, many EU jurisdictions (e.g. Germany, UK, France, Belgium) allow for minimum thresholds for applying the requirements for identified staff under CRD IV, often to avoid creating a disproportionate administrative burden caused by deferring small amounts of variable remuneration and where these amounts are sufficiently small that their deferral would imply that they would almost be entirely discounted by individuals.

We expected that levels of fixed pay will increase as a result.

By removing the proportionality principle, the draft Guidelines appear to no longer allow for such approaches to be applied. However, as drafted, the Guidelines will also apply all requirements to all subsidiaries, including for the identification of risk takers. The combined result of these changes will mean an increase in the number of lower paid employees, particularly in control functions, being identified, with no way to alleviate them from some of the rules of the structure of their remuneration. Firms' ability to retain these employees will be severely hampered, and this is envisaged to be the largest issue for smaller legal entities. In addition to retention issues, it will also become increasingly difficult for firms to encourage the internal development of employees as senior roles will become less attractive. It will also be harder to attract talent from non-EU jurisdictions to work within EU regulated firms.

With regards to the treatment of asset managers in a wider group, individuals should be considered in relation to their risk taking for the consolidated group. This is consistent with the purpose of the Directive and would reduce the arbitrary inconsistency of treatment with asset managers operating outside CRD IV groups to which the ratio cap does not apply. For similar reasons, if an employee of an asset management firm or other group entity which is not subject to CRD IV is identified as a material risk taker under the quantitative criteria, that should not mean that they are necessarily a material risk taker on a consolidated basis, whether or not an application has been made to disapply that individual under the applicable Regulatory Technical Standards.

Accordingly, any staff that are not material risk takers at the consolidated level should be exempt from the requirements. In particular, specific remuneration structures such as carried interest plans are used in the asset management industry and by nature do not fit into the constraints of a 1:1 or 1:2 ratio (see the list of examples below for further information). If clear exemptions from the CRDIV remuneration requirements are not provided for in the Guidelines, a substantial competitive disadvantage between asset managers belonging to a CRDIV group and those who do not will be created, and there will be an unnecessary increase in the number of requests for quantitative exemptions, creating unnecessary administrative burdens for firms and National Competent Authorities alike. Moreover, when other sectoral legislation is of application (e.g. AIFMD, UCITS), there is no clear rationale as to why the provisions of the CRDIV should have precedence over these other requirements which are precisely designed to cater for the specificities of these industries. In this regard, we urge the EBA to consider the approach taken at § 18 of the ESMA Guidelines on sound remuneration policies under the AIFMD. This exempts employees who may otherwise be covered by the remuneration provisions of AIFMD if they are subject to regulatory requirements on remuneration that are equally as effective as those provisions.

In conclusion, we believe that the rules on proportionality as outlined in the CEBS 2010 Guidelines and as implemented by National Competent Authorities:

- Meet the requirements of CRDIV Article 92;
- Are working well in resolving issues as illustrated in the examples below; and
- Give the flexibility envisaged in CRD to regulate institutions based on “the size, internal organisation and nature, scope and complexity of institutions’ activities”.

Should the EBA wish to harmonise the application of this principle throughout EU Member States, we would recommend uniform thresholds be set at both the entity and individual (variable remuneration threshold) levels.

<u>Examples of how the removal of proportionality will impact firms:</u>

- On the basis of a sample of our member firms[1], the removal of the proportionality principle would result in a 12 fold increase in the number of legal entities being affected. Given the diversity in group structures and different head quarters of the firms in this sample, the change in the number of legal entities ranges from 0 to more than 40 times the existing number of entities on an individual firm basis. According to the same sample, the number of individuals that would be covered by the CRD remuneration provisions would, overall, more than triple compared to the current situation. The minimum estimated impact in this sample is a 33% increase in numbers of staff and the maximum impact is an increase of above470%.
- Firms indicate that the bulk of the increase in the identified staff population would stem from retail banking or specialised finance activities with relatively lower levels of variable remuneration. Given their activity, these employees do not have any significant impact on the risk profile of a firm. The removal of the proportionality principle seems thus in contradiction with the objective of CRDIV to target the staff members who can have a material impact on risks. The operational burden will also be immense.
- A non-material Russian Bank subsidiary of a UK regulated institution would be subject to both the EU rules and Central Bank of Russia (CBR) remuneration rules. As an example, EU rules state that the ratio of fixed to variable remuneration cannot exceed 1:1 (1:2 with a shareholder resolution) which means the variable component cannot exceed 50% or 66% of

[1] The figures provided here are based on the estimates undertaken by member firms on a best efforts basis.

the total remuneration. CBR rules state that the variable component cannot be less than 40% of total remuneration. This means there is no or very little flexibility on the amount of remuneration. By using proportionality and because the Russian subsidiary was immaterial within the group structure, the institution was allowed to apply proportionality to that Russian subsidiary to disapply the EU rules, including the ratio, so as to focus on compliance with the CBR rules.

