

10/21

Financial Services Authority

Implementing CRD3 requirements on the disclosure of remuneration

Feedback on CP10/27 and final rules

December 2010

Contents

	List of acronyms used in this Policy Statement	
1	Overview and update on recent developments	5
2	Analysis of responses received	10
3	The new disclosure framework	17
	Annex 1: List of respondents to CP10/27	
	Annex 2: An extract from CEBS' final guidelines (disclosure of remuneration)	
	Appendix 1: Handbook text	
	Appendix 2: General guidance on proportionality	

This Policy Statement reports on the main issues arising from Consultation Paper 10/27 (Implementing CRD3 requirements on the disclosure of remuneration) and publishes final rules.

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List of acronyms used in this Policy Statement

BCBS	Basel Committee on Banking Supervision
BIPRU	Prudential sourcebook for Banks, Building Societies and Investment Firms
CAD	Capital Adequacy Directive
CBA	Cost benefit analysis
CEBS	Committee of European Banking Supervisors
CP	Consultation Paper
CRD3	The latest amendments to the Capital Requirements Directive
EEA	European Economic Area
EU	European Union
FSB	Financial Stability Board
MiFID	Markets in Financial Instruments Directive
PERG	The Perimeter Guidance Manual (Handbook)
PS	Policy Statement
RemCo	Remuneration Committee.
SYSC	Senior Management Arrangement, Systems and Controls (Handbook)

1 Overview and update on recent developments

Purpose

- 1.1 In Consultation Paper 10/27 (CP10/27) we set out our proposed approach to implementing the requirements on disclosure of remuneration contained in the latest amendments to the Capital Requirements Directive (CRD3). This Policy Statement (PS) reports on the responses and feedback we have received to our consultation and the decisions we have made as a result.

Background

- 1.2 In the wake of the recent financial crisis, remuneration became a key point of focus among international financial regulatory organisations. In 2009, the Financial Stability Board issued high-level principles and standards on remuneration, including a principle on disclosure. The European Union meanwhile included specific rules in CRD3 on remuneration and disclosure.
- 1.3 In mid-2010, following announcement of the CRD3 rules, it was decided by the Treasury that we would assume responsibility for implementing these rules in the UK. To this end, we issued CP10/27 in early November 2010.
- 1.4 On 29 July 2010 we published CP10/19, which consulted on our proposals for revising the Remuneration Code. Following the consultation, we are publishing the PS and final rules on remuneration in PS10/20, to accompany this document.

Outcome of our consultation

- 1.5 We received 22 responses to CP10/27 from a range of interested parties including trade associations, professional services firms, law firms and financial institutions. A list of respondents is provided in Annex 1.
- 1.6 The vast majority of respondents agreed with our approach to implementing the disclosure requirements of CRD3, and with our proposals on form and frequency

of disclosure. There were a few challenges to the proposed wording of the draft Handbook text – however, in this we are constrained by the text of CRD3 itself.

- 1.7 There were different opinions on how the principle of proportionality should be applied. While the majority of respondents agreed with the four-tier approach set out in Chapter 4 of CP10/27, some respondents voiced concerns about the different types of firm captured in the same tier, while others sought clarification on finer details and definitions.
- 1.8 We also sought feedback on whether there would be any meaningful disadvantages to extending the scope of disclosure requirements to third-country BIPRU firms (in effect, the UK branches of non-EEA firms). The response to this was more mixed; some respondents felt that this would contribute to a level playing field, while others questioned the benefits of such a move, pointing out that such branches do not form a material part of the UK financial market. Many respondents expressed concerns over the impact on the competitiveness of the UK's financial sector. This feedback will be taken into account when we decide whether to launch a consultation process on this issue in early 2011.

Summary of our policy response

- 1.9 We have given careful consideration to the comments received in the consultation process, as well as to the need to ensure consistency with final guidelines on implementing CRD3 remuneration requirements published by the Committee of European Banking Supervisors (CEBS) on 10 December (discussed in further detail in the next section). Details of our policy response are set out in Chapter 2. In view of the largely positive response to our proposed implementation, we have made no significant changes to our proposals as set out in CP10/27. In summary, these are:
 - We will implement requirements on disclosure of remuneration which are consistent with CRD3. We believe this will help to improve market transparency and create a level playing field in Europe.
 - Our proposals on frequency and form of disclosure provide sufficient flexibility for firms to comply without undue difficulty. CEBS' final guidelines are also less prescriptive than the initial draft version on the expected form of disclosure.
 - We recognise the importance of proportionality and have carefully considered respondents' comments, as well as CEBS' final guidelines which allow some rules to be 'neutralised' for certain types of firm. We believe our four-tier approach takes account of firms' risk profiles to an extent that is practicable and enforceable.
 - We will require related group entities to report on a consolidated basis at the level of the highest proportionality tier of any entity in the group.
- 1.10 We received useful and informative feedback on whether there would be any meaningful disadvantages to extending the disclosure requirements to third-country BIPRU firms. Given our current operating timescale, we have not yet reached a decision on our next steps. If we decide to consult on taking this forward, we are likely to do so in early spring 2011.

Update on recent developments

CEBS final guidelines

- 1.11 At the time of publishing CP10/27, CEBS had issued a set of draft guidelines on implementing CRD3, including the requirements on disclosure of remuneration. Our comments in CP10/27 were based on that draft.
- 1.12 The final guidelines were published on 10 December 2010, including some changes in the area of remuneration disclosure. The relevant final guidelines are at Annex 2. The main changes are summarised below; in our view, none of these is so significant as to require major changes to our consultation process.

Key changes between CEBS draft and final guidelines on disclosure of remuneration		
Draft version	Final version	Impact
<p>Form of disclosure</p> <p>'...may take the form of a stand-alone report or may be included in the institution's annual report and accounts.'</p> <p>...the institution must ensure that access to the location of the disclosure is readily available."</p>	<p>'...the institution should ensure that the disclosure is easily accessible.'</p> <p>'...the institution should ensure that the disclosures on remuneration provide appropriate cross-references to other information and disclosures in the Pillar 3 context which may be of relevance to users.'</p>	See our response to Question 2
<p>Timing/frequency of disclosure</p> <p>'Supervisors will expect the first institution's disclosure reports in 2011.'</p>	<p>'Supervisors expect institutions to provide the first disclosure reports in compliance with the requirements in the course of 2011.'</p>	See our response to Question 2
<p>Pillar 3 exemptions</p> <p>'...certain types of disclosure may be exempted on the grounds that the information is not material, or is proprietary or confidential.'</p>	<p>'Given the aggregate nature of the quantitative disclosures on remuneration, it is unlikely that these exemptions will be applicable. The disclosure requirements are without prejudice to Directive 95/46/EC.'</p>	See our response to Question 6

Key messages in this PS

Objectives of the new rules

- 1.13 The recitals to CRD3 state that 'good governance structures, transparency and disclosure are essential for sound remuneration policies'. The aim of this PS is to implement the requirements on disclosure of remuneration set out in CRD3. We

believe this will help to improve market transparency and market discipline, as well as to create a level playing field in Europe. It is also consistent with our view that stakeholders will benefit from greater clarity regarding a firm's remuneration practices, notably whether and how these practices support effective risk management.

- 1.14 More broadly, the fundamental objectives of our remuneration policy are to sustain market confidence and promote financial stability through removing the incentives for inappropriate risk-taking by firms, and thereby to protect consumers.

