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Directeur Général Délégué

Paris, July 22, 2013

Dear Madam,
Dear Sir,

The French Banking Federation (FBF) welcomes the opportunity to respond to the consultation on EBA's draft Regulatory Technical Standard (RTS) setting criteria (qualitative and quantitative) to identify categories of staff whose professional activities have a material impact on the institution's risk profile (hereafter 'material risk takers') within the framework of CRD IV.

You find attached the FBF's contributions on the EBA Consultation on draft Regulatory Technical Standards for the definition of material risk takers for remuneration purposes.

We thank you in advance for your consideration.

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July 11, 2013

CONSULTATION PAPER ON RTS ON CRITERIA TO IDENTIFY MATERIAL RISK TAKERS

We welcome the opportunity to respond to the consultation on draft Regulatory Technical Standard (RTS) setting criteria (qualitative and quantitative) to identify categories of staff whose professional activities have a material impact on the institution's risk profile (hereafter "material risk takers" or "MRT") in the framework of CRD IV.

In order to improve the process of MRT identification and to reach a higher level of harmonization across the banking industry, we agree with the proposed approach based on a combination of internal criteria developed by institutions and other regulatory qualitative and quantitative criteria to ensure consistency across institutions.

However, we would like to take the opportunity of this consultation to draw your attention to level playing field concerns and to the operational difficulties of applying the numerous proposed criteria. The quantitative remuneration related criteria, as proposed, will weigh very heavily in the balance and in practice will prevail over the internal criteria and the qualitative and quantitative risk related criteria. The underlying concern is that key principles set out in the level 1 text such as proportionality (i.e. consideration of size, internal organization, business model and the risk profile of institution) and the notion of effective material impact of the staff member will be lost under the proposed drafting.

In an international context, differences in absolute remuneration levels are in general more influenced by the local economic context in each jurisdiction (i.e. the cost of living, market practices, prevalence/scarcity of specific profiles), rather than a direct link to the risk impact of the staff member. Therefore, the fixing of "all inclusive" remuneration criteria does not take into consideration the significant international diversity in remuneration practices and as such, within large international banking groups, the remuneration criteria will capture very different staff profiles, with a disproportionate number of staff being identified in key financial centers outside of the EU, thus exacerbating level playing field concerns relating to CRDIV remuneration provisions applying outside of the EEA.

As developed below, we would prefer an approach whereby absolute or relative remuneration criteria were used as test criteria to verify that all Material Risk Takers have indeed been identified via the internal and other qualitative and quantitative criteria related to role, function and ability to commit to material levels of credit risk or market risk exposure.

Finally, taking into account the proportionality principle, in the context of a complex international banking group, it is absolutely necessary that these criteria be assessed at Group level and not on a subsidiary by subsidiary basis within the EEA, in order to take into account group level supervision on key issues such as risk policy and business strategy and the internal organization within groups, including hierarchical reporting lines between staff members in subsidiaries and in the parent institution.

We summarize hereafter our key requests for alternative regulatory choices, followed by detailed comments on each Article and responses to the specific questions.

Key requests for alternative regulatory choices regarding the proposed MRT identification criteria:

The two major concerns raised above and developed hereafter could be addressed by alternative regulatory approaches:

- **Request that the provisions of Article 4, which provide the possibility to make an assessment/demonstration of the effective material risk influence of the staff member and taking into account the levels of remuneration which are market practice in different jurisdictions, can be applied to all staff members identified solely as a result of any one of the remuneration related criteria under Article 3 (2) (i.e. without limiting this possibility to only points (a) and (b) of such Article).**
- **In a consolidated Group context, to take into the account the influence of parent level supervision and hierarchical reporting lines between staff members of the subsidiaries and of the parent institution, request that all the criteria in the RTS be assessed at the consolidated Group level and not on a subsidiary by subsidiary basis within the EEA, with the possible exception of subsidiaries that are significant in relation to their local market, as suggested below under Article 1.**