- The proposed Guidelines state that staff who are subject to other sectoral legislation e.g. AIFMD and UCITS and are part of a CRD IV Group have to comply with the fixed to variable remuneration ratio. The remuneration plan of such entities includes an industry specific remuneration structure, a carried interest plan. The carried interest plan is not part of the regular annual remuneration cycle. Moreover, these plans are aligned to fund life cycles and with clients' interests, with vesting periods that typically range from e.g. 3 to 8 years. A recipient of a carried interest award in one year may not receive another such award for many years to come. As a result, including the value of a carried interest plan award in a ratio calculation for a particular single year would be unworkable due to the irregular nature of such awards. Carried interest plans are long term, irregular and carry a real risk of non-payout. The current application of proportionality to a non-material AIFMD or UCITS regulated subsidiary means that such subsidiaries do not need to change their remuneration policies from industry standards and can continue to compete with other similar businesses not subject to CRD.
- As pointed out during the EBA's public hearing on these Guidelines, there are many examples of European banking groups with a large number of relatively lowly paid employees with small amounts of variable pay. The current application of proportionality means that the deferral principle does not need to be applied, with a significant saving in administrative complexity, and an ability to retain these employees. On the contrary, removing proportionality could mean that such bonus amount, which are typically in the region of EUR1 000, would be subject to the entire suite of the CRDIV's remuneration rules.

Q 6: Are the Guidelines on the identification of staff appropriate and sufficiently clear?

While we understand the need for process around the identification of the MRT population, we believe that the rules as drafted are overly prescriptive and bureaucratic, and in some cases contradictory. The rules will be both unnecessarily burdensome for firms and National Competent Authorities and it is unlikely that any resulting benefits would outweigh the cost of implementation in these areas. For example:

- §86 – it should not be mandatory to consider standard benefit costs, particularly the value of pension benefits, which are part of fixed pay (per § 118) and are formulaic across the population should in the identification process. They are often of small value and inclusion is contradictory to the Guidelines in §185 which we agree with, that, "institutions may omit some of the fixed remuneration components, where they are not material, e.g., where proportionate non-monetary benefits are awarded." These standard plans for all employees are clearly not specific to an individual employee's role with the firm. Additionally, there are certain national requirements around benefits (i.e., specified required levels of coverage) and market-driven factors for the cost of certain standard benefits which do not reflect an employee's role as an MRT (i.e. the benefit value is not indicative of risk, level or function).
- §87-§91– National Competent Authorities should determine the appropriate process. The specific requirements as drafted in the Guidelines are not commercial and would be time consuming and administratively cumbersome for supervisors to manage.

- § 93 – The requirement on the approval of exclusions is not clear: do the exemption requests have to be presented each year or every two years: "the prior approval should only concern the financial year in which the prior approval was requested and the following financial year". In terms of timing, presenting all exemption requests might be problematic when reorganisations occur and are effective only at the end of the first semester of the year. Derogations should be provided for in such contexts.

Part-year exemption

We suggest that a temporary exception be applied to identified staff (MRTs) that have taken up role part way through the year (i.e. where the individual has not held a role representative of an MRT risk profile for a significant part of the year) or senior staff of a parent entity outside the EU that have de minimis involvement with the CRD entity. An example would be an employee participating in a short-term assignment which gives them the opportunity to develop a new skill-set, participate in a new project and/or support an understaffed team for a shorter, specified time frame. Without this exception there is a risk that employees will be reluctant to take up an identified staff (MRT) role as remuneration for the entire performance period will be subject to the more stringent requirements. In turn, this could create a prolonged vacancy which could impact on the succession planning of the business and increase people and operational risks or disincentivise employees from participating in developmental opportunities.

Identification process on solo and consolidated levels

Typically, firms view 'identified Staff' (MRTs) at a consolidated level only, as this is the level that is most significant in assessing the impact on the institutions risk profile.

- §100 - it is not clear why identification of risk takers would be required to be conducted on a legal entity basis as opposed to a significant/material legal entity basis. It is also not clear why identification would be required on a sub-consolidated level. This requirement would be overly burdensome.
- According to §101, it appears that the role-based qualitative criteria in Article 3 of the RTS on identified staff should apply on a consolidated level only, e.g. if a staff member is a member of the management body of a subsidiary, he/she would only be captured by the RTS criterion if he/she is also a member of the management body of the EU parent institution). Paragraphs 100 and 103 however appear to contradict this. We would therefore welcome clarification that this qualitative criteria does indeed apply only on a consolidated level.
- With regards to § 107, it does not seem proportionate to require branches in third countries to conduct an identification process as risk takers will be identified on a consolidated basis.

Q 7: Are the Guidelines regarding the capital base appropriate and sufficiently clear?

Yes the Guidelines are clear.

