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EBA CONSULTATION
Draft guidelines on sound remuneration policies
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AMAFI's answer

Preamble

As mandated by the CRD4, the EBA has issued draft guidelines on sound remuneration policies, open for consultation from 4 March 2015 up to 4 June 2015.

Hereafter is the answer of AMAFI, who represents financial market participants in France. It acts on behalf of credit institutions, investment firms and trading and post-trade infrastructures, regardless of where they operate or where their clients or counterparties are located. AMAFI's members operate for their own account or for clients in different segments, particularly organised and over-the-counter markets for equities, fixed-income products and derivatives, including commodities. Nearly one-third of its members are subsidiaries or branches of non-French institutions and almost half of them are small sized entities with fewer than 50 employees.

In its answer, AMAFI raises particular concerns as regards the approach taken by the EBA to proportionality. Such approach seems guided by an objective of harmonisation that should ensure a level playing field among EU institutions. However, the proposed guidelines would actually create major competitive distortions, not only between industries but also among CRD4 institutions themselves depending on their legal structure. Without any explanation, these guidelines would also significantly differ from recent interpretations of the same principle of proportionality made by sister European supervisory authorities, creating inconsistent regulation EU-wise, contrary to the objective of the EU rule-book.

Such approach to proportionality, if unchanged, will jeopardise the business model of smaller firms, which currently align remuneration with risk following the principles set by the CRD4 without necessarily applying all the rules or to the full extent. The guidelines have the potential to render these firms non competitive from a remuneration point of view and jeopardise their continuity. Such consequences should be considered in their wider economic context, where the guidelines would actually increase concentration of the industry into a limited number of big players with systemic impact. This would be detrimental risk wise but also from an economic point of view since smaller firms are often developing niche services to domestic companies not covered by larger players. The role played by these firms is endangered by the proposed guidelines, an outcome which contrasts sharply with the Capital Market Union initiative, seeking to foster growth by fostering financing to small and medium companies.

It is essential that domestic regulators maintain the ability to apply the rules in a proportionate way to the smaller institutions they supervise directly. A well-tailored regulation is necessary, which does not stifle national financial ecosystems and does not encourage concentration.

Contact: Stéphanie Hubert, Director of compliance, +331 53 83 00 87 shubert@amafi.fr

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

1. The definition of “staff” in g) includes “*any person acting on behalf of the institution and its subsidiaries*”. This is problematic as a person acting on behalf of the institution includes external contractors and providers, whose staff are legally bound by the remuneration policy of their employer, not the one of the client institution.

As the term remuneration is defined as all forms of fixed and variable remuneration awarded in exchange for professional services rendered by staff, it should be made clear that the fees paid for services rendered by third parties acting on behalf of the institution are not considered as remuneration and that the employees of these third parties are not subject to this regulation.

2. The definition of “*shareholders*” in v. is not clear:

- “*other owners*”: it is not clear what “*other*” refers to as shareholder is not defined elsewhere in the CRD;
- “*members of the institution*”: this reference is wide and imprecise, the intention behind its use should be explained possibly through the use of examples.

3. No additional definition seems needed.

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

4. In paragraph 10, it is stated that “*all institutions should (...) consider which elements of the remuneration policy on the variable remuneration of identified staff (...) should be included in the remuneration policy for all staff*”. Then Annex 1 indicates which requirements of the CRD4 applicable to identified staff should be extended to all staff, either as an obligation stemming for these guidelines or as a voluntarily action from the firm or under a recommendation by the EBA.

Without considering the merits or drawbacks of each proposed extensions, it must be noted that this proposal is not consistent with CRD4. The guidelines are actually overstepping the level 1 text agreed by the Parliament and the Council, which has expressly imposed some obligations on identified staff only. It is outside EBA’s powers to impose requirements on institutions that are not set at level 1, so that although it can make recommendations, it cannot consider that any of the provisions listed in the annex is mandatory institution-wide for all staff by virtue of the guidelines.

5. In terms of syntax, paragraph 15 should be rewritten as the issue is not to create “*conflict of interest regarding the compliance with insider trading rules*” but rather not to create “*conflict with insider trading rules*”.

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

6. It is not clear what the four eyes principle cited at the end of paragraph 20 involves in terms of obligations for an institution, other than the care already required from the management body, the risk function and the risk committee in setting this policy. This should be removed or further explained.

