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EBA – Consultation on Draft RTS for the definition of material risk takers for remuneration purposes (EBA/CP/2013/11)

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on the EBA Consultation on Draft RTS for the definition of material risk takers for remuneration purposes (EBA/CP/2013/11)and would like to submit the following position:

General remarks:

It has to be stressed that all regulations should have the focus on what criteria are relevant to identify material risk takers. However the draft regulations seem obviously not beeing in line with their legal basis (Art 92 (2) and Art 94 (2) CRD IV), which refer to “staff, whose activities have a material impact on the institution’s risk profile”. On the contrary the draft technical standards refer to “persons, (…) whose activities could have a material impact on the institution’s risk profile”. This would mean that institutions would have to identify also persons who could only potentially have an influence on certain decisions. This doenst seem to be in line with the legal basis.

Regarding small banks the principle of proportionality is not regarded in the proposed text, as the qualitative and quantitative criteria suggested by EBA are detailed and extensive with almost no room for consideration of the institutions individual situation and risk profile. Therefore a differentiation between the different types of banks would have to be implemented.

We believe that the regulations would lead to the identification of a significant number of staff members who have in fact no material risk impact, like legal, HR, IT, budgeting, economic analysis.

Furthermore we ask for a clear statement that the technical standards should be applied to the remunerations of performances after 31.12.2013.

Q 1: Is the list of specific functions listed appropriate or should additional functions be added?

The list of specific functions is too extensive and is based on a generalization which does not sufficiently reflect business reality and day-to-day management of the business or the control
functions.

The list of functions should be limited to members of senior management. A staff member heading a function as described (for example budgeting, IT, etc) could be located in a unit which is not deemed to have a material impact on the entity's risk profile.

Moreover there should not be a taxative list of responsibility areas, as it should be evaluated during the assessment process if a specific function has a material impact on the risk profile. For example, the head of IT or the head of Economic Analysis might be assessed as not having a significant impact on the risk profile, but are merely responsible for providing relevant information or the necessary infrastructure for the decision making bodies.

The general inclusion of staff members heading service functions like e.g. legal and tax is inappropriate, as tasks and activities of these persons may in fact not have a material risk impact (and this rule may consequently lead to identification of a significant number of employees who have no actual material risk impact) and furthermore the Directive itself does not at all refer to these service functions.

Furthermore the list should be subject to a principle of proportionality. Especially in small entities, some of the listed functions may not have a material impact on their entity's risk profile due to a holding control framework they are integrated in. A taxative list of functions to be included is therefore inconsistent with the "Proportionality Principle" as these criteria would be applied to small credit institutions and big investment banks in the same way without any differentiation.

The function descriptions of the list may not be appropriate for non-credit-institutions.
As regards groups, it should be clarified that only staff employed by credit institutions is concerned.

Anyhow if the list would be upheld it should not be further extended, however, certain precisions are in our view necessary.

Point (a) includes all members of the management body, and by consequence also the members of supervisory boards in a two tier board system. Treating these people as "staff" is not appropriate, as supervisory board members are not employees. Moreover, they may not receive remuneration at all. If they do, they either do not receive variable remuneration, or they are paid in attendance fees of symbolic value, or their salary is indexed. Even when remunerated, they often earn significantly less than employees at the lower salary range.

Thus, being a member of the supervisory board should not per se lead to being classified as a material risk taker.

Finally, it would be necessary to provide for a minimum level (based on the size of the organization) or proportionality with reference to a group exposure.

Q 2: Can the above criteria be easily applied and are the levels of staff identified and the provided threshold appropriate?

We consider a threshold of Common Equity Tier 1 capital as an inappropriate figure with regards to credit risk exposures. We rather feel that a risk-based approach should be considered, where the limits of commitment to credit risk exposure is linked to the risk rating of the client.

Moreover we deem as necessary to further clarify the definition of “authority to commit to credit risk exposure". It may be questionable whether this applies to the customer manager who wants to grant the loan or to the risk function, whose competence it is to evaluate the risk and approve the transaction.

