Capital Requirements Directive/ Regulation

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Chapter 12

Commission Delegated Regulation (EU) No 604/2014

Preamble

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, and in particular Article 94(2) thereof,

01/01/2021

Whereas:

(1) Directive 2013/36/EU, and in particular Article 74 thereof, requires institutions to have robust governance arrangements and effective processes to identify, manage, monitor and report the risks that they are or might be exposed to. These arrangements and processes are to be comprehensive and proportionate to the nature, scale and complexity of the risks inherent in the business model and the institution's activities. They must take into account, amongst others, the specific risks identified in Articles 79 to 87 of that Directive. The arrangements and processes are evaluated by competent authorities as part of the supervisory review and evaluation process pursuant to Article 97 of that Directive. The risks identified are considered by institutions within the internal capital adequacy assessment process pursuant to Article 73 of that Directive.

(2) The framework for prudential supervision established by Directive 2013/36/EU requires that all institutions identify all members of staff whose professional activities have a material impact on the institution's risk profile. The criteria that are used to assess the materiality of the influence of the professional activities of staff on the risk profile should take into account the potential impact of staff on the institution's risk profile based on their authority and responsibilities and the institution's risk and performance indicators. The institution's internal organisation and the nature, scope and complexity of its activities should be taken into account in the assessment. The criteria should fully reflect all risks to which the institution or group is or may be exposed. This should also enable institutions to set proper incentives within the remuneration policy to ensure the prudent behaviour of staff and should ensure that the identification of those members of staff whose professional activities have a material impact on the institution's risk profile reflects the level of risk of different activities within the institution.

(3) In 2012, the European Banking Authority (EBA) published the results of a survey on national implementation and the practical application of the guidelines issued by the

Committee of European Banking Supervisors on remuneration policies and practices (the CEBS Guidelines), which contained general criteria for the assessment of the materiality of the influence of staff on the institution's risk profile. The survey showed that the implementation by institutions and competent authorities of the remuneration provisions laid down in Directive 2006/48/EC of the European Parliament and of the Council did not result in a sufficient degree of harmonisation. The range of remuneration practices remained inappropriately broad and, in particular, the criteria used to identify staff did not always sufficiently consider the impact of staff's professional activities on the institution's risk profile. Significant discrepancies remained in the approaches taken by different institutions and Member States to identify those staff. These regulatory technical standards should therefore build on the experience gathered in applying Directive 2006/48/EC and the CEBS Guidelines and aim to achieve a higher level of harmonisation. EBA will issue new guidelines on sound remuneration policies which comply with the principles set out in Directive 2013/36/EU, pursuant to Article 75(2) of that Directive.

(4) A set of clear qualitative and appropriate quantitative criteria should be established in order to identify the core categories of staff whose professional activities have a material impact on an institution's risk profile, ensuring a harmonised approach across the Union and covering a common set of the most relevant risks. In accordance with Article 94(2) of Directive 2013/36/EU, all the categories of staff identified by those criteria must be of staff whose professional activities have a material impact on an institution's risk profile. Institutions should also take into account the results of their own risk assessments within their internal procedures. Competent authorities should ensure a complete identification of all staff whose professional activities have a material impact on an institution's risk profile.

(5) Members of the management body have the ultimate responsibility for the institution, its strategy and activities and therefore are always able to have a material impact on the institution's risk profile. This applies both to the members of the management body in its management function who take decisions and to members of the supervisory function who oversee the decision making process and challenge decisions made.

(6) The senior management and senior staff responsible for material business units, for management of specific risk categories such as liquidity, operational or interest rate risk, and for control functions within an institution are responsible for the day-to-day management of the business, its risks, or its control functions. This includes the responsibility for making strategic or other fundamental decisions on the business's activities or the control framework applied. The risks taken by the business and the way they are managed are the most important factors for the institution's risk profile.

(7) In addition to those responsible for creating additional business, functions responsible for providing internal support which are crucial to the operation of the business and have authority to take decisions in those areas expose the institution to material operational and other risks. Therefore the professional activities of staff members in such functions also have a material impact on the institution's risk profile.

