Frankfurt am Main,
3 June 2015

BVI Position on draft guidelines on sound remuneration policies under Article 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013

BVI[1] gladly takes the opportunity to present its views on EBA's consultation paper regarding draft Guidelines on sound remuneration policies under the requirements of the CRD IV.

Our members are asset managers providing management services to collective investment undertakings such as UCITS or AIF. Most of them are investment management companies within the meaning of the UCITS Directive 2009/65/EC or the AIFM Directive 2011/61/EU for which the CRD does not apply. However, some of them will affected by the future guidelines if they are part of a banking group. Other members are investment firms which directly fall within the scope of the CRD and the proposed guidelines because they provide investment services such as portfolio management, investment advice or execution of orders on behalf of clients. In principle, these investment firms are not considered as significant institutions due to their remuneration structure and the nature, scale, complexity, risk content and international scope of their business activities. They therefore use 'neutralisations' of certain remuneration requirements under the previous guidelines for the whole institution or identified staff receiving only a low amount of variable remuneration.

In both cases, for investment management companies being part of a banking group and small or non-complex investment firms, we see grounds for practical and substantial legal objections regarding the interpretation of the principle of proportionality and the broad scope of application as suggested in the consultation paper. In this context, we would like to draw EBA's attention to our key issues and concerns before turning to detailed remarks on the questions for consultation.

I. Key issues

1. Principle of proportionality

We strongly disagree with the proposed interpretation of the proportionality principle according to which the remuneration requirements of the CRD are supposed to be applicable without exemptions and exceptions to all institutions, particular to small and non-complex institutions, and identified staff. In detail:

a. We do not see any practical reason to change the current approach.

(1) The current approach is sufficiently effective

The current approach is sufficiently effective in order to protect and foster financial stability within the Union. Consistent, efficient and effective supervisory practices are already in place. In particular, major efforts involving great costs have been undertaken by investment firms to implement the remuneration requirements under the CRD III and more recently under the CRD IV in 2014.

[1] BVI represents the interests of the German investment fund and asset management industry. Its 89 members manage assets in excess of EUR 2.6 trillion in UCITS, AIFs and assets outside investment funds. As such, BVI is committed to promoting a level playing field for all investors. BVI members manage, directly or indirectly, the assets of 50 million private clients over 21 million households. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

According to EBA's draft impact assessment (paragraph 42, page 104), EBA is claiming that the current approach taken was not sufficiently effective and did not lead to an appropriate level of harmonisation in particular regarding the application of deferral, retention, pay out in instruments and the application of malus and claw back. EBA has not, however, provided any proof that this assertion is correct. In particular, the outcome of a baseline scenario and a cost-benefit analysis are missing in the impact assessment. Therefore, we cannot ascertain whether the approaches used by the institutions 'differ significantly and without performing specific risk assessments'. However, it is an implication of the principle of proportionality that different solutions are in place taking into account the size, internal organisation and the nature, scope and complexity of institutions' activities. Moreover, remuneration policies without performing specific risk assessments should be reviewed by competent authorities; this question is not subject of the interpretation of the principle of proportionality.

(2) Cost-benefit analysis

Changing the interpretation of the principle of proportionality one and a half year after the implementation date of the CRD IV and two years after the implementation of the remuneration rules of the AIFMD means that asset managers are obliged to change their remuneration principles fundamentally which involves additional and avoidable costs. In relation to the risk situation in the asset management area, the burden of the implementation and the cost impact would be too heavy.

b. We do not see any legal basis to change the current approach.

(1) Principle based approach of the Recommendation of the European Commission

According to Article 75 paragraph 2 of the CRD IV, EBA's guidelines shall take into account the principles on sound remuneration policies set out in the Commission's Recommendation 2009/384/EC of 30 April 2009 (hereafter: the Recommendation). According to the Recommendation, a risk-focused remuneration policy should be adopted which is consistent with effective risk management and does not entail excessive risk exposure (cf. recital 12 of the Recommendation). The Commission determines as follows:

> "Indeed, some of the general principles on sound remuneration practices may be of more relevance to certain categories of financial institutions than others. Therefore, in order to avoid unjustified costs and to ensure proportionality, it is foreseen that Member States, when implementing the general principles, may adapt and complement them according to the situation of the financial institutions concerned."

