

Chapter 19C

BIPRU Remuneration Code

19C.1 General application and purpose

Who? What? Where?

- 19C.1.1** **R** (1) The *BIPRU Remuneration Code* applies to a *BIPRU firm* and a *third country BIPRU firm*.
- (2) In relation to a *third country BIPRU firm*, the *BIPRU Remuneration Code* applies only in relation to activities carried on from an establishment in the *United Kingdom*.
- 19C.1.1A** **G** The *AIFM Remuneration Code* (■ SYSC 19B) also applies to a *BIPRU firm* which is a *full-scope UK AIFM* (ie, a *full-scope UK AIFM* that is an *AIFM investment firm* subject to *BIPRU*). Such a *full-scope UK AIFM* that complies with ■ SYSC 19B will also comply with ■ SYSC 19C. In such cases, the *FCA* will not require the *full-scope UK AIFM* to demonstrate compliance with ■ SYSC 19C.
- 19C.1.1B** **G** (1) The *UCITS Remuneration Code* (■ SYSC 19E) also applies to a *BIPRU firm* that is a *UK UCITS management company* (that is, a *UK UCITS management company* that is a *UCITS investment firm* subject to *BIPRU*).
- (2) A *BIPRU firm* that is a *UK UCITS management company* will meet its obligations under ■ SYSC 19C and ■ SYSC 19E by complying with ■ SYSC 19E.
- (3) Under (1) and (2), the *FCA* will not require the *UK UCITS management company* to demonstrate compliance with ■ SYSC 19C.
- 19C.1.2** **G** Part 2 of ■ SYSC 1 Annex 1 provides for the application of ■ SYSC 4.1.1 R and ■ SYSC 4.1.1C R (General Requirements). In particular, and subject to the provisions on group risk systems and controls requirements in ■ SYSC 12, this means that:
- (1) the *BIPRU Remuneration Code*:
- (a) applies to *regulated activities*, *ancillary activities* and applicable *ancillary services*; and
 - (b) [deleted]
 - (c) takes into account activities of other *group* members; and
- (2) where the *BIPRU Remuneration Code* applies, it applies to:

- (a) a *firm's* UK activities;
- (b) a *firm's* *passported* activities carried on from a *branch* in another EEA State; and
- (c) a UK domestic *firm's* activities wherever they are carried on, in a *prudential context*.

When?

- 19C.1.3 **R** A *firm* must apply the *remuneration* requirements in ■ SYSC 19C.3 to:
- (1) *remuneration* awarded, whether under a contract or otherwise, on or after 1 January 2014;
 - (2) *remuneration* due on the basis of contracts concluded before 1 January 2014 which is awarded or paid on or after 1 January 2014; and
 - (3) *remuneration* awarded, but not yet paid, before 1 January 2014, for services provided in 2013.

- 19C.1.4 **G** Subject to the requirements of ■ SYSC 19C.1.5 R, in the *FCA's* view ■ SYSC 19C.1.3 R does not require a *firm* to breach requirements of applicable contract or employment law.

- 19C.1.5 **R**
- (1) This *rule* applies to a *firm* that is unable to comply with the *BIPRU Remuneration Code* because of an obligation it owes to a *BIPRU Remuneration Code staff member* under a provision of an agreement made on or before 29 July 2010.
 - (2) A *firm* must take reasonable steps to amend or terminate the provision in (1) in a way that enables it to comply with the *BIPRU Remuneration Code* at the earliest opportunity.
 - (3) Until the provision in (1) ceases to prevent the *firm* from complying with the *BIPRU Remuneration Code*, the *firm* must adopt specific and effective arrangements, processes and mechanisms to manage the risks raised by the provision.

Purpose

- 19C.1.6 **G** The aim of the *BIPRU 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.

Notifications to the FCA

- 19C.1.7 **G**
- (1) The *BIPRU 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) In particular, in relation to *remuneration* matters, such 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 *BIPRU Remuneration Code*;
 - (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 *firms* risk profile or resources; and
 - (d) fraud, errors and other irregularities described in ■ SUP 15.3.17 R which may suggest weaknesses in, or be motivated by, the *firm's* *remuneration* policies, procedures or practices.
- (3) Such notifications should be made immediately the *firm* becomes aware of those circumstances, or has information which reasonably suggests that those circumstances have, or may have, occurred or may occur in the foreseeable future.

