CLEARY GOTTLIEB Alert Memo

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EU Initiatives Regarding Remuneration Policies for the Financial Services Sector

On April 20, 2009 the Committee of European Banking Supervisors ("CEBS")[1] published its "High-level principles for Remuneration Policies" (the "Principles") for financial institutions.[2] On April 29, 2009, the EU Commission followed with its somewhat more elaborate recommendation regarding the remuneration in the financial services sector (the "Commission Recommendation")[3], which is in substance largely consistent with the Principles. With their respective guidelines, both CEBS and the EU Commission picked up one of the hot topics of financial markets reform, which was recently addressed by, among others, the G20[4], the Financial Stability Forum[5] and The High-Level Group on Financial Supervision in the EU[6].

The Principles are addressed to EU banking and financial services regulators ("Supervisors") and EU banks and financial services companies ("Financial Institutions"). Although they are non-binding in nature and explicitly recognize each Financial Institution's (and, where applicable corporate law so provides, the Financial Institution's shareholders') responsibility for its remuneration policy, the Principles set out certain guidelines that are expected to be implemented by Financial Institutions by the end of the third quarter of 2009, subject to a transitional period where necessary, *e.g.*, to renegotiate existing employment or service agreements. The Commission Recommendation is addressed to the Member States, covering the financial services industry at large, in particular Financial Institutions, insurance companies, pension funds and investment funds as well as other undertakings performing similar business activities, whether regulated or not ("Financial Undertakings"). At present, private equity and hedge fund management companies should not qualify as Financial Undertakings. Like the Principles, the Commission Recommendation is non-binding. It

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1 By way of background, CEBS is a so-called level 3 committee within the Lamfalussy process, a framework for the development of EU-wide legislation for the financial services industry. More specifically, members of CEBS are representatives of the national banking and financial services regulators in the various EU member states, as well as representatives of the European Central Bank and the national central banks in the various EU member states. The main functions of CEBS are (i) providing advice to the European Commission (the "Commission") on the Commission's preparation of EU implementing legislation and (ii) the improvement and harmonization of supervisory practices within the EU.

2 Attached hereto as Annex A.

3 The final text is expected to be published soon under http://ec.europa.eu/internal_market/company/directors-remun/index_en.htm.

4 Action Plan of November 15, 2008; Declaration on Strengthening the Financial System of April 2, 2009.

5 Principles for Sound Compensation Practices of April 2, 2009.

6 Report of February 25, 2009.

is designed to encourage Member States to take the necessary action to promote the implementation of the guidelines set forth therein. The Commission Recommendation also clarifies that each Financial Undertaking's remuneration policy and its compliance with the principles spelled out in the Commission Recommendation should be reviewed and monitored by the relevant Supervisor, taking into account the individual circumstances of each Financial Undertaking.

The EU Commission has already announced that the Commission Recommendation will be followed by European legislation on the supervisory review of remuneration policies. Such legislation, which will be part of the package of modifications of the EU Capital Requirements Directive ("CRD") will introduce, among other things, a binding obligation for Financial Institutions to have in place sound remuneration policies and will subject an Institution's remuneration policy to supervisory review. In this context, the Commission Recommendation will provide guidance to Financial Institutions as to how to comply with such binding obligation and a framework for Supervisors when assessing the remuneration structures of Financial Institutions. As a first step towards the intended modification of the CRD, on April 29, 2009, the EU Commission Services published for consultation a working paper on proposed amendments to the CRD regarding remuneration.[7] According to the working paper, CEBS shall maintain guidelines on sound remuneration policies that support the principles spelled out in the Commission Recommendation. It is unclear whether the Principles published by CEBS already reflect what the working paper asks for or whether CEBS is supposed to come out with further guidance.

The following provides a brief overview of the Principles and the Commission Recommendation. Unless indicated otherwise, the guidelines described below are included in the Principles and the Commission Regulation in similar form. In addition, the overview will point out (in italics), where the Commission Recommendation is different from, goes beyond, or is more specific than, the Principles. Also, you will find comments on some potential practical difficulties in connection with the implementation of the Principles and the Commission Recommendation.

1. Scope

- The Principles and the Commission Recommendation apply to all Financial Institutions and Financial Undertakings, as the case may be, on a stand-alone and a consolidated basis.

  The Commission Recommendation specifically mentions that relevant subsidiary undertakings established in offshore financial centers should be included in the relevant remuneration policy.

