



BANK OF ENGLAND
PRUDENTIAL REGULATION
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Policy Statement | PRA PS12/15
| FCA PS15/16

Strengthening the alignment of risk and reward: new remuneration rules

June 2015

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This policy statement contains the final rules and guidance to implement the proposals made in Consultation Paper PRA CP15/14 FCA CP14/14 in relation to remuneration.

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1 Introduction

Background

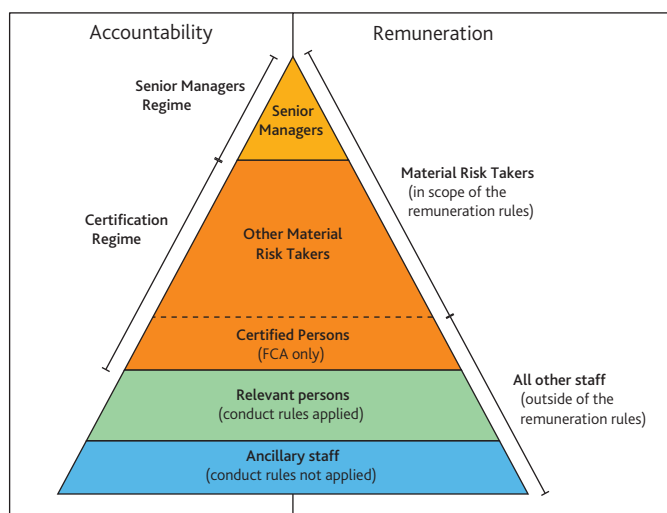
1.1 This policy statement includes feedback, final rules, and guidance in relation to proposals under the Consultation Paper (CP) 15/14 'Strengthening the alignment of risk and reward: new remuneration rules'⁽¹⁾ published jointly by the Prudential Regulatory Authority (PRA) and the Financial Conduct Authority (FCA). The consultation proposed changes to existing remuneration requirements and considered options to implement the remuneration recommendations of the Parliamentary Commission on Banking Standards (PCBS) report '*Changing banking for good*'.⁽²⁾

1.2 Whilst significant progress has been made on reforming the structure of remuneration in the financial services sector, the PRA and the FCA take the view that more should be done to discourage excessive risk-taking and short-termism and to encourage more effective risk management. The proposals on which we consulted therefore sought to build on the existing remuneration framework and further align risk and reward in the banking sector. The policy options were developed with the aim of furthering the PRA statutory objective to improve the safety and soundness of firms and the resilience of the financial system and supporting the FCA statutory objectives regarding consumer protection and market integrity.

Application

1.3 The changes to the PRA Rulebook and the FCA Handbook apply to banks, building societies and PRA-designated investment firms, including UK branches of non-EEA headquartered firms. These rules apply to all Material Risk Takers (MRTs)⁽³⁾ at these firms, including Senior Managers designated under the Senior Managers Regime (SMR) from 2016. The interaction between remuneration and the SMR is illustrated in Figure 1.⁽⁴⁾

Figure 1 Interrelationship between remuneration and accountability



1.4 The final provisions on clawback (staff member agrees to return ownership of an amount of remuneration to the institution under certain circumstances) and deferral (period during which variable remuneration is withheld following the end of the accrual period) will apply to variable remuneration awarded for performance periods beginning on or after 1 January 2016. The rest of the requirements will apply from 1 July 2015.

The PRA Rulebook

1.5 The Remuneration Part added to the PRA Rulebook, including the previous remuneration reporting requirements, is in Annex 1, together with a related instrument making consequential amendments to the PRA Handbook and repealing SYSC 19A from the PRA Handbook. There are minor changes to the rule on the bonus cap which was consulted on to ensure that it more closely reflects Capital Requirement Directive (CRD) wording. However these changes do not in any way change the policy meaning. The accompanying supervisory statement, which clarifies PRA expectations of firms in relation to the PRA Rulebook, is in Annex 2.

1.6 These documents should be read in conjunction with existing supervisory statements LSS8/13 'Remuneration standards: the application of proportionality'⁽⁵⁾ and SS2/13 'PRA expectations regarding the application of malus to variable remuneration',⁽⁶⁾ both of which have been amended to reflect consequential changes arising from the move to the PRA Rulebook.

The FCA Handbook

1.7 The FCA instrument '*Senior Management Arrangements, Systems and Controls (Remuneration Code) (No 6) Instrument 2015*' is included in Annex 3. The instrument:

- (i) creates a new chapter SYSC 19D which contains the dual-regulated firms' Remuneration Code;

- (1) PRA Consultation Paper CP15/14: 'Strengthening the alignment of risk and reward: new remuneration rules', July 2014; www.bankofengland.co.uk/pr/Pages/publications/cp/2014/cp1514.aspx, FCA Consultation Paper CP14/14, July 2014; www.fca.org.uk/your-fca/documents/consultation-papers/cp14-14.
- (2) www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf.
- (3) Material Risk Takers as identified in the Capital Requirements Directive (CRD) article 92(2) and Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers).
- (4) The PRA recognises that the definition of MRT in the Remuneration Rules in Annex 1 differs slightly from the criteria used in defining a 'significant risk taker' in the Certification rules published in PS3/15 in March 2015. Having previously made clear that its intention is to align the scope of the Certification Regime as closely as possible with the MRT population, the PRA intends to consult on amending the definition of a significant risk taker in the Certification rules to include any employee whose professional activities have a material impact on the firm's risk profile, including any employee who is deemed to have a material impact on the firm's risk profile in accordance with criteria set out in Articles 3 to 5 of the Material Risk Takers Regulation.
- (5) 'Remuneration standards: the application of proportionality' — LSS8/13; www.bankofengland.co.uk/pr/Pages/publications/ss/2015/lss813update.aspx.
- (6) PRA expectations regarding the application of malus to variable remuneration — SS2/13; www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss213update.aspx.

- (ii) makes amendments to the Glossary of definitions to the existing SYSC 19A which will become the Remuneration Code for IFPRU investment firms, and to the supervision manual (SUP); and
- (iii) makes changes (identical to those by the PRA) to the rule on the bonus cap which was consulted on to ensure that it more closely reflects CRD wording. These changes do not in any way change the policy meaning.

1.8 The FCA rules on deferral (SYSC 19D.3.59R) and clawback (SYSC 19D.3.61R) use a term 'PRA-designated senior management function'⁽¹⁾ when they refer to MRTs that perform such a function. This term will be defined in rules on accountability that the FCA expects to make later in the year but well in advance of when the deferral and clawback provisions will apply to such MRTs. Under SYSC 19D.1.3R(3), these requirements will apply to those MRTs in relation to variable remuneration awarded for performance periods beginning on or after 1 January 2016.

1.9 The FCA also consulted on new general guidance on proportionality which has been created for dual regulated firms (SYSC 19D in the FCA Handbook) and amendments were also made to two pieces of existing proportionality guidance under SYSC 19A and SYSC 19C of the FCA Handbook. Only a few responses were received, all of which were positive. These three pieces of non-Handbook general guidance will be maintained on the FCA website and are presented in Annex 4.

1.10 The FCA is also issuing non-Handbook guidance on the application of malus to variable remuneration and *ex-post* risk adjustment. This was subject to consultation in FCA CP14/14 and to a second consultation which closed on 7 May 2015.⁽²⁾ The second consultation proposed amendments to the previous guidance as consulted on in July 2014 to share the latest good practice observed in the 2014 remuneration round and to clarify the FCA's expectations on how relevant firms meet the Remuneration Code requirements on *ex-post* risk adjustment. This guidance has effect from 1 July 2015. The FCA response to feedback and its final guidance is included in Annex 5.

2 Consultation feedback and final proposals

2.1 The PRA and FCA received 32 responses to the consultation (main proposals set out in Box 1). The following section summarises key issues raised in those responses and sets out final policy proposals.

Deferral length

2.2 Deferral periods which lengthen the time between the award of variable remuneration and vesting with an individual, combined with malus whereby unvested awards are cancelled

or reduced, are key tools for aligning incentives. In order to ensure effective risk management, the deferral period should reflect the timeframe during which risks are likely to crystallise and the results of poor performance, poor risk management or misconduct come to light.

2.3 The PCBS proposed no single period, and recognised the need for flexibility, but did propose that PRA and FCA rules should include 'a new power for the regulators to require that a substantial part of (variable) remuneration is deferred for up to ten years, where it is necessary for effective long-term risk management'.⁽³⁾ In their responses, both the PRA and FCA noted they already had the power to require extended deferral where necessary for these purposes.

2.4 The PRA and FCA agreed that deferral periods should generally be longer than current minima for certain categories of staff in order to better align the vesting of awards with the real risk horizons of the business, the longer-term safety and soundness of the firm and the consumer impacts of the firm's conduct. The proposals drew a distinction between those senior executives who collectively determine the overall business strategy of a firm or take ultimate responsibility for risk management and the wider population of MRTs.

2.5 The PRA and FCA proposed two levels of deferral:

- extended deferral periods for Senior Managers as defined under the SMR to no less than seven years, with vesting no faster than on a pro rata basis from the third anniversary of the award; and
- extended deferral periods for all other MRTs to five years, with pro rata vesting from the first anniversary of the award.

2.6 The majority of respondents commented on the deferral proposals. Industry responses generally recognised the principle of further aligning incentives with the business cycle by extending minimum deferral periods but questioned whether our proposals went too far, particularly given that the proposed deferral periods went beyond minimum EU requirements under CRD. Firms also suggested that extended deferral periods could have a limited impact on the risk-taking behaviour of staff due to employees

(1) In the current FCA draft 'PRA-designated senior management function' is 'a PRA controlled function that is a designated senior management function'. The PRA uses a similar definition, the 'PRA senior management function' which it made in PRA PS3/15. See Annex A of PS3/15; www.bankofengland.co.uk/pradocuments/publications/ps/2015/ps315.pdf.

(2) FCA GC15/2 General guidance on the application of *ex-post* risk adjustment to variable remuneration www.fca.org.uk/your-fca/documents/guidance-consultations/gc15-02. Also, the European Banking Authority (EBA) recently consulted on guidelines on sound remuneration policies in EBA/CP/2015/03 which explain how the remuneration provisions of CRD IV should be applied by competent authorities. Once finalised, these guidelines may lead to consequential changes in the FCA's approach that affect the extent to which firms in SYSC 19D are required to apply this guidance.

(3) www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf.

Box 1

Consultation proposals (July 2014)

Deferral

- To increase deferral periods applied to variable remuneration awarded to PRA-designated Senior Managers to seven years, with payment (vesting) of the award in equal tranches from year three.
- To extend the deferral period applied to variable remuneration awarded to all other MRTs to five years, vesting in equal tranches from year one.

Clawback

- FCA to introduce a rule on recovering variable remuneration already paid to MRTs (clawback) for a period of seven years from date of award, in line with existing PRA rules.
- The FCA and PRA to introduce a rule to extend the seven-year clawback period to ten years for PRA-designated Senior Managers only, if the firm has been notified of a regulatory investigation or commenced an internal investigation which is likely to lead to the need for adjustments to remuneration.

Bailed-out banks

- To strengthen an existing rule that the presumption against payment of variable remuneration extends to all discretionary payments, including loss of office and discretionary pension payments.

Buy-outs

To seek views on a number of options for addressing issues relating to bought-out awards:

- approach one: ban buy-outs;
- approach two: require firms to maintain unvested awards in the event that an employee leaves;
- approach three: apply malus (reducing or cancelling unvested variable remuneration) to buy-outs; and
- approach four: rely on clawback rules.

Risk-adjustment (PRA only)

- To require all UK-regulated firms excluding branches to calculate profits for the purpose of determining the size of annual bonus pools by adjusting the fair value accounting profit figure by the incremental year-on-year change in the prudent valuation adjustment (PVA) figure.
- To require firms not to rely on simple revenue-based measures such as return on equity, earnings per share and total shareholder return when determining variable remuneration at aggregate or individual level, except as part of a balanced and risk-adjusted scorecard.

Remuneration of non-executive directors

- To introduce an explicit requirement that non-executive directors (NEDs) should not receive variable remuneration in respect of activity carried out in their roles as non-executives.

psychologically discounting the deferred amount and the firm compensating for this with increases in fixed pay, which was an issue highlighted in our original consultation. The impact of extended deferral as a tool for aligning incentives was further questioned in relation to more junior MRTs or those awarded lower variable remuneration.

2.7 The former members of the PCBS, on the other hand, published a statement⁽¹⁾ in November welcoming the consultation proposals but suggesting that the deferral periods 'are still not as long as may be necessary in some cases' and went on to propose that 'the regulators should consider lengthening their proposed deferral periods.'

2.8 The PRA and FCA have considered the responses and issues raised. In general these issues had been taken into account in formulating the original proposals. The PRA and FCA recognise that the proposed deferral periods exceed the minimum requirements under CRD but take the view that the longer deferral periods for certain categories of staff are justified by the need to improve the alignment of risk and

reward. Similarly, as highlighted in the original CP, the PRA and FCA are familiar with the argument that longer deferral periods could lead to variable awards being less valued or discounted by staff and that this may result in a greater reliance on fixed remuneration. However, the PRA and FCA would not welcome any further increase in fixed remuneration and consider that it is important to balance this argument against the need to extend risk horizons, particularly for more senior risk-takers.

Deferral scope

2.9 The PRA and FCA also received substantive feedback regarding the scope of the proposals. Respondents commented that, in seeking to apply the increased deferral periods to all MRTs, the PRA and FCA were failing to take account of the breadth of the MRT population, which had substantially expanded this year following the application of a European Banking Authority (EBA) regulatory technical

(1) www.parliament.uk/documents/commons-committees/treasury/Statement_by_former_Members_of_PCBS.pdf.

standard (RTS) on the identification of staff with a material impact on the risk profile of a firm.⁽¹⁾ This significant increase in the population of MRTs was also observed in supervisory evidence gathered by the PRA and FCA after the consultation.

2.10 The PRA and FCA are therefore persuaded that it would be disproportionate to apply five-year deferral to all MRTs below Senior Manager, particularly for those with relatively junior roles and limited authority to commit the firm to risk. However, given the population of firms to which the rules apply and the existing approach to proportionality, the PRA maintains that five-year deferral is appropriate for those MRTs with senior, managerial or supervisory roles.

2.11 The PRA therefore proposes to draw a distinction between risk managers at PRA-regulated firms and all other MRTs, using the qualitative criteria of the EBA RTS as summarised at **Table A** below. Under this approach, senior managers who retain the greatest influence over the strategic direction of the business will be subject to the seven-year deferral requirement and those with responsibility for managing or supervising risk-taking or significant risk functions will be subject to the five-year deferral requirement. All other MRTs, who are subject to a greater degree of management oversight, will remain subject to the CRD minimum deferral period of three to five years.⁽²⁾

Table A Deferral requirements at PRA-regulated firms

Category	Definition	Deferral period
Senior Managers		
	<i>As per SMR</i>	Seven years
Risk Managers, excluding those covered by the SMR		
Members of the management body	Articles 3(1)–(3)	Five years
Risk managers and direct reports, except those identified solely due to committee membership	Articles 3(4)–(5) Article 3(7) Article 3(10)	
Heads of material business units and their direct reports	Article 3(6) Article 3(8)	
Heads of functions	Article 3(9)	
Managers of risk-taking MRTs	Article 3(13) Article 3(15)	
All other MRTs		
Individual exposing firm to credit risk	Article 3(11)	Three to five years
Individual exposing firm to trading book/market risk	Article 3(12)	
Individual approving introduction of new products	Article 3(14)	
Individual on local risk committee	Article 3(10)	
MRTs identified solely under quantitative criteria if subject to managerial oversight	Article 4(1)	

2.12 This approach will ensure a greater alignment of incentives and accountability of those individuals responsible for strategic decision-making and the supervision of risk-taking staff. With regard to the wider population, it is important to

note that all MRTs remain subject to clawback for seven years from the date of award, which will ensure the accountability of both risk managers and all other MRTs across the seven-year period.

2.13 In terms of impact, the population to which extended five-year deferral is applied remains similar in absolute terms to our original proposal. In addition, affected firms are already required to apply the qualitative criteria of the EBA RTS to identify relevant staff, and we therefore expect minimal incremental costs on firms as a result of the requirement to identify risk managers. As a result, the affected population and compliance costs remain in line with those on which we consulted and the impacts set out in the original cost-benefit analysis remain appropriate.

2.14 Given their greater seniority and responsibility, the FCA will also require that firms apply deferral periods of no less than seven years to the variable remuneration of senior managers.

2.15 The FCA will maintain the CRD minimum deferral period for MRTs who are not senior managers. This is partly to ensure consistency for these staff in FCA solo-regulated firms. It is also because the risk manager category is based on EBA RTS criteria that are largely prudentially based, tailoring it to the identification of staff whose actions present greater prudential rather than conduct risk.

2.16 The PRA and FCA deferral requirements for each tier of MRTs are set out in Box 2.

Clawback

2.17 The PRA introduced a rule from 1 January 2015 requiring firms to apply clawback (reclaiming vested awards) in instances of misconduct or failures in risk management up to seven years from the date of a variable remuneration award. The FCA announced in the consultation paper its intention to introduce a comparable rule. There was general consensus in consultation responses that the FCA should align with the PRA on this rule, and the FCA will therefore introduce a rule to require a minimum clawback period for all MRTs of seven years from the date of award.

2.18 The PRA and FCA also consulted on a rule that the seven-year clawback period should have the possibility of extension to ten years for PRA-designated Senior Managers where either:

- a firm has commenced its own internal inquiry into a possible material failure which could potentially lead to the application of clawback; or

(1) EBA RTS on MRTs www.eba.europa.eu/documents/10180/526386/EBA-RTS-2013-11+%28On+identified+staff%29.pdf/c313a671-269b-45be-a748-29e1c772ee0e.

(2) Art.94(m) CRD requires variable remuneration to be 'deferred over a period which is not less than three to five years'.

Box 2

Summary of deferral requirements

- **Senior Managers** as defined under the SMR must apply deferral periods of no less than **seven years** to variable remuneration awards, with no vesting prior to the third anniversary of award, and vesting no faster than on a *pro rata* basis. (*PRA and FCA requirement*)
- **Risk managers at PRA-regulated firms** as set out in **Table A** must apply deferral periods of no less than **five years** to

variable remuneration awards, with vesting no faster than *pro rata* from year one. (*PRA requirement*)

- **All other MRTs** must apply at least three years by applying the CRD deferral requirements of no less than **three to five years** to variable remuneration awards, with vesting no faster than *pro rata* from year one. (*PRA and FCA requirement*)

- a firm has been notified by a regulatory authority (including an overseas authority) that an investigation has been commenced which the firm considers could lead to the application of clawback.

2.19 A majority of responses disagreed with the proposal to extend the period during which variable remuneration is subject to clawback to ten years where an investigation is ongoing. Concerns cited related to discounting of rewards, complexities in application, implementation, and enforcement of the clawback period. There were also concerns regarding the impact on competitiveness and potential difficulty in attracting talented staff to senior positions.

2.20 In considering these responses, the PRA and FCA note that the original proposal for a clawback period of seven years for Senior Managers balanced the time horizon over which the risks inherent in major business decisions might be expected to crystallise against the tendency for individuals to discount the value of long-term delayed vesting and reduce the effect on incentives. Without an extension, the effective clawback period would be seven years less the time taken to carry out an investigation, making implementation and enforcement more difficult and so weakening its incentivising effects.

2.21 The PRA and FCA are therefore implementing rules to extend the clawback period by up to three years on top of the seven years for PRA-designated Senior Managers where there are outstanding internal or regulatory investigations at the end of the normal seven-year clawback period.

Bailed-out banks

2.22 The PCBS also considered remuneration awarded to individuals at a bank in receipt of taxpayer support. In particular, the PCBS recommended that the regulator should have discretion to render void or cancel deferred compensation, entitlements to payments for loss of office, change or control or unvested pension rights.⁽¹⁾

2.23 The PRA and FCA acknowledged the important public policy and regulatory interest in avoiding instances where

individuals are effectively rewarded for failure through the payment of discretionary awards despite the need for government intervention. In line with EU requirements under CRD, the PRA and FCA have already implemented a rule that no variable remuneration should be paid to the management body of a firm in receipt of exceptional government intervention unless justified. We therefore proposed to build on this rule by making explicit that the presumption against payment or vesting extends to all discretionary payments, including payment for loss of office and discretionary pension benefits.

2.24 Most consultation responses agreed with this presumption and the PRA and FCA therefore propose to implement the rule as described in the consultation. However, clarification was sought on some of the detailed definitions and implementation of the proposal.

2.25 In considering implementation issues, the PRA and FCA makes clear that this rule will apply to any firm which receives exceptional government intervention, whether in the form of direct support or a guarantee. The rule will apply from the commencement of the rules and will not apply to firms as a consequence of such interventions that have happened in the past, even if elements of that support are still in place. The rule will also not apply to any firm which avails itself of emergency liquidity assistance.

Buy-outs

2.26 Under the consultation, the PRA and the FCA discussed the widespread practice of buy-outs, whereby a firm compensates a new employee for any unvested remuneration that is cancelled when they leave their previous firm. Whilst this practice can be used by firms as a tool to overcome the retention effect that deferral of remuneration has on staff, it removes the ability of the previous firm to apply malus to the outstanding deferred award should misconduct come to light after an individual switches employer. As such, it is possible

(1) www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf.

that the individual may avoid full accountability for their actions, undermining the beneficial incentives that deferral and malus are designed to deliver.

2.27 However, as we acknowledged, the options for tackling the impact of buyouts pose a number of practical difficulties. We sought views on four broad options:

- approach one: ban buyouts;
- approach two: require firms to maintain unvested awards in the event that an employee leaves;
- approach three: require buyouts awards to be held in a form that permitted them to be subject to malus by the previous employer;
- approach four: rely on clawback rules.

2.28 Respondents generally argued against options one and two, which were regarded as posing insurmountable practical difficulties and/or exposing firms to disproportionate disadvantages in terms of competition with firms outside the scope of the rules in the absence of concerted international action. Some respondents favoured a form of escrow account in line with option three. However, the majority considered that the practical difficulties of implementing options two and three suggested we should rely solely on clawback as under option four.

2.29 Given the support for exploring option three further, the PRA and FCA will consider whether more detailed proposals for option three should be brought forward. In parallel, we will seek to ensure that clawback arrangements at firms are robust.

Risk adjustment (PRA only)

2.30 The PRA consulted on a proposal for UK-incorporated regulated firms to calculate profit for the purposes of awarding remuneration on the basis of prudent valuation principles in order to exclude unrealised profits from thinly traded or illiquid markets from being counted as profit to determine remuneration. It was proposed that firms retained the ability to make further adjustments to this preliminary pool figure based on risk adjustment metrics or discretionary factors.

2.31 Responses to the consultation recognised the need to introduce greater transparency into the methodology for deriving the pre-risk adjusted bonus pool from profit and/or revenue. It was widely accepted that prudent valuation was an appropriate way of achieving greater transparency, provided that remuneration committees retained overall discretion for setting the final pool. However, clarity was requested on the mechanics of the adjustment and this is reflected in the final rule and supervisory statement.

2.32 In terms of application, all UK-incorporated regulated firms (including UK subsidiaries of overseas firms) have been required since 2012 to file quarterly reports which show the differences between prudent valuation and the fair valuation used in relevant firms' financial statements. The final rule therefore requires those firms to calculate profit for the purpose of determining the initial size of their pre-risk adjusted bonus pool by adjusting their fair value accounting profit with the year-on-year change in the prudent valuation adjustment (PVA) figure.

2.33 UK subsidiaries of international firms are required to file quarterly prudent valuation adjustments for portfolios booked in UK entities only. Therefore firms that do not set a UK-specific bonus pool will not be required to apply the incremental movement in the PVA for the UK subsidiary to the global pool. For firms that do not have a UK bonus pool where the bonus pool is determined and allocated by the parent company, the PRA will require the firm to provide evidence that the incremental change in the PVA for the UK subsidiary has been applied to the profits of the UK regulated entity that feed into the global bonus pool.

2.34 As branches of overseas firms are not required to submit prudent valuation returns, they will be out of scope of this new requirement. However, the PRA will expect those firms to apply an appropriate adjustment to profit based on comparable principles to the extent it is achievable in the jurisdiction in which the global pool is determined.

Performance metrics (PRA only)

2.35 Since the introduction of the Remuneration Code, the PRA has sought to discourage firms from determining remuneration using a narrow set of metrics based on short-term revenue or profit such as return on equity, earnings per share and total shareholder return. In CP15/14 the PRA proposed an explicit rule against such over-reliance.

2.36 Consultation responses indicated that standard industry practice already ensures to a large degree that revenue-based metrics are used as part of a balanced, risk-adjusted score card when determining variable remuneration.

2.37 The PRA is therefore introducing the proposed rule that simple revenue or profit-based measures may not be relied on to determine variable remuneration at aggregate or individual level, except as part of a balanced and risk-adjustment scorecard.

Remuneration of NEDs

2.38 The PCBS considered that the award of variable remuneration to NEDs could compromise their position as independent members of boards. Payment of variable remuneration to NEDs is already rare and the PRA and FCA proposed to introduce rules to prevent the payment of variable remuneration to employees in respect of a NED role.

2.39 Almost all responses agreed with the proposal and noted that this is already current practice in most UK firms.

2.40 The PRA and FCA will therefore introduce a rule that NEDs should not receive variable remuneration in respect of activity carried out in their roles as non-executives.

Impact of the final proposals

2.41 With the exception of deferral scope, the final proposals are those consulted on. For deferral, the population of non-senior manager MRTs subject to a minimum five year deferral has been revised in light of evidence received during and following the consultation. The PRA is applying a minimum five year deferral period to those who qualify as risk managers, while the FCA is applying the CRD minimum deferral period. The affected population to which extended five year deferral is applied and the compliance costs of implementing deferral remain similar to the original proposals. Given the other proposals are those consulted on, the impacts set out in the original cost-benefit analysis remain appropriate to the final proposals.

3 FCA response to feedback on its non-handbook guidance

General guidance on proportionality guidance

3.1 The FCA also consulted on changes to the existing guidance on proportionality under SYSC 19A and SYSC 19C of the FCA Handbook, as well as the creation of a new proportionality guidance for dual regulated firms (SYSC 19D of the FCA Handbook).

3.2 The FCA did not receive any negative responses to this proportionality guidance and therefore is issuing the guidance as consulted on.

General guidance on the application of *ex-post* risk adjustment to variable remuneration

3.3 In Annex 6 of PRA CP15/14 (FCA CP14/14), the FCA consulted on proposed FCA-only guidance primarily in relation to the application of malus. The FCA subsequently published GC15/2 general guidance on the application of *ex-post* risk adjustment to variable remuneration on 26 March 2015. This guidance consultation amended and replaced the draft FCA guidance previously consulted on in Appendix 6 of the consultation paper.

3.4 GC15/2 proposed new guidance to share the latest good practice observed in the 2014 remuneration round and clarify the FCA's expectations on how relevant firms meet the Remuneration Code requirements on *ex-post* risk adjustment.

3.5 In summary, the FCA proposals for consultation in GC15/2 covered:

- **Scope (within firms)** — Adjustments are sufficiently wide-ranging to include all those whose roles and responsibilities include areas where failures or poor performance contributed to, or failed to prevent, the crystallisation of risk, including up the management chain and to control functions.
- **Expectations in relation to the application of *ex-post* risk adjustment** — individual and collective adjustments reflect the magnitude of the event based on a range of financial and non-financial factors, the degree of involvement or responsibility of the individuals concerned and are effective at driving positive behaviours and culture.
- **Timing and consideration of *ex-post* risk adjustment** — adjustments are considered once events have been identified, and reductions applied, as soon as reasonably possible, with awards frozen where investigations remain ongoing.
- **Procedure for considering *ex-post* risk adjustment** — events are considered using a clearly defined, robust and well-documented process that considers a range of relevant factors. This includes applying *ex-post* adjustments separately from other factors at the end of the process and clearly communicating the impact of *ex-post* adjustments to staff in writing and as a group.
- **Co-operation with the FCA** — firms under review submit all relevant information early and in line with the FCA's requested timetable.

3.6 It was proposed that this draft guidance would apply to firms in scope of the proposed SYSC 19D, a change in approach from the proposals originally set out in PRA CP15/14/FCA CP14/14, which also proposed the application to solo-regulated firms in scope of SYSC 19A (Remuneration Code).

3.7 The FCA received 4 responses to GC15/2 from trade bodies and major deposit-takers which were broadly supportive of the proposals.

3.8 Below we set out the FCA's responses to the most significant issues raised in the feedback to the guidance consultation, noting those areas where changes are being made to the original policy proposals.

GC15/2 Q1: Do you agree with the proposals in each of the five areas set out in this guidance consultation?

Expectations in relation to the application of *ex-post* risk adjustment

3.9 One respondent requested greater clarity on the size of adjustment the FCA considers to be appropriately material.

3.10 The FCA is supportive of the aim of ensuring greater consistency in the application of *ex-post* risk adjustment across firms. Section 3 of the guidance aims to assist firms in making consistent judgements on the appropriate magnitude of adjustments by setting out a range of factors that firms should consider.