7. In paragraph 23, the purpose of the remuneration policy is not to set the role descriptions as is stated.

8. AMAFI does not agree that compliance, according to paragraph 24, should have significant input into the setting of bonus pools where it has concerns regarding some staff behaviour on the riskiness of a business.

Compliance does have an important role to play in setting the performance criteria and participating in the performance assessment of staff, especially as regards improper staff behaviour, as it also has a role to play in identifying risky areas of the firm and escalating any issues. It is however outside of its mandate to be engaged in setting the amount of the bonuses (the bonus pool). Compliance has a dual role of advising and controlling the business as regards compliance risks. Setting the bonus pools is outside of this remit. For it to be involved in the levels of remuneration of the businesses it controls would be contrary to the necessary independence it needs to have from the business to carry out its role properly.

9. Similarly, the statement in paragraph 29 that the compliance function should analyse the effect of the remuneration policy on the risk culture of the firm is too wide. This would imply that compliance is responsible for the overall risk culture of the firm. However, compliance is dealing with compliance risk only, as other departments, such as risk functions, are dealing with other risks, such as the prudential ones. The reference to "*risk culture*" should therefore be amended to read '*compliance risk culture*".

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

10. The articulation between paragraphs 51 and 52 for institutions that do not belong to a group should be clarified. Surely, the obligation to perform an independent review at least annually (§ 52) would be complied with as long as the internal audit function of the firm has performed a review (§51)? This would be consistent with the exemption that seems to be provided for subsidiaries, and would avoid smaller firms incurring costs in mandating a third party to carry out this review.

11. The application of the rules to staff of asset management or insurance activities should be clarified.

<u>**Only individuals who have responsibilities at group level should be subject to the remuneration rules of the CRD4**</u>. If other individuals are considered as identified staff due to their remuneration level or their inclusion in a material business unit, they would in effect be subject to rules that are not applicable to their activity as per sectoral regulations. <u>These employees would be caught only because they belong to a group subject to the CRD4, not because their activity is risky enough to justify the application of the CRD4 provisions.</u>

<u>**Such application would create a major distortion of the playing field among the asset management and insurance industries, as pure players would be able to carry out their activities with a significant competition edge on salaries**</u>.

This also runs contrary to the diversification of risks that some groups seek to achieve with non banking activities, as these activities would lose their competitiveness and become non attractive to carry out in a CRD4 group.

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.

LACK OF LEGAL GROUND FOR CHANGING THE INTERPRETATION OF THE PROPORTIONALITY PRINCIPLE

12. **The wording and location of the proportionality principle in the CRD4 has not changed when compared to the CRD3. This means that neither the Parliament nor the Council expressed the need to recalibrate proportionality at level 1**. Yet, the European Commission considers that proportionality should not be interpreted in the same way as under CRD3, basing its interpretation on a legal analysis which is informed by no recital, nor the experience built from other regulations also using this principle, nor current application by Member States.

This results in guidelines that considerably depart from the CEBS guidelines based on CRD3, and which are overly restrictive, in effect banning proportionality for smaller and non complex institutions.

Such approach is contrary to the level 1 text, which does authorise neutralisation as stated in recital (66) of the Directive 2013/36/UE: "*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 organization 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****.* "

Surely, one can consider that if the legislators had the intention to curb the application of proportionality, such recital would not have been maintained. **In addition, the legislators have not expressed in the level 1 text any limitation as to the application of the proportionality principle, including to any particular remuneration requirements or any particular type of institution**.

THE PROPORTIONALITY PRINCIPLE IS INHERENT TO THE APPROACH TAKEN BY THE EU TO BASEL RULES

13. The Basel rules are designed to apply to very large institutions with an international reach. The EU however has chosen to translate these rules into EU legislation by systematically applying them to all institutions. By doing so, the EU recognised the risk that the rules may not be adapted to some institutions, hence the insertion of the proportionality principle. The purpose of this insertion is thus definitely not only to allow more stringent application by complex and large firms but also and primarily to allow for alleviation for smaller and less complex firms.

If the proportionality principle were to be inapplicable in allowing flexible application, the EU policy to transpose Basel rules to all institutions, including investment firms, should then be reassessed. The decision around the meaning of the proportionality principle therefore pertains to the legislator, not to the EBA, and should not stem from a level 3 text.

