

MEMO# 29085

June 11, 2015

Response to European Banking Authority Consultation Paper on Draft Guidelines on Sound Remuneration Policies

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TO: ICI GLOBAL REGULATED FUNDS COMMITTEE No. 31-15
INTERNATIONAL COMMITTEE No. 32-15 RE: RESPONSE TO EUROPEAN BANKING AUTHORITY CONSULTATION PAPER ON DRAFT GUIDELINES ON SOUND REMUNERATION POLICIES

As we previously informed you, in March the European Banking Authority issued a consultation paper regarding revised guidance on the remuneration aspects of the Fourth Capital Requirements Directive (CRD IV). [\[1\]](#) We submitted the attached response to the consultation on June 4.

In general, institutions that are subject to CRD IV have to apply sound remuneration policies to all staff and specific requirements for the variable remuneration of staff whose professional activities have a material impact on the institutions' risk profile. Under CRD IV, the EBA is required to develop guidelines on remuneration policies for all staff as part of the institution's internal governance arrangements, as well as remuneration policies for identified staff.

As described in more detail below, the EBA's proposed guidelines with respect to application in the group context and proportionality raise a great deal of concern for UCITS and AIF managers, both in their implementation through the EBA guidelines as well as potential alignment of UCITS V and the AIFMD with these positions.

Group Context: EBA seeking application of CRD IV to all subsidiaries of a bank even though these are already subject to a strict remuneration framework

The EBA's proposed guidelines provide that a consolidating institution must ensure that all subsidiaries within the group even those that are not themselves subject to CRD IV apply the group-wide remuneration policies to all staff and the additional requirements to those staff member whose professional activities have a material impact on the group's risk

profile. The EBA states additionally that, where specific CRD requirements conflict with sectorial requirements (e.g., those under AIFMD or UCITS), a firm's remuneration policy should set out for the identified staff which requirements should apply within the entity on an individual basis. Concretely, the potential consequence of this, if adopted, would be the imposition of cap on bonuses for UCITS and/or AIF manager captured by these provisions as subsidiary of a banking group. The consultation sought feedback on whether these guidelines on group context are appropriate and sufficiently clear.

In our response, we explain that the guidelines regarding remuneration policies and group context are not appropriate because: (i) they are built on an overly-expansive reading of CRD IV Article 92(1); (ii) they undermine the political agreements found between co-legislators at Level 1 in respect of other legislative pieces (i.e., UCITS V and AIFMD) as these legislation pieces do not cross-reference CRD IV but impose a framework adapted to the sector they regulate; and (iii) they would create an un-level playing field for UCITS and/or AIF managers. The requirements should apply, in our view, only when these affiliates are not already subject to sectoral regulation fully inspired from the same principles – e.g., UCITS and/or AIF managers. We further argued that the EBA does not need to apply the remuneration guidelines in the manner contemplated because, to the extent a relevant Member State banking regulator believes a significant risk exists in a particular circumstance, the banking regulator would have ample authority to step in to stop the banking entity from such perceived risky organization.

Proportionality: Concept put on its head

Perhaps even more troubling than the EBA's proposed position on remuneration in group context are the EBA's proposed guidelines on proportionality. On this issue, the EBA states that, based on preliminary legal analysis of the remuneration principles, the approach to the application of the principle of proportionality has been changed compared to the 2010 CEBS Guidelines with respect to the possibility to "neutralize" some of the principles such as the deferral of variable remuneration, the pay out in instruments and the application of malus and clawback. The EBA takes the position that CRD IV does not provide for any explicit provision that allows for a waiver of provisions, and that the particular remuneration requirements have to be applied at least at the minimum thresholds set by the CRD IV.

In an effort to gain certainty on this issue, the EBA asked the European Commission for its view on the application of the principle of proportionality. [\[2\]](#) In the response to the EBA, the Acting Director General of the Commission's Directorate-General Justice and Consumers (the banking remuneration topic has been switched to another Commissioner portfolio) expresses the opinion that the remuneration requirements must be applied without exemptions and exceptions to all institutions. [\[3\]](#) The EBA sought input from the industry on the impact of the application of these principles in full to all institutions (and in particular to small and non-complex institutions).

In our response we express our firm belief that the EBA's preliminary legal analysis is incorrect, and further, that this approach is inappropriate from a policy perspective. We explain that the EBA's interpretation is contrary to the CRD IV Level 1 text, inconsistent with the proportionality principle under EU law, and contrary to legitimate expectation and legal certainty. We further argue that the EBA's interpretation would lead to a dual-regime and un-level playing field for UCITS and/or AIF managers, depending on the applicability of the CRD IV requirements to the manager. In particular, for UCITS and/or AIF managers to which the CRD IV remuneration framework would apply, there may be significant negative impact both with respect to the firm's financial operations and the quality of talent the fund

manager could retain. We stress that “upward” and “downward” proportionality affords firms the flexibility to address issues such as remuneration on a global level in a tailored, reasonable manner.

Next Steps

As mentioned above, we are gravely concerned about the impact on UCITS and/or AIF managers should the EBA’s guidelines be adopted as proposed because of the direct impact on UCITS and/or AIF managers that would fall under the CRD IV remuneration framework and, then, potential contagion to all UCITS and/or AIF managers. Our concerns about the interpretation of proportionality are further heightened because ESMA is currently considering its own guidance on remuneration under UCITS V and we understand that, at this point, some ESMA members and, to some extent, ESMA staff are minded to accept the EBA interpretation of proportionality on the ground it is backed by the European Commission. Although UCITS V does not contain a bonus cap, it does include specific requirements regarding deferred and variable compensation, which would then only be allowed to be applied proportionately “upward.” Similarly, although AIFMD remuneration guidelines have already been adopted, including with the more flexible interpretation of proportionality, our first discussions with ESMA members make us believe this interpretation could be challenged in the future.

We are actively engaging with EU institutions (EC’s DG FISMA and DG Justice and Consumers; MEPs; potentially EBA; and ESMA) and Member State regulators and policymakers on this important issue and will keep members apprised of key developments as they occur.

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[Attachment](#)

endnotes

[1] The consultation is available at:
<http://www.eba.europa.eu/documents/10180/1002374/EBA-CP-2015-03+%28CP+on+GLs+on+Sound+Remuneration+Policies%29.pdf>

[2] See the attached letter from Andrea Enria, Chairperson, European Banking Authority, to Paraskevi Michou, Acting Director-General, European Commission Directorate-General for Justice and Consumers, dated 8 January 2015.

[3] See the attached letter from Paraskevi Michou, Acting Director-General, European Commission Directorate-General for Justice and Consumers to Andrea Enria, Chairperson, European Banking Authority, dated 23 February 2015.