Regulatory Special HR Community Chat

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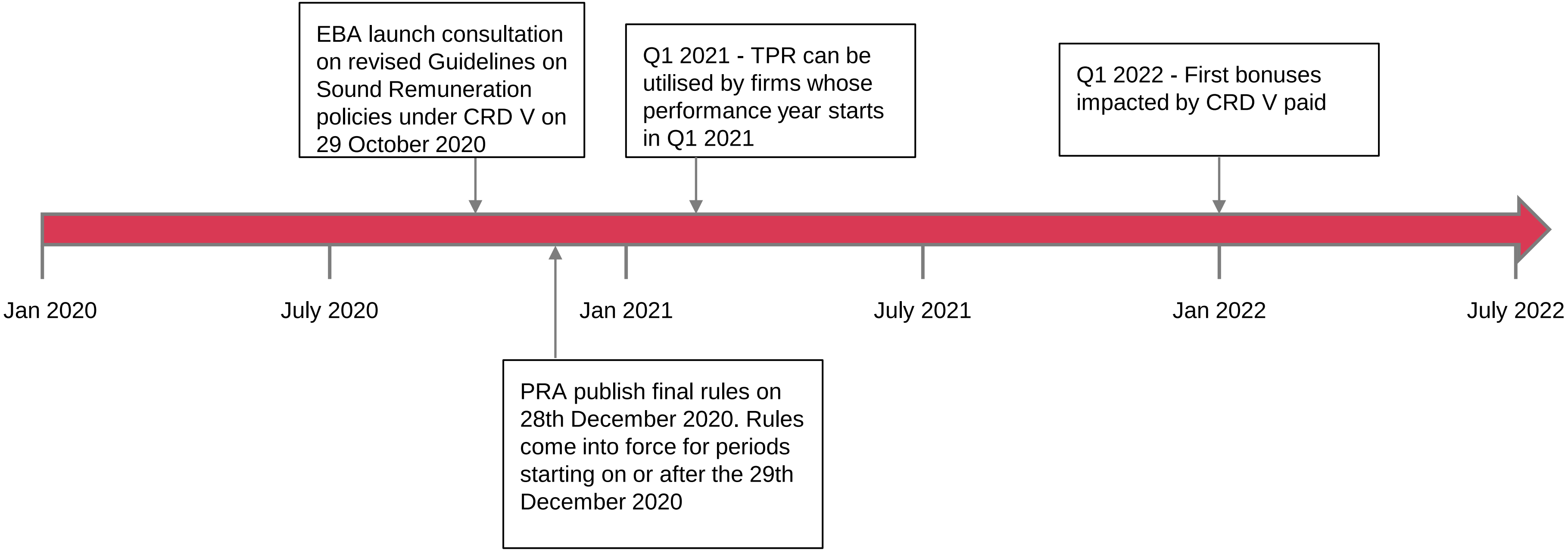
Agenda

1. CRD V (including UK exit from the EU)
2. COVID-19 - PRA update
3. The Investment Firms Regime
4. Brexit and FS

CRD V

Timeline



CRD V

Overview

MRT identification

- UK to use EBA RTS but specify GBP thresholds
- MRTs identified on a solo and consolidated basis
- No need to notify for those earning under €750k or to notify the EBA for those earning over €1m

Governance

- Required to maintain 'gender neutral' rem policies and report data on gender pay gap
- Need to demonstrate equal pay
- New RPS templates
- Continue high earners reporting

Malus and clawback

- Malus, clawback and buyout reporting regime will now apply to MRTs at all firms
- Should apply firmwide as appropriate
- Level 3s with deferral will need to comply with minimum clawback periods

Structural requirements

- Extension of requirements to limit variable pay to 100% of fixed pay, extending the deferral period to 4-5 years, to distinguish between those earning > £500k and > ⅓ variable and others.
- Companies can use share linked instruments/equivalent non cash instruments

Proportionality

- Small CRR firms will be able to apply proportionality for deferral and payment in instruments
- If below £4bn total assets threshold firms don't need to consider secondary criteria and if in between £4bn and £13bn firms will need to satisfy all secondary criteria
- De-minimis thresholds have been reduced to individual variable pay of £44,000 and less than a third of total pay is variable

EBA Guidelines

- Sets expectations for gender neutrality and how firms demonstrate this including with respect to equal pay
- Majority independent RemCo for G-SIIs and O-SIIs
- Extended remit for RemCo for embedding risk and gender neutrality
- Additional clarifications on severance pay, retention bonuses and the use of malus and clawback

CRD V

UK exit from the EU

Timing

If a firm's performance year starts within the first 3 months of 2021 firms are not required to apply the rules until the 2022 performance year.