INCONSISTENT INTERPRETATION OF THE PROPORTIONALITY PRINCIPLE ACROSS EU LEGISLATION AND UNLEVEL PLAYING FIELD BETWEEN ASSET MANAGEMENT AND BANKING INDUSTRIES

14. It is also noticeable that the proportionality principle exists in several other regulations in the same terms as the ones used in CRD4.

It is noticeably the case of AIFMD as regards its provisions in remuneration (*Directive 2011/61/EU, recital (25), article 13.2, annex II*). The guidelines that ESMA produced on this subject (*ESMA/2013/201*), as mandated by the Directive, clearly state in § 25 that "*proportionality may lead, on an exceptional basis and taking into account specific facts, to the disapplication of some requirements if this is reconcilable with the risk profile, risk appetite and the strategy of the AIFM and the AIFs it manages and within the limits set by the present guidelines".*

It is then further specified in § 26 that some of the rules may not apply: "*This means that some AIFMs, either for the total of their identified staff or for some categories within their identified staff, may decide not to apply the requirements on:*

- *variable remuneration in instruments;*
- *retention;*
- *deferral;*
- *ex post incorporation of risk for variable remuneration".*

This shows that the same proportionality principle is currently interpreted by another European supervisory authority as authorising neutralisation, including in such matters as remuneration. It would therefore be highly inconsistent that the EBA decide otherwise as regards its guidelines.

This would also create competitive distortion between two financial industries, asset management and banking, with no argued purpose or reasoning.

ECONOMIC IMPACT OF THE PROPOSED INTERPRETATION ON SMALLER FIRMS AND THE FINANCING OF SMES

15. **From an economic point of view, the approach proposed in the draft guidelines is a major concern for the competitiveness of smaller and non complex firms on salaries and creates serious concerns as to their continuity (see the example provided below)**. Many of these firms do rely on variable remuneration to adjust to difficult years and avoid affecting their capital base.

However, the draft guidelines would induce them to reduce variable pay and increase fixed pay because:

- Their fixed salaries are in the lower end of the market, hence the bonus cap is reached more quickly;
- More of their employees would be considered MRTs as per the quantitative criteria, notably because the manager of the firm is generally the owner and therefore receives a low amount of remuneration (typically the manager relies on dividends and growing value of the business, not on salaries).

Removing the adjustment capacity of using variable pay would significantly increase their fixed costs, putting them at risk of bankruptcy in downturns, while contradicting the CRD4 objective of reinforcing firms' capital base.

16. In addition, applying all these requirements to small institutions is disproportionate when considering that these firms generally have a very limited number of staff to deal with regulatory and HR matters, let alone the complexity of about a hundred pages of guidelines on remuneration alone … This administrative burden is well beyond their capacity and raises concerns as to the effectiveness of these guidelines in reaching their objectives in practice.

17. **<u>Such approach would seem to bring consistency at European level (although this is highly debatable – see next paragraph) but without any respect for the situations of smaller firms and the larger goal of fostering economic growth in the EU</u>**.

This is a matter of principle that is highly critical to consider, especially in the context of the Capital Market Union. As AMAFI states in its answer to the green paper (*<u>see AMAFI/15-28 EN</u>*), the different historical, social and cultural backgrounds of individual countries may lead common European standards to be the subject of differing interpretations or adjustments, not all of which are unwarranted. Treating them all as barriers to a higher principle of harmonisation would be counterproductive if they have real value for the local ecosystem and generate positive effects. This is especially the case as regards business financing, which is ensured by a diversity of firms and in particular for SMEs by smaller domestic firms closer to them than global institutions.

<u>Harmonising the standards is important of course – as is removing unjustified barriers – and must be pursued, but should be prioritised only insofar as it contributes towards orderly markets and growth and does not risk weakening local ecosystems. The draft guidelines endanger these ecosystems by removing the financial basis on which the business model of a number of smaller firms is built, contributing to further concentration of the industry into large players.</u>

<u>THE PROPOSED INTERPRETATION WOULD CREATE AN UNLEVEL PLAYING FIELD AMONG CRD4 INSTITUTIONS</u>

18. By the same token, the draft guidelines also create a significant unlevel playing field between smaller firms which are part of a group and smaller firms which are independent.