Article 1 – Subject matter and scope

The scope of application covers all institutions covered by CRD IV. Article 1 (2) and Recital (2) specify that the criteria should be applied at group, parent and subsidiary levels. Those firms who are not covered institutions themselves, but who are within the consolidated or sub-consolidated scope of a covered parent institution do not have to apply the criteria themselves, but should be included in the assessment done at group level. Therefore, it appears that CRDIV covered institutions would have a similar "core" population of Material Risk Takers (management body, senior management, heads of business units, staff responsible for internal risk control/compliance/internal audit, head of legal, tax, HR, IT, budgeting, economic analysis, business continuity planning, 0.3% of highest paid staff...) irrespective of their size, internal organization and the nature and scope and the complexity of their activities. This seems in contradiction with the proportionality principle specified in the Level 1 text[1]. For example, in a Group context, each separate legal entity within the Group will have the above mentioned functions in scope, but this does not take into account the fact that many of such staff are only responsible for implementing the Group policies and strategy (including, in particular, risk policies and procedures) rather than defining them, will often report to a superior in the parent company and therefore cannot take material decisions at their own level.

It is unclear to us how a sufficient level of harmonization is to be obtained across the EEA if the criteria are identical, irrespective of the size and activity of the institution. If, subsequently, application of proportionality and the ability to neutralize the most stringent remuneration rules (deferral, retention, variable remuneration in instruments and ex post risk adjustment) is left to national supervisory authorities, who today apply proportionality rules very differently, it will lead to uneven application of the rules between EEA institutions and also between institutions within the same Group.

[1] Art. 88 of CRDIV: "......institutions comply with the following principles in a way and to the extent that is appropriate to their size, internal organization and the nature, the scope and the complexity of their activities:"

Recommendation: The RTS should provide that in a consolidated Group context, the criteria should be assessed at Group level and not at the level of each EEA subsidiary subject to CRDIV. Exceptions could be made to this rule for institutions that are significant subsidiaries of an EU parent institution and those subsidiaries which are of material significance for their local market, who would apply the criteria on an individual or sub-consolidated basis. This would align the perimeter of identification of Material Risk Takers with the scope of disclosure requirements for remuneration under the CRR.
The notions of significant subsidiary / material significance in the local market should be clearly defined and aligned with other regulatory texts (i.e. the proposed European Parliament definition in Article 7. 1a of the draft Recovery and Resolution Directive).
In addition, the RTS should clarify that identification under such criteria as a Material Risk Taker, does not preclude a subsequent neutralization of the requirements on the pay-out-process for all or some categories of such staff, under the application of proportionality as provided under CEBS guidance of December 2010.

Article 2 – Internal identification process

We have no comments concerning this Article.

Article 3 – Qualitative and quantitative criteria

(1) Staff shall be identified as having a material impact on an institution's risk profile if they meet one or more of the following criteria:

a. the staff member is a member of the management body;

b. the staff member is a member of the senior management;

c. the staff member is responsible and accountable to the management body for the activities of the internal risk control function, the compliance function or the internal audit function;

d. the staff member heads a business unit (within the meaning of Article 137(1)(3) of Regulation (EU) No xxxx/2013 [CRR]);

Article 137 (1) (3) reads: 'business unit' means any separate organizational or legal entities, business lines, geographical locations;

e. the staff member heads a function responsible for legal affairs, taxation, human resources, information technology, budgeting, economic analysis, or business continuity planning;

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

The proposed specific functions are appropriate, subject to the ability to make the assessment in a group context of which functions have a material risk impact taking into account internal organization within the Group (see recommendation under Article 1 above).

If the analysis had to be performed at a more granular level, it is essential that the materiality of the function be assessed in light of the actual role and internal organization with the group. Indeed, in Group structures, key roles and responsibilities are essentially at Group level, these roles at a lower level of the organization (in some business units or geographical locations) are limited to the implementation and the management of decisions taken at Group level by heads of functions/businesses. Consequently, the identification of staff members heading a function such as those defined in the point e. above should be limited to significant business units, legal entities or major geographical locations assessed both in relation to the Group and taking into account relevance to the local market.

