



The voice of banking
& financial services

27 September 2012

European Securities and Markets Authority

Dear Sirs,

**Consultation paper - Guidelines on sound remuneration policies under the AIFMD –
ESMA / 2012 / 406**

The BBA is pleased to respond to the consultation.

Key messages

The original intention of the Financial Stability Board (FSB) Principles on Sound Compensation Practices was to ensure a coordinated response to reforming remuneration in the Financial Services Sector. It was viewed as essential that these principles were coordinated centrally and implemented consistently to ensure a global level playing field to allow firms to compete fairly in the global market place.

The ESMA guidelines, which go far beyond regulatory requirements in other international markets, are applicable globally to all EEA headquartered organisations. This means that non-EEA organisations will enjoy a competitive advantage in jurisdictions where they are not bound by such prescriptive rules on remuneration policy. The BBA is keen to understand how ESMA intends to address this issue and would urge ESMA to be flexible in the way that the rules are applied to subsidiaries outside the EU to mitigate the severe competitive impacts on European firms.

UK firms have already aligned their practices so that their remuneration policies are consistent with and promote sound and effective risk management. They have also complied with the principles established by the Financial Stability Board through the requirements of the 2009 FSA Remuneration Code. As part of this code, the FSA signed off on the remuneration policy statements of UK credit institutions and investment firms in 2010 and 2011.

The industry recognises that effective measures on remuneration are important. However, if these are not progressed in a practical and proportionate manner there is a risk that key personnel will either seek to relocate outside the EU, or be reluctant to move to the EU. Over time this would have an increasingly significant impact on the amount of financial services jobs, activities and revenues located in the EU. Other regions, notably North America and Asia-Pacific, would stand to gain.

Furthermore, depending on how prescriptively and conservatively the rules and guidance are implemented, the impact is likely to be felt most intensely in only a small number of larger international markets (i.e. London, Paris and Frankfurt).

Given the heavy concentration of global markets activity in these three EU Member States, the key focus of new rules should be about ensuring a level playing across the EU. High quality standards should have the flexibility to support the EU's ability to compete for global talent while ensuring that it supports effective risk management. We would urge ESMA to take the lead to ensure that this happens.

Some of our members, both British and continental-headquartered, have reported difficulties in recruiting and/or retaining employees in third countries in the past few years. Not only do the new rules make it more difficult for EU firms to execute their strategy, which have often been agreed with supervisors as part of the capital management process, they make it more difficult for these banks to support their clients in key, often emerging, markets.

The fact that some third countries scope banks into their rules, which are derived from the FSB's principles, but not other financial institutions, adds to the uneven playing field.

We would also encourage ESMA to take a more granular approach in considering which employee groups requirements should focus on. In particular, we would suggest that the relatively small number of globally mobile staff should be recognized as a different group within distinct recruitment and retention issues that must be dealt with at a global level to ensure a consistent, fair and robust approach.

Technical issues

Retention

The industry would appreciate clarity on two issues. Firstly, we would like to know ESMA's intention regarding the use of a retention period. In particular, the BBA is interested in understand if equity that is fully vested during the retention period must be structured as requiring outright ownership of the shares by the employee, or can notional ownership be continued, but with malus/clawback conditions ceasing to apply?

Secondly, a number of operational implications arise as a direct result of the use of a retention period. For instance, in the United Kingdom a potential tax charge would arise at the time the upfront equity is awarded for higher rate tax payers. As the position stands, an employee would be prohibited from selling a portion of the shares to settle this tax liability. On this basis they would be required to use the upfront cash award, and potentially some of their own personal income, to settle the tax due, significantly reducing the value of the cash award, in some cases to nil. Given these fundamental issues, which extend to multiple jurisdictions, firms would welcome comments from ESMA on the extent to which the impact of tax and the potential for personal tax liabilities has been considered.

We believe that the examples provided by ESMA where shorter retention periods are allowable are unrealistic. The total deferral and retention period needed to satisfy the requirements is in excess of a normal employee's life cycle at most firms.