This is because the level 1 provisions duly consider the case of smaller entities in a group as reminded by § 60 of the draft guidelines, "*competent authorities may make use of the derogation provided for in Article 7 of the CRR in accordance with article 109 (1) of CRD*", which means that they can waive the application of the remuneration rules on an individual basis. As a result, an entity belonging to a group may be applied the rules at group level, which would result in fewer identified persons, whereas a competitor of this entity, not belonging to a group, would be subject to the full application of the rules, at its own level.

Similarly, paragraph 101 states that the qualitative criteria referring to certain functions need to apply for staff members of a subsidiary only if the staff members are responsible for these functions on a consolidated or sub consolidated basis, such that a member of the management body of the subsidiary would not be an indentified staff if he or she is not also a member of the management body of the EU parent institution.

This approach, although certainly justified for subsidiaries, **<u>would result in an unlevel playing field between smaller or non complex firms depending on their belonging to a group. Any smaller or non complex firm should therefore be able to apply proportionality in a way that enables the non application of certain rules to adapt its remuneration policy and structure to its situation and be able to compete on similar ground with competitors</u>**.

<u>THE NEED FOR A CERTAIN DEGREE OF FLEXIBILITY WITHIN LIMITS FIXED AT EUROPEAN LEVEL</u>

19. National authorities are the best placed to identify the specific risks caused by activities of smaller entities, which often only have domestic activities and serve domestic clients. National authorities are closer to these firms and should be able to assess the risks caused by their remuneration policies and the appropriateness of their arrangements <u>considering features specific to their domestic market</u>. **Some**

flexibility should be allowed in their supervision as long as these firms are of a limited size, which could be set by the guidelines for consistency purpose.

20. Finally, the draft guidelines do no longer allow firms to disapply requirements such as deferral, payment in instruments and retention periods for employees whose variable remuneration is low.

This departs drastically from current practices of the vast majority of national competent authorities which have recognised the need for flexibility in this area to ensure the rules make sense for firms and their employees.

If arrangements for small amounts of variable compensation were no longer possible, this would have major impacts on a large number of employees with the lowest remuneration levels even though their impact on the risk profile of the company is low, or indeed nil.

If the CRD IV constraints had to be applied to each staff member identified at consolidated as well as at individual level, it would be very difficult to attract and retain staff members in functions, businesses or countries which have low variable remuneration levels. In practice, this could lead to increase fixed pay which would contradict the CRDIV objectives of aligning remuneration and risk.

CONCLUSION

21. **As a conclusion, the proposed interpretation of the proportionality principle does not appear to be legally based, nor serving the purpose of CRD4.**

AMAFI therefore suggests maintaining a flexible approach to proportionality by:

- **Defining a single common threshold at EEA level under which national supervisors can allow the application of less stringent rules, to promote a consistent application of the rules between Member States.**

- **As regards assert management and insurance activities, applying the CRD4 provisions only to individuals who have responsibilities at group level.**

- **As regards individuals with low variable remuneration, (i) maintaining flexibility in the application of the proportionality principle as per the CEBS' guidelines, with the possible neutralisation of some requirements or (ii) defines a single *de minimis* threshold (such as 100k€ of variable remuneration) under which such neutralisation would be possible. The concerned requirements relate to deferral, payment in instruments and retention periods.**

Example of a small and non complex investment firm

This example is not theoretical; it is based on the true facts of a member of AMAFI.

The firm

The firm is an investment firm licensed for the services of execution of orders on behalf of clients, reception and transmission of orders and placement without a firm commitment basis, on financial instruments excluding derivatives and funds.

It is a limited liability company with a board of directors and a supervisory board composed of independent persons with no executive function. It has a capital of 5 million euros.

The members of the boards collectively own 70% of the company's shares, none holding less than 35%. The rest is held by employees of whom there are 23.

Its activity

The firm has a single activity directed by the members of the board.

This activity consists in trading bonds and convertibles with institutional clients and large corporates on the secondary market (all clients are categorised as professional clients or eligible counterparties under MiFID). Its activity consisting uniquely in matching interests of third parties, it holds no own positions on its books overnight.

Its risks

The risks associated with the activity are settlement risk (which is limited by the delivery-versus-payment settlement of bond transactions), counterparty risk (which exists until the final settlement of transactions) and operational risk. As bond transactions settle T+2 and the firm holds no proprietary position, its settlement and counterparty risks have a length of time of only 2 days, except when a counterparty fails in its settlement.