3.11 However, the FCA has observed a high degree of variability in the magnitude of cases and the extent of individual involvement or responsibility even in relation to cases that might appear similar. The FCA does not therefore consider there to be a single answer that can be applied in all cases. Rather, it is important that the risk adjustments reflect the specificities of the case and are sufficiently wide-ranging and material in size to drive positive individual behaviours and culture within firms.

Timing and consideration of *ex-post* risk adjustment

3.12 The guidance consultation proposed that firms freeze the vesting of all variable remuneration potentially due to individuals undergoing internal or external investigation that could result in material *ex-post* risk adjustment until such an investigation has concluded and the firm has made a decision and communicated it to the relevant employee(s).

3.13 This is similar to the text included in PRA SS2/13 and is derived from the requirement of SYSC 19A.3.51R(1) which states that awards cannot be paid or allowed to vest unless sustainable according to the financial situation of the firm, or justified by performance.

3.14 However, the point was raised that this could act as a disincentive to thorough examination of a relevant event and that there may be circumstances where a conclusion has been reached in relation to all or part of an award for particular individuals.

3.15 We have taken note of these concerns and have amended the final guidance text to make clear that the guidance does not preclude the vesting of some or all variable remuneration in relation to particular individuals once certainty has been reached that *ex-post* risk adjustment of certain amounts is not required.

3.16 Whilst respondents generally recognised the advantages of considering cases as they arise, concerns were raised that firms have well-established year-end performance processes where certain adjustment decisions, particularly those not made in a disciplinary context, are made.

3.17 We recognise these concerns and are comfortable that the current drafting provides sufficient flexibility to accommodate existing processes within firms as appropriate.

Procedure for considering *ex-post* risk adjustment

3.18 Two respondents raised concerns that clearly communicating the size of *ex-post* risk adjustments for particular events may have the unintended consequence of encouraging excessive risk-taking if the size of the potential reward is seen to outweigh the risk of the downward adjustment.

3.19 The FCA considers clear communication of the impact of material crystallised risks and adverse performance outcomes on variable remuneration as crucial to ensuring that individual incentives are fully aligned with risk-adjusted performance. It is important that remuneration policies and employment contracts make clear that variable remuneration is contingent on sustained risk-adjusted performance and that *ex-post* risk adjustments are sufficient in size to achieve this.

3.20 Over the longer-term, ensuring that variable remuneration is fully risk-adjusted should drive a virtuous circle whereby clearly communicated and robust action reduces the incentives to take excessive risk, in turn generating a positive conduct culture where fewer material events occur that require *ex-post* risk adjustment.

3.21 Respondents were also keen to see consistency of expectations and approach as far as possible maintained between the FCA and PRA on *ex-post* risk adjustment. We are supportive of this aim and whilst each regulator has its own statutory objectives and supervisory focus, the FCA and PRA both seek to ensure that incentives are fully risk-adjusted and work closely together to achieve this.

Annexes

1 PRA Instruments

- 1.1 PRA Rulebook: CRR Firms: Remuneration Instrument 2015
- 1.2 Handbook (Remuneration Consequentials) Instrument 2015

2 PRA Supervisory statement

- 2.1 Supervisory Statement — Remuneration (SS27/15)
(see SS27/15 landing page: www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss2715.aspx)

3 FCA Statutory Instrument

- Senior Management Arrangements, Systems and Controls (Remuneration Code) (No. 6) Instrument 2015
- Amendments to the Glossary of definitions
- Amendments to the Senior Management Arrangements, Systems and Controls sourcebook (SYSC)
- Amendments to the Supervision manual (SUP)

4 FCA General Guidance on Proportionality

- The IFPRU Remuneration Code (SYSC 19A)
- The BIPRU Remuneration Code (SYSC 19C) and Pillar 3 disclosures on Remuneration (BIPRU 11)
- The Dual-regulated firms Remuneration Code (SYSC 19D)

5 FCA non-handbook General Guidance on ex-post risk adjustment

PRA RULEBOOK: CRR FIRMS: REMUNERATION INSTRUMENT 2015

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (The PRA’s general rules);
 - (2) section 137H (General rules about remuneration);
 - (3) section 137T (General supplementary powers); and
 - (4) section 138C (Evidential provisions).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook: CRR Firms: Remuneration Instrument 2015

- D. The PRA makes the rules in Annexes A to H to this instrument.

Commencement

- E. This instrument comes into force on 1 July 2015.

Citation

- F. This instrument may be cited as the PRA Rulebook: CRR Firms: Remuneration Instrument 2015.

By order of the Board of the Prudential Regulation Authority

19 June 2015

Annex A

REMUNERATION

Chapter content

1. APPLICATION AND DEFINITIONS
2. APPLICATION DATES
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4. GROUPS
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11. RISK ADJUSTMENT
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13. PERSONAL INVESTMENT STRATEGIES
14. NON-COMPLIANCE
15. REMUNERATION STRUCTURES
16. BREACH OF THE REMUNERATION RULES
17. REMUNERATION BENCHMARKING REPORTING REQUIREMENT
18. HIGH EARNERS REPORTING REQUIREMENT

Links:

1 APPLICATION AND DEFINITIONS

1.1 Unless otherwise stated, this Part applies to:

- (1) a *CRR firm* in relation to its;
 - (a) *UK activities*;
 - (b) *passport activities* carried on from a *branch* in another *EEA State*; and
 - (c) other activities wherever they are carried on, in a *prudential context*; and
- (2) a *third country CRR firm* in relation to its activities carried on from an establishment in the *UK*.

1.2 This Part applies:

- (1) in relation to *regulated activities*;
- (2) in relation to the *regulated activity*, specified in Article 14 of the *Regulated Activities Order* (Dealing in investments as principal), disregarding the exclusion in Article 15 of the *Regulated Activities Order* (Absence of holding out etc.);
- (3) in relation to *ancillary activities* and (in relation to *MiFID business*) *ancillary services*;
- (4) in relation to the carrying on of *unregulated activities* in a *prudential context*; and
- (5) taking into account activities of other members of a *group* of which the *firm* is a member.

1.3 In this Part, the following definitions shall apply:

accounting reference date

means

- (1) (in relation to a *body corporate* incorporated in the *UK* under the Companies Acts) the accounting reference date of that *body corporate* determined in accordance with section 391 of the Companies Act 2006; or
- (2) (in relation to any other body) the last day of its financial year.

consolidation group entity

means an *institution* or *financial institution* which is, in relation to a *CRR firm* responsible for consolidation:

- (1) the *CRR firm* responsible for consolidation;
- (2) a *subsidiary* of the *CRR firm* responsible for consolidation; or
- (3) a *subsidiary* of the *EEA parent financial holding company* or *EEA parent mixed financial holding company* by which the *CRR firm* responsible for consolidation is controlled.

CRR firm responsible for consolidation

means a *CRR firm* which is either:

- (1) an *EEA parent institution*; or
- (2) controlled by an *EEA parent financial holding company* or by an *EEA parent mixed financial holding company* and to which supervision on a *consolidated basis* by the *PRA* applies in accordance with Article 111 of *CRD*.

high earner

means an *employee* (of a *firm* or of any *consolidation group entity*) whose total annual *remuneration* is €1 million or more per year or its equivalent in another currency determined by reference to the conversion rate applicable to the corresponding *High Earners Report* under Chapter 18.

High Earners Report

means the report by which a *firm* provides to the *PRA* the information required in Chapter 18.

material risk taker

has the meaning given in 3.1.

Material Risk Takers Regulation

means Commission Delegated Regulation (EU) No 604/2014 of 4 March 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to 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.

Remuneration Benchmarking Information Report

means the report by which a *firm* provides to the *PRA* the information required in Chapter 17.

remuneration requirements

means the requirements in 6 to 15.

share

means the investment specified in Article 76 of the *Regulated Activities Order* (Shares etc).

total assets

means:

- (1) in relation to a *CRR firm* or an *EEA bank*, its total assets as set out in its balance sheet on the relevant *accounting reference date*; and
- (2) in relation to a *third country CRR firm*, the total assets of the *third country CRR firm* as set out in its balance sheet on the relevant *accounting reference date* that cover the activities of the *branch* operation in the *UK*.

- 1.4 Unless otherwise defined, any italicised expression used in this Part and in the *CRD* or *CRR* has the same meaning as in the *CRD* or *CRR*.

2 APPLICATION DATES

- 2.1 Subject to 2.2 and 2.3, a *firm* must apply the *remuneration requirements* in relation to:
- (1) *remuneration* awarded, whether pursuant to a contract or otherwise, on or after 1 January 2011;
 - (2) *remuneration* due on the basis of contracts concluded before 1 January 2011 which is awarded or paid on or after 1 January 2011; and
 - (3) *remuneration* awarded, but not yet paid, before 1 January 2011, for services provided in 2010.
- 2.2 A *firm* must apply 15.9(3) and 15.10 in relation to *remuneration* awarded for services provided or performance from the year 2014 onwards, whether due on the basis of contracts concluded before, on or after 31 December 2013.
- [Note: Art. 162(3) of the *CRD*]**
- 2.3 A *firm* must apply 15.17(1)(b) and (c), 15.20(2), (3) and (4), 15.23 and 16.1(3) in relation to *remuneration* awarded in relation to a performance year starting on or after 1 January 2016.

3 MATERIAL RISK TAKERS

- 3.1 A *firm* must, save where otherwise stated, apply the requirements of this Part in relation to a *person* (a “material risk taker”) who is:
- (1) an *employee* of a *CRR firm* whose professional activities have a material impact on the *firm’s* risk profile, including any *employee* who is deemed to have a material impact on the *firm’s* risk profile in accordance with criteria set out in articles 3 to 5 of the *Material Risk Takers Regulation*; or
 - (2) subject to 3.2, an *employee* of a *third country CRR firm* who would fall within 3.1(1) if it had applied in relation to him or her.
- 3.2 A *third country CRR firm* may deem an *employee* not to be a *material risk taker* where:
- (1) the *employee*:
 - (a) would meet any of the criteria in Article 4(1) of the *Material Risk Takers Regulation*,
 - (b) would not meet any of the criteria in Article 3 of the *Material Risk Takers Regulation*; and
 - (c) was awarded total *remuneration* of less than €750,000 in the preceding financial year; and

(2) the *third country CRR firm* determines that the professional activities of the *employee* do not have a material impact on its risk profile on the grounds described in Article 4(2) of the *Material Risk Takers Regulation*.

3.3 Where a *third country CRR firm* deems an *employee* not to be a *material risk taker* as set out in 3.2, it must notify the *PRA*, applying exactly the approach described in Article 4(4) of the *Material Risk Takers Regulation*.

3.4 A *firm* must maintain a record of its *material risk takers* in accordance with the Record Keeping Part.

3.5 A *firm* must take reasonable steps to ensure that its *material risk takers* understand the implications of their status as such, including the potential for *remuneration* which does not comply with certain requirements of this Part to be rendered void and recoverable by the *firm*.

4 GROUPS

4.1 A *firm* must apply the requirements at *group*, *parent undertaking* and *subsidiary undertaking* levels, including those *subsidiaries* established in a country or territory which is not in an *EEA State*.

4.2 A *firm* must:

(1) ensure that the risk management processes and internal control mechanisms of the other members of the *group* of which it is a member comply with the obligations set out in this Part on a *consolidated basis* or *sub-consolidated basis*; and

(2) ensure that compliance with (1) enables the members of the *group* of which it is a member to have arrangements, processes and mechanisms that are consistent and well integrated and that any data relevant to the purpose of supervision can be produced.

[Note: Arts. 92(1) and 109 of the CRD]

5 PROPORTIONALITY

5.1 A *firm* must comply with this Part in a way and to the extent that is appropriate to its size, internal organisation and the nature, the scope and the complexity of its activities, when establishing and applying the total *remuneration* policies for *material risk takers*.

5.2 5.1 does not apply to the requirement in 7.4 for significant *firms* to have a *remuneration* committee.

[Note: Art. 92(2) of the CRD]

6 REMUNERATION POLICIES

6.1 In this Chapter, 6.2 and 6.5 apply to *firms* in relation to *firms' remuneration* policies, practices and procedures generally, not only in relation to *material risk takers*.

- 6.2 A *firm* must establish implement and maintain a *remuneration* policy, practices and procedures which are consistent with and promote sound and effective risk management and do not encourage risk-taking that exceeds the level of tolerated risk of the *firm*.

[Note: Arts. 74(1) and 92(2)(a) of the CRD]

- 6.3 A *firm* must ensure that its *remuneration* policy is in line with the business strategy, objectives, values and long-term interests of the *firm*.

[Note: Art. 92(2)(b) of the CRD]

- 6.4 A *firm* must ensure that its *remuneration* policy includes measures to avoid conflicts of interest.

[Note: Art. 92(2)(b) of the CRD]

- 6.5 A *firm* must ensure that its *remuneration* policies, practices and procedures, including performance appraisal processes and decisions, are clear and documented.

7 GOVERNANCE

- 7.1 In this Chapter, 7.4 applies generally, not only in relation to *material risk takers*.

- 7.2 A *firm* must ensure that its *management body* in its *supervisory function* adopts and periodically reviews the general principles of the *remuneration* policy and is responsible for overseeing its implementation.

[Note: Art. 92(2)(c) of the CRD and Standard 1 of the FSB Compensation Standards]

- 7.3 A *firm* must ensure that the implementation of the *remuneration* policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for *remuneration* adopted by the *management body* in its *supervisory function*.

[Note: Art. 92(2)(d) of the CRD and Standard 1 of the FSB Compensation Standards]

- 7.4 A *CRR firm* that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities must establish a *remuneration* committee, and ensure that the committee:

- (1) is constituted in a way that enables it to exercise competent and independent judgment on *remuneration* policies and practices and the incentives created for managing risk, capital and liquidity;
- (2) comprises a chairman and members who are members of the *management body* who do not perform any executive function in the *firm*;
- (3) is responsible for the preparation of decisions regarding *remuneration*, including those which have implications for the risk and risk management of the *firm* and which are to be taken by the *management body*; and
- (4) takes into account, when preparing such decisions, the long-term interests of shareholders, investors and other stakeholders in the *firm* as well as the public interest.

[Note: Art. 95 of the CRD and Standard 1 of the FSB Compensation Standards]

- 7.5 A *firm* that maintains a website must explain on the website how the *firm* complies with this Part.

[Note: Art. 96 of the CRD]

8 CONTROL FUNCTIONS

- 8.1 A *firm* must ensure that *employees* engaged in control functions:

- (1) are independent from the business units they oversee;
- (2) have appropriate authority; and
- (3) are *remunerated*:
 - (a) adequately to attract qualified and experienced *employees*; and
 - (b) in accordance with the achievement of the objectives linked to their functions, independent of the performance of the business areas they control.

[Note: Art. 92(2)(e) of the CRD and Standard 2 of the FSB Compensation Standards]

- 8.2 A *firm* must ensure that the remuneration of the senior officers in risk management and compliance functions is directly overseen by the *remuneration* committee referred to in 7.4, or, if such a committee has not been established, by the *governing body* in its *supervisory function*.

[Note: Art. 92(2)(f) of the CRD]

9 REMUNERATION AND CAPITAL

- 9.1 A *firm* must ensure that total variable *remuneration* does not limit the *firm's* ability to strengthen its capital base.

[Note: Art. 94(1)(c) of the CRD and Standard 3 of the FSB Compensation Standards]

10 EXCEPTIONAL GOVERNMENT INTERVENTION

- 10.1 A *firm* that benefits from exceptional government intervention must ensure that:

- (1) variable *remuneration* is strictly limited as a percentage of net revenues when it is inconsistent with the maintenance of a sound capital base and timely exit from government support;
- (2) it restructures *remuneration* in a manner aligned with sound risk management and long-term growth, including when appropriate establishing limits to the *remuneration* of members of its *management body*; and
- (3) no variable or discretionary *remuneration* of any kind is paid to members of its *management body* unless this is justified.

[Note: Art. 93 of the CRD and Standard 10 of the FSB Compensation Standards]

11 RISK ADJUSTMENT

- 11.1 (1) A *firm* must ensure that any measurement of performance used to calculate variable *remuneration* components or pools of variable *remuneration* components:
- (a) includes adjustments for all types of current and future risks and takes into account the cost and quantity of the capital and the liquidity required; and
 - (b) takes into account the need for consistency with the timing and likelihood of the *firm* receiving potential future revenues incorporated into current earnings.
- (2) A *firm* must ensure that the allocation of variable *remuneration* components within the *firm* also takes into account all types of current and future risks.

[Note: Arts. 94(1)(j) and (k) of the CRD and Standard 4 of the FSB Compensation Standards]

- 11.2 A *firm* must have a clear and verifiable mechanism for measuring performance, with risk adjustment applied thereafter in a clear and transparent manner.
- 11.3 A *firm* must base assessments of financial performance used to calculate variable *remuneration* components or pools of variable *remuneration* components principally on profits. To determine profits for this purpose, a *firm* (other than a *branch*) must adjust its fair valuation accounting model profit figure by the incremental change in its regulatory prudent valuation adjustment figure across the relevant performance period.
- 11.4 A *firm*'s risk-adjustment approach must reflect both ex-ante adjustment (which adjusts *remuneration* for intrinsic risks that are inherent in its business activities) and ex-post adjustment (which adjusts *remuneration* for crystallisation of specific risk events).
- 11.5 A *firm* must not base the ex-ante risk adjustments referred to in 11.4 on revenue-based measures, except as part of a balanced, risk-adjusted scorecard.
- 11.6 A *firm* must ensure that its total variable *remuneration* is generally considerably contracted where subdued or negative financial performance of the *firm* occurs, taking into account both current *remuneration* and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.

[Note: Art. 94(1)(n) of the CRD and Standard 5 of the FSB Compensation Standards]

12 PENSION POLICY

- 12.1 A *firm* must ensure that:
- (1) its pension policy is in line with its business strategy, objectives, values and long-term interests;
 - (2) when an *employee* leaves the *firm* before retirement, any discretionary pension benefits are held by the *firm* for a period of five years in the form of instruments referred to in 15.15; and

- (3) when an *employee* reaches retirement, discretionary pension benefits are paid to the *employee* in the form of instruments referred to in 15.15 and subject to a five-year retention period.

[Note: Art. 94(1)(o) of the CRD]

13 PERSONAL INVESTMENT STRATEGIES

- 13.1 (1) A *firm* must ensure that its *employees* undertake not to use personal hedging strategies to undermine the risk alignment effects embedded in their *remuneration* arrangements.
- (2) A *firm* must ensure that its *employees* undertake not to use *remuneration*-related or liability-related *contracts of insurance* to undermine the risk alignment effects embedded in their *remuneration* arrangements.
- (3) A *firm* must maintain effective arrangements designed to ensure that *employees* comply with their undertaking.

[Note: Art. 94(1)(p) of the CRD and Standard 14 of the FSB Compensation Standards]

14 NON-COMPLIANCE

- 14.1 A *firm* must ensure that variable *remuneration* is not paid through vehicles or methods that facilitate non-compliance with obligations arising from *CRR*, *CRD* or this Part.

[Note: Art. 94(1)(q) of the CRD]

15 REMUNERATION STRUCTURES

General Requirement

- 15.1 A *firm* must ensure that the structure of an *employee's remuneration* is consistent with and promotes effective risk management.
- 15.2 A *firm* must ensure that its *remuneration* policy makes a clear distinction between criteria for setting:
- (1) basic fixed *remuneration* that primarily reflects an *employee's* professional experience and organisational responsibility as set out in the *employee's* job description and terms of employment; and
- (2) variable *remuneration* that reflects performance in excess of that required to fulfil the *employee's* job description and terms of employment and that is subject to performance adjustment in accordance with this Part.

[Note: Art. 92(2)(g) of the CRD]

- 15.3 A *firm* must not award variable *remuneration* to a *non-executive director* in relation to his or her role as such.

Assessment of performance

- 15.4 A *firm* must ensure that where *remuneration* is performance-related:
- (1) the total amount of *remuneration* is based on a combination of the assessment of the performance of:
 - (a) the individual;
 - (b) the business unit concerned; and
 - (c) the overall results of the *firm*; and
 - (2) when assessing individual performance, financial as well as non-financial criteria are taken into account.

[Note: Art. 94(1)(a) of the CRD and Standard 6 of the FSB Compensation Standards]

- 15.5 A *firm* must clearly explain the performance assessment process referred to in 15.4 to relevant *employees*.
- 15.6 A *firm* must ensure that the assessment of performance is set in a multi-year framework in order to ensure that the assessment process is based on longer-term performance and that the actual payment of performance-based components of *remuneration* is spread over a period which takes account of the underlying business cycle of the *firm* and its business risks.

[Note: Art. 94(1)(b) of the CRD]

Specific award structures: guaranteed variable remuneration and buy-outs

- 15.7 A *firm* must ensure that guaranteed variable *remuneration* is not part of prospective *remuneration* plans. A *firm* must not award, pay or provide guaranteed variable *remuneration* unless:
- (1) it is exceptional;
 - (2) it occurs in the context of hiring a new *employee*;
 - (3) the *firm* has a sound and strong capital base; and
 - (4) it is limited to the first year of service.

[Note: Arts. 94(1)(d) and (e) of the CRD and Standard 11 of the FSB Compensation Standards]

- 15.8 A *firm* must ensure that *remuneration* packages relating to compensation for, or buy out from, an *employee's* contracts in previous *employment* align with the long-term interests of the *firm* including appropriate retention, deferral and performance and clawback arrangements.

[Note: Art. 94(1)(i) of the CRD]

Ratio between fixed and variable components of total remuneration

- 15.9 A *firm* must set an appropriate ratio between the fixed and variable components of total *remuneration* and ensure that:
- (1) fixed and variable components of total *remuneration* are appropriately balanced;

- (2) the level of the fixed component represents a sufficiently high proportion of the total *remuneration* to allow the operation of a fully flexible policy on variable *remuneration* components, including the possibility to pay no variable *remuneration* component; and
- (3) subject to 15.10, the level of the variable component of total *remuneration* must not exceed 100% of the fixed component of total *remuneration* for each *material risk taker*.

[Note: Arts. 94(1)(f) and 94(1)(g)(i) of the CRD]

- 15.10 A *firm* may set a higher maximum level of the ratio between the fixed and variable components of *remuneration* provided:
- (1) the overall level of the variable component does not exceed 200% of the fixed component of the total *remuneration* for each *material risk taker*; and
 - (2) is approved by the shareholders or owners or members of the *firm* in accordance with 15.11.
- 15.11 A *firm* must ensure that any approval by the shareholders or owners or members of the *firm* for the purposes of 15.10 is carried out in accordance with the following procedure:
- (1) the *firm* must give reasonable notice to all shareholders or owners or members of the *firm* that the *firm* intends to seek approval of the proposed higher ratio;
 - (2) the *firm* must make a detailed recommendation to all shareholders or owners or members of the *firm* giving the reasons for, and the scope of, the approval sought, including the number of staff affected, their functions and the expected impact on the requirement to maintain a sound capital base;
 - (3) the *firm* must, without delay, inform the *PRA* of the recommendation to its shareholders or owners or members, including the proposed higher ratio and the reasons therefor and must demonstrate to the *PRA* that the proposed higher ratio does not conflict with the *firm's* obligations under the *CRD* and the *CRR*, having regard in particular to the *firm's* own funds obligations;
 - (4) the *firm* must ensure that *employees* who have an interest in the proposed higher ratio are not allowed to exercise, directly or indirectly, any voting rights they may have as shareholders or owners or members of the *firm* in respect of the approval sought; and
 - (5) the higher ratio is approved by:
 - (a) at least 66% of the shares or equivalent ownership rights represented, if at least 50% of the shares or equivalent ownership rights in the *firm* are represented; or
 - (b) at least 75% of the shares or equivalent ownership rights represented if less than 50% of the shares or equivalent ownership rights in the *firm* are represented.

[Note: Art. 94(1)(g)(ii) of the CRD]

- 15.12 A *firm* must notify without delay the *PRA* of the decisions taken by its shareholders or members or owners including any approved higher maximum ratio.

[Note: Art. 94(1)(g)(ii) of the CRD]

- 15.13 A *firm* may apply a discount rate to a maximum of 25% of an *employee's* total variable *remuneration* provided it is paid in instruments that are deferred for a period of not less than

five years. In applying this discount rate, *firms* must apply the EBA Guidelines on the applicable notional discount rate for variable remuneration of 27 March 2014.

[Note: Art. 94(1)(g)(iii) of the CRD]

Payments related to early termination

15.14 A *firm* must ensure that payments relating to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure or misconduct.

[Note: Art. 94(1)(h) of the CRD and Standard 12 of the FSB Compensation Standards]

Retained shares or other instruments

15.15 A *firm* must ensure that:

- (1) a substantial portion, which is at least 50%, of any variable *remuneration* consists of an appropriate balance of:
 - (a) *shares* or equivalent ownership interests, subject to the legal structure of the *firm* concerned, or *share-linked* instruments or equivalent non-cash instruments in the case of a non-listed *firm*; and
 - (b) where possible other instruments which are eligible as *Additional Tier 1 instruments* or are eligible as *Tier 2 instruments* or other instruments that can be fully converted to *Common Equity Tier 1 instruments* or written down, that in each case adequately reflect the credit quality of the *firm* as a going concern and are appropriate for use as variable *remuneration*; and
- (2) the instruments referred to in paragraph (1) are subject to an appropriate retention policy designed to align incentives with the longer-term interests of the *firm*.

15.16 A *firm* must apply 15.15 to both the portion of the variable *remuneration* component deferred in accordance with 15.17 and 15.18 and the portion not deferred.

[Note: Art. 94(1)(l) of the CRD and Standard 8 of the FSB Compensation Standards]

Deferral

- 15.17 (1) A *firm* must not award, pay or provide a variable *remuneration* component unless a substantial portion of it, which is at least 40%, is deferred over a period which is not less than:
- (a) in the case of a *material risk taker* who is not subject to (b) or (c), three years, vesting no faster than on a pro-rata basis;
 - (b) in the case of a *material risk taker* who does not perform a *PRA senior management function*, but whose professional activities meet the qualitative criteria set out in Article 3(1) to 3(9), 3(10) (but only by virtue of being responsible for a committee referred to therein), 3(13) or 3(15) of the *Material Risk Takers Regulation*, five years, vesting no faster than on a pro-rata basis; or
 - (c) in the case of a *material risk taker* who performs a *PRA senior management function*, seven years, with no vesting to take place until three years after award, and vesting no faster than on a pro-rata basis thereafter.

15.18 In the case of a variable *remuneration* component:

- (1) of £500,000 or more; or
- (2) payable to a *director* of a *firm* that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities;

at least 60% of the amount must be deferred on the basis set out in 15.17.

- 15.19 Subject to 15.17, the length of the deferral period must be established in accordance with the business cycle, the nature of the business, its risks and the activities of the *employee* in question.

[Note: Art. 94(1)(m) of the CRD and Standards 6 and 7 of the FSB Compensation Standards]

Performance adjustment

- 15.20 A *firm* must ensure that:

- (1) any variable *remuneration*, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the *firm* as a whole, and justified on the basis of the performance of the *firm*, the business unit and the individual concerned;
- (2) any variable *remuneration* is subject to clawback, such that it is only awarded if an amount corresponding to it can be recovered from the individual by the *firm* if the recovery is justified on the basis of the circumstances described in 15.21(2) or 15.22; and
- (3) any variable *remuneration* is subject to clawback for a period of at least 7 years from the date on which the variable *remuneration* is awarded;
- (4) in the case of a *material risk taker* who performs a *PRA senior management function*, the *firm* can, by notice to the *employee* to be given no later than 7 years after the variable *remuneration* was awarded, extend the period during which variable *remuneration* is subject to clawback to at least 10 years from the date on which the variable *remuneration* is awarded, where:
 - (a) the *firm* has commenced an investigation into facts or events which it considers could potentially lead to the application of clawback were it not for the expiry of the clawback period; or
 - (b) the *firm* has been notified by a regulatory authority (including an overseas regulatory authority) that an investigation has been commenced into facts or events which the *firm* considers could potentially lead to the application of clawback by the *firm* were it not for the expiry of the clawback period; and
- (5) it considers on an ongoing basis whether to use the power in (4).

[Note: Art. 94(1)(n) of the CRD and Standards 6 and 9 of the FSB Compensation Standards]

- 15.21 A *firm* must:

- (1) set specific criteria for the application of malus and clawback; and
- (2) ensure that the criteria for the application of malus and clawback in particular cover situations where the *employee*:

- (a) participated in or was responsible for conduct which resulted in significant losses to the *firm*; or
- (b) failed to meet appropriate standards of fitness and propriety.