The international context

- 1.15 CRD3 aims to align principles on remuneration across the EU. In terms of **remuneration structures**, this appears to harden the distinction in approach between the EU and other major jurisdictions.
- 1.16 In terms of **disclosure**, however, this distinction is less pronounced, partly because many non-EU jurisdictions are awaiting the outcome of the Basel Committee on Banking Supervision's (BCBS) consultation on remuneration disclosure. Having contributed extensively to the BCBS's draft proposals, we are of the view that they do not differ significantly from those of CRD3, and therefore that there is less likelihood of significant differences developing.
- 1.17 We work closely with our colleagues in both the EU and BCBS arenas and will continue to keep in close contact with them to ensure continuing alignment of supervisory practices. In particular, we provided significant input into the final guidelines on implementing CRD3 issued by CEBS.

Timing

- 1.18 EU member states are required to implement the new CRD3 rules by **1 January 2011**. CRD3 requires firms to provide 'regular, at least annual, updates' to the public, mirroring the Pillar 3 rule in BIPRU 11 which requires firms to publish disclosures 'on an annual basis at a minimum'.
- 1.19 Guidance from CEBS advises that '[t]he disclosure should be published on, at least, an annual basis and as soon as practicable'. The first reports will be expected 'in the course of 2011'. We are setting a deadline of **31 December 2011** for firms to make their first disclosure under these provisions.

Who should read this PS?

- 1.20 This PS should be read by all FSA-authorized banks, building societies and Capital Adequacy Directive (CAD) investment firms. This audience corresponds to credit institutions subject to Banking Consolidation Directive (Directive 2006/48/EC) and investment firms as defined in the CAD (Article 3(1)(b)). It does not apply to exempt CAD firms.¹ It should also be read by third-country BIPRU firms operating through branches in the UK. This PS may also be of interest to shareholders, creditors and firms' other stakeholders, as well as trade associations and consumer groups.

¹ See PERG 13 for guidance on the scope of a CAD investment firm.

Structure of this PS

1.21 This PS is structured as follows:

- Chapter 2 summarises the comments and feedback to the questions posed in CP10/27, and our responses.
- Chapter 3 sets out the key aspects of the new disclosure framework.
- Annex 1 lists the respondents to CP10/27.
- Annex 2 contains the relevant extract from CEBS' final guidelines on disclosure of remuneration.
- Appendix 1 contains the final Handbook text.
- Appendix 2 sets out general guidance on our approach to implementing the principle of proportionality.

Cost benefit analysis

1.22 CP10/27 included a cost benefit analysis (CBA). We have not received any feedback challenging the cost estimates or the description of the benefits published in CP10/27. We do not think there will be any increase in costs arising from the new framework (over and above those stated in the CBA) or if there will be any such increases, they will be minimal. The CBA published in CP10/27 therefore continues to apply.

Compatibility statement

1.23 CP10/27 included a compatibility statement that explained why we considered our proposals to be compatible with our general duties under section 2 of FSMA and with our regulatory objectives, set out in sections 3 to 6 of FSMA. Given the nature of the amendments, we believe this statement is still valid.

Next steps

1.24 The key steps for implementation will be:

- 1 January 2011 – all EU member states to implement CRD3.
- By 28 February 2011 – FSA to decide on next steps with regard to consultation on extending disclosure requirements to third country BIPRU firms.
- 31 December 2011 – all firms in scope to have made the first annual requisite disclosures on remuneration.

2 Analysis of responses received

Overview

- 2.1 This chapter summarises the feedback we received to the questions posed in CP10/27. Given the tight timescale of our consultation process, we were satisfied with the level of response received. Our respondents included seven major trade associations (representing over 2,200 firms), professional services firms, law firms and financial institutions – reflecting the broad range of interest in this subject. We outline the views of respondents on each question, set out our responses to these views, and explain how we intend to proceed.
- 2.2 CP10/27 contained two different groups of questions: those for consultation (Questions 1, 2, 5, 6 and 7) and those seeking feedback and discussion (Questions 3 and 4). We address these two groups separately in this chapter.

Questions for consultation

Required items of disclosure

- 2.3 In Chapter 3 of CP10/27, we set out the proposed items of information on remuneration that firms would be required to disclose. These were derived directly from the text of CRD3. We asked:
 - Q1: Do you agree with our proposed approach to implement the remuneration disclosure requirements of CRD3?
- 2.4 The vast majority of respondents expressed support for our proposed approach. Respondents variously described this approach as ‘appropriate’, ‘sensible’ and ‘reasonable and clear’.
- 2.5 A few respondents asked why there was a need to implement new disclosure requirements. One respondent pointed out that disclosure rules already exist, e.g. under the Executives’ Remuneration Reports Regulations. Two respondents questioned whether disclosure of remuneration would be of any value to shareholders, consumers or other stakeholders.

- 2.6 Respondents from the asset management sector emphasised the need for the rules to take account of the difference between banks' and asset managers' business structure and remuneration models.
- 2.7 Several respondents raised concerns that the requirement for **quantitative** information to be disclosed would have implications for confidentiality. One respondent commented that 'full and transparent disclosure of qualitative information...should be sufficient to satisfy relevant stakeholders and investors'. This was also raised in the context of Pillar 3 exemptions under Question 6, and is discussed under that question below.
- 2.8 There were a number of questions surrounding the finer points of implementation, such as the precise definition of terms such as 'business areas'. One respondent also criticised the wording of the draft Handbook text, complaining that parts of it were vague or confusing.

Our response

We believe that our proposed approach to implementing CRD3 requirements on remuneration disclosure will help to improve market transparency and market discipline, as well as to create a level playing field in Europe. We are aware that some disclosure requirements already exist. In our view, however, these do not provide the level of granularity that is needed to improve market transparency in the particular circumstances of the financial sector.

We are also aware of the differences in remuneration models between banks and other types of financial institution. This is reflected in our proposals on proportionality, which should result in less onerous disclosure requirements for firms undertaking agency business. This is discussed in greater detail under Question 5 below.

We understand that some terms and concepts used in the draft Handbook text may require further clarification. We are to some extent constrained by the drafting of the CRD3 text, but it is our intention to co-operate closely with firms to clarify these points, helping them to make complete and accurate disclosure on a timely basis.

Frequency and form of disclosure

- 2.9 In Chapter 4 of CP10/27, we set out proposals for the form in which firms should make disclosures, and how frequently these should be published. We asked:
- Q2: Do you agree with our proposed requirements in terms of frequency and form of disclosure as set out in paragraphs 4.3 to 4.7 of CP10/27?
- 2.10 There was near-unanimous support for our proposals on the frequency and form of disclosure. Respondents agreed with the proposed requirement for annual reporting, and welcomed the flexible approach to the required form of reporting.
- 2.11 One respondent noted that implementing the disclosure requirements via the BIPRU 11 framework would help investment fund managers to transition smoothly to the disclosure requirements under the Alternative Investment Fund Managers Directive (AIFMD) when that Directive is fully implemented.

- 2.12 Some respondents asked how firms should comply if their financial year-end differs from the calendar year-end. They felt that if a firm's financial year-end was late in the year (e.g. October 2011), it would face challenges in preparing the necessary disclosure by 31 December 2011. It was suggested that such firms should be given an extended deadline to comply.

Our response

We believe that our proposed requirements on the frequency and form of disclosure, including the publication deadline of 31 December 2011, provide sufficient flexibility for firms to comply without undue difficulty. After the first disclosure, firms should continue to disclose on an annual basis.

This deadline is consistent with CEBS' final guidelines, which state that firms are expected to publish their first disclosures 'in the course of 2011'. We recognise there may be challenges for firms whose financial year ends in late 2011, but in our view these firms will have sufficient time to make the necessary arrangements.

Regarding the form of disclosure, CEBS' final guidelines are less prescriptive than the draft version, merely stating that 'the institution should ensure that the disclosure is easily accessible' and that it should 'provide appropriate cross-references to other information and disclosures in the Pillar 3 context which may be of relevance to users'. We believe this too will make the 31 December 2011 deadline less of a challenge.