  Comment. When looking at the corporate group formed by a Financial Institution or Financial Undertaking together with its consolidated subsidiaries,

[7] Attached hereto as Annex B. - Different from actual proposed legislation, a "working paper" is only an indication of the approach which the Commission may take, but does not represent or pre-empt future formal proposals of the EU Commission.

the broad scope of the Principles and the Commission Recommendation raises the question of whether a group's remuneration policy will also have to cover subsidiaries outside the financial services sector. The Recitals of the Commission Recommendation as well as the FAQ published together with the press release accompanying the Commission Recommendation clearly state that only such group entities "who exercise activities of the financial sector on a professional basis," i.e., not only occasionally or on an ancillary basis, will be covered. Potential issues of group-wide application, which may arise in international groups (involving non-EU entities) due to conflicting local requirements are not addressed in the Principles or the Commission Recommendation.

- The Principles apply to the remuneration policy for all levels of a Financial Institution and all categories of employees (including members of the management body); special attention should be paid to senior employees and other risk-takers and risk-managers.

  By contrast, the Commission Recommendation applies only to the remuneration policy for risk-taking staff, i.e., staff whose activities have an impact on the risk profile of the Financial Institution.

2. Summary of the Principles and Commission Recommendation

- Key objectives of the remuneration policy for Financial Institutions and Financial Undertakings:

  - A Financial Institution's or Financial Undertaking's remuneration policy should align the personal objectives of its relevant employees and senior management with the Institution's or Undertaking's business strategy, objectives, values and long-term interests;

  - The remuneration policy should be consistent with and promote sound risk management and not encourage excessive risk taking;

  - Severance pay or pay upon change of control or the occurrence of similar events should be based upon past performance and avoid rewarding failure;

  - Internal control functions should be adequately compensated, in particular independently of the (performance of) the business units controlled.

    Comment. It is unclear whether the above guideline means that internal control functions must not receive compensation that is affected by the performance of the Financial Institution or Financial Undertaking as a whole. If that was the case, recruiting and retention of talented and qualified personnel for internal control functions might become difficult.

- Transparency requirements:

  - The general principles underlying the remuneration policy should be accessible to all employees to whom they apply; those employees should be informed in advance of the criteria used for the determination of their remuneration;

  - The appraisal process preceding the determination of the compensation should be adequately documented and transparent to the employee concerned;

  - The relevant information on the remuneration policy should be disclosed to external stakeholders (subject to data protection and confidentiality requirements).

    The Commission Recommendation specifies a catalogue of information that should be disclosed, including, inter alia, information on the decision-making process used for determining the remuneration policy (including on the involvement of a remuneration committee and external consultants, if any), sufficient information on the linkage between pay and performance, the criteria used for performance measurement and risk adjustment, the performance criteria relating to variable bonus components and the main parameters and rationale for any annual bonus scheme and any other non-cash benefits.

    <u>Comment</u>. The above guidance on disclosure is so high-level and unspecific that it is very difficult to imagine what kind of disclosure to the public would meet the best practice-standard reflected in the Principles and the Commission Recommendation, as the case may be. Unless disclosure is required otherwise under applicable law, the disclosure of individual pay levels and terms does not seem to be required.

  - The remuneration policy should be memorialized, *e.g.*, in a "remuneration policy statement", and regularly reviewed.

- Decision-making and oversight regarding pay and bonuses

  - The directors on a Financial Institution's or Financial Undertaking's board performing supervisory functions (in a single tier structure) or the Institution's supervisory board (in a dual tier structure) should

    - Decide on the compensation of the Institution's or Undertaking's directors performing management functions or the Institution's or Undertaking's management board, as the case may be,

    - Approve the general principles of an Institution's or Undertaking's overall remuneration policy, and

  - Oversee the application and implementation of the remuneration policy.

- The Principles encourage the delegation of the decision-making and oversight responsibility of the supervisory function of a Financial Institution's or Financial Undertaking's board of directors or a Financial Institution's or Financial Undertaking's supervisory board to a remuneration committee.

  The Commission Recommendation makes reference to a Financial Institution's or Financial Undertaking's remuneration committee, but does not explicitly recommend delegation of remuneration-related responsibilities to a remuneration committee.

- A Financial Institution's or Financial Undertaking's internal control functions, human resources department and, to the extent required by applicable corporate law, shareholders should be involved in the design and operation of the remuneration policy.

