

The Regulation of Remuneration: Where are we now with the Remuneration Codes?

July 2016



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Introduction

More than 6 years on from the original adoption by the FSA of a Remuneration Code, the regulation of pay in the financial services industry remains a hot topic, with change driven by European Directives that include the Third Capital Directive (CRD III), the Fourth Capital Directive (CRD IV), the Alternative Investment Funds Managers Directive (AIFMD) and the UCITS V Directive on Undertakings for Collective Investment in Transferable Securities. The FCA now boasts in its Handbook no less than five separate Remuneration Codes. Meanwhile the interpretation and application of the obligations created by the Directives remains something of a moving feast as the European Commission, the European Securities and Markets Authority (ESMA) and national regulators such as the Financial Conduct Authority each produce and from time to time revise their guidance on how the various directive requirements are to be applied, with the concept of "proportionality" being a particularly hot topic. Add into the mix the effect of Brexit.

In this paper, we take stock of where the different regimes have got to as at July 2016, consider the similarities and differences between the regimes, and look at some of the difficulties in applying the regimes.

Where have we got to with these regimes?

Key landmarks for the adoption of the various remuneration codes are set out below:

Event	CRD firms	AIFMD firms	UCITS firms
Enabling legislation	CRD III 2010 CRD IV 2013	AIFMD 2011	UCITS V July 2014
CEBS/ ESMA Guidelines	CEBS Guidelines published December 2010. Revised ESMA guidelines published November 2013	ESMA Guidelines originally published Feb 2013 Revised Final Guidelines published 31 March 2016	ESMA Final Guidelines published 31 March 2016
FSA/FCA/ PRA adoption of a Code	Remuneration Code originally published 1 January 2010. Revised Code to meet CRD III introduced Jan 2011. Revisions splitting this into two Remuneration Codes to reflect CRD IV in force from 1 January 2014. Further revisions in force from 1 July 2015 to create separate IFPRU Remuneration Code, BIPRU Remuneration Code and Dual Regulated Remuneration Code	AIFM Remuneration Code adopted 1 July 2013	UCITS Remuneration Code in effect from 18 March 2016

Broadly, from 1 July 2015, the date when the IFPRU Remuneration Code, BIPRU Remuneration Code and Dual-Regulated Firms Remuneration Code took effect, there have been in force three Codes applicable under CRD III/IV and another Code for managers of alternative investment funds (AIFMs). Since 18 March 2016 there has been another code for UCITS firms.

It should be noted that the FCA's Codes cannot be regarded as the last word on these matters. The FCA's Codes (and other guidance) operate as a supplement to the ESMA guidelines, and do not replace the ESMA guidelines. This may lead to some uncertainty in applying two sets of guidance, which are not always clearly expressed.

What are these provisions looking to achieve?

The rules originally created under CRD III, were designed to ensure that banks and investment firms have in place remuneration policies and practices that do not encourage or reward excessive risk-taking and so that the total variable remuneration paid by a firm must not limit its ability to strengthen its capital base. The focus therefore is on protecting the firm, particularly where that firm is of a size such that it matters.

The regimes under AIFMD and UCITS V have a different aim - *to promote sound and effective risk management and not to encourage risk taking which is inconsistent with the risk profiles and rules of the relevant funds*. The focus is on protecting investors rather than the fund management company. This clear distinction has however become slightly blurred in more recent iterations of these codes.

A concerted effort has been made to keep the different regimes as similar as possible but as indicated in the annexed table, there are differences, and in particular differences between the CRD regimes and those for UCITS managers or AIFMs.

What do these provisions cover?

Each of the enabling Directives imposes requirements relating to the setting of remuneration policy and mandates a series of principles applicable to remuneration policies, which are to be established and applied to the relevant staff, subject in each case to relevant principles of proportionality.

A side-by-side summary of the key provisions and principles appears as the Annex to this document.

Who and what does this affect?

Which firms are covered by which Codes?

As mentioned above there are currently therefore potentially five regimes that may apply to someone working in the financial sector:

- the **IFPRU Remuneration Code** in SYSC 19A, which applies to "**IFPRU Investment firms**" – broadly firms that are sole regulated by the FCA providing investment services under the Markets in Financial Instruments Directive (MiFID) that have been categorised as being of sufficient importance to be subject to full prudential supervision under CRD IV. This excludes firms that are only authorised to carry on one or more of the following MiFID investment activities/services: (a) reception and transmission of orders, (b) execution of orders on behalf of clients, (c) discretionary portfolio management, and (d) investment advice provided that they do not safeguard and administer assets or hold client money or assets and place themselves in debt with clients;
- the **AIFMD Remuneration Code** in SYSC 19B, applicable to full-scope authorised AIFMs;
- the **BIPRU Remuneration Code** in SYSC 19C, which applies to firms that fall within the definition of "**BIPRU firm**" broadly firms that are sole regulated by the FCA providing investment services under MiFID but not falling within the IFPRU Investment Firm definition and so not subject to full CRD IV prudential supervision; and
- the **Dual-regulated Firms Remuneration Code** in SYSC 19D which applies to building societies, banks, and all other investment firms authorised in the UK investment firms that have not been designated by the PRA as being of sufficient importance to be subject to prudential supervision by the PRA.

The IFPRU Remuneration Code, BIPRU Remuneration Code and Dual-Regulated Firms Remuneration Code generally include very similar provisions, with minor differences in wording. There are really only two major substantive differences between them.

One is the guidance on how proportionality is to be applied to the requirements and in relation to some of the rules about variable remuneration and reporting, reflecting the greater systemic importance of the generally larger firms caught by the IFPRU Remuneration Code and the Dual-Regulated Firms Remuneration Code.