[Note: Art. 94(1)(n) of the CRD]

- 15.22 (1) A *firm* should reduce unvested deferred variable *remuneration* when, as a minimum:
- (a) there is reasonable evidence of *employee* misbehaviour or material error;
 - (b) the *firm* or the relevant business unit suffers a material downturn in its financial performance; or
 - (c) the *firm* or the relevant business unit suffers a material failure of risk management.
- (2) For performance adjustment purposes, awards of deferred variable *remuneration* made in *shares* or other non-cash instruments should provide the ability for a *firm* to reduce the number of *shares* or other non-cash instruments.
- (3) Contravention of any of (1) or (2) may be relied on as tending to establish contravention of 15.20(1). Contravention of (1) or (2) does not give rise to any of the consequences provided for by provisions of *FSMA* other than section 138C.
- 15.23 A *firm* must make all reasonable efforts to recover an appropriate amount corresponding to some or all vested variable *remuneration* where either of the following circumstances arise during the period in which clawback applies (including any part of such period occurring after the relevant employment has ceased):
- (1) there is reasonable evidence of *employee* misbehaviour or material error; or
 - (2) the *firm* or the relevant business unit suffers a material failure of risk management.
- A *firm* must take into account all relevant factors (including, where the circumstances described in (2) arise, the proximity of the *employee* to the failure of risk management in question and the *employee's* level of responsibility) in deciding whether and to what extent it is reasonable to seek recovery of any or all of their vested variable *remuneration*.

16 BREACH OF THE REMUNERATION RULES

- 16.1 Subject to 16.2 to 16.7, the voiding provisions in 16.9 to 16.13 apply in relation to the prohibitions on *material risk takers* being *remunerated* in the ways specified in:
- (1) 15.7 (guaranteed variable *remuneration*);
 - (2) 15.17 to 15.19 (deferred variable *remuneration*);
 - (3) 15.20(2) (performance adjustment – clawback); and
 - (4) 16.16 (replacing payments recovered or property transferred).
- 16.2 16.1 applies only to those prohibitions as they apply in relation to a *firm* that satisfies either Condition 1 or Condition 2, as set out in 16.3 and 16.4.
- 16.3 Condition 1 is that the *firm* is a *CRR firm* that has relevant total assets exceeding £50 billion.

- 16.4 Condition 2 is that the *firm*:
- (1) is a *credit institution* or a *UK designated investment firm*; and
 - (2) is part of a *group* containing a *firm* that has relevant total assets exceeding £50 billion and that is a *CRR firm*.
- 16.5 For the purposes of 16.3 and 16.4 “relevant total assets” means the arithmetic mean of the *firm’s* total assets as set out in its balance sheet on its last three accounting reference dates.
- 16.6 The voiding provisions in 16.9 to 16.13 do not apply in relation to the prohibition on *material risk takers* being *remunerated* in the way specified in 15.7 (guaranteed variable *remuneration*) if both the conditions in paragraphs (2) and (3) of that *rule* are met.
- 16.7 The voiding provisions in 16.9 to 16.13 do not apply in relation to a *material risk taker* (X) in respect of whom both the following conditions are satisfied:
- (1) Condition 1 is that X’s variable *remuneration* is no more than 33% of total *remuneration*; and
 - (2) Condition 2 is that X’s total *remuneration* is no more than £500,000.
- 16.8 In relation to 16.7:
- (1) references to *remuneration* are to *remuneration* awarded or paid in respect of the relevant performance year;
 - (2) the amount of any *remuneration* is:
 - (a) if it is money, its amount when awarded;
 - (b) otherwise, whichever of the following is greatest: its value to the recipient when awarded; its market value when awarded; or the cost of providing it at the time of the award;
 - (3) where *remuneration* is, when awarded, subject to any condition, restriction or other similar provision which causes the amount of the *remuneration* to be less than it otherwise would be, that condition, restriction or provision is to be ignored in arriving at its value; and
 - (4) it is to be assumed that the *material risk taker* will remain so for the duration of the relevant performance year.

Voiding provisions

- 16.9 Any provision of an agreement that contravenes a prohibition on *persons* being *remunerated* in a way specified in a *rule* to which this *rule* applies (a “contravening provision”) is void.
- 16.10 A contravening provision does not cease to be void because:
- (1) the *firm* concerned ceases to satisfy any of the conditions set out in 16.3 to 16.4; or
 - (2) the *material risk taker* concerned starts to satisfy both of the conditions set out in 16.7 (1) and (2).
- 16.11 A contravening provision that, at the time a *rule* to which this *rule* applies was first made (including any corresponding *rules* specified in SYSC 19A.3.54R of the *PRA Handbook*), is

contained in an agreement made before that time is not rendered void by 16.9 unless it is subsequently amended so as to contravene such a *rule*.

- 16.12 (1) A pre-existing provision is not rendered void by 16.9.
- (2) In this Chapter, a pre-existing provision is any provision of an agreement that would (but for this *rule*) be rendered void by 16.9 that was agreed at a time when either:
- (a) the *firm* concerned did not satisfy any of the conditions set out in 16.3 to 16.4; or
 - (b) the *material risk taker* concerned satisfied both of the conditions set out in 16.7(1) and (2).
- (3) But an amendment to, or in relation to, a pre-existing provision is not to be treated as a pre-existing provision where the amendment is agreed at a time when both:
- (a) the *firm* concerned satisfies at least one of the conditions set out in 16.3 to 16.4; and
 - (b) the *material risk taker* concerned does not satisfy both of the conditions set out in 16.7(1) and (2).
- 16.13 For the purposes of this Chapter, it is immaterial whether the law which (apart from 16.9 to 16.16) governs a contravening provision is the law of the *UK*, or of a part of the *UK*.

Recovery of payments made or property transferred pursuant to a void contravening provision

- 16.14 In relation to any payment made or other property transferred in pursuance of a contravening provision other than a pre-existing provision, a *firm* must take reasonable steps to:
- (1) recover any such payment made or other property transferred by the *firm*; and
 - (2) ensure that any other *person* recovers any such payment made or other property transferred by that *person*.
- 16.15 16.14 continues to apply in one or both of the following cases:
- (1) the *firm* concerned ceases to satisfy any of the conditions set out in 16.3 to 16.4;
 - (2) the *material risk taker* concerned starts to satisfy both of the conditions set out in 16.7(1) and (2).

Replacing payments recovered or property transferred

- 16.16 (1) A *firm* must not award, pay or provide variable *remuneration* to a *person* who has received *remuneration* in pursuance of a contravening provision other than a pre-existing provision (the "contravening *remuneration*") unless the *firm* has obtained a legal opinion stating that the award, payment or provision of the *remuneration* complies with this Part.
- (2) This *rule* applies only to variable *remuneration* relating to a performance year to which the contravening *remuneration* related.
- (3) The legal opinion in (1) must be properly reasoned and be provided by an appropriately qualified independent individual.

- (4) Paragraph (1) continues to apply in one or both of the following cases:
- (a) the *firm* concerned ceases to satisfy any of the conditions set out in 16.3 to 16.4;
 - (b) the *material risk taker* concerned starts to satisfy both of the conditions set out in 16.7(1) and (2).

17 REMUNERATION BENCHMARKING REPORTING REQUIREMENT

- 17.1 This Chapter applies to a *firm* to which this Part applies, which had *total assets* equal to or greater than £50 billion on an unconsolidated basis on the *accounting reference date* immediately prior to the *firm's* last complete financial year.
- 17.2 A *firm* must submit a *Remuneration Benchmarking Information Report* to the *PRA* annually.
- 17.3 The *firm* must provide to the *PRA*, by way of its *Remuneration Benchmarking Information Report*, the information disclosed in accordance with the criteria for disclosure established in points (g), (h) and (i) of Article 450(1) of the *CRR*.
- [Note: Art. 75(1) of the CRD]**
- 17.4 The *firm* must submit the *Remuneration Benchmarking Information Report* to the *PRA* within four months of the *firm's* *accounting reference date*.
- 17.5 A *firm* that is not, and does not have, an *EEA parent institution*, an *EEA parent financial holding company* or an *EEA parent mixed financial holding company* must complete that report on an unconsolidated basis in respect of *remuneration* awarded to *employees* of the *firm* in the last completed financial year.
- 17.6 A *firm* that is a *CRR firm responsible for consolidation* must complete that report on a consolidated basis in respect of *remuneration* awarded to all *employees* of all *consolidation group entities* in the last completed financial year.
- 17.7 The *firm* must ensure that the information in the *Remuneration Benchmarking Information Report* is denominated in euro, determined by reference to the exchange rate used by the European Commission for financial programming and the budget for December of the reported year.

[Note: EBA/GL/2014/08]

18 HIGH EARNERS REPORTING REQUIREMENT

- 18.1 The Chapter applies in relation to *high earners* and not only in relation to *material risk takers*.
- 18.2 A *firm* must submit a *High Earners Report* to the *PRA* annually.
- 18.3 The *firm* must submit that report to the *PRA* within four months of the end of the *firm's* *accounting reference date*.
- 18.4 A *firm* that is not, and does not have, an *EEA parent institution*, an *EEA parent financial holding company* or an *EEA parent mixed financial holding company* must complete that report on an unconsolidated basis in respect of *remuneration* awarded in the last completed

financial year to all *high earners* of the *firm* who mainly undertook their professional activities within the *EEA*.

18.5 A *firm* that is a *CRR firm responsible for consolidation* must complete that report on a *consolidated basis* in respect of *remuneration* awarded in the last completed financial year to all *high earners* who mainly undertook their professional activities within the *EEA* at:

- (1) the *EEA parent institution*, *EEA parent financial holding company* or the *EEA parent mixed financial holding company* of the *consolidation group*;
- (2) each *consolidation group entity* that has its registered office (or if it has no registered office, its head office) in an *EEA State*; and
- (3) each *branch* of any other *consolidation group entity* that is established or operating in an *EEA State*.

18.6 The *firm's High Earners Report* must report, in pay brackets of €1m, the number of *high earners*, including their job responsibilities, the business area involved and the main elements of salary, bonus, long-term award and pension contribution. The number of *high earners* must be reported as the number of natural persons, independent of the number of working hours on which their contract is based.

[Note: Art. 75(3) of the CRD]

18.7 The *firm* must ensure that the information in the *High Earners Report* is denominated in euro, determined by reference to the exchange rate used by the European Commission for financial programming and the budget for December of the reported year.

[Note: EBA/GL/2014/07]

Annex B

Amendments to the Glossary

In the Glossary Part of the PRA Rulebook, insert the following new definitions:

consolidation group

means the *undertakings* included in the scope of consolidation pursuant to Articles 18(1), 18(8), 19(1), 19(3) and 23 of the *CRR* and Groups 2.1 to 2.3.

EEA parent financial holding company

means a *parent financial holding company in an EEA State* which is not a *subsidiary* of an *institution* authorised in any *EEA State* or of another *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

EEA parent institution

means a *parent institution in an EEA State* which is not a *subsidiary* of another *institution* authorised in an *EEA State* or of a *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

EEA parent mixed financial holding company

means a *parent mixed financial holding company in an EEA State* which is not a *subsidiary* of an *institution* authorised in any *EEA State* or of another *financial holding company* or *mixed financial holding company* set up in any *EEA State*.

remuneration

means any form of remuneration, including salary, discretionary pension benefits and benefits of any kind.

third country CRR firm

means an *overseas firm* that:

- (1) is not an *EEA firm*;
- (2) has its head office outside the *European Economic Area*; and
- (3) would be a *CRR firm* if it had been a *UK undertaking*, had carried on all of its business in the *UK* and had obtained whatever authorisations for doing so as are required under *FSMA*.

Annex C

Amendments to the Remuneration Reporting Requirements Part

Remuneration Reporting Requirements is deleted in its entirety. This text is not shown.

Annex D

Amendments to the Internal Capital Adequacy Assessment Part

In this Annex deleted text is struck through.

1 APPLICATION AND DEFINITIONS

...

1.2 In this Part, the following definitions shall apply:

...

~~*consolidation group*~~

~~means the undertakings included in the scope of consolidation pursuant to Articles 18(1), 18(8), 19(1), 19(3) and 23 of the CRR and Groups 2.1–2.3.~~

...

Annex E

Amendments to the Notifications Part

In this Annex deleted text is struck through.

1 APPLICATION AND DEFINITIONS

...

1.2 In this Part, the following definitions shall apply:

...

~~*consolidation group*~~

~~means the *undertakings* included in the scope of consolidation pursuant to Articles 18(1), 18(8), 19(1), 19(3) and 23 of the *CRR* and Groups 2.1–2.3.~~

...

Annex F

Amendments to the Recovery Plans Part

In this Annex deleted text is struck through.

1 APPLICATION AND DEFINITIONS

...

1.2 In this Part, the following definitions shall apply:

...

~~EEA parent financial holding company~~

~~means a parent financial holding company in an EEA State which is not a subsidiary of an institution authorised in any EEA State or of another financial holding company or mixed financial holding company set up in any EEA State.~~

~~EEA parent institution~~

~~means a parent institution in an EEA State which is not a subsidiary of another institution authorised in an EEA State or of a financial holding company or mixed financial holding company set up in any EEA State.~~

~~EEA parent mixed financial holding company~~

~~means a parent mixed financial holding company in an EEA State which is not a subsidiary of an institution authorised in any EEA State or of another financial holding company or mixed financial holding company set up in any EEA State.~~

...

Annex G

Amendments to the Resolution Pack Part

In this Annex deleted text is struck through.

1 APPLICATION AND DEFINITIONS

...

1.2 In this Part, the following definitions shall apply:

...

~~EEA parent financial holding company~~

~~means a parent financial holding company in an EEA State which is not a subsidiary of an institution authorised in any EEA State or of another financial holding company or mixed financial holding company set up in any EEA State.~~

~~EEA parent institution~~

~~means a parent institution in an EEA State which is not a subsidiary of another institution authorised in an EEA State or of a financial holding company or mixed financial holding company set up in any EEA State.~~

~~EEA parent mixed financial holding company~~

~~means a parent mixed financial holding company in an EEA State which is not a subsidiary of an institution authorised in any EEA State or of another financial holding company or mixed financial holding company set up in any EEA State.~~

...

Annex H

Amendments to the Group Financial Support Part

In this Annex deleted text is struck through.

1 APPLICATION AND DEFINITIONS

...

1.2 In this Part, the following definitions shall apply:

...

~~EEA parent financial holding company~~

~~means a parent financial holding company in an EEA State which is not a subsidiary of an institution authorised in any EEA State or of another financial holding company or mixed financial holding company set up in any EEA State.~~

~~EEA parent institution~~

~~means a parent institution in an EEA State which is not a subsidiary of another institution authorised in an EEA State or of a financial holding company or mixed financial holding company set up in any EEA State.~~

~~EEA parent mixed financial holding company~~

~~means a parent mixed financial holding company in an EEA State which is not a subsidiary of an institution authorised in any EEA State or of another financial holding company or mixed financial holding company set up in any EEA State.~~

...

HANDBOOK (REMUNERATION CONSEQUENTIALS) INSTRUMENT 2015

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (The PRA’s general rules); and
 - (2) section 137T (General supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Handbook (Remuneration Consequentials) Instrument 2015

- D. The PRA makes the rules in Annexes A and B to this instrument.

Commencement

- E. This instrument comes into force on 1 July 2015.

Amendments to the PRA Handbook

- F. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- G. The Senior Management Arrangements, Systems and Controls sourcebook (SYSC) is amended in accordance with Annex B to this instrument.

Citation

- H. This instrument may be cited as the Handbook (Remuneration Consequentials) Instrument 2015.

By order of the Board of the Prudential Regulation Authority

19 June 2015

Annex A

Amendments to the Glossary of Definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Amend the following definitions as shown:

discretionary pension benefit (A) ~~In the PRA Handbook:~~

~~(in SYSC 19A) enhanced pension benefits granted on a discretionary basis by a firm to an employee as part of that employee's variable remuneration package, but excluding accrued benefits granted to an employee under the terms of his company pension scheme. [deleted]~~

~~[Note: article 4(49) of the *Banking Consolidation Directive*]~~

(B) In the FCA Handbook:

...

investment firm (A) In the PRA Handbook:

...

~~(5) (in SYSC 19A) a firm in (3) except for a BIPRU firm [deleted]~~

(B) In the FCA Handbook:

...

parent undertaking (A) In the PRA Handbook:

(1) ...

(c) (for the purposes of *BIPRU* (except *BIPRU* 12), *GENPRU* (except *GENPRU* 3) and *INSPRU* as they apply on a consolidated basis and for the purposes of *SYSC* 12 (Group risk systems and controls requirement) ~~and SYSC 19C (Remuneration Code for BIPRU firms)~~ and in relation to whether an *undertaking* is a *parent undertaking*) an *undertaking* which has the following relationship to another *undertaking* ("S"):

(i) a relationship described in (a) other than (a)(vii); or

- (ii) it effectively exercises a dominant influence over S;

and so that (a)(v) does not apply for the purpose of *BIPRU* as it applies on a consolidated basis (including *BIPRU* 8 (Group risk - consolidation)) or *BIPRU* 10.

(2) ...

- (3) (for the purposes of *GENPRU* 3, *BIPRU* 12, and *IFPRU* ~~and *SYSC* 19A (Remuneration Code)~~) has the meaning in article 4(1)(15) of the *EU CRR* but so that (in accordance with article 2(9) of the *Financial Groups Directive*) article 4(1)(15)(b) applies for the purpose of *GENPRU* 3.

(B) In the FCA Handbook:

...

...

Remuneration Code ~~*SYSC* 19A (Remuneration Code)~~[deleted]

Remuneration Code general requirement ~~*SYSC* 19A.2.1R~~[deleted]

Remuneration Code staff (A) ~~In the PRA Handbook:~~

~~(for a *CRR* firm and an overseas firm in *SYSC* 19A1.1.1R(1)(f)) has the meaning given in *SYSC* 19A.3.4R~~ [deleted]

(B) In the FCA Handbook:

...

remuneration principles proportionality rule ~~(in *SYSC* 19A) has the meaning given in *SYSC* 19A.3.3R.~~ [deleted]

Annex B

Amendments to the Senior Management Arrangements, Systems and Controls sourcebook (SYSC)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 Application and purpose

1.1A Application

...

- 1.1A.1 G The application of this sourcebook is summarised at a high level in the following table. The detailed application is set out in SYSC 1 Annex 1 and in the text of each chapter.

Type of firm	Applicable chapters
<i>Insurer</i>	Chapters 2, 3, 11 to 18, 21
<i>Managing agent</i>	Chapters 2, 3, 11, 12, 18, 21
<i>Society</i>	Chapters 2, 3, 12, 18, 21
Every other <i>firm</i>	Chapters 4 to 12, 18, 19A, <u>19D,</u> and 21

Firms that SYSC 19D applies to should also refer to the Remuneration part of the PRA Rulebook

...

1.4 Application of SYSC 11 to SYSC 21

...

- 1.4.1A R SYSC 12, SYSC 19A, SYSC 19D, SYSC 20 and SYSC 21 do not apply to a *firm* in relation to its carrying on of *auction regulation bidding*.

- 1.4.1B G Apart from SYSC 12, SYSC 19A, SYSC 19D, SYSC 20 and SYSC 21 which are disapplied by SYSC 1.4.1A R, the other chapters of SYSC 11 to SYSC 17 do not apply in relation to a *firm's* carrying on of *auction regulation bidding* because they only apply to an *insurer*. SYSC 18 provides guidance on the Public Interest Disclosure Act.

...

4 General organisational requirements

4.1 General Requirements

...

4.1.2 R For a *common platform firm*, the arrangements, processes and mechanisms referred to in SYSC 4.1.1R must be comprehensive and proportionate to the nature, scale and complexity of the risks inherent in the business model and of the *common platform firm's* activities and must take into account the specific technical criteria described in SYSC 4.1.7R, SYSC 5.1.7R, SYSC 7 ~~(for a firm to which SYSC 19A applies)~~ SYSC 19A or for a *full scope UK AIFM*) SYSC 19 Band whichever of the following as applicable:

- (1) (for a firm to which SYSC 19A applies) SYSC 19A (IFPRU Remuneration Code);
- (2) (for a full-scope UK AIFM) SYSC 19B (AIFM Remuneration Code);
- (3) (for a firm to which SYSC 19C applies) SYSC 19C (BIPRU Remuneration Code);
- (4) (for a firm to which SYSC 19D applies) SYSC 19D (Dual-regulated firms Remuneration Code); or
- (5) (for a firm to which the Remuneration part of the PRA Rulebook applies) the Remuneration part of the PRA Rulebook.

...

6 Compliance, internal audit and financial crime

6.1 Compliance

...

6.1.4-A G In setting the method of determining the *remuneration of relevant persons* involved in the compliance function:

- (1) *firms that SYSC 19A applies to will also need to comply with the Remuneration Code; and*
- (2) *BIPRU firms will also need to comply with the BIPRU Remuneration Code;*
- (3) *firms that SYSC 19D applies to will also need to comply with the Dual-regulated firms Remuneration Code; and*
- (4) *firms that the Remuneration part of the PRA Rulebook applies to will also need to comply with it.*

...

7 Risk control

7.1 Risk control

7.1.7B G In setting the method of determining the *remuneration of employees* involved in the risk management function;

...

(1) *firms that SYSC ~~19A~~ 19D applies to will also need to comply with the Dual-regulated firms Remuneration Code; and*

(2) *firms that the Remuneration part of the PRA Rulebook applies to will also need to comply with it.*

...

12 Group risk systems and control requirements

12.1 Application

...

CRR firms and non-CRR firms that are parent financial holding companies in a Member State

12.1.13 R If this *rule* applies under SYSC 12.1.14 R to a *firm*, the *firm* must:

...

(2) ensure that the risk management processes and internal control mechanisms at the level of any *consolidation group* or non-EEA *sub-group* of which it is a member comply with the obligations set out in the following provisions on a consolidated (or sub-consolidated) basis:

...

(dA) *the Remuneration Code or the Dual-regulated Firms Remuneration Code, whichever is applicable;*

...

...

21.1 Risk control: guidance on governance arrangements

...

Chief Risk Officer

21.1.2 G

(1) A Chief Risk Officer should:

...

- (j) provide risk-focused advice and information into the setting and individual application of the *firm's remuneration* policy (Where the *Remuneration Code* applies, see in particular SYSC 19A.3.15 E. Where the BIPRU Remuneration Code applies, see in particular SYSC 19C.3.15E. Where the *Dual-regulated Remuneration Code* applies, see in particular SYSC 19D.2.16E. Where the Remuneration part of the *PRA Rulebook* applies, see the *PRA's Supervisory Statement on Remuneration*).

[Note: The *PRA's Supervisory Statement on remuneration* is available on the *PRA* website at

<http://www.bankofengland.co.uk/pr/Pages/default.aspx>.]

...

SYSC 19A is deleted in its entirety. This text is not shown.

SYSC TP3 Remuneration Code is deleted in its entirety. This text is not shown.

**SENIOR MANAGEMENT ARRANGEMENTS, SYSTEMS AND CONTROLS
(REMUNERATION CODE) (NO 6) INSTRUMENT 2015**

Powers exercised

- A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1)
 - (a) section 137A (The FCA’s general rules);
 - (b) section 137H (General rules about remuneration);
 - (c) section 137T (General supplementary powers);
 - (d) section 138C (Evidential provisions);
 - (e) section 138D (Action for damages); and
 - (f) section 139A (Power of the FCA to give guidance); and
 - (2) the other rule and guidance making powers listed in Schedule 4 (Powers exercised) to the General Provisions of the FSA’s Handbook.
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 1 July 2015.

Amendments to the Handbook

- D. The modules of the FCA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes in this instrument listed in column (2) below.

(1)	(2)
Glossary of definitions	Annex A
Senior Management Arrangements, Systems and Controls sourcebook (SYSC)	Annex B
Supervision manual (SUP)	Annex C

Notes

- E. In the Annexes to this instrument, the “notes” (indicated by “**Note:**”) are included for the convenience of readers but do not form part of the legislative text.

Citation

- F. This instrument may be cited as the Senior Management Arrangements, Systems and Controls (Remuneration Code) (No 6) Instrument 2015.

By order of the Board of the Financial Conduct Authority
4 June 2015

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definitions and amendments in the appropriate alphabetical position. The text is not underlined

<i>dual-regulated firm</i>	(in SYSC 19D) a <i>firm</i> that is <i>bank</i> , a <i>building society</i> or a <i>UK designated investment firm</i> .
<i>dual-regulated firms Remuneration Code</i>	SYSC 19D (Dual-regulated firms Remuneration Code) for <i>dual-regulated firms</i> and <i>overseas firms</i> in SYSC 19D.1.1R(1)(d) that would have been a <i>bank</i> , <i>building society</i> or <i>UK designated investment firm</i> if it had been a <i>UK domestic firm</i> .
<i>dual-regulated firms Remuneration Code staff</i>	(in relation to a <i>dual-regulated firm</i> and an <i>overseas firm</i> in SYSC 19D.1.1R(1)(d) that would have been a <i>bank</i> , <i>building society</i> or <i>UK designated investment firm</i> if it had been a <i>UK domestic firm</i>) has the meaning in SYSC 19D.3.4R which is, in summary, an <i>employee</i> whose professional activities have a material impact on the <i>firm's</i> risk profile, including any <i>employee</i> who is deemed to have a material impact on the <i>firm's</i> risk profile in accordance with Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers).
<i>dual-regulated firms remuneration principles proportionality rule</i>	SYSC 19D.3.3R which, in summary, requires a <i>dual-regulated firm</i> to apply the remuneration principles for <i>dual-regulated firms</i> in SYSC 19D proportionate to its size, internal organisation and the nature, the scope and the complexity of its activities.
<i>EBA</i>	European Banking Authority.

Amend the following definitions as shown:

<i>discretionary pension benefit</i>	...
	(2) (in <i>IFPRU</i> , and SYSC 19A (IFPRU Remuneration Code) and SYSC 19D (Dual-regulated firms Remuneration Code) has the meaning in article 4(1)(73) of the <i>EU CRR</i> .
<i>investment firm</i>	...

	...
	(5) (in SYSC 19A (<u>IFPRU Remuneration Code</u>)) a <i>firm</i> in (3).
	(6) (<u>in SYSC 19D (Dual-regulated firms Remuneration Code)</u>) a <i>firm</i> in (3) that is a <u>UK designated investment firm</u> .
parent undertaking	...
	(3) (for the purposes of <i>GENPRU 3</i> , <i>BIPRU 12</i> , <i>IFPRU</i> , and <u>SYSC 19A (IFPRU Remuneration Code) and SYSC 19D (Dual-regulated firms Remuneration Code)</u>) has the meaning in article 4(1)(15) of the <i>EU CRR</i> but so that (in accordance with article 2(9) of the <i>Financial Groups Directive</i>) article 4(1)(15)(b) applies for the purpose of <i>GENPRU 3</i> .
Remuneration Code	<u>SYSC 19A (IFPRU Remuneration Code) for IFPRU investment firms and overseas firms in SYSC 19A.1.1R(1)(d) that would have been an IFPRU investment firm if it had been a UK domestic firm.</u>
Remuneration Code staff	...
	(for a CRR firm <u>an IFPRU investment firm and an overseas firm in SYSC 19A.1.1R(1)(d)</u>) that would have been an <u>IFPRU investment firm if it had been a UK domestic firm</u>) has the meaning given in <u>SYSC 19A.3.4R which is, in summary, an employee whose professional activities have a material impact on the firm's risk profile, including any employee who is deemed to have a material impact on the firm's risk profile in accordance with Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers).</u>
UK designated investment firm	...
	(in <i>BIPRU 12</i> and <u>SYSC 19D</u>) a <i>designated investment firm</i> which is a <i>body corporate</i> or <i>partnership</i> formed under the law of any part of the <i>UK</i> .

Annex B

Amendments to the Senior Management Arrangements, Systems and Controls sourcebook (SYSC)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 Application and purpose

1.1A Application

- 1.1A.1 G The application of this sourcebook is summarised at a high level in the following table. The detailed application is cut back in SYSC 1 Annex 1 and in the text of each chapter.

Type of firm	Applicable chapters
<i>Insurer</i>	Chapters 2, 3, 11 to 18, 21
<i>Managing agent</i>	Chapters 2, 3, 11, 12, 18, 21
<i>Society</i>	Chapters 2, 3, 12, 18, 21
Every other <i>firm</i>	Chapters 4 to 12, 18, 19A , <u>19D</u> , 21

Firms that SYSC 19D applies to should also refer to the Remuneration part of the PRA Rulebook.

- 1.1A.1A G The application of this sourcebook to *firms* that are not *PRA-authorised persons* is summarised at a high level in the following table. The detailed application is cut back in SYSC 1 Annex 1 and in the text of each chapter.

<u>Type of firm</u>	<u>Applicable chapters</u>
<u><i>Full-scope UK AIFM</i></u>	<u>Chapter 19B, 21</u>
<u><i>BIPRU firm (including a third-country BIPRU firm)</i></u>	<u>Chapters 4 to 10, 12, 18, 19C, 21</u>
<u><i>IFPRU investment firm (including an overseas firm that would have been an IFPRU investment firm if it had been a UK domestic firm)</i></u>	<u>Chapters 4 to 10, 12, 18, 19A, 21</u>

...

1.4 Application of SYSC 11 to SYSC 21

...