• Performance-related remuneration

- Performance measures should include individual and collective (*e.g.*, business unit-, company- and group-related) performance criteria;

- Individual performance measures should be based on financial and non-financial performance criteria (*e.g.*, skills acquired, personal development, compliance with the institution's systems and controls, commitment to the Institution's business strategies and its major policies and contribution to the performance of the team);

- The performance measure used to calculate bonuses or bonus pools should be adjusted for risks (including liquidity risks) and the cost of (economic) capital.

  <u>Comment</u>. It is not entirely clear from the Principles or the Commission Recommendation how such risk adjustment would work, e.g., whether risks taken individually and/or collectively (business unit, company, group) would have to be taken into account and how the adjustment would be calculated.

  The Commission Recommendation is somewhat more explicit in this regard by specifying that adjustments should be made for the current and future risks related to the underlying performance.

- The Principles provide that the remuneration of a Financial Institution's or Financial Undertaking's non-executive directors should not be linked to the Institution's short term results, but take into account the time invested and the responsibilities assumed by each member.

Comment. No such best practice is included in the Commission Recommendation since it covers only risk-takers.

- *Without a parallel provision in the Principles, the Commission Recommendation provides that the performance appraisal should cover a multi-year period to reflect the longer term performance of the relevant employee or executive; similarly, the actual payment of bonuses should be spread over the business cycle of the Institution.*

- Form of remuneration

  - The ratio of fixed component (base pay) and variable component (bonus) should be proportionate – employees should not have to rely on bonuses.

    According to the Commission Recommendation, the remuneration policy should even provide for a maximum percentage of the variable component compared to the total remuneration; the fixed component should represent a sufficiently high percentage of the total remuneration allowing the Institution to operate a fully flexible bonus policy (i.e., allowing the Institution to withhold bonuses entirely or partly if individual or collective performance criteria are not met or if the Institution's situation deteriorates significantly).

    Comment. This concept does not necessarily serve the purpose of promoting sound risk management. If an employee or executive knows he or she gets paid an equal amount, no matter what happens to his or her employer, this may very well result in a drop of personal efforts, commitment and care.

  - Bonuses should not be in the form of pure up-front cash payments but contain a deferred component (*e.g.*, shares, options or other funds held in a trust or similar account) linked to (risk-adjusted) measures of future performance;

    The Commission Recommendation even recommends that the major part of the bonus should be deferred (deferred part to be determined in relation to the total amount of the bonus as compared to the total amount of the remuneration).

    Comment. Neither the Principles nor the Commission Recommendation specify a minimum deferment period. In Germany, for example, a draft bill regarding the compensation of management board members in general (i.e., not limited to the financial sector) proposes a minimum holding (i.e., vesting) period for stock options of four years (current law provides for a two-year holding period).

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- Under the Principles the remuneration policy should provide for the claw back of any up-front bonus payment should it later turn out to have resulted from fraud.

  Under the Commission Recommendation the remuneration policy should provide for a claw back in any situation where a bonus has been awarded for performance based on data which has subsequently proven to be inaccurate.

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If you have any questions in connection with this Alert Memorandum, please feel free to contact any of your regular contacts at the firm.

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High-level principles for Remuneration Policies

Introduction

1. The recent market turbulence has, amongst other things, highlighted the risks inherent in institutions having inadequate remuneration policies and structures. The absence of a coherent and adequate remuneration policy generates potential risks for a financial institution that need to be adequately analysed and contained. The following list of principles aims to address the most critical aspects to a well functioning remuneration policy, while recognising that the responsibility for the policy rests ultimately with the institution itself and, where applicable, the shareholders. The principles should be applied by all those institutions within the remit of CEBS and implemented before the end of Q3 2009.Institutions may allow for a transitional period following implementation, e.g. in order to take the necessary steps to renegotiate existing contracts.

Scope

2. In line with the CEBS's internal governance work, the guidelines are addressed both to regulators and regulated institutions. Within the institutions, the guidelines are intended to cover the entirety of the remuneration policy, including members of the management body, with special emphasis on senior employees and other risk-takers and risk-managers in the institution. The remuneration policy should include all levels of the organisation and all categories of employees.

3. The implementation of these guidelines and thus the exact form of an institution's remuneration policy should take account of its nature and scale and the complexity of its activities. The principles should be applied both at solo and group levels and be implemented in a proportionate way.

4. Further consideration will be given to how the supervisory review and evaluation process (SREP), which includes an assessment of all risks to an institution, can address those risks emanating from the remuneration policy. Within this process supervisors will consider the range of measures available under Pillar 2 to address and mitigate these risks.