The firm has no systemic impact on the market and its activity is low risk to itself, the main risk being operational in nature (its operational risk amount to 2.5 mm euros and its total risk to 2.7 mm euros). Due to its low level of risks, its total capital requirements amount to 300k euros.

Variability of the activity and remuneration as an adjustment variable

The business cycle of the firm is 2 days.

The firm's business is not based on an order book that would allow for forward planning: its activity is by nature driven by daily demand and there is no expectation that next month or next year activity level will be identical. The turnover of the firm is therefore highly cyclical - in the last 10 years, it experienced maximum year-on-year rises of 80 % and downturns of 35 %.

Salaries, including employers' tax contributions, represent 70% of the overall costs of the firm. Fixed salaries represent 20% of the firm's fixed costs, which allows the firm to retain a good proportion of variable costs to adapt to changing economic cycles.

The high proportion of salaries in the overall costs and the cyclical nature of the activity mean that variable salaries are effectively the only adjustment variable for the firm to avoid losses and reduction of its capital base in downturns. In this context, variable remuneration is not an incentive for staff to take on more risk and expose the firm over the coming years (as the activity in itself carries low risks and the business cycle is short), it is a reward for performance and a necessary adjustment variable in downturns to ensure the firm's continuity.

At the employee level, the variable remuneration is truly variable, i.e. it can be drastically diminished (down to zero) in case of non performance.

Long-term view of the activity

Members of the boards are the owners of the firm – they therefore have an inherent interest in ensuring its continuity. Their interests are fully aligned with those of the firm, as they are the first in line in case of bankruptcy. This ownership structure is an important factor to ensure short term profits do not take precedence on the firm's long term sustainability.

Half of the employees are shareholders, owning shares that they purchased directly rather than via a stock option plan, of which there is none in the firm. They are therefore committed to the firm's continuity as they have engaged capital in it. Their shares are valued based on the firm's net assets. This creates a strong alignment to risk for these employees, who are the most senior and therefore the most likely to be identified as MRTs.

Finally, the employees benefit from a profit sharing plan by which they receive a percentage of the net income, this percentage being the same for all employees.

Salary competitiveness of the firm

The fixed salaries of the revenue makers are typically 20% lower than industry average, which is detrimental to the firm's salary competitiveness. This is offset by opportunities to buy shares, a family atmosphere and variable remuneration that rewards true performance based on non arbitrary criteria. This means that the ratio between variable and fixed remuneration can range from 0 to 8, depending on the members of staff.

Since implementation of CRD3, the firm has raised the fixed salary of a few members of staff to retain a certain level of salary competitiveness, as the fixed portion of the remuneration has increased at competitors and has created a higher risk of staff leaving the firm. As described below, such rise can only be limited however, at the risk otherwise of endangering the firm.

Impact of the application of all remuneration rules and in particular the cap on variable remuneration

Impact on fixed remuneration

Out of a total staff of 25, 20 are salespersons and 5 belong to support functions. Application of the qualitative criteria of Regulation No 604/2014 to these staff members would result in the identification as MRTs of the members of the boards and the compliance officer.

Assuming staff members, who were awarded last year a total remuneration of EUR 500 000 or more or a total remuneration equal or above that of the members of the board of directors, effectively have an impact on the firm's risk profile when compared to the impact of staff members identified according to the qualitative criteria, 10 staff members could be further identified as MRTs.

These staff members being the best performers, the firm cannot afford to lose them. Application of the bonus cap would mean that, in order to retain them, fixed salaries would need to be raised. The firm could not afford though to raise them to a level compensating for the reduction of the variable remuneration in good years and would have to support additional fixed costs in bad years.

Example: The tables below compare the current costs and net income for the firm for a turnover of 13 mm euros and the costs and net income if 10 members of staff were identified as MRTs with increase in fixed salary from 75k euros to 120k euros. These tables do not include the administrative costs of setting up new arrangements to comply with the regulation.