Guarantees

We believe that limiting guarantees in the ways proposed, in particular the limitation to only offer guarantees to new hires and only in the first year of service, will produce a "poachers' paradise" by incentivising companies to focus on external hiring (rather than developing and rewarding their own talent). This will be particularly important in times of instability, for example during change of control conditions, when employers will be unable to motivate current staff with guaranteed variable remuneration and so will focus instead on external hiring. This requirement will also prevent companies from responding to external approaches on their staff, and make retaining the most talented and desired employees extremely difficult, particularly in non-EEA markets. Within the EU this will lead to structural instability into the labour market (through higher turnover and potentially

higher remuneration), which is unlikely to be consistent with good risk management. In addition, we believe that retention bonuses for existing staff should be permitted in exceptional limited circumstances.

Ratio of fixed to variable pay

The application of a potential ratio (fixed versus variable) may lead to an increase in the overall level of fixed compensation and a reduction in variable compensation, with employers aiming to keep the level of total compensation whole. This would reduce the amount and proportion of compensation already subject to forfeiture or adjustment provisions. Clearly, this is not in line with ESMA's intended outcome as any reduction in variable compensation also reduces the ability of firms to apply risk adjustment measures as well as decreasing the opportunity to reduce total compensation where the performance of the business or individuals is below expectations.

Further to the above reference to ratios, there should be no hard caps on fixed and variable pay. This will allow firms greater flexibility when implementing the revised Code.

Firms should have the opportunity to justify circumstances where there is unusually high leverage between fixed and variable pay at the point awards are recommended, rather than setting a pre-defined ratio.

Other issues

Proportionality

The BBA welcomes ESMA's recognition through proportionality clauses of the huge variety of size and business model in firms that will be covered by the Guidelines. We also support a flexible approach that allows firms to balance a variety of risk-adjustment techniques to achieve a remuneration model that best matches their business requirements and risk frameworks. We also welcome an approach in which local supervisors are free to respond to breaches of remuneration requirements in a way which best suits the nature of the breach and the company involved without necessarily resorting to automatic, punitive quantitative measures.

Alignment

For global firms it is likely that several sets of remuneration regulations, home and host, EU and third country, will apply. We would welcome further guidance from ESMA on how this would work in practice. Therefore, we urge ESMA to ensure a practicable solution, for example by way of colleges of supervisors as per the college of supervisors that operate under the auspices of the European Banking Authority. We would also welcome co-operation between international regulators to reduce the need to demonstrate compliance separately to each regulator in every country in which a banking group operates. Our members would also welcome the opportunity of only dealing with one, lead, regulator in the EU whichever structure is adopted.

We would also like to draw ESMA's attention to overlaps between the proposals made by the Capital Requirements Directive (CRD) and Solvency II. We urge ESMA to liaise with the EBA and EIOPA to ensure that no contradictions arise and there is no double counting of capital when making adjustments.

Conclusion

Firms should have the autonomy to decide on the most appropriate mix of remuneration provided it supports sound risk management. Remuneration policy and practice should be consistent with risk management and the avoidance of excessive risk.

The financial services industry operates in a global and competitive environment so a global solution is needed. The failure to align practice between the EU and the rest of the world may lead to arbitrage and the loss of business as firms locate operations outside the EU, and to less regulated and/or more tax-advantageous jurisdictions.

Many firms operating in the EU have global remuneration policies that are set outside the EU. Without a co-ordinated global approach, further reform will be difficult to implement consistently and have only partial effect.

Annexes 1 and 2 to our letter contain our formal response to the consultation, and further specific observations and questions arising from the proposals.

We hope that you will find our comment useful. Please contact me by way of e-mail (irving.henry@bba.org.uk) or telephone on (00 44) 20 7216 8862 should you require further information.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'I. Henry', with a stylized flourish at the end.

Irving Henry
Director, Prudential Capital and Risk

Annex 1

The 50% rule and the limit on upfront cash bonuses

ESMA has taken a different view to the FSA on the application of the CRD 3 “50% rule”. The ESMA Guidelines state explicitly that the requirement to deliver 50% of any variable remuneration in the form of shares and other non-cash instruments must be applied (separately) to both the non-deferred and deferred portion of variable remuneration. This means that the maximum cash bonus that can be delivered to Identified Staff (Code Staff for the purposes of the FSA Remuneration Code) is, respectively 20% (in a case where 60% deferral is applied) and 30% (in cases where a 40% deferral is applied).