Individual guidance

19C.1.8

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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 9.2.5 G). 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 *BIPRU Remuneration Code*, including the general requirement for *remuneration* policies, procedures and practices to be consistent with and promote sound and effective risk management.



19C.2 General requirement

Remuneration policies must promote effective risk management

- 19C.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.
- 19C.2.2 **G**
 - (1) If a firm's remuneration policy is not aligned with effective risk management, it is likely that employees will have incentives to act in ways that might undermine effective risk management.
 - (2) The BIPRU 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. In applying the BIPRU Remuneration Code, a firm should have regard to applicable good practice on remuneration and corporate governance, such as guidelines on executive contracts and severance produced by the Association of British Insurers (ABI) and the National Association of Pension Funds (NAPF). In considering the risks arising from its remuneration policies, a firm will also need to take into account its statutory duties in relation to equal pay and non-discrimination.
 - (3) As with other aspects of a firm's systems and controls, in line with SYSC 4.1.2 R and SYSC 4.1.2AA R, remuneration policies, procedures and practices must be comprehensive and proportionate to the nature, scale and complexity of the firm's activities. Therefore, what a firm must do to comply with the BIPRU Remuneration Code will vary. For example, while the BIPRU 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.
 - (4) The principles in the BIPRU Remuneration Code are used by the FCA to assess the quality of a firm's remuneration policies and whether they encourage excessive risk-taking by a firm's employees.
 - (5) The FCA may also ask remuneration committees to provide the FCA with evidence of how well the firm's remuneration policies meet the BIPRU 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)*.

(6) The *BIPRU Remuneration Code* is principally concerned with the risks created by the way *remuneration* arrangements are structured, not with the absolute amount of *remuneration*, which is generally a matter for *firms' remuneration* committees.

19C.2.3 G

- (1) The specific *remuneration* requirements in this chapter may apply only to certain categories of *employee*. However, the *FCA* expects *firms*, in complying with the *BIPRU Remuneration Code* general requirement, to apply certain principles on a *firm-wide* basis.
- (2) In particular, the *FCA* considers that *firms* should apply the principle relating to guaranteed variable *remuneration* on a *firm-wide* basis (Remuneration Principle 12(c); ■ SYSC 19C.3.40 R to ■ SYSC 19C.3.43 G.
- (3) The *FCA* also expects *firms* to apply, as a minimum, the principles relating to risk management and risk tolerance (Remuneration Principle 1); supporting business strategy, objectives, values and long-term interests of the firm (Remuneration Principle 2); conflicts of interest (Remuneration Principle 3); governance (Remuneration Principle 4); risk adjustment (Remuneration Principle 8); pension policy (Remuneration Principle 9); personal investment strategies (Remuneration Principle 10); payments related to early termination (Remuneration Principle 12(e)) and deferral (Remuneration Principle 12(g)) on a *firm-wide* basis.

Record-keeping.....

19C.2.4 G

In line with the record-keeping requirements in ■ SYSC 9, a *firm* should ensure that its *remuneration* policies, practices and procedures are clear and documented. Such policies, practices and procedures would include performance appraisal processes and decisions.

Interpretation of references to remuneration.....

19C.2.5 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*.

19C.2.6 G

Remuneration includes, for example, payments made by a seconding organisation which is not subject to the *BIPRU Remuneration Code* to a secondee in respect of their employment by a *firm* which is subject to the *BIPRU Remuneration Code*.

19C.3 Remuneration principles

Application: groups

- 19C.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 outside the *United Kingdom*.
- (2) Paragraph (1) does not limit ■ SYSC 12.1.13 R and ■ SYSC 12.1.15 R (which relate to the application of the *BIPRU Remuneration Code* within *UK consolidation groups* and *non-UK sub-groups*).