Recommendation:

- **Point d. should read "staff member heads a significant business unit"**
- **Add the specification, "In a consolidated group context, the above functions are identified at consolidated group level. At the level of each subsidiary within the group, the material impact of such function should be assessed in the light of inter-group reporting lines and the effective material risk impact of such functions assessed in the group context and taking into account the material significance of the subsidiary in the local market".**

f. the staff member has, individually or collectively with other staff members, authority to commit to credit risk exposures of a nominal amount per transaction which represents 0,25% of the institution's Common Equity Tier 1 capital;

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

The proposed approach of a threshold expressed as a % of CET1 is relevant as CET1 is indeed the most appropriate indicator to ensure a consistent approach between institutions and taking into account size and risk profile. However, 0, 25% appears to be very low compared to the objective of the text ("significant impact on the risk profile"): we do not believe such low threshold reflects faithfully the CRDV goal. In this respect, a 1%level would be more appropriate.

Recommendation:

- **Add the specification, "In a consolidated group context, the assessment is made in relation to consolidated group CET1.**
- **Use 1% as threshold and not 0, 25%.**

g. in relation to an institution to which the derogation for small trading book business under Article 89(1) of Regulation (EU) No xxxx/2013 [CRR] does not apply, the staff member has, individually or collectively with other staff members, authority to commit to transactions on the trading book which in aggregate represent one of the following:

i. where the standardized approach is used, an own funds requirement for market risks of 0.25% or more of the institution's Common Equity Tier 1 capital;

ii. where an internal model based approach is used, 5% or more of the institution's internal value-at-risk limit for trading book exposures at a 95th percentile, one-tailed confidence interval level;

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

The assessment with respect to value-at-risk (VAR) limits for market risks is appropriate, notwithstanding the need for certain specifications:

- **Criterion g. ii. permits the institution to use an internal model based approach, however, the reference exposure at the 95th percentile is not in line with some institutions' internal model approaches (I.e. some banks internal models are based on VaR at the 99th percentile). The RTS should give the flexibility for institutions to base the market risk exposure assessment based on their existing internal models.**
- **The text refers to "collectively" and "authority to commit to transactions on the trading book which in the aggregate represent..." as well as the text in Recital (9) which specifies "Limits of**

authority in the trading area should therefore be based on the aggregated exposures taken by a trading desk, encompassing all staff who have the authority to enter into such positions". While the assertion that market risk exposure is generally managed at the desk level is correct, the definition of Material Risk Taker should target the individual staff member who is directly accountable for the limit of authority (i.e. generally the desk head) and not all traders on the desk, to the extent that this would encompass many junior traders who are simply executing instructions from their line management and are only authorized to take positions/commit to transactions subject to a significant level of internal supervision.

- **As for previous question, we strongly believe that 5% of VAR limit is definitively too low to capture "significant impact on the risk profile" for VAR at 99th percentile. A 10%level would appear more relevant there.**

Recommendation:

- **Article 3 (1) g. ii should read "……10% or more of the institution's internal value-at-risk limit for trading book exposure at a 95th percentile or such higher percentile used in the internal model as approved by the relevant supervisory body (i.e. 99th percentile), …"**
- **Article 3 (1) g. and Recital (9) should specify "Where trading limits of authority are based on aggregate exposures at the trading desk level, this encompasses the staff member who is directly accountable for the limit/threshold and who supervises the group of staff who can enter into positions within such limit".**

h. the staff member has managerial responsibility for a group of staff members who have individual authorities to commit the institution to transactions, and the sum of those authorities equals or exceeds a threshold set out in point (f) or in point (g);

To the extent that it is not possible to "sum" risk exposures due to netting effects, this criterion is difficult to apply in practice. Such a "sum" would rapidly exceed 5% of VAR limit, but does not take into account the effective overall risk exposure due to risk diversification across traders/desks and netting effects. Moreover, as an illustration, a manager of 100 employees with each of them entitle to a credit delegation of 0.0025% of CET1 (a significantly low level of delegation) would be identified as MRT, even if he/she as an individual would not have necessarily a material impact on the risk profile of the institution. Authority of managers to commit to credit risk exposures or to commit to transactions on trading books can only be appreciated according to their own delegation level, to their own VAR limit or to their responsibility within validation committees for fixing limits or authorizing transactions of staff members under their supervision, but not as the sum of individual delegations of employees under their responsibility. Consequently this criterion, as proposed, does not seem appropriate.