Proportionality

- 2.13 In Chapter 4 and Annex 3 of CP10/27, we described how we propose to apply the principle of proportionality by setting different disclosure requirements for institutions based on their size, internal organisation and the nature, scope and complexity of their activities. We asked:

Q5: Do you agree with our proposed application of the principle of proportionality to institutions as set out in paragraphs 4.18 to 4.20 of CP10/27?

- 2.14 The majority of respondents agreed in principle with our tiered approach to proportionality, in particular our proposal that limited licence and limited activity firms should only be required to disclose basic quantitative and qualitative information.
- 2.15 However, many respondents also felt that our framework should take greater account of each firm's risk profile. Some respondents felt it was not appropriate for lower-risk retail-focused institutions to be placed in the same tier as higher-risk wholesale or investment banking firms. One respondent asked if firms would be able to move between tiers during the year if their business or risk profile were to change, or whether there would be a cut-off point at which each firm would be allocated to a tier.
- 2.16 In CP10/27, we proposed that where related group entities are each allocated to different tiers, all entities should report at the level of the highest tier. Respondents voiced concerns that in some circumstances this might be disproportionate, and argued that some firms should still be allowed to report on a stand-alone basis.

Our response

We recognise the importance of this issue for the large and diverse range of firms within scope, and have carefully considered respondents' suggestions and concerns about proportionality. We have also taken account of CEBS' final guidelines which recognise the importance of proportionality and allow some rules to be 'neutralised' for certain types of firm.

In our four-tier approach, proportionality tiers one and two are intended to include larger banks and building societies and broker dealers that engage in significant proprietary trading or investment banking activities. Proportionality tier three will consist primarily of small banks and building societies, and firms that may occasionally take overnight/short-term risk on their balance sheet. Proportionality tier four will contain firms that generate income from agency business without putting their balance sheets at risk. We believe this approach takes account of firms' risk profiles to an extent that is practicable and enforceable.

We intend to adhere to our proposal that related group entities should report at the level of the highest proportionality tier of any entity in the group. See also our comments in paragraph 3.2.

Scope of application to staff and types of information

2.17 In Chapter 4 of CP10/27, we described our proposed approach to implementing the disclosure requirements in respect of staff and types of information. We asked:

Q6: Do you agree with our proposals on implementation with regard to staff and types of information, as set out in paragraphs 4.21 and 4.22?

2.18 The vast majority of respondents agreed with our proposal to link disclosure requirements to a firm's Code Staff population. Some respondents continued to have issues with the definition of Code Staff – these are dealt with in our separate Policy Statement (PS10/20) for the Remuneration Code. One respondent pointed out that due to the flexibility of the definition, a firm's population of Code Staff might fluctuate from year to year, affecting the comparability of the disclosed remuneration figures over time.

2.19 We received various comments on our proposed application of BIPRU 11 (Pillar 3) exemptions. These potentially exempt firms from disclosing information if it is proprietary, confidential or not material. In summary, the comments were:

- The 'proprietary nature' exemption should be allowed where incentives are tied to commercially sensitive information.
- The 'materiality' exemption will be difficult to implement as there is wide disagreement over the impact of remuneration on risk.
- It was argued that the 'confidentiality' exemption (which received the most attention) should apply when disclosure of the highest severance payment (as required by the rules) could lead to the identity of the recipient being known. One respondent stated that firms should be given the option to merge quantitative data for different categories to preserve confidentiality. Another

respondent suggested that confidential disclosures should be made only to supervisors. A further response highlighted that disclosures might in effect force limited liability partnerships (LLPs) to disclose their partnership agreements.

- 2.20 Broadly, respondents were content to disclose qualitative but not quantitative information. One respondent commented that ‘full and transparent disclosure of qualitative information...should be sufficient to satisfy relevant stakeholders and investors’.

Our response

We believe that linking disclosure requirements to a firm’s Code Staff population will ensure the relevance of the information disclosed. At the same time, we recognise that Code Staff populations may fluctuate, affecting the comparability of data over time. To address this, firms may disclose a per capita figure in addition to the CRD3 requirements if they feel this is relevant.

We have considered the comments on the BIPRU 11 (Pillar 3) exemptions, but we are also aware that these exemptions were provided largely for disclosures on capital and risk. We further take account of CEBS’ final guidelines on these exemptions, which state that ‘given the aggregate nature of the quantitative disclosures on remuneration, it is unlikely that these exemptions will be applicable’.

Regarding confidentiality, we have made it clear that disclosures are to be made without prejudice to the Data Protection Directive (Directive 95/46/EC) as implemented in the UK primarily through the Data Protection Act 1998.

We take the view that qualitative disclosures alone will not meet the requirements as set out in CRD3. For that reason, we require a certain level of quantitative disclosure for all tiers, although this will be applied on a proportionate basis.

Cost benefit analysis

- 2.21 In Annex 4 of CP10/27, we set out our cost benefit analysis (CBA) for our proposed implementation of disclosure requirements. We asked:

Q7: Do you have any observations on the cost benefit analysis?

- 2.22 We received only three responses to this question. One respondent remarked that limiting the reporting scope would keep costs down, and that the benefits would be greater if the disclosure format was simple and easily understood.
- 2.23 Two other respondents commented that the analysis did not include the impact of increased remuneration driven by greater transparency (i.e. increasing pay levels to keep up with rivals).

Our response

We have not received any feedback directly challenging the cost estimates or the description of the benefits published in CP10/27. Increased disclosure could indeed lead to increased remuneration levels at firms that feel under pressure to keep up with rivals, but this effect should be mitigated by additional market and public discipline.

Questions for discussion and feedback

Extending disclosure requirements to third-country BIPRU firms

- 2.24 In Chapter 4 of CP10/27, we noted the implications of implementing disclosure requirements via the Basel Pillar 3 framework, and sought feedback on whether third-country BIPRU firms operating in the United Kingdom (in effect, UK-based branches of non-EEA firms) should be brought within scope of the requirements. We asked:
- Q3: Do you think there would be any meaningful disadvantages in extending the scope of our disclosure requirements to third-country BIPRU firms in relation to their activities carried on from establishments in the United Kingdom?
- 2.25 We also sought feedback on the costs and benefits of extending the scope. We asked:
- Q4: Do you have any comments on the potential costs and benefits that would be incurred in implementing the above proposal?
- 2.26 The level of response here was moderate, with just over half the respondents providing feedback on the two questions raised. Among the responses, there appeared to be two opposing views. Most major financial institutions argued that there were no meaningful disadvantages to the proposals as they would help to create a level playing field between subsidiaries and branches in the UK. These respondents tended not to comment on the potential cost aspects.
- 2.27 Trade associations on the other hand argued that there would be meaningful disadvantages to the proposal. One respondent stated that it was not clear how extending the disclosure requirements to non-EEA branches would contribute to market discipline, adding that staff at these branches would already be subject to disclosure requirements imposed by their home regulator. Another respondent claimed that imposing this requirement would lead to ‘internal resentment’ in a firm because only staff in the UK branch would have to disclose the information.
- 2.28 A respondent commented that ‘any policy in respect of third-country branches should be determined at an EU level – rather than at an individual member state level – taking into account the outcome of the Basel/FSB proposal for Pillar 3 Disclosure Requirements for Remuneration and the implications of article 38 of the Capital Requirements Directive’.
- 2.29 One argument put forward by respondents on both sides of the debate was the need to safeguard the competitiveness of the UK financial sector. It was pointed out by one respondent that the proposal should be seen in the context of other factors such as the 50% rate of tax. Taken altogether, and given that the cumulative benefits of extending the requirements to non-EEA branches would be small, the respondent felt that this was not a cost worth incurring.

- 2.30 Other respondents highlighted the ‘unintended increase in the overall cost of remuneration’, which would ‘outweigh the benefit to shareholders, regulators and other stakeholders’.