- 19C.3.2 **G** The effect of ■ SYSC 12.1.13 R (2)(dA) and ■ SYSC 12.1.15 R is that the *firm* is required to ensure that the risk management processes and internal control mechanisms at the level of any *consolidation group* or *non-UK sub-group* of which a *firm* is a member comply with the obligations set out in this section on a consolidated (or sub-consolidated) basis.

Application: categories of staff and proportionality

- 19C.3.3 **R** (1) This section applies to *BIPRU Remuneration Code staff*, except as set out in (3).
- (2) When establishing and applying the total *remuneration* policies for *BIPRU 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, scope and complexity of its activities (the *BIPRU remuneration principles proportionality rule*).
- (3) Paragraphs (1) and (2) do not apply to the requirement for significant *firms* to have a *remuneration committee* (■ SYSC 19C.3.12 R).

[**Note:** In addition to the *guidance* in this section which relates to the *BIPRU remuneration principles proportionality rule*, the *FCA* has published *guidance* on the operation of the *BIPRU remuneration principles proportionality rule*. This *guidance* is available at www.fca.org.uk/firms/remuneration.]

- 19C.3.4 **R** *BIPRU 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.

19C.3.5

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A firm must:

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

19C.3.6

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(1) In the FCA's view:

- (a) a firm's staff includes its employees;
- (b) a person who performs a significant influence function for, or is a senior manager of, a firm would normally be expected to be part of the firm's *BIPRU Remuneration Code* staff;
- (c) the table in (2) provides a non-exhaustive list of examples of key positions that should, subject to (d), be within a firm's definition of staff who are risk takers;
- (d) firms should consider how the examples in the table in (2) apply to their own organisational structure;
- (e) firms may find it useful to set their own metrics to identify their risk takers based, for example, on trading limits; and
- (f) a firm should treat a person as being *BIPRU Remuneration Code* staff in relation to *remuneration* in respect of a given performance year if they were *BIPRU Remuneration Code* staff for any part of that year.

[Note: The FCA has published guidance on the application of particular rules on *remuneration* structures in relation to individuals who are *BIPRU Remuneration Code* staff for only part of a given performance year. This guidance is available at www.fca.org.uk/firms/remuneration

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(2) High-level category	Suggested business lines
Heads of significant business lines (including regional heads) and any individuals or groups within their control who have a material impact on the firm's risk profile	Fixed income
	Foreign exchange
	Commodities
	Securitisation
	Sales areas
	Investment banking (including mergers and acquisitions advisory)
	Commercial banking
	Equities
	Structured finance
	Lending quality
	Trading areas

(2) High-level category	Suggested business lines
Heads of support and control functions and other individuals within their control who have a material impact on the <i>firm's</i> risk profile	Research
	Credit/market/operational risk
	Legal
	Treasury controls
	Human resources
	Compliance
	Internal audit

Remuneration Principle 1: Risk management and risk tolerance

19C.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*.

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

19C.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*.

Remuneration Principle 3: Avoiding conflicts of interest

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

Remuneration Principle 4: Governance

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

19C.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 *governing body* in its *supervisory function*.

19C.3.12 **R**

- (1) A *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.
- (2) The *remuneration* committee must be 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.
- (3) The chairman and the members of the *remuneration* committee must be members of the *governing body* who do not perform any executive function in the *firm*.

- (4) The *remuneration* committee must be 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 *governing body* in its *supervisory function*.
- (5) When preparing such decisions, the *remuneration* committee must take into account the long-term interests of shareholders, investors and other stakeholders in the *firm*.

[Note: The *guidance* referred to in the note to ■ SYSC 19C.3.3 R also gives *guidance* on proportionality in relation to *remuneration* committees]

19C.3.13 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 *BIPRU Remuneration Code* and, where relevant, should take into account relevant guidance, such as that issued by the International Organization of Securities Commissions (IOSCO).
- (3) The periodic review of the implementation of the *remuneration* policy should assess compliance with the *BIPRU Remuneration Code*.
- (4) Guidance on what the *supervisory function* might involve is set out in ■ SYSC 4.3.3 G.