A more appropriate criterion would be that any staff member who has managerial responsibility for Material Risk Taker identified under Article 2 or under criteria (1) a. through g. of Article 3 would be more feasible to implement.

Recommendation:

- **Merge Articles 3 (1) h and i to read "the staff member has managerial responsibility for another staff member whose professional activities have or may have a material impact on the institution's risk profile according to the internal risk identification process in Article 2 and the criteria (1) a. through g. in this Article 3.**

i. the staff member has managerial responsibility for a staff member whose professional activities have or may have a material impact on the institution's risk profile according to the internal risk identification process in Article 2;

See comments under point h.

j. the staff member has, individually or collectively with other staff members, the authority to take, approve or veto decisions on the introduction of new products, material processes, or material systems.

We agree with a criterion based on the authority to take, approve or veto material decisions. However an extensive application of "collectively" could potentially capture not only employees who will take final decisions but also all employees who take part of the decisional processes (such as credit analysts, advisors, research worker...) and whose impact on the risk profile is often not material at all and who do not have the capacity to take or materially influence the final decision. The scope should be limited to staff members who have a significant impact on the risk profile due to their effective final decisional powers (see recommendation under Article 3 (3)).

Article 3 (2) (i.e. Criteria relating to remuneration level)

(2) Staff shall be identified as having a material impact on an institution's risk profile if they meet one or more of the following criteria, subject to Article (4):

As a general comment, the remuneration criteria are too numerous and would therefore create a significant administrative burden for institutions. The remuneration related criteria should represent backstop criterion in order to verify whether all Material Risk Takers have indeed been identified through the other criteria, but should not represent the principle criteria. The number of individuals identified "ex ante" (i.e. due to function/role, ability to commit to market/credit risk exposure, etc.) should constitute the vast majority of material risk takers and the number identified "ex post" (i.e. due to their remuneration level) should be minimal. This is both in the interest of institutions, for whom it is difficult to manage remuneration regulations over time from a HR standpoint for a very volatile perimeter of staff, but also for supervisors and stakeholders (i.e. shareholders, etc.) who use publicly disclosed data to make year-on-year comparisons of the remuneration pool allotted to such staff.

In our opinion, the quantitative criterion on remuneration should only aim at ensuring that the best-rewarded employees of the institution have been exhaustively tested with regards to their material impact on the risk profile and that they would not be encouraged to take more risk in their activity to maximize their variable remuneration: it must so be a "test"criteria only, and not a capture-all principle.

a. the staff member could, in accordance with the institution's remuneration policy, be awarded variable remuneration that exceeds both of the following amounts

i. 75% of the fixed component of remuneration;

ii. EUR 75 000;

Q4 a) Is this criterion appropriate to identify risk takers? Q4 b) Are the thresholds set in the criterion appropriate? 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?

This criterion is particularly difficult to implement since the criteria is conditional, "could be awarded under the remuneration policy". If the institution's remuneration policy does not fix formal caps for variable remuneration awards, it would be particularly difficult to identify the population concerned as it could potentially mean all staff in the institution, even if in reality such variable levels are not awarded. With regards to remuneration market practices in some countries (i.e. in particular, the US, the UK, certain Asian markets) the caps proposed are too low and would capture a significant number of staff ex post: the process of demonstrating to supervisors that each staff member concerned does not in fact have the capacity to take material risk would be lengthy, costly and burdensome. Finally, this criteria does not appear to be in line with the remuneration criterion included in the level one text which is "...any employee receiving total remuneration that takes them into the same remuneration bracket...", not "...any employee who could receive total remuneration...".

