

SWEDISH SECURITIES DEALERS ASSOCIATION

EUROPEAN SECURITIES AND MARKETS AUTHORITY

www.esma.europa.eu

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RESPONSE TO CONSULTATION PAPER ON GUIDELINES ON REMUNERATION POLICIES AND PRACTICES (ESMA 2012/570)

The Swedish Securities Dealers Association (SSDA, register id 7777147632-40) represents the common interest of banks and investment firms active on the Swedish securities market. The mission of SSDA is to work for a sound, strong and efficient securities market in Sweden. The SSDA's main tasks include to promote high confidence in the securities market (inter alia through self-regulation, standards and guidance) and to promote members' views with regard to regulatory, market and infrastructure related issues. The SSDA also provides services to members by distribution of information and know-how in matters of common interest.

The SSDA has a close cooperation with other trade associations in Sweden, the Nordic area and Europe.

General remarks

ESMA argues that remuneration policies are part of conflicts of interest within firms as well as that remuneration practices and policies always have been part of being MiFID compliant. The SSDA agrees with this statement and notes that firm's remuneration policies therefore already should be MiFID compliant. In this connection, we question the timing of these detailed guidelines on remuneration policies and practices. A better approach would in our opinion be to deal with these issues in the context of the on-going MiFID-review. Moreover, the SSDA notes that rules of remuneration are currently being negotiated in the context of other EU-legislation and would therefore also like to urge ESMA to liaise with EBA in order to avoid duplication of requirements when preparing technical standards/guidelines on remuneration.

The SSDA would also like to underline that it is very important that the guidelines allow for necessary flexibility, in order to leave room for investment firms different organisational structures and business models. Some of the proposed rules are in our opinion too detailed. It should be remembered that it is not in a firm's interest to construct inappropriate bonus schemes as this

incentivize wrong behavior or lead to wrong pay-outs of large bonuses. Firms therefore already have governance processes in place and normally allow for discretionary adjustments of bonus outcomes etc. rather than applying strict mathematical (commission-style) bonus schemes that risk giving “wrong” outcomes.

The SSDA welcomes the statement by ESMA made in the introduction that the guidelines should be read together with the principle of proportionality. However, it is not clear from the actual guidelines how this principle of proportionality is intended to apply in practice as regards the policies and practices on remuneration. We would like to underline that clarity on this point is of importance both for investment firms and competent authorities in their supervision. Therefore, we believe that it would be very useful if ESMA would put some additional efforts into providing more detailed guidelines on how this principle of proportionality is to be applied, preferably under relevant sections of the guidelines.

In this connection, the SSDA would also like to stress that it is important that ESMA while issuing new guidelines avoids using terms and expressions which are not used in the level 1 or level 2 texts. There is a substantial risk that ESMA in such situations only creates new uncertainties and problems of interpretation. Moreover, it is important that where a term is given a specific meaning in the level 1 or 2 text (or in other EU legislation), such terms are not given another meaning in ESMA guidelines. For instance, the SSDA finds it very unfortunate that ESMA uses the term “relevant persons” in these guidelines on remuneration and gives it another meaning than in the MiFID level 2. In order to avoid confusion and also to provide clearer rules as to the scope of the guidelines, SSDA proposes that ESMA uses another term instead which is properly defined in the guidelines.

It is of great importance both for investment firms and competent authorities that the scope of the guidelines from ESMA is clear. The SSDA notes that in the consultation document, many important rules as regards scope follow from the introductory text and not from the actual guidelines. One example of this is the statement regarding focus on retail clients and sales activities.

Finally, the SSDA is concerned with the fact that depending on the level of detail used in the ESMA guidelines, employment contracts may need to be re-negotiated. For larger firms this may take some time and it is therefore important that the implementation times are reasonable.

Detailed remarks

Q1 Do you agree that firm’s remuneration policies and practices should be aligned with effective conflicts of interest management duties and conduct of business risk management obligations so as not to create incentives that may lead relevant persons to favor their own interest, or the firm’s interests, to the potential detriment of clients? Please also state the reasons for your answer.

Yes, we agree. It is important that investment firms have clear policies and procedures so as to avoid incentives that their employees favor their own interests at the detriment of clients. However, we believe that this already follow from MiFID and will, according to latest compromise texts, be even further emphasized under MiFID II. It is important not avoid detailed rules which fail to accommodate the need for flexibility depending on e.g. different organizational structures and/or business models.

Q2 Do you agree that, when designing remuneration policies and practices, firms should take into account factors such as the role performed by relevant persons, the type of products offered, and the methods of distribution? Please also state the reasons for your answer.

Yes, we agree that a remuneration policy should take into account the role of the employees and type of products offered. A variable remuneration should not be linked to the sale of one specific product. However, it is important that firms are able to design their policies to serve their business models best and to assess how the structure best fulfill the client's best interests. In addition, policies must allow for managers formulating which factors are to be seen as relevant for their subordinates.

As mentioned above, we do believe that the use of the term "relevant persons" may create a risk of confusion considering that this term has another meaning in MiFID Level 2 regulation.

Q3 Do you agree that when designing remuneration policies and practices firms should ensure that the fixed and variable components of the total remuneration are appropriately balanced?

We agree that the fixed and variable components of the remuneration should be balanced and consider such general requirement to be in line with the current interpretation of CRD rules. An employee shall not be tempted to take undue risks or give unsuitable advice so as to meet bonus targets. However, we do not agree to ESMA's general statement that a high variable remuneration necessarily creates always short term profit interests as this also depends on whether the policy is constructed and followed-up in an appropriate manner.