Remuneration Principle 5: Control functions

19C.3.14 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 staff; and
 - (b) in line with the achievement of the objectives linked to their functions, independent of the performance of the business areas they control.

19C.3.15 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 19C.3.14R (2)).

19C.3.16 **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 19C.3.12 R, or, if such a committee has not been established, by the *governing body* in its *supervisory function*.

19C.3.17 **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 do 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* generally expects 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 6.1.4 R (4) article 22(3) of the *MiFID Org Regulation*).

Remuneration Principle 6: Remuneration and capital

19C.3.18 **R** A *firm* must ensure that total variable *remuneration* does not limit the *firm's* ability to strengthen its capital base.

19C.3.19 **G** This Remuneration Principle underlines the link between a *firm's* variable *remuneration* costs and the need to manage its capital base, including forward-looking capital planning measures. Where a *firm* needs to strengthen its capital base, its variable *remuneration* arrangements should be sufficiently flexible to allow it to direct the necessary resources towards capital building.

Remuneration Principle 7: Exceptional government intervention

19C.3.20 **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 alignment with sound risk management and long-term growth, including when appropriate establishing limits to the *remuneration* of *senior personnel*; and
- (3) no variable *remuneration* is paid to its *senior personnel* unless justified.

19C.3.21 **G** The *FCA* would normally expect it to be appropriate for the ban on paying variable *remuneration* to *senior personnel* of a *firm* that benefits from exceptional government intervention to apply only in relation to *senior personnel* who were in office at the time that the intervention was required.

Remuneration Principle 8: Profit-based measurement and risk adjustment

19C.3.22 **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, taking 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.

19C.3.23 **G** (1) This Remuneration Principle stresses the importance of risk adjustment in measuring performance, and the importance of applying judgment and common sense. 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.

(2) A number of risk-adjustment techniques and measures are available, and a *firm* should choose those that are most appropriate to its circumstances. Common measures include those that are based on economic profit or economic capital. Whichever technique is chosen, the full range of future risks should be covered. The *FCA* expects a *firm* to be able to provide it with details of all adjustments that the *firm* has made under a formulaic approach.

- (3) The *FCA* expects a *firm* to apply qualitative judgments and common sense in the final decision about the performance-related components of variable *remuneration* pools.
- (4) A *firm's governing body* (or *remuneration committee*, where appropriate) should take the lead in determining the measures to be used. It should offer the appropriate checks and balances to prevent inappropriate manipulation of the measures used. It should consult closely and frequently with the *firm's* risk management functions, in particular those relating to operational, market, credit and liquidity risk.

19C.3.24 **G**

- (1) Long-term incentive plans should be treated as pools of variable *remuneration*. Many common measures of performance for long-term incentive plans, such as earnings per *share* (EPS), are not adjusted for longer-term risk factors. Total shareholder return (TSR) includes dividend distributions in its measurement, which can also be based on unadjusted earnings data. If incentive plans mature within a two- to four-year period and are based on EPS or TSR, strategies can be devised to boost EPS or TSR during the life of the plan, to the detriment of the longer-term health of a *firm*. For example, increasing leverage is a technique which can be used to boost EPS and TSR. *Firms* should take account of these factors when developing risk-adjustment methods.
- (2) *Firms* that have long-term incentive plans should structure them with vesting, subject to appropriate performance conditions, and at least half of the award vesting after not less than five years and the remainder after not less than three years.
- (3) Long-term incentive plan awards may be included in the calculation of the deferred portion of variable *remuneration* only if upside incentives are adequately balanced by downside adjustments. The valuation of the award should be based on its value when the award is granted, and determined using an appropriate technique.

19C.3.25 **R**

Assessments of financial performance used to calculate variable *remuneration* components or pools of variable *remuneration* components must be based principally on profits.

19C.3.26 **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 as to enable a *firm* to see as accurate a picture of contributions of relevant staff to a *firm's* performance, as reasonably practicable. If revenue or turnover is used as a component in performance assessment, processes should be in place to ensure that the quality of business undertaken or services provided and their appropriateness for *clients* are taken into account.

19C.3.27 **R** 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.