- 1.4.1A R *SYSC 12, SYSC 19A, SYSC 19D, SYSC 20 and SYSC 21 do not apply to a firm in relation to its carrying on of auction regulation bidding.*
- 1.4.1B G *Apart from SYSC 12, SYSC 19A, SYSC 19D, SYSC 20, and SYSC 21, which are disapplied by SYSC 1.4.1AR, the other chapters of SYSC 11 to SYSC 17 do not apply in relation to a firm's carrying on of auction regulation bidding because they only apply to an insurer. SYSC 18 provides guidance on the Public Interest Disclosure Act.*

...

4 General organisational requirements

4.1 General requirements

...

- 4.1.2 R *For a common platform firm, the arrangements, processes and mechanisms referred to in SYSC 4.1.1R must be comprehensive and proportionate to the nature, scale and complexity of the risks inherent in the business model and of the common platform firm's activities and must take into account the specific technical criteria described in SYSC 4.1.7R, SYSC 5.1.7R, SYSC 7 and ~~(for a firm to which SYSC 19A applies) SYSC 19A or (for a full-scope UK AIFM) SYSC 19B~~ whichever of the following as applicable:*
- (1) (for a firm to which SYSC 19A applies) SYSC 19A (IFPRU Remuneration Code);*
 - (2) (for a full-scope UK AIFM) SYSC 19B (AIFM Remuneration Code);*
 - (3) (for a firm to which SYSC 19C applies) SYSC 19C (BIPRU Remuneration Code);*
 - (4) (for a firm to which SYSC 19D applies) SYSC 19D (Dual-regulated firms Remuneration Code); or*
 - (5) (for a firm to which the remuneration part of the PRA Rulebook applies) the remuneration part of the PRA Rulebook.*

...

6 Compliance, internal audit and financial crime

6.1 Compliance

...

6.1.4-A G In setting the method of determining the *remuneration of relevant persons* involved in the compliance function:

- (1) *firms that SYSC 19A applies to will also need to comply with the Remuneration Code; and*
- (2) *BIPRU firms will also need to comply with the BIPRU Remuneration Code;*
- (3) *firms that SYSC 19D applies to will also need to comply with the dual-regulated firms Remuneration Code; and*
- (4) *firms that the remuneration part of the PRA Rulebook applies to will also need to comply with it.*

...

7 Risk control

7.1 Risk control

...

7.1.7B G In setting the method of determining the *remuneration of employees* involved in the risk management function;

- (1) *firms that SYSC ~~19A~~ 19D applies to will also need to comply with the dual-regulated firms Remuneration Code; and*

...

- (2) *firms that the remuneration part of the PRA Rulebook applies to will also need to comply with it.*

7.1.7BC G In setting the method of determining the *remuneration of employees* involved in the risk management function, *firms that SYSC 19A applies to will also need to comply with the Remuneration Code.*

...

12 Group risk systems and control requirements

12.1 Application

...

CRR firms and non-CRR firms that are parent financial holding companies in a Member State

- 12.1.13 R If this *rule* applies under SYSC 12.1.14R to a *firm*, the *firm* must:
- ...
- (2) ensure that the risk management processes and internal control mechanisms at the level of any *consolidation group* or non-EEA *sub-group* of which it is a member comply with the obligations set out in the following provisions on a consolidated (or sub-consolidated) basis:
- ...
- (dA) the Remuneration Code or the dual-regulated firms Remuneration Code, whichever is applicable;
- ...
- ...

19A **IFPRU Remuneration Code**

19A.1 **General application and purpose**

Who? What? Where?

- 19A.1.1 R (1) The *Remuneration Code* applies to :
- (a) ~~a *building society*; [deleted]~~
- (b) ~~a *bank*; [deleted]~~
- (c) an *IFPRU investment firm*;
- (d) an *overseas firm* that;
- ...
- ...

19A.3 **Remuneration principles for banks, building societies and IFPRU investment firms**

...

- 19A.3.4 R ~~*Remuneration Code staff* comprises categories of staff including senior management, risk takers, staff engaged in control functions and any~~

~~employee receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers, whose professional activities have a material impact on the firm's risk profile.~~

- (1) Remuneration Code staff comprises:
- (a) an employee of an IFPRU investment firm whose professional activities have a material impact on the firm's risk profile, including any employee who is deemed to have a material impact on the firm's risk profile in accordance with Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers); or
 - (b) subject to (2) and (3), an employee of an overseas firm in SYSC 19A1.1.1R(1)(d) (i.e., an overseas firm that would have been an IFPRU investment firm if it had been a UK domestic firm) whose professional activities have a material impact on the firm's risk profile, including any employee who would meet any of the criteria set out in articles 3 or 4(1) of Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers) if it had applied to him.
- (2) An overseas firm in SYSC 19A1.1.1R(1)(d) (i.e., an overseas firm that would have been an IFPRU investment firm if it had been a UK domestic firm) may deem an employee not to be Remuneration Code staff where:
- (a) the employee:
 - (i) would meet the criteria in article 4(1) of Regulation (EU) No 604/2014 of 4 March 2014;
 - (ii) would not meet any of the criteria in article 3 of Regulation (EU) No 604/2014 of 4 March 2014;
and
 - (iii) was awarded total remuneration of less than €750,000 in the previous year;

and
 - (b) the overseas firm determines that the professional activities of the employee do not have a material impact on its risk profile on the grounds described in article 4(2) of Regulation (EU) 604/2014 of 4 March 2014.
- (3) Where the overseas firm deems an employee not to be Remuneration Code staff as set out in (2), it must notify the FCA, applying the approach described in article 4(4) of Regulation

(EU) 604/2014 of 4 March 2014.

[**Note:** article 92(2) of *CRD* and articles 3 and 4 of Regulation (EU) No 604/2014 of 4 March 2014.]

19A.3.4A G Where an overseas firm in SYSC 19A1.1.1R(1)(d) (i.e., an overseas firm that would have been a IFPRU investment firm if it had been a UK domestic firm) wishes to deem an employee who earns more than €750,000 not to be Remuneration Code staff, the overseas firm may apply for a waiver of the requirement in SYSC 19A.3.4R in respect of that employee.

...

Remuneration Principle 12(d): Remuneration structures - ratios between fixed and variable components of total remuneration

19A.3.44 R A firm must set an appropriate ratios ratio between the fixed and variable components of total remuneration and ensure that:

...

- (2) the level of the fixed component represents a sufficiently high proportion of the total remuneration to allow the operation of a fully flexible policy on variable remuneration components, including the possibility to pay no variable remuneration component; and
- (3) subject to SYSC 19A.3.44AR, the ratio level of the variable component of total remuneration must not exceed 100% of the fixed component of total remuneration for each Remuneration Code staff does not exceed 1:1.

[**Note:** ~~Paragraph 23(1) of Annex V to the Banking Consolidation Directive and~~ article 94(1)(f) and 94(1)(g)(i) of the CRD]

19A.3.44A R A firm may set a higher maximum level of the ratio between the fixed and ~~the~~ variable components of total remuneration ~~that exceeds 1:1~~ provided ~~the ratio:~~

- (1) ~~does not exceed 1:2~~ the overall level of the variable component does not exceed 200% of the fixed component of the total remuneration for each Remuneration Code staff; and

...

19A.3.44B R A firm must ensure that any approval by ~~the~~ its shareholders or owners or members ~~of the firm~~ for the purposes of SYSC 19A.3.44AR of a ratio that exceeds 1:1 is carried out in accordance with the following procedure:

- (1) the firm must give reasonable notice to all its shareholders or owners or members ~~of the firm~~ that the firm intends of its intention to seek approval of a ratio that exceeds 1:1 the proposed higher

ratio;

- (2) the *firm* must make a detailed recommendation to all its shareholders or owners or members ~~of the *firm* giving the reasons for, and the scope of, the approval sought, including the number of staff affected, their functions and the expected impact on the requirement to maintain a sound capital base; that includes:~~
- (a) the reasons for, and the scope of, the approval sought;
 - (b) the number of staff affected and their functions; and
 - (c) the expected impact on the requirement to maintain a sound capital base;
- (3) the *firm* must, ~~without delay, inform the *appropriate regulator* of the recommendation to its shareholders or owners or members, including the proposed ratio and the reasons therefor and must demonstrate to the *appropriate regulator* that the proposed higher ratio does not conflict with the *firm's* obligations under the *CRD* and the *CRR*, having regard in particular to the *firm's* own funds obligations;~~
- (a) without delay, inform the *FCA* of the recommendation to its shareholders or owners or members, including the proposed higher ratio and the reasons therefor; and
 - (b) demonstrate to the *FCA* that the proposed higher ratio does not conflict with its obligations under the *CRD* and the *EU CRR*, having particular regard to the *firm's* own funds obligations;
- ...
- (5) the higher ratio is approved by a majority of:
- (a) ~~at least 66% of shareholders or owners or members of the *firm* the shares or equivalent ownership rights represented, provided that if at least 50% of the shareholders or owners or members shares or equivalent ownership rights in the *firm* are represented; or~~
 - (b) ~~at least 75% of shareholders or owners or members of the *firm* the shares or equivalent ownership rights represented, if less than 50% of the shareholders, members or owners shares or equivalent ownership rights in the *firm* are represented.~~

[Note: article 94(1)(g)(ii) of the *CRD*]

...

19A.3.44E R In applying the discount rate in SYSC 19A.3.44DR, a *firm* must apply the *EBA Guidelines on the applicable notional discount rate for variable remuneration published on 27 March 2014.*

[Note: the *EBA Guidelines on the applicable notional discount rate for variable remuneration* can be found at:

<http://www.eba.europa.eu/documents/10180/643987/EBA-GL-2014-01+%28Final+Guidelines+on+the+discount+rate+for+remuneration%29.pdf/e8b3b3f6-6258-439d-a2d9-633e6e5de5e9>]

...

19A.3.54 R ...

(1B) Condition 1 is that the *firm* is a ~~*UK bank, a building society, a designated investment firm, or a relevant IFPRU 730k firm*~~ that has relevant total assets exceeding £50 billion.

...

(1D) Condition 2 is that the *firm*:

(a) is a ~~*full credit institution, a designated investment firm, a relevant IFPRU 730k firm*~~ or a relevant *third country IFPRU 730k firm*; and

(b) is part of a *group* containing a *firm* that has relevant total assets exceeding £50 billion and that is a ~~*UK bank, a building society, a designated investment firm*~~ or a relevant *IFPRU 730k firm*.

...

After SYSC 19C (BIPRU Remuneration Code) insert the following new section. The text is not underlined.

19D Dual-regulated firms Remuneration Code

19D.1 Application and purpose

Who? What? Where?

19D.1.1 R (1) The *dual-regulated firms Remuneration Code* applies to:

(a) a *building society*;

(b) a *bank*;

- (c) a *UK designated investment firm*;
- (d) an *overseas firm* that;
 - (i) is not an *EEA firm*;
 - (ii) has its head office outside the *EEA*; and
 - (iii) would be a *firm* in (a), (b) or (c) if it had been a *UK domestic firm*, had carried on all of its business in the *United Kingdom* and had obtained whatever authorisations for doing so as are required under the *Act*.

- (2) For a *firm* which falls under (1)(a), (1)(b) or (1)(c), the *dual-regulated firms Remuneration Code* applies, in a *prudential context*, in relation to:
 - (a) its *UK* activities;
 - (b) its *passported activities* carried on from a *branch* in another *EEA State*; and
 - (c) a *UK domestic firm's* activities wherever they are carried on.
- (3) For a *firm* that falls under (1)(d), the *dual-regulated firms Remuneration Code* applies only in relation to activities carried on from an establishment in the *United Kingdom*.

19D.1.2 R Subject to the provisions on group risk systems and controls requirements in SYSC 12 (Group risk systems and controls requirements), the *dual-regulated firms Remuneration Code*:

- (1) applies in relation to *regulated activities*, activities that constitute *dealing in investments as principal* (disregarding the exclusion in article 15 of the *Regulated Activities Order* (Absence of holding out etc)), *ancillary activities* and (in relation to *MiFID business*) *ancillary services*;
- (2) applies in relation to the carrying on of *unregulated activities* in a *prudential context*; and
- (3) takes into account activities of other *group* members.

When?

19D.1.3 R (1) Except as set out in (2) and (3), a *firm* must apply the *remuneration* requirements in SYSC 19D.3 (Remuneration principles) in relation to:

- (a) *remuneration* awarded, whether pursuant to a contract or otherwise, on or after 1 January 2011;
- (b) *remuneration* due on the basis of contracts concluded before 1 January 2011 which is awarded or paid on or after 1 January 2011; and
- (c) *remuneration* awarded, but not yet paid, before 1 January 2011, for services provided in 2010.

[**Note:** article 3(2) of Directive 2010/76/EU]

- (2) A *firm* must apply the *remuneration* requirements in SYSC 19D.3.48R(3) (1:1 ratio of variable to fixed components) and SYSC 19.3.49R (1:2 ratio of fixed to variable components) in relation to *remuneration* awarded for services provided or performance from the year 2014 onwards, whether due on the basis of contracts concluded before, on or after 31 December 2013.

[**Note:** article 162(3) of CRD]

- (3) A *firm* must apply the *remuneration* requirements in SYSC 19D.3.59R(1)(b), SYSC 19D.3.61R(2), SYSC 19D.3.61R(3), SYSC 19D.3.61R(4), SYSC 19D.3.61R(5), SYSC 19D.3.64R and SYSC 19D.3.67R(1)(c) in relation to variable *remuneration* awarded in relation to the performance year starting on or after 1 January 2016.

19D.1.4 G Subject to SYSC 19D.1.5R, SYSC 19D.1.3R does not require a *firm* to breach requirements of applicable contract or employment law.

[**Note:** recital 14 of Directive 2010/76/EU]

Conflict with other obligations

- 19D.1.5 R
- (1) Where a *firm* is unable to comply with the *dual-regulated firms Remuneration Code* because to do so would breach a provision of a prior contract (including a provision in a contract with a *dual-regulated firms Remuneration Code staff member*), it must take reasonable steps to amend or to terminate the provision in question in a way which enables it to comply with the *dual-regulated firms Remuneration Code* at the earliest opportunity.
 - (2) Until the provision in (1) ceases to prevent the *firm* from complying with the *dual-regulated firms Remuneration Code*, it must adopt specific and effective arrangements, processes and mechanisms to manage the risks raised by the provision.

Purpose

- 19D.1.6 G
- (1) The aim of the *dual-regulated firms Remuneration Code* is to ensure that *firms* have risk-focused *remuneration* policies, which

are consistent with and promote effective risk management and do not expose them to excessive risk. It expands upon the general organisational requirements in SYSC 4.

- (2) The *dual-regulated firms Remuneration Code* implements the main provisions of the *CRD* which relate to *remuneration*. The Committee of European Banking Supervisors published Guidelines on Remuneration Policies and Practices on 10 December 2010. Provisions of the Capital Requirements Regulations 2013 (SI 2013/3115) together with the *EBA*'s Guidelines to article 75 of the *CRD* relating to the collection of *remuneration* benchmarking information and high earners information have been implemented through *SUP* 16 Annex 33AR and *SUP* 16 Annex 34AR. The Guidelines can be found at <http://www.eba.europa.eu/documents/10180/757286/EBA-GL-2014-08+%28GLs+on+remuneration+benchmarking+%29.pdf/9d87c18b-ed79-4ceb-a3f6-64928cc26065> and <http://www.eba.europa.eu/documents/10180/757283/EBA-GL-2014-07+%28GLs+on+high+earners+data+collection%29.pdf/da42488f-09c1-4558-ae4e-6258e11b8345>.

Notifications to the FCA

- 19D.1.7 G (1) The *dual-regulated firms Remuneration Code* does not contain specific notification requirements. However, general circumstances in which the *FCA* expects to be notified by *firms* of matters relating to their compliance with requirements under the *regulatory system* are set out in *SUP* 15.3 (General notification requirements).
- (2) For *remuneration* matters in particular, those circumstances should take into account *unregulated activities*, as well as *regulated activities* and the activities of other members of a *group*, and would include each of the following:
- (a) significant breaches of the *dual-regulated firms Remuneration Code*, including any breach of a *rule* to which the provisions on voiding and recovery in SYSC 19D Annex 1 apply;
 - (b) any proposed *remuneration* policies, procedures or practices which could:
 - (i) have a significant adverse impact on the *firm*'s reputation; or
 - (ii) affect the *firm*'s ability to continue to provide adequate services to its *customers* and which could result in serious detriment to a *customer* of the *firm*;

or

- (iii) result in serious financial consequences to the *financial system* or to other *firms*;
 - (c) any proposed changes to *remuneration* policies, practices or procedures which could have a significant impact on the *firm's* risk profile or resources;
 - (d) fraud, errors and other irregularities described in SUP 15.3.17R (notification of fraud, errors and other irregularities) which may suggest weaknesses in, or be motivated by, the *firm's remuneration* policies, procedures or practices.
- (3) Notifications should be made immediately as the *firm* becomes aware or has information which reasonably suggests that those circumstances have occurred, may have occurred or may occur in the foreseeable future.

Individual guidance

- 19D.1.8 G The *FCA's* policy on individual *guidance* is set out in SUP 9. *Firms* should particularly note the policy on what the *FCA* considers to be a reasonable request for *guidance* (see SUP 9.2.5G). For example, where a *firm* is seeking *guidance* on a proposed *remuneration* structure, the *FCA* will expect the *firm* to provide a detailed analysis of how the structure complies with the *dual-regulated firms Remuneration Code*, including the general requirement for *remuneration* policies, procedures and practices to be consistent with, and promote, sound and effective risk management.

Interpretation

- 19D.1.9 G Except as provided in the *Glossary*, any expression used in, or for the purpose of, this chapter which is defined or used in *EU CRR* has the meaning given by, or used in, those Regulations.

19D.2 General requirement

Remuneration policies must promote effective risk management

- 19D.2.1 R A *firm* must establish, implement and maintain *remuneration* policies, procedures and practices that are consistent with, and promote, sound and effective risk management.

[**Note:** article 74(1) of *CRD*]

- 19D.2.2 G (1) The *dual-regulated firms Remuneration Code* covers all aspects of *remuneration* that could have a bearing on effective risk

management, including salaries, bonuses, long-term incentive plans, options, hiring bonuses, severance packages and pension arrangements.

- (2) As with other aspects of a *firm's* systems and controls, in accordance with SYSC 4.1.2R (general organisational requirements) *remuneration* policies, procedures and practices must be comprehensive and proportionate to the nature, scale and complexity of the *common platform firm's* activities. What a *firm* must do in order to comply with the *dual-regulated firms Remuneration Code* will therefore vary. For example, while the *dual-regulated firms Remuneration Code* refers to a *firm's remuneration committee* and risk management function, it may be appropriate for the *governing body* of a smaller *firm* to act as the *remuneration committee* and for the *firm* not to have a separate risk management function.
- (3) The *FCA* may also ask *remuneration committees* to provide it with evidence of how well the *firm's* remuneration policies meet the *dual-regulated firms Remuneration Code's* principles, together with plans for improvement where there is a shortfall. The *FCA* also expects relevant *firms* to use the principles in assessing their exposure to risks arising from their *remuneration* policies as part of the *internal capital adequacy assessment process (ICAAP)*.
- (4) The *FCA* would also expect *firms* to apply, on a *firm-wide* basis, at least the following principles relating to:
 - (a) risk management and risk tolerance (Remuneration Principle 1);
 - (b) supporting business strategy, objectives, values and long-term interests of the firm (Remuneration Principle 2);
 - (c) avoiding conflicts of interest (Remuneration Principle 3);
 - (d) governance (Remuneration Principle 4);
 - (e) risk adjustment (Remuneration Principle 8);
 - (f) pension policy (Remuneration Principle 9);
 - (g) personal investment strategies (Remuneration Principle 10);
 - (h) payments related to early termination (Remuneration Principle 12(e)); and
 - (i) deferral (Remuneration Principle 12(g)).

Record keeping

- 19D.2.3 R In line with the record-keeping requirements in SYSC 9, a *firm* must ensure that its *remuneration* policies, practices and procedures, including performance appraisals processes and decisions, are clear and documented.

Interpretation of references to remuneration

- 19D.2.4 R (1) In this chapter, references to *remuneration* include *remuneration* paid, provided or awarded by any *person* to the extent that it is paid, provided or awarded in connection with *employment* by a *firm*.
- (2) Paragraph (1) is without prejudice to the meaning of *remuneration* elsewhere in the *Handbook*.
- 19D.2.5 G For example, *remuneration* includes payments made by a seconding organisation which is not subject to the *dual-regulated firms Remuneration Code* to a secondee in respect of their *employment* by a *firm* which is subject to the *dual-regulated firms Remuneration Code*.

19D.3 Remuneration principles

Application: groups

- 19D.3.1 R (1) A *firm* must apply the requirements of this section at *group*, *parent undertaking* and *subsidiary undertaking* levels, including those *subsidiaries* established in a country or territory which is not an *EEA State*.
- (2) Paragraph (1) does not limit SYSC 12.1.13R(2)(dA) (which relates to the application of the *dual-regulated firms Remuneration Code* within *UK consolidation groups* and *non-EEA sub-groups*).

[**Note:** article 92(1) of *CRD*]

- 19D.3.2 G SYSC 12.1.13R(2)(dA) requires the *firm* to ensure that the risk management processes and internal control mechanisms at the level of any *UK consolidation group* or *non-EEA sub-group* of which a *firm* is a member, comply with the obligations in this section on a consolidated basis (or sub-consolidated basis).

Application: categories of staff and proportionality

- 19D.3.3 R (1) This section applies in relation to *dual-regulated firms Remuneration Code staff*, except as set out in (3).
- (2) When establishing and applying the total *remuneration* policies for *dual-regulated firms Remuneration Code staff*, a *firm* must comply with this section in a way, and to the extent, that is appropriate to

its size, internal organisation and the nature, the scope and the complexity of its activities (the *dual-regulated firms remuneration principles proportionality rule*).

- (3) Paragraphs (1) and (2) do not apply to the requirement for significant *firms* to have a *remuneration committee* (SYSC 19D.3.12R).

[**Note:** article 92(2) of *CRD*]

[**Note:** In addition to the *guidance* in this section about the *dual-regulated firms remuneration principles proportionality rule*, the *FSA* gave guidance on the division of *firms* into categories for the purpose of providing a framework for the operation of the *dual-regulated firms remuneration principles proportionality rule*. This *guidance* is available on the *FCA* website at <https://www.fca.org.uk/firms/being-regulated/remuneration-codes>.]

- 19D.3.4 R (1) *Dual-regulated firms Remuneration Code staff* comprises:
- (a) an *employee* of a *dual-regulated firm* whose professional activities have a material impact on the *firm's* risk profile, including any *employee* who is deemed to have a material impact on the *firm's* risk profile in accordance with Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers); or
 - (b) subject to (2) and (3), an *employee* of an *overseas firm* in SYSC 19D.1.1R(1)(d) (i.e., an *overseas firm* that would have been a *bank, building society* or *UK designated investment firm* if it had been a *UK domestic firm*) whose professional activities have a material impact on the *firm's* risk profile, including any *employee* who would meet any of the criteria set out in articles 3 or 4(1) of Regulation (EU) 604/2014 of 4 March 2014 if it had applied to him.
- (2) An *overseas firm* in SYSC 19D1.1.1R(1)(d) (i.e., an *overseas firm* that would have been a *dual-regulated firm* if it had been a *UK domestic firm*) may deem an *employee* not to be a *dual-regulated firms Remuneration Code staff* where:
- (a) the *employee*:
 - (i) would meet the criteria in article 4(1) of Regulation (EU) No 604/2014 of 4 March 2014;
 - (ii) would not meet any of the criteria in article 3 of Regulation (EU) No 604/2014 of 4 March 2014; and

(iii) was awarded total remuneration of less than €750,000 in the previous year;

and

(b) the *overseas firm* determines that the professional activities of the *employee* do not have a material impact on its risk profile on the grounds described in article 4(2) of Regulation (EU) 604/2014 of 4 March 2014.

(3) Where the *overseas firm* deems an *employee* not to be *dual-regulated firms Remuneration Code staff* as set out in (2), it must notify the *FCA*, applying the approach described in article 4(4) of Regulation (EU) 604/2014 of 4 March 2014.

[**Note:** article 92(2) of *CRD* and articles 3 and 4 of Regulation (EU) No 604/2014 of 4 March 2014.]

19D.3.5 G Where an *overseas firm* in SYSC 19D1.1.1R(1)(d) (i.e., an *overseas firm* that would have been a *dual-regulated firm* if it had been a *UK domestic firm*) wishes to deem an *employee* who earns more than €750,000 not to be *dual-regulated firms Remuneration Code staff*, the *overseas firm* may apply for a *waiver* of the requirement in SYSC 19D.3.4R in respect of that *employee*.

19D.3.6 R A *firm* must:

- (1) maintain a record of its *dual-regulated firms Remuneration Code staff* under the general record-keeping requirements (SYSC 9); and
- (2) take reasonable steps to ensure that its *dual-regulated firms Remuneration Code staff* understand the implications of their status as such, including the potential for *remuneration* which does not comply with certain requirements of the *dual-regulated firms Remuneration Code* to be rendered void and recoverable by the *firm*.

Remuneration Principle 1: Risk management and risk tolerance

19D.3.7 R A *firm* must ensure that its *remuneration* policy is consistent with, and promotes, sound and effective risk management and does not encourage risk-taking that exceeds the level of tolerated risk of the *firm*.

[**Note:** article 92(2)(a) of *CRD*]

Remuneration Principle 2: Supporting business strategy, objectives, values and long-term interests of the firm

19D.3.8 R A *firm* must ensure that its *remuneration* policy is in line with the business strategy, objectives, values and long-term interests of the *firm*.

[**Note:** article 92(2)(b) of *CRD*]

Remuneration Principle 3: Avoiding conflicts of interest

- 19D.3.9 R A *firm* must ensure that its *remuneration* policy includes measures to avoid conflicts of interest.

[**Note:** article 92(2)(b) of *CRD*]

Remuneration Principle 4: Governance

- 19D.3.10 R A *firm* must ensure that its *management body* in its *supervisory function* adopts and periodically reviews the general principles of the *remuneration* policy and is responsible for overseeing its implementation.

[**Note:** article 92(2)(c) of *CRD* and Standard 1 of the *FSB Compensation Standards*]

- 19D.3.11 R A *firm* must ensure that the implementation of the *remuneration* policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for *remuneration* adopted by the *management body* in its *supervisory function*.

[**Note:** article 92(2)(d) of *CRD* and Standard 1 of the *FSB Compensation Standards*]

- 19D.3.12 R
- (1) A *firm* that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities must establish a *remuneration committee*.
 - (2) A *firm* in (1) must ensure that:
 - (a) the *remuneration committee* is constituted in a way that enables it to exercise competent and independent judgement on *remuneration* policies and practices and the incentives created for managing risk, capital and liquidity;
 - (b) the chairman and the members of the *remuneration committee* must be members of the *management body* who do not perform any executive function in the *firm*;
 - (c) the *remuneration committee* is responsible for the preparation of decisions regarding *remuneration*, including those which have implications for the risk and risk management of the *firm* and which are to be taken by the *management body*; and
 - (d) when preparing those decisions, the *remuneration committee* must take into account the long-term interests of shareholders, investors and other stakeholders in the *firm*

and the public interest.

[**Note:** article 95 of *CRD* and Standard 1 of the *FSB Compensation Standards*]

19D.3.13 R A *firm* that maintains a website must explain on the website how it complies with the *dual-regulated firms Remuneration Code*.

[**Note:** article 96 of the *CRD*]

- 19D.3.14 G
- (1) A *firm* should be able to demonstrate that its decisions are consistent with an assessment of its financial condition and future prospects. In particular, practices by which *remuneration* is paid for potential future revenues whose timing and likelihood remain uncertain should be evaluated carefully and the *governing body* or *remuneration committee* (or both) should work closely with the *firm's* risk function in evaluating the incentives created by its *remuneration* system.
 - (2) The *governing body* and any *remuneration committee* are responsible for ensuring that the *firm's* *remuneration* policy complies with the *dual-regulated firms Remuneration Code* and, where relevant, should take into account relevant guidance, such as that issued by the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors (IAIS) and the International Organization of Securities Commissions (IOSCO).
 - (3) Guidance on what the *supervisory function* might involve is set out in *SYSC* 4.3.3G (responsibility of senior personnel, in particular, the *supervisory function*).

Remuneration Principle 5: Control functions

19D.3.15 R A *firm* must ensure that *employees* engaged in control functions:

- (1) are independent from the business units they oversee;
- (2) have appropriate authority; and
- (3) are *remunerated*:
 - (a) adequately to attract qualified and experienced *employees*; and
 - (b) in accordance with the achievement of the objectives linked to their functions, independent of the performance of the business areas they control.

[**Note:** article 92(2)(e) of *CRD* and Standard 2 of the *FSB Compensation Standards*]

19D.3.16 E (1) A *firm's* risk management and compliance functions should have

appropriate input into setting the *remuneration* policy for other business areas. The procedures for setting *remuneration* should allow risk and compliance functions to have significant input into the setting of individual *remuneration* awards where those functions have concerns about the behaviour of the individuals concerned or the riskiness of the business undertaken.