Our response

We have found the feedback on these questions to be useful and informative. We will consider further whether to put forward proposals for consultation on this question. If we do decide to consult, we will aim to do so in spring 2011.

3 The new disclosure framework

What we intend to implement

- 3.1 In the appendix to CP10/27, we set out our draft Handbook text, incorporating amendments to BIPRU to implement disclosure requirements on remuneration. Having taken account of the responses to the CP, and the final guidelines issued by CEBS on 10 December, we have made the Handbook text attached at Appendix 1 to this PS. These will come into effect as of 1 January 2011 in line with the deadline imposed by CRD3.
- 3.2 In our draft Handbook text, BIPRU 11.5.20R(2) stated that '(f)irms 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'. We intend to implement the new disclosure requirements in a proportionate manner as described in Chapter 4 and Annex 3 of CP10/27. This will be done by allocating firms into one of four tiers depending on the level of each firm's capital resources or type of licence or permission. General guidance (under section 157 of FSMA) is provided in Appendix 2 to this PS in relation to the proportionality tiers and their required levels of disclosure. This guidance also covers proportionality in relation to the Remuneration Code; of particular relevance to disclosure is Part G.

What we expect to see

Frequency and form of disclosure

- 3.3 In Chapter 4 of CP10/27, we proposed a deadline of 31 December 2011 for firms to make their first disclosure under the new provisions. We also took account of CEBS draft guidance on the form of disclosure.
- 3.4 We believe the 31 December 2011 deadline remains appropriate, especially in view of CEBS' less prescriptive final guidance on the form of disclosure (as summarised in paragraph 1.12 above). Firms may make the disclosure in the form they find most appropriate, provided that this is easily accessible by users, and provides appropriate cross-references to other relevant information and disclosures in the Pillar 3 context.

- 3.5 Consistent with CEBS' final guidelines, we will expect firms to publish these disclosures on at least an annual basis, and as soon as practicable.

Pillar 3 exemptions and waivers

- 3.6 In its final guidelines, CEBS takes note of the possible exemptions to Pillar 3 disclosure (on the basis of materiality, proprietary nature or confidentiality), but indicates that 'given the aggregate nature of the quantitative disclosures on remuneration, it is unlikely that these exemptions will be applicable'. CEBS also refers to the Data Protection Directive, noting that CRD3 says that 'the disclosure requirements are without prejudice to Directive 95/46/EC'. Our views, as contained in paragraph 4.22 of CP10/27, are consistent with CEBS' views on these points.
- 3.7 In paragraph 4.16 of CP10/27, we also indicated that non-EEA firms that have been granted a waiver on the basis of comparable disclosure at a consolidated level in the home state would not be required to make a solo disclosure. CEBS' final guidelines state that 'this waiver is, however, only available where an institution is a subsidiary of a non-EU institution and the latter prepares equivalent disclosures at parent level (article 72 (3) CRD)'.
- 3.8 Firms with existing waivers will have to assess whether their parent company provides equivalent disclosures on remuneration. If it does not, they may need to make additional disclosures at the level of the UK firm.

List of respondents to CP10/27

Association for Financial Markets in Europe (AFME)
Alternative Investment Management Association (AIMA)
Allianz Global Investors Capital
Association of Private Client Investment Managers and Stockbrokers (APCIMS)
Barclays Plc
BlackRock Group Ltd
British Bankers Association (BBA)
Building Societies Association (BSA)
British Private Equity and Venture Capital Association (BVCA)
Cazenove Capital Management Ltd
Chi-X Europe Ltd
Co-operative Financial Services Plc
Furness Building Society
Hargreaves Lansdown Asset Management Ltd
Investment Management Association (IMA)
Legal & General Group Plc
MM&K Ltd
National Bank of Ukraine
Nationwide Building Society
Share Plan Lawyers Group
Standard Chartered Plc
Unite the Union

An extract from CEBS final guidelines (disclosure of remuneration)

5.1.1. Specific and general requirements on disclosure

- 146 Institutions should disclose, to the public, detailed information regarding their remuneration policies and practices for members of staff whose professional activities have a material impact on the institution's risk profile. Institutions should also provide general information about the basic characteristics of their institution-wide remuneration policies and practices.
- 147 The overall Pillar 3 requirements do not specify where an institution should disclose information. In all cases, however, the institution should ensure that the disclosure is easily accessible. The institution should ensure that the disclosures on remuneration provide appropriate cross-references to other information and disclosures in the Pillar 3 context which may be of relevance to users.
- 148 Pillar 3 remuneration disclosures may be made on a proportionate basis and the overall remuneration proportionality principle will apply to the type and amount of information disclosed. Small or non-complex institutions will only be expected to provide some qualitative information and very basic quantitative information where appropriate. In practice, this could mean that such institutions are not expected to provide (all) the information under point 15 (g) of Annex XII. Institutions should disclose how they have applied the proportionality principle, including possible neutralizations of some of the provisions at their institution.
- 149 Existing Pillar 3 provisions exempt certain types of information from being disclosed on the basis of materiality, proprietary nature, or confidentiality. Given the aggregate nature of the quantitative disclosures on remuneration, it is unlikely that these exemptions will be applicable. The disclosure requirements are without prejudice to Directive 95/46/EC. According to article 72 (1) and (2) CRD, Pillar 3 remuneration disclosures are to be made at consolidated level. Certain institutions may also be subject to a waiver so that they do not have to comply with the disclosure requirements; this waiver is, however, only available where an institution is a subsidiary of a non- EU institution and the latter prepares equivalent disclosures at parent level (article 72 (3) CRD). Thus, the disclosures still cover the entity with a waiver, albeit indirectly at the consolidated level.

- 150 The disclosure should be published on, at least, an annual basis and as soon as practicable. Supervisors expect institutions to provide the first disclosure reports in compliance with the requirements in the course of 2011; it is also expected that institutions' disclosures will evolve over time to reflect developments within peer groups and in markets.

5.1.2. Policy and practices

- 151 The disclosure report should set out the decision-making process used to determine the remuneration policy for the individuals to which it applies. This may include the governance procedure relating to the development of the remuneration policy and should include information about the bodies (including their composition and mandate), such as the Rem Co or external consultants, which played a significant role in the development of the remuneration policy. Institutions should outline the role of all relevant stakeholders involved in the determination of the remuneration policy. Additionally, the disclosure should include a description of the regional scope of the institution's remuneration policy, the types of staff considered as material risk takers and the criteria used to determine such staff.
- 152 The report should include information on how pay and performance are linked. Such information should include a description of the main performance metrics utilized for: the institution, top-level business lines, and for individuals (i.e. scorecards). Institutions should disclose information relating to the design and structure of remuneration processes, such as the key features and objectives of the remuneration policy and how the institution ensures that staff members in control functions are remunerated independently of the businesses they oversee. The report should also include a description of the different forms of variable remuneration utilized (i.e. cash, equity, options, other capital instruments, and long-term incentive plans) and should include the rationale for using these different forms and for allocating them to different categories of staff. Additionally, the report should include a discussion of the parameters used to allocate deferred and non-deferred remuneration for different staff categories.
- 153 Disclosure reports should describe how the institution takes into account current and future risks to which they are exposed when implementing remuneration methodologies and what these risks are. Also, institutions should describe the measures used to take account of these risks and the ways in which these measures affect remuneration. In addition, institutions should disclose the ways in which they seek to adjust remuneration to take account of longer-term performance – as in the institution's policy on deferral, vesting and performance adjustment.
- 154 It would be useful to ensure that the disclosure is produced and owned by the management body that has the ultimate sign-off on remuneration decisions.