Sufficiently, in our view, a threshold of 0.25% is inappropriate as it is much too low. It does not reflect business reality, especially in cases of collective authority.
Provided that a risk-based approach as the most suitable approach should not be considered, we propose to use a credit risk exposure of 1.5% Common Equity Tier 1 ratio over two consecutive years. As a minimum, the threshold of 0.25% ECT1 should be calibrated depending on the size and the risk profile of the credit institution. This criterion is particularly relevant when very small banks are concerned. By consequence, the rule would lead to the identification of staff members with rather limited income, which neither seems justified.
Finally, the scope seems to be extended by virtue of Art 3.3, to include supporting and advisory functions as well. It is questionable whether these functions are material risk takers given their limited direct responsibility (see also question 8).

Moreover, fixed quantitative criteria are inconsistent with the principle of proportionality, as these criteria would be applied to small credit institutions and big investment banks in the same way without any differentiation.

The proposed criteria would lead to identification of a high number of roles which actually have no material impact on the risk. The proposal, as it stands, would generate additional administration and cost.

Q 3: Can the above criteria be easily applied and are the levels of staff identified and the provided thresholds appropriate?

The criteria can be applied. However, the proposed credit risk exposure of 0.25% would lead to inclusion of employees who do not have a significant material impact on the risk profile of the company. Please refer to our answer regarding thresholds to Q2.

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

We think that these criteria are not appropriate for determining material risk takers. The criteria neglect local market pay practices and existing pay gaps within Europe. An institution operating in various European – and especially in Eastern European - countries will have difficulties to impose equal pay levels in all countries. As long as there do not exist equal salary levels and payment practices in Europe it is inappropriate to impose equal regulatory standards.

In light of the current regulatory treatment of deferral the criteria must be questioned. Initial bonus is based on company and individual performance whereas deferrals are based primarily on company performance. Hence, the length of deferrals disregards the emotional appeal between future (small sized) deferral pay-outs and past decisions. For example, in Austria for material risk takers the threshold level for bonus deferral is at 30.000 EUR (over 5 years), which means a pay-out of about 2.400 EUR in consecutive years. This amount is less than a monthly salary.
The criterion is also inappropriate because staff members being granted a bonus slightly below the limit find themselves in a better position than persons with a bonus slightly above the limit. This way, top performers will be disadvantaged by the deferral regulation. Furthermore, in the light of the unequal pay levels within Europe as described above, the disparity between comparable performers gets even worse.

When it comes to actual applicability of remuneration principles only paid amounts should be taken into account. Otherwise employees would suffer through e.g. deferrals for compensation when the actual payments (e.g. based on company performance) are below the "award amounts", which might define thresholds.
In this regard it remains unclear whether this article should be interpreted as referring to employees who could possibly receive variable income exceeding 75% of the fixed component of their remuneration, or employees for whom the variable income has a target level of 75%.

Furthermore when a bonus pool is used, it is not possible to define ex ante how high the variable income can possibly become. Thus in 3 (2) (a) of the proposal should be clarified, that only paid amounts should be taken into account.

It is challenging to provide an appropriate justification for each staff member. Insofar Article 4 would be impractical.

Q4 b: Are the thresholds set in the criterion appropriate?

As described above under Q4 a, the absolute amount neglects local market pay practices in the EU countries as well as countries outside the EU where typically the regulators expect EU regulations to be applied. We therefore plead for a relative limit only and for withdrawing the fixed amount of 75 000 EUR. A relative threshold (percentage) of the fixed component of remuneration would enable the institutions to adapt group-wide payment standards in a fair manner to all countries in which it undertakes business and allows the institution to react adequately to different pay structures.

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

One bigger Austrian banking group provided the following data:

These criteria would lead to an increase of identified staff members with about 480 employees.

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?

The same banking group provided the following data:
It would lead to an average salary increase of 15-35% to the population that could reach bonus amounts over 75 000 EUR. This would be about 1 000 employees. The increase in base salary would dis-balance the internal equity pay structure; thus indirectly posing strains on other staff as well (especially in risk management, compliance, audit, and middle management positions).

Q5 a: Can the above criterion be easily applied?

We see some difficulties in the application of this criterion with regard to the bonus budget available for a certain year.It is not in line with the CRD IV objectives to target the incentives created by variable remuneration to get involved in risk taking behaviour.

In any year there might be an identified risk taker with low total gross remuneration for various reasons (joining the institution at a late stage in the year, lacking work experience and thus receiving a "low" income according to the collective agreement, not receiving a bonus payment, etc). If such a lower compensation represents the hurdle rate, many other employees with higher remuneration would be identified although there is no objective reason for it.