In detail, according to Section II No. 4.3, 4.4 and 4.6 of the Recommendation, **deferral arrangements, the pay out in instruments and malus arrangements** should only be apply for institutions, where a **significant bonus** is awarded. Therefore, the current approach using 'neutralisations' of such remuneration requirements for identified staff receiving only a low amount of variable remuneration is in line with the Recommendation and must be considered by EBA in establishing remuneration guidelines in the meaning of Article 75 paragraph 2 of the CRD IV. Any discussion on this matter is missing in the consultation paper.

(2) Unmodified legal position under the requirements of CRD IV

Moreover, according to Article 75 paragraph 2 of the CRD IV, EBA shall issue guidelines on sound remuneration policies which comply with the principles set out in Articles 92 to 95 of the CRD in the light of the proportionality principle. EBA's new interpretation of the principle of proportionality is not consistent with the requirements of Article 92 paragraph 2 of the CRD which states that proportionality should be applied to institutions "**in a manner and to the extent that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities**". This provision exactly corresponds to the requirements of the CRD III. With regard to the draft cost-benefit analysis/impact assessment (page 96 of the consultation paper), EBA itself did not identify the proportionality principle as a change introduced by the CRD IV so there is no need for a new interpretation of the principle of proportionality and to change the current approach established under the CEBS guidelines.

(3) Recital 66 of the CRD IV

EBA's proposed new approach fails to take into account Recital 66 of the CRD which states as follows:

> "In order to ensure that the design of remuneration policies is integrated in the risk management of the institution, the management body should adopt and periodically review the remuneration policies in place. The provisions of this Directive on remuneration should reflect differences between different types of institutions in a proportionate manner, taking into account their size, internal organisation and the nature, scope and complexity of their activities. **In particular it would not be proportionate to require certain types of investment firms to comply with all of those principles.**"

This Recital of the CRD IV is equal to Recital 3 of the CRD III which states that remuneration principles should recognise that credit institutions and investment firms may apply the provisions in different ways according to their size, internal organisation and the nature, scope and complexity of their activities and, in particular, that it may not be proportionate for investment firms referred to in Article 20(2) and (3) of Directive 2006/49/EC to comply with all of the principles. The legislator's intention regarding the interpretation of the proportionality principle under the CRD III which is considered in the CEBS' guidelines with the opportunity to neutralise certain remuneration requirements is therefore unchanged under the rules of the CRD IV.

(4) Absence of discussion concerning the global competition

In addition, a discussion concerning the effects on global competition between financial institutions is missing in the consultation paper. The Commission states in its recital 6 of the Recommendation:

> "Given the competitive pressures in the financial services industry and the fact that many financial undertakings operate cross-border, it is important to ensure that principles on sound remuneration policy are applied consistently throughout the Member States. **However, it is acknowledged that to be more effective, principles on sound remuneration policy would need to be implemented globally and in a consistent manner."**

In our assessment of the legal positions in other countries outside from Europe we gained the impression that the principle of proportionality is implemented in a more principle based manner similar to the current interpretations under the CEBS guidelines. For instance, in the US, different agencies

have designed 'Guidance on sound incentive compensation policies'[2] to help ensure that incentive compensation policies at banking organisations do not encourage imprudent risk-taking and are consistent with the safety and soundness of the organisation. In this context, stricter requirements in Europe would lead to competitive disadvantages for the financial industry in the Union.

(5) Intention of the Financial Stability Board (FSB)

Finally, it must be noted that the remuneration requirements are based on the FSB Principles for Sound Compensation Practices. These principles are intended to apply to significant financial institutions, but they are especially critical for large, systemically important firms.

We note that the consultation paper in no way anticipates or prevents further analysis in subject of the issues named above. Rather, EBA is referring to a letter of the European Commission (dated: 23 February 2015) with regard to the interpretation of Article 92(2) of the CRD IV which is not part of the consultation paper. EBA has published that letter much later then the new proposal restricting the principle of proportionality which was not accepted by the market participants at the hearing on 8 May 2015. Moreover, the letter of the European Commission is a result of EBA's request because EBA's legal department has raised concerns regarding the current interpretation of the principle of proportionality. At the same time, we have every right to be astonished that, according to a statement made by EBA at the hearing, the interpretation of the principle of proportionality should not be part of the consultation but only the question why the new proposed interpretation of the legal text would be harmful for the investment firms.