BBA: How long will national supervisors have to consult and change their existing/proposed rules to implement what ESMA requires?

The 50% rule – non-cash instruments

Unlisted entities are able to satisfy the requirement to deliver 50% of any variable remuneration in the form of a non-cash instrument by offering shares and share-linked instruments or non-cash instruments.

BBA: ESMA has not provided any substantive guidance on the sorts of instruments that would fall within this description.

ESMA has not elaborated what unlisted firms or legal entities that are not joint stock companies should do or what would be a safe harbour for them.

The 50% rule – retention policy

ESMA has indicated that firms should establish a “minimum retention period” for the 50% of any upfront payment delivered in the form of shares and other non-cash instruments. Although the appropriate retention period is left up to the firm in question, ESMA has said that for senior staff the retention period in some circumstances should be longer than the three or five year deferral period for the deferred instrument.

BBA: No guidance is given as to what these circumstances are, or what an appropriate period may be. If there is no retention, or the period is not acceptable to supervisors, will a capital charge be imposed on the firm?

The 50% rule – general comments

It would be appropriate to allow a de minimis bonus threshold to be set under which bonuses do not have to be deferred or retained for Code Staff.

The guidelines indicate that where appropriate and applicable, the proportion of the variable remuneration that is paid out in instruments (either upfront or deferred) must be a combination, appropriately balanced, of both categories. This requirement generates complexity for employees on the nature of their remuneration and so has an impact on the perceived value. Some of our cross-border members would also like to highlight that there are circumstances where local legislation prohibits variable remuneration from being paid in equity or such instruments – we believe this would be an allowable exception to this requirement.

There should be alignment between the FSB and ESMA to drive global consistency. Firms should be able to determine the relevant deferral and retention periods which can be explained and justified to national supervisors.

Proportionality

ESMA confirms that some institutions may be exempt from applying significant parts of the remuneration principles (including those relating to remuneration structures) depending on their size scope and complexity. The guidelines state that it will be up to the relevant institution to determine whether it would be disproportionate to apply the remuneration principles in full.

BBA: Without additional detailed guidance on the criteria to be applied by an institution making this assessment, this creates uncertainty and the risk that firms will all approach this exercise in different ways. It could also be problematic if the relevant authority takes a different view at the end of the year when that institution comes to make bonus payments as it will be difficult to ensure compliance retrospectively given the need to amend contracts and set up deferred remuneration schemes.

The ability to dis-apply certain aspects of the remuneration proposals on proportionality grounds is welcome. We hope that the FSA will expand its guidance to the revised Remuneration Code to provide greater clarity for small credit institutions and investment firms on the extent to which they may dis-apply the Code.

The ESMA guidelines also suggest that, as well as allowing some institutions to dis-apply aspects of the remuneration principles on the basis of their institution's nature, scale, scope and complexity, they will also allow institutions to dis-apply aspects of the principles in respect of specified groups of staff within the institution on the same grounds.

BBA: We welcome the avoidance of a one size fits all approach. Without greater clarity, the concept of inter-firm proportionality could lead to wide variation in the expectations of national regulators from different firms. For significantly smaller firms, governance processes should be simpler as there is greater line of sight between decision-makers and the employees over which they have remuneration oversight. However, the concept of proportionality could be exploited by some firms in order to deliver a lower standard of governance. We do not believe this is the intention of the proportionality approach.

We would also ask how ESMA anticipates their approach to proportionality will interact with the proportionality principles under CRD, and in particular, which will take precedence.

Other issues

"Sign-on" bonuses - The guidelines confirm that "sign-on" bonuses will be treated in the same way as guaranteed bonuses.

BBA: no comment

- Individuals covered by the Remuneration Principles - ESMA have confirmed that individuals that fall into the same remuneration bracket as senior managers and SIFs (significant influence function) still have to be "material risk takers" in order to qualify as "Identified Staff" (FSA Code Staff), meaning that employees do not fall into this category on the basis of pay levels alone.