5.1.3. Aggregate quantitative information

- 155 Institutions should provide aggregate quantitative information by business area and on remuneration for members of staff whose actions have a material impact on the risk profile of the institution. The information for each of the major business areas at an institution, i.e. investment banking business area, retail banking business area, etc. should include: number of staff, total remuneration and total variable remuneration. Some institutions may only have one or two business areas.
- 156 More detailed qualitative information on remuneration should be disclosed for senior managers and other members of staff whose actions have a material impact on the risk profile of the institution including aggregate information on amounts of remuneration, amounts and forms of variable remuneration, and amounts of outstanding deferred remuneration. Other more detailed quantitative information is also required as per the Directive.
- 157 Quantitative information on remuneration should also be disclosed separately on an aggregate basis at the level of directors (within the meaning of Article 11 of the Directive) for institutions that are significant in terms of their size, internal organisation and the nature, scope and complexity of their activities. This will be a separate category of disclosure information to the categories of senior management and other staff members who have a material impact on the risk profile of the institution.

5.2. Internal disclosure

- 158 The remuneration policy of a credit institution or investment firm should be accessible to all staff members of that institution. Institutions should ensure that the information regarding the remuneration policy disclosed internally reveals at least the details which are disclosed externally. Therefore, according to the size, internal organisation and the nature, scope and complexity of the activities of the institution, the information provided to staff members might contain some of the elements listed in Annex XII, Part 2, Point 15. The staff members should know in advance the criteria that will be used to determine their remuneration. The appraisal process should be properly documented and should be transparent to the member of staff concerned. Confidential quantitative aspects of the remuneration of staff members shall not be subject to internal disclosure.

Handbook text

**PRUDENTIAL SOURCEBOOK FOR BANKS, BUILDING SOCIETIES AND
INVESTMENT FIRMS (REMUNERATION DISCLOSURES) INSTRUMENT 2010**

Powers exercised

- A. The Financial Services 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) section 138 (General rule-making power);
 - (2) section 139A (General rules about remuneration);
 - (3) section 156 (General supplementary powers); and
 - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 1 January 2011.

Amendments to the Handbook

- D. The Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU) is amended in accordance with the Annex to this instrument.

Notes

- E. In the Annex 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 Prudential Sourcebook for Banks, Building Societies and Investment Firms (Remuneration Disclosures) Instrument 2010.

By order of the Board
16 December 2010

Annex

Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)

In this Annex, underlining indicates new text.

11.5 Technical criteria on disclosure: General requirements

...

Disclosures: remuneration

- 11.5.18 R A firm must disclose the following information, including regular, at least annual, updates, regarding its remuneration policy and practices for those categories of staff whose professional activities have a material impact on its risk profile:
- (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;
 - (2) information on the link between pay and performance;
 - (3) the most important design characteristics of the remuneration system, including information on the criteria used for performance measurement and risk adjustment, deferral policy and vesting criteria;
 - (4) information on the performance criteria on which the entitlement to shares, options or variable components of remuneration is based;
 - (5) the main parameters and rationale for any variable component scheme and any other non-cash benefits;
 - (6) aggregate quantitative information on remuneration, broken down by business area;
 - (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, indicating the following:
 - (a) the amounts of remuneration for the financial year, split into fixed and variable remuneration, and the number of beneficiaries;

- (b) the amounts and forms of variable remuneration, split into cash, shares, share-linked instruments and other types;
- (c) the amounts of outstanding deferred remuneration, split into vested and unvested portions;
- (d) the amounts of deferred remuneration awarded during the financial year, paid out and reduced through performance adjustments;
- (e) new sign-on and severance payments made during the financial year, and the number of beneficiaries of those payments;
- (f) the amounts of severance payments awarded during the financial year, number of beneficiaries and highest such award to a single person.

[Note: Paragraph 15 of Annex XII to the *Banking Consolidation Directive*.]

11.5.19 **G** The FSA would normally consider the requirements to publish disclosures in accordance with BIPRU 11.3.8R and 11.3.9R in respect of BIPRU 11.5 as a whole to meet the requirement in paragraph 15 of Annex XII to the *Banking Consolidation Directive* to publish “regular, at least annual, updates” (as implemented in BIPRU 11.5.18R).

- 11.5.20 **R** (1) A 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.
- (2) 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 and without prejudice to the UK or other national transposition of Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data.

[Note: Paragraph 15 of Annex XII to the *Banking Consolidation Directive*.]

[Note: The FSA has given guidance for the purpose of providing a framework for complying with the disclosure requirements of BIPRU 11.5.18R in accordance with the proportionality test set out in BIPRU 11.5.20R(2). The guidance divides firms into four tiers, and indicates which requirements should be complied with for each tier. It was published in Policy Statement 10/21 ‘Implementing CRD requirements on the disclosure of remuneration: Feedback on CP10/27 and final rules’ and is available at <http://www.fsa.gov.uk/Pages/Library/Policy/Policy/index.shtml>.

11.5.21 **G** In the FSA’s view, the exemptions from disclosure provided for in BIPRU

11.3.5R (materiality) and BIPRU 11.3.6R (proprietary or confidential information) are unlikely to apply to the disclosure required by BIPRU 11.5.18R (having regard, amongst other things, to the fact that the requirements set out in BIPRU 11.5.18R are to be complied with in the manner described in BIPRU 11.5.20R(2)).

General guidance on proportionality

**GENERAL GUIDANCE ON PROPORTIONALITY:
THE REMUNERATION CODE (SYSC 19A) &
PILLAR 3 DISCLOSURES ON REMUNERATION (BIPRU 11)**

PART A: INTRODUCTION & INTERPRETATION	2
<i>Introduction</i>	2
Status of guidance statement	2
Remuneration principles proportionality rule.....	2
Guidance on the remuneration principles proportionality rule	2
Guidance on proportionality in relation to remuneration committees and Pillar 3 remuneration disclosures	3
Individual guidance	3
Arrangement of guidance statement.....	3
<i>Interpretation</i>	3
PART B: PROPORTIONALITY TIERS	5
PART C: PROCESS FOR DIVIDING FIRMS INTO PROPORTIONALITY TIERS	6
<i>Overview</i>	6
<i>Solo Remuneration Code firms</i>	6
BIPRU firms	6
Third country BIPRU firms.....	7
<i>Groups with more than one Remuneration Code firm</i>	8
PART D: GUIDANCE TO FIRMS IN PARTICULAR PROPORTIONALITY TIERS	10
<i>Purpose of proportionality tiers</i>	10
<i>Firms to continue to consider proportionality in their individual circumstances, etc.</i>	10
<i>Disapplication of certain remuneration principles for firms in particular proportionality tiers</i> ..	11
PART E: GUIDANCE ABOUT PART-YEAR REMUNERATION CODE STAFF	12
<i>Introduction</i>	12
<i>Part-year Remuneration Code staff for more than three months</i>	12
<i>Certain part-year Remuneration Code staff for three months or less</i>	14
<i>Part-year Remuneration Code staff for three months or less, but where exceptional etc. payments made</i>	14
PART F: REMUNERATION COMMITTEES.....	16
<i>General</i>	16
<i>Subsidiaries of overseas groups / third country BIPRU firms</i>	16
PART G: PILLAR 3 REMUNERATION DISCLOSURES (BIPRU 11)	17
<i>Requirement to make Pillar 3 remuneration disclosures</i>	17
<i>Pillar 3 remuneration disclosures & proportionality</i>	17
APPENDIX 1: SUPPLEMENTAL GUIDANCE ON DIVIDING FIRMS INTO PROPORTIONALITY TIERS.....	18
<i>Groups with more than one Remuneration Code firm: examples</i>	18
<i>Role of individual guidance</i>	19
APPENDIX 2: PILLAR 3 DISCLOSURE REQUIREMENTS BY PROPORTIONALITY TIER	20

16 December 2010

PART A: INTRODUCTION & INTERPRETATION

Introduction

Status of guidance statement

1. This statement is general *guidance* given by the *FSA* under section 157(1) of the *Act*. It relates both to—
 - (1) the *Remuneration Code* of SYSC 19A of the *Handbook*, and
 - (2) the requirement to make Pillar 3 disclosures in relation to *remuneration* (in accordance with *BIPRU* 11 of the *Handbook*).
2. Paragraphs 14 and 15 make provision about the interpretation of this *guidance* statement. Expressions in italics either bear the meaning in the *Handbook Glossary*, or in the table in paragraph 15.
3. This *guidance* statement has effect from 1 January 2011.