By doing this, EBA completely denies the intention of the European co-legislators and the original intention of the Financial Stability Board creating remuneration guidelines for large and systemically important firms. Such overstretching of the EBA regulatory remit has no basis in the ESAs' founding acts or in Article 75 paragraph 2 of the CRD and might conflict with the principle of separation of powers endorsed by the EU Treaties. Moreover, this is particularly surprising as EBA itself describes in its letter to the European Commission that a strong majority of the members of the Board interpreted the wording of the CRD IV – in light of recital 66 of the CRD IV – in a way that allows small and non-complex institutions to partially or fully waive certain CRD IV provisions.

As the European Commission points out in its letter, it is neither for national competent authorities nor indeed for EBA to decide that certain rules adopted by the co-legislator shall not apply. This applies particularly in the opposite case: EBA has no authority to decide that certain rules shall apply. In this context, EBA and the European Commission should take into account the agenda of Jean-Claude Juncker (President of the European Commission)[3]:

> 'This Commission was elected on the basis of a clear political mandate: the ten priorities set out in our Political Guidelines. Today's Work Programme is the translation of those ten priorities into concrete first deliverables. Citizens expect the EU to make a difference on the big economic and social challenges and they want less interference where Member States are better equipped to give the right response. **That is why we committed to driving change and to leading an EU that is bigger and more ambitious on big things, and smaller and more modest on small things**."

[2] https://www.fdic.gov/news/news/press/2010/pr10138a.pdf.
[3] http://europa.eu/rapid/press-release_IP-14-2703_en.htm.

Finally, the new approach raises questions as the German legislator has implemented the principle of proportionality in law and in a separate Regulation in the meaning of the CEBS Guidelines and recital 66 of the CRD IV and has decided that some of the remuneration rules shall not apply (such as the pay-out process and the bonus limit for small investment firms). Therefore, the legal text of the German law is binding.

Therefore, we urge EBA to maintain the risk-focused and principle-based approach under the current CEBS guidelines on remuneration policies and practices with the approach of neutralisation, particular for small and non-complex institutions. Moreover, there is no need to suggest legislative amendments that would allow for a broader application of the proportionality principle.

2. Group context

We strongly disagree with the provided definition of staff including subsidiaries not subject to the CRD such as management companies in the meaning of the AIFMD or the UCITS Directive and the proposed requirements to fulfil the bonus cap of the CRD IV. There is no legal basis for this approach under the CRD IV. In particular, investment management companies are subject to their own specific remuneration requirements under the AIFMD and the UCITS V Directive.

Moreover, extending the CRD IV pay rules (and in particular the variable pay cap) exclusively to non-CRD regulated entities that are subsidiaries of CRD IV groups would create competitive disadvantages and unlevel playing fields in these businesses or geographies where entities that are operating outside CRD IV groups (e.g. US parented asset managers) are not required to apply the same set of rules. Certainly with the number of entities and individuals affected by the CRD IV requirements to rise accordingly this is another area where, viewed in the context of the changes to the proportionality principle, there will be significant cost impacts.

Therefore, we request EBA to change the group approach in such a way that parent undertakings must only ensure that subsidiaries for which other special remuneration requirements such as under the AIFMD, UCITS Directive apply comply with their special requirements concerning remuneration systems.

II. Specific comments

We would like to answer EBA's questions as follows:

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

We strongly disagree with the provided definition of staff including subsidiaries not subject to the CRD, in particular investment management companies in the meaning of the AIFMD and UCITS Directive which are part of a banking group.

Investment management companies are subject to their own specific remuneration requirements such as Article 13 including Annex II of the AIFMD and Article 14a of the UCITS V Directive. Moreover, they are offering services and products under different EU frameworks such as UCITS Directive, AIFMD and MiFID and are legally required to comply with three different sets of rules with regard to remuneration of

their personnel. In addition, investment management companies being part of a banking group are affected by the CRD IV standards on remuneration. Asset managers belonging to an insurance group could also be affected by the future Solvency II remuneration rules. These five EU regimes – UCITS Directive, AIFMD, MiFID, CRD and Solvency II – co-exist on separate grounds and differ considerably in many details concerning the remuneration structures. This leads to major difficulties in the practical application of these provisions, since management services in an entity are generally structured according to the expertise of specialised management teams. Thus, it is very common for asset management firms to have management teams for e.g. European corporate bonds, North American or South-East Asian equities which then provide services to all portfolios focusing on the relevant markets. In this situation the affected fund managers need to be remunerated according to CRD/Solvency II, AIFMD, UCITS and MiFID rules within one employment contract which is barely possible to be put into effect. This situation would be further exacerbated by the proposed guidelines that aggravate the legal competition problem in relation to the fund frameworks.