BBA: This suggests that control functions (audit, risk and compliance) should not necessarily fall into scope, which is welcome as their impact on the risk profile of the firm is quite different from that of traders, relationship managers etc. This is a welcome recognition that these functions are sufficiently paid to maintain their independence and to recruit and retain high quality staff.

Employees exercising significant influence functions (SIFs) are easily identifiable in the United Kingdom given the Financial Services Authority's (FSA) strong governance rules. The industry would benefit from more rigorous perimeters around who are regarded as "senior management" and, more importantly, "material risk takers". Consistent application of these terms also falls within the notion of a level playing field.

It is important to identify which individuals can have a significant impact on the risk profile of the firm. The BBA welcomed the definition set out in the FSA Code and believes that current differences between ESMA and the FSA are due to drafting of the requirements rather than an intended material difference. With appropriate governance structures in place, groups of individuals should not, under normal circumstances, be able to have an impact on the risk profile of the firm. Therefore, we would suggest that ESMA removes this from their definition.

Identified / Code Staff population should be structured so that it covers all appropriate roles and there should not be a separate population (i.e. control functions) whose remuneration the Remuneration Committee is required to approve as well.

- "Golden parachute" – The guidelines strongly discourage such arrangements. Severance payments can include payments relating to notice period, redundancy, loss of office and for entering into restrictive covenants, but should not reward failure.

BBA: no comment

- Fixed and variable remuneration - The guidelines say an institution should set in its remuneration policy explicit maximum ratio(s) on the variable component in relation to the fixed component of remuneration. ESMA has stopped short of saying what that ratio should be, but have provided guidance on what factors firms ought to take into account when setting such a policy.

BBA: A bigger fixed component adds to the cost base, which may encourage the firm to pursue higher risk strategies so that it generates enough returns to cover its costs. The right balance, respecting the nature, scale and complexity of the firm, should be struck.

- Forfeiture/performance adjustment conditions

BBA: The guidelines on forfeiture and performance adjustment conditions exceed the requirements of CRD (3), which state that total variable remuneration should be considerably contracted when subdued or negative financial performance of the firm occurs.

The ESMA approach reflects the approach adopted by the FSA in its draft Remuneration Code in making reference to evidence of behaviour or serious error by staff or a significant failure of risk management in the institution or relevant business unit. It is important that this issue is implemented consistently across Member State regulators to prevent competitive disadvantage.

Ex-post risk adjustment is appropriate at an individual or team level where performance fails to crystallise or was materially misstated. However, this would not be appropriate at a divisional or organisational level, as individual accountability should be able to be attributed. Similarly where there is a material downturn in a firm's financial or business unit performance this should drive ex-ante risk adjustment of forward looking remuneration rather than ex-post from previously awarded remuneration.

- Geographical scope – The guidelines make it clear that the AIFMD remuneration principles apply in respect of an EEA subsidiary of a non EEA group at the level of the EEA subsidiary (or its EEA holding company) and cover its subsidiaries and other companies (both EEA and non-EEA) subject

to EU consolidated supervision. However, the non-EEA parent company does not have to apply the remuneration principles at the parent company level.

BBA: The application of the remuneration principles to EU bank subsidiaries in non-EEA countries has the potential of placing the EU bank at a competitive disadvantage if non EEA banks operating in that jurisdiction are not subject to such stringent rules. In addition there may also be difficulties in complying with the principles if the local jurisdiction's employment, company or other legislative provisions conflict with the remuneration principles.

- Conflicting Directives

BBA: The guidelines acknowledge that some firms coming within the scope of the CRD (3) requirements may subsequently be caught by remuneration provisions contained in the Alternative Investment Fund Managers Directive. It is to be hoped that the final version of the ESMA guidelines acknowledges the importance of consistency of approach across the two Directives or in the alternative that a proportionate approach would allow an institution to elect to comply with the remuneration provisions of one regime only.

If the guidelines were implemented by the FSA without any amendment we think a serious conflict between the AIFMD requirements to defer remuneration into fund units and the FSA's Code to defer into equity would be created. Bearing this in mind we would stress the need for a flexible approach to be taken in the application of the directive.