The other is that the IFPRU Remuneration Code and the Dual-Regulated Firms Remuneration Code do, but the BIPRU Remuneration Code does not, include the so-called "bonus cap" - the controversial requirement to cap variable remuneration at one times fixed remuneration (or up to two times fixed remuneration if specifically authorised by shareholders). There is also an interesting technical difference affecting IFPRU firms and Dual-Regulated Firms that if a contract contains a provision that breaches certain of the rules in the relevant Code, that provision is rendered void, whereas there is no equivalent provision in the other Codes.

The AIFM Remuneration Code and the UCITS Remuneration Code also include extremely similar provisions to one another with only minor differences in wording and they generally also follow very similar wording to the other rules with changes reflecting the different aims for these codes.

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Overlapping regimes

No firm should fall within more than one of the IFPRU Remuneration Code, the BIPRU Remuneration Code and the Dual-Regulated Firms Remuneration Code – the categories are mutually exclusive. However, all firms covered by the AIFMD Remuneration Code or the UCITS Remuneration Code will also be caught by these first three codes. A firm might also be covered by both the AIFMD Remuneration Code and the UCITS Remuneration Code if it manages both types of fund. Depending on their job functions, staff within a firm covered by more than one regime might be covered by one or more of the relevant codes.

For BIPRU firms there are deeming provisions so that compliance with the AIFMD Remuneration Code or the UCITS Remuneration Code is deemed to constitute compliance with the BIPRU Code. There is no equivalent provision for the IFPRU Remuneration Code or the Dual-Regulated Firms Remuneration Code. This could cause difficulties for some firms, who in theory could be obliged to follow two regimes which to some degree at least contradict one another. It is not expected that many firms will fall within this classification, and where they do any difficulty may be mitigated by the FCA's guidance that considerations of proportionality may in many cases result in the disapplication of certain rules (as explained further below).

Where there is a conflict between differing rules, the choices for a firm would be:

- to follow a "lowest common denominator" approach on each issue and adopt rules that comply with whichever regimes is the most strict on each issue so that it can be argued that both codes have been complied with, or
- to justify a division of the remuneration between that provided for the AIFM and/or UCITS duties and the other duties and apply the relevant rules to each portion of remuneration. The FCA allows a fair degree of flexibility in deciding in what proportions to split such remuneration.

The FCA will provide individual guidance where this is needed.

Which payments?

The guidelines relate to "remuneration", defined in a very broad way under each of the regimes. There are small differences in the wording of each Code, but generally remuneration is broadly drafted and would include all forms of payment or benefits paid by the firm in exchange for professional services rendered by the relevant identified staff. In the case of an AIFM it would include any amount paid by a fund managed by the firm and in particular for an AIF, carried interest (but not a pro-rata return on any investment made by those staff members from their own funds and not funded from outstanding loans from the AIFM).

Remuneration includes fixed remuneration, variable remuneration and may include benefits such as cash, shares, cancellation of loans on dismissal, pension contributions and fringe benefits.

Distinguishing fixed remuneration and variable remuneration is key to the application of many of the rules. There have been high-

profile cases where a lack of precision in the definitions has been exploited. Notably RBS has been criticised for avoiding the bonus cap by providing its senior executives with a monthly award of shares in RBS and regarding this as part of the fixed remuneration, despite the fact that this element of the monthly pay would be reviewed annually and might be withdrawn. In its report ([Com \(2016\)510 final](#)) the European Commission criticised the rise of "role-based" allowances" as a way of classifying remuneration as being fixed.

Remuneration does not include dividends "*or similar distributions that partners receive as owners of a firm*" unless the material outcome of the payment... "*results in a circumvention of the relevant remuneration rules*". As discussed below, the distinction between remuneration and the fruits of ownership may be difficult to apply in practice.

There are obligations to ensure the variable remuneration is not paid through vehicles or through any other methods with a view to evading artificially the provisions in the relevant Code's guidelines.

Which staff does this apply to?

The guidelines apply to categories of staff defined in each regime as "identified staff". Again there are nuances to how staff are defined in each Code, but broadly "identified staff" include:

- executive and non-executive members of the governing body of the firm;
- senior management;
- control functions (which includes staff responsible for risk management, compliance, internal audit and similar functions);
- staff responsible for heading the portfolio management, administration, marketing and human resources; and other "risk takers" if they can (individually or collectively) exert material influence on the firm or the fund's risk profile or take decisions materially affecting risk provisions. This could include sales persons, individual traders and specific trading desks.

However, staff falling within these categories may fall outside the definition of "identified staff" if it is demonstrated that they have no material impact on the risk profile of the firm (or, in the case of the AIFM or UCITS Remuneration Codes, the funds it manages).

Conversely, staff who are not within one of the above categories, but are in the same "remuneration bracket" as senior managers and risk takers should be included as identified staff if they have a material impact on the risk profile of the firm or the funds it manages.

The definitions are generally impressively vague, and it is probably best to assume that there is in effect a burden of proof on the firm, if it wishes to consider a staff member to be exempted from this definition, to demonstrate that the staff member does not contribute to the risk profile of the firm or, where relevant, the funds it manages.

Applying proportionality

Proportionality

The detailed requirements of the remuneration principles are onerous and difficult to apply for smaller firms, and proportionality has always been recognised as an important issue. For many firms the application of proportionality regimes will substantially alleviate the extent to which they are affected by the relevant Code. The FCA's guidance (issued separately for each of these codes and available on the FCA website) takes this principle quite a long way, to the extent that many of the Code requirements can be entirely excluded. The European Commission and the European Banking Authority (EBA) do not agree that this approach to proportionality is admissible under the wording of the CRD IV Directive. However in its report ([Com \(2016\)510 final](#)) the European Commission has proposed that it will study proposals for amending legislation to allow this.