Independently of these practical problems, EBA's proposal is not compatible with the requirements of the CRD IV. According to Article 75 of the CRD, EBA shall issue guidelines on sound remuneration policies which comply with the principles set out in Articles 92 to 95 of the CRD. With regard to Article 92 of the CRD, the application of the remuneration requirements shall be ensured by competent authorities **for institutions** at group, parent company and subsidiary levels, including those established in offshore financial centres. With regard to Article 3 paragraph 1 (3) of the CRD IV with reference to Article 4 paragraph 1 (3) of Regulation (EU) No 575/2013, "institutions" are defined as credit institutions or investment firms. This does not include investment management companies in the meaning of the AIFMD or UCITS Directive. Therefore, the guidelines could only apply to staff of institutions.

To be distinguished from this question is the responsibility of a parent company to ensure group-wide consistency as stated in Article 109 of the CRD. **However, the interpretation of Article 109 of the CRD is not subject of EBA's competence set out in Article 75 of the CRD.**

Moreover, according Article 109 of the CRD, the consolidating institution shall ensure that subsidiaries not subject to the CRD implement arrangements, processes and mechanisms in a consistent and well integrated manner. Contrary to EBA's statement under paragraph 66 of the consultation paper such subsidiaries are not required to "**apply**" the group wide remuneration policies. The rule only seeks to ensure that subsidiaries which themselves are not subject to the CRD "**implement**" a remuneration policy. Because the remuneration policies under the CRD are consistent with the requirements under the AIFMD (or the UCITS Directive)[4], there is no need to extent their scope to the non-bank entities such as entities subject to the AIFMD or the UCITS Directive.

Finally, clarification is requested as to whether the definition of 'staff' includes contingent workers (externals). In principle, the institution has no impact on the compensation of contingent workers, therefore would be unable to directly influence their compensation per the Guidelines. Attempts to mandate how externals are to be paid could result in the loss of contractor employment.

However, the other definitions provided by EBA are sufficiently clear.

[4] Cf. ESMA's Questions and Answers – Application of the AIFMD; Q&A 4 page. 6:

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

Yes. In particular, we welcome the approach that dividends paid on invested shares or equivalent ownership interests that staff receive as shareholders or owners of an institution are not part of the remuneration for the purpose of the guidelines.

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

In principle, the guidelines seem sufficiently clear. However, as a general remark, the proposal regarding the remuneration policy will likely have to be amended upon implementation of the revised shareholder rights directive (SRD II). According to the current discussion, in case of companies whose shares are admitted to trading on a regulated market situated or operating within a Member State, e.g. the remuneration policy will have to be approved by the general meeting. Further, it might be worth analysing whether some of the wording could already be aligned with the SRD II wording.

Further, EBA proposes that the management body in its supervisory function should be responsible for adopting and maintaining the remuneration policy of the institution (see **paragraph 17**). This requirement is not entirely clear for jurisdictions where a two-tier system (separation of the management function and the supervisory function in different bodies) is required (e.g. in Germany). EBA should clarify that the body responsible for supervision should be in responsible for design and oversight of the remuneration policy.

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

1. Governance of remuneration

Section 6 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. This does not fit with the German two-tier structure. In accordance with the German Stock Corporation Act, our members have a two-tier board structure made up of the supervisory board, which is an independent control body, and the management board, representing the executive officers of the institution. Flexibility in the definition and composition of the 'remuneration committee' is important.

With regard to **paragraph 42**, we request to delete the requirement that the '*majority of members of the remuneration committee should qualify as independent*'. We consider this to be too far-reaching, particularly as Article 95 paragraph 1 of the CRD only states that the remuneration committee shall be constituted in such a way as to enable it to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk, capital and liquidity.

We suggest a clarification on **paragraph 39** that subsidiaries such as investment management companies can be drawn on any central processes (e. g. use of a central remuneration committee) if it is part of a group and one of the group companies has to apply the banking or insurance sector rules on remuneration. Therefore, clarification is requested, specifically, whether the requirement for remuneration committees on a legal entity basis can be delegated to the parent company.

