European Banking Authority

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12 August 2013

European Banking Authority

Consultation Paper 2013-11: 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 90 (2) of the proposed Capital Requirements Directive

Dear Sirs,

The Investment Management Association (IMA) is the trade body for the UK asset management industry, representing around EUR5 trillion of funds under management. Its member firms include managers of a wide range of asset classes for a wide range of clients, including institutional funds, authorised unit trusts and open ended investment companies.

We welcome the opportunity to comment on the latest consultation.

Key messages

We support the efforts of the authorities, at all levels, to implement remuneration requirements and, with regard to cross-border financial institutions, to align their approaches.

Our members that are in scope are essentially limited license investment firms, but also some limited activity investment firms. They merely act as agents for their clients. Their activities do not extend to the provision of credit, the acceptance of deposits or dealing on their own account, which recitals eight and nine, and article two of the regulation refer to with regard to credit and market risks. Therefore, a proportionate approach should be applied to them.

It is for this very reason that CEBS 2010 *Guidelines on Remuneration Policies and Practices* currently disapply the CRD's more prescriptive elements (around remuneration committees and pay out processes) under CRD's principle of proportionality. CEBS *Guidelines* ensure that Limited licence investment firms are not subject to those CRD requirements that are intended solely for the credit and market risks posed by credit institutions and proprietary trading investment firms – banks and investment banks.

Our first request is that a proportionate approach should continue to apply to limited licence investment firms, and that CEBS *Guidelines* under CRD III should either be formally extended to CRR / CRD IV or that EBA should copy over CEBS *Guidelines* into new *Guidelines* under CRD IV such that they continue to have the same effect.

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We note that this request is already in line with European Commission, EBA and European Parliament thinking around maintaining a "proportionate" approach between banks, investment banks and asset managers:

- Recital 66 of CRD IV takes up Recital 4 of CRD III in requiring member-state legislators to differentiate between types of institutions in a proportionate manner – and in particular so as not to require certain types of investment firms to comply with all of the principles;

- CRD IV's more complete and over-arching disapplication of rules for MiFID firms that neither trade on their own account (nor operate Multilateral Trading Facilities) nor hold client money (under CRR Article 4 and CRD IV Article 3) extends proportionality in such a way that "limited limited licence firms" (so to speak) are able to disapply CRD IV as a whole; and finally

- the European Parliament's recent acknowledgment that bank remuneration policy (the prescriptive 1:1 bonus cap) is inappropriate for aligning risks within UCITS managers ensures that the same read-across of the proportionality principle from CRD to AIFMD is now logically extended to UCITS. Limited licence investment firms, less "risky" AIFMs and less "risky" UCITS managers are now all entitled to disapply those elements of CRD policy that they deem inappropriate in the context of the credit and market risks they pose.

Our second request is that this proportionate approach should also be extended to include the ability to disapply the EBA's proposed RTS on identifying categories of staff that have a material impact on an institution's profile when that institution is a limited licence firm. We would thus recommend that the EBA's proposed RTS are explicitly qualified by Recital 66 of CRD IV (replicating Recital 4 of CRD III) and that Member States are required to differentiate the application of the RTS themselves on the basis of institution type.

We believe that this is a logical extension of the proportionate approach introduced by CRD III and retained by CRD IV (as above) and in this context, we welcome the recognition of the fact that an employee's high pay does not automatically mean that the person has an impact on the risk profile of the firm and the ability of firms to demonstrate that, as confirmed in the open hearing on 4 July 2013. However, in addition to this, we maintain that the very nature of a limited licence firm means that its members of staff will never pose the credit or market risks that the EBA's RTS are designed to realign.

Again, we note that this request is already in line with EBA thinking around maintaining a "proportionate" approach under the proposed RTS, where there is the "possibility" of excluding employees, using the quantitative criteria, from the list of code staff based on an assessment of risk where they fall under the first two categories of quantitative measures (Article 3 (2) (a) and (b)), but not under (c) and (d) (i.e. where the employee's total remuneration exceeds EUR 500,000.00 or the employee is in the top 0.3% of staff. We assume that these categories are the ones referred to under "staff receiving a particularly high remuneration...where it can be assumed that they always have a material impact on the institution's risk profile", but would argue the risk assessment should be extended to the exclusion of (c) and (d) at the very least. At least under this change, the onus would be on the employer to demonstrate that the employee does not have a material risk impact.