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

We think that the EBA should exercise caution and avoid being too prescriptive, particularly with fixed pay, where national employment laws may contradict the interpretation of the EBA. Some of the following may be helpful by way of example:

- There are cases where employees having the same positions may not have the same fixed pay because the level of fixed pay may be driven by tenure or a different prior experience level or various other historical factors.
- In some countries, fixed pay can be reduced on the sole decision of the employer (e.g. Singapore).
- Payments can be suspended during periods of 'unpaid' absence such as maternity leave.

Ultimately, fixed pay depends on many different parameters and not just on the role. Indeed, seniority, period of service, educational level, geographies, previous career paths, etc. are all used to determine fixed pay. In fact, there is no reasonable basis to require individuals performing similar roles to be paid the same amount (see also question 9 below). Additionally, fixed pay can be modified even when the role and its responsibilities are unchanged.

National laws do not impose such requirements on employers and to require this in the EBA Guidelines would be to impose a "same pay principle" for which there is no basis in CRDIV and no power to create such a condition under the relevant treaties.

<u>§117 – fixed remuneration conditions</u>

We note that national laws may conflict with sub-paragraphs d, e and f of §117. In addition, sub-paragraph c may be difficult to achieve in full because different levels of fixed pay are provided for the same role as noted above.

Further, in regards to sub-paragraph f and as described above in our introductory comments on "Balanced remuneration packages and the merits of variable pay", there is no reason in principle why an institution cannot retain a contractual right to reduce fixed remuneration for prudential reasons in order to preserve capital, in the event of serious misconduct or a material failure of risk management, or in other situations where the individual would not be exercising its role, provided that such reductions are not a proxy for individual performance. Retaining the ability to make reductions in fixed pay in such narrowly defined circumstances further incentivises positive behaviours and aligns risk and reward in keeping with the overall objective of CRDIV.

In general, if the amount of an allowance is determined and communicated to an employee at the beginning of a performance year, it is difficult to see how this type of remuneration could incentivise risk taking or otherwise be defined as variable remuneration.

<u>§120 – LTIP valuation/classification</u>

We do not agree with the requirement described in §120. As currently proposed, the requirement does not reflect the nature or incentive purpose of a typical 'LTIP' (where the value of the award remains fully 'at risk' subject to the achievements of performance conditions) nor does it consider the difficulties for institutions to implement a remuneration package that provides upfront clarity of the appropriate balance between fixed and variable pay (as required under CRD) and as a result will have an impact on the variable pay cap.

The definition of LTIPs should be reconsidered. As already noted in our response to question 1 above, an LTIP provides participants with an award grant made in a given year based on individual prior year performance. This grant is then subject to, typically, a three or five-year performance period (the performance cycle) and only vests, in whole or as a proportion of the initial award, depending on the achievement of **pre-determined** company performance measures.

The purpose of an LTIP is to align participants (normally limited to senior employees whose performance can directly influence that of the company) with the interests of shareholders by requiring long term value creation of a company. As such, investors appreciate the objectives of such plans and advise that they form part of a variable remuneration package[2].

However, the EBA's proposed measurement of the LTIP on vest rather than at grant presents a number of practical considerations and, in turn, unintended consequences:

1. Institutions would be unable to provide upfront clarity/planning of the appropriate balance between fixed and different components of variable pay and work within the parameters of a bonus cap. At vest, depending on the value of the underlying shares, LTIPs may ultimately be worth nothing. However, even a modest increase in the shares could "crowdout" future annual bonus payments; a more substantial increase could result in an unintended breach in the bonus cap.
2. Institutions would need to wait until the award vests (the amount depending on performance achieved) in order to calculate the proportion of the cap taken by this award. This could encourage some firms to circumvent the purpose of the cap by backfilling any headroom remaining in the cap with short term variable awards (i.e. annual bonus) at the point of vesting. Additionally, this would be particularly difficult to assess.
3. In cases where an employee changes role or becomes part-time after an LTIP is awarded, their fixed pay may need to be reduced and could lead to a breach of the variable remuneration cap when the LTIP vests.
4. A further consideration relates to how discounting will be applied to an LTIP if the valuation is undertaken at vesting.
5. Institutions may cease to use LTIPs as a viable incentive due to the complexities explained above and which is also likely to reduce their perceived value to employees. This could be problematic given shareholders and key stakeholders largely support the use of LTIPs as a means to appropriately motivate employees who drive firm performance over the long-term.

For the reasons provided above, we encourage the EBA to reconsider the requirement provided in §120 and consider LTIPs as remuneration for the year in which they are granted and not the year that conditions are met (as supported by the principle outlined in § 180 of the Guidelines that states "the ratio set is the ratio between the variable remuneration that could be awarded as a maximum for the following performance periods and the fixed remuneration of the following performance period").

[2] See for instance the Investment Management Association's Principles of Remuneration

Investments in firms' funds

It is important not to inadvertently capture investments in vehicles that have no features of variable pay. By way of example, certain employees may be given the opportunity to invest in a firm's funds. This is at the discretion of the employee, utilising individual's post-tax monies, and there is no guarantee on the performance of the fund. Any preferential terms for employees are typically *de minimis* (e.g. waiving the minimum investment threshold).