Q4 Do you agree that the ratio between the fixed and variable components of remuneration should therefore be appropriate in order to take into account the interests of the clients of the firm? Please also state the reasons for your answer.

See reply to Q 2 and 3. Firms should be able to design their policies to serve their business model and assess how the structure best fulfill the client's best interests. It is important that ESMA guidelines should not set any quantitative thresholds or require exact ratios between fixed and variable components but leave to the firm how to best protect client's best interest.

Q5 Do you agree that the performance of relevant persons should take account of non-financial (such as compliance with regulation and internal rules, market conduct standards, fair treatment of clients etc.), as well as financial, criteria? Please also state the reasons for your answer.

As a matter of principle, we believe that also non-financial criteria are important. But it is also important to leave it to firms to decide what is a good balance between these criteria as well as what criteria to use in different services and for different types of staff. From a practical perspective, there could also be some challenges as to the control and supervision of some types of non-financial criteria.

Q6 Do you agree that the design of remuneration policies and practices should be approved by senior management or, where appropriate, the supervisory function after taking advice from the compliance function? Please also state the reasons for your answer.

Yes, this proposal is in our opinion in line with existing interpretations of CRD-requirements. It is important that the compliance function is involved in order to ascertain that the remuneration policy complies with applicable regulation. However, also the involvement of other control functions could in some cases be relevant, such as risk control function. We therefore propose that the phrase "after taking advice from the compliance function" be replaced by "after taking advice from relevant internal control functions". This is important in order to ensure appropriateness for different organizational setups for internal control.

Q7 Do you agree that senior management should be responsible for the implementation of remuneration policies and practices, and for preventing and dealing with any the risks that remuneration policies and practices can create? Please also state the reasons for your answer.

Yes. This is important in order to make sure that there is an awareness of conflicts of interests and risks attached to remuneration policies. In our opinion, the proposal is in line with current interpretation of CRD-rules.

Q8 Do you agree that the organizational measures adopted for the launch of new products or services should take into account the remuneration policies and practices and the risks that the new products or services may pose? Please also state the reasons for your answer.

All investment firms should in our opinion have an NPAP (new product approval process) in place. As a part of this process, conflicts of interests (including those arising from remuneration policies) should generally be taken into account. However, it is not necessary that a launch of a new product per se triggers a legal requirement to review existing remuneration policies or processes. The firm should always review its policies or processes on an annual basis and where relevant. The guidelines should be clarified on this point.

Q9 Do you agree that the process for assessing whether the remuneration features related to the distribution of new products or services comply with the firm's remuneration policies and practices should be appropriately documented by firms? Please also state the reasons for your answer.

See reply to Q 8. Documentation is important and shall be ensured. However, in order not to create excessive administrative burden on firms and for the sake of organizational effectiveness, it is investment firms must have some freedom to decide how to comply with applicable documentation requirements. ESMA should in this connection clarify that the principle of proportionality applies.

Q10 Do you agree that firms should make use of management information to identify where potential conduct of business and conflict of interest risks might be occurring as a result of specific features in the remuneration policies and practices, and take corrective action as appropriate? Please also state the reasons for your answer.

Yes. This proposal is in line with current interpretation of CRD-requirements, i.e. requiring firms to have a risk analysis in place and to annually review how remuneration policies and practices are implemented and, if necessary, take remedial actions. Monitoring should be performed in accordance with a risk based approach and the risks relating to remunerations should be considered in the light of other business risks in the firm.

Q11 Do you agree that firms should set up controls on the implementation of their remuneration policies and practices to ensure compliance with the MiFID conflicts of interest and conduct of business requirements, and that these controls should include assessing the quality of the service provided to the client? Please also state the reasons for your answer.

Yes. It is important with appropriate control that employees follow the regulations, including MiFID conflicts of interests and conduct of business requirements. However, whereas some controls relating to remuneration policies and practices could be carried out by the compliance functions, we believe that assessing the quality of the service provided to the client is better done by management i.e. defining performance criteria relevant for the position and respecting firms' general values. See also reply to Q 10.

Q12 Do you agree that the compliance function should be involved in the design process of remuneration policies and practices before they are applied to relevant staff? Please also state the reasons for your answer.

Yes. See above reply to Q 5.

Q13 Do you agree that it is difficult for a firm, in the situations illustrated above in Annex I, to demonstrate compliance with the relevant MiFID rules?

Yes, we agree that in the situations illustrated in Annex I it could be difficult to demonstrate MiFID compliance. However, we note that some examples of “good and bad practices” are also included in the actual guidelines and would prefer that all such examples instead follow from the annex. Moreover, it is important the ESMA properly balances the benefits of illustrative examples to the risks of creating new problems of interpretation. As mentioned above, it is also important that any guidelines regarding remuneration models allow for some flexibility by discretionary judgment. Too mathematical reward systems risks creating wrong incentives as well as wrong payouts. Assuming that a firm’s starting point is to not pay out excessive bonus amounts, the firm will ensure proper governance models and remuneration policies allowing for flexibility/discretionary adjustments.

Q14 If you think some of these feature may be compatible with MiFID rules, please describe for each of (a), (b), (c) and (d) in Annex I above which specific requirements (i.e. stronger controls, etc.) they should be subject to.

In our opinion, the general description of “in-house products” in example 2 a very wide in scope should be narrowed down.

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