5. The set of principles is as follows:

General

i. ***The financial institution should adopt an overall remuneration policy that is in line with its business strategy and risk tolerance, objectives, values and long-term interests. It should not encourage excessive risk-taking. The remuneration policy should cover the institution as a whole and contain specific arrangements that take into account the respective roles of senior management, risk takers and control functions. Control functions should be adequately rewarded to attract skilled individuals.***

This principle is aimed at a key objective of an institution's remuneration policy: any policy should aim at aligning personal and company objectives with a view to the long-term. This must include the overall business strategy as well as other company values such as compliance culture, ethics, behaviour towards customers, measures to mitigate conflicts of interest, etc.. This also implies that remuneration policies should not encourage excessive risk taking. An institution should not reward individuals for taking risks in excess of the institution's risk tolerance and at all times give due consideration to the longer term.

Control functions (such as Risk Control, Compliance and Internal Audit) should be adequately compensated in accordance with their own objectives and not in relation to the performance of the business units they control.

Severance pay or pay related to other scenarios such as mergers and acquisitions should be related to performance achieved over time and be designed in such a way as not to reward failure.

ii. ***The remuneration policy should be transparent internally and adequately disclosed externally.***

The remuneration policy should be accessible to all employees. The employees should know in advance the criteria that will be used to determine their remuneration. The appraisal process should be properly documented and transparent to the employee concerned.

Whilst respecting confidentiality, relevant information on the remuneration policy should be disclosed in a clear and easily understandable way to external stakeholders.[1]

An institution should be able to clearly articulate its remuneration policy to its supervisory authority upon request. This could, for example, take the form of a remuneration policy statement which is subject to regular review.

[1] In particular, listed companies should apply the European Commission's Recommendation on 'fostering an appropriate regime for the remuneration of directors of listed companies' - http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:385:0055:0059:EN:PDF

GOVERNANCE

iii. The management body, in its supervisory function, should determine the remuneration of the management body in its management function[2]. In addition the management body, in its supervisory function, should approve the principles of the overall remuneration policy of the institution and maintain oversight of their application. The implementation of the remuneration policy should be subject to central and independent review.

This principle addresses an institution's oversight and decision-making regarding pay and bonuses.

Ultimate oversight of the remuneration policy should rest with the institution's management body (supervisory function). One way of achieving this could be by setting up an independent Remuneration Committee or other relevant committees which report to the management body (supervisory function).

Centralised decision-making bodies will be better able to align individual remuneration packages with the company's overall performance.

Any policy should be subject to regular (at least annual) and independent internal review, with specific attention to preventing incentives for excessive risk taking and other adverse behaviours.

In addition to the management body's general responsibility for overall remuneration and its review, adequate involvement of the following is required:

- Control functions (such as Risk Control, Compliance and Internal Audit);
- Human Resources; and
- the shareholders, where applicable.

A commercial business unit should not be able to determine the remuneration of its control functions as this would create a potential conflict of interest.

MEASUREMENT OF PERFORMANCE AS A BASIS FOR REMUNERATION

iv. Where the pay award is performance related, remuneration should be based on a combination of individual and collective performance. When defining individual performance, factors apart from financial performance should be considered. The

[2] For a definition of the management board in either its supervisory or management capacity, please refer to the definition provided on page 6 of GL03. The definition is designed to address both single and dual tier structures within the EU.

measurement of performance, as a basis for bonus awards, should include adjustments for risks and the cost of capital.

This principle targets the measurement of performance as the basis for the awarding of pay and bonuses. This may not be applicable to all categories of employees. The measurement of employees' performances is central to a good remuneration policy. Defining the pay award should not be a purely mechanical process based on measurable performance criteria, but should include the ability to exercise judgement.

Any performance measure should include variables relating to individual as well as collective performance (for example business unit, company and group performance). While the overall company and/or group performance is important, this does not mean that remuneration policies cannot vary in nature depending on the business unit to reflect the objectives of the specific area.

For individual performance measurement, while financial criteria may be one dimension in determining performance, other non-financial factors should also be considered such as skills acquired, personal development, compliance with the institution's systems and controls, commitment to the business strategies and its major policies and contribution to the performance of the team. Where it is appropriate, poor performance in the non-financial variables should override good performance in terms of profit generation, i.e. unethical or non-compliant behaviour cannot be compensated for by good financial performance.