(8) Credit risk and market risk are typically entered into in order to generate business, therefore the impact of the activities generating those risks on the risk profile can be assessed using criteria based on limits of authority which are calculated at least annually on the basis of capital figures and approaches used for regulatory purposes, while applying a *de minimis* threshold for credit risks to ensure the proportionate application of the criteria within small institutions.

(9) The criteria to identify staff whose professional activities have a material impact on the institution's risk profile should take account of the facts that the requirements relating to the trading book can be waived for some institutions under Regulation (EU) No 575/2013 of the European Parliament and of the Council and that limits are set in different ways between institutions using different approaches for the calculation of the capital requirements.

(10) Considering that the outcome of decisions is often influenced by the staff initiating the decision while the formal decision making power rests with more senior staff or committees, the criteria should take into account the material elements in such decision-making processes.

(11) Staff in a managerial position are responsible for the business activities in the area under their management. Therefore, appropriate criteria should ensure that members of staff are identified as having a material impact on the institution's risk profile where they are responsible for groups of staff whose activities could have a material impact on the institution's risk profile. This includes situations where the activities of individual staff members under their management do not individually have a material impact on the institution's risk profile but the overall scale of their activities could have such an impact.

(12) In addition to the qualitative criteria, appropriate quantitative criteria should be established to identify categories of staff whose professional activities have a material impact on the institution's risk profile. Total remuneration awarded depends principally on the contribution that staff make to the successful achievement of the institution's business objectives and therefore on the responsibilities, duties, abilities and skills of staff and the performance of staff and the institution. Where a member of staff is awarded total remuneration which exceeds an appropriate threshold, it is reasonable to presume that this is linked to the staff member's contribution to the institution's business objectives and to the impact of the staff member's professional activities on the risk profile of the institution. Accordingly, it is appropriate to base those quantitative criteria on the total remuneration a member of staff receives, both in absolute terms and relative to other members of staff within the same institution. In applying those quantitative criteria, account should, where appropriate, be taken of the fact that payment levels differ across jurisdictions. Clear and appropriate thresholds should be established to identify staff whose professional activities have a material impact on the institution's risk profile, taking into account the data collected by EBA and by competent authorities. These quantitative criteria form a strong presumption that staff have a material impact on the institution's risk profile. However, such presumptions based on quantitative criteria should not apply where institutions establish on the basis of additional objective conditions that staff do not in fact have a material impact on the institution's risk profile, taking into account all risks to which the institution is or may be exposed. The exclusion of the highest earning staff identified under these criteria should be subject to the approval of the competent authority to ensure effective and consistent application of those criteria. For staff awarded more than EUR 1000000 (high earners) competent authorities should inform EBA before exclusions are approved to ensure the coherent application of those criteria, in particular in such exceptional circumstances. The identification process, including the application of exclusions, should nevertheless always be subject to supervisory review in accordance with Article 92(2) of Directive 2013/36/EU.

(13) The fact that staff members are in the same remuneration bracket as senior management or risk takers may also be an indicator that the staff member's professional activities have a material impact on the institution's risk profile. When establishing the bracket, the remuneration paid to staff in control functions, support functions and members of the management body in the supervisory function should not be taken into account. In the application of this criterion, account should also be taken of the fact that payment levels differ across jurisdictions. Institutions should be allowed to demonstrate that staff

who fall within that remuneration bracket, but do not meet any of the qualitative or other quantitative criteria, do not have a material impact on the institution's risk profile, taking into account all risks to which the institution is or may be exposed. The exclusion of staff with a high level of total remuneration from this criterion should be subject to a notification procedure to allow for a timely supervisory review, in order to ensure consistent application of this criterion.

(14) Competent authorities should ensure that institutions maintain a record of the assessment made and of the staff whose professional activities have been identified as having a material impact on their risk profile to enable the competent authority and auditors to review the assessment. The documentation should also include staff who have been identified under criteria based on their remuneration but for whom the professional activities are assessed as not having a material impact on the institution's risk profile.

(15) This Regulation is based on the draft regulatory technical standards submitted by EBA to the Commission.