Remuneration principles proportionality rule

4. The *remuneration principles proportionality rule* is set out in SYSC 19A.3.3R(2).
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

6. General *guidance* is given in relation to specific aspects of the *remuneration principles proportionality rule* in SYSC itself.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*.
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.
9. This *guidance* statement represents our initial *guidance* in a field where new requirements relating to *remuneration* are being implemented within the *EEA*. The *FSA* recognises this will be an evolving process, and intends to keep the *guidance* set out in this *guidance* statement under review.

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) and the transitional *guidance* given in SYSC TP3.5G and SYSC TP3.6G.

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

10. The *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 *rules*, on which *guidance* is given in Parts F and G of this *guidance* statement.

Individual guidance

11. The *FSA* may give individual *guidance* to a *firm*, either on its own initiative or on the application of the *firm*. The *FSA*'s policy on individual *guidance* is set out in *SUP 9*. In consequence, the *FSA* may give individual *guidance* to a *firm* in relation to the *remuneration principles proportionality rule*. Such *guidance* may relate to the application of the *rule* by the *firm* generally, or in specific areas.

Arrangement of guidance statement

12. This general *guidance* statement is divided into seven Parts:
- (1) This Part, Part A: Introduction & interpretation.
 - (2) Part B: Proportionality tiers.
 - (3) Part C: Process for dividing firms into proportionality tiers.
 - (4) Part D: Guidance to firms in particular proportionality tiers.
 - (5) Part E: Guidance about part-year Remuneration Code staff.
 - (6) Part F: Remuneration committees.
 - (7) Part G: Pillar 3 remuneration disclosures (*BIPRU 11*).
13. It is supplemented by two Appendices:
- (1) Appendix 1: Supplemental guidance on dividing firms into proportionality tiers.
 - (2) Appendix 2: Pillar 3 disclosure requirements by proportionality tier.

Interpretation

14. This *guidance* statement is to be interpreted as if it was an Annex to *SYSC 19A* (other than Part G and Appendix 2, 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.
15. 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>CEBS Guidelines</i>	'Guidelines on Remuneration Policies and Practices' of 10 December 2010 of

	the Committee of European Banking Supervisors.
<i>group</i>	has the meaning given in the <i>Glossary</i> under paragraph (3).
<i>proportionality tier</i>	has the meaning given in paragraph 17, and references to <i>proportionality tier one</i> , etc. are to be construed accordingly.
<i>Remuneration Code firm</i>	a <i>BIPRU firm</i> or <i>third country BIPRU firm</i> to whom the Remuneration Code applies (in accordance with SYSC 19A.1.1R).
<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 other <i>Remuneration Code firms</i> .

PART B: PROPORTIONALITY TIERS

16. SYSC 19A.1.1R provides that the *Remuneration Code* applies to a *BIPRU firm* and a *third country BIPRU firm* (in the case of a *third country BIPRU firm*, in relation to the activities carried on from an establishment in the *United Kingdom*). In this *guidance* statement, such *firms* are referred to as *Remuneration Code firms*.
17. This *guidance* statement provides for the division of *Remuneration Code firms* into four categories—
 - (1) *proportionality tier one*,
 - (2) *proportionality tier two*,
 - (3) *proportionality tier three*, and
 - (4) *proportionality tier four*.
18. The process by which firms are divided into *proportionality tiers* is provided in Part C (as supplemented by Appendix 1), and may also depend on individual *guidance*.
19. The *proportionality tiers* provide a framework for the operation of the *remuneration principles proportionality rule*. *Guidance* is given to *firms* in different *proportionality tiers* in Part D.
20. The *proportionality tiers* are also used as the basis for *guidance* on separate *proportionality rules* which apply in relation to *remuneration committees* (Part F) and Pillar 3 remuneration disclosures (Part G and Appendix 2).

PART C: PROCESS FOR DIVIDING FIRMS INTO PROPORTIONALITY TIERS

Overview

- 21. This Part provides the process by which a *Remuneration Code firm* should ascertain the *proportionality tier* into which it falls. Appendix 1 provides supplementary *guidance* (including examples).
- 22. A *Remuneration Code firm*, in order to ascertain its *proportionality tier*, 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 tier* will depend on its individual characteristics (as determined in accordance with paragraphs 24 to 26).
 - (2) If the *firm* is part of such a *group*, its *proportionality tier* will depend on a two-stage process (as provided in paragraphs 27 and 28).

(This requires all *Remuneration Code firms* that are part of the *group* to fall into the highest *proportionality tier* that any individual *Remuneration Code firm* in the *group* would fall into on the assumption that it was a *solo Remuneration Code firm*.)
- 23. Individual *guidance* may vary the *proportionality tier* into which a *firm* would otherwise fall under paragraphs 24 to 28.

Solo Remuneration Code firms

- 24. A *solo Remuneration Code firm's proportionality tier* depends on whether it is—
 - (1) a *BIPRU firm*, or
 - (2) a *third country BIPRU firm*.

BIPRU firms

- 25. The following table shows the *proportionality tier* into which a *solo Remuneration Code firm* that is a *BIPRU firm* falls:
 - (1) A *firm* of the description given in the second column falls into the *proportionality tier* listed in the first column.
 - (2) Where applicable, the *firm's proportionality tier* will further depend on whether it held *capital resources* on its last *accounting reference date* of the amount listed in the third column of the table.

Table 2: Proportionality tiers: solo Remuneration Code firms which are BIPRU firms

Proportionality tier	Type of firm	Capital resources on last accounting reference date of firm (where applicable)
-----------------------------	---------------------	---

<i>Proportionality tier one</i>	<i>UK Bank.</i>	Exceeding £1 billion.
	<i>Building society.</i>	Exceeding £1 billion.
	<i>BIPRU 730k firm that is a full scope BIPRU investment firm.</i>	Exceeding £750 million.
<i>Proportionality tier two</i>	<i>UK Bank.</i>	Exceeding £50 million, but not exceeding £1 billion.
	<i>Building society.</i>	Exceeding £50 million, but not exceeding £1 billion.
	<i>BIPRU 730k firm that is a full scope BIPRU investment firm.</i>	Exceeding £100 million, but not exceeding £750 million.
<i>Proportionality tier three</i>	<i>UK Bank.</i>	Not exceeding £50 million.
	<i>Building society.</i>	Not exceeding £50 million.
	<i>Any full scope BIPRU investment firm that does not fall within proportionality tier one or proportionality tier two (in accordance with this Table).</i>	Not applicable.
<i>Proportionality tier four</i>	<i>BIPRU limited licence firm.</i>	Not applicable.
	<i>BIPRU limited activity firm.</i>	Not applicable.

Third country BIPRU firms

26. The following table shows the *proportionality tier* into which a *solo Remuneration Code firm* that is a *third country BIPRU firm* falls:

- (1) A *firm* of the description given in the second column falls into the *proportionality tier* listed in the first column.
- (2) Where applicable, the *firm's proportionality tier* will further depend on whether it held relevant total assets on the last relevant date of the amount listed in the third column of the table.
- (3) In (2)—
 - (a) “relevant total assets” means the total assets of the *firm* that cover the activities of the branch operation in the *United Kingdom*;
 - (b) “relevant date” means 31 December 2010, and each subsequent anniversary.