2. Group context

According to **paragraph 63** of the consultation paper, staff within entities that fall within the scope of the AIFMD and UCITS Directive have to comply with the bonus cap if their professional activities have material impact on the group's risk profile on a consolidated basis. As mentioned above, we strongly disagree with the proposed group context. In detail:

a) Reference is made to our response to question 1.

b) In addition, the application to subsidiaries then overrides the intention of the European legislator in explicitly excluding UCITS V and AIFMD from the bonus cap. Neither the AIFMD nor the UCITS Directive applies a bonus cap to AIFMs or UCITS management companies. In particular, UCITS V management firms were explicitly exempted from the bonus cap after thorough discussion in the European Parliament and among Member States. The reason why legislators rejected the bonus cap for UCITS was that they recognised that asset manager remuneration is aligned with the client's experience as variable remuneration is linked to long term performance. Moreover, the European Parliament's acknowledgment in UCITS V that bank remuneration policy (the prescriptive variable remuneration limit) is inappropriate for aligning risks within UCITS managers is indicative for the need to apply remuneration policies in a proportionate way to asset management firms falling under both CRD and AIFMD. The remuneration provisions in both AIFMD and UCITS Directive are in many other respects nearly identical to the provisions of the CRD.

c) Furthermore, there is no direct link between the professional activities of investment management company staff and the solvency of the institution's balance sheet as they do not trade on the own books of the company. Hence, there is no risk that remuneration policies and incentives have a direct link with the investment management company's solvency. Therefore, fundamental differences exist between the business models of management companies and the banking and investment banking sector.

   However, as EBA refers to any operational risks taken by the investment management company which could have an impact on the group's risk profile, such risks are very low. The reason for this is that UCITS's and AIF's assets are segregated from the own assets of the management company and from other clients' assets. Investment management companies are required to measure, manage and monitor operational risks (including reputational risks). This involves that investment management companies are obliged to cover operational risks (such as professional liability risks) through additional own funds (cf. Article 14 of the Delegated Regulation (EU) No 231/2013 of 19 December 2012). This measurement minimizes the parent institution's capital requirement for operational risks on the consolidated basis. Moreover, in practice, operational risks taken by an investment management company amount to about average 30,000 Euro per year and each investment management company over a period of the last five years.[5] In our view, this amount is in principle not capable of having a **material impact** on the group's risk profile on a consolidated basis.

[5] Cf. BVI statistic on losses that have occurred through operational risks.

d) However, an initial reference point for identification of staff should be the fact that staff's professional activities have material impact on the group's risk profile on a consolidated basis. However, such a proposal is not likely to work in practice. This applies particularly to the proposal in **paragraph 106** of the consultation paper that for subsidiaries not subject to the CRD the identification assessment should be performed by the consolidating institution based on information provided by the subsidiary.

   It should be noted, according to the remuneration requirements under the AIFMD and the UCITS Directive, that investment management companies are responsible to identify their staff, to define the basis on which staff are being paid and to negotiate wages. In this context they need to know the impact of their staff's responsibilities on the company's or managed funds' risk profiles. However, they are not able to identify the group's risk profile or whether their staff have material impact on the group's risk profile. This simply means that they do not know the group's risk profile on the consolidated basis. Therefore, they are not able to take into account staff's impact on group's risk profile.

   On the other hand, the parent company knows the group's risk profile on consolidated basis but the risk takers of the investment management company which could have material impact on such a risk profile are unknown or even non-existent (see above).

e) In this context, EBA's proposal using the criteria in Articles 3 and 4 of the RTS on identified staff to identify staff of the subsidiaries such as investment management companies not subject to the CRD exceeds the powers conferred on EBA by extending the RTS in the meaning of Article 94 paragraph 2 and Article 92 paragraph 2 of the CRD on subsidiaries not subject to the CRD. The scope of the RTS is limited to staff of institutions in the meaning of Article 92 paragraph 1 of the CRD subject to the CRD. As mentioned above, this does not include investment management companies in the meaning of the AIFMD or UCITS Directive.

   Moreover, it would be strange if a large UCITS management company acting purely as agent running funds with a low level of leverage was subject to the same level of requirements as a large bank, although they do not represent the same risk to the system or to investors. In this respect we believe that more qualitative criteria rather than size-based criteria should be the deciding factor in determining the proportionate application of the CRD rules especially in respect of remuneration.