Current costs and net income

		20 salespersons	1 Compliance	3 support staff
Fixed salary per person		75 000	50 000	
Total fixed salaries per function		1 500 000	50 000	140 000
Turnover	**13 000 000**			
Total variable remuneration		3 600 000	-	-
Tax on salaries		3 162 000	-	-
Profit sharing		400 000	30 000	120 000
Tax on profit sharing		120 000	9 000	36 000
Total remuneration charges per function		8 782 000	89 000	296 000
Total remuneration charges	**9 167 000**			
Other variable charges	**120 000**			
General expenses	**3 000 000**			
Net income before tax	**713 000**			

Costs and net income with 10 MRTs, a salary increase from 75 000 to 120 000 euros for these MRTs and no change in turnover

		10 MRTs	10 salespersons	1 Compliance	3 support staff
Fixed salary per person		120 000	75 000	50 000	
Total fixed salaries per function		1 200 000	750 000	50 000	140 000
Turnover	**13 000 000**				
Total variable remuneration		2 060 000	1 090 000	-	-
Tax on salaries		2 021 200	1 140 800	-	-
Profit sharing		315 000	195 000	30 000	120 000
Tax on profit sharing		94 500	58 500	9 000	36 000
Total remuneration charges per function		5 690 700	3 234 300	89 000	296 000
Total remuneration charges	**9 310 000**				
Other variable charges	**120 000**				
General expenses	**3 000 000**				
Net income before tax	**570 000**				

Current costs and net income with a decrease in turnover to 10.231 mm euros

		20 salespersons	1 Compliance	3 support staff
Fixed salary per person		75 000	50 000	
Total fixed salaries per function		1 500 000	50 000	140 000
Turnover	**10 231 000**			
Total variable remuneration		2 772 000	-	-
Tax on salaries		2 648 640	-	-
Profit sharing		-	-	-
Tax on profit sharing		-	-	-
Total remuneration charges per function		6 920 640	50 000	140 000
Total remuneration charges	**7 110 640**			
Other variable charges	**120 000**			
General expenses	**3 000 000**			
Net income before tax	**360**			

The net income is flat. The variable remuneration has decreased to adjust to the decrease in turnover.

Costs and net income with a decrease in turnover to 10.231 mm euros, 10 MRTs and a salary increase from 75 000 to 120 000 euros for these MRTs.

		10 MRTs	10 salespersons	1 Compliance	3 support staff
Fixed salary per person		120 000	75 000	50 000	
Total fixed salaries per function		1 200 000	750 000	50 000	140 000
Turnover	**10 231 000**				
Total variable remuneration		1 586 200	839 300	-	-
Tax on salaries		1 727 444	985 366	-	-
Profit sharing		-	-	-	-
Tax on profit sharing		-	-	-	-
Total remuneration charges per function		4 513 644	2 574 666	50 000	140 000
Total remuneration charges	**7 278 310**				
Other variable charges	**120 000**				
General expenses	**3 000 000**				
Net income before tax	- **167 310**				

N.B. The tax on salaries constitutes a significant portion of the costs due to French tax policy. This weights on the net income of the firm but applying lower tax rate would anyway show a significant impact on the net income of the classification as MRTs of 10 members of staff.

In the same economic situation, the firm makes a loss because it has tranformed some of its variable charges into fixed charges.

Conclusion : The firm has lost some flexibility to adjust to downturns and would have to further impact the remuneration of its staff to compensate for a higher break-even point. Such ability is however limited by labour laws and jurisprudence, which severely constrain or even impede reductions of variable remuneration.

Identification of MRTs

- The relative criterion based on the remuneration of the members of the board is an issue for the firm.

The members of the board receive a fixed salary and, in theory, could also receive dividends. However, due to the tax levied on the distribution of dividends, the firm makes an arbitrage between paying dividends or variable remuneration. This means that the total remuneration of the members of the board is actually highly dependent on tax matters, which in turns means that the number of MRTs (staff paid the same or more than the board members) will depend on tax arbitrage, and not at all on risk.

This relative criterion to identify MRTs has been designed for large firms with senior managers who own only a small portion of shares. It does not make sense though for small firms owned by their senior managers.

- The variability of the activity means that the remuneration of staff members can differ a lot year on year, making the situation of MRTs unstable.

If a staff member is considered an MRT for year n based on quantitative criteria related to n-1, they will be considered an MRT during the whole year n even if they do not perform during this year. This means that the break-even point for the profitability of this staff member will have increased, due to the higher cost associated to their status, making them more at risk of redundancy because of the lesser sustainability of this situation for the firm.