The payments received by an employee in respect of such funds should properly be treated as investment income as they would be for any other investor unless there are reasons to conclude that such payments have been made by way of avoidance. This is an assessment that should be made by national regulators in particular cases.

§121 – Carried instruments- classification:

Subject to our comments above in respect of investments in firm's funds, with regard to the term "payment" used in § 121, it is not clear whether the reference is to "actual" payout or "value at grant".

It would be logical if the term "payment" refers to "value at grant" as this is immediately quantifiable and calculable for ratio purposes for the performance year for which it is granted. Also, the value of the carried interest granted is made to reward performance in the immediately preceding performance year. It is not made in respect of a future performance year.

However if the meaning of the word "payment" is "actual" payout, then this would create issues in the performance year in which payout is made where the payout would result in a breach of the ratio. Similar to LTIP awards, in such circumstances, fixed pay would have to be reduced in order to ensure that the ratio is not breached. Alternatively, the payout would have to be reduced in order to be within the ratio. This would be hugely dis-incentivising for employees and would create retention issues..

Utilising 'actual payout' for ratio determination purposes would be akin to using the future value of vested shares for calculation of the value of deferred share awards, which is not a logical approach.

We therefore strongly support the definition of the term "payment" as meaning "value at grant" rather than "actual payout".

Q 9: Are the requirements regarding allowances appropriate and sufficiently clear?

No. Firms will maintain internal records in line with their internal processes and governance requirements. However, the requirements of §122-124 introduce an additional layer of unnecessary complexity and administrative burden. Whilst the requirements set out in § 122 (and the criteria set out in section 11) reflect the EBA opinion published in October 2014, the requirement in §123 (a) to specifically document the reasons for allocating allowances to the fixed component of remuneration when they are granted only to identified staff is unnecessary and unduly burdensome. The requirement assumes that the identified staff category is role

independent; however, this is clearly not the case. Material risk takers are designated as such precisely because of the type of roles they play within an organisation. This can lead to a circular definition.

The guidance provided in § 124 suggests that a comparable allowance should be applied to comparable roles, however there needs to be acknowledgement that at senior levels many roles are unique. Therefore whilst roles could be categorised in accordance with hierarchy, rank, global grading structure etc., there will be no 'hard and fast' mechanism to align 'comparable roles'. Additionally, as mentioned in question 8 above, there is no reasonable basis to require individuals performing similar roles to be paid the same allowance. The impact of applying such a requirement is to effectively impose a formal pay grading structure for allowances where no such obligation exists for salaries or other forms of fixed remuneration. The requirement would create a higher bar/standard for allowances than currently exists for salaries. A further impact of this will be to increase fixed pay more generally. By way of example, if in order to attract a prospective employee to a position / take on additional responsibilities, a firm needs to pay a certain level of fixed pay, then the provision would require the firm to increase the fixed remuneration of all existing employees with similar responsibilities. A race to the higher level of fixed pay has counter-prudential implications and reduces the resilience of financial institutions.

We question also the definition that is footnoted in Section 12 of the Guidelines which states that an 'Identified Staff member should not be considered as a role or function'. We would encourage the EBA to be consistent with its arguments around what constitutes an identified staff member (i.e. material risk taker).

In its RTS on the criteria to identify 'material risk takers', the EBA argues that where an individual is identified by the criteria such as 'where an individual is awarded very high total remuneration (i.e. total remuneration more than €500,000), this is usually linked to the impact of their professional activities on the institution's risk profile'.

Therefore, when an individual no longer meets any of the MRT criteria (i.e. total remuneration less than €500,000), this should in turn be indicative that the role and accountabilities and its impact on the institutions risk profile has changed and consequently should be a sufficient explanation for the removal of an allowance in respect of § 117 (d) of the proposed Guidelines.

Lastly, it should be clarified that when allowances qualify as fixed remuneration, they should of course be taken into account in the fixed portion of remuneration for comparison purposes.

Q 10: Are the requirements on the retention bonus appropriate and sufficiently clear?

We disagree that retention payments be taken into account in the calculation of the ratio as proposed.

Firstly, § 126 requires that a "*retention bonus should be taken into account within the calculation of the ratio between the variable and the fixed remuneration as variable remuneration consistent over time with its actuarial value in line with the applied accounting standards or on a linear pro rata basis."* It is not clear what this means. An actuarial value would not typically be attributed to a retention bonus. A provision may be made in an employer's accounts for longer term arrangements but not for payments promised and paid out within the same year.

It is also not clear why retention bonuses would be counted, for these purposes, in a manner which is different to any other variable remuneration, such as deferred bonuses or LTIPs, which are valued at vesting, or as we would prefer (see our response to question 8 above) to reflect actual market practice, upon grant.

Lastly, § 182 requires that "*the ratio between the variable and fixed remuneration components should be set independent of any potential future ex post risk adjustments or fluctuation in the price of instruments*". Retention bonuses are precisely used to incentivise extremely valuable personnel to carry out functions such as business reorganisations.