The limit confining relevant total assets to those that cover the activities of the branch operation in the *United Kingdom* is taken from *SUP*

16.12.3R(1)(iv), which relates to a reporting requirement in relation to *non-EEA banks* (among others). The *FSA* considers that a *firm* which needs to ascertain its relevant total assets should, as appropriate, apply an analogous methodology to that used by a *non-EEA bank* in completing data element A14 of FSA044 (so, for example, the general policy on valuation set out in *GENPRU* 1.3 should be applied).

These definitions are intended to apply on an interim basis, as FSA044 is to be withdrawn. The *FSA* will in due course consider whether to revise the definitions relating to the tier thresholds for *third country BIPRU firms*.

Table 3: Proportionality tiers: solo Remuneration Code firms which are third country BIPRU firms

Proportionality tier	Type of firm	Relevant total assets on last relevant date (where applicable)
<i>Proportionality tier one</i>	<i>Third country BIPRU firm that is not a limited licence firm or limited activity firm.</i>	Exceeding £25 billion.
<i>Proportionality tier two</i>	<i>Third country BIPRU firm that is not a limited licence firm or limited activity firm.</i>	Exceeding £2 billion, but not exceeding £25 billion.
<i>Proportionality tier three</i>	<i>Third country BIPRU firm that is not a limited licence firm or limited activity firm.</i>	Not exceeding £2 billion.
<i>Proportionality tier four</i>	<i>Limited licence firm.</i>	Not applicable.
	<i>Limited activity firm.</i>	Not applicable.

Groups with more than one Remuneration Code firm

27. 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 tier* into which it would fall on the assumption that it was a *solo Remuneration Code firm*.
 - (2) Where each *Remuneration Code firm* falls into the same *proportionality tier* on the assumption that it was a *solo Remuneration Code firm*, each *firm* falls into that *proportionality tier*.
 - (3) Where the *Remuneration Code firms* fall into different *proportionality tiers* on the assumption that they were *solo Remuneration Code firms*, each *firm* falls into the highest *proportionality tier*.

- (4) For the purposes of (3), *proportionality tier one* is the highest and *proportionality tier four* is the lowest.
28. Appendix 1 provides examples of this approach. A *firm* which has a higher *proportionality tier* as a result of the *guidance* in paragraph 27 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 tier* (as discussed in paragraphs 5 and 6 of Appendix 1).

PART D: GUIDANCE TO FIRMS IN PARTICULAR PROPORTIONALITY TIERS

Purpose of proportionality tiers

29. In relation to the *remuneration principles proportionality rule*, the *proportionality tiers* provide the following:

- (1) A framework for the FSA's supervisory approach, and a broad indication of the FSA's likely expectations.
- (2) *Guidance* on which *remuneration* principles may normally be disapplied under the *remuneration principles proportionality rule*.

As noted above, this is initial *guidance* in an evolving field.

30. The *proportionality tiers* also provide *guidance* on the separate but similar *proportionality rules* that apply in relation to—

- (1) *remuneration* committees (Part F), and
- (2) Pillar 3 disclosures in relation to *remuneration* (Part G and Appendix 2).

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

31. It follows from the nature of the *remuneration principles proportionality rule*, and the limited purposes noted in paragraph 29, that the *proportionality tiers* 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.

32. A *firm* should bear in mind that the *Remuneration Code* may require different responses from *firms* that fall into the same *proportionality tier*. This is illustrated by the following example:

- (1) Firm A is a global bank with capital resources of £10 billion, with substantial investment banking business, foreign exchange exposures and a complex business model seeking aggressive growth. It falls into *proportionality tier one*.
- (2) Firm B is a large mortgage and savings bank with capital resources of £1.5 billion and a comparatively simple, conservative business model. It falls into *proportionality tier one*.
- (3) Firm C is a large building society, with capital resources of £800 million and a comparatively simple, conservative business model. It falls into *proportionality tier 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 tier*. 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 tiers

33. The *Banking Consolidation Directive* can be interpreted such that it may not be necessary for certain *firms* to apply certain *remuneration* principles at all.² This has been endorsed and elaborated in the *CEBS Guidelines*.³
34. In the view of the *FSA*, it will normally be appropriate for a *firm* in *proportionality tier three* or *proportionality tier four* to disapply under the *remuneration principles proportionality rule* the following *rules*—
 - (1) retained *shares* or other instruments (*SYSC 19A.3.47R*),
 - (2) deferral (*SYSC 19A.3.49R*), and
 - (3) performance adjustment (*SYSC 19A.3.51R*).
35. The following *guidance* applies to *firms* in *proportionality tier four* that are *limited licence firms* or *limited activity firms*:⁴
 - (1) In the view of the *FSA*, it will normally be appropriate for such a *firm* to disapply under the *remuneration principles proportionality rule* the rule on ratios between fixed and variable components of total *remuneration* (*SYSC 19A.3.44R*).
 - (2) The *FSA* also endorses the *CEBS Guidelines* where they state that such *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” as discussed further in section 4.2.2.a of the *Guidelines*.⁵
36. 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, the *FSA*, in line with the *CEBS Guidelines*, does not consider that the *remuneration principles proportionality rule* permits a *firm* to apply lower numerical criteria.⁶ (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 *Banking Consolidation Directive*, Annex V, paragraph 23 provides that the principles should be applied by *firms* “in a way and to the extent that is appropriate to their size, internal organisation and the nature, the scope and complexity of their activities” (emphasis added).

³ *CEBS Guidelines*, paragraphs 19 to 23.

⁴ Under the approach set out in paragraphs 24 to 26, *proportionality tier four* will compromise only *limited licence firms* or *limited activity firms*. However, a firm other than a *limited licence firm* or *limited activity firm* could conceivably fall into *proportionality tier four* as a result of individual *guidance*.

⁵ *CEBS Guidelines*, paragraph 20.

⁶ *CEBS Guidelines*, paragraph 19.

PART E: GUIDANCE ABOUT PART-YEAR REMUNERATION CODE STAFF

Introduction

37. SYSC 19A.3.34G provides *guidance* on when the FSA does not generally consider it necessary for a *firm* to apply to certain *Remuneration Code staff* certain *rules* relating to *remuneration* structures. This Part provides further *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.
38. In giving this *guidance*, the FSA has taken account of the *remuneration principles proportionality rule*.

Part-year Remuneration Code staff for more than three months

39. 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*;
 - (e) “threshold amount” means £500,000 multiplied by the relevant fraction.
 - (3) The FSA does 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 one or both of the conditions in (3) are not satisfied (and accordingly where the *firm* should apply in relation to A the rules referred to in (4)).
- (6) Where this sub-paragraph applies, the *FSA* generally considers 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) 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* for the entire 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 A1's *Remuneration Code staff* role A1's fixed *remuneration* increases to £250,000. For the performance year, A1 is awarded variable *remuneration* of £120,000.
 - (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 £40,110 (£120,000 multiplied by 122/365). A1's total qualifying *remuneration* is £123,670. 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*, so 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 £40,110.
- (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 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*, so 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

40. Paragraphs 41 and 42 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*.
41. Where this paragraph applies, the *FSA* does 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).
42. Where this paragraph applies, the guidance in paragraph 39(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

43. Paragraph 44 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 as *Remuneration Code staff*.
44. The guidance in paragraph 39 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.