(16) EBA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council,

HAS ADOPTED THIS REGULATION:

Article B1 Definitions

In this Regulation:

"appropriate regulator" has the meaning given by regulation 2(1) of the Capital Requirements Regulations 2013;

"authorised person" has the same meaning as in FSMA (see sections 31(2) and 417(1) of that Act);

"Directive 2013/36/EU UK law" means the law of the United Kingdom (or any part of it) which, immediately before IP completion day, implemented Directive 2013/36/EU as that law has effect on IP completion day;

"the FCA" means the Financial Conduct Authority;

"FSMA" means the Financial Services and Markets Act 2000;

"the PRA" means the Prudential Regulation Authority;

"PRA-authorised person" has the same meaning as in FSMA (see sections 2B(5) and 417(1) of that Act);

a reference to a provision of the PRA rulebook is to the rules made by the PRA under FSMA as amended by rule-making instruments made before IP completion day under FSMA or EU Exit Instruments made at any time under the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018;

a reference to a provision of a sourcebook is to a sourcebook in the FCA Handbook of Rules and Guidance made by the FCA under FSMA as amended by rule-making instruments made before IP completion day under FSMA or EU Exit Instruments made at any time under the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018.

Article 1 Subject matter and scope

This Regulation establishes regulatory technical standards with respect to qualitative and appropriate quantitative criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile, as referred to in Article 92(2) of Directive 2013/36/EU, at group, parent company and subsidiary levels, including institutions established in offshore financial centres.

Article 2 Application of the criteria

Staff who meet any of the qualitative criteria set out in Article 3 of this Regulation or any of the quantitative criteria in Article 4 of this Regulation shall be identified as having a material impact on an institution's risk profile.

Article 3 Qualitative criteria

Staff shall be deemed to have a material impact on an institution's risk profile where any of the following qualitative criteria are met:

(1) the staff member is a member of the management body in its management function;

(2) the staff member is a member of the management body in its supervisory function;

(3) the staff member is a member of the senior management;

(4) the staff member is responsible and accountable to the management body for the activities of the independent risk management function, compliance function or internal audit function;

(5) the staff member has overall responsibility for risk management within a business unit as defined in Article 142(1)(3) of Regulation (EU) No 575/2013 which has had internal capital distributed to it in accordance with Directive 2013/36/EU UK law which implemented Article 73 of Directive 2013/36/EU that represents at least 2 % of the internal capital of the institution (a "material business unit");

(6) the staff member heads a material business unit;

(7) the staff member has managerial responsibility in one of the functions referred to in point (4) or in a material business unit and reports directly to a staff member identified pursuant to point (4) or (5);

(8) the staff member has managerial responsibility in a material business unit and reports directly to the staff member who heads that unit;

(9) the staff member heads a function responsible for legal affairs, finance including taxation and budgeting, human resources, remuneration policy, information technology, or economic analysis;

(10) the staff member is responsible for, or is a member of, a committee responsible for the management of a risk category provided for in Directive 2013/36/EU UK law which

implemented Articles 79 to 87 of Directive 2013/36/EU other than credit risk and market risk;

(11) with regard to credit risk exposures of a nominal amount per transaction which represents 0.5 % of the institution's Common Equity Tier 1 capital and is at least EUR 5 million, the staff member:

(a) is responsible for initiating credit proposals, or structuring credit products, which can result in such credit risk exposures; or

(b) has authority to take, approve or veto a decision on such credit risk exposures; or

(c) is a member of a committee which has authority to take the decisions referred to in point (a) or (b);

(12) in relation to an institution to which the derogation for small trading book business provided for in Article 94 of Regulation (EU) No 575/2013 does not apply, the staff member:

(a) has authority to take, approve or veto a decision on transactions on the trading book which in aggregate meet one of the following thresholds:

(i) where the standardised approach is used, an own funds requirement for market risks which represents 0.5 % or more of the institution's Common Equity Tier 1 capital; or

(ii) where an internal model-based approach is approved for regulatory purposes, 5 % or more of the institution's internal value-at-risk limit for trading book exposures at a 99th percentile (one-tailed confidence interval); or

(b) is a member of a committee which has authority to take decisions set out in point (a);

(13) the staff member has managerial responsibility for a group of staff members who have individual authorities to commit the institution to transactions and either of the following conditions is met:

(a) the sum of those authorities equals or exceeds a threshold set out in point 11(a), point 11(b) or point 12(a)(i);

(b) where an internal model-based approach is approved for regulatory purposes those authorities amount to 5 % or more of the institution's internal value-at-risk limit for trading book exposures at a 99th percentile (one-tailed confidence interval). Where the institution does not calculate a value-at-risk at the level of that staff member the value-at-risk limits of staff under the management of this staff member shall be added up;

(14) with regard to decisions to approve or veto the introduction of new products, the staff member:

(a) has the authority to take such decisions; or

(b) is a member of a committee which has authority to take such decisions;

(15) the staff member has managerial responsibility for a staff member who meets one of the criteria set out in points (1) to (14).