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

No. We recommend that the Guidelines align the treatment for redundancy and severance payments to be made in accordance with existing firm policies which are applicable to all staff.

Jurisdiction

It should be clarified that the Guidelines only apply to the extent possible under local law (which would include legislation, regulations, case law and custom and practice) and should be viewed from a local perspective. In addition there are a number of paragraphs that are unworkable for many countries outside of Europe. It is recommended that outside of Europe, this section of the Guidelines apply to identified staff only or that other sections are limited in scope to reflect local law and custom.

Definition and types of severance payments

The definition of severance payments is unclear and what is intended to be covered in this section needs to be clarified.

Treating all severance payments in the same manner and applying all clauses to them is unworkable. A distinction should be made between severance payments due to (i) redundancy situations such as business closures/reduction etc. (ii) litigation (actual or potential) settlements (iii) other severance payments. "Standard" severance payments are remuneration for loss of employment and are not payments for performance whether or not they are set within the firm's remuneration policy.

Maximum amounts

- We note that a severance payment can be very dependent on circumstances and is often used as a negotiation tool. To have a maximum amount prescribed through regulation would mitigate against the ability and discretion of an institution to use a severance payment as a tool with which to negotiate an employee's exit.

- In non-redundancy situations and in some countries (such as APAC) such payments are set by market practice and employee representative/work council agreements/pressure and so cannot be determined by a maximum amount.
- Payments due under local law and which are mandatory following decision of a court (see § 152a) should be excluded from all provisions as there is no opportunity to adjust these payments.
- Applying a maximum limit to litigation settlements is unworkable, as such payments should reflect legal risk and maximum potential remuneration which will vary from case to case and between relevant individuals.

Adjustments to payments

In some jurisdictions, while there may be a performance or misconduct issue which is the primary cause for an employee's exit, the only legitimate (and commercial) way to exit them is by way of a severance payment due to the restrictions under local law. Restricting this ability will create legal risk (such as the employee being reinstated if no payment is made) or extend failures/issues/costs for the employer who will have to continue to employ the employee. Similarly, litigation settlements (for actual or potential claims) may be paid without reflect performance over time or where there is an underlying performance issue or misconduct issue but due to the legal risks involved it is better both from a cost and risk perspective to settle the case. Such settlements should be based on the legal risk and financial exposure.

§ 142 states that 'the amount of severance pay awarded should be risk-adjusted'. We would welcome clarification from the EBA on what type of risk-adjustments are envisaged. For example, adjusting true redundancy payments for risk, business failure (§ 149 in particular would be unworkable in the majority of cases) or case by case individual assessment (including not rewarding failure or misconduct) does not reflect the general basis for redundancy, i.e. a no blame dismissal where payments are usually set by pre-defined criteria. .See also our comments above regarding litigation settlements and the basis of a risk assessment for these.

Restrictions on severance payments

§ 143 needs clarifying to understand what is envisaged by "allows for immediate cancellation" and whether this is based on local law requirements. Paragraph 143b is unworkable in some jurisdictions, for example in Asia, where there is no concept of redundancy and redundancy situations (such as wind downs and country exits) are managed via mutual agreement where the employee "voluntarily" resigns. The employee may take up another role but this doesn't remove the obligation from the organisation to pay a severance payment.

Classification of severance payments

With respect to § 153 we disagree with the inclusion of a severance payment in variable remuneration for the last performance period as this may preclude the employee from receiving an annual bonus legitimately earned if the ratio beis breached.

For the above reasons we propose that severance pay that is not related to performance be excluded in its entirety from variable remuneration for ratio purposes.

If a distinction is maintained between § 152 and §153, then §152b needs clarifying. Is the intention that a payment in relation to a non-compete payment should be limited to the annual fixed salary or is the reference to settlement intended that the cumulative amount of any payments made under the terms of a settlement which include a non-compete restriction should be limited to annual fixed salary? The latter case is unworkable and does not reflect the rest of the Guidelines.

Other comments on this section

- The interaction of the paragraphs is unclear. Provisions would be better ordered to commence with the definition of severance payment which should be a combination of § 144, 145, 146 and 152, or with an explanation of why these paragraphs are separated and distinguished. This should be followed by an explanation of impact on variable pay as referred to in § 152 and 153 (subject to the comments above).
- The requirements for involvement of control function (§ 141) are unclear.
- In addition, the reference to garden leave (§152 and 153) does not make sense since garden leave usually only applies during a notice period and payments for this are expressly excluded (§ 145).
- Local definitions of redundancy can be broader than that described in § 146 and the paragraph excludes situations which would result in redundancy payment under local law/local policy. Moreover, reference to "active" is not helpful as it implies the employee has to be in work and not on leave (e.g. maternity or sick etc.).
- Lastly there is some confusion between the use of "annual fixed salary" (§ 152) and "basic salary" (§ 153). We suggest using fixed remuneration to align with the rest of the Guidelines.