- Taxation

Regulation should not give rise to tax liabilities that do not currently arise or impact upon the ability of firms and individuals to pay their tax bills in the way they do now. In particular, deferral requirements should not impede the receipt of cash by individuals to enable them to pay their tax bills.

The above is linked to the geographical scope of the requirements and the companies within a group that are subject to the requirements. There are wider international issues for non-UK individuals who may have tax liabilities in other jurisdictions.

ESMA's proposal of an additional retention period (by the employee) after vesting (paragraphs 129 – 136), i.e. when ownership of the shares and cash transfers from the employer to the employee, has an impact on UK tax policy.

Under British tax practice, shares become legally the employee's property upon vesting, which results in a tax liability for the employee. Typically under existing arrangements, employees would sell shares to meet the tax liability.

At the end of the vesting period ESMA is proposing a further retention period (which may be equal to the vesting period). This would also apply to the proportion of non-deferred award that must be held in shares and vests immediately.

The tax liability may be deemed due on vesting, but due to the retention period the employee would not be able to sell shares to satisfy the tax liability. Given the 50/50 split between shares and cash on both the deferred and non-deferred elements, and assuming a 50% tax rate then all of the net cash could be taken up paying the cash liability.

Tax applies to the value of the shares at vesting. However, the value of the shares may in theory fall to zero by the time the employee has the right to sell them (after the expiry of the retention date) meaning they could pay a tax charge for no realised value.

For example:

100 units variable pay, delivered as:

20 immediate cash
 20 immediate shares but with retention period
 30 deferred cash
 30 deferred shares with retention period to follows

The 20 immediate shares potentially trigger a tax charge of 10, which would be paid by the net value of the immediate cash.

The 30 deferred shares potentially trigger a tax charge of 15 on vesting, which would be paid by the net value of the deferred cash.

The end result of this is no cash being paid to the employee.

There are also tax implications with regard to discretionary pension benefits.

In short, the combination of deferral, vesting and internationally mobile employees creates a large degree of complexity for both organisations and individuals. This could result in an employee having a tax liability for remuneration which ultimately has no value at the end of the retention period.

- Governance of remuneration

Remuneration of members of the management and supervisory function (to be decided by the Remuneration Committee): This is already the case in the United Kingdom.

Composition (Remuneration Committee): There may be a lack of candidates due to the greater role of and need for non-executive directors, and their new and increased legal obligations (vide the UK's Walker Review). Therefore, a transition or regulatory forbearance is in order.

- Role of the Remuneration Committee

We believe that the Remuneration Committee should approve the compensation of Identified / Code Staff as an effective governance model. We do not believe it is necessary for the Remuneration Committee to also recommend remuneration proposals for the highest paid individuals, should these individuals sit outside the Code Staff population.

- Disclosure

We believe that the key focus should be to align disclosure requirements across different national supervisors, so that the home country disclosure satisfies all national supervisors across the EEA. However, there needs to be a balance between transparency and the public being able to identify individual remuneration details.

We would also ask whether the Group's global Compensation Statement will be sufficient for the purposes of compliance with principle 194, or whether there is a requirement for a separate remuneration statement/ disclosure for the AIFM.

- Performance measurement

The mix of approaches is correct.

- Risk adjustment

The mix of approaches is correct.

- Time horizon and vesting

There may be suggestion that deferral applies to either cash or shares, but not both.

- Kind of (non-cash) instruments

Basel III and the CRD address the issue of capital being raised by means of hybrid and other non-equity instruments. Basel III, to be followed by CRD IV, gives greater prominence to equity due to its loss bearing characteristics. Therefore, hybrid capital will play a lesser role in the structure of banks.

Annex 2

List of questions

II. Background

Q1: Do you agree with the approach suggested above for developing the present Guidelines? If not, please state the reasons for your answer and also suggest an alternative approach.

We support this approach as it aligns with the EBA's guidelines, and welcome the recognition that the concept of risk and reward differs between banks and asset managers.