However, according to **paragraph 63** of the consultation paper, risk takers of an entity subject to the AIFMD or the UCITS Directive should be limited to pay the variable remuneration in the alternative investment funds instruments or UCITS instruments. In case that such risk takers even exist, in our view, pay out instruments of the banking group would be more suitable to consider the material impact of the risk taker on the group's risk profile.

Moreover, the interaction of different guidelines under the UCITS/AIFMD regime and the CRD IV should be clarified in such a manner that parent undertakings must at least ensure that subsidiaries for which other special remuneration requirements such as under the AIFMD, UCITS Directive apply, comply with their special requirements concerning remuneration systems.

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***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 strongly disagree with the proposed interpretation of the proportionality principle according to which the remuneration requirements of the CRD are supposed to be applicable without exemptions and exceptions to all institutions, particular to small and non-complex institutions (please see for more details our key issues).

However, changing the interpretation of the principle of proportionality one and a half year after the implementation date of the CRD IV means that investment firms are obliged to change their remuneration principles fundamentally which involves additional and avoidable costs.

In general, our members anticipate the following changes in the case of changing the interpretation of the principle of proportionality in the proposed manner:

- Adjusting the content of the remuneration policies (such as changing the scope of the remuneration policy with regard to the identified staff and the payout process)
- Implementation of a payout process for parts of the bonus (such as deferral arrangements, pay out in instruments, application of malus) including software adaption for the payout process and adjusting the accounting systems (such as implementation of different payment methods and new employees' accounts, monitoring of the deferral arrangements, initiation of subsequent payments)
- In cases where a payout process is partially in place, changing the implemented processes for salary payments (such as changing the calculation process for the deferred part of the bonus and the timeline of the deferred period)
- Implementation of a bonus limit
- Adjusting the employment contracts of the identified staff including conduct of negotiations with the employers
- Informing the works council and requiring the consent of the works council (including complying with the requirements of the Equal Treatment Law); in practice, there are open questions what happens if the works council fails to give its approval under employment legislation or collective agreements (e.g. consent for malus agreements).
- Clarification of legal issues by internal/external lawyers
- Hiring external service providers for the implementation of the new requirements

Moreover, asset managers as small and non-complex investment firms make decisions with a material impact of the company or the managed funds only after consultation with the supervisory board or the investment management company which has outsourced the portfolio management of the funds. In

these cases, identified staff is not able to take high risks because of an individual interest. In relation to this risk situation, the burden of the above named implementation would be too heavy.

Overall, the cost impact is significant. This means that asset managers are forced to create at least than one new position and to pay legal and consulting fees. Moreover, asset managers are concerned about legal action relating to the payment of discretionary or variable compensation for previous years.

- **Deferral arrangements**

The administration of the new proposed requirements regarding the deferral arrangements is becoming increasingly complex. This involves less transparency in the procedures for the identified staff for which the deferral arrangements shall apply. The question therefore arises whether such a system is designed to create positive and risk-oriented incentives.

This applies particularly for identified staff receiving only a low amount of variable remuneration (such as up to 50.000 Euro). In such cases, investment firms are required to deferral parts of the bonus. Such measures are not associated with steering effects. Rather, the low amount of variable remuneration is not an incentive to take high risks.

- **The pay out in instruments**

The pay out in instruments would lead to the situation that a substantial portion of the variable remuneration shall consist of shares or equivalent ownership interests or other Equity Tier 1 instruments. However, asset managers provide management services to collective investment undertakings such as UCITS or AIF. The instruments referred to above are not designed to align incentives with the longer-term interests of the asset manager. Suitable instruments are not available.

- **Malus**

The application of malus or claw back arrangements must be individually agreed between the investment firm and the identified staff. Moreover, such measures must be part of a decision-making tool to obtain the necessary acceptance by employees. Malus and claw back arrangements will have the opportunity to influence the payroll-accounting, in particular the calculation of the income tax. The practical consequences are not foreseeable yet.

Moreover, the amounts of the payments which would fall under malus and claw back arrangements would be very small. Therefore, it is questionable whether the objective of avoiding a shortfall can be achieved. However, this is offset by risks that exist for the identified staff member.