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

While we understand the rationale behind the requirements and have always operated in accordance with the underlying principle, here again a proportionate approach, particularly to the process by which organisations monitor compliance, would be more appropriate as institutions' means for ensuring staff do not undertake such practices may be limited in practice. For example, not all firms have the operational trading structures in place for their employees which allow them to track the actions of individuals. Moreover, it can be against national laws for an institution as an employer to ask other institutions to provide banking information related to their employees' activities. We therefore suggest that self-certification should be recognised as a means of complying with the requirements in this section. An alternative could be to require employees to undertake not to enter into personal hedging strategies.

We note the requirements in § 166 which state that fixed remuneration paid out in instruments renders the fixed component of remuneration to be linked to the performance of the institution. However, it is the purpose of the payment that should be determinative. In addition, components of fixed remuneration paid in shares are unlikely to provide an incentive for excessive 'risk-taking' but rather should create an alignment with the on-going performance and stability of an institution. This in turn encourages long term value creation by adopting the correct behaviours.

In some countries, corporate governance requirements and shareholder voting policies encourage a large proportion of remuneration, including elements of fixed pay, to be paid in the form of shares. Therefore, a fixed payment in the form of shares, providing that they are not contingent on performance conditions/hurdles, should not be viewed as a method of circumvention of the requirements.

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

We strongly agree with §177, but note that the rules in Sections 11 (categories of remuneration) and 12 (particular cases of remuneration components) do not follow this paragraph. Moreover, § 179 and §166 contradict each other.

We are however confused by section 15.2 (ratio between fixed and variable) which could be read to suggest that, unless exceptional or duly justified, the same fixed and variable ratio should apply to all identified staff in the same category of staff. This contradicts large amounts of the rest of the Guidelines: a fully flexible policy with the possibility for there to be no variable remuneration is irreconcilable with a requirement for the application of the same ratio of fixed/variable to all staff.

We do not understand in §182 how firms could obtain shareholder approval for potentially hundreds of different ratios for different employees and locations. Additionally, § 183 seems to contradict the prior paragraphs. We also do not understand how § 85 can be anything other than an actual ratio between the variable and fixed components that are awarded in a particular year.

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

In general, there should not be a rigid, exhaustive set of criteria for how risk should be managed as part of remuneration; rather, it should be considered throughout the remuneration process.

We agree with the requirement in §201 that it is important that objectives and measures are relevant and achievable for the individual. Within reason, and where it is possible to link the success or otherwise to the individual, the actual results and outcomes should be measured. For example, in the case of a lending officer, we suggest that it is more realistic to conduct on-going reviews of, for example, loan performance and then to investigate individuals as appropriate where consistent poor practice is found.

We agree with the requirement in §202 that it is important to use an appropriate set of risk-adjusted measures throughout the organisation, tailored where appropriate to the business area in which the employee works. Setting objectives and assessing performance against a number of measures that include a risk segment should be sufficient to meet this requirement for most employees.

Again, we agree with the requirement in §206 that there should be sufficient independent oversight of the performance of the control functions. However, we do not agree that assessment and reward for control functions performance should be entirely exclusive of overall business performance. Organisations need their functions, franchises and senior management to work together in pursuit of a common purpose, not in silos. Commercial success depends on collective accountability for driving business performance, which is done through leadership and fostering a collaborative, team-driven environment. It is important that Control Function Heads have a seat at the most senior decision making tables and that they feel a sense of shared ownership and accountability for the success of the institution.

Q 15: Are the provisions on deferral appropriate and sufficiently clear?

We support the principle of deferral as it promotes the alignment of employees' incentives with the performance of a firm. This is particularly true when the deferral period is adapted to a firm's risk horizon. Deferral can also be an extremely useful tool to retain employees and it facilitates the recovery of awards through malus should any circumstances that warrant ex-post adjustments come to light.

However, we encourage the EBA to be mindful of the fact that the longer individuals are required to wait for awards to vest and become free of the possible application of malus (or clawback), the more the perceived value of their variable pay decreases.

The decrease in perceived value of variable pay has recently been evidenced in a piece of research, "The Psychology of Incentives", carried out by PwC in conjunction with the London School of Economics and Political Science. This research shows that the Material Risk Takers (MRT) population is likely to discount the value of awards significantly more given longer proposed deferral periods. This in turn creates more pressure for banks to increase fixed pay. The effects of further fixed pay rises are well known and include increases in banks' cost base, a lower capacity to reduce costs in times of stress and a limitation on the usefulness of remuneration as an incentive tool.

The removal of the proportionality principle implies that larger, complex firms must apply deferral periods above 3 years. MRTs in these firms will therefore be penalised in comparison to less complex organisations or to positions with similar levels of responsibility in other sectors and jurisdictions which are not subject to such rules. This has potentially serious implications for the prospect of ensuring sufficiently skilled and qualified people fill senior positions in the industry in general. We are also doubtful that the extensions will create the desired regulatory outcomes (alignment of risk and rewards) because of the reduced perceived value of these deferred awards and their power as an incentive.