IV. Scope of the Guidelines

Q2: Do you agree with the above considerations on the scope of the Guidelines? In particular, do you agree with the clarifications on what should be considered as a remuneration falling into scope and what should be considered an ancillary payment or benefit falling outside the scope of the Guidelines? If not, please state the reasons for your answer and also suggest an alternative approach.

We would welcome further clarification from ESMA as to how to distinguish payments as outlined at principle 21 (i) and (ii).

We are concerned with an application of the AIFMD remuneration principles to any payment made by the AIFM or the AIF to an entity to which an activity has been delegated. The provisions regarding delegation are already quite restrictive; firms are required to prove that the entity to which an activity has been delegated has been diligently chosen. We would also emphasize the fact that the delegated investment managers are often compensated on the basis of a market-based fee, which covers the compensation as well as cost incurred by the investment manager. Furthermore it is important to note that the delegated investment manager will usually be subject to MiFID and as such see no need to impose further restrictions within the scope of the AIFMD

Q3: Do you see any benefit in setting a quantitative or qualitative threshold at which the portion of the payment made by the AIF exceeding the pro-rata investment return for the investment made by the relevant staff members is transformed into carried interest? If yes, please make suggestions on the threshold to be used.

BBA has no comments.

Q4: Do you agree that the AIFMD remuneration principles should not apply to fees and commissions received by intermediaries and external service providers in case of outsourced activities?

BBA has no comments.

Q5: Notwithstanding the fact that the provisions of the AIFMD seem to limit the scope of the principles of remuneration to those payments made by the AIFM or the AIF to the benefit of certain categories of staff of the AIFM, do you consider that the AIFMD remuneration principles (and, therefore, these Guidelines) should also apply to any payment made by the AIFM or the AIF to any entity to whom an activity has been delegated by the AIFM (e.g. to the remuneration of a delegated investment manager)?

BBA has no comments.

Q6: Do you consider that payments made directly by the AIF to the AIFM as a whole (e.g. payment of a performance fee or carried interest) shall be considered as payments made to the benefit of the relevant categories of staff of the AIFM and, therefore, fall under the scope of the AIFMD remuneration rules (and, therefore, of these Guidelines)?

BBA has no comments.

Q7: Do you agree with the categories of staff identified above which should be subject to the remuneration principles set out in the Guidelines? If not, please state the reasons for your answer and also suggest an alternative approach.

It should be noted that terms used such as “control functions” and “other risk takers” are not defined which is likely to create uncertainty as to the range of employees to be potentially captured. Human Resources, Marketing employees etc will be identified staff unless it can be demonstrated that they have no impact on the material risk profile of the AIFM. It would be beneficial to have further clarification on how a firm will be deemed to have ‘demonstrated’; for example, is the onus on the AIFM to make a decision, and is documentation required?

We would also request that further clarification is provided on the proposed timing of implementation; will it be 22 July 2013 as outlined at principle 34 will the regulations apply to compensation paid or earned after that date, or is the intention that the regulations will apply to any payments made during 2013 (which would potentially capture amounts earned in 2012 but paid in 2013)

Q8: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section IV (Scope of the Guidelines) would imply.

BBA has no comments.

V. Proportionality principle

Q9: Do you agree with the clarifications proposed above for the application of the proportionality principle in relation to the different criteria (i.e. size, internal organisation and nature, scope and complexity of activities)? If not, please state the reasons for your answer and also suggest an alternative approach.

We welcome the flexibility.

Q10: Do you agree with the clarifications proposed above for the application of the proportionality principle to the AIFM’s categories of staff? If not, please state the reasons for your answer and also suggest an alternative approach.

We welcome the flexibility.

Q11: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section V (Proportionality principle) would imply.

BBA has no comments.

VI. AIFMs being part of a group

Q12: Do you agree that there is a need for consistency in the potential application of different requirements for AIFMs which belong to a group subject to other principles?

Yes, we agree with the need for consistency. This applies to groups in terms of sectoral frameworks and jurisdictions.

Q13: Do you agree that the proposed alignment of the CRD and AIFMD remuneration provisions will reduce the existence of any conflicting remuneration requirements at group level for AIFMs whose parent companies are credit institutions subject to the CRD? If not, please state the reasons for your answer and provide quantitative details on any additional costs implied by the proposed approach.