According to the German Remuneration Regulation for Institutions (InstVV), an institution could apply a 50,000 Euro de minimis threshold for applying the requirements for identified staff under CRD IV. The draft Guidelines do not allow for such thresholds. However, the Guidelines also apply all requirements to all subsidiaries, including for the identification of risk takers. This will result in lowly paid employees being subject to the remuneration requirements for risk takers. The 50,000 Euro threshold was introduced into the InstVV to avoid a disproportionate amount of administrative work caused by deferring 40 % of a variable remuneration award of 15,000 Euro over three years (€ 2,000 in years 1, 2 and 3, with 50 % of this in shares). However, a more critical result of removing the threshold will be the reten-

tion of the lower paid employees now subject to these requirements. This is envisaged to be the largest issue for smaller legal entities.

The Guidelines state that staff who are subject to other sectorial legislation e.g. AIFMD and UCITS and are employed by a Group member have to comply with the fixed to variable remuneration ratio. While the appropriateness of this approach may be argued for a base plus discretionary bonus scenario, it is almost impossible to work towards a 1:1 or 1:2 ratio when considering industry specific remuneration structures such as Carried interest Plans. Carried Interest Plans are not part of the regular annual compensation cycle and 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 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-pay out and therefore exclusion from a ratio calculation or at the very least being subject to a broader ratio (e.g. 1:5) would be more appropriate.

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

Please see our answer to question 4.

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

It is not clear whether the guidelines regarding the capital base apply on a consolidated level only or also on a solo entity level.

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

In general, the requirements regarding categories of remuneration are appropriate and clear. However with regard to the term “payment” in **paragraph 121**, it is not clear whether the reference is to “actual” payout or “value at grant”. We strongly support the definition of the term “payment” as meaning “value at grant” rather than “actual payout”.

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 breach of the ratio. In such circumstances, fixed pay would have to be increased 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 additional red tape.

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

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

With regard to **Section 13.2** of the consultation paper, a severance payment is very dependent on the circumstances and is often used as a negotiation tool. To have a maximum amount prescribed in the regulations 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.

Paragraph 142 states that 'the amount of severance pay awarded should be risk-adjusted'. Please clarify what types of risk-adjustments are envisaged.

In **paragraph 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 due to the ratio being breached. For this reason we propose that severance pay is excluded in its entirety from variable remuneration for ratio purposes.

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

We disagree with the proposed section on circumvention which should be deleted. In particular, establishing guidelines according to circumvention criteria is not subject of EBA's competence set out in Article 75 of the CRD.

Moreover, asset managers being supervised and strictly regulated companies are legally obliged to act in accordance with the law. Lawful and ethical conduct is the basis for any action of management board, supervisory board, and employees. However, in respect of any instance of maladministration in the implementation of remuneration rules, it is the primary task of the competent authority to review the conduct of compliance and enforcement at national level, not least through directives by the authorities and obligations such as administrative action.

In this context, we strongly disagree with the proposed principles under **paragraph 163** of the consultation paper that institutions should implement appropriate checks to ensure that the proposed criteria of circumvention cannot be manipulated. This means that institutions are required to implement additional monitor and review processes. Moreover, some of the defined criteria in **paragraph 162** cannot be monitored. For instance, the defined criteria involve an obligation to carry out investigations by third parties. However, if any process is needed, it should be sufficient that the employer confirms that he is acting in line with the legal requirements.

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

Generally, the requirements of this section are clear. However, we would like to clarify the intention of **paragraph 206** which deals with the variable remuneration determination for control functions. In practice, the remuneration could be determined with reference to key group metrics such as the Core Tier 1 capital ratio, and variable remuneration for control functions, as for other divisions, is dependent on the group's ability to meet the targets. Linking the variable remuneration of control functions to such items as audit findings (as specified in the draft guidelines) would lead to great conflict of interest.

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

The application of **paragraph 240** would likely lead to different approaches in different jurisdictions. For a global organisation, regional approaches in a global system (e.g. in Germany, where actual 'claw-back' would not be possible under local labour law) creates disparity. In such locations, where deferrals and malus periods would need to be significantly increased to meet the requirements, talent retention would again be a serious issue. Furthermore, regional differences could lead to the relocation of business and/or talent to other locations with less stringent rules.

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

Paragraph 264 a) suggests 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.

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

We not agree with the impact assessment and its conclusion regarding the remuneration policies in a group context and the interpretation of the principle of proportionality. Please see our key issues under Section I and our answers to questions 1, 4 and 5.

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.*

Please see our answer to question 5.