We also think that firms should be given the flexibility to distinguish between various populations of MRTs and to apply tailored schemes to each of these categories. This will be particularly necessary for firms to be able to attract the right people to fulfil important roles, especially in compliance and risk functions. For example, the EBA could allow firms to have flexibility between choosing a straight deferral or a shorter deferral with an additional locked in holding period where the alternatives would amount to the same number of years being covered.

We note further that the application of §240 would likely lead to different approaches in different jurisdictions and, for global organisations, regional approaches in a global system create disparities. For instance, in countries such as Germany where local labour law prohibits clawback, deferrals and malus periods would need to be significantly increased to meet the requirements, thus making talent retention a serious issue.

Q 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.

Share linked instruments

According to the Guidelines, it would now be impossible for listed stock corporations to use share linked instruments

- From an operational standpoint (IT; HR; governance; accounting and tax; external and internal communication), the distribution of shares is very complicated and costly.
- In some countries there are even legal/regulatory impediments to use shares(if the company is not listed in the country, the employees cannot receive shares: Russia, US).
- There could be also other major obstacles in several countries:
  - In terms of governance, the grant of shares to identified staff could be refused by the general meeting of shareholders, who have to provide their authorisation on such operation, or capped at a lower amount than that required.
  - Since the shares are issued at Group level, the charge corresponding to the amount of variable remuneration paid in such shares should be re-invoiced to each entity. In some countries, where the corresponding charge is not tax deductible, the payment in shares would not be possible, due to tax risks.
  - For confidentiality reasons, in countries where a very limited number of employees are identified, it would not possible to implement payment in instruments, since the re-invoicing of corresponding variable remuneration amounts is not feasible.

The attribution of variable remuneration in cash instruments indexed on the evolution of the instruments price is easier and less costly to put in place, whereas it contributes in the same way as a payment of instruments in terms of alignment of the employee with the performance and risks of the Group.

We propose that the EBA maintain the possibility for firms to use these types of instruments or contracts, which have exactly the same objective as shares (aligning staff members on long term performance with the interests of the shareholders) but are easier to put in place, can be awarded in a uniform manner to all MRTs and are less costly.

Subordinated debt instruments

The use of subordinated debt instruments (bail-inable debt) is recommended only if these instruments are effectively available within the institution.

While such instruments could reinforce the alignment of the employees with the credit quality of the institution, their granting in some cases may not be appropriate as these are instruments dedicated to large institutional investors and not to individuals. Moreover, such instruments are not meant to be repurchased by the institution itself (regulatory constraints) and there is no secondary market for employees to sell these type of instruments at the end of the retention period (liquidity very difficult to ensure).

We propose that the EBA should maintain flexibility on the use of such instruments which are quite complex to put in place for “retail” populations. In general, consideration should be afforded to the complexity of the instruments used versus the perceived value of awards. The employee value proposition should be clear, simple and aligned to the business strategy.

Payment of dividends/interest

We disagree with the proposal in §255.

We understand the EBA’s view that institutions should not construct deferred instruments with disproportionate interests arising during the deferral period, but where interest or dividend-equivalents are aligned with commercial rates and/or receipts available to other market investors, there should be no prohibition on paying equivalent amounts to employees. Dividends/interest on instruments that have been awarded as variable remuneration under deferral arrangements should therefore be paid to employees receiving those awards. Disallowing this would further decrease the value of deferred remuneration and accentuate the differences between MRTs and non-MRTs as well as the differences between firms in the EU and other jurisdictions. We also consider that this would be contradictory to the requirements in other sectors, e.g. for Alternative Investment Managers. Moreover, not including interest or dividend payments should lead to a discount in the valuation of the award, the fair value of awards taking such payments into account. As such, a restriction on the payment of dividend equivalents would also create a disparity in the true value of awards taken into account for the purpose of the variable/fixed pay ratio between an institution that pays dividends to its external shareholders and an institution that does not pay dividends (and may decide to retain the funds or uses the funds to buy-back shares).

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

In general we consider that the setting of retention periods should be considered in parallel with deferral periods (please see our answer to question 15 above).

We wish however to make the following additional comments:

- § 264 a. seems to suggest that the retention periods of upfront awards for members of the management body and senior management should be the combined length of the deferral and retention periods, i.e. 6 years. This would be a significant departure from current practice and also exponentially higher than the proposed one year retention period for deferred awards. In essence this makes the upfront non-deferred element into a deferred element. Such a structure is unnecessarily complex and bureaucratic. It would be easier simply to have a higher deferral percentage and pay the upfront portion in cash.
- Fixed retention periods of 1 year could have negative fiscal impacts for employees as in some Member States taxes and social charges are required to be paid at the acquisition date, not at the end of the retention period. If both acquisition and end of retention period

do not take place in the same fiscal year, employees will have difficulties paying these charges.
- In other Member States, permission will be given for employees to sell shares to meet tax obligations. In such cases, the retention period should only apply to after tax shares.