The alignment is all to the good. It requires supervisors to be sensitive to the differences between sectors, and even jurisdictions, and how recruitment and retention differ. However, there is a concern that stricter requirements in one legislation would automatically trigger the adjustment of the previous legislation without properly assessing the adequacy of such an adjustment and ultimately leading to overly prescriptive guidelines.

Leading on from this it would be useful to know how ESMA anticipates the interaction of the guidelines with CRD III. For example, in the circumstances where an Asset Manager is part of a Tier 1 organisation which is already under the scope of CRDIII, are these new rules intended to apply? Or are the guidelines instead designed to capture AIFM that weren't previously captured? If the guidelines are intended to apply, will application be limited to the Alternative Investment businesses of the Asset Manager and not the broader business (i.e. would not apply to traditional investment areas or sales staff?)

Q14: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section VI (AIFMs being part of a group) would imply.

BBA has no comments.

VII. Financial situation of the AIFM (Annex II, paragraph 1(o) of the AIFMD)

Q15: Do you agree with the above principle aimed at preserving the soundness of the AIFM's financial situation? If not, please state the reasons for your answer and also suggest an alternative approach.

We are satisfied this mirrors what happens in banks.

However, we would question if defining a principle in relation to the financial soundness of the AIFM lies within ESMA's remit. One could argue the financial security of an AIFM is already addressed through the licensing of the asset manager. There is also potential conflict with national labour laws, in particular in regards to claw-backs.

Q16: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section VII (Financial situation of the AIFM) would imply.

BBA has no comments.

VIII. Governance of remuneration

Q17: Do you agree with the proposed split of competences between the members of the management function and those of the supervisory function? If not, please provide explanations.

We agree with the split, but caution that the approach should depend on the complexity of the firm.

Q18: Do you agree with the guidelines above on the shareholders' involvement in the remuneration of the AIFM?

We agree that shareholders should have a say on pay.

Q19: Do you agree with the criteria above for determining whether or not a RemCo has to be set up? If not, please provide explanations and alternative criteria.

The guidance is sensible.

Q20: Do you agree that in assessing whether or not an AIFM is significant, consideration should be given to the cumulative presence of a significant size, internal organization and nature, scope and complexity of the AIFM's activities? If not, please provide explanations and alternative criteria.

The criteria are fine.

Q21: Please provide quantitative data on the costs and benefits that the proposed criteria to determine whether a RemCo has to be set up would imply.

The costs would depend on the business model.

Q22: Do you see merits in adding further examples of AIFMs which should not be required to set up a RemCo? If yes, please provide details on these additional examples.

There is enough for firms to work with.

Q23: Do you agree with the principles relating to the composition of the RemCo? Please provide quantitative data on the costs and benefits that the proposed principles on the composition of the RemCo would imply.

We agree.

Q24: Do you see any need for setting out additional rules on the composition of the RemCo?

There are enough rules for firms to work with.

Q25: Do you agree with the role for the AIFM's RemCo outlined above? If not, please provide explanations.

We agree.

Q26: Do you agree with the principles above on the process and reporting lines to be followed by the RemCo? If not, please provide explanations.

We agree.

Q27: Do you consider that the AIFM's RemCo should provide adequate information about the activities performed not only to the AIFM's shareholders' meeting, but also to the AIFs' shareholders' meetings? When providing your answer, please also provide quantitative details on the additional costs involved by such requirement.

We do not believe that this is necessary. The entities are different.

Q28: Do you agree with the above criteria on the remuneration of the control functions? If not, please provide explanations.

We agree.

Q29: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section VIII (Governance of remuneration) would imply.

BBA has no comments.

IX. General requirements on risk alignment

Q30: Do you agree with the principles related to the treatment of discretionary pension benefits? If not, please provide explanations.

We do not dispute the need the need to align interests, but with regard to pensions, there are local regulations, e.g. tax, that need further consideration.

Q31: Do you consider appropriate to add any further guidance on the payments related to the early termination of a contract? If yes, please provide suggestions.

There are enough guidelines for industry to work with.