Bonuses or bonus pools should be calculated using a measure of performance which is adjusted for risks (including liquidity risk) and the cost of capital. Where possible, this should be based on an institution's economic capital model. The aim of such an adjustment is to ensure that the longer term interests of the institution or group are fully taken into account, such as the sustainable growth and profitability prospects of the institution.

The remuneration of non-executive directors should not be linked to the financial institution's short term results, but take into account other factors, such as the time invested and their respective responsibilities.

FORM OF REMUNERATION

v. ***There should be a proportionate ratio between base pay and bonus. Where a significant bonus is paid, the bonus should not be a pure up-front cash payment but contain a flexible, deferred component; it should consider the risk horizon of the underlying performance.***

The relation between base pay and bonus should be of reasonable proportion. Employees should not have to rely on bonuses.

This principle addresses the form of the pay-out. Whilst cash pay awards may be appropriate for base pay, when bonus payments are of significant size the award should at least include a deferred component (for example company shares, options or other funds held in a trust or similar account) to take into consideration the risk horizon of the underlying performance. The deferred payment should therefore be linked to measures of future performance within a reasonable time horizon. In such a situation, it is desirable that these measures are risk adjusted as set out in principle (iv).

Big bonuses should not be awarded purely in up-front cash.

Whilst taking into account all legal and fiscal constraints, any up-front bonus payment should be subject to claw back if it is later established that it resulted from fraudulent activities.

Important note:

This document is a working document of the Commission services for consultation.

It does not purport to represent or pre-judge the formal proposals of the Commission.

You are invited to comment on the proposals in this paper. The proposals are only an indication of the approach the European Commission may take and do not represent the Commission's final policy position.

As well as expressing your views on the specific proposals, we also ask you to respond to the following questions:

- To what extent do your existing remuneration policies comply with the requirements of the proposals?
- To the extent that they are not compliant with the proposals, please indicate in which areas will you need to modify your policies to bring them in line with the proposals;
- Please indicate whether, and to what extent, modification of your policies will imply incurring additional costs. Please distinguish between one-off and recurrent costs.

While responding to the above, please do not take into account any savings, direct or indirect, with regard to the remunerations themselves, however substantial they may be.

This consultation will run for one week from Wednesday the 29th of April until the 6th of May. Please provide your responses to markt-h1@ec.europa.eu

Remuneration Policies

Recitals

● Excessive and imprudent risk-taking in the banking sector has led to the failure of individual financial institutions and systemic problems in Member States and globally. While the causes of such risk-taking are many and complex, there is agreement by supervisors and regulatory bodies, including the G20 and the Committee of European Banking Supervisors, that inappropriate remuneration structures have been a contributory factor. Poorly designed remuneration policies that reward short-term profit and give incentives to take risks that exceed the general level of risk tolerated by the institution can undermine sound and effective risk management and exacerbate excessive risk-taking behaviour.

● Directive 2006/48/EC requires credit institutions to have arrangements, strategies, processes and mechanisms to manage the risks to which they are exposed, and Directive 2004/39/EC imposes similar requirements relating to internal control in investment firms. Directive 2006/48/EC requires competent authorities to review those internal arrangements, strategies, processes and mechanisms, and to determine whether the own funds held by the credit institution or investment firm ensure a sound management and coverage of the risks to which the institution or firm is or might be exposed ('Pillar 2 supervisory review'). That supervision is carried out on a consolidated basis in relation to banking groups, and includes financial holding companies and affiliated financial institutions in all jurisdictions. In appropriate cases where the internal arrangements adopted by credit institutions and investment firms do not meet the relevant requirements on a consolidated basis, competent authorities must require the relevant entities to take measures to rectify the deficiency. Those measures include obliging the credit institution or investment firm to hold own funds in excess of the minimum level required under Article 75 of Directive 2006/48/EC.

● In order to address the potentially detrimental effect of poorly designed remuneration structures on the sound management of risk and control of risk-taking behaviour by individuals, the requirements of Directive 2006/48/EC and Directive 2004/39/EC mentioned above should be supplemented by an express obligation for credit institutions and investment firms to establish and maintain remuneration polices and practices that are consistent with effective risk management. Member States should ensure that when drawing up and implementing their remuneration policies, credit institutions and investment firms take into account the principles on sound remuneration policies set out in the Commission Recommendation of […] on remuneration policies in the financial services sector.