The guideline implies that a staff member with limited bonus potential becomes material risk taker because the Board of Directors decides in a certain year not to pay a bonus to those who are material risk taker. In a good year the bonus budget is bigger than in a bad year. Hence in a year where bonus payment is zero in the next first year of bonus all employees with a high base salary but very low bonus potential are material risk takers. Example: a bonus of 5 000 EUR gets deferred over a period of 5 years.

Furthermore it should be clarified if the guideline is considered to be applied entity-wide or if it covers a comparison across the entire institute? In case of the latter, low-income countries such as Bulgaria are likely to dominate the pay practice for material risk-takers in Germany. That is expatriates coming from low-wage countries typically keep a price-level under the host market practices. On the other side, expatriates from high-income countries would influence the amount of Identified Staff in low-wage countries. We doubt that this is the intention of the regulator.

We also see difficulties for the application in cases of internal moves or advancements of staff, either from one function to another or from one country to another with a different level of remuneration. It is unclear how these persons should be considered in the calculation of thresholds – will they be considered just for the year in which the move/advancement took place, or for the preceding year as well? We clearly vote for an exemption in these cases.

Besides, we feel that the persons who are targeted by this criterion will be already identified according to the other criteria anyway.

It should be clarified which “entity” is considered to be the reference: the group (a holding including all subsidiaries), or a group member?

Concerning the credit institution's possibility to declare that those persons do not have material impact on risks, it must be borne in mind that this justification would be difficult to exercise.

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

No.

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

This question cannot be answered as potential cost relate not only to administrative efforts but also to PEREX.

Q 6: Can the above criterion be easily applied and are the threshold and the levels of staff identified appropriate?

In our view this criterion is not appropriate as it refers to the past. Past salary payments are not a suitable indicator for decisions taken now that impact the risk and, consequently, future salary payments.

The criterion uses total income as a definition, while the CRD IV rules are aimed at variable income. The reference to total remuneration could result in the classification of staff members as Identified Staff who do not receive any variable remuneration at all.
See also General Comment above. Therefore, it would make more sense to use a criterion based on the amount of variable, instead of total, remuneration.

Q 7: Can the above criteria be easily applied and are the levels of staff identified appropriate?

This criterion contributes to the administrative complexity, especially in combination with Article 3 (2) b. Especially for entities with a rather equal distribution of remuneration this criterion could lead to an unjustified high number of identified staff.

Again, the article uses a definition based on total income. Based on the explanations in points 26 and 27 of the annexed impact assessment, the only aim of this article seems to be to identify higher paid employees (which is not in line with the objectives of CRD IV). A criterion based on variable income would seem more appropriate.

Again, the figure of 0,3% seems to be chosen at random.

Our estimate is that the population falling within this category would have been identified according to other criteria anyway.

Ad Q 5-7:
We would in general argue that at least two of the outlined criteria have to be fulfilled in order to qualifiy as a material risk taker.

Q 8: Are there additional criteria which should be used to identify staff having a material impact on the institutions risk profile?

We do not agree with the definition in (3) which includes staff advising on or initiating commitments or decisions. Such a definition would automatically include staff who are not deemed to have a material impact on the risk profile, like ordinary compliance or legal staff members without decision authority. We rather feel that the approval of commitments or decisions would be an appropriate criterion to identify risk takers. However, such persons will be identified according to other criteria anyway, thus, this provision does not provide added value to the staff identification process.Moreover this criterion could become problematic for small banks. Even staff with no impact on the risk profile of the institution could be affected. Also the general inclusion of “advising on or initiating committees” in 3 (3) (a) is not suitable, as it is not clear which staff member should fall under this provision and again a significant number of employees who have no impact on the material risk would be encompassed by this provision.

Identified staff selection should provide with the possibility to be applied and implemented by institutions in line with proportionality principle.

We believe that criterion Art 3(1)(f) is not in line with article 92(2) of the CRD, as regarding the proposed text even the possibility of influencing the risk profile of a bank would be sufficient.

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?

The more complex requirements of identifying staff become, the more expertise from business units is required, not only in the implementation phase, but also on an on-going basis. We think that costs relating to legal advice and to internal and external audit are missing.

Kindly give our remarks due consideration.

Yours sincerely,

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