Requirements

Per the PRA guidelines, the enhanced PRA application of the following remuneration requirements will apply to third country branches:

- Deferral
- Clawbacks
- Buyouts
- Risk adjustment
- Personal investment strategies

Application

The TPR will only apply to Firms in TPR or ex-passporting firms that have gained Part 4A authorisation.

COVID-19

PRA update

Overview

The PRA confirmed that dividends can resume in relation to full year 2020 results and variable awards in cash can be made.

For 2021 distribution the PRA propose return to using standard approach to capital setting and distribution.

Full system wide stress test to be undertaken in mid 2021, firms can accrue appropriately prudent 2021 dividends but they should not be paid out.

Bonuses

Given the uncertain outlook and the need for banks to deploy capital to support the wider economy, PRA expects firms to '*exercise a high degree of caution and prudence in determining the size of any cash bonuses granted to senior staff.'*

To ensure large banks have applied PRA remuneration regime properly and appropriately, the PRA have said they will scrutinise proposed pay-outs closely.

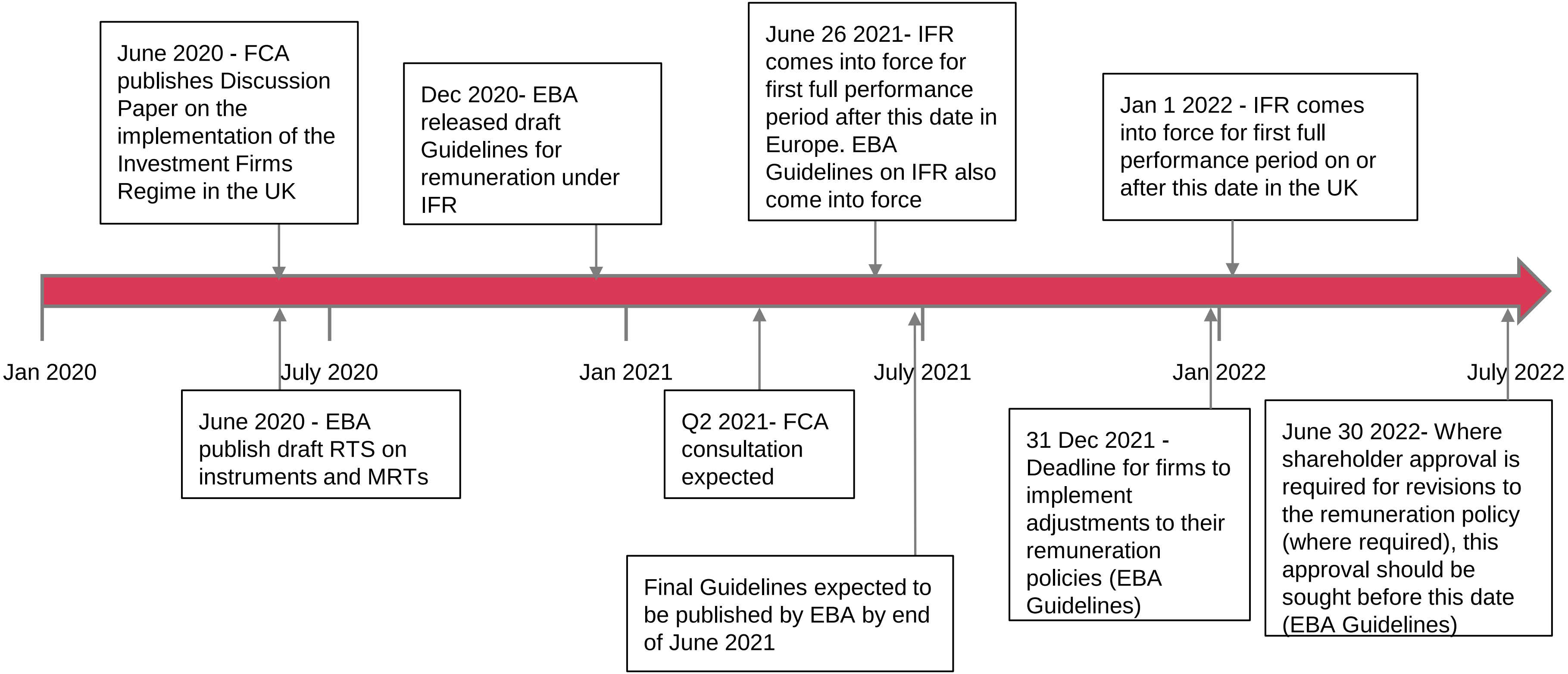
Dividend distributions

Any dividend distributions should be prudent and within specific guardrails which are the higher of:

- 25% of cumulative 8 quarter profits covering 2019 and 2020 (after deducting prior distributions); or
- 20 basis points of the RWA position at the end of 2020.