[Note: Standard 5 of the *FSB Compensation Standards*]

19C.3.28 **G** Where a *firm* makes a loss, the *FCA* generally expects no variable *remuneration* to be awarded. Variable *remuneration* may nevertheless be justified, for example to incentivise *employees* involved in new business ventures which could be loss-making in their early stages.

Remuneration Principle 9: Pension policy

19C.3.29 **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 19C.3.47R (1); and
- (3) when *employees* reach retirement, *discretionary pension benefits* are paid to the *employee* in the form of instruments in ■ SYSC 19C.3.47R (1) and subject to a five-year retention period.

Remuneration Principle 10: Personal investment strategies

- 19C.3.30** **R**
- (1) A *firm* must ensure that its *employees* undertake not to use personal hedging strategies or *remuneration-* or liability-related *contracts of insurance* to undermine the risk-alignment effects embedded in their *remuneration* arrangements.
 - (2) A *firm* must maintain effective arrangements designed to ensure that *employees* comply with their undertaking.

19C.3.31 **G** Circumstances in which a *person* will be using a personal hedging strategy include entering into an arrangement with a third party under which the third party will make payments, directly or indirectly, to that *person* linked to, or commensurate with, the amounts by which the *person's remuneration* is subject to reductions.

Remuneration Principle 11: Avoidance of the Remuneration Code

19C.3.32 **R** A *firm* must ensure that variable *remuneration* is not paid through vehicles or methods that facilitate the avoidance of the *BIPRU Remuneration Code*.

Remuneration Principle 12: Remuneration structures - introduction

19C.3.33 **G** This Remuneration Principle consists of a series of *rules, evidential provisions* and *guidance* relating to *remuneration* structures.

19C.3.34 **G**

(1) Taking account of the *BIPRU 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 requires that X's variable *remuneration* is no more than 33% of total *remuneration*; and

(b) condition 2 requires that X's total *remuneration* is no more than 500,000.

(2) The *rules* referred to in (1) relate to:

(a) guaranteed variable *remuneration* (■ SYSC 19C.3.40 R);

(b) retained *shares* or other instruments (■ SYSC 19C.3.47 R);

(c) deferral (■ SYSC 19C.3.49 R); and

(d) performance adjustment (■ SYSC 19C.3.51 R).

[**Note:** The *FCA* has published *guidance* on the application of certain *rules* on *remuneration* structures in relation to individuals who are *BIPRU Remuneration Code staff* for only part of a given performance year. This guidance is available at www.fca.org.uk/firms/remuneration.]

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

19C.3.35 **R** A *firm* must ensure that the structure of an *employee's remuneration* is consistent with, and promotes, effective risk management.

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

19C.3.36 **R** 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.

19C.3.37 **G** Non-financial performance metrics should form a significant part of the performance assessment process and should include adherence to effective risk management and compliance with the *regulatory system* and with relevant overseas regulatory requirements. Poor performance as 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. The performance assessment process and the importance of non-financial assessment factors in the process should be clearly explained to relevant *employees* and implemented. A balanced scorecard can be a good technique.

19C.3.38 R A *firm* must ensure that the assessment of performance is set in a multi-year framework, 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.

19C.3.39 G The requirement for assessment of performance to be in a multi-year framework reflects the fact that profits from a *firm's* activities can be volatile and subject to cycles. The financial performance of *firms* and individual *employees* can be exaggerated as a result. Performance assessment on a moving average of results can be a good way of meeting this requirement. However, other techniques, such as good quality risk adjustment and deferral of a sufficiently large proportion of *remuneration*, may also be useful.

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

19C.3.40 R A *firm* must not award, pay or provide guaranteed variable *remuneration* unless it:

- (1) is exceptional;
- (2) occurs in the context of hiring new *BIPRU Remuneration Code staff*; and
- (3) is limited to the first year of service.

19C.3.41 E (1) A *firm* should not award, pay or provide guaranteed variable *remuneration* in hiring new *BIPRU Remuneration Code staff* (X) unless:

- (a) it has taken reasonable steps to ensure that the *remuneration* is not more generous in its amount or terms (including any deferral or retention periods) than the variable *remuneration* awarded or offered by X's previous employer; and
- (b) it is subject to appropriate performance adjustment requirements.