In conclusion, we consider that including this criterion will have no impact on the number of MRT finally identified and presents no benefit considering the wide scope already identified under all the other criteria.

b. the staff member has been awarded total gross remuneration in one of the two preceding financial years which is equal to or greater than the lowest total remuneration that was awarded in that year to a member of staff who performs professional activities for the same entity and who either is a member of senior management or meets one of the criteria in paragraph (1) or one of the internal criteria referred to in Article 2;

Q5 a) Can the above criterion be easily applied? Q5 b) Would it be more appropriate to use remuneration which potentially could be awarded as a basis for this criterion? Q5 c) What would be the difference in implementation costs if the potentially awarded remuneration would be used as a basis?

This criterion is the most closely aligned with the level 1 text ("...any employee receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers"). However, if in practice the remuneration bracket is very wide, this could lead to a significant administrative burden and costs of identifying a large circle of staff and reviewing their risk profile. If "entity" encompasses all branches, in different geographical locations, forming part of an institution, the remuneration bracket will be very wide.

Moreover, in the case of an individual or collective low performance, most otherwise identified MRTs would not receive any variable remuneration (in accordance with the Directive); this test would result in screening a large number of employees without any material risk impact. This could also lead to the unintended incentive not to award zero bonus to MRT already identified according to the other criteria, in order to avoid including many additional people in the scope.

It would be helpful to have a relatively stable reference remuneration bracket in order to reduce the administrative burden of reviewing the risk profile of all staff receiving remuneration in this bracket. This could be achieved by:

- **Making the analysis at the level of each entity (i.e. subsidiary or branch) in a given location;**
- **Excluding control function and infrastructure staff from the reference remuneration bracket. This seems to be the spirit of the Level 1 text;**
- **Making reference to the lowest gross remuneration that could potentially be awarded to senior management and risk takers (i.e. taking into account the institutions maximum variable/fixed remuneration ratio) OR the average annual total compensation awarded to such staff. This would reduce the volatility of the lower bracket which would occur when even just one member of the**

senior management/risk taker categories received no variable remuneration due to poor performance.

c. the staff member has been awarded total gross remuneration of EUR 500 000 or more in one of the two preceding financial years.

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

The problem of having an all inclusive total remuneration criteria is the issue already raised above of having too many staff identified ex post and therefore a very variable year-on-year population of Material Risk Takers. In addition, individuals could fall in or out of this category simply due to a small fluctuation in exchange rates.

Finally, due to very different cost-of-living levels across different countries, this level would capture a disproportionate level of staff in some locations (i.e. New York, London, Hong Kong), some of whom have no material impact on the risk profile of the institution or group and on the contrary would be irrelevant in many EEA countries. The concern that EEA-headquartered institutions are subject to competitive distortion when having to apply CRDIV remuneration provisions outside of the EEA will be even more acute if such institutions have to encompass all staff remunerated above a fixed threshold, irrespective of their material risk impact. We should bear in mind one of the major objectives of the Directive which is to establish a link between compensation and risk-taking. Some employees can have a high level of compensation without having any impact on the risk profile of the bank (for example, commissions, advisory fees, asset management for third party, scarce control function resources ...).

To the extent that remuneration levels vary significantly across jurisdictions, the review of risk profile and "levels of remuneration which can be awarded in different jurisdictions" provided under Article 4 should apply to those staff members identified under Article 3 (2) c. If it is deemed absolutely necessary to have an "all inclusive" remuneration criteria in order to capture in all cases the highest earning staff in the major financial centers, at the very least the threshold should be higher in line with remuneration practices and taking into account the cost of living in such locations.

d. the staff member is within the 0.3% of staff who received the highest total gross remuneration in either the most recent financial year or in the preceding financial year.

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

The proposed 0.3% of highest paid staff is a useful reference for large institutions, but does not take into account proportionality and therefore could create unnecessary rules for small non complex institutions. As mentioned above, in line with CEBS guidance of December 2010, proportionality should allow neutralization of the pay-out-process rules for small, non-complex institutions (see recommendations under Article 1).