Article 4 Quantitative criteria

(1) Subject to paragraphs 2 to 5, staff shall be deemed to have a material impact on an institution's risk profile where any of the following quantitative criteria are met:

(a) the staff member has been awarded total remuneration of EUR 500000 or more in the preceding financial year;

(b) the staff member is within the 0.3 % of the number of staff, rounded up to the next integer, who have been awarded the highest total remuneration in the preceding financial year;

(c) the staff member was in the preceding financial year awarded total remuneration that is equal to or greater than the lowest total remuneration awarded in that financial year to a member of senior management or to a member of staff who meets any of the criteria in points (1), (5), (6), (8), (11), (12), (13) or (14) of Article 3.

(2) A criterion set out in paragraph 1 shall not be deemed to be met where the institution determines that the professional activities of the staff member do not have a material impact on the institution's risk profile because the staff member, or the category of staff to which the staff member belongs:

(a) only carries out professional activities and has authorities in a business unit which is not a material business unit; or

(b) has no material impact on the risk profile of a material business unit through the professional activities carried out.

(3) The condition set out in point (b) of paragraph 2 shall be assessed on the basis of objective criteria which take into account all relevant risk and performance indicators used by the institution to identify, manage and monitor risks in accordance with Directive 2013/36/EU UK law which implemented Article 74 of Directive 2013/36/EU and on the basis of the duties and authorities of the staff member or category of staff and their impact on the institution's risk profile when compared with the impact of the professional activities of staff members identified by the criteria set out in Article 3 of this Regulation.

(4) An institution shall notify the appropriate regulator of the application of paragraph 2 in relation to the criterion in point (a) of paragraph 1. The notification shall set out the basis on which the institution has determined that the staff member concerned, or the

category of staff to which the staff member belongs, meets one of the conditions laid down in paragraph 2 and shall, if applicable, include the assessment carried out by the institution pursuant to paragraph 3.

(5) The application of paragraph 2 by an institution in respect of a staff member who was awarded total remuneration of EUR 750000 or more in the preceding financial year, or in relation to the criterion in point (b) of paragraph 1, shall be subject to the prior approval of the appropriate regulator.

The appropriate regulator shall only give its prior approval where the institution can demonstrate that one of the conditions set out in paragraph 2 is satisfied, having regard, in respect of the condition in point (b) of paragraph 2, to the assessment criteria set out in paragraph 3.

Where the staff member was awarded total remuneration of EUR 1000000 or more in the preceding financial year the appropriate regulator shall only give its prior approval in exceptional circumstances.

Article 5 Calculation of remuneration awarded

(1) For the purposes of this Regulation, remuneration which has been awarded but has not yet been paid shall be valued as at the date of the award without taking into account the application of the discount rate referred to in applicable remuneration rules or reductions in payouts, whether through clawback, malus, or otherwise. All amounts shall be calculated gross and on a full-time equivalent basis.

(1A) In paragraph 1 “applicable remuneration rules” means—

(a) in the case of PRA-authorised persons, rule 15.13 of the Remuneration Part of the PRA rulebook and rule 19D.3.52 of the Senior Management Arrangements, Systems and Controls sourcebook;

(b) in the case of other authorised persons, rule 19A.3.44D of the Senior Management Arrangements, Systems and Controls sourcebook.

(2) For the purpose of the application of points (b) and (c) of Article 4(1), the remuneration awarded may be considered separately for each country where the institution has an establishment and staff shall be assigned to the country where they carry on the predominant part of their activities.

Article 6 Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Signature

01/01/2021 This Regulation shall be binding in its entirety and directly applicable in all Member States.

01/01/2021 Done at Brussels, 4 March 2014.

01/01/2021 *For the Commission*

01/01/2021 *The President*

01/01/2021 José Manuel BARROSO