Proportionality regimes have been developed for each of the different Codes.

Proportionality tiers under the IFPRU Remuneration Code and the Dual-Regulated Firms Remuneration Code

The FCA has divided firms covered by the IFPRU Remuneration Code into three tiers and will adopt a different proportionate approach to the implementation of the Remuneration Principles depending on the internal organisation, skill, scope and complexity of activities carried out by the firm.

Broadly proportionality is looked at by reference to the size of the firm, and if the firm is in a group containing other Remuneration Code firms, by reference to the size of the largest Remuneration Code firm within the group, however this general principle is supplemented by a great deal of further guidance and commentary.

The three tiers of proportionality are set out in the table below:

Proportionality level	Type of firm	Relevant total assets on relevant date of firm
<i>Proportionality level one</i>	<i>IFPRU 730k Investment firm that is a full scope IFPRU investment firm</i>	Exceeding £50bn
<i>Proportionality level two</i>	<i>IFPRU 730k Investment firm that is a full scope IFPRU investment firm</i>	Exceeding £15bn, but not exceeding £50bn
<i>Proportionality level three</i>	<i>Any full scope IFPRU Investment firm that does not fall within proportionality level one or proportionality level two.</i>	Not applicable
	<i>IFPRU limited licence firm</i>	
	<i>IFPRU limited activity firm</i>	

A similar three-tier banding is used for proportionality purposes for the Dual-Regulated Firms Remuneration Code:

Proportionality level	Type of firm	Relevant total assets on relevant date of firm
<i>Proportionality level one</i>	<i>UK Bank, Building Society; UK designated investment firm that is a CRD full-scope firm</i>	Exceeding £50bn
<i>Proportionality level two</i>	<i>UK Bank, Building Society; UK designated investment firm that is a CRD full-scope firm</i>	Exceeding £15bn, but not exceeding £50bn
<i>Proportionality level three</i>	<i>UK Bank, Building Society</i>	Not applicable
	<i>UK designated investment firm that is a limited licence firm</i>	
	<i>UK designated investment firm that is a limited activity firm</i>	

Firms close to a boundary between two proportionality tiers should discuss with the FCA which tier is applicable to them. The FCA may authorise a firm to treat itself as being in the lower proportionality tier.

The FCA will also consider applications from firms within higher proportionality tiers that may be considered within a lower proportionality tier, on the basis of the firm's risk.

The FCA considers it normally appropriate for a firm in proportionality level three to disapply:

- (1) the requirements for retaining shares or other instruments granted to an employee by way of variable remuneration;
- (2) the requirements for deferral of variable remuneration; and
- (3) the requirements for later adjustment of variable consideration by reference to performance.

The FCA considers also that it may also be appropriate for certain proportionality level three firms to disapply the specific ratio between fixed and variable components of total remuneration and for other firms falling within the definition of limited licence firms and limited activity firms to disapply the 1:1 to 1:2 specific ratios between fixed and variable components of total remuneration although, if requested by the FCA, the FCA will expect the firm's senior management to be able to demonstrate why the firm believes it is reasonable to do this.

Proportionality is also written into some of the individual rules which apply only to larger firms or larger pay-packets.

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Proportionality under the BIPRU Remuneration Code

Where a BIPRU Remuneration Code firm is part of the same group as another firm to which the IFPRU Remuneration Code or Dual-Regulated Firms Remuneration Code applies, the proportionality rules applicable to the BIPRU Remuneration Code do not apply. The matter is instead determined by the proportionality rules applicable to the other relevant Remuneration Code.

Again the general rule is that the BIPRU Remuneration Code requires firms to apply the remuneration principles of that code in a way and to the extent that is appropriate to the firm's size, internal organisation and the nature, the scope and the complexity of its activities.

It may not be necessary for BIPRU firms to apply BIPRU remuneration principles at all. The FCA states its view that it will normally be appropriate for a BIPRU firm to disapply for proportionality reasons the following rules:

- the requirement to retain shares or other instruments (SYSC 19C.3.47R);
- the deferral requirements (SYSC 19C.3.49R);
- performance adjustment (SYSC 19C.3.51R); and
- the ratios between fixed and variable components of total remuneration (SYSC 19C.3.44R).

The FCA also notes that a BIPRU firm 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'.

However, where 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) and are not capable of disapplication under the approach set out above, the FCA does not consider that the remuneration principles proportionality rule permits a firm to apply lower numerical criteria.

Guidance is also provided on:

- where it might be appropriate not to maintain a separate Remuneration Committee; and
- where it might be appropriate to avoid application of disclosure rules requiring qualitative and quantitative information to be provided by firms considered "significant" (which FCA defines by reference to a relevant total assets test of £50bn).

Proportionality under the AIFM Remuneration Code and the UCITS Remuneration Code

Both the AIFMD and the UCITS V provisions also include a principle of proportionality based on a similar overarching requirement that the fund managers are required to comply with the remuneration principles "in a way and to the extent that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities".