The Investment Firms Regime

Timeline



The Investment Firms Regime

Overview

Application

- All MIFID firms (including top up)

Proportionality

- Firms split into significant and non significant
- FCA intend to use a balance sheet asset threshold of ‘at least’ €300m
- Tested on a solo and consolidated basis

Requirements for significant firms

- 40-60% deferral for at least 3 years, FCA to apply 60% > £500k
- 50% of upfront and deferred remuneration in instruments
- Establish an independent gender balanced RemCo

MRT identification

- New EBA RTS with quantitative and qualitative criteria
- Need to consider the in scope population, impact of consolidation, governance structures, use of the de minimis and approach to exclusion

Performance assessment for MRTs

- Combination of financial, non financial, firm, business unit and individual performance
- Control function independence must be maintained
- Bonus pools must link to profits and be adjusted for risk

Malus and clawback

- Required for all variable pay for MRTs

Ratio of fixed and variable remuneration

- Disclose ratio publically (there is no limit or ‘cap’)
- Can set different ratios for different categories of staff

Interaction with other regimes

- Rules apply on a solo and consolidated basis
- AIFMD and UCITS V will continue to apply with the most onerous requirements applying where there is a conflict

The Investment Firms Regime

Draft EBA Guidelines

Proportionality

- Lists an additional set of criteria for setting proportionality thresholds
- Threshold for significance applied on a solo and consolidated basis

MRT identification

- Provides useful points of clarity particularly with respect to the process firms are expected to undertake as part of their assessment

Structural requirements

- Prescriptive about requirements for various different ‘special’ types of remuneration
- Bonus accrual periods should not be less than one year
- Significant firms must apply a 5 year deferral period for members of the management body
- May only use ‘alternative’ instruments for the purposes of delivering variable remuneration where cannot use more conventional instruments
- May not pay dividends or interest on instruments awarded as variable remuneration for the duration of the deferral period
- Variable pay delivered in instruments must be subject to a retention period of at least 12 months

Governance

- The remuneration policy should align with the business strategy including consideration of risks, including operational risk, ESG risk and mis-selling risk
- Remuneration policies must be gender neutral

Control function pay

- Control function remuneration should be ‘predominantly fixed’ which may create an effective cap on variable pay of 100% of fixed pay

Performance assessment for MRTs

- Sets out examples of metrics that are considered inherently risk adjusted and those that aren’t and therefore require risk adjustment
- Provides examples of qualitative criteria

The Investment Firms Regime

Next steps

Entities in scope & consolidation
Work with risk / finance to identify MiFID entities and consolidated groups

Thresholds
Assess position against significance thresholds (solo and consolidated)

MRTs
Identify MRTs against the new criteria to understand the impacted population

Gap Analysis
Analyse current approach against new requirements to identify gaps

Stakeholder management
Brief stakeholders on changes required

Implementation
Implement changes as required, particularly deferral, instruments, malus and clawback and governance.

Documentations
Update internal and external reporting and disclosure

Brexit and FS

On 24 December 2020, the EU and the UK finalised the negotiation of a new trade treaty - known as the Trade and Cooperation Agreement (TCA)

- The TCA is a “narrow” trade agreement. There are only limited provisions for financial services. The treaty establishes a single, cross-sector governance framework.
- The UK/EU relationship on financial services will be addressed through unilateral regulatory equivalence determinations.
- The EU-UK Declarations, which support the TCA include a shared commitment to agree a Memorandum of Understanding that should establish the “framework for cooperation”, including on equivalence decisions, by the end of March 2021.

What should FS firms focus on now?

- EEA firms in the Temporary Permissions Regime should ensure that they are compliant with the new regulatory requirements which came into effect from 31 December 2020, and prepare for those additional requirements which are subject to a transitional period. PRA update expected early 2021.
- UK-based firms should complete the changes agreed with EU regulators as part of the authorisation, or increase in scope, of their EU legal entities

https://www.pwc.co.uk/the-eu-referendum/beyond-brexit-insights/what-does-the-tca-mean-for-fs-firms.html

Thank you