

Policy Statement | PS7/17

# The PRA's expectations on remuneration

April 2017



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This policy statement provides feedback on responses to Consultation Paper (CP) 33/16 'The PRA's expectations on remuneration'.



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## 1 Overview

1.1 This Prudential Regulation Authority (PRA) Policy Statement (PS) provides feedback on responses to Consultation Paper (CP) 33/16 'The PRA's expectations on remuneration'.<sup>1</sup> The PS also includes Supervisory Statement (SS) 2/17 'Remuneration',<sup>2</sup> which brings together the PRA's existing supervisory statements on proportionality, the application of malus and other elements of remuneration, and sets out additional expectations of firms.

1.2 The PS and SS are relevant to all firms regulated by the PRA which fall within the scope of the Remuneration Part of the PRA Rulebook (the Remuneration Part), and should be read alongside the Remuneration Part.

1.3 SS2/17 replaces the following SSs and letters to firms:

- Legacy Supervisory Statement (LSS) 8/13 'Remuneration standards: the application of proportionality';<sup>3</sup>
- SS2/13 'PRA expectations regarding the application of malus to variable remuneration';<sup>4</sup> and
- SS27/15 'Remuneration';<sup>5</sup>
- 'Remuneration – PRA expectations', 8 December 2014;<sup>6</sup> and
- 'Procedure to increase the permitted ratio of fixed to variable remuneration', 8 April 2014.<sup>7</sup>

1.4 The PRA received four responses to the consultation. The PRA's feedback to responses and final decisions are discussed in Chapter 2. Following consideration of feedback, the PRA has made minor changes to the draft SS included in CP33/16.

1.5 The PRA is required by the Financial Services and Markets Act 2000 (FSMA) to publish a cost benefit analysis of any changes to the consultation proposals which the PRA considers to be significant, and to publish a statement on the impact of rules on mutuals where the final rule differs from the draft of the proposed rule.

1.6 The proposed amendments to the policy as consulted on provide additional clarification of certain parts of the text. The amendments do not depart from the original policy intent. As such, in the PRA's opinion, the cost benefit analysis and the statement on the impact of rules on mutuals in the consultation paper still stand and no revision is required.

1.7 This policy has been designed in the context of the current UK and EU regulatory framework. The PRA will keep the policy under review to assess whether any changes would be required due to changes in the UK regulatory framework, including those arising once any new arrangements with the European Union take effect.

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1 September 2016: [www.bankofengland.co.uk/prapublications/cp/2016/cp3316.aspx](http://www.bankofengland.co.uk/prapublications/cp/2016/cp3316.aspx).

2 April 2017: [www.bankofengland.co.uk/prapublications/ss/2017/ss217.aspx](http://www.bankofengland.co.uk/prapublications/ss/2017/ss217.aspx).

3 June 2015: [www.bankofengland.co.uk/prapublications/ss/2015/lss813update.aspx](http://www.bankofengland.co.uk/prapublications/ss/2015/lss813update.aspx).

4 June 2015: [www.bankofengland.co.uk/prapublications/ss/2015/ss213update.aspx](http://www.bankofengland.co.uk/prapublications/ss/2015/ss213update.aspx).

5 June 2015: [www.bankofengland.co.uk/prapublications/ss/2015/ss2715.aspx](http://www.bankofengland.co.uk/prapublications/ss/2015/ss2715.aspx).

6 [www.bankofengland.co.uk/pradocuments/remuneration/remunerationpraexpectations.pdf](http://www.bankofengland.co.uk/pradocuments/remuneration/remunerationpraexpectations.pdf).

7 [www.bankofengland.co.uk/pradocuments/supervision/remuneration/proceduretoincreasethepermittedratiooffixedtovariable remuneration.pdf](http://www.bankofengland.co.uk/pradocuments/supervision/remuneration/proceduretoincreasethepermittedratiooffixedtovariable remuneration.pdf).

## 2 Feedback to responses

2.1 The PRA is required by FSMA to have regard to any representations made to the proposals in a consultation, to publish an account in general terms of those representations and its response to them, and to publish details of any significant differences in the text as published.

### Material risk takers (MRTs)

2.2 One respondent asked for clarity whether the conditions in Chapter 2, paragraph 2.20 could be applied in the case of a part-year MRT of less than 3 months who is in receipt of a guaranteed variable remuneration award. The PRA has clarified that the conditions in paragraph 2.20 for disapplying the remuneration rules at the individual level can be applied in these circumstances. Paragraph 3.18 in SS2/17 now refers to paragraph 3.14 to make this clear.

2.3 A heading has been included before paragraph 3.16 after one respondent commented that it was unclear what the annualised rate was intended to be used for. The heading now provides clarity that paragraph 3.16 relates to determining the fixed component of total remuneration for the fixed to variable ratio. In light of the comment received, this paragraph has been re-written to make it clearer.