ESMA had proposed in its original AIFM consultation a rather less comprehensive application of proportionality - that proportionality might affect the application of the principles, but could not neutralise them, even in relation to some principles which CEBS (ESMA's forerunner), in relation to the equivalent regulations for banks, had agreed could be neutralised. However in its final guidance ESMA was persuaded to align the provisions of the AIFMD and UCITS guidelines with the CEBS guidelines and allow that proportionality may lead, on an exceptional basis, to the disapplication of some requirements, in particular the requirement for a remuneration committee and the so-called "Pay-out Process Rules". These rules, arguably the most contentious aspect of the remuneration rules, include the requirements that:

- a substantial proportion and in any event at least 50% of any variable remuneration should consist of units or shares of the AIF concerned or equivalent ownership interests;
- such units, shares or interests must be subject to an appropriate retention policy designed to align incentives to the long-term interests of the AIFM and AIFs it manages;
- a substantial portion, and at least 40% of variable remuneration must be deferred over a period that is appropriate to the life cycle of the AIF concerned; and
- variable remuneration be paid or vest only if it is sustainable according to the financial situation of the AIFM and justified according to the performance of the AIF.

The ESMA guidelines allowed a certain degree of inflexibility in how proportionality can be applied, in that specific numerical criteria (the minimum deferral period of 3 to 5 years; the minimum proportion of 40 to 60% of variable remuneration to be deferred; and the minimum portion of 50% of variable remuneration that should be paid in instruments) can (in exceptional circumstances) be disappplied, but not relaxed by lowering the thresholds.

The FCA has made full use of the latitude provided by ESMA. The FCA's approach to proportionality on these matters is to apply a (rebuttable) presumption based on the size of assets under management as to whether these rules are appropriate as follows:

Type of firm	AuM threshold	Presumption
AIFMs which manage portfolios of AIFs including assets acquired through use of leverage	Less than £1 billion	it is appropriate to disapply <i>Pay-out Process Rules</i>
	Greater than £1 billion	it is not appropriate to disapply <i>Pay-out Process Rules</i>
AIFMs which manage portfolios of AIFs that are unleveraged and have no redemption rights exercisable during a period of 5 years following the date of initial investment in each AIF	Less than £5 billion	it is appropriate to disapply <i>Pay-out Process Rules</i>
	Greater than £5 billion	it is not appropriate to disapply <i>Pay-out Process Rules</i>

However these presumptions cannot be applied simplistically and the guidance lists a series of other "proportionality elements" that firms should take into account in deciding whether the presumption created by these thresholds should apply. These elements include:

- the size of the firm (and in particular of its management team);
- its internal organisation (including whether the fund manager is a quoted company or has a significant proportion of its equity held by investors not working in the business, both being indications that the rules should not be disapplied);
- the nature, scope and complexity of its activities (including its risk profile and delegation arrangements); and
- the nature of fee structures such as performance fees or carried interest, particularly where the design of the structures may satisfy the object of aligning interests with investors).

Investment Managers that are "significant" in terms of their size, internal organisation and the nature, scope and complexity of their activities must establish a remuneration committee. The FCA's guidance is that all three of the proportionality elements mentioned above need to be satisfied for the obligation to have a separate remuneration committee to apply and applies the size thresholds above to provide a (rebuttable) presumption as to the proportionality of requiring a remuneration committee.

In relation to proportionality for the UCITS Remuneration Code the FCA has adopted rules that take account of the same elements as are mentioned above, but has not so far published guideline thresholds as it did for AIFMs.

The FCA does provide however that it does not generally consider it necessary for a firm to apply requirements for retaining shares or other instruments, deferral and performance adjustment in relation to an individual, his variable remuneration is no more than 33% of total remuneration and his total remuneration is no more than £500,000.

Some difficult issues

What is an "award"; when is "vesting"?

In order to know how these rules (and especially the pay-out process rules) apply, it is necessary to determine when an award is "made" and when it is "vested". These concepts are recognisable in the context of the type of traditional bonus scheme such as an LTIP, STIP or share option scheme that one might see operated within a major institution, but may be less easy to apply to the messy and bespoke arrangements that one can find with private firms or partnerships, or when dealing with remuneration through a carried interest scheme. Disappointingly, the FCA has not put forward detailed guidance on this point.

In our opinion the broad concept is that an award can be regarded as having been made whenever a specific payment, or fixed

method of calculation of the payment is agreed. If there are no conditions or clawback arrangements, then the award is regarded as vested at the same time (even if it is paid out only later). If there are significant conditions, then vesting occurs when these conditions are met.

It may be difficult in applying the analysis to make a distinction between conditions that determine vesting has taken place and conditions that would cause the imposition of malus or clawback (which is recognised as something that happens at a later stage than vesting). As new arrangements are designed with the relevant remuneration principles in mind, no doubt appropriate language will be used to characterise the different stages of making awards so that it is clear how these arrangements apply.

Applying these concepts to an existing carried interest structure is particularly interesting. If a carried interest vehicle is used then awards and vesting will probably be recognisable according to the rules used to provide interests to individuals out of the carried interest vehicle. However in cases where the carried interest is apportioned out to named individuals, and is a true interest in the fund vehicle, then there may be a strong argument that the award was made at that point (and perhaps already is vested). Such an analysis may be helpful where the arrangements were designed in the past without anticipating the new rules since it may allow one to conclude that these can be regarded as having happened before the new rules come into effect.

Carried Interest as remuneration

During the consultation carried out by ESMA when developing its proposed guidance on applying the remuneration provisions in the AIFMD, some respondents to the consultation sought to argue that carried interest was of a nature that should not count as remuneration because carried interest arrangements are already designed to create an alignment between the interest of investors and of management, and there is scope for argument on the extent to which carried interests should be regarded as remuneration. ESMA considered itself bound by the definition of "Carried Interest" in the AIFMD but did provide guidance excluding from the definition of remuneration return on investments made by staff in so far as this relates to their proportionate return on the amount they have invested.

