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REMCO CHAIR ADDRESS

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Dear **REMCO CHAIR NAME**

EMBEDDING THE APPLICATION OF EX POST PERFORMANCE ADJUSTMENT (MALUS) - update for 2014/2015 Remuneration Round

1. The purpose of this letter, as we go into the 2014/15 remuneration round, is to highlight our key expectations on the application of malus that we expect the Remuneration Committee to meet. We are sending this letter to all firms that fall into proportionality level 1¹ and it should be considered in the context of any previous firm-specific feedback you have previously received and which still remains valid. We would also highlight the importance of providing us with sufficient early information on malus and clawback events to aid in the provision of the FCA's non-objection.
2. Last year marked the first time the FCA, jointly with the PRA, undertook the annual Remuneration Round. For the FCA, our specific focus was on the application of malus in response to cases of misconduct which impact consumers and market integrity. This supports the FCA's statutory objectives by incentivising behaviours that enhance the integrity of the UK financial system, secure an appropriate degree of protection for consumers, and promote effective competition in the interests of consumers. Following on from this we identified a number of learning points, which are set out for consultation in CP14/14 Appendix 6 'General guidance on the application of malus to variable remuneration and ex-ante risk adjustments' as proposed new FCA guidance to share this good practice. This highlights our current thinking, and some of the main areas where the Remuneration Committee can assist.

The Importance of Remuneration Committees

3. The primary purpose of the Remuneration Code (SYSC 19A) is to ensure greater alignment between risk and individual reward, to discourage excessive risk-taking and short-termism, encourage more effective risk management, and in turn to support a strong conduct culture within firms.

¹ General Guidance on Proportionality: The Remuneration Code (SYSC 19A) - <http://www.fca.org.uk/your-fca/documents/finalised-guidance/remuneration-code>

4. The role of Remuneration Committee Chair and the decisions taken by the Remuneration Committee are key drivers in supporting and effectively delivering the aims of the Remuneration Code and actually driving forward and embedding expectations on the application of malus to continue to promote positive behaviours and culture within your firm.
5. The proposed guidance in CP14/14 highlights good practice. Whilst this is in draft, it provides a clear indication of the FCA's expectations on the application of malus and is broken down into seven areas:
 - **Scope** – Application to an appropriate range of individuals including those who were not directly involved in the misconduct such as those who failed to act, or those who by virtue of their seniority could be deemed indirectly responsible or accountable.
 - **Expectations in relation to the application of malus** – Staff in firms are clear on the fully discretionary nature of their variable remuneration and appropriately sized reductions are robustly applied, including taking account of any fines.
 - **Timing in the consideration of malus** – Events are considered early on and reductions applied as soon as reasonably possible.
 - **Procedure for considering malus** – Events are considered using a clearly defined, robust and well documented process that considers a range of relevant factors.
 - **Transparency in the consideration of malus** – The process clearly shows the difference between awards pre and post application of malus and is clearly communicated to employees.
 - **Ex-ante risk adjustments** – Firms take into account the risk of conduct failings which have not yet crystallised when setting the size of the bonus pool, making larger adjustments where they believe these risks have increased.
 - **Co-operation with the FCA** – Information is provided in sufficient detail and at an early enough point to facilitate the process of reaching agreement on bonus plans.

2014/15 Remuneration Round

6. As with last year, the FCA and PRA will be working closely together to carry out the annual review of your remuneration policies and practices against the principles of the Remuneration Code. Whilst the FCA's focus will be on the application of malus, we will also be looking to see compliance in all areas of the Remuneration Code, including how you have taken into account the risk of misconduct in setting current year awards. We will also be particularly interested to see how you have updated your approach to take account of changes arising from CRD IV such as the bonus cap and the identification of material risk takers. You will need to obtain the FCA's non-objection to your firm's proposals for the 2014/15 remuneration round in advance of your firm executing those proposals.

Provision of information

7. Finally, during the last remuneration round, a number of firms were unable to provide the information we required for our review in an appropriate timeframe and, in at least one case, this led to a delay in the communication and distribution of awards.
8. As with last year, we are requesting information three months ahead of the date by which you are seeking our non-objection to the communication and distribution of awards as set

out in the Remuneration Policy Statement (RPS). We recognise that it may not be possible in all cases to provide full information on in-year adjustments at that stage. In this case, your submission should be supplemented with estimates, followed by final figures as soon as they are known. The exact timing of final data should be agreed with your FCA and PRA supervision teams.

9. To aid in the provision of this data, we have already sent to your firm a new quantitative data collection template 'RPS Table 7' with your firm at working level, developed in consultation with the PRA. This is intended to complement the existing more qualitative data which is already requested in RPS Annex 1.
10. If you wish to discuss the contents of this letter further, please speak to **SUPERVISOR NAME** or **SUPERVISOR NAME** on your Supervision Team.

Yours sincerely

A handwritten signature in black ink, appearing to read "H. Allen", with a long horizontal flourish extending to the right. Below the signature is a single horizontal line.