30 August 2017

EBF_028459

EBF answer to the FSB consultative document on "Supplementary Guidance to the FSB Principles and Standards on Sound Compensation Practices."

1. Should the Guidance be more specific with regard to the respective roles of the board or that of senior managers with regard to compensation and misconduct?

We consider that the Board of directors at Group level (or a board sub-committee with delegated powers if legally feasible) should be responsible for reviewing and validating the Group compensation policy, including the general principles that should be taken into account in the performance assessment and for the employees compensation awards in case of misconduct. The policy and principles validated by the Board of directors at Group level could be adapted by each subsidiary according to any necessary modification, in particular to accommodate differences in local legislation.

However, we consider that the operational implementation of these compensation principles, the day-to-day monitoring of the compensation policy and the effective management of compensation and misconduct risk should remain the duty of senior managers, at each business line level with the involvement of control functions and in the framework of the local legislation.

The criteria/KPI/metrics to be taken into consideration to define misconduct situations and on which the employees should be assessed, should be defined by HR, compliance and risk functions, business lines and validated by senior management. Ex-post, a reporting including a synthesis of the most significant cases of misconduct with the impact on the variable compensation awarded could be communicated to the Board at least annually.

European Banking Federation aisbl

Brussels / Avenue des Arts 56, 1000 Brussels, Belgium / +32 2 508 3711 / info@ebf.eu
Frankfurt / Weißfrauenstraße 12-16, 60311 Frankfurt, Germany
EU Transparency Register / ID number: 4722660838-23

www.ebf.eu

As a consequence, on page 8 of the document, the references to the Board defining misconduct risk as well as to the Board effectively managing risk misconduct shall be deleted.

Lastly, in the 5th bullet point of page 8, the reference to the Board of directors challenging senior management's compensation assessments and recommendations is not clear. It should be clarified that the Board of directors is not the right body to review and assess the compensation for all the company's employees; this shall remain within the senior management's scope of missions. The role of the Board of directors, concerning individuals, is limited to senior executives (CEO/deputy CEO(s)) as it has the power to nominate and revoke them, as well as, if provided for under applicable law, the head of the risk function and, as the case may be, the heads of other control functions. We recommend the wording is changed as follows:

> ***Boards of directors should assess the compensation of senior executives (limited to the CEO/deputy CEO(s) and, if provided under applicable law, the heads of control functions) and make recommendations if warranted, when senior executives' misconduct occurs and ensure that new rules and policies are adopted, as necessary, to prevent it from happening again.***

2. The Guidance suggests that qualitative, non-financial assessments should have a direct impact on compensation and that they are important in determining how to align compensation with risk. Would additional guidance be helpful? Please provide data if your firm uses such provisions including the types of metrics used, and a discussion of any challenges you face in their use.

We consider that qualitative and non-financial criteria should be taken into account in the annual performance appraisal that is performed by managers and considered for the determination of the annual variable compensation. It is important that flexibility is given to institutions to define criteria and metrics that should be taken into account depending on each situation. However, we consider that the type and number of criteria used should be proportionate according to the category of employees and their impact on the Group/company risk profile. Indeed, we consider that a deep and specific attention should be paid in particular to employees identified as Group Material Risk Takers and other Group senior managers.

3. The Guidance identifies three tools most commonly used to address misconduct: in-year adjustment (adjustment to the current year's variable compensation before it is awarded); malus (reduction of deferred compensation before it has vested or fully transferred); and clawback, which permits recovery of variable compensation that has already been paid and vested. Given the particular characteristics of misconduct risk, do you believe that all three tools need to be available to a firm to establish appropriate incentives to deter misconduct?

We agree that these tools can be used to address misconduct, however all these tools are not applicable to all categories of staff. Indeed, whereas the current year's variable compensation could be potentially adjusted for each category of staff benefitting from variable compensation, the application of malus is only possible concerning employees subject to deferral, and for the part of their variable compensation that is deferred (in particular employees identified as material risk takers), which seems to be appropriate according to their potential impact on the Group/company risk profile. Concerning clawback provision, which enables the institution to recover all or part of variable compensation already paid, it is not applicable in many countries due to local labour law that prohibits such mechanisms. In particular, in France, according to the labour code, pecuniary sanctions are prohibited and any provision consisting of a pecuniary sanction is considered as null and void.

We believe that combination of those three tools (or two, in countries where clawback provisions are not allowed) is enough and appropriate to address misconduct situations.

4. The Guidance suggests minimum scenarios where adjustment of compensation should occur. Are there additional circumstances in which adjustments to compensation should be expected? What are the advantages and disadvantages of suggesting such minimum conditions? In particular, is there evidence from past use of such tools that might be instructive in how to formulate such scenarios?

Even if we agree that some scenarii should be presented in the guidance for which compensation adjustment may occur, flexibility should be given to institutions to define at their level the different scenarii for which adjustments of compensation should occur, according to their size, activities, organisation, local legal framework and according to the categories of staff. These scenarii should be defined on the basis of the minimum misconduct situations such as breach of risk control rules, of internal policies, procedures and Code of conduct, and should be updated according to the feedback from past use of such tools and material failure or breaches experienced by institutions.

5. How much variable compensation should be placed at risk of adjustment in order to effectively impact incentives for excessive risk-taking or other inappropriate conduct?

The answer to this question should depend on the category of staff, their absolute amount of variable compensation and the weight of the variable compensation in their total package.

In any case, we consider that the variable compensation should be sufficient enough to be adjusted in case of economic downturn and/or in case of misconduct to have material impact on employees' behaviour. Consequently, it should be possible to reduce the total variable compensation to zero, in particular, in case of gross misconduct situations that have significant financial impact on the institution.

6. Does the Guidance adequately cover compensation incentives that may be relevant to addressing misconduct risk in all sectors of the financial industry? Are there additional specific provisions that should be considered to better address misconduct risks in particular financial sectors? Are there specific provisions in the guidance that may not be relevant to a particular financial sector?

We consider that compensation is important to address misconduct but should not be the only key driver to address conduct risk. Indeed, a strong governance process with the promotion of compliance and risk culture for all Group employees with a clear communication of Group Code of Conduct requirements including identification of bad and good behaviour, and mandatory training (including via e-learning) on conduct expectations together with the promotion and reinforcement of positive employee behaviour on risk and compliance management are also relevant and efficient means to address misconduct risk and to improve institutions' conduct culture.

About EBF

The European Banking Federation is the voice of the European banking sector, uniting 32 national banking associations in Europe that together represent some 4,500 banks - large and small, wholesale and retail, local and international - employing about 2.1 million people. EBF members represent banks that make available loans to the European economy in excess of €20 trillion and that securely handle more than 300 million payment transactions per day. Launched in 1960, the EBF is committed to creating a single market for financial services in the European Union and to supporting policies that foster economic growth.

www.ebf.eu @EBFeu

For more information contact:

Blazej Blasikiewicz
Policy Adviser
b.blasikiewicz@ebf.eu
+32 2 508 37 47