- (2) Contravention of (1) may be relied on as tending to establish contravention of the *rule* on *employees* engaged in control functions having appropriate authority (*SYSC* 19D.3.15R(2)).

19D.3.17 R A *firm* must ensure that the *remuneration* of the senior officers in risk management and compliance functions is directly overseen by the *remuneration committee* referred to in *SYSC* 19D.3.12R or, if such a committee has not been established, by the *governing body* in its *supervisory function*.

[**Note:** article 92(2)(f) of *CRD*]

19D.3.18 G (1) This Remuneration Principle is designed to manage the conflicts of interest which might arise if other business areas had undue influence over the *remuneration* of *employees* within control functions. Conflicts of interest can easily arise when *employees* are involved in the determination of *remuneration* for their own business area. Where these could arise, they need to be managed by having in place independent roles for control functions (including, notably, risk management and compliance) and human resources. It is good practice to seek input from a *firm's* human resources function when setting *remuneration* for other business areas.

(2) The need to avoid undue influence is particularly important where *employees* from the control functions are embedded in other business areas. This Remuneration Principle does not prevent the views of other business areas being sought as an appropriate part of the assessment process.

(3) The *FCA* would generally expect the ratio of the potential variable component of *remuneration* to the fixed component of *remuneration* to be significantly lower for *employees* in risk management and compliance functions than for *employees* in other business areas whose potential bonus is a significant proportion of their *remuneration*. *Firms* should nevertheless ensure that the total *remuneration* package offered to those *employees* is sufficient to attract and retain staff with the skills, knowledge and expertise to discharge those functions. The requirement that the method of determining the *remuneration* of *relevant persons* involved in the compliance function must not compromise their objectivity or be likely to do so also applies (see *SYSC* 6.1.4R(4)).

Remuneration Principle 6: Remuneration and capital

19D.3.19 R A *firm* must ensure that total variable *remuneration* does not limit the *firm's* ability to strengthen its capital base.

[**Note:** article 94(1)(c) of the *CRD* and Standard 3 of the *FSB Compensation Standards*]

19D.3.20 G A *firm* should have variable *remuneration* arrangements that are sufficiently flexible to allow it to direct the necessary resources towards capital building.

Remuneration Principle 7: Exceptional government intervention

19D.3.21 R A *firm* that benefits from exceptional government intervention must ensure that:

- (1) variable *remuneration* is strictly limited as a percentage of net revenues when it is inconsistent with the maintenance of a sound capital base and timely exit from government support;
- (2) it restructures *remuneration* in a manner aligned with sound risk management and long-term growth, including (when appropriate) establishing limits to the *remuneration* of members of its *management body*; and
- (3) no variable or discretionary *remuneration* of any kind is paid to members of its *management body* unless this is justified.

[**Note:** article 93 of the *CRD* and Standard 10 of the *FSB Compensation Standards*]

19D.3.22 G The *FCA* would normally expect it to be appropriate for the ban on paying variable *remuneration* to members of the *management body* of a *firm* that benefits from exceptional government intervention to apply only to members of the *management body* who were in office at the time that the intervention was required.

Remuneration Principle 8: Profit-based measurement and risk adjustment

- 19D.3.23 R
- (1) A *firm* must ensure that any measurement of performance used to calculate variable *remuneration* components or pools of variable *remuneration* components:
 - (a) includes adjustments for all types of current and future risks and takes into account the cost and quantity of the capital and the liquidity required; and
 - (b) takes into account the need for consistency with the timing and likelihood of the *firm* receiving potential future revenues incorporated into current earnings.
 - (2) A *firm* must ensure that the allocation of variable *remuneration*

components within the *firm* also takes into account all types of current and future risks.

[**Note:** article 94(1)(j), (k) of the *CRD* and Standard 4 of the *FSB Compensation Standards*]

- 19D.3.24 G (1) This Remuneration Principle stresses the importance of risk adjustment in measuring performance, and the importance within that process of applying judgment and common sense. The *FCA* expects that a *firm* will apply qualitative judgements and common sense in the final decision about the performance-related components of variable *remuneration* pools.
- (2) A number of risk-adjustment techniques and measures are available, and a *firm* should choose those most appropriate to its circumstances.
- (3) We consider good practice in this area to be represented by those *firms* who provide a quantitative reference or starting point that explicitly includes risk-adjusted metrics, before the application of more discretionary factors. Common measures include those based on economic profit or economic capital. Whichever technique is chosen, the full range of future risks should be covered.
- (4) The *FCA* expects a *firm* to be able to provide it with details of all adjustments that the *firm* has made whether through application of formulae or the exercise of discretion. This will enable the *FCA* to ensure that the *firm's* risk adjustment framework is sufficiently robust. Where discretion has been applied, the *firm* should be able to provide a clear explanation for, and quantification of such adjustments.
- (5) A *firm* should ask the risk management function to validate and assess risk-adjustment techniques, and to attend a meeting of the *governing body* or *remuneration committee* for this purpose.
- 19D.3.25 R A *firm* must have a clear and verifiable mechanism for measuring performance, with risk adjustment applied thereafter in a clear and transparent manner.
- 19D.3.26 G A *firm* may apply discretionary factors to the extent that is appropriate and consistent with the overall aims of the risk adjustment exercise. Where such further adjustments have been made, *firms* should provide clear quantification and explanation to ensure their risk adjustment frameworks are sufficiently transparent.
- 19D.3.27 R A *firm* must base assessments of financial performance used to calculate variable *remuneration* components or pools of variable *remuneration* components principally on profits.
- 19D.3.28 G (1) Performance measures based primarily on revenues or turnover are

unlikely to pay sufficient regard to the quality of business undertaken or services provided. Profits are a better measure provided they are adjusted for risk, including future risks not adequately captured by accounting profits.

- (2) Management accounts should provide profit data at such levels within the *firm's* structure to enable it to see as accurate a picture of contributions of relevant staff to a *firm's* performance as is reasonably practicable.

- 19D.3.29 R
- (1) A *firm's* risk-adjustment approach must reflect both ex-ante adjustment (which adjusts remuneration for intrinsic risks that are inherent in its business activities) and ex-post adjustment (which adjusts remuneration for crystallisation of specific risks events).
 - (2) A *firm* must ensure that its total variable *remuneration* is generally considerably contracted where subdued or negative financial performance of the *firm* occurs, taking into account both current *remuneration* and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.

[**Note:** article 94(1)(n) of *CRD* and Standard 5 of the *FSB Compensation Standards*]

- 19D.3.30 G
- (1) Aligning variable awards to sustainable financial performance requires *firms* to make appropriate ex-ante adjustments to take account of the potential for future unexpected losses. Performance measures commonly used (such as earnings per *share* (EPS), total shareholder return (TSR) and return on equity (RoE)) are not suitably adjusted for longer-term risk factors and have a tendency to incentive highly leveraged activities.
 - (2) Long-term incentive plans should be treated as pools of variable *remuneration*. *Firms* that have long-term incentive plans should ensure that the structure of the award is compliant with the *dual-regulated firms Remuneration Code's* deferral and vesting requirements and that performance conditions required for vesting are appropriate. The valuation of the award should be based on its value when the award is granted, and determined using an appropriate technique.
 - (3) *Firms* should demonstrate that both the ex-ante intrinsic risks and the ex-post crystallisation of risk event have been considered as part of their risk-adjustment approach.

[**Note:** In addition to the *guidance* in this section on the Remuneration Principle 8 (Profit-based measurement and risk adjustment), the *FSA* gave guidance on the application of the requirements on risk adjustments. This *guidance* is available on the *FCA* website at <https://www.fca.org.uk/firms/being-regulated/remuneration-codes.>]

Remuneration Principle 9: Pension policy

- 19D.3.31 R A *firm* must ensure that:
- (1) its pension policy is in line with its business strategy, objectives, values and long-term interests;
 - (2) when an *employee* leaves the *firm* before retirement, any *discretionary pension benefits* are held by the *firm* for a period of five years in the form of instruments referred to in SYSC 19D.3.56R(1); and
 - (3) when an *employee* reaches retirement, *discretionary pension benefits* are paid to the *employee* in the form of instruments referred to in SYSC 19D.3.56R(1) and subject to a five-year retention period.

[**Note:** article 94(1)(o) of the *CRD*]

Remuneration Principle 10: Personal investment strategies

- 19D.3.32 R
- (1) A *firm* must ensure that its *employees* undertake not to use personal hedging strategies to undermine the risk alignment effects embedded in their *remuneration* arrangements.
 - (2) A *firm* must ensure that its *employees* do not use *remuneration-* or liability-related *contracts of insurance* to undermine the risk alignment effects embedded in their *remuneration* arrangements.
 - (3) A *firm* must maintain effective arrangements designed to ensure that *employees* comply with their undertaking.

[**Note:** article 94(1)(p) of the *CRD* and Standard 14 of the *FSB Compensation Standards*]

- 19D.3.33 G In the *FCA*'s view, circumstances in which a *person* will be using a personal hedging strategy include (and are not limited to) entering into an arrangement with a third party under which the third party will make payments, directly or indirectly, to that *person* that are linked to or commensurate with the amounts by which the *person's remuneration* is subject to reductions.

Remuneration Principle 11: Non-compliance with the dual-regulated firms Remuneration Code

- 19D.3.34 R A *firm* must ensure that variable *remuneration* is not paid through vehicles or methods that facilitate non-compliance with obligations arising from the *Remuneration Code*, the *EU CRR* or the *CRD*.

[**Note:** article 94(1)(q) of the *CRD*]

Remuneration Principle 12: Remuneration structures - introduction

- 19D.3.35 G (1) Taking account of the *dual-regulated firms remuneration principles proportionality rule*, the FCA does not generally consider it necessary for a *firm* to apply the *rules* in (2) where, in relation to an individual (X), both the following conditions are satisfied:
- (a) Condition 1 is that X's variable *remuneration* is no more than 33% of total *remuneration*; and
 - (b) Condition 2 is that X's total *remuneration* is no more than £500,000.
- (2) The *rules* referred to in (1) are those relating to:
- (a) guaranteed variable *remuneration* (SYSC 19D.3.44R);
 - (b) retained *shares* or other instruments (SYSC 19D.3.56R);
 - (c) deferral (SYSC 19D.3.59R); and
 - (d) performance adjustment (SYSC 19D.3.61R).

[Note: The FSA also gave *guidance* on the application of certain *rules* on *remuneration* structures about individuals who are *dual-regulated firms Remuneration Code staff* for only part of a given performance year. This guidance is available on the FCA website at <https://www.fca.org.uk/firms/being-regulated/remuneration-codes>.

Remuneration Principle 12(a): Remuneration structures - general requirement

- 19D.3.36 R A *firm* must ensure that the structure of an *employee's remuneration* is consistent with, and promotes, effective risk management.
- 19D.3.37 R A *firm* must ensure that the *remuneration* policy makes a clear distinction between criteria for setting:
- (1) basic fixed *remuneration* that primarily reflects an *employee's* professional experience and organisational responsibility, as set out in the *employee's* job description and terms of *employment*; and
 - (2) variable *remuneration* that reflects performance in excess of that required to fulfil the *employee's* job description and terms of *employment* and that is subject to performance adjustment in accordance with the *dual-regulated firms Remuneration Code*.

[Note: article 92(2)(g) of the *CRD*]

- 19D.3.38 R A *firm* must not award variable *remuneration* to a *non-executive*

director acting as such.

Remuneration Principle 12(b): Remuneration structures - assessment of performance

- 19D.3.39 R (1) A *firm* must ensure that where *remuneration* is performance-related:
- (a) the total amount of *remuneration* is based on a combination of the assessment of the performance of:
 - (i) the individual;
 - (ii) the business unit concerned; and
 - (iii) the overall results of the *firm*; and
 - (b) when assessing individual performance, financial as well as non-financial criteria are taken into account.

[**Note:** article 94(1)(a) of the *CRD* and Standard 6 of the *FSB Compensation Standards*]

- 19D.3.40 G The non-financial criteria in SYSC 19D.3.39R(1)(b) should include the extent of the *employee's* adherence to effective risk management, and compliance with the *regulatory system* and with relevant overseas regulatory requirements.
- 19D.3.41 G Poor performance assessed by non-financial metrics, such as poor risk management or other behaviours contrary to *firm* values, can pose significant risks for a *firm* and should, as appropriate, override metrics of financial performance.
- 19D.3.42 R A *firm* must clearly explain the performance assessment process in SYSC 19D.3.39R to relevant *employees*.
- 19D.3.43 R A *firm* must ensure that the assessment of performance is set in a multi-year framework in order to ensure that:
- (1) the assessment process is based on longer-term performance; and
 - (2) the actual payment of performance-based components of *remuneration* is spread over a period which takes account of the underlying business cycle of the *firm* and its business risks.

[**Note:** article 94(1)(b) of *CRD*]

Remuneration Principle 12(c): Remuneration structures - guaranteed variable remuneration, buy-outs

- 19D.3.44 R (1) A *firm* must ensure that guaranteed variable *remuneration* is not part of prospective *remuneration* plans.

- (2) A *firm* must not award, pay or provide guaranteed variable *remuneration* unless:
- (a) it is exceptional;
 - (b) it occurs in the context of hiring new *dual-regulated firms Remuneration Code staff*;
 - (c) the *firm* has a sound and strong capital base; and
 - (d) it is limited to the first year of service.

[**Note:** article 94(1)(d) and (e) of the *CRD* and Standard 11 of the *FSB Compensation Standards*]

- 19D.3.45 R A *firm* must ensure that *remuneration* packages relating to compensation for, or buy out from, an *employee's* contracts in previous *employment* align with its long-term interests including appropriate retention, deferral and performance and clawback arrangements.

[**Note:** article 94(1)(i) of *CRD*]

- 19D.3.46 G (1) Guaranteed variable *remuneration* should be subject to the same requirements applicable to variable *remuneration* awarded by the *firm* including deferral, malus and clawback.
- (2) The *FCA* expects that guaranteed variable awards and retention awards should not be common practice for *dual-regulated firms Remuneration Code staff* and should be limited to rare, infrequent occurrences. The *FCA* expects a *firm* to provide prior notification to the *FCA* of any such proposed awards.

- 19D.3.47 G Retention awards should form part of variable *remuneration* for the purpose of SYSC 19D.3.48R.

Remuneration Principle 12(d): Remuneration structures - ratios between fixed and variable components of total remuneration

- 19D.3.48 R A *firm* must set an appropriate ratio between the fixed and variable components of total *remuneration* and ensure that:
- (1) fixed and variable components of total *remuneration* are appropriately balanced;
 - (2) the level of the fixed component represents a sufficiently high proportion of the total *remuneration* to allow the operation of a fully flexible policy on variable *remuneration* components, including the possibility to pay no variable *remuneration* component; and
 - (3) subject to SYSC 19D.3.49R, the level of the variable component of total *remuneration* must not exceed 100% of the fixed component

of total *remuneration* for each *dual-regulated firms Remuneration Code staff*.

[**Note:** article 94(1)(f) and 94(1)(g)(i) of the *CRD*]

- 19D.3.49 R A *firm* may set a higher maximum level of the ratio between the fixed and variable components of total *remuneration* provided:
- (1) the overall level of the variable component does not exceed 200% of the fixed component of the total *remuneration* for each *dual-regulated firms Remuneration Code staff*; and
 - (2) is approved by the shareholders or owners or members of the *firm* in accordance with SYSC 19D.3.50R.

[Note: article 94(1)(g)(ii) of *CRD*]

- 19D.3.50 R A *firm* must ensure that any approval by its shareholders or owners or members, for the purposes of SYSC 19D.3.49R, is carried out in accordance with the following procedure:
- (1) the *firm* must give reasonable notice to all its shareholders or owners or members of its intention to seek approval of the proposed higher ratio;
 - (2) the *firm* must make a detailed recommendation to all its shareholders or owners or members that includes:
 - (a) the reasons for, and the scope of, the approval sought;
 - (b) the number of staff affected and their functions; and
 - (c) the expected impact on the requirement to maintain a sound capital base;
 - (3) the *firm* must:
 - (a) without delay, inform the *FCA* of the recommendation to its shareholders or owners or members, including the proposed higher ratio and the reasons therefor; and
 - (b) demonstrate to the *FCA* that the proposed higher ratio does not conflict with its obligations under the *CRD* and the *EU CRR*, having particular regard to the *firm's own funds* obligations;
 - (4) the *firm* must ensure that *employees* who have an interest in the proposed higher ratio are not allowed to exercise, directly or indirectly, any voting rights they may have as shareholders or owners or members of the *firm* in respect of the approval sought; and

- (5) the higher ratio is approved by a majority of:
- (a) at least 66% of the shares or equivalent ownership rights represented, if at least 50% of the shares or equivalent ownership rights in the *firm* are represented; or
 - (b) at least 75% of the shares or equivalent ownership rights represented, if less than 50% of the shares or equivalent ownership rights in the *firm* are represented.

[**Note:** article 94(1)(g)(ii) of the *CRD*]

19D.3.51 R A *firm* must notify the *FCA* without delay of the decisions taken by its shareholders or members or owners including any approved higher maximum ratio.

[**Note:** article 94(1)(g)(ii) of the *CRD*]

19D.3.52 R A *firm* may apply a discount rate to a maximum of 25% of an *employee's* total variable *remuneration* provided it is paid in instruments that are deferred for a period of not less than five years.

[**Note:** article 94(1)(g)(iii) of the *CRD*]

19D.3.53 R In applying the discount rate in *SYSC* 19D.3.52R, a *firm* must apply the *EBA* Guidelines on the applicable notional discount rate for variable remuneration published on 27 March 2014.

[**Note:** the *EBA* Guidelines on the applicable notional discount rate for variable remuneration can be found at:

<http://www.eba.europa.eu/documents/10180/643987/EBA-GL-2014-01+%28Final+Guidelines+on+the+discount+rate+for+remuneration%29.pdf/e8b3b3f6-6258-439d-a2d9-633e6e5de5e9>]

Remuneration Principle 12(e): Remuneration structures - payments related to early termination

19D.3.54 R A *firm* must ensure that payments relating to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure or misconduct.

[**Note:** article 94(1)(h) of the *CRD* and Standard 12 of the *FSB Compensation Standards*]

19D.3.55 G A *firm* should review existing contractual payments related to termination of *employment* with a view to ensuring that these are payable only where there is a clear basis for concluding that they are consistent with *SYSC* 19D.2.1R, which states that remuneration policies must be consistent with, and promote, sound and effective risk management.

[**Note:** Standard 12 of the *FSB Compensation Standards*]

Remuneration Principle 12(f): Remuneration structures - retained shares or other instruments

- 19D.3.56 R (1) A *firm* must ensure that a substantial portion, which is at least 50%, of any variable *remuneration* consists of an appropriate balance of:
- (a) *shares* or equivalent ownership interests, subject to the legal structure of the *firm* concerned, or *share*-linked instruments or equivalent non-cash instruments in the case of a non-listed *firm*; and
 - (b) where possible, other instruments that in each case adequately reflect the credit quality of the *firm* as a going concern and are appropriate for use as variable remuneration, such as:
 - (i) those which are eligible as *additional tier 1 instruments* or *tier 2 instruments*; or
 - (ii) those that can be fully converted to *common equity tier 1 instruments* or written down;

(where the expressions in italics are defined, with the conditions for eligibility, in the Definition of the Capital part of the *PRA* Rulebook).
- (2) The instruments in (1) must be subject to an appropriate retention policy designed to align incentives with the longer-term interests of the *firm*.
- (3) This *rule* applies to both the portion of the variable *remuneration* component deferred in accordance with SYSC 19D.3.59R and the portion not deferred.
- [**Note:** article 94(1)(l) of the *CRD* and Standard 8 of the *FSB Compensation Standards*]
- 19D.3.57 G The *FCA* would normally consider a period of retention of six months to be sufficient, provided that other risk management techniques within the *firm* are operating to secure sound and effective risk management.
- 19D.3.58 G (1) The Committee of European Banking Supervisors has given guidance on the interpretation of the *CRD* provision transposed by SYSC 19D.3.56R(3). Its guidelines provide that this requirement means that the 50% minimum threshold for instruments must be applied equally to the non-deferred and the deferred components; i.e., *firms* must apply the same chosen ratio between instruments and cash for their total variable *remuneration* to both the upfront and deferred components. (Guidelines on Remuneration Policies and Practices, 10 December 2010, paragraph 133,

<https://www.eba.europa.eu/documents/10180/106961/Guidelines.pdf>.)

- (2) This simplified example illustrates the operation of (1). The variable remuneration of a material risk taker (X) is 100 and, under SYSC 19D.3.59R(2), X is required to defer 60%. X's upfront component is 40 and X's deferred component is 60. At least 20 of X's upfront component, and at least 30 of X's deferred component, must be in instruments referred to in SYSC 19D.3.56R(1).

Remuneration Principle 12(g): Remuneration structures - deferral

- 19D.3.59 R (1) A *firm* must not award, pay or provide a variable *remuneration* component unless a substantial portion of it, which is at least 40%, is deferred over a period which is not less than:
- (a) for *dual-regulated firms Remuneration Code staff* who do not perform a *PRA-designated senior management function*, three to five years, with no vesting taking place until one year after the award, and vesting no faster than on a pro-rata basis.
 - (b) for *dual-regulated firms Remuneration Code staff* who perform a *PRA-designated senior management function*, seven years, with no vesting taking place until three years after the award, and vesting no faster than on a pro-rata basis.
- (2) In the case of a variable *remuneration* component:
- (a) of £500,000 or more, or
 - (b) payable to a *director* of a *firm* that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities;
- at least 60% of the amount must be deferred on the basis set out in SYSC 19D.3.59R(1).
- (3) Subject to (1), the length of the deferral period must be established in accordance with the business cycle, the nature of the business, its risks and the activities of the *employee* in question.

[**Note:** article 94(1)(m) of the *CRD* and Standards 6 and 7 of the *FSB Compensation Standards*]

- 19D.3.60 G (1) Deferred *remuneration* paid in:
- (a) *shares* or *share-linked* instruments should be made under a scheme which meets appropriate criteria, including risk adjustment of the performance measure used to determine

the initial allocation of *shares*;

- (b) cash should also be subject to performance criteria.
- (2) The *FCA* would generally expect a *firm* to have a *firm*-wide policy (and *group*-wide policy, where appropriate) on deferral. The proportion deferred should generally rise with the ratio of variable *remuneration* to fixed *remuneration* and with the amount of variable *remuneration*. While any variable *remuneration* component of £500,000 or more paid to *dual-regulated firms Remuneration Code staff* must be subject to 60% deferral, *firms* should also consider whether lesser amounts should be considered to be 'particularly high' taking account, for example, of whether there are significant differences within *dual-regulated firms Remuneration Code staff* in the levels of variable *remuneration* paid.

Remuneration Principle 12(h): Remuneration structures - performance adjustment (affordability, malus, clawback)

19D.3.61 R A *firm* must ensure that:

- (1) any variable *remuneration*, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the *firm* as a whole, and justified on the basis of the performance of the *firm*, the business unit and the individual concerned;
- (2) any variable *remuneration* is subject to clawback, such that it is only awarded if an amount corresponding to it can be recovered from the individual by the *firm* if the recovery is justified on the basis of the circumstances described in SYSC 19D.3.62R(2) and SYSC 19D.3.64R;
- (3) any variable *remuneration* is subject to clawback for a period of at least seven years from the date on which the variable *remuneration* is awarded; and
- (4) for *dual-regulated firms Remuneration Code staff* who perform a *PRA-designated senior management function*, it can, by notice to the *employee* to be given no later than seven years after the variable *remuneration* was awarded, extend the period during which variable *remuneration* is subject to clawback to at least ten years from the date on which the variable *remuneration* is awarded, where:
- (a) the *firm* has commenced an investigation into facts or events which it considers could potentially lead to the application of clawback were it not for the expiry of the clawback period; or
- (b) the *firm* has been notified by a regulatory authority

(including an overseas regulatory authority) that an investigation has been commenced into facts or events which the *firm* considers could potentially lead to the application of clawback by the *firm* were it not for the expiry of the clawback period; and

- (5) it considers on an ongoing basis whether to use the power in (4).

[**Note:** article 94(1)(n) of the *CRD* and Standards 6 and 9 of the *FSB Compensation Standards*]

19D.3.62 R A *firm* must:

- (1) set specific criteria for the application of malus and clawback; and
- (2) ensure that the criteria for the application of malus and clawback in particular cover situations where the *employee*:
 - (a) participated in, or was responsible for, conduct which resulted in significant losses to the *firm*; or
 - (b) failed to meet appropriate standards of fitness and propriety.

[**Note:** article 94(1)(n) of the *CRD* and Standards 6 and 9 of the *FSB Compensation Standards*]

[**Note:** The *FSA* also gave *guidance* on the application of the requirements on risk adjustments. This *guidance* is available on the *FCA* website at <https://www.fca.org.uk/firms/being-regulated/remuneration-codes>.]

- 19D.3.63 E
- (1) A *firm* should reduce unvested deferred variable remuneration when, as a minimum:
 - (a) there is reasonable evidence of *employee* misbehaviour or material error; or
 - (b) the *firm* or the relevant business unit suffers a material downturn in its financial performance; or
 - (c) the *firm* or the relevant business unit suffers a material failure of risk management.
 - (2) For performance adjustment purposes, awards of deferred variable remuneration made in shares or other non-cash instruments should provide the ability for the *firm* to reduce the number of shares or other non-cash instruments.
 - (3) Contravention of any of (1) or (2) may be relied on as tending to establish contravention of *SYSC* 19D.3.61R(1) on performance adjustment.

- 19D.3.64 R (1) A *firm* must make all reasonable efforts to recover an appropriate amount corresponding to some or all vested variable *remuneration* where either of the following circumstances arise during the period in which clawback applies (including any part of such period occurring after the relevant *employment* has ceased):
- (a) there is reasonable evidence of *employee* misbehaviour or material error; or
 - (b) the *firm* or the relevant business unit suffers a material failure of risk management.
- (2) A *firm* must take into account all relevant factors (including, where the circumstances described in (1)(b) arise, the proximity of the *employee* to the failure of risk-management in question and the *employee's* level of responsibility) in deciding whether, and to what extent it is reasonable, to seek recovery of any or all of their vested variable *remuneration*.
- 19D.3.65 G The *governing body* (or, where appropriate, the *remuneration committee*) should approve performance adjustment policies, including the triggers under which adjustment would take place. The *FCA* may ask *firms* to provide a copy of their policies and expects *firms* to make adequate records of material decisions to operate the adjustments.

Effect of breaches of the Remuneration Principles

- 19D.3.66 R SYSC 19D Annex 1 makes provision about voiding and recovery.
- 19D.3.67 R (1) Subject to (2) to (7), the *rules* in SYSC 19D Annex 1.1R to 1.6R apply in relation to the prohibitions on *dual-regulated firms Remuneration Code staff* being *remunerated* in the ways specified in:
- (a) SYSC 19D.3.44R (guaranteed variable *remuneration*);
 - (b) SYSC 19D.3.59R (non-deferred variable *remuneration*);
 - (c) SYSC 19D.3.61R(2) (performance adjustment – clawback); and
 - (d) SYSC 19D Annex 1.10R (replacing payments recovered or property transferred).
- (2) Paragraph (1) applies only to those prohibitions as they apply in relation to a *firm* that satisfies either Condition 1 or Condition 2 as set out in (3) and (4).
- (3) Condition 1 is that the *firm* is a *UK bank*, a *building society*, or a *UK designated investment firm*, that has relevant total assets exceeding £50 billion.

- (4) Condition 2 is that the *firm*:
- (a) is either a *full credit institution* or a *UK designated investment firm*; and
 - (b) is part of a *group* containing a *firm* that has relevant total assets exceeding £50 billion and that is a *bank, a building society or a UK designated investment firm*.
- (5) For the purposes of this *rule*, ‘relevant total assets’ means the arithmetic mean of the *firm's* total assets as set out in its balance sheet on its last three *accounting reference dates*.
- (6) This *rule* does not apply in relation to the prohibition on *dual-regulated firms Remuneration Code staff* being *remunerated* in the way specified in SYSC 19D.3.44R (guaranteed variable *remuneration*) if both the conditions in paragraphs (2) and (3) of that *rule* are met.
- (7) This *rule* does not apply in relation to *dual-regulated firms Remuneration Code staff (X)* in respect of whom both the following conditions are satisfied:
- (a) Condition 1 is that X’s variable *remuneration* is no more than 33% of total *remuneration*; and
 - (b) Condition 2 is that X’s total *remuneration* is no more than £500,000.
- (8) In relation to (7):
- (a) references to *remuneration* are to *remuneration* awarded or paid in respect of the relevant performance year;
 - (b) the amount of any *remuneration* is:
 - (i) if it is money, its amount when awarded;
 - (ii) otherwise, whichever of the following is greatest:
 - (A) its value to the recipient when awarded;
 - (B) its market value when awarded; and
 - (C) the cost of providing it;
 - (c) where *remuneration* is, when awarded, subject to any condition, restriction or other similar provision which causes the amount of the *remuneration* to be less than it otherwise would be, that condition, restriction or provision is to be ignored in arriving at its value; and

- (d) it is to be assumed that the member of *dual-regulated firms Remuneration Code staff* will remain so for the duration of the relevant performance year.
- 19D.3.68 G (1) Sections 137H and 137I of the *Act* enable the *FCA* to make *rules* that render void any provision of an agreement that contravenes specified prohibitions in the *dual-regulated firms Remuneration Code*, and that provide for the recovery of any payment made, or other property transferred, in pursuance of such a provision.
- (2) *SYSC 19D.3.66R* and *SYSC 19D.3.67R* (together with *SYSC 19D Annex 1*) are:
- (a) *rules* referred to in (1) that render void provisions of an agreement that contravene the specified prohibitions on guaranteed variable *remuneration*, non-deferred variable *remuneration* and replacing payments recovered or property transferred; and
- (2) the exception to the general position set out in section 138E(2) of the *Act* that a contravention of a *rule* does not make any transaction void or unenforceable.