In addition, the firm regularly has experiences of employees who perform well over a quarter or a year and who are unable to repeat this performance (variations at an individual level range from one to three times the previous year's turnover). There is therefore a high degree of volatility in the total compensation of a single member of staff, which makes the assessment of MRTs based on quantitative criteria very volatile. A member of staff could therefore be an MRT a year but not the following and therefore experience totally different remuneration structures year on year.

The firm would have to set up a complex compensation structure to accommodate such situations, with a high degree of uncertainty for staff, as the compensation structure would become particularly unclear and volatile.

This is accentuated by the fact that, in France, it is almost impossible to reduce fixed salaries (to adapt to an economic downturn for example) and that labour law makes layoffs lengthy and costly.

In this respect, the firm's financials are very sensitive to staff disputes with labour courts. Due to its small size, the firm's net income can be rendered negative depending on the outcome of such a dispute.

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

22. Paragraph 83 states that all institutions should conduct a self-assessment in order to identify all staff whose professional activities have "*or may have*" a material impact on the institution's risk profile. The words in inverted commas are an addition to the level 1 text (*article 92 of Directive 2013-36-UE*) and should therefore be removed.

23. Paragraph 88 requires keeping updated at all times the assessment "*at least*" with regard to the criteria under Article 3 of the RTS, which refer to the qualitative criteria. However, it is impossible to keep updated at all times the assessment related to the quantitative criteria, especially since these quantitative criteria all refer to the preceding year. Also, there is no point in performing the identification every day when the award process occurs only once a year. The update should therefore be done at the same frequency as the award process, or at a minimum, the words "*at least*" should be removed.

24. Point d. of paragraph 88 is not clear: should the self-assessment include legal provisions from the CRD to document the identification outcome or should it include the documentation itself of the outcome?

25. The identification process on a solo and consolidated level is also subject to comments in our answer to Question 5.

26. In paragraph 93, the request for prior approval under article 4 (5) of the RTS on identified staff should be made each year, which is not logical. The approval should be valid until there is a change of position or in case of significant salary increase. It should not be required to ask again for approval on the same grounds for the same person every year.

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

27. In paragraph 113, it is stated that when a firm had a bad year and did not award variable pay, it cannot compensate for this in later years. This is not logical. Why would this not be possible if there is no detriment to the capital base of the firm and it is in line with actual performances achieved?

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

28. Some of the conditions applying to fixed remuneration are not appropriate:

- fixed salary can be reviewed upwards outside of collective bargaining or national criteria (criterion e);
- in some countries, fixed salary can be reduced upon the employer's sole decision, even if there is no change in the role or responsibilities of the staff member (criterion f).

29. An institution-wide profit sharing scheme which is non-discretionary and part of routine employment packages, which for example is based on the institution's ROE, and which does not create incentives for risk assumptions, should be considered as 'fixed remuneration'.

30. Mandatory severance payments for termination of an employment contract under national law should not be considered as remuneration. If it is decided otherwise then they should be considered as fixed remuneration because they comply with the conditions of paragraph 117: they are predetermined, permanent, not discretionary, transparent to staff, non-revocable, cannot be suspended or cancelled by the institution and do not provide incentives for risk assumption.

Q 9: Are the requirements regarding allowances appropriate and sufficiently clear?

31. AMAFI has no comment.

Q 10: Are the requirements on the retention bonus appropriate a sufficiently clear?

32. AMAFI has no comment.

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

33. AMAFI has no comment.

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

34. Paragraph 159 *states that "notification of any custodial accounts* [held by employees] *outside the institution should also be made mandatory."*

Such obligation cannot stem from guidelines, which have no legal status in front of a court. This requirement goes against the law on banking secrecy and the protection of personal data in France and cannot be complied with.

Such practices do exist in some countries but they cannot be implemented in France without violating the law. This provision should therefore be removed and the declaration of self commitment should be the only requirement.

Q 13: Are the requirements on remuneration policies in section 15 appropriate and sufficiently clear?

35. It is not clear what paragraph 174 seeks to achieve: if instruments are paid to complement cash, why should this be well reasoned and approved?

36. In paragraph 181, it is not clear what is meant by the requirement to set the ratio *"in a sufficiently granular way".*

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

37. Paragraphs 195, 196, 197, 202, 211, section 16.2.2, are examples of developments that are too complex to understand and implement for small institutions.