Proportionality should apply both with respect to the size of the institution, but also the nature of the activities performed within the institution. While the 0.3% is a relatively low threshold, it may still lead to a disproportionate number of risk takers being identified within a large retail bank taking into account the risk profile of the institution.

As such, the possibility to apply Article 4 to those staff members identified under Article 3 (2) d. should be given in order to take into account the different risk profiles between institutions.

Recommendation:

- **Article 4 should apply to those staff identified under Article 3 (2) c and Article 3 (2) d. At the very least proportionality rules should apply and if deemed absolutely necessary to have an "all inclusive" remuneration threshold under 3 (2) c to capture high earners, this threshold should be increased to take into account market remuneration practices in the major financial centers.**
- **Delete Article 3 (2) a. which is inoperable in many institutions due to its conditional nature and which is disconnected from the remuneration levels of senior management and risk taker functions in an international context.**
- **Article 3 (2) b. should read "the staff member has been awarded gross remuneration in one of the two preceding financial years which is equal to or greater than the lowest total remuneration that could, in accordance with the institution's remuneration policy, have been awarded in that year (OR the average total remuneration awarded in that year) to a member of staff who performs professional activities for the same entity and who either is a member of senior management or a risk taker. For purposes of this assessment the senior management and risk taker categories include those staff identified in paragraph (1) or under Article 2, with the exception of control function and infrastructure staff. "Entity" is understood to be a parent, subsidiary or branch in a given location.**

Article 3 (3)

In paragraph (1), a reference to staff members having, individually or collectively with other staff members, authority to commit to transactions or exposures or to take, approve or veto a decision includes both of the following categories of staff:

a. staff who are responsible for advising on or initiating such commitments or decisions;
b. staff who are members of a committee which has authority to make such commitments or to take such decisions.

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

This criterion is potentially very extensive since it considers all staff who participate in committees and who advise on or initiate material commitments or decisions. In order to avoid capturing larger numbers of more junior staff such as credit analysts and other control or operational risk functions who may involved in advising on a specific transaction or decision (refer to j.), the wording should be more specific in order to capture only significant influence functions whose position could considerably weigh on the ultimate decision. Without such specification, this criterion could have the unintended consequence of undermining the governance that has been strengthened since the crisis by creating the incentive for staff to no longer give their opinion and to participate in the committees in which material commitments are made or decisions taken.

Recommendation:

- **Either delete sub-paragraph (3) a. of Article 3 or clarify through re-wording "....staff in a significant influence function who are responsible for advising on or initiating such material commitments or decisions".**

Article 4 - Staff with no material impact on the risk profile

Given the very large number of staff who could be subject to review after having been identified under the remuneration based criteria, it should be possible to exempt categories of staff (i.e. by activity and/or function) rather than on a individual case by case basis which would be very time consuming and burdensome.

Recommendation:

- **Add to the end of Article 4 "In the situation where a significant number of staff are subject to review under this Article, the assessment can be made for each category of staff (i.e. with the same activity and/or function) rather than on an individual basis.**

Article 5 - Entry into force

According to the calendar set by the CRDIV, the publication of the RTS could take place as late as mid-2014 (i.e. submission to the Commission by end March 2014 and subsequent validation by the Commission prior to publication). However, since the remuneration provisions (i.e. in particular the variable/fixed maximum ratio) apply to remuneration awarded for the 2014 performance year, Institutions really need to have a clear picture of the final criteria by end 2013 for operational implementation of the new rules (i.e. adjustment of processes and information systems to take into account the identification criteria, communication to employees, modification of any contractual arrangements, immediate implementation of the maximum ratio in January 2014 for any staff whose variable remuneration is paid on a monthly basis, preparation of the Annual General Shareholders Meeting, etc.) .

Recommendation:

- **Request for the publication of the final RTS on identification criteria for Material Risk Takers by end 2013.**