PART F: REMUNERATION COMMITTEES

General

45. Remuneration Principle 4 (Governance) provides, in SYSC 19A.3.12R(1), that 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.
46. The following table provides *guidance* on when the *FSA* considers it would be appropriate for a *remuneration* committee to be established under SYSC 19A.3.12R, based on the *proportionality tier* into which the *firm* falls (as determined in accordance with Part C of this *guidance* statement (as supplemented by Appendix 1))—

Table 4: Guidance on whether SYSC 19A.3.12R remuneration committee required

Proportionality tier	SYSC 19A.3.12R remuneration committee?
<i>Proportionality tier one</i> and <i>proportionality tier two</i>	The <i>FSA</i> considers that such a <i>remuneration</i> committee should be established.
<i>Proportionality tiers three</i> and <i>proportionality tier four</i>	The <i>FSA</i> considers that it would be desirable for such a <i>remuneration</i> committee to be established, and would normally expect larger <i>proportionality tier three</i> and <i>proportionality tier four</i> firms to do so. But the <i>FSA</i> accepts that it may be appropriate for the <i>governing body</i> of the <i>firm</i> to act as the <i>remuneration</i> committee.

Subsidiaries of overseas groups / third country BIPRU firms

47. This *guidance* relates, broadly speaking, to a *Remuneration Code firm* which is a *third country BIPRU firm*, or a *BIPRU firm* that is part of a *group* not subject to consolidated supervision by the *FSA*.
48. The *FSA* accepts that it may be possible for certain such *firms* to justify on the ground of proportionality not establishing under SYSC 19A.3.12R at solo level a *remuneration* committee. However, 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. The *FSA* would expect as a minimum to be satisfied that the operational arrangements ensured sufficient independence from those performing executive functions at *firm* or *group* level, and were discharged with sufficient authority.

PART G: PILLAR 3 REMUNERATION DISCLOSURES (BIPRU 11)

Requirement to make Pillar 3 remuneration disclosures

49. *BIPRU 11* requires certain *Remuneration Code firms* to disclose a series of qualitative and quantitative information relating to *remuneration* (*BIPRU 11.3* and *BIPRU 11.5.18R*). The basis of the disclosure (which may be on a consolidated basis) is set out in *BIPRU 11.2*.
50. *BIPRU 11* applies only to certain *Remuneration Code firms* (in that it applies to *BIPRU firms*, but not *third country BIPRU firms*).

Pillar 3 remuneration disclosures & proportionality

51. 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)*).
 - (2) *BIPRU firms* must comply 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)*).
52. The *FSA* considers that it is appropriate to give *guidance* on these proportionality tests by reference to the *proportionality tiers* determined in accordance with Part C of this *guidance* statement (as supplemented by Appendix 1). However, as the disclosure requirement applies only to *BIPRU firms*, when applying the guidance in paragraph 27, only *Remuneration Code firms* which are *BIPRU firms* should be taken into account.
53. In relation to the proportionality test referred to in paragraph 51(1), the *FSA* considers that a *firm* should be regarded as “significant” if it falls into *proportionality tier one*.
54. In relation to the proportionality test set referred to in paragraph 51(2), the table in Appendix 2 sets out the categories of information that the *FSA* considers *firms* in different *proportionality tiers* should disclose.

APPENDIX 1: SUPPLEMENTAL GUIDANCE ON DIVIDING FIRMS INTO PROPORTIONALITY TIERS

Groups with more than one Remuneration Code firm: examples

1. The following non-exhaustive examples illustrate the operation of the *guidance* provided in paragraph 27 of Part C. (It should be borne in mind that in each case individual *guidance* could vary the outcome of the operation of the *guidance* provided in that paragraph.)
2. Example 1:
 - (1) Firm A is the *parent undertaking* of Firm B.
 - (2) Firm A is a *UK bank* that had *capital resources* of £1.5 billion 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 tier one* and Firm B falls into *proportionality tier four*.
 - (4) As a result of the guidance at paragraph 27 of Part C, both Firms A and B fall into *proportionality tier one*.
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 *capital resources* of £1.5 billion on its last *accounting reference date*.
 - (3) On the assumption that they were *solo Remuneration Code firms*, Firm C falls into *proportionality tier four* and Firm D falls into *proportionality tier one*.
 - (4) As a result of the guidance at paragraph 27 of Part C, both Firms C and D fall into *proportionality tier one*.
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 *Remuneration Code firms*.
 - (b) Firm F is a *BIPRU 730k firm* that is a *full scope BIPRU investment firm* and that had *capital resources* of £500 million on its last *accounting reference date*.
 - (c) Firms G and J are *limited activity firms*.
 - (d) Firm I is a *UK bank* that had *capital resources* of £20 million on its last *accounting reference date*.
 - (3) On the assumption that they were *solo Remuneration Code firms*—
 - (a) Firm F falls into *proportionality tier two*,

- (b) Firms G and J fall into *proportionality tier four*, and
 - (c) Firm I falls into *proportionality tier three*.
- (4) As a result of the guidance at paragraph 27 of Part C, Firms F, G, I and J all fall into *proportionality tier two*.

Role of individual guidance

5. Individual *guidance* may vary the *proportionality tier* into which a *firm* would fall under the general *guidance* set out in Part C and supplemented by this Appendix. In consequence, the definitions and thresholds provided in Part C do not provide an immutable classification. The *CEBS Guidelines* also provide guidance on applying proportionality between different institutions.⁷
6. The following provide non-exhaustive high level examples of where the *FSA* might consider providing individual *guidance* to vary a *proportionality tier*:
- (1) Where a *firm* was just below the threshold for a particular *proportionality tier* (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 tier*.
 - (2) Where a *group* of *firms* contained several *firms* falling into a common *proportionality tier*, but where the aggregate prudential risk posed by the *group* suggested that a higher *proportionality tier* was more appropriate.
 - (3) Where a *firm* falls into a higher *proportionality tier* as a result of the guidance at paragraph 27 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.

⁷ *CEBS Guidelines*, paragraphs 24 and 25.

APPENDIX 2: PILLAR 3 DISCLOSURE REQUIREMENTS BY PROPORTIONALITY TIER

BIPRU 11.5.18R disclosure requirement	Relevant proportionality tier			
	Proportionality tier one	Proportionality tier two	Proportionality tier three	Proportionality tier four
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”).	✓	✓	✓	✓
BIPRU 11.5.18R(2) (‘information on the link between pay and performance’).	✓	✓	✓	✓
BIPRU 11.5.18R(3) (‘the most important design characteristics of the remuneration system, including information on the criteria used for performance measurement and risk adjustment, deferral policy and vesting criteria’).	✓	✓		
BIPRU 11.5.18R(4) (‘information on the performance criteria on which the entitlement to shares, options or variable components of remuneration is based’).	✓			
BIPRU 11.5.18R(5) (‘the main parameters and rationale for any variable component scheme and any other non-cash benefits’).	✓			
BIPRU 11.5.18R(6) (‘aggregate quantitative information on remuneration, broken down by business area’).	✓	✓	✓	✓
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 <i>firm</i> ...’) ...indicating the following:	✓	✓	✓	✓
BIPRU 11.5.18R(7)(a) (‘the amounts of remuneration for the financial year, split into fixed and variable remuneration, and the number of beneficiaries’).	✓	✓	✓	
BIPRU 11.5.18R(7)(b) (‘the amounts and forms of variable remuneration, split into cash, shares, share-linked instruments and other types’).	✓			
BIPRU 11.5.18R(7)(c) (‘the amounts of outstanding deferred remuneration, split into vested and unvested portions’).	✓			
BIPRU 11.5.18R(7)(d) (‘the amounts of deferred remuneration awarded during the financial year, paid out and reduced through performance adjustments’).	✓			
BIPRU 11.5.18R(7)(e) (‘new sign-on and severance payments made during the financial year, and the number of beneficiaries of those payments’).	✓			
BIPRU 11.5.18R(7)(f) (‘the amounts of severance payments awarded during the financial year, number of beneficiaries and highest such award to a single person’).	✓			

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