In particular as regards paragraph 211, it is not possible in a small firm that the variable remuneration of a controller be "*independent from the performance of the institution they control*".

38. In paragraph 222, it is mentioned that factors such as budget constraints should not dominate the distribution of the bonus pools. But if the budget constraints exist because the firm does not make money, there is no money to distribute, and therefore no pool... Hence, budget constraints are indeed a determining factor in setting bonus pools. These words should be removed.

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

39. Section 17.2 is another example of requirements that are too complex for a small institution. As an anecdote, it is not realistic to expect a firm of 20 people to take into account, as per paragraph 238, the EBA remuneration benchmarking report, to define whether its variable remuneration constitutes a particular high amount...

Q 16: Are the provisions on the award of variable remuneration in instruments appropriate and sufficiently clear? Listed institutions are asked to provide an estimate of the impact and costs that would be created due to the requirement that under Article 94(1)(l)(i) CRD only shares (and no share linked instruments) should be used in parallel, where possible, to instruments as set out in the RTS on instruments. Wherever possible the estimated impact and costs should be quantified and supported by a short explanation of the methodology applied for their estimation.

40. Paragraph 248 a. fails to list "*equivalent non-cash instruments*" mentioned in Art. 94(l)(i) of the CRD for non-listed institutions.

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

41. In paragraph 263, the minimum retention period is set at 12 months, whereas most local implementations are currently based on a minimum of 6 months. A 12 months period creates negative tax consequences for the staff concerned because tax are levied at attribution based on the instruments' value at that time, so that it is important to set this minimum at 6 months.

Q 18: Are the requirements on the ex post risk adjustments appropriate and sufficiently clear?

42. Paragraphs 268 and 270 and section 17.7.2 are other examples of complex requirements for small institutions.

Q 19: Are the requirements in Title V sufficiently clear and appropriate?

43. AMAFI has no comment.

Q 20: Are the requirements in Title VI appropriate and sufficiently clear?

44. It should be made clear that the guidelines apply for the performance year 2016 and onwards. In addition, the guidelines are likely to be published during the second semester of 2015, which will be too late for institutions to be ready by the 1st of January. Institutions should be given six months at least from the date of publication to implement the guidelines.

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

45. No, AMAFI does not agree that the overall cost impact of the guidelines is low with a medium benefit.

As explained in its answer to Q5, the approach to proportionality needs to be assessed not only in terms of costs but also in terms of impact on risk and business models.

Smaller firms will be put at a competitive disadvantage from a remuneration point of view due to their cost structure. Although the guidelines could have a sizeable impact on costs due to the organisational arrangements that would be needed for smaller firms, the true impact will be on their capacity to continue business, as their key staff are likely to move to other areas not subject to such constraints on remuneration (asset management, insurance, non regulated activities...) or to other institutions (large groups with the capacity to offer higher fixed salaries and therefore higher variable remuneration) or to countries outside of the EU. This reality should be considered in the impact assessment.

It is not correct to state in paragraph 123 that the guidelines will provide for sound risk management: for these firms, they would on the contrary create a sizeable risk on their capacity to consolidate their capital base, quite the opposite of the CRD4 objective. This is particularly paradoxical as these firms do not create a systemic risk to financial stability and will never receive State support were they to go bankrupt.

46. The guidelines will also have an impact on staff in terms of morale and incentives, especially if staff with lower level of variable remuneration are applied the rules, whereas there is no rationale for such application. This will create misunderstanding and social malaise, or will lead to the rise of fixed salaries and the loss of flexibility, both impacts that are not cost related but would need to be considered in terms of additional resulting risk.

47. Finally, it must be stressed that the objectives of the EBA mentioned in paragraph 12 of section 6, to reach a level playing field is not all met with the guidelines, as these will on the opposite create competitive distortions among industries and among similar market players depending on their belonging to a group (see our answer to Q5).

Additionally, it is not correct to state, in the same paragraph, that "*the development of common procedures and practices is expected to reduce the compliance burden on the institutions*" as regards smaller institutions, because due to the guidelines, they will face a level of administration and complexity for their remuneration structure that they have never faced until now.

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.

48. The guidelines, because they depart from the level 1 text on the matter of proportionality, will create implementation costs for smaller institutions, which have not implemented all rules of the CRD4 or not to their full extent.