The FCA's guidance appears to have accepted the view that carried interest arrangements as used within traditional private equity structures are already designed to create an alignment between the interest of investors and of management. In one of a series of examples provided within its guidance as to the application of the principle of proportionality, it accepts an argument that where carried interest arrangements may reasonably be thought of as creating this alignment the principle of proportionality may be used to exclude the operation of the pay-out process rules. This approach seems neatly to sidestep the conclusion that ESMA had reached that it had no scope but to treat carried interest as remuneration for the purpose of applying these rules.

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Carry payments made by an AIF to the AIFM

ESMA rejected a submission that payments made directly by the AIF to the AIFM as a whole should not be regarded as payments made to the benefit of the relevant categories of staff of the AIFM. It is difficult following the reasoning here, or how such an analysis is to be applied if such payments are received by the AIFM in a different period to the period in which they are allocated out to staff or indeed if they are paid out by way of dividend to non-staff owners. It is surprising that this point has not been picked up in the FCA's guidance.

Dealing with situations where it is impractical to pay variable remuneration in the form of shares, units or other instruments

In its guidance relating to the AIFMD Remuneration Code, the FCA accepts that there may be practical difficulties in paying remuneration in the form of shares, units or other instruments resulting from the nature of the fund or marketing or tax restrictions and applies the proportionality principle to allow a firm not to apply this rule in such a situation. It also recognises that this rule may be inappropriate for some staff (for example senior management or compliance or audit staff). It recommends that firms in such situations instead make the payment in shares or other interests in the AIFMD itself, its parent company or in an instrument linked to the weighted average of AIFs managed by the AIFM.

Excluding business owners from the definition of "identified staff"

The members of an LLP or owners of a small company are not excluded from the definition of "identified staff", although it is recognised that the dividends paid to shareholders and profit allocations to members of an LLP should not be considered to constitute remuneration as long as this is not being used as a means of circumventing the requirements of the Directive.

In the context of the AIFMD Remuneration Code, the FCA has provided guidance on possible approaches on how to distinguish "remuneration" from the fruits of ownership of the business in the case of a partnership or LLP. The FCA suggests two approaches to this.

The first approach would be to look at how profit-sharing is carried out to see if this discernibly breaks down into an equivalent of fixed salary, bonus and residual profit share. For example if there are senior or founding partners who receive residual profit share (and other partners working within the business do not), their share could be regarded as the true profit element and not regarded as remuneration. If there are arrangements for a fixed drawing taken out in advance of profits being earned, this can be regarded as a fixed element of remuneration. This approach seems a little confused from the strict legal viewpoint (it confuses drawings, which technically may be a borrowing against future profit allocations with the allocation of profit). However, the approach could be a practical one in some circumstances as it will often accord with how the partners in

question see their remuneration being structured.

The second possible approach is based on benchmarking against what is paid as salary by competitor companies; or considering what can be regarded as a reasonable return on investment; or looking at how the pay out of partnership earnings occurs and how profits are shared.

The concept of benchmarking in this context seems an extremely difficult one to apply. First as practical matter the accounts of general partnerships are not publicly available and the accounts of LLPs do not break down the remuneration of members between salary equivalent, bonus and other profit share¹. Even if figures can be obtained (and one can see some of the remuneration consultancies looking forward to good times ahead in compiling and charging for these figures), there is no agreed basis on which the benchmarks will apply. For example the precise scope of the function of a staff member may not be clear from his or her job title. There may be different levels of responsibility according to the arrangements in place for delegation of functions. The responsibility levels may be very different from different sizes of fund. Founder members of an LLP with an ownership arrangement may be happy to take a very small fixed remuneration and have no arrangements for bonuses factored in as whatever is not paid out as remuneration will eventually come to them as a profit share.

It will be interesting to see how firms respond to these alternatives – one rational response might be to finesse the arrangements for sharing profits within an LLP or other partnership to create something that clearly falls within the model of fixed remuneration, bonus tranche and variable profits tranche so as to sidestep the difficult questions raised by the concept of benchmarking.

The FCA also acknowledged in its AIFMD Remuneration Code guidance that insofar as the pay-out process rules apply and require the deferral of a profit pay-out, or a pay-out otherwise than in cash, this could give rise to a difficult tax position, as the tax is payable by partners or members of an LLP whether or not profits are paid out. The FCA sought to ameliorate this potential difficulty by allowing deferrals of income to apply on a net-of-tax basis. However there is now less need for such flexibility as the tax rules now allow, where there is such a deferment, for the partners or members not to have to declare such tax in their own tax returns and instead for any such tax to be paid by the LLP, prior to the remuneration vesting with the individuals concerned, and the individuals later receiving such benefits then to obtain a credit for the tax paid.

Application to service providers and delegates

The ESMA guidelines extended the scope of the remuneration principles so that they would apply to cover staff working for firms to which the AIFM or UCITS Manager delegates portfolio

¹ A distinction is made in statutory accounts under the SORP applicable to LLPs between profit share received by way of remuneration and other profit share but this is not applied in a way that would be relevant to the breakdown required for these purposes.

management or risk management where those activities have a material impact on the fund's profile. However this requirement does not apply where the delegate is complying with the rules and guidelines that are "equally effective" as the remuneration principles. The FCA has adopted a wide interpretation of what is meant by "equally effective". It suggests that a service provider complying with the IFPRU Remuneration Code or the BIPRU Remuneration Code (or other implementations of the CRD and MiFID remuneration regimes elsewhere in Europe) would be considered to be operating equivalent arrangements and will accept a delegate as being subject to such an equally effective regime even if it is in a Member State that has not applied the full CRD remuneration regime to that firm (perhaps as a result of proportionality).