**19D
Annex 1** **Detailed provisions on voiding and recovery (SYSC 19D.3.66R and SYSC 19D.3.67R)**

Rendering contravening provisions of agreements void		
1	R	Any provision of an agreement that contravenes a prohibition on <i>persons</i> being <i>remunerated</i> in a way specified in a <i>rule</i> to which this <i>rule</i> applies (a ‘contravening provision’) is void.
2	R	A contravening provision does not cease to be void because:
		(1) the <i>firm</i> concerned ceases to satisfy any of the conditions set out in <i>SYSC 19D.3.67R</i> (3) to (4); or
		(2) the member of <i>dual-regulated firms Remuneration Code staff</i> concerned starts to satisfy both of the conditions set out in <i>SYSC 19D.3.67R</i> (7)(a) and (b).
3	R	A contravening provision that, at the time a <i>rule</i> to which this <i>rule</i> applies was first made (including any previous <i>rules</i> in the <i>FCA Handbook</i>), is contained in an agreement made before that time is not rendered void by <i>SYSC 19D Annex 1.1R</i> , unless it is subsequently amended so as to contravene such a <i>rule</i> .
4	G	The effect of <i>SYSC 19D Annex 1.3R</i> , in accordance with sections 137H and 137I of the <i>Act</i> , is to prevent contravening provisions

			being rendered void retrospectively. However, contravening provisions may be rendered void if they are contained in an agreement made after the <i>rule</i> containing the prohibition is made by the <i>FCA</i> but before the <i>rule</i> comes into effect.
5	R	(1)	A pre-existing provision is not rendered void by SYSC 19D Annex 1.1R.
		(2)	In this Annex, a pre-existing provision is any provision of an agreement that would (but for this <i>rule</i>) be rendered void by SYSC 19D Annex 1.1R that was agreed at a time when either:
		(a)	the <i>firm</i> concerned did not satisfy any of the conditions set out in SYSC 19D.3.67R(3) to (4); or
		(b)	the member of <i>dual-regulated firms Remuneration Code staff</i> concerned satisfied both of the conditions set out in SYSC 19D.3.67R(7)(a) and (b).
		(3)	But an amendment to, or in relation to, a pre-existing provision is not to be treated as a pre-existing provision where the amendment is agreed at a time when both:
		(a)	the <i>firm</i> concerned satisfies at least one of the conditions set out in SYSC 19D.3.67R(3) to (4); and
		(b)	the member of <i>dual-regulated firms Remuneration Code staff</i> concerned does not satisfy both of the conditions set out in SYSC 19D.3.67R(7)(a) and (b).
6	R		For the purposes of this chapter, it is immaterial whether the law which (apart from this annex) governs a contravening provision is the law of the <i>United Kingdom</i> , or of a part of the <i>United Kingdom</i> .
Recovery of payments made or property transferred pursuant to a void contravening provision			
7	R		In relation to any payment made or other property transferred in pursuance of a contravening provision other than a pre-existing provision, a <i>firm</i> must take reasonable steps to:
		(1)	recover any such payment made or other property transferred by the <i>firm</i> ; and
		(2)	ensure that any other <i>person</i> (P) recovers any such payment made or other property transferred by that <i>person</i> .
8	R		SYSC 19D Annex 1.7R continues to apply in one or both of the following cases:
		(1)	the <i>firm</i> concerned ceases to satisfy any of the conditions set

			out in SYSC 19D.2.67R(3) to (4);
		(2)	the member of <i>dual-regulated firms Remuneration Code</i> staff concerned starts to satisfy both of the conditions set out in SYSC 19D.2.67R(7)(a) and (b).
9	G		The <i>rule</i> in SYSC 19D Annex 1.7R(2) would, for example, apply in the context of a secondment. Where a <i>group</i> member seconded an individual to a <i>firm</i> and continues to be responsible for the individual's <i>remuneration</i> in respect of services provided to the <i>firm</i> , the <i>firm</i> would need to take reasonable steps to ensure that the <i>group</i> member recovers from the secondee any <i>remuneration</i> paid in pursuance of a contravening provision.
Replacing payments recovered or property transferred			
10	R	(1)	A <i>firm</i> must not award, pay or provide variable <i>remuneration</i> to a <i>person</i> who has received <i>remuneration</i> in pursuance of a contravening provision other than a pre-existing provision (the 'contravening <i>remuneration</i> ') unless the <i>firm</i> has obtained a legal opinion stating that the award, payment or provision of the <i>remuneration</i> complies with the <i>dual-regulated firms Remuneration Code</i> .
		(2)	This <i>rule</i> applies only to variable <i>remuneration</i> relating to a performance year to which the contravening <i>remuneration</i> related.
		(3)	The legal opinion in (1) must be properly reasoned and be provided by an appropriately qualified independent individual.
		(4)	Paragraph (1) continues to apply in one or both of the following cases:
		(a)	the <i>firm</i> concerned ceases to satisfy any of the conditions set out in SYSC 19D.3.67R(3) to (4);
		(b)	the member of <i>dual-regulated firms Remuneration Code</i> staff concerned starts to satisfy both of the conditions set out in SYSC 19D.3.67R(7)(a) and (b).
Notification to the FCA			
11	G		The <i>FCA</i> considers any breach of a <i>rule</i> to which this annex applies to be a significant breach which should be notified to the <i>FCA</i> in accordance with SUP 15.3.11R (Breaches of rules and other requirements in or under the Act). Such a notification should include information on the steps which a <i>firm</i> or other <i>person</i> has taken or intends to take to recover payments or property in accordance with SYSC 19D Annex 1.7R.

Amend the following as shown.

21.1 Risk control: guidance on governance arrangements

...

Chief Risk Officer

21.1.2 G (1) A Chief Risk Officer should:

...

- (j) provide risk-focused advice and information into the setting and individual application of the *firm's remuneration* policy (Where the *Remuneration Code* applies, see in particular SYSC 19A.3.15E. Where the BIPRU Remuneration Code applies, see in particular SYSC 19C.3.15E. Where the *dual-regulated firms Remuneration Code* applies, see in particular SYSC 19D.2.16E. Where the remuneration part of the *PRA Rulebook* applies, see the *PRA's Supervisory Statement on Remuneration*).

[Note: The *PRA's Supervisory Statement on remuneration* is available on the *PRA* website at <http://www.bankofengland.co.uk/pr/Pages/default.aspx>.]

...

Sch 5 Right of action for damages

...

Sch 5.4 G

Chapter/ Appendix	Section/ Annex	Paragraph	Right of action under section 138D		
			For private person?	Removed?	For other person?
...					
<i>SYSC 11 to SYSC 19A₂ and SYSC 19D</i>			No	Yes <i>SYSC 1.4.2R</i>	No

Annex C

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text.

13A Annex 1G Application of the Handbook to Incoming EEA firms

...

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
...		
SYSC	... <u>SYSC 19A, and 19B, 19C and 19D</u> do not apply.	<u>SYSC 19A, 19C and 19D</u> does do not apply.
...		

...

Annex 4 (Part 1) – Finalised non-handbook guidance

General Guidance on Proportionality

The IFPRU Remuneration Code (SYSC 19A)

1 July 2015

[Note: In this Annex, with the exception of paragraph numbers, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.]

1 Part A: Introduction and interpretations

Introduction and status of guidance statement

- 1.1 This statement is general *guidance* given under section 139A(1) of the Financial Services and Markets Act (FSMA). It relates to the *Remuneration Code* of SYSC 19A of the *Handbook*.
- 1.2 Paragraphs ~~13 and 14~~ 1.13 and 1.14 make provision about the interpretation of this *guidance* statement. Expressions in italics either bear the meaning given in the *Handbook Glossary*, or in ~~the table in paragraph 15~~ Table 1.
- 1.3 This *guidance* statement has effect from ~~1 January 2014~~ 1 July 2015.

Remuneration principles proportionality rule

- 1.4 The *remuneration principles proportionality rule* is set out in SYSC 19A.3.3R (2).
- 1.5 The *Remuneration Code* requires (amongst other things) a *firm* to apply requirements in SYSC 19A.3 to *Remuneration Code staff*. The *remuneration principles proportionality rule* requires a *firm*, when establishing and applying the total *remuneration* policies for *Remuneration Code staff*, to comply with SYSC 19A.3 in a way and to the extent that is appropriate to its size, internal organisation and the nature, the scope and the complexity of its activities.

Guidance on the remuneration principles proportionality rule

- 1.6 General *guidance* is given in relation to specific aspects of the *remuneration principles proportionality rule* in SYSC 19A.3 itself.¹

General Guidance

- 1.7 Part D of this *guidance* statement provides additional general *guidance* in relation to the application of the *remuneration principles proportionality rule* to different types of *firm*.
- 1.8 Part E of this *guidance* statement provides additional general *guidance* in relation to the application of the *remuneration principles proportionality rule* to *Remuneration Code staff* who have, in relation to a given performance year, been *Remuneration Code staff* for only part of the year.
- 1.9 This *guidance* statement represents our *guidance* in a field where requirements relating to *remuneration* are being implemented within the EEA. We recognise this will be an evolving process, and intend to keep the *guidance* set out here under review.

Individual guidance

- 1.10 We may give individual *guidance* to a *firm*, either on its own initiative or on the application of the *firm*. Our policy on individual *guidance* is set out in *SUP 9*. In consequence, we may give individual *guidance* to a *firm* in relation to the *remuneration principles proportionality rule* (*SYSC 19A.3.3R*). Such guidance may relate to the application of the rule by the *firm* generally, or in specific areas.

Arrangement of guidance statement

- 1.11 This general *guidance* statement is divided into five Parts:
 1. This Part, Part A: Introduction & interpretation.
 2. Part B: *Proportionality levels*.
 3. Part C: Division of *firms* into *proportionality levels*.
 4. Part D: *Guidance* to *firms* in particular *proportionality levels*.
 5. Part E: *Guidance* about part-year *Remuneration Code staff*.
- 1.12 It is supplemented by Annex 1 – Supplemental *guidance* on dividing *firms* into *proportionality levels*.

Interpretation

- 1.13 This *guidance statement* is to be interpreted as if it was an Annex to *SYSC 19A.3 R*. In consequence, *GEN 2* (interpreting the Handbook) applies to the interpretation of this *guidance* statement.
- 1.14 In particular, an expression in italics which is defined in the *Glossary* has the meaning given there (*GEN 2.2.7R*). Where an expression in italics is not defined in the *Glossary*, it has the meaning given by the following table:

¹ The main provisions of guidance which specifically refer to the *remuneration principles proportionality rule* are *SYSC 19A.3.34G* (giving guidance in relation to *Remuneration Code staff* and certain rules on *remuneration* structures)

Table 1: Glossary of terms defined in this guidance statement

Defined expression	Definition
<i>group</i>	has the meaning given in the <i>Glossary</i> under paragraph (3).
<i>overseas Remuneration Code firm</i>	An <i>overseas firm</i> that: (i) is not an <i>EEA firm</i> ; (ii) has its head office outside the <i>EEA</i> ; and (iii) would be a building society, a bank, an IFPRU <i>investment firm</i> if it had been a <i>UK domestic firm</i> , had carried on all its business in the United Kingdom and had obtained whatever authorisation for doing so as required under the <i>Act</i> .
<i>proportionality level</i>	has the meaning given in paragraph 2.3 17 , and references to <i>proportionality level one</i> , etc. are to be construed accordingly.
<i>Remuneration Code firm</i>	a <i>firm</i> specified in SYSC 19A.1.1 R(1) (a) -(c).
<i>relevant total assets</i>	has the meanings given in paragraph 22(3) 3.4(3).
<i>relevant date</i>	has the meanings given in paragraph 22(3) 3.4(3).
<i>solo Remuneration Code firm</i>	a <i>Remuneration Code firm</i> which is not part of a <i>group</i> containing one or more further <i>Remuneration Code firms</i> .

2 Part B: Proportionality Levels

- 2.1 SYSC 19A.1.1R provides that the *Remuneration Code* applies to a *Remuneration Code firm* and an *overseas Remuneration Code firm*, in relation to the activities carried on from an establishment in the UK.
- 2.2 This *guidance* statement provides for the division of *Remuneration Code firms* into three categories:
1. *proportionality level one*;
 2. *proportionality level two*; and
 3. *proportionality level three*.
- 2.3 The process by which firms are divided into *proportionality levels* is provided in Part C (as supplemented by Annex 1), and may also depend on individual *guidance*.
- 2.4 The *proportionality levels* provide a framework for the operation of the *remuneration principles proportionality rule*. *Guidance* is given to *firms* in different *proportionality levels* in Part D.

3 Part C: Process for Dividing Firms into Proportionality Levels

Overview

- 3.1 This Part provides the process by which a *Remuneration Code firm* should ascertain the *proportionality level* into which it falls. Annex 1 provides supplementary *guidance* (including examples).
- 3.2 A *Remuneration Code firm*, in order to ascertain its *proportionality level*, must first establish whether it is part of a *group* which contains one or more other *Remuneration Code firms*:
1. If the *firm* is not part of such a *group* (a *solo Remuneration Code firm*), its *proportionality level* will depend on its individual characteristics (as determined in accordance with paragraph ~~22~~3.4).
 2. If the *firm* is part of such a *group*, its *proportionality level* will depend on a two-stage process (as provided in paragraphs ~~23 and 24~~3.5 to 3.7).

(This requires all *Remuneration Code firms* that are part of the *group* to fall into the highest *proportionality level* that any individual *Remuneration Code firm* in the *group* would fall into on the assumption that it was a *solo Remuneration Code firm*.)
- 3.3 Individual *guidance* may vary the *proportionality level* into which a *firm* would otherwise fall under paragraphs ~~22 to 24~~3.4 to 3.7.

Solo Remuneration Code firms

- 3.4 The following table shows the *proportionality level* into which a *solo Remuneration Code firm* that is an *IFPRU investment firm* or an *overseas Remuneration Code firm* falls:
1. A *firm* of the description given in the second column falls into the *proportionality level* listed in the first column.
 2. Where applicable, the *firm's proportionality level* will further depend on whether it held *relevant total assets* on the *relevant date* of the amount listed in the third column of the table.
 3. In (2) —
 - b. '*relevant total assets*' means:
 - i. for *IFPRU investment firms*, the average of the *firm's* total assets on the *firm's* last three *relevant dates*; and
 - ii. for *overseas Remuneration Code firms*, the average of the *firm's total assets* that covered the activities of the branch operation in the *United Kingdom* on the *firm's* last three *relevant dates*;
 - c. '*relevant date*' means:
 - i. for *IFPRU investment firms*, an accounting reference date; and
 - ii. for *overseas Remuneration Code firm* '*relevant date*' means 31 December.

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The limit confining ~~relevant total assets~~ to those that cover the activities of the branch operation in the UK is taken from ~~SUP 16.12.3R(1)(a)(iv)~~, which relates to a reporting requirement in relation to ~~non-EEA banks~~ (among others). We consider that a *firm* which needs to ascertain its ~~relevant total assets~~ should apply the valuation requirements set out in the *EU CRR*.

Table 2: Proportionality levels: solo Remuneration Code firms which include IFPRU Investment firms and overseas Remuneration Code firms

Proportionality level	Type of firm	Relevant total assets on relevant date of firm
<i>Proportionality level one</i>	<i>UK Bank</i>	Exceeding £50bn
	<i>Building society</i>	Exceeding £50bn
	<i>IFPRU 730k Investment firm that is a full scope IFPRU investment firm</i>	Exceeding £50bn
<i>Proportionality level two</i>	<i>UK Bank</i>	Exceeding £15bn but not exceeding £50bn
	<i>Building society</i>	Exceeding £15bn but not exceeding £50bn
	<i>IFPRU 730k Investment firm that is a full scope IFPRU investment firm</i>	Exceeding £15bn, but not exceeding £50bn
<i>Proportionality level three</i>	<i>UK Bank</i>	Not exceeding £15bn
	<i>Building society</i>	Not exceeding £15bn
	<i>Any full scope IFPRU Investment firm that does not fall within proportionality level one or proportionality level two (in accordance with this Table).</i>	Not applicable
	<i>IFPRU limited licence firm.</i>	
	<i>IFPRU limited activity firm.</i>	

Groups with more than one Remuneration Code firm

- 3.5 This paragraph applies where a *Remuneration Code firm* is part of a *group* containing one or more other *Remuneration Code firms*:
1. Each *Remuneration Code firm* in the *group* must determine the *proportionality level* into which it would fall on the assumption it was a *solo Remuneration Code firm*.
 2. Where each *Remuneration Code firm* falls into the same *proportionality level* on the assumption that it was a *solo Remuneration Code firm*, each *firm* falls into that *proportionality level*.
 3. Where the *Remuneration Code firms* fall into different *proportionality levels* on the assumption that they were *solo Remuneration Code firms*, each *firm* falls into the highest *proportionality level*.
 4. For the purposes of (3), *proportionality level one* is the highest and *proportionality level three* is the lowest.
- 3.6 Annex 1 provides examples of this approach. A *firm* which has a higher *proportionality level* as a result of the *guidance* in paragraph ~~23~~3.5 than would have been the case had the *firm* been a *solo Remuneration Code firm* should note the scope to apply for individual *guidance* to vary its *proportionality level* (as discussed in paragraphs ~~5 and 6~~5 and 6.5 and 6.6 of Annex 1).
- 3.7 Where a *Remuneration Code firm* is part of a *group* in which a *firm* to which SYSC 19D applies is a member, this *guidance* does not apply, SYSC 19D and its applicable general *guidance* on *proportionality* apply instead.

4 Part D: Guidance to firms in particular proportionality levels

Purpose of proportionality levels

- 4.1 In relation to the *remuneration principles proportionality rule*, the *proportionality levels* provide the following:
1. A framework for our supervisory approach, and a broad indication of our likely expectations; and
 2. *Guidance* on which remuneration principle may normally be disapplied under the *remuneration principles proportionality rule*.

Firms to continue to consider proportionality in their individual circumstances etc.

- 4.2 It follows from the nature of the *remuneration principles proportionality rule*, and the limited purposes noted in paragraph 254.1, that the *proportionality levels* do not provide comprehensive *guidance* on how the *remuneration principles proportionality rule* will apply to a particular *firm*. A *firm* will still need to consider the application of the *remuneration principles proportionality rule* to its individual circumstances.
- 4.3 A *firm* should bear in mind that the *Remuneration Code* may require different responses from *firms* that fall into the same *proportionality level*. This is illustrated by the following example:
1. Firm A is a *full scope IFPRU investment firm* with *relevant total assets* of £800bn with complex business operations with substantial foreign exchange exposures. It falls into *proportionality level one*.
 2. Firm B is a *full scope IFPRU investment firm* with *relevant total assets* of £100bn and a comparatively simple, conservative business model. It falls into *proportionality level one*.
 3. Firm C is an *full scope IFPRU investment firm*, with *relevant total assets* of £25bn and a comparatively simple, conservative business model. It falls into *proportionality level two*.
 4. Remuneration Principle 8 requires, amongst other things, a *firm* to risk-adjust performance measures to take account of all types of current and future risks (SYSC 19A.3.22R(1)(a)).
 5. Clearly the processes necessary to identify such risks will need to be more sophisticated for Firm A than for Firm B, despite the fact that they fall into the same *proportionality level*. Indeed, the difference in the necessary sophistication is likely to be greater as between Firm A and Firm B than as between Firm B and Firm C.

Disapplication of certain remuneration principles for firms in particular proportionality levels

- 4.4 The *CRD* can be interpreted such that it may not be necessary for certain *firms* to apply certain *remuneration* principles at all.²
- 4.5 In our view, it will normally be appropriate for a *firm* in *proportionality level three* to disapply under the *remuneration principles proportionality rule* one or more of the following *rules*:
1. retained *shares* or other instruments (SYSC 19A.3.47R)
 2. deferral (SYSC 19A.3.49R)
 3. performance adjustment (SYSC 19A.3.51R – SYSC 19A.3.51A)
- 4.6 It may also be appropriate for:
1. *proportionality level three full scope IFPRU investment firms* to disapply the specific ratio between fixed and variable components of total *remuneration* (SYSC 19A.3.44R (3)); and
 2. *IFPRU limited licence firms* and *IFPRU limited activity firms* to disapply, under the *remuneration principles proportionality rule*, the ratios between fixed and variable components of total *remuneration* (SYSC 19A.3.44R);
- 4.7 In both cases ~~(a) and (b)~~ 4.6(1) and 4.6(2) above, if requested by the *FCA*, the *FCA* will expect the *firm's* senior management to be able to demonstrate why the *firm* believes it is reasonable to disapply it in the light of the *remuneration principles proportionality rule*.

We are also of the opinion that such firms may 'take into account the specific features of their types of activities in applying the 'requirement on multi-year framework, in particular the accrual and ex- ante risk adjustment aspects of it. ³

- 4.8 However, *firms* should also note that some *remuneration* principles set specific numerical criteria (such as on the minimum period of deferral, the minimum portion to be deferred and the minimum portion to be issued in *shares*). The following *guidance* applies where such principles apply to *Remuneration Code staff* and are not capable of disapplication under the approach set out above. In such circumstances, we do not consider that the *remuneration principles proportionality rule* permits a *firm* to apply lower numerical criteria. (For the avoidance of doubt, this *guidance* does not apply where a firm chooses to use deferral or issuance in shares more widely than required by SYSC 19A.3, for example in order to comply with the *Remuneration Code general requirement*).

² *CRD* Article 92(2) provides that the principles should be applied 'in a manner and to the extent that is appropriate to their size, internal organisation and the nature, the scope and complexity of their activities'.

³ As per the FSA's Policy Statement 10/20. See link http://www.fsa.gov.uk/pubs/policy/ps10_20.pdf

5 Part E: Guidance about part year Remuneration Code staff

Introduction

- 5.1 SYSC 19A.3.34G provides *guidance* on when we do not generally consider it necessary for a *firm* to apply to certain *Remuneration Code staff* certain *rules* relating to *remuneration* structures. This Part provides supplementary guidance on how certain *rules* on *remuneration* structures might normally be applied to *Remuneration Code staff* who have, in relation to a given performance year, been *Remuneration Code staff* for only part of the year.
- 5.2 In giving this *guidance*, we have taken account of the *remuneration principles proportionality rule*.

Part-year Remuneration Code staff for more than three months

- 5.3 This paragraph applies where an individual (A) has, in relation to a given performance year, been *Remuneration Code staff* for a period more than three months, but less than 12 months:
1. Sub-paragraphs (3) and (4) explain how the *guidance* in SYSC 19A.3.34G (as mentioned in the introduction to this Part) is to be applied in relation to A. Sub-paragraphs (5) and (6) provide that in certain circumstances it may be appropriate to apply certain rules to only a proportion of A's variable *remuneration*. Sub-paragraphs (7) to (9) provide examples.
 2. In this paragraph:
 - a. 'relevant fraction' means the fraction derived by dividing the number of days in the given performance year for which A has been *Remuneration Code staff* by the number of days in the year;
 - b. 'qualifying fixed remuneration' means A's annual fixed remuneration in A's capacity as *Remuneration Code staff* multiplied by the relevant fraction;
 - c. 'qualifying variable *remuneration*' means:
 - i. In the case where A was an *employee* of the *firm* for the whole of the given performance year, A's variable *remuneration* in relation to the performance year multiplied by the relevant fraction
 - ii. in the case where A was only ever employed in the given performance year as *Remuneration Code staff*, A's actual variable *remuneration*;
 - d. 'total qualifying *remuneration*' means qualifying fixed *remuneration* added to qualifying variable *remuneration*; and
 - e. 'threshold amount' means £500,000 multiplied by the relevant fraction.

3. We do not generally consider it necessary for a *firm* to apply the rules referred to in (4) where, in relation to A, the following conditions are satisfied:
 - a. Condition 1 is that A's qualifying variable *remuneration* is no more than 33% of total qualifying remuneration, and
 - b. Condition 2 is that A's total qualifying *remuneration* is no more than the threshold amount.
4. The rules referred to in (3) are those relating to
 - a. guaranteed variable *remuneration* (SYSC 19A.3.40R);
 - b. retained *shares* or other instruments (SYSC 19A.3.47R);
 - c. deferral (SYSC 19A.3.49R); and
 - d. performance adjustment (SYSC 19A.3.51R).
5. Sub-paragraph (6) applies where the conditions in (3) are not satisfied and the *firm* should apply the rules referred to in (6).
6. Where this sub-paragraph applies, we generally consider that it would be appropriate to apply the following rules to qualifying variable *remuneration* only
 - a. retained *shares* or other instruments (SYSC 19A.3.47R), (b);
 - b. deferral (SYSC 19A.3.49R); and
 - c. performance adjustment (SYSC 19A.3.51R).
7. The examples in (8) and (9) illustrate this guidance. The performance year in each case is 1 January to 31 December.
8. Example 1:
 - a. A1 is an *employee* of the *firm* through the performance year and is promoted to a *Remuneration Code staff* role with effect from 1 September. A1's previous fixed *remuneration* was £150,000. In his *Remuneration Code staff* role A1's fixed remuneration increases to £250,000. For the performance year, A1 is awarded variable *remuneration* of £130,000.
 - b. The relevant fraction is 122/365. A1's qualifying fixed *remuneration* is £83,560 (£250,000 multiplied by 122/365). A1's qualifying variable *remuneration* is £43,452 (£130,000 multiplied by 122/365). A1's total qualifying *remuneration* is £127,012. The threshold amount is £167,120 (£500,000 multiplied by 122/365).
 - c. A1's total qualifying *remuneration* is below the threshold amount, so condition 2 of (3) is satisfied. But A1's qualifying variable remuneration is more than 33% of A1's total qualifying *remuneration*, and condition 1 of (3) is not satisfied.
 - d. The rule on guaranteed variable *remuneration* applies to A1. In addition, the rules on retained *shares* and other instruments, deferral and performance adjustment must be applied to A1's qualifying variable *remuneration* of £43,452.

9. Example 2:

- a. A2 joins the *firm* as a *Remuneration Code staff* member with effect from 1 July. A2's annual fixed *remuneration* is £450,000. For the period of 1 June to 31 December, A2 is awarded variable *remuneration* of £50,000.
- b. The relevant fraction is 184/365. A2's qualifying fixed *remuneration* is £226,850 (£450,000 multiplied by 184/365). A2's qualifying variable *remuneration* is £50,000 (the actual amount). A2's total qualifying *remuneration* is £276,850. The threshold amount is £252,050 (£500,000 multiplied by 184/365).
- c. A2's qualifying variable *remuneration* is not more than 33% of A2's total qualifying *remuneration*, and condition 1 of (3) is satisfied. But A2's total qualifying *remuneration* is more than the threshold amount, so condition 2 of (3) is not satisfied.
- d. The rule on guaranteed variable *remuneration* applies to A2. In addition, the rules on retained *shares* and other instruments, deferral and performance adjustments must be applied to A2's qualifying variable *remuneration* of £50,000.

Certain part-year Remuneration Code staff for three months or less

5.4 Paragraphs ~~35 and 36~~ 5.5 and 5.6 apply where:

1. an individual (B) has, in relation to a given performance year, been *Remuneration Code staff* for a period of three months or less, and
2. an exceptional or irregular payment (such as a sign-on award) has not been or is not to be made in relation to B's appointment as *Remuneration Code staff*.

5.5 Where this paragraph applies, we do not generally consider it necessary to apply the following rules in relation to B for the performance year in question:

1. retained *shares* or other instruments (SYSC 19A.3.47R);
2. deferral (SYSC 19A.3.49R); and
3. performance adjustment (SYSC 19A.3.51R).

5.6 Where this paragraph applies, the *guidance* in paragraph ~~33(2), (3) and (4)(a)~~ 5.3 (2), 5.3 (3) and 5.3 (4)(a) should be applied for the purposes of determining whether or not it will generally be necessary to apply the rule on guaranteed variable *remuneration* to B (substituting in that paragraph, for references to 'A', references to 'C').

Part-year Remuneration Code staff for three months or less, but where exceptional etc. payments made

5.7 Paragraph ~~38~~ 5.8 applies where an individual (C) has, in relation to a given performance year, been *Remuneration Code staff* for a period of three months or less, but where an exceptional or irregular payment (such as a sign-on award) has or is to be made in relation to C's appointment.

