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Cap on Bankers' Bonuses: More Guidance Issued

European Banking Authority publishes regulatory technical standards for the identification of "material risk takers", reducing the potential impact of the new rules on bonus caps.

The Capital Requirements Directive IV (CRD IV), which contains a new cap on bonuses payable to certain classes of employees within the financial services sector, is due to come into force across the EU from 1 January 2014.[1] It introduces, among other things, a maximum limit for bonus payments of 100% of an affected individual's basic salary. This cap may be raised to 200% of basic salary only if shareholder approval is obtained. Article 94(2) of CRD IV mandates the European Banking Authority (EBA) to prepare draft regulatory technical standards (RTS) on the basis of CRD IV.

Once in force, CRD IV will apply to all bonus payments made to "material risk takers", which commentators initially assumed would, in broad terms, amount to those employees previously identified as "code staff" under the Financial Conduct Authority's Remuneration Code. However, in May 2013, the EBA published a consultation paper in which it sought to significantly widen the class of employees who would be caught by the bonus cap. After receiving negative feedback to the consultation paper, the EBA, on December 16, issued its final draft RTS,[2] which adopt a far narrower approach.

Original Guidance

The original EBA consultation paper suggested that an individual will be considered to be a "material risk taker" for the purposes of CRD IV if the individual meets one of the following criteria:

- The individual's total remuneration exceeds €500,000 per year.
- The individual is part of the 0.3% of staff with the highest remuneration in the institution or firm.
- The individual's remuneration bracket is equal to or greater than the lowest total remuneration of senior management and other risk takers.
- The individual's bonus payments exceed €75,000 or 75% of the fixed component of remuneration.

New Guidance

Under the final draft RTS approved by the EBA's Board of Supervisors, the definition of "material risk taker" has been narrowed significantly. The main changes are as follows:

- The €75,000/75% criterion is removed completely.
- An individual earning up to €750,000 can be excluded from the cap if it is determined by the employer that the individual is not, in fact, taking or managing risks.

1. For more information on the bonus cap rules in CRD IV, see our 24 May 2013 LawFlash, "European Banking Authority Guidance on Financial Services Bonus Cap", available at http://www.morganlewis.com/index.cfm/fuseaction/publication.detail/publicationID/d12e1135-2db7-41fe-9c84-fa0444aa36f7.

2. View EBA's final draft RTS at http://www.eba.europa.eu/documents/10180/526386/EBA-RTS-2013-11+(On+identified+staff).pdf.

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- An individual earning between €750,000 and €1 million can be excluded from the cap if the exclusion is approved by the national regulator (e.g., the Prudential Regulation Authority in the UK).
- An individual earning €1 million or more can be excluded from the cap if the exclusion is approved by the EBA itself.

Impact

This narrower approach may significantly reduce the number of employees who will be caught by the bonus cap, which is the most controversial element of CRD IV. As such, financial institutions will no doubt consider this to be a very welcome development.

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