Conclusion

The Remuneration Codes have not been popular within the financial services industry. The industry has been generally sceptical about both the benefits of these rules and of the motivation behind them – with the accusation being that this is more based on populist banker-bashing than evidence-based policy. Whilst the principles ostensibly behind these rules cannot be disagreed with, it may be questioned whether the prescriptiveness of individual rules are really likely to promote these principles. The enthusiasm with which the FCA has taken as far as possible the concepts of proportionality in applying such rules may be seen as showing some sympathy for that view.

Unfortunately we cannot say that this is an area where no further development is expected in the near future. MiFID II will be weighing in to superimpose further principles for affected firms including a principle that the remuneration policy of persons involved in the provision of services to clients should encourage "*responsible conduct, fair treatment of clients as well as avoiding conflict of interest*" (Article 9(3)(c) and "*an investment firm which provides investment services to clients should not remunerate or assess the performance of its staff in a way that conflicts with its duty to act in the best interests of its clients*" (Article 24(10)).

Brexit will not change the application of these Codes in the short-term, and even following the UK's exit from the EU it is doubtful whether we will see any radical change to these regimes—the UK adopted the original Remuneration Code before this was an EU requirement and there is likely to continue to be a need or desire to maintain 'equivalence' with EU regulation. It is possible however that individual rules such as the bonus cap might in time be altered.

Whatever the rights and wrongs of these rules they are now a fact of life within the financial services industry and firms must learn to live with them.

To the extent that they have not already done this, firms should now:

- ensure that they understand which Code(s) affect them and how they are affected by the proportionality rules;

- identify which staff are affected (and if more than one Code applies, by which Code); and
- identify what should be regarded as the fixed and variable elements of the pay of the relevant staff.

Having taken these preliminary steps, firms should ensure both that they have the relevant governance arrangements in place (including an appropriate remuneration committee where this is required) and that they are geared up to integrate line management, the HR function and the risk and compliance function within the firm to develop remuneration arrangements that will meet operational requirements, the letter of these Codes, the overarching principles behind the Codes and the guidance at European level as well as that at national level. This will all need to be done and documented in a way so that the thinking behind the remuneration policy can be justified to the FCA, and in a way that has regard to existing contracts and employment law.

None of this is easy, and many firms will require outside advice. We at Fieldfisher would be delighted to help.

Annex - Comparison of remuneration provisions in the UK Remuneration Codes and the UCITS V requirements

[Note table excludes guidance and some rules and occasionally resorts to paraphrase – it is not a substitute for reading the actual rules]

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
<p>Proportionality rule SYSC 19A.3.3 / SYSC 19D.3.3 / SYSC 19C.3.3</p> <p>When establishing and applying the total remuneration policies for IFPRU/ Dual-Regulated firms/BIPRU Remuneration Code staff, a firm must comply with this section in a way and to the extent that is appropriate to its size, internal organisation and the nature, the scope and the complexity of its activities.</p> <p>This does not apply to the requirement for significant firms to have a remuneration committee.</p>			<p>Proportionality rule SYSC 19B.1.4</p> <p>When establishing and applying the total remuneration policies for AIFM Remuneration Code staff (inclusive of salaries and discretionary pension benefits), an AIFM must comply with the AIFM remuneration principles in a way and to the extent that is appropriate to its size, internal organisation and the nature, scope and complexity of its activities.</p> <p>This does not apply to the requirement for significant AIFMs to have a remuneration committee.</p> <p>The AIFM remuneration principles apply to remuneration of any type paid by the AIFM, to any amount paid directly by the AIF itself, including carried interest, and to any transfer of units or shares of the AIF made to the benefits of AIFM Remuneration Code staff.</p>	<p>Proportionality rule SYSC 19E.2.4</p> <p>When establishing and applying the remuneration policies for UCITS Remuneration Code staff, a management company must comply with the UCITS remuneration principles in a way and to the extent that is appropriate to its size, internal organisation and the nature, scope and complexity of its activities.</p> <p>This does not apply to the requirement for significant management companies to have a remuneration committee.</p> <p>The UCITS remuneration principles apply to any benefit of any type paid by the management company, any amount paid directly by the UCITS itself, including performance fees, for the benefit of UCITS Remuneration Code staff, and any transfer of units or shares of the UCITS made for the benefit of UCITS Remuneration Code staff.</p>	<p>IFPRU, Dual-Regulated firms, BIPRU and UCITS Remuneration Codes do not specifically mention "salaries and discretionary pension benefits".</p> <p>It is doubtful whether anything turns on this.</p> <p>The AIFM and UCITS Remuneration Codes also specifically set out to which types of remuneration each code applies.</p>
<p>Staff affected SYSC 19A.3.4 / SYSC 19D.3.4</p> <p>IFPRU/Dual-Regulated firms Remuneration Code staff comprises an employee of the firm whose professional activities have a material impact on the firm's risk profile. It includes certain employees of overseas firms that would be IFPRU/ Dual-Regulated firms had they been a UK domestic firm.</p> <p>SYSC 19A.3.5 / SYSC 19D.3.5 / SYSC 19C.3.5</p> <p>A firm must maintain a record of its Remuneration Code in accordance with the general record-keeping requirements (SYSC 9), and take reasonable steps to ensure that its Remuneration Code staff understand the implications of their status as such, including the potential for remuneration which does not comply with certain requirements of the Remuneration Code to be rendered void and recoverable by the firm.</p>		<p>Staff affected SYSC 19C.3.4</p> <p>BIPRU Remuneration Code staff comprises categories of staff including senior management, risk takers, staff engaged in control functions and any employee receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers, whose professional activities have a material impact on the firm's risk profile.</p>	<p>Staff affected SYSC 19B.1.3</p> <p>AIFM Remuneration Code staff comprise those categories of staff whose professional activities have a material impact on the risk profiles of the AIFMs or of the AIFs the AIFM manages. This includes senior management, risk takers, control functions, and any employees receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers.</p>	<p>Staff affected SYSC 19E.2.2</p> <p>UCITS Remuneration Code staff comprise those categories of staff, whose professional activities have a material impact on the risk profiles of the management company or the UCITS that the management company manages.</p> <p>UCITS Remuneration Code staff must comprise senior management, risk takers, staff engaged in control functions and any employees receiving total remuneration that takes them into the same remuneration bracket of senior management and risk takers.</p>	<p>The requirement for IFPRU, Dual-Regulated firms and BIPRU Remuneration Code staff focuses on risk to the firm; the requirement for AIFM/UCITS staff focuses both on risk to the firm and to the funds it manages.</p>