5.8 The *guidance* in paragraph ~~33~~ 5.3 applies in relation to C (substituting in that paragraph, for references to 'A', references to 'C'). The amount of exceptional or irregular payment is to be added to C's qualifying variable *remuneration* without pro rating.

6 Annex 1: Supplemental guidance on dividing firms into proportionality levels

Groups with more than one Remuneration Code firm: examples

- 6.1 The following non-exhaustive examples illustrate the operation of the *guidance* provided in paragraph ~~2-3.5~~ of Part C. (It should be borne in mind that in each case individual *guidance* could vary the outcome provided by the operation of the guidance provided in that paragraph.)
- 6.2 Example 1:
1. Firm A is the *parent undertaking* of Firm B
 2. Firm A is a *full scope IFPRU investment firm* (that is an *IFPRU 730k investment firm*) that had *relevant total assets* of £800bn on its last accounting reference date. Firm B is a *limited activity firm*.
 3. On the assumption that they were *solo Remuneration Code firms*, Firm A falls into *proportionality level one* and Firm B falls into *proportionality level three*.
 4. As a result of the *guidance* at paragraph ~~2-3.5~~ of Part C, both Firms A and B fall into *proportionality level one*.
- 6.3 Example 2:
1. Firm C is the *parent undertaking* of Firm D.
 2. Firm C is a *limited activity firm* and Firm D is a *full scope IFPRU investment firm* (that is an *IFPRU 730k investment firm*) that had *relevant total assets* of £100bn on its last accounting reference date.
 3. On the assumption that they were *solo Remuneration Code firms*, Firm C falls into *proportionality level three* and Firm D falls into *proportionality level one*.
 4. As a result of the *guidance* at paragraph ~~2-3.6~~ of Part C, both Firms C and D fall into *proportionality level one*.
- 6.4 Example 3
1. Company E is the *parent undertaking* of Firms F and G and Company H. Company H is the *parent undertaking* of Firm I. Firm J is a member of the group because of an *Article 12(1) consolidation relationship*.
 2. The firms and companies have the following characteristics:
 - e. Neither Companies E nor H are *Remuneration Code firms*;
 - f. Firm F is a *full scope IFPRU investment firm* (that is an *IFPRU 730k investment firm*) and that had *relevant total assets* of £40bn on its last accounting reference date;
 - g. Firms G and J are *limited activity firms*; and
 - h. Firm I is a *limited license firm* that had *relevant total assets* of £10bn on its last accounting reference date.

General Guidance

3. On the assumption that they were *solo Remuneration Code firms*
 - i. Firm F falls into *proportionality level two*;
 - j. Firms G and J fall into *proportionality level three*; and
 - k. Firm I falls into *proportionality level three*.
4. As a result of the *guidance* at paragraph ~~23~~3.5 in Part c, Firms F, G, I and J all fall into *proportionality level two*.

Role of individual guidance

- 6.5 Individual *guidance* may vary the *proportionality level* into which a *firm* would fall under the general *guidance* set out in Part C and supplemented by this Annex. In consequence, the definitions and thresholds provided in Part C do not provide an immutable classification.
- 6.6 The following provide non-exhaustive high level examples of where we might consider providing individual *guidance* to vary a *proportionality level*:
 1. Where a *firm* was just below the threshold for a particular *proportionality level* (as determined in accordance with Part C), but where features of its business model or growth strategy suggest that it should fall within the higher *proportionality level*.
 2. Where a *group of firms* contained several *firms* falling into a common *proportionality level*, but where the aggregate prudential risk posed by the *group* suggested that a higher *proportionality level* was more appropriate.
 3. Where a *firm* falls into a higher *proportionality level* as a result of the *guidance* at paragraph ~~23~~3.5 of Part C than would be the case on the assumption that it was a *solo Remuneration Code firm*, depending on the particular circumstances of the case.

Annex 4 (Part 2) – Finalised non-handbook guidance

General Guidance on Proportionality

The BIPRU Remuneration Code (SYSC 19C) and Pillar 3 disclosures on Remuneration (BIPRU 11)

1 July 2015

[Note: In this Annex, with the exception of paragraph numbers, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.]

1 Part A: Introduction and interpretations

Introduction

Status of guidance statement

- 1.1 This statement is general *guidance* given under section 139A (1) of the Financial Services and Markets Act (FSMA). It relates both to:
 1. the *BIPRU Remuneration Code* of SYSC 19C of the *FCA Handbook*, and
 2. the requirement to make Pillar 3 disclosures in relation to *remuneration* (in accordance with *BIPRU 11* of the *Handbook*).
- 1.2 Paragraphs ~~14 and 15~~1.13 and 1.14 make provision about the interpretation of this *guidance* statement. Expressions in italics either bear the meaning given in the *Handbook Glossary*, or in ~~the table in paragraph 15~~Table 1.
- 1.3 This *guidance* statement has effect from ~~1 January 2014~~ 1 July 2015.

Remuneration principles proportionality rule

- 1.4 The *BIPRU remuneration principles proportionality rule* is set out in SYSC 19C.3.3R (2).
- 1.5 The *BIPRU Remuneration Code* requires (amongst other things) a *firm* to apply requirements in SYSC 19C.3 to *BIPRU Remuneration Code staff*. The *BIPRU remuneration principles proportionality rule* requires a *firm*, when establishing and applying the total *remuneration* policies for *BIPRU Remuneration Code staff*, to comply with SYSC 19C.3 in a way and to the extent that is appropriate to its size, internal organisation and the nature, the scope and the complexity of its activities.

Guidance on the remuneration principles proportionality rule

- 1.6 General *guidance* is given in relation to specific aspects of the *remuneration principles proportionality rule* in SYSC 19C.3 itself.¹
- 1.7 Part C of this *guidance* statement provides additional general *guidance* in relation to the application of the *BIPRU remuneration principles proportionality rule* to *BIPRU Remuneration Code staff* who have, in relation to a given performance year, been *BIPRU Remuneration Code staff* for only part of the year.
- 1.8 This *guidance* statement represents our *guidance* in a field that may be subject to change, we intend to keep the *guidance* set out here under review.

Guidance on proportionality in relation to remuneration committees and Pillar 3 remuneration disclosures

- 1.9 The *BIPRU remuneration principles proportionality rule* does not apply to the requirement to establish a *remuneration* committee or to make disclosures in relation to *remuneration* under *BIPRU 11* (as part of Pillar 3). But these requirements are governed by similar proportionality tests, on which *guidance* is given in Parts D and E of this *guidance* statement.

Individual guidance

- 1.10 We may give individual *guidance* to a *firm*, either on its own initiative or on the application of the *firm*. Our policy on individual *guidance* is set out in *SUP 9*. In consequence, we may give individual *guidance* to a *firm* in relation to the *remuneration principles proportionality rule* (SYSC 19C.3.3R). Such *guidance* may relate to the application of the *rule* by the *firm* generally, or in specific areas.

Arrangement of guidance statement

- 1.11 This general *guidance* statement is divided into five Parts:
 1. This Part, Part A: Introduction & interpretation
 2. Part B: Guidance to BIPRU firms on the application of proportionality
 3. Part C: Guidance about part-year *Remuneration Code staff*.
 4. Part D: Remuneration committees.
 5. Part E: Pillar 3 *remuneration* disclosures (*BIPRU 11*).
- 1.12 It is supplemented by one Annex:
 1. Annex 1: Pillar 3 disclosure requirements by proportionality level

¹ The main provisions of guidance which specifically refer to the *remuneration principles proportionality rule* are SYSC 19C.3.34G (giving guidance in relation to *BIPRU Remuneration Code staff* and certain rules on *remuneration* structures).

Interpretation

- 1.13 This *guidance* statement is to be interpreted as if it was an Annex to SYSC 19C.3 (other than Part E and Annex 1, which are to be interpreted as if they were an Annex to BIPRU 11). In consequence, *GEN 2* (interpreting the *Handbook*) applies to the interpretation of this *guidance* statement.
- 1.14 In particular, an expression in italics which is defined in the *Glossary* has the meaning given there (*GEN 2.2.7R*). Where an expression in italics is not defined in the *Glossary*, it has the meaning given by the following table:

Table 1: Glossary of terms defined in this guidance statement

Defined expression	Definition
<i>group</i>	has the meaning given in the <i>Glossary</i> under paragraph (3).
<i>BIPRU Remuneration Code firm</i>	a <i>BIPRU firm</i> or <i>third country BIPRU firm</i> to which the <i>BIPRU Remuneration Code</i> applies (in accordance with SYSC 19C.1.1R).

2 Part B: Guidance to BIPRU firms on the application of proportionality

BIPRU firms that are part of a group

- 2.1 Where a *BIPRU Remuneration Code firm* is part of a *group* comprised only of *BIPRU Remuneration Code firms*, each *firm* should apply this guidance.
- 2.2 Where a *BIPRU Remuneration Code firm* is part of a *group* in which:
 1. a *firm* to which SYSC 19A applies is a member, this *guidance* does not apply, SYSC 19A and applicable *guidance* applies instead;
 2. a *firm* to which SYSC 19D applies is a member, this *guidance* does not apply, SYSC 19D and applicable *guidance* applies instead.

Disapplication of certain remuneration principles for BIPRU firms

- 2.3 It may not be necessary for *BIPRU firms* to apply *BIPRU remuneration* principles at all.
- 2.4 In our view, it will normally be appropriate for a *BIPRU firm* to disapply under the *BIPRU remuneration principles proportionality rule* the following *rules*
 1. retained *shares* or other instruments (SYSC 19C.3.47R);
 2. deferral (SYSC 19C.3.49R);
 3. performance adjustment (SYSC 19C.3.51R); and
 4. the ratios between fixed and variable components of total *remuneration* (SYSC 19C.3.44R).

BIPRU firms may 'take into account the specific features of their types of activities' in applying the 'requirement on the multi-year framework, in particular the accrual and ex-ante risk adjustment aspects of it'.²

- 2.6 However, *BIPRU firms* should also note that some *remuneration* principles set specific numerical criteria (such as on the minimum period of deferral, the minimum portion to be deferred and the minimum portion to be issued in *shares*). The following *guidance* applies where such principles apply to *BIPRU Remuneration Code staff* and are not capable of disapplication under the approach set out above. In such circumstances, we do not consider that the *remuneration principles proportionality rule* permits a *firm* to apply lower numerical criteria. (For the avoidance of doubt, this *guidance* does not apply where a *firm* chooses to use deferral or issuance in *shares* more widely than required by SYSC 19C.3, for example in order to comply with the *BIPRU Remuneration Code general requirement*.)

² As per FSA's Policy Statement 10/20. See link at http://www.fsa.gov.uk/pubs/policy/ps10_20.pdf.

3 Part C: Guidance about part-year BIPRU Remuneration Code staff

Introduction

- 3.1 SYSC 19C.3.34G provides *guidance* on when we do not generally consider it necessary for a *firm* to apply to certain *BIPRU Remuneration Code staff* certain *rules* relating to *remuneration* structures. This Part provides supplementary guidance on how certain *rules* on *remuneration* structures might normally be applied to *BIPRU Remuneration Code staff* who have, in relation to a given performance year, been *BIPRU Remuneration Code staff* for only part of the year.
- 3.2 In giving this *guidance*, we have taken account of the *remuneration principles proportionality rules*.³

Part-year Remuneration Code staff for more than three months

- 3.3 This paragraph applies where an individual (A) has, in relation to a given performance year, been *BIPRU Remuneration Code staff* for a period more than three months, but less than 12 months:
1. Sub-paragraphs (3) and (4) explain how the *guidance* in SYSC 19C.3.34G (as mentioned in the introduction to this Part) is to be applied in relation to A. Sub-paragraphs (5) and (6) provide that in certain circumstances it may be appropriate to apply certain *rules* to only a proportion of A's variable *remuneration*. Sub-paragraphs (7) to (9) provide examples;
 2. In this paragraph:
 - a. 'relevant fraction' means the fraction derived by dividing the number of days in the given performance year for which A has been *BIPRU Remuneration Code staff* by the number of days in the year;
 - b. 'qualifying fixed *remuneration*' means A's annual fixed *remuneration* in A's capacity as *BIPRU Remuneration Code staff* multiplied by the relevant fraction;
 - c. 'qualifying variable *remuneration*' means:
 - i. in the case where A was an *employee* of the *firm* for the whole of the given performance year, A's variable *remuneration* in relation to the performance year multiplied by the relevant fraction; and
 - ii. in the case where A was only ever employed in the given performance year as *BIPRU Remuneration Code staff*, A's actual variable *remuneration*.

³ As per FSA's Policy Statement 10/20. See link at http://www.fsa.gov.uk/pubs/policy/ps10_20.pdf.

- d. 'total qualifying *remuneration*' means qualifying fixed *remuneration* added to qualifying variable *remuneration*; and
 - e. 'threshold amount' means £500,000 multiplied by the relevant fraction.
3. We do not generally consider it necessary for a *firm* to apply the rules referred to in (4) where, in relation to A, the following conditions are satisfied:
 - a. Condition 1 is that A's qualifying variable *remuneration* is no more than 33% of total qualifying *remuneration*; and
 - b. Condition 2 is that A's total qualifying *remuneration* is no more than the threshold amount.
4. The rules referred to in (3) are those relating to:
 - a. guaranteed variable *remuneration* (SYSC 19C.3.40R);
 - b. retained *shares* or other instruments (SYSC 19C.3.47R);
 - c. deferral (SYSC 19C.3.49R); and
 - d. performance adjustment (SYSC 19C.3.51R).
5. Sub-paragraph (6) applies where the conditions in (3) are not satisfied and the *firm* should apply the rules referred to in (6).
6. Where this sub-paragraph applies, we generally consider that it would be appropriate to apply the following rules to qualifying variable *remuneration* only:
 - a. retained *shares* or other instruments (SYSC 19C.3.47R);
 - b. deferral (SYSC 19C.3.49R); and
 - c. performance adjustment (SYSC 19C.3.51R).
7. The examples in (8) and (9) illustrate this *guidance*. The performance year in each case is 1 January to 31 December.
8. Example 1
 - a. A1 is an *employee* of the *firm* through the performance year and is promoted to a *BIPRU Remuneration Code staff* role with effect from 1 September. A1's previous fixed *remuneration* was £150,000. In his *BIPRU Remuneration Code staff* role A1's fixed *remuneration* increases to £250,000. For the performance year, A1 is awarded variable *remuneration* of £130,000.
 - b. The relevant fraction is 122/365. A1's qualifying fixed *remuneration* is £83,560 (£250,000 multiplied by 122/365). A1's qualifying variable *remuneration* is £43,452 (£130,000 multiplied by 122/365). A1's total qualifying *remuneration* is 127,012. The threshold amount is £167,120 (£500,000 multiplied by 122/365).

- c. A1's total qualifying *remuneration* is below the threshold amount, so condition 2 of (3) is satisfied. But A1's qualifying variable *remuneration* is more than 33% of A1's total qualifying *remuneration*, and condition 1 of (3) is not satisfied.
 - d. The rule on guaranteed variable *remuneration* applies to A1. In addition, the *rules* on retained shares and other instruments, deferral and performance adjustment must be applied to A1's qualifying variable *remuneration* of £43,452.
9. Example 2
- a. A2 joins the *firm* as a *BIPRU Remuneration Code staff* member with effect from 1 July. A2's annual fixed *remuneration* is £450,000. For period of 1 June to 31 December, A2 is awarded variable *remuneration* of £50,000.
 - b. The relevant fraction is 184/365. A2's qualifying fixed *remuneration* is £226,850 (£450,000 multiplied by 184/365). A2's qualifying variable *remuneration* is £50,000 (the actual amount). A2's total qualifying *remuneration* is £276,850. The threshold amount is £252,050 (£500,000 multiplied by 184/365).
 - c. A2's qualifying variable *remuneration* is not more than 33% of A2's total qualifying *remuneration*, and condition 1 of (3) is satisfied. But A2's total qualifying *remuneration* is more than the threshold amount, so condition 2 of (3) is not satisfied.
 - d. The rule on guaranteed variable *remuneration* applies to A2. In addition, the *rules* on retained shares and other instruments, deferral and performance adjustment must be applied to A2's qualifying variable *remuneration* of £50,000.

Certain part-year Remuneration Code staff for three months or less

3.4 Paragraphs ~~25 and 26~~ 3.5 and 3.6 apply where:

1. an individual (B) has, in relation to a given performance year, been *BIPRU Remuneration Code staff* for a period of three months or less, and;
2. an exceptional or irregular payment (such as a sign-on award) has not been or is not to be made in relation to B's appointment as *BIPRU Remuneration Code staff*.

3.5 Where this paragraph applies, we do not generally consider it necessary to apply the following rules in relation to B for the performance year in question:

1. retained *shares* or other instruments (SYSC 19C.3.47R);
2. deferral (SYSC 19C.3.49R), and
3. performance adjustment (SYSC 19C.3.51R).

General Guidance

- 3.6 Where this paragraph applies, the *guidance* in paragraph ~~23(2), (3) and (4)(a)~~3.3 (2), (3) and (4)(a) should be applied for the purposes of determining whether or not it will generally be necessary to apply the rule on guaranteed variable *remuneration* to B (substituting in that paragraph, for references to 'A', references to 'B').

Part-year Remuneration Code staff for three months or less, but where exceptional etc. payments made

- 3.7 Paragraph ~~283.8~~ applies where an individual (C) has, in relation to a given performance year, been *BIPRU Remuneration Code staff* for a period of three months or less, but where an exceptional or irregular payment (such as a sign-on award) has or is to be made in relation to C's appointment
- 3.8 The *guidance* in paragraph ~~23.3~~3.3 applies in relation to C (substituting in that paragraph, for references to 'A', references to 'C'). The amount of exceptional or irregular payment is to be added to C's qualifying variable *remuneration* without pro rating.

4 Part D: Remuneration Committees

Remuneration Committee for BIPRU firms and third country BIPRU firms

- 4.1 Remuneration Principle 4 (Governance) provides, in SYSC 19C.3.12R(1), that a *BIPRU firm* that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities must establish a *remuneration* committee

- 4.2 With regards to larger *BIPRU firms*, it would be desirable for a *remuneration* committee to be established under SYSC 19C.3.12R and we would normally expect such *firms* to do so. However, we accept that it may be possible for such *firms* to justify on the ground of proportionality not establishing under SYSC 19C.3.12R at solo level a *remuneration* committee of the *BIPRU Remuneration Code firm*. In such circumstances it would be necessary to show how the functions which would otherwise have been performed by such a *remuneration committee* would be discharged with sufficient authority, and with sufficient independence from those performing executive functions within the *firm*. Where, for example, members of the *governing body* of the *firm* acted together with a *group remuneration committee* to discharge these functions, we would expect as a minimum to be satisfied that the operational arrangements ensured sufficient independence from those performing executive functions at *BIPRU Remuneration Code firm* or *group* level, and allowed the *governing body* of the *firm* to exercise sufficient authority in relation to the *BIPRU Remuneration Code firm*.

5 Part E: Pillar 3 Remuneration Disclosures (BIPRU 11)

Requirement to make Pillar 3 remuneration disclosures

- 5.1 *BIPRU 11* requires certain *Remuneration Code firm* to disclose a series of qualitative and quantitative information relating to *remuneration* (*BIPRU 11.3* and *BIPRU 11.5.18R*).
- 5.2 *BIPRU 11* applies only to *BIPRU firms*.

Pillar 3 remuneration disclosures and proportionality

- 5.3 Two proportionality tests apply in relation to the requirement to make Pillar 3 disclosures in relation to *remuneration*:
1. A *BIPRU firm* that is significant in terms of its size, internal organisation and the nature, scope and the complexity of its activities must also disclose the quantitative information referred to in *BIPRU 11.5.18R* at the level of *senior personnel* (*BIPRU 11.5.20R(1)*); and
 2. *BIPRU firms* must comply with the requirements set out in *BIPRU 11.5.18R* in a manner that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities (*BIPRU 11.5.20R (2)*).
- 5.4 In relation to the proportionality test referred to in paragraph ~~33(1)~~5.3 (1), the *FCA* considers that a *firm* should be regarded as 'significant' if on *relevant date* a *firm* has *relevant total assets* exceeding £50bn.
- 5.5 In relation to the proportionality test set referred to in paragraph ~~33(2)~~5.3 (2) the table in Appendix 1 sets out the categories of information that we consider *BIPRU firms* should typically disclose –where applicable.

Annex 1: Pillar 3 disclosure requirements by proportionality level

BIPRU 11.5.18R disclosure requirement
<i>BIPRU 11.5.18R (1) ('information concerning the decision-making process used for determining the remuneration policy, including if applicable, information about the composition and the mandate of a remuneration committee, the external consultant whose services have been used for the determination of the remuneration policy and the role of the relevant stakeholders')</i>
<i>BIPRU 11.5.18R (2) ('information on link between pay and performance')</i>
<i>BIPRU 11.5.18R (6) ('aggregate quantitative information on remuneration, broken down by business area')</i>
<i>BIPRU 11.5.18R (7) ('aggregate quantitative information on remuneration, broken down by senior management and members of staff whose actions have a material impact on the risk profile of the firm...')</i>

Annex 4 (Part 3) – Finalised non-handbook guidance

General Guidance on Proportionality

The Dual-regulated firms Remuneration Code (SYSC 19D)

1 July 2015

[Note: In this Annex, the following text is new and is not underlined]

1 Part A: Introduction and interpretations

Introduction and status of guidance statement

- 1.1 This statement is general *guidance* given under section 139A(1) of the Financial Services and Markets Act (FSMA). It relates to the *Dual-regulated firms Remuneration Code* of SYSC 19D of the *Handbook*.
- 1.2 Paragraphs 1.13 and 1.14 make provision about the interpretation of this *guidance* statement. Expressions in italics either bear the meaning given in the *Handbook Glossary*, or in Table 1.
- 1.3 This *guidance* statement has effect from 1 July 2015.

Dual-regulated firms remuneration principles proportionality rule

- 1.4 The *Dual-regulated firms remuneration principles proportionality rule* is set out in SYSC 19D.3.3R (2).
- 1.5 The *Dual-regulated firms Remuneration Code* requires (amongst other things) a *firm* to apply requirements in SYSC 19D.3 to *Dual-regulated firms Remuneration Code staff*. The *Dual-regulated firms remuneration principles proportionality rule* requires a *firm*, when establishing and applying the total *remuneration* policies for *Dual-regulated firms Remuneration Code staff*, to comply with SYSC 19D.3R in a way and to the extent that is appropriate to its size, internal organisation and the nature, the scope and the complexity of its activities.

Guidance on the Dual-regulated remuneration principles proportionality rule

- 1.6 General *guidance* is give in relation to specific aspects of the *Dual-regulated firms remuneration principles proportionality rule* in SYSC 19D.3.3R itself.¹

General Guidance

- 1.7 Part D of this *guidance* statement provides additional general *guidance* in relation to the application of the *Dual-regulated firms remuneration principles proportionality rule* to different types of *firm*.
- 1.8 Part E of this *guidance* statement provides additional general *guidance* in relation to the application of the *Dual-regulated firms remuneration principles proportionality rule* to *Dual-regulated firms Remuneration Code staff* who have, in relation to a given performance year, been *Dual-regulated firms Remuneration Code staff* for only part of the year.
- 1.9 This *guidance* statement represents our *guidance* in a field where requirements relating to *remuneration* are being implemented within the EEA. We recognise this will be an evolving process, and intend to keep the *guidance* set out here under review.

Individual guidance

- 1.10 We may give individual *guidance* to a *firm*, either on its own initiative or on the application of the *firm*. Our policy on individual *guidance* is set out in SUP 9. In consequence, we may give individual *guidance* to a *firm* in relation to the *remuneration principles proportionality rule* (SYSC 19D.3.3R). Such *guidance* may relate to the application of the *rule* by the *firm* generally, or in specific areas.

Arrangement of guidance statement

- 1.11 This general *guidance* statement is divided into five Parts:
 1. This Part, Part A: Introduction and interpretation;
 2. Part B: *Proportionality levels*;
 3. Part C: Division of firms into proportionality levels;
 4. Part D: Guidance to firms in particular proportionality level; and
 5. Part E: Guidance about part-year Dual-regulated firms Remuneration Code staff.
- 1.12 It is supplemented by Annex 1 – Supplemental guidance on dividing firms into proportionality levels.

¹ The main provisions of guidance which specifically refer to the *Dual-regulated firms remuneration principles proportionality rule* are SYSC 19D.3.35G (giving guidance in relation to *Dual-regulated firms Remuneration Code staff* and certain rules on *remuneration* structures).

Interpretation

- 1.13 This *guidance* statement is to be interpreted as if it was an Annex to SYSC 19D.3.3 R. In consequence, *GEN 2* (interpreting the Handbook) applies to the interpretation of this *guidance* statement.
- 1.14 In particular, an expression in italics which is defined in the *Glossary* has the meaning given there (*GEN 2.2.7R*). Where an expression in italics is not defined in the *Glossary*, it has the meaning given by the following table:

Table 1: Glossary of terms defined in this guidance statement

Defined expression	Definition
<i>group</i>	has the meaning given in the <i>Glossary</i> in paragraph (3)
<i>overseas Dual-regulated Remuneration Code firm</i>	an <i>overseas firm</i> that: (i) is not an <i>EEA firm</i> ; (ii) has its head office outside the <i>EEA</i> ; and (iii) would be a <i>building society</i> , a <i>bank</i> or a <i>UK designated investment firm</i> if it had been a <i>UK domestic firm</i> , had carried on all its business in the United Kingdom and had obtained whatever authorisation for doing so as required under the <i>Act</i> .
<i>proportionality level</i>	has the meaning given in paragraph 2.3, and references to <i>proportionality level one</i> , etc. are to be construed accordingly.
<i>Dual-regulated Remuneration Code firm</i>	a <i>firm</i> specified in SYSC 19D.1.1 R(1)(a)-(c).
<i>relevant total assets</i>	has the meanings given in paragraph 3.4 (3).
<i>relevant date</i>	has the meanings given in paragraph 3.4 (4).
<i>solo Dual-regulated Remuneration Code firm</i>	a <i>Dual-regulated Remuneration Code firm</i> which is not part of a <i>group</i> containing one or more further <i>Dual-regulated Remuneration Code firms</i> .

2 Part B: Proportionality Levels

- 2.1 SYSC 19D.1.1R provides that the *Dual-regulated firms Remuneration Code* applies to a *Dual-regulated Remuneration Code firm* and an *overseas Dual-regulated Remuneration Code firm*, in relation to the activities carried on from an establishment in the UK.
- 2.2 This *guidance* statement provides for the division of *Dual-regulated Remuneration Code firms* into three categories:
 - a. *proportionality level one*;
 - b. *proportionality level two*; and
 - c. *proportionality level three*.
- 2.3 The process by which firms are divided into *proportionality levels* is provided in Part C (as supplemented by Annex 1), and may also depend on individual *guidance*.
- 2.4 The *proportionality levels* provide a framework for the operation of the *remuneration principles proportionality rule*. *Guidance* is given to *firms* in different *proportionality levels* in Part D.

3 Part C: Process for dividing firms into proportionality levels

Overview

- 3.1 This Part provides the process by which a *Dual-regulated Remuneration Code firm* should ascertain the *proportionality level* into which it falls. Annex 1 provides supplementary *guidance* (including examples).
- 3.2 A *Dual-regulated Remuneration Code firm*, in order to ascertain its *proportionality level*, must first establish whether it is part of a *group* which contains one or more other *Dual-regulated Remuneration Code firms*:
1. If the *firm* is not part of such a *group* (a *solo Dual-regulated Remuneration Code firm*), its *proportionality level* will depend on its individual characteristics (as determined in accordance with paragraph 3.4).
 2. If the *firm* is part of such a *group*, its *proportionality level* will depend on a two-stage process (as provided in paragraphs 3.5 and 3.6).

(This requires all *Dual-regulated Remuneration Code firms* that are part of the *group* to fall into the highest *proportionality level* that any individual *Dual-regulated Remuneration Code firm* in the *group* would fall into on the assumption that it was a *solo Dual-regulated Remuneration Code firm*.)
- 3.3 Individual *guidance* may vary the *proportionality level* into which a *firm* would otherwise fall under paragraphs 3.4 to 3.6.

Solo Dual-regulated Remuneration Code firms

- 3.4 The following table shows the *proportionality level* into which a *solo Dual-regulated Remuneration Code firm* or an *overseas Dual-regulated Remuneration Code firm* falls:
1. A *firm* of the description given in the second column falls into the *proportionality level* listed in the first column;
 2. Where applicable, the *firm's proportionality level* will further depend on whether it held *relevant total assets* on the *relevant date* of the amount listed in the third column of the table (2);
 3. In (2) 'relevant total assets' means:
 - a. 'for a *Dual-regulated Remuneration Code firm*, the average of the *firm's total assets* on the *firm's last three relevant dates*; and
 - b. for an *overseas Dual-regulated Remuneration Code firm*, the average of the *firm's total assets* that covered the activities of the branch operation in the *United Kingdom* on the *firm's last three relevant dates*.

