

European Banking Authority
By email: EBA-CP-2013-11@eba.europa.eu

20 August 2013

Dear Sir/Madam

We welcome the opportunity to comment on the European Banking Authority's consultation on its Draft Regulatory Technical Standards on criteria to identify material risk takers. We firmly acknowledge the importance of such standards given the lack of consistency between different Member States and different banks' approaches to the issue of who falls into this key category, as revealed by the EBA Survey.

By way of background, Hermes is a leading fund manager in the City of London. As part of our Equity Ownership Service (EOS), we also respond to consultations on behalf of many clients from across Europe and around the world. In all, EOS advises clients with regard to assets worth a total of €149 billion (as at March 31 2013).

We share the EBA's concern about the banking sector and the need to ensure that risks are appropriately managed and mitigated, and welcome the overall approach to having tighter controls on remuneration, not least given that the experience of the past indicates that inappropriate remuneration can incentivise reckless behaviour. We have been active in the debate about finding better pay structures within the banking sector. We are generally supportive of the EBA's approach but we have some doubts about whether some of the proposed criteria are practically deliverable or are set at the appropriate level, as there is a risk that some of the proposals may increase the cost burden without having any positive effect on risk management.

We respond to relevant questions below and also make some general comments on the broader text within the draft, in order as they appear in the document, below.

Yours sincerely



Paul Lee
Director



Questions and other comments

Article 2 (4)

We would suggest adding a further subparagraph, which we believe would be valuable in encouraging the review processes to be as substantive and considered as they should be:

- (d) a description of the outcome of the review process

Article 3 (1) d

We note the inclusion of leadership of any geographical location. On the face of it, this criterion could potentially encompass individuals heading units generating no significant risk factors of the nature sought to be addressed by the code – such as the manager of a call centre, which might be the sole operation in a geography or even country. We would suggest that this criterion of leadership of a geographical location be included in the scope of Article 4 such that there is an opportunity, in limited circumstances, for a bank to exclude those staff who have no material impact on the risk profile.

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

We are not convinced that it is appropriate or necessary to include the head of budgeting in the list. Further, we would recommend the inclusion of the head of treasury, a crucial role that sometimes bears significant risk.

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

While not having direct knowledge, we believe that the application of this rule should be straightforward. We also believe that the level of the threshold is appropriate.

We comment below on the issue of the term “collectively”.

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

While not having direct knowledge, we believe that the application of this rule should be straightforward. We also believe that the level of the threshold is appropriate.

We comment below on the issue of the term “collectively”.

Q4:

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

(b) Are the thresholds set in the criterion appropriate?

We acknowledge that a significant variable portion of pay is an indicator that an individual is a risk taker. However, we believe that the thresholds are set too low to include only material risk takers. Instead, we would recommend that

individuals should be included whose bonuses both exceed 100% of fixed pay, and €100,000.

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

We have no information in response to this question.

(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?

We welcome the scope for exclusions to be applied in circumstances where this criterion captures staff who are not material risk takers, and do not believe that the costs should be too substantial - provided that our proposed increases in the thresholds are made, as this would significantly reduce the need for any such exclusions.

Q5:

(a) Can the above criterion be easily applied?

We do not regard this requirement as workable. It is too complex as it currently stands. Our favoured simplification would be simply to compare the gross remuneration (as currently, the higher of the last two years) to that of senior management. This would leave the end of the criterion reading simply: "...awarded in that year to a member of senior management."

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

We believe that using potential remuneration would add a further unhelpful complication, and might encourage some gaming of the standard - through the manipulation of potential rewards for management and others.

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

We do not support this possible alternative.

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

Yes this can be simply applied and would capture an appropriate level of staff.

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

Yes this can be simply applied. However, we would commend a shift in the threshold to 0.2% as this would reduce the overall impact of this criterion; as it currently stands, this is very significant. One in 500 staff seems a more appropriate mopping up criterion than one capturing one in 300.

Article 3 (3)

We are significantly concerned by the term 'collectively' as potentially this could require the aggregation of significant numbers of individuals whose impact individually is minimal and yet as a collectivised force all could be deemed to be material risk takers. We believe that the EBA's intention is that individuals are only to be deemed to be acting collectively where they fall either into category (a) or (b), and our firm view is that this should be the intention, so that the umbrella of the concept of "collectively" does not extend inappropriately far. This means that the current language "includes both the following categories" is misleading by implying that collective status can be delivered in additional, alternative ways. We believe that this paragraph needs substantial redrafting to ensure that it captures only the collective situations that are intended.

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

We believe that the combination of these criteria will successfully identify all material risk takers, and so we do not believe there is a need for any further criteria. Indeed, it will be clear from our above comments that we believe the likelihood is too often in the opposite direction: that non-material risk takers may be captured by the regime, adding to cost burdens without affecting the overall risk profile of any bank. We have proposed a number of simple ways in which to reduce any such likelihood, and believe that these must be adopted. There may be a need to consider further steps to address this.

Q9: Could you indicate whether all the main drivers of direct costs from the RTS have been identified in the table above? Are there any other costs or benefits missing? If yes, could you specify which ones?

Q10: For institutions, could you indicate which type of costs (a, b, c, d) are you more likely to incur? Could you explain what exactly drives these costs and give us an indication of their expected scale?

Q11: Do you agree with our analysis of the impact of the proposals in this CP? If not, can you provide any evidence or data that would explain why you disagree or might further inform our analysis of the likely impacts of these proposals?

We have no basis to provide input on the questions on the cost impacts of these proposals.