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
<p>Remuneration Principle 1: Risk management and risk tolerance SYSC 19A.3.7 / SYSC 19D.3.7 / SYSC 19C.3.7</p> <p>A firm must ensure that its remuneration policy is consistent with and promotes sound and effective risk management and does not encourage risk-taking that exceeds the level of tolerated risk of the firm.</p>			<p>AIFM/ UCITS Remuneration Principle 1: Risk management SYSC 19B.1.5 / SYSC 19E.2.5</p> <p>A firm/management company must ensure that its remuneration policy is consistent with and promotes sound and effective risk management, and does not encourage risk-taking that is inconsistent with the risk profile of the instrument constituting the fund of the AIFs/UCITS it manages.</p>		<p>The IFPRU, Dual-Regulated firms and BIPRU Remuneration Code requirements are focused on the risk management of the employing firm, whereas the AIFM and UCITS requirements are focused on the risk profile of the funds managed. Theoretically under these latter codes, a remuneration policy could be criticised for not incentivising risk.</p> <p>The requirement to ensure UCITS remuneration policies "do not impair compliance with the management company's duty to act in the best interest of the UCITS" from the UCITS V Directive was not included in the UCITS Remuneration Code.</p>
<p>Remuneration Principle 2: Supporting business strategy etc. SYSC 19A.3.8 / SYSC 19D.3.8 / SYSC 19C.3.8</p> <p>A firm must ensure that its remuneration policy is in line with the business strategy, objectives, values and long-term interests of the firm.</p>			<p>AIFM/UCITS Remuneration Principle 2: Supporting business strategy etc. SYSC 19B.1.6 / SYSC 19E.2.6</p> <p>An AIFM/management company must ensure that its remuneration policy is in line with the business strategy, objectives, values and interests of the AIFM/management company and the AIFs/UCITS it manages or the investors of such AIFs/UCITS, and includes measures to avoid conflicts of interest.</p>		<p>The IFPRU, Dual-Regulated firms and BIPRU Remuneration Codes are focused on the strategy of the employing firm, whereas the AIFM and UCITS requirements also focus on the funds managed.</p> <p>The AIFM and UCITS Remuneration Codes include conflicts of interest under this Principle whereas the IFPRU, Dual-Regulated firms and BIPRU Remuneration Codes contain a separate Principle 3 below.</p>
<p>Remuneration Principle 3: Conflicts of interest SYSC 19A.3.9 / SYSC 19D.3.9 / SYSC 19C.3.9</p> <p>A firm must ensure that its remuneration policy includes measures to avoid conflicts of interest.</p>			See row above.	See row above.	

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
<p>Remuneration Principle 4: Governance SYSC 19A.3.10 -12A / SYSC 19D.3.10-13 / SYSC 19C.3.10 -12</p> <p>A firm must ensure that its [management]/governing body in its supervisory function adopts and periodically reviews the general principles of the remuneration policy and is responsible for [overseeing] its implementation.</p> <p>A firm must ensure that the implementation of the remuneration policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for remuneration adopted by the [management]/governing body in its supervisory function.</p> <p>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.</p> <p>The remuneration committee must be constituted in a way that enables it to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk, capital and liquidity. The chairman and the members of the remuneration committee must be members of the [management]/governing body who do not perform any executive function in the firm.</p> <p>The remuneration committee must be responsible for the preparation of decisions regarding remuneration, including those which have implications for the risk and risk management of the firm and which are to be taken by the [management]/governing body.</p> <p>When preparing such decisions, the remuneration committee must take into account the long-term interests of shareholders, investors and other stakeholders in the firm [and the public interest].</p> <p>[A firm that maintains a website must explain on the website how it complies with the Remuneration Code.]*</p> <p><i>* Words in square brackets not applicable in the BIPRU Remuneration Code.</i></p>			<p>AIFM Remuneration Principle 3: Governance SYSC 19B.1.7-9</p> <p>An AIFM must ensure that the governing body of the AIFM, in its supervisory function, adopts and periodically reviews the general principles of the remuneration policy and is responsible for its implementation</p> <p>An AIFM must ensure the implementation of the remuneration policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for remuneration adopted by the governing body in its supervisory function.</p> <p>An AIFM 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.</p> <p>The remuneration committee must be constituted in a way that enables it to exercise competent and independent judgment on remuneration policies and practices, and the incentives created for managing risk.</p> <p>The chairman and the members of the remuneration committee must be members of the governing body who do not perform any executive function in the AIFM.</p> <p>The remuneration committee must be responsible for the preparation of decisions regarding remuneration, including those which have implications for the risk and risk management of the AIFM or the AIF concerned and which are taken by the governing body in its supervisory function.</p>	<p>UCITS Remuneration Principle 3: Governance SYSC 19E.2.7-9</p> <p>A management company must ensure that its management body in its supervisory function adopts and reviews at least annually the general principles of the remuneration policy and is responsible for the implementation of the general principles of the remuneration policy.</p> <p>The above tasks must be undertaken only by members of the management body who do not perform any executive functions in the management company concerned and have expertise in risk management and remuneration.</p> <p>A management company must ensure the implementation of the remuneration policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for remuneration adopted by the management body in its supervisory function.</p> <p>A management company must establish a remuneration committee if it is significant in terms of its size, the size of the UCITS that it manages, the complexity of its internal organisation or the nature, the scope and the complexity of its activities.</p> <p>The remuneration committee must be constituted in a way that enables it to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk.</p> <p>The remuneration committee must be responsible for the preparation of decisions regarding remuneration, including those which have implications for the risk and risk management of the management company or the UCITS concerned and are taken by the management body in its supervisory function.</p> <p>The chairman and the members of the remuneration committee must be members of the management body who do not perform any executive function in the management company.</p> <p>When preparing its decisions, the remuneration committee must take into account the long-term interest of investors and other stakeholders and the public interest.</p>	<p>For IFPRU and Dual-Regulated Remuneration Code firms, the management bodies must be responsible for overseeing the implementation of the remuneration policy.</p> <p>For BIPRU Remuneration Code firms, the governing bodies must be responsible for the implementation of the remuneration policy. It is doubted whether much turns on the difference in phrasing.</p> <p>AIFMD does not include a provision that, if national law exists that requires employee representation on the management body, there must be employee representatives on the remuneration committee.</p> <p>AIFMD does not include the requirement that decisions of the remuneration committee must "take into account the long-term interest of investors and other stakeholders and the public interest".</p> <p>The BIPRU, AIFMD and UCITS codes do not include a requirement for such firms to explain how they comply on their websites.</p>