● In order to ensure effective supervisory oversight of the risks posed by inappropriate remuneration structures, the remuneration polices and practices adopted by credit institutions and investment firms should be included in the scope of the Pillar 2 supervisory review. In reviewing remuneration policies and practices and assessing their potential impact on risk management, competent authorities should have due regard to the general principles on sound remuneration policies set out in Commission Recommendation of […] on remuneration policies in the financial services sector, on which guidelines to be published by the Committee of European Banking Supervisors should be based.

● Because poorly designed remuneration policies and incentive schemes are capable of increasing the risks to which credit institutions and investment firms are exposed, it is appropriate that competent authorities should impose measures on the relevant entities that are designed to address problems that have been identified in relation to remuneration policies in the Pillar 2 supervisory review. Those measures should include a requirement to hold additional own funds in appropriate cases. Competent authorities should also be able to impose financial or non-financial penalties on credit institutions and investment firms that have remuneration policies that are not consistent with sound and effective risk management.

● In order to ensure fast and effective enforcement, competent authorities should also have the power to impose either financial or non-financial penalties for any breach of a requirement under Directive 2006/48/EC, and the penalties available should be effective, proportionate and dissuasive. Divergent levels of financial penalties across Member States may undermine the effectiveness of enforcement. Accordingly, the Commission should have the power to adopt technical implementing measures, in accordance with the regulatory procedure, to specify minimum levels of financial penalties if this is necessary to ensure a properly effective and dissuasive sanctions regime.

Amendments to Directive 2006/48/EC

[Article 22

Changes to paragraph 1.

Home Member State competent authorities shall require that every credit institution have robust governance arrangements, which include a clear organisational structure with well-defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks it is or might be exposed to, ~~and~~ adequate internal control mechanisms, including sound administration and accounting procedures, and remuneration polices and practices that are consistent with and promote sound and effective risk management.

Article 54

The existing text of Article 54 is numbered paragraph 1.

Insert new paragraph 2

2. Member States shall ensure that, for the purposes of paragraph 1, their respective competent authorities have the power to impose both financial and non-financial penalties, which must be effective, proportionate and dissuasive.

Article 136

Insert new paragraph 3

3. When determining the appropriate level of own funds under Section 1 of Chapter 2 in the supervisory review process under Article 124 to cover all the risks to which a credit institution might be exposed, and in order to assess whether any imposition of a specific own funds requirement in excess of the minimum level is required under paragraph 2 of this Article, competent authorities shall take into account both the quantitative and qualitative aspects of

credit institutions' internal capital assessment under Article 123 and credit institutions' arrangements, processes, mechanisms and strategies under Article 22 and 123.

Article 150

In paragraph 2, insert new sub-paragraph (g)

(g) specification of minimum levels of financial penalties provided for in Article 54;

Annex V

New section 11

11. Risk arising in connection with remuneration policies

16. When establishing and applying their remuneration policies, credit institutions shall comply with the following principles in a way that is appropriate to their size, internal organisation and the nature and scope or their activities:

    - The remuneration policy is designed so as not to encourage risk-taking that exceeds the level of tolerated risk of the credit institution, is consistent with and promotes sound and effective risk management and does not have an adverse effect on the long-term interests of the credit institution.

    - The remuneration policy and its application are subject to oversight by the management body (supervisory function) of the credit institution, and to regular independent internal review with a view to assessing that it does not encourage imprudent risk-taking, create conflicts of interest, or otherwise undermine sound and effective risk management.

    - Remuneration of individuals engaged in control functions is based on the achievement of objectives linked to their functions, and is determined independently of the performance of the business areas they control or oversee.

    - The measurement of performance used to calculate bonuses or bonus pools includes an adjustment for current and future risks and takes into account the cost of the capital employed and the liquidity required.

    - Fixed and variable components of remuneration should be appropriately balanced so that the fixed component represents a sufficiently high proportion of the total remuneration to allow the credit institution to operate a fully flexible bonus policy, with the ability to pay no bonus if appropriate.

    - Payment of the major part of a significant bonus, irrespective of the form in which it is to be paid, is deferred for a period which is appropriate for the nature of the business in which the individual is engaged and its risks.

- Payment of the deferred part is linked to the future performance of the firm and, to the extent practicable, to the performance of the division or business unit of the individual.

- Where remuneration is performance related, its total amount is based on a combination of the assessment of the performance of the individual and of the business unit concerned and of the overall results of the credit institution.

- The assessment of individual performance takes into account non-financial criteria such as compliance with internal rules and procedures, and compliance with the standards governing the relationship with clients.

17. The Committee of European Banking Supervisors shall maintain guidelines on sound remuneration policies that support the principles set out in paragraph 16.