We believe that Article 3 (2) (a) may increase the pressure to shift the balance of pay to mitigate this.

If the EBA continues the CEBS approach, then the cap will only apply to Credit Institutions and Investment Firms, but not to Limited Licence and Limited Activity Investment Firms.

This would seem sensible as the relationship between Fixed and Variable Remuneration is really a Credit Institution defence and that Credit Institutions are not subject to the Fixed Overhead Requirement, hence increasing Fixed Remuneration is not an issue for Credit Institutions in terms of the level of capital they need to maintain. Limited Licence/Limited Activity Investment Firms on the other hand are subject to the Fixed Overhead Requirement and, hence, increased Fixed Remuneration becomes a real issue as it would increase their Capital Resources Requirement by EUR 1 or every EUR 4 increase in Fixed Remuneration.

There is also the issue of Fixed versus Variable which applies to Partners/Members of Partnerships/LLPs. Profit might be deemed all Variable and, hence, the cap is not appropriate.

Extension of the scope will need time to be implemented by firms, for example changes to employment contracts, so a reasonable transition would be helpful.

Further to the EBA's open hearing last month, the IMA was pleased to hear that:

- The new rules will apply for performance year 2014.
- The rules will be applied proportionately. There is the possibility of excluding staff from the scope by using the qualitative aspects, but this will have to be documented and the rationale accepted by supervisors.
- The thresholds are backstops, which is the trend in prudential regulation, but could be changed if evidence emerges to the contrary in the consultation.
- The EBA accepted that the phrase "could be awarded" should be changed to "could be and has been awarded". In addition, references to credit and market risks and banking were not appropriate for the investment firms that are in scope of CRD IV due to them simply holding client money (but which do not deal on their own account).The EBA will consult on instruments that can be eligible for inclusion as variable remuneration next month.

Conclusion

The IMA looks forward to working with the international standard setters to develop a framework that is appropriate and effective for all stakeholders.

Annex 1 to our letter contains our formal response to the consultation, and further specific observations and questions arising from the proposals.

We hope that you will find our comments useful. Please contact me by way of e-mail (ihenry@investmentuk.org) or telephone on (00 44) (0) 20 7831 0898 should you require further information.

Yours faithfully,

Irving Henry

Prudential Specialist

Investment Management Association

Annex 1

Q1: Is the list of specific functions listed appropriate or should additional functions be added?

The list feels definitive, which will make it harder to exclude employees from the scope. There should be a test of materiality based on economic analysis.

Some of the functions listed may be combined at some firms. There should be regard to business models and an avoidance of granular interpretation.

Q2: Can the above criteria be easily applied and are the levels of staff identified and the provided threshold appropriate?

The criteria use banking terms, which are not appropriate for limited licence investment firms.

Q3: Can the above criteria be easily applied and are the levels of staff identified and the provided thresholds appropriate?

There are references to the use of internal models and trading book, neither of which apply to our members.

Q4 a) Is this criterion appropriate to identify risk takers?

We are concerned by the increasing scope of the rules, particularly J. The focus should be on genuine risk takers and measures that cater for the variety of firms in scope.

Q4 b) Are the thresholds set in the criteria appropriate?

No comment.

Q4 c) What would be the number of staff members identified in addition to all other criteria within the RTS?

Q4 d) What would be the additional costs of implementation for the above criterion if an institution applies Article 4 in order to exclude staff from the group of identified staff?

No comment.

Q5 a) Can the above criterion be easily applied?

We are concerned by the increasing scope of the rules. The focus should be on genuine risk takers.

Q5 b) Would it be more appropriate to use remuneration which potentially could be awarded as a basis for this criterion?

The phrase "which potentially could be awarded" is vague. A formulaic approach should be avoided as firms vary in nature, scale and complexity.

Q5 c) What would be the difference in implementation costs if the potentially awarded remuneration would be used as a basis?

No comment.

Q6: Can the above criterion be easily applied and are the threshold and the levels of staff identified appropriate?

Guidance from the EBA, especially for staff that are not senior management, would be helpful.

Q7: Can the above criteria be easily applied and are the levels of staff identified appropriate?

No comment.

Q8: Are there additional criteria which should be used to identify staff having a material impact on the institutions risk profile?

No comment.