4. Relevant date means:
 - a. for *Dual-regulated Remuneration Code firm*, an accounting reference date; and
 - b. for overseas *Dual-regulated Remuneration Code firm* 'relevant date' means 31 December.
5. The limit confining *relevant total assets* to those that cover the activities of the bank operation in the *UK* is taken from *SUP 16.12.3R(1)(a)(iv)*, which relates to a reporting requirement in relation to *non-EEA banks* (among others). We consider that a *firm* which needs to ascertain its *relevant total assets* should apply the valuation requirements set out in the *EU CRR*.

Table 2: Proportionality levels: solo Dual-regulated Remuneration Code firms and overseas Dual-regulated Remuneration Code firms

Proportionality level	Type of firm	Relevant total assets on relevant date of firm
<i>Proportionality level one</i>	<i>UK Bank</i>	Exceeding £50bn
	<i>Building society</i>	Exceeding £50bn
	<i>UK designated investment firm that is a CRD full-scope firm</i>	Exceeding £50bn
<i>Proportionality level two</i>	<i>UK Bank.</i>	Exceeding £15bn but not exceeding £50bn
	<i>Building society.</i>	Exceeding £15bn, but not exceeding £50bn
	<i>UK designated investment firm that is a CRD full-scope firm</i>	Exceeding £15bn, but not exceeding £50bn
<i>Proportionality level three</i>	<i>UK Bank.</i>	Not exceeding £15bn
	<i>Building society.</i>	Not exceeding £15bn
	<i>Any UK designated investment firm that is a CRD full-scope firm that does not fall within proportionality level one or proportionality level two (in accordance with this Table).</i>	Not applicable
	<i>UK designated investment firm that is a limited licence firm.</i>	
	<i>UK designated investment firm that is a limited activity firm.</i>	

Groups with more than one Dual-regulated Remuneration Code firm

- 3.5 This paragraph applies where a *Dual-regulated Remuneration Code firm* is part of a group containing one or more other *Dual-regulated Remuneration Code firms*:
1. Each *Dual-regulated Remuneration Code firm* in the group must determine the *proportionality level* into which it would fall on the assumption it was a solo *Dual-regulated Remuneration Code firm*;
 2. Where each *Dual-regulated Remuneration Code firm* falls into the same *proportionality level* on the assumption that it was a solo *Dual-regulated Remuneration Code firm*, each firm falls into that *proportionality level*;
 3. Where the *Dual-regulated Remuneration Code firms* fall into different *proportionality levels* on the assumption that they were solo *Dual-regulated Remuneration Code firms*, each firm falls into the highest *proportionality level*; and
 4. For the purposes of (3), *proportionality level one* is the highest and *proportionality level three* is the lowest.
- 3.6 Annex 1 provides examples of this approach. A *firm* which has a higher *proportionality level* as a result of the *guidance* in paragraph 3.5 than would have been the case had the *firm* been a solo *Dual-regulated Remuneration Code firm* should note the scope to apply for individual *guidance* to vary its *proportionality level* (as discussed in paragraphs 6.5 and 6.6 of Annex 1).

4 Part D: guidance to firms in particular proportionality levels

Purpose of the proportionality levels

- 4.1 In relation to the *Dual-regulated firms remuneration principles proportionality rule*, the *proportionality levels* provide the following:
1. A framework for our supervisory approach, and a broad indication of expectations; and
 2. Guidance on which remuneration principles may normally be disapplied under the *Dual-regulated firms remuneration principles proportionality rule*.

Firms to continue to consider proportionality in their individual circumstances

- 4.2 It follows from the nature of the *Dual-regulated firms remuneration principles proportionality rule*, and the limited purposes noted in paragraph 4.1, that the *proportionality levels* do not provide comprehensive guidance on how the *Dual-regulated firms remuneration principles proportionality rule* will apply to a particular firm. A firm will still need to consider the application of the *Dual-regulated firms remuneration principles proportionality rule* to its individual circumstances.
- 4.3 A firm should bear in mind that the *Dual-regulated firms Remuneration Code* may require different responses from firms that fall into the same *proportionality level*. This is illustrated by the following example:
1. Firm A is a global bank with *relevant total assets* of £800bn, with substantial investment banking business, foreign exchange exposures and a complex business model seeking aggressive growth. It falls into *proportionality level one*.
 2. Firm B is a large mortgage and savings bank with *relevant total assets* of £100bn and a comparatively simple, conservative business model. It falls into *proportionality level one*.
 3. Firm C is a large building society, with *relevant total assets* of £25bn and a comparatively simple, conservative business model. It falls into *proportionality level two*.
 4. *Remuneration Principle 8* requires, amongst other things, a firm to risk-adjust performance measures to take account of all types of current and future risks (SYSC 19D.3.23R(1)(a)).
 5. Clearly the processes necessary to identify such risks will need to be more sophisticated for Firm A than for Firm B, despite the fact that they fall into the same *proportionality level*. Indeed, the difference in the necessary sophistication is likely to be greater as between Firm A and Firm B than as between Firm B and Firm C.

Disapplication of certain remuneration principles for firms in particular proportionality levels

- 4.4 The *CRD* can be interpreted such that it may not be necessary for certain *firms* to apply certain *remuneration* principles at all.²
- 4.5 In our view, it will normally be appropriate for a *firm* in *proportionality level three* to disapply under the *Dual-regulated firms remuneration principles proportionality rule one* or more of the following *rules*:
1. retained *shares* or other instruments (SYSC 19D.3.56R)
 2. deferral (SYSC 19D.3.59R)
 3. performance adjustment (SYSC 19D.3.61R – SYSC 19D.3.62R)

4.6 It may also be appropriate for:

1. *proportionality level three UK designated investment firm that is a CRD full-scope firm* to disapply the specific ratio between fixed and variable components of total *remuneration* (SYSC 19D.3.48R (3)); and
2. a *UK designated investment firm* that is a *limited licence firm* or a *limited activity firm* to disapply, under the *Dual-regulated firms remuneration principles proportionality rule*, the ratios between fixed and variable components of total *remuneration* (SYSC 19D.3.49R);

In both cases (1) and (2) above, if requested by the *FCA*, the *FCA* will expect the *firm's* senior management to be able to demonstrate why the *firm* believes it is reasonable to disapply it in the light of the *Dual-regulated firms remuneration principles proportionality rule*.

We are also of the opinion that such *firms* may 'take into account the specific features of their types of activities in applying the 'requirement on multi-year framework, in particular the accrual and ex- ante risk adjustment aspects of it.'³

- 4.7 However, *firms* should also note that some *remuneration* principles set specific numerical criteria (such as on the minimum period of deferral, the minimum portion to be deferred and the minimum portion to be issued in *shares*). The following *guidance* applies where such principles apply to *Dual-regulated firms Remuneration Code staff* and are not capable of disapplication under the approach set out above. In such circumstances, we do not consider that the *Dual-regulated firms remuneration principles proportionality rule* permits a *firm* to apply lower numerical criteria. (For the avoidance of doubt, this *guidance* does not apply where a *firm* chooses to use deferral or issuance in *shares* more widely than required by SYSC 19D.3).

² *CRD* Article 92(2) provides that the principles should be applied 'in a manner and to the extent that is appropriate to their size, internal organisation and the nature, the scope and complexity of their activities'.

³ As per the *FSA's* Policy Statement 10/20. See link http://www.fsa.gov.uk/pubs/policy/ps10_20.pdf

5 Part E: Guidance about part-year Dual regulated firms

Dual-regulated firms Remuneration Code staff introduction

- 5.1 SYSC 19D.3.35G provides *guidance* on when we do not generally consider it necessary for a *firm* to apply to certain *Dual-regulated firms Remuneration Code staff* certain *rules* relating to *remuneration* structures. This Part provides supplementary *guidance* on how certain *rules* on *remuneration* structures might normally be applied to *Dual-regulated firms Remuneration Code staff* who have, in relation to a given performance year, been *Dual-regulated firms Remuneration Code staff* for only part of the year
- 5.2 In giving this *guidance*, we have taken account of the *remuneration principles proportionality rule*.

Part-year Dual regulated firms Remuneration Code staff for more than three months

- 5.3 This paragraph applies where an individual (A) has, in relation to a given performance year, been *Dual-regulated firms Remuneration Code staff* for a period more than three months, but less than 12 months.
1. Sub-paragraphs (3) and (4) explain how the *guidance* in SYSC 19D.3.35G (as mentioned in the introduction to this Part) is to be applied in relation to A. Sub-paragraphs (5) and (6) provide that in certain circumstances it may be appropriate to apply certain *rules* to only a proportion of A's variable *remuneration*. Sub-paragraphs (7) to (9) provide examples;
 2. In this paragraph:
 - a. 'relevant fraction' means the fraction derived by dividing the number of days in the given performance year for which A has been *Dual-regulated firms Remuneration Code staff* by the number of days in the year; and
 - b. 'qualifying fixed *remuneration*' means A's annual fixed *remuneration* in A's capacity as *Dual-regulated firms Remuneration Code staff* multiplied by the relevant fraction.
 - c. 'qualifying variable *remuneration*' means:
 - (i). in the case where A was an *employee* of the *firm* for the whole of the given performance year, A's variable *remuneration* in relation to the performance year multiplied by the relevant fraction;
 - (ii) in the case where A was only ever employed in the given performance year as *Dual-regulated firms Remuneration Code staff*, A's actual variable *remuneration*.

- d. 'total qualifying *remuneration*' means qualifying fixed *remuneration* added to qualifying variable *remuneration*;
 - e. 'threshold amount' means £500,000 multiplied by the relevant fraction.
3. We do not generally consider it necessary for a firm to apply the rules referred to in (4) where, in relation to A, the following conditions are satisfied:
 - a. Condition 1 is that A's qualifying variable *remuneration* is no more than 33% of total qualifying *remuneration*, and
 - b. Condition 2 is that A's total qualifying *remuneration* is no more than the threshold amount.
4. The rules referred to in (3) are those relating to:
 - a. guaranteed variable *remuneration* (SYSC 19D.3.44R)
 - b. retained *shares* or other instruments (SYSC 19D.3.56R),
 - c. deferral (SYSC 19D.3.59R), and
 - d. performance adjustment (SYSC 19D.3.61R).
5. Sub-paragraph (6) applies where the conditions in (3) are not satisfied and the firm should apply the rules referred to in (6).
6. Where this sub-paragraph applies, we generally consider that it would be appropriate to apply the following rules to qualifying variable remuneration only:
 - a. retained shares or other instruments (SYSC 19D.3.56R)
 - b. deferral (SYSC 19D.3.59R)
 - c. performance adjustment (SYSC 19D.3.61R)
7. The examples in (8) and (9) illustrate this guidance. The performance year in each case is 1 January to 31 December.
8. Example 1
 - a. A1 is an *employee* of the *firm* through the performance year and is promoted to a *Dual-regulated firms Remuneration Code staff* role with effect from 1 September. A1's previous fixed *remuneration* was £150,000. In his *Dual-regulated firms Remuneration Code staff* role A1's fixed *remuneration* increases to £250,000. For the performance year, A1 is awarded variable *remuneration* of £130,000.
 - b. The relevant fraction is 122/365. A1's qualifying fixed *remuneration* is £83,560 (£250,000 multiplied by 122/365). A1's qualifying variable *remuneration* is £43,452 (£130,000 multiplied by 122/365). A1's total qualifying *remuneration* is £127,012. The threshold amount is £167,120 (£500,000 multiplied by 122/365).

- c. A1's total qualifying *remuneration* is below the threshold amount, so condition 2 of (3) is satisfied. But A1's qualifying *remuneration* is more than 33% of A1's total qualifying *remuneration*, and condition 1 of (3) is not satisfied.
 - d. The rule on guaranteed variable remuneration applies to A1. In addition, the *rules* on retained shares and other instruments, deferral and performance adjustment must be applied to A1's qualifying variable *remuneration* of £43,452.
9. Example 2
- a. A2 joins the *firm* as a *Dual-regulated firms Remuneration Code staff* member with effect from 1 July. A2's annual fixed *remuneration* is £450,000. For the period of 1 June to 31 December, A2 is awarded variable *remuneration* of £50,000.
 - b. The relevant fraction is 184/365. A2's qualifying fixed *remuneration* is £ 226,850 (£450,000 multiplied by 184/365). A2's qualifying variable *remuneration* is £50,000 (the actual amount). A2's total qualifying *remuneration* is £ 276,850. The threshold amount is £252,050 (£500,000 multiplied by 184/365).
 - c. A2's qualifying variable *remuneration* is not more than 33% of A2's total qualifying *remuneration*, and condition 1 of (3) is satisfied. But A2's total qualifying *remuneration* is more than the threshold amount, so condition 2 of (3) is not satisfied.
 - d. The rule on guaranteed variable *remuneration* applies to A2. In addition, the rules on retained shares and other instruments, deferral and performance adjustment must be applied to A2's qualifying remuneration of £50,000.

Certain part-year Dual regulated firms Remuneration Code staff for three months or less

5.4 Paragraphs 5.5 and 5.6 apply where:

1. an individual (B) has, in relation to a given performance year, been *Dual-regulated firms Remuneration Code staff* for a period of three months or less, and
2. an exceptional or irregular payment (such as a sign-on award) has not been or is not to be made in relation to B's appointment as *Dual-regulated firms Remuneration Code staff*.

5.5 Where this paragraph applies, we do not generally consider it necessary to apply the following rules in relation to B for the performance year in question:

- a. retained shares or other instruments (SYSC 19D.3.56R)
- b. deferral (SYSC 19D.3.59R)
- c. performance adjustment (SYSC 19D.3.61R)

General Guidance

- 5.6 Where this paragraph applies, the guidance in paragraph 5.3(2), 5.3 (3) and 5.3 (4)(a) should be applied for the purposes of determining whether or not it will generally be necessary to apply the rule on guaranteed variable *remuneration* to B (substituting in that paragraph, for references to 'A', references to 'B').

Part-year Dual regulated firms Remuneration Code staff for three months or less, but where exceptional etc. payments made

- 5.7 Paragraph 5.8 applies where an individual (C) has, in relation to a given performance year, been *Dual-regulated firms Remuneration Code staff* for a period of three months or less, but where an exceptional or irregular payment (such as a sign-on award) has or is to be made in relation to C's appointment.
- 5.8 The guidance in paragraph 5.3 applied in relation to C (substituting in that paragraph for references to 'A', references to 'C'). The amount of exceptional or irregular payment is to be added to C's qualifying variable *remuneration* without pro rating.

6 Annex 1: Supplemental guidance on dividing firms into proportionality levels

Groups with more than one Dual-regulated Remuneration Code staff firm: examples

6.1 The following non-exhaustive examples illustrate the operation of the guidance provided in paragraph 3.5 of Part C. (It should be borne in mind that in each case individual *guidance* could vary the outcome provided by the operation of the guidance provided in that paragraph.)

6.2 Example 1.

1. Firm A is the *parent undertaking* of Firm B.
2. Firm A is a *UK bank* that had *relevant total assets* of £800bn on its last accounting reference date. Firm B is a *limited activity firm*
3. On the assumption that they were solo *Dual-regulated Remuneration Code firms*, Firm A falls into *proportionality level one* and Firm B falls into *proportionality level three*.
4. As a result of the guidance at paragraph 3.5 of Part C, both Firms A and B fall into *proportionality level one*.

6.3 Example 2

1. Firm C is the *parent undertaking* of Firm D.
2. Firm C is a *limited activity firm* and Firm D is a *UK bank* that had *relevant total assets* of £100bn on its last accounting reference date.
3. On the assumption that they were solo *Dual-regulated Remuneration Code firms*, Firm C falls into *proportionality level three* and Firm D falls into *proportionality level one*
4. As a result of the *guidance* at paragraph 3.5 of Part C, both Firms C and D fall into *proportionality level one*.

6.4 Example 3

1. Company E is the *parent undertaking* of Firms F and G and Company H. Company H is the *parent undertaking* of Firm I. Firm J is a member of the *group* because of an *Article 12(1) consolidation relationship*.
2. The *firms* and companies have the following characteristics:
 - a. Neither Companies E nor H are *Dual-regulated Remuneration Code firms*;

- b. Firm F is an *UK designated investment firm* that is a *CRD full-scope firm* and that had *relevant total assets* of £40bn on its last accounting reference date;
 - c. Firms G and J are *limited activity firms*; and
 - d. Firm I is a *UK bank* that had *relevant total assets* of £10bn on its last accounting reference date.
3. On the assumption that they were *solo Dual-regulated Remuneration Code firms*:
 - a. Firm F falls into *proportionality level two*;
 - b. Firms G and J fall into *proportionality level three*; and
 - c. Firm I falls into *proportionality level three*.
4. As a result of the *guidance* at paragraph 3.5 of Part C, Firms F, G, I and J all fall into *proportionality level two*.

Role of individual guidance

- 6.5 Individual *guidance* may vary the *proportionality level* into which a *firm* would fall under the general *guidance* set out in Part C and supplemented by this Annex. In consequence, the definitions and thresholds provided in Part C do not provide an immutable classification.
- 6.6 The following provide non-exhaustive high level examples of where we might consider providing individual *guidance* to vary a *proportionality level*:
 1. Where a *firm* was just below the threshold for a particular *proportionality level* (as determined in accordance with Part C), but where features of its business model or growth strategy suggest that it should fall within the higher *proportionality level*.
 2. Where a *group of firms* contained several *firms* falling into a common *proportionality level*, but where the aggregate prudential risk posed by the *group* suggested that a higher *proportionality level* was more appropriate.
 3. Where a *firm* falls into a higher *proportionality level* as a result of the *guidance* at paragraph 3.5 of Part C than would be the case on the assumption that it was a *solo Dual-regulated Remuneration Code firm*, depending on the particular circumstances of the case.

Annex 5 – Finalised non-handbook guidance

General guidance on the application of ex-post risk adjustment to variable remuneration

1 July 2015

[Note: In this Annex, the following text is new and is not underlined]

1 Introduction

- 1.1 This statement is general guidance under section 139A(1) of the Financial Services and Markets Act 2000 (FSMA). This guidance statement has effect from 1 July 2015.
- 1.2 This guidance is aimed at all firms to whom the Financial Conduct Authority's Dual-regulated firms Remuneration Code in SYSC 19D¹ applies. Its main purpose is to set out the FCA's expectations of the way in which firms comply with the requirements on ex-post risk adjustment (also referred to as performance adjustment). Where firms consider an alternative approach to be justified in meeting the requirements on ex-post risk adjustment in the Dual-regulated firms Remuneration Code, this should be consistent with the general requirement to promote sound and effective risk management set out in SYSC 19D.2.1R.
- 1.3 The Prudential Regulation Authority (PRA) has also issued a Supervisory Statement (SS2/13) entitled 'PRA expectations regarding the application of malus to variable remuneration' published in October 2013².
- 1.4 The primary purpose of the Dual-regulated firms Remuneration Code is to ensure greater alignment between risk and individual reward, to discourage excessive risk taking and short-termism, and encourage more effective risk management, and in turn to support

¹ The creation of SYSC 19D has been consulted on in CP14/14.

² PRA expectations regarding the application of malus to variable remuneration (October 2013) is available at: <http://www.bankofengland.co.uk/pr/Documents/publications/policy/2013/appofmalusss2-13.pdf>.

positive behaviours and a strong and appropriate conduct culture within firms. This advances our objectives of securing an appropriate degree of protection for consumers and protecting and enhancing the integrity of the UK financial system.

- 1.5 The effective, meaningful and timely use of ex-post risk adjustment including malus, is essential to these aims.
- 1.6 Ex-post risk adjustment refers to the adjustment of variable remuneration to take account of a specific crystallised risk or adverse performance outcome including those relating to misconduct (a 'relevant event'). Ex-post risk adjustments include reducing current year awards, the application of malus (reducing or cancelling deferred incentive awards that have not yet vested), and clawback (recouping already vested awards).
- 1.7 The FCA expects firms to consider the application of ex-post risk adjustment for relevant events where there has been a materially adverse impact on any of the relevant criteria set out in 3.8. Ex-post risk adjustment should be applied as a minimum in the event of circumstances that fall within the meaning of SYSC 19D.3.62R - SYSC19D.3.64R including for material cases of misconduct.
- 1.8 The importance of ex-post risk adjustment has been underscored both in Directive 2013/36/EU (the Capital Requirements Directive or CRD), which requires up to 100% of the total variable remuneration to be subject to malus or clawback arrangements, and the Parliamentary Commission on Banking Standards' final report.
- 1.9 Firms should comply with the Dual-regulated firms Remuneration Code's provisions on risk and performance adjustment in their spirit as well as to the letter.
- 1.10 Where a firm has a Remuneration Committee, the FCA expects the Chair to ensure that the decisions taken by this committee on ex-post risk adjustment support the purpose and objectives of the Dual-regulated firms Remuneration Code to promote positive behaviours and culture within the firm.

2 Scope

- 2.1 All unvested variable remuneration should, in principle, be capable of forfeiture or recovery through ex-post risk adjustment. Deferred remuneration for the purposes of adjustment includes Long-Term Incentive Plans (LTIPs).
- 2.2 The use of ex-post risk adjustment should not be limited to employees who engaged directly in misconduct. In all cases, the FCA expects firms to consider applying ex-post risk adjustment to those employees whose roles and responsibilities include areas where failures or poor performance contributed to, or failed to prevent, the crystallisation of risk including cases of misconduct. Ex-post risk adjustment should be applied, including for individuals who:
- a. could have been reasonably expected to be aware of the failure, misconduct or weakness in approach that contributed to, or failed to prevent, the crystallisation of risk at the time but failed to take adequate steps to promptly identify, assess, report, escalate or address it; or
 - b. by virtue of their role or seniority are indirectly responsible or accountable for the relevant event, including senior staff who drive the firm's culture and set its strategy.
- 2.3 Section 2.2 above includes individuals within control functions (e.g. compliance, risk, internal audit etc.) for the weaknesses and failings identified within these functions. The FCA expects firms to place primary responsibility on the business for meeting standards expected of them and expects the amount and nature of adjustments made to control functions to reflect that allocation of responsibility.
- 2.4 The FCA expects all firms subject to ex-post risk adjustment to have a firm-wide policy on the application of ex-post risk adjustment (and group-wide policy, where appropriate) for staff subject to the relevant Dual-regulated firms Remuneration Code for whom the latter can be partially dis-applied due to their level of earnings under the proportionality rule.

3 Expectations in relation to the application of ex-post risk adjustment

- 3.1 Firms' remuneration policies and employment contracts should make it clear that variable remuneration awards are conditional, discretionary and contingent upon a sustainable and risk-adjusted performance. They are therefore capable of forfeiture or reduction at the employer's discretion.
- 3.2 Ex-post risk adjustment can be applied collectively at bonus pool level, to groups of employees and to individuals. Firms should apply an appropriate balance of ex-post risk adjustments across these levels.
- 3.3 The primary focus in applying ex-post risk adjustments should be on individuals. Collective ex-post risk adjustments are likely to be appropriate -where there are widespread failings or to meet all or a significant part of the cost of regulatory action and fines, redress and other associated costs from bonus pools. Where a relevant event has a material impact on any of the relevant criteria in paragraph 3.8, the FCA expects to see a similarly material adjustment as a proportion of a firm's bonus pool.
- 3.4 Where the misconduct, failings or poor performance which led to a relevant event occurred primarily in particular business units or divisions, collective adjustments should be weighted towards those areas.
- 3.5 Firms should ensure that individuals do not profit from a relevant event. Firms should consider the extent to which past bonuses were earned as a result of identified failings and also give appropriate consideration to the cost of consequent redress and other financial impacts. Firms should apply further ex-post risk adjustment to reflect this and should do so robustly and fairly.
- 3.6 In considering how much further ex-post risk adjustment to apply to individuals, the FCA expects firms to consider the degree of culpability, involvement or responsibility of an individual and the relevant criteria listed in paragraph 3.8.
- 3.7 For cases with a high degree of personal responsibility and a high impact in relation to any of the relevant criteria in paragraph 3.8, up to 100% ex-post risk adjustment should be the starting point. For lower degrees of responsibility and impact, proportionately less ex-post risk adjustment may be applied. In all cases, firms should ensure that the size of ex-post reductions reflect the severity of the relevant event, are material in size and are sufficient to drive positive individual behaviours and culture within the firm.
- 3.8 When deciding the amounts to be adjusted, the FCA expects firms to take into account all relevant criteria, including:

- a. The impact on the firm's customers, counterparties and the wider market;
- b. The impact of the failure on the firm's relationships with its other stakeholders including shareholders, employees, creditors, the taxpayer and regulators;
- c. The cost of fines and other regulatory actions (e.g. Section 166 of FSMA reviews);
- d. Direct and indirect financial losses attributable to the relevant failure; and
- e. Reputational damage.

4 Timing in the consideration of ex-post risk adjustment

- 4.1 Firms should start to consider ex-post risk adjustment once relevant events have been identified and impose reductions as soon as reasonably possible.
- 4.2 Where ex-post risk adjustments are made to current or prior year awards before the full impact of the relevant event is known, subsequent consideration and, where appropriate, subsequent adjustments should be made to ensure the final value of the adjustment fully reflects the impact of the incident.
- 4.3 Firms should update the FCA on any relevant pending investigations and ahead of any payment of outstanding awards to individuals under investigation for misconduct.
- 4.4 Risk management failures and misconduct can take years to come to light. This should not prevent firms from applying ex-post risk adjustment to the extent that the relevant individuals have variable remuneration capable of reduction, even where this does not relate to performance in the year in which the relevant event occurred or came to light.
- 4.5 Firms should freeze the vesting of all variable remuneration potentially due to individuals undergoing internal or external investigation that could result in material ex-post risk adjustment until such an investigation has concluded and the firm has made a decision and communicated it to the relevant employee(s). This does not preclude the vesting of some or all variable remuneration in relation to particular individuals once the firm has established with certainty that ex-post risk adjustment of these amounts is not required.

5 Procedure for considering ex-post risk adjustment

- 5.1 The FCA expects firms to develop and maintain an adequate procedure for deciding cases that could result in the use of ex-post risk adjustment as part of or alongside regular internal performance management and disciplinary proceedings. This procedure should:
- a. Identify which roles, departments, functions and committees are responsible for identifying, escalating and deciding cases that may trigger the use of ex-post risk adjustment.
 - b. Ensure that control functions including Internal Audit, Compliance, Finance, Human Resources, Legal, Reward and Risk provide relevant information and contribute to discussions as required.
 - c. Set out clear criteria on the kind of cases that may trigger the use of ex-post risk adjustment. These criteria should be indicative and non-exhaustive. Remuneration Committees should retain full discretion to introduce additional criteria where appropriate.
 - d. Set out a clear process for determining the degree of culpability, responsibility or accountability, including allowing individuals under investigation to make representations.
 - e. Promote consistency, fairness and robustness in the application of ex-post risk adjustment.
 - f. Firms should ensure that the initial process for determining bonus pools is sufficiently transparent to enable them to quantify and articulate clearly the impact of any ex-post risk adjustments they might make prior to them being approved.
 - g. Clearly record the value of awards and the rationale for why they are that size prior to and following ex-post risk adjustments being applied.
 - h. Clearly record the value of the adjustments made at individual, business unit and firm levels so that it is possible to determine the value of each adjustment per incident and at the individual employee level. Firms should make consistent judgments and be able to explain how adjustments have been made and why any differences exist between incidents or the individuals concerned.
 - i. Ex-post risk adjustments should be applied separately after all other factors relevant to setting awards (including those set out in Principle 8 - Profit-based measurement and risk adjustment- and Principle 12b -Remuneration structures – assessment of performance) have been considered to ensure that subsequent adjustments are not

made that would reduce or undermine the effect of ex-post risk adjustment at bonus pool or individual level.

- j. Firms should ensure that the value of ex-post risk adjustments made to an individual's variable remuneration and the reasons for the adjustments are clearly communicated to the affected individuals in writing and that the value and reasons for collective adjustments are clearly communicated to staff as a group.

- 5.2 The operation of an effective procedure for considering ex-post risk adjustment is not a substitute for taking account of known increases in risk as they arise, including those relating to conduct. The FCA would expect firms to take these risks into account including for example, where weaknesses in systems and controls have been identified or where there is an increased level of customer complaints, when determining the appropriate size and value of new awards.

6 Co-operation with the FCA

- 6.1 Firms are expected to provide the FCA with information on their application of ex-post risk adjustment as requested. This information should be sufficient for the FCA to assess the firm's ex-post risk adjustment decisions.

- 6.2 Where a firm's policies and practices on variable remuneration are under review by the FCA, these firms should comply with the timetable set by the regulators, providing sufficient time for the FCA to form a view before the date by which they intend to communicate and distribute their awards. Please refer to the FCA and PRA websites for the most up-to-date data collection templates and review timetable.

- 6.3 Where a firm does not meet the timetable set by the regulators, there is likely to be a commensurate impact in the provision of the FCA's view to the firm which may delay the firm's own timetable for communicating and distributing awards