Q32: Do you consider that the above guidance is sufficiently broad to cover any kind of hedging strategies that may be pursued by a member of the staff of an AIFM? If not, please provide details on how the scope of the guidance should be enlarged.

We believe that to be the case. However, further clarification is required on whether the requirement for staff to undertake not to use personal hedging strategies extend to the hedging of foreign exchange risk associated with compensation awards.

Q33: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section IX (General requirements on risk alignment) would imply.

BBA has no comments.

X. Specific requirements on risk alignment

Q34: Do you consider these common requirements for the risk alignment process appropriate? If not, please provide explanations and alternative requirements.

The requirements are appropriate and allow firms the flexibility to design measures suitable for themselves. However, on closer inspection there appears to be a contradiction between principles 125 and 126.

Q35: Do you agree with the proposed criteria on risk measurement? If not, please provide explanations and alternative criteria.

We agree.

Q36: Do you agree that in order to take into account all material risks AIFMs should also take into account the risks arising from the additional management of UCITS and from the services provided under Article 6(4) of the AIFMD?

BBA has no comments.

Q37: Do you agree with the proposed guidance for the financial and non-financial criteria to be taken into account when assessing individual performance? If not, please provide explanations and alternative guidance.

We agree. This mirrors practice in banking, which goes back to the 1990s.

Q38: Do you agree with the proposal to distinguish between absolute and relative performance measures on one side and between internal and external performance measures on the other? If not, please provide explanations.

The guidelines are very prescriptive; firms need to be allowed a certain level of discretion.

Q39: Do you agree with the requirement set out above to document the policy for the award process and ensure that records of the determination of the overall variable remuneration pool are maintained? If not, please provide explanations and an alternative procedure.

We agree. This mirrors practice in banking and, in accordance with the FSA's SYSC rules, go back a decade in the UK.

Q40: Do you agree with the proposal according to which AIFMs should use both quantitative and qualitative measure for the ex-ante risk adjustment? If not, please provide explanations and an alternative proposal.

We agree. This mirrors practice in banking. There is flexibility that is appropriate for different business models.

Q41: Do you agree with the guidance on the different components to be considered in relation with the deferral schedule for the variable remuneration? If not, please provide explanations and alternative guidance.

We agree. This mirrors practice in banking.

Q42: Do you agree with the types of instruments composing the variable remuneration which have been identified by ESMA? If not, please provide explanations.

Please see annex 1.

Q43: Do you consider that additional safeguards should be introduced in these Guidelines in order to ensure that the payment of the Identified Staff with instruments does not entail/facilitate any excessive risk-taking by the relevant staff in order to make short-term gains via the instruments received? If yes, please provide details.

The measures proposed are sufficient.

Q44: Do you agree with the proposed guidance for the retention policy relating to the instruments being a consistent part of the variable remuneration? If not, please provide explanations and alternative guidance.

Please refer to our main letter above.

Q45: Do you agree with the proposed guidance for the ex-post risk adjustments to be followed by AIFMs? If not, please provide explanations and alternative guidance.

We agree.

Q46: Do you agree with the analysis on certain remuneration structures which comply with the criteria set out above? If not, please provide explanations.

We agree.

Q47: Do you consider that there is a need for submitting to an equivalent/similar treatment any other form of remuneration? If yes, please provide details of the remuneration structure(s) and of the specific treatment that you consider appropriate.

We do not believe that this is necessary.

Q48: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section X (Specific requirements on risk alignment) would imply.

BBA has no comments.

XI. Disclosure

Q49: Do you consider appropriate to require AIFMs to apply the same level of internal disclosure of remuneration as they apply to their external disclosure? Please state the reasons of your answer.

As the disclosures are to different parties, with different objectives, they are necessarily different.

Q50: Please provide qualitative and quantitative data on the costs and benefits that the rules proposed in this Section XI (Disclosure) would imply.

BBA has no comments.

Annex 3

The British Bankers' Association ("BBA") is the leading trade association for the UK banking and financial services sector. We represent over 230 banking members, which are headquartered in 60 countries and have operations in 180 countries worldwide. These member banks collectively provide the full range of banking and financial services, and make up the world's largest international banking centre.