(2) Contravention of (1) may be relied on as tending to establish contravention of the *rule* on guaranteed variable *remuneration* (■ SYSC 19C.3.40 R).

19C.3.42 G Guaranteed variable *remuneration* should be subject to the same deferral criteria as other forms of variable *remuneration* awarded by the *firm*.

19C.3.43 **G** Variable *remuneration* can be awarded to *BIPRU Remuneration Code staff* in the form of retention awards where it is compatible with the BIPRU Remuneration Code general requirement to do so. The *FCA* considers this is likely to be the case only where a *firm* is undergoing a major restructuring and a good case can be made for retention of particular key staff members on prudential grounds. Proposals to give retention awards should form part of any notice of the restructuring proposals required in accordance with *Principle 11* and the general notification requirements in ■ SUP 15.3.

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

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

- (1) fixed and variable components of total *remuneration* are appropriately balanced; and
- (2) 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.

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

19C.3.45 **R** A *firm* must ensure that payments related to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure.

19C.3.46 **G** *Firms* 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 the *BIPRU Remuneration Code* general requirement.

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

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

19C.3.47 **R**

- (1) A *firm* must ensure that a substantial portion, 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 for a non-listed *firm*; and
 - (b) where appropriate, *capital instruments* which are eligible for inclusion at stage B1 of the calculation in the *capital resources table*, where applicable, adequately reflect the credit quality of the *firm* as a going concern.
- (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 the portion of the variable *remuneration* component deferred, and not deferred, in line with ■ SYSC 19C.3.49 R.

[Note: Standard 8 of the *FSB Compensation Standards*]

19C.3.48 G

- (1) Regarding ■ SYSC 19C.3.47R (3), the 50% minimum threshold for instruments must be applied equally to the non-deferred and the deferred components; in other words, *firms* must apply the same chosen ratio between instruments and cash for their total variable *remuneration* to both the upfront and deferred components.
- (2) This simplified example illustrates the operation of (1). The variable remuneration of a material risk taker (X) is 100, and by ■ SYSC 19C.3.49R (3) 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 19C.3.47R (1).

Remuneration Principle 12(g): Remuneration structures - deferral

19C.3.49 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 of not less than three to five years.
- (2) *Remuneration* under (1) must vest no faster than on a pro-rata basis.
- (3) In the case of a variable *remuneration* component:
 - (a) of a particularly high amount; or
 - (b) payable to a *director* of a *firm* that is significant in its size, internal organisation and the nature, scope and complexity of its activities; at least 60% of the amount must be deferred.
- (4) Paragraph (3)(b) does not apply to a *non-executive director*.
- (5) The length of the deferral period must be established in line with the business cycle, the nature of the business, its risks and the activities of the *employee* in question.

[Note: Standards 6 and 7 of the *FSB Compensation Standards*]

- (6) 500,000 is a particularly high amount for the purpose of (3)(a).
- (7) Paragraph (6) is without prejudice to the possibility of lower sums being considered a particularly high amount.

19C.3.50 G

- (1) Deferred *remuneration* paid in *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. Deferred *remuneration* paid in cash should also be subject to performance criteria.
- (2) The *FCA* generally expects 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 *BIPRU 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 *BIPRU Remuneration Code staff* in the levels of variable *remuneration* paid.

Remuneration Principle 12(h): Remuneration structures - performance adjustment, etc.

- 19C.3.51 **R** A *firm* must ensure that 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 according to the performance of the *firm*, the business unit and the individual concerned.
- [Note: Standards 6 and 9 of the *FSB Compensation Standards*]
- 19C.3.52 **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 (1) or (2) may be relied on as tending to establish contravention of the *rule* on performance adjustment (■ SYSC 19C.3.51 R).
- 19C.3.53 **G**
- (1) Variable *remuneration* may be justified, for example, to incentivise *employees* involved in new business ventures which could be loss-making in their early stages.
 - (2) 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.