We propose that the EBA should maintain a minimum 6 month retention period.

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

Yes, we are supportive of the Guidelines in this area as they will help to achieve consistent practice throughout the EU. However the application of clawback as envisaged, particularly at § 271 will have negative tax consequences. Any award that vests will be subject to tax and social charges. Any recovery from the employee at more than the net after tax amount may impose an unfair penalty as it is unlikely to be possible in all locations to recover taxes paid. We would therefore encourage the EBA to require any clawback to be for the net (after tax) amount of any paid out award.

Q 19: Are the requirements in Title V sufficiently clear and appropriate?

We have no comments on this section.

Q 20: Are the requirements in Title VI appropriate and sufficiently clear?

We have no comments on this section.

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

Q 22: Institutions are welcome to provide costs estimates with regarding the costs which will be triggered for the implementation of these Guidelines. When providing these estimates, institutions should not take into account costs which are encountered by the CRD IV provisions itself.

In response to questions 21 and 22, we note that impact assessments used in the past have consistently underestimated the amount of time and effort and therefore cost involved in implementing regulations, and we expect the same on this occasion. The level of detail and the prescriptive nature of the rules, particularly around the abolition of the proportionality principles will add significantly to the workload of organisations. We have tried to outline the likely increase in the volume of entities and employees covered by the rules in question 5. For the member firms taking part in our survey, the number of legal entities would increase by a factor of 12, with the number of individuals being subject to the rules increasing by 3 times compared to the current situation.

Appendix - Potential conflicts between local corporate governance rules and arrangements and the requirements set out in Section 6

Example 1

Section 6 of the Guidelines imparts the responsibilities and governance oversight of the remuneration policy to the supervisory board. It also specifies that the remuneration committee should be staffed by supervisory board members. These requirements do not fit with the German two-tier board structure (under the German Stock Corporation Act) which is made up of the Supervisory Board, an independent control body, and the Management Board, who are the executive officers of the Bank.

For instance, the granular role that the proposed Guidelines afford to Supervisory Board members in the design of the remuneration policy and duties of the remuneration committee would be performed by the Management Board in this instance. Following German requirements, the Management Board reports an overview of the principle remuneration policy and structures annually to the Supervisory Board, which is supported by a "supervisory remuneration committee". This Committee establishes a closer link to, and focus on, Group remuneration matters by the Supervisory Board by monitoring the structure of remuneration systems for senior management and employees.

Example 2

The draft Guidelines state that remuneration committees need to "provide support and advice to the supervisory function on the design of the institution's remuneration policy...; and support the supervisory function in overseeing the remuneration policies, practices and processes"….(§44a and b). The boards of UK firms will normally delegate authority to their remuneration committees to perform supervisory function duties in respect of remuneration policy matters. This is also in line with the provisions of the UK Corporate Governance Code. Under this arrangement, the remuneration committee would effectively sit at the top of the remuneration governance hierarchy and would not therefore normally provide support and advice to, or be responsible for preparing decisions for, a more senior committee. It would be helpful if the EBA could reassure firms that this type of arrangement is in keeping with the spirit and the letter of the Guidelines as some of the language within the Guidelines is potentially confusing in this respect.

Example 3

The draft Guidelines require the supervisory function to take into account the input provided by all competent corporate functions and bodies, including the nomination committee (§47). It is accepted that remuneration committees should seek input from other functions and committees, however the reference to the nomination committee is not required here as this committee would not normally have a role to play in remuneration matters, new joiner arrangements being the responsibility of remuneration committees themselves.

Example 4

The draft Guidelines require all significant institutions at individual, parent company and group level to establish a remuneration committee (§39). We understand that this would require, for example, a non-EU headquartered firm to establish several remuneration committees for each of its significant entities in the European Union.

The role of these local remuneration committees as envisaged by the Guidelines (§44) could conflict with the firm's regulatory obligations. Taking a US-headquartered firm as an example, it could conflict with the obligations of the group level remuneration committee to review employee compensation at the parent company level and approve senior officer consistent with the statements made in public filings, for example if such an employee was also a member of a local (CRD) management body.

It is also unclear how the required decision-making powers of these local remuneration committees would interact with the autonomy of the group-level remuneration committee, which is responsible to the firm's Board of Directors, and ultimately the firm's shareholders, for setting the firm-wide remuneration policy and decisions consistent with public filings, as well as people and the terms and conditions associated with ex post facto adjustments.

Similarly, the composition of these multiple remuneration committees as contemplated by the Guidelines (§42) could result in multiple layers of independent individuals providing conflicting advice to different groups of senior management with respect to individuals who are part of individual, parent and group level compensation programs, making responsibility and accountability less transparent. This outcome would conflict with any important messaging and communication with impacted individuals. This impacts the complexity of remuneration governance, and reduces its quality, an issue further compounded by the lack of access of local remuneration committee to line of business and global peer information outside of the legal entity it is directly concerned with