2.4 One respondent commented that the wording of paragraph 3.30 in the draft SS appeared to indicate that the Remuneration Part does not need to be applied to group MRTs outside the United Kingdom if they do not have responsibilities in relation to the UK-regulated entity. This referred to the paragraph about handling instances where an MRT in a third country firm has reporting lines into other jurisdictions as well as the United Kingdom. However it is now clear that the incidence of such cases is extremely rare. It is therefore proposed that, when such cases do arise, the specific circumstances will be considered by the PRA and Financial Conduct Authority (FCA) on a case-by-case basis. Paragraph 3.30 of the draft SS has therefore been removed.

### Other elements of remuneration

2.5 One respondent asked for clarity on how guaranteed variable remuneration in the form of a 'lost opportunity' award should be treated for the fixed to variable ratio when an individual resigns from their current employer late in one performance year and does not join their new employer until later in the following performance year. Paragraph 5.33 in SS2/17 now clarifies that the 'lost opportunity' award should be included within the variable component of the fixed to variable ratio in the relevant performance period in which the award is made.

2.6 Respondents requested clarity on a number of sections of the European Banking Authority Guidelines on Sound Remuneration Policies (EBA Guidelines). Firms must comply with all aspects of the EBA Guidelines except for the provision that the bonus cap must be applied to all firms subject to the Capital Requirements Directive (CRD).<sup>1</sup> Remuneration proportionality level one and two firms must continue to apply the bonus cap. The PRA considers that it does not need to provide further expectations at this stage on other elements of the EBA Guidelines. Firms should consider the EBA Guidelines along with all domestic requirements.

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<sup>1</sup> Directive 2013/36/EU (<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:176:0338:0436:En:PDF>).

## Additional amendments made to the draft SS

2.7 Some additional amendments have been made to the draft SS which were identified during the consultation timeframe but were not received as a formal consultation response. These have been set out below.

### Proportionality

2.8 Paragraph 2.16 has been amended to set out that it may be appropriate for a firm in proportionality level three to disapply the rules on buy-outs (Remuneration 15A). CP2/16 'Buy-outs of variable remuneration'<sup>1</sup> proposed that, in accordance with the PRA's existing approach to proportionality, the buy-out rules in the Remuneration Part would not need to be applied for firms that fall within level three of the proportionality framework. Although not included in PS26/16 'Buy-outs of variable remuneration',<sup>2</sup> the PRA's approach to this issue has not changed. The change to the SS has been made to provide clarification for level three firms.

2.9 Paragraph 2.20 has been amended to remove reference to Remuneration 15.8 (buy-outs) as this rule was deleted on 1 January 2017 and has been replaced by Remuneration 15A (buy-outs). As a result, Remuneration 15A applies to all MRTs, including where the individual meets both of the conditions set out in paragraph 2.20.

### Personal investment strategies

2.10 Paragraph 5.28 now references Remuneration 13.1 to clarify the circumstances in which employees must not undertake to use personal hedging strategies to undermine the risk alignment effects embedded in their remuneration arrangements.

### Specific award structures: guaranteed variable remuneration, buy-outs and retention awards

2.11 In paragraph 5.34 the PRA has clarified that notification of guaranteed variable remuneration is not required. The PRA, however, expects that firms should notify the PRA and provide justification when a retention award is offered to an individual and this has been further clarified in paragraph 5.39.

### Application date of EBA Guidelines

2.12 The EBA Guidelines, effective from 1 January 2017, require institutions to have in place on 1 January 2017 the respective governance arrangements; remuneration policies, practices and procedures for 2017. The EBA Guidelines apply to the structure of variable remuneration awards granted for the performance year 2017 onwards.

### Remuneration committees

2.13 As outlined in CP33/16, the PRA expects remuneration committees to fulfil the roles and functions required under Remuneration 7.4 and the EBA Guidelines. In CP2/17 'Occasional Consultation Paper'<sup>3</sup> the PRA consulted on a proposal to amend Remuneration 7.4 so that it applies to 'firms' (rather than 'CRR firms' under the current wording). The proposed amendment would align this rule with the position that applies to dual-regulated firms under SYSC 19D3.12R of the FCA Handbook.

1 January 2016: [www.bankofengland.co.uk/pr/Pages/publications/cp/2016/cp216.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/cp/2016/cp216.aspx).

2 September 2016: [www.bankofengland.co.uk/pr/Pages/publications/ps/2016/ps2616.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ps/2016/ps2616.aspx).

3 February 2017: [www.bankofengland.co.uk/pr/Pages/publications/cp/2017/cp217.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/cp/2017/cp217.aspx).

## Appendix

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- 1 **Supervisory Statement 2/17 'Remuneration' available at [www.bankofengland.co.uk/pr/Pages/publications/ss/2017/ss217.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ss/2017/ss217.aspx)**