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
Remuneration Principle 5: Control functions SYSC 19A.3.14-16 / SYSC 19D.3.15-17 / SYSC 19C.3.14-16 <p>A firm must ensure that employees engaged in control functions are independent from the business units they oversee, that they have appropriate authority and that they are remunerated adequately to attract qualified and experienced staff and in accordance with the achievement of the objectives linked to their functions, independent of the performance of the business areas they control.</p> <p>A firm must ensure that the remuneration of the senior officers in risk management and compliance functions is directly overseen by the remuneration committee or, if such a committee has not been established, by the governing body in its supervisory function.</p>			AIFM/UCITS Remuneration Principle 4: Control functions SYSC 19B.1.10-11 / SYSC 19E.2.10-11 <p>An AIFM/management company must ensure that employees engaged in control functions are compensated according to the achievement of the objectives linked to their functions, independent of the performance of the business areas they control/those that are within their remit.</p> <p>An AIFM/management company must ensure the remuneration of the senior officers in the risk management and compliance functions is directly overseen by the remuneration committee, or, if such a committee has not been established, by the governing body in its supervisory function.</p>		<p>The guidance for IFPRU, Dual-Regulated firms and BIPRU Remuneration Codes suggests seeking input from HR and other business areas. They suggest that the variable: fixed component ratio of remuneration should be significantly lower for those in risk management and compliance.</p>
Remuneration Principle 6: Remuneration and capital SYSC 19A.3.18 / SYSC 19D.3.19 / SYSC 19C.3.18 <p>A firm must ensure that total variable remuneration does not limit the firm's ability to strengthen its capital base.</p>			No equivalent provision.	No equivalent provision.	
Remuneration Principle 7: Exceptional government intervention SYSC 19A.3.20 / SYSC 19D.3.21 / SYSC 19C.3.20 <p>A firm that benefits from exceptional government intervention must ensure that variable remuneration is strictly limited as a percentage of net revenues when it is inconsistent with the maintenance of a sound capital base and timely exit from government support, that it restructures remuneration in a manner aligned with sound risk management and long-term growth, including when appropriate establishing limits to the remuneration of members of its management body/senior personnel, and that no variable remuneration is paid to members of its management body unless this is justified.</p>			No equivalent provision.	No equivalent provision.	
Remuneration Principle 8: Profit-based measurement and risk adjustment SYSC 19A.3.22-25 / SYSC 19D.3.23-27 / SYSC 19C.3.22-25 <p>A firm must ensure that any measurement of performance used to calculate variable remuneration components or pools of variable remuneration components includes adjustments for all types of current and future risks and takes into account the cost and quantity of the capital and the liquidity required, and takes into account the need for consistency with the timing and likelihood of the firm receiving potential future revenues incorporated into current earnings.</p> <p>A firm must ensure that the allocation of variable remuneration components within the firm also takes into account all types of current and future risks.</p> <p>Assessments of financial performance used to calculate variable remuneration components or pools of variable remuneration components must be based principally on profits.</p>			AIFM/UCITS Remuneration Principle 6: Measurement of performance SYSC 19B.1.21 / SYSC 19E.2.24 <p>An AIFM/management company must ensure the measurement of performance used to calculate variable remuneration components, or pools of variable remuneration components, includes a comprehensive adjustment mechanism to integrate all relevant types of current and future risks.</p>		<p>Only the IFPRU and Dual-Regulated firms Remuneration Codes add the possibility of malus or clawback arrangements for reducing payouts of amounts previously earned.</p>
SYSC 19A.3.27 <p>A firm must ensure that its total variable remuneration is generally considerably contracted where subdued or negative financial performance of the firm occurs, taking into account both current remuneration and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.</p>	SYSC 19D.3.25-29 <p>A firm must ensure that its total variable remuneration is generally considerably contracted where subdued or negative financial performance of the firm occurs, taking into account both current remuneration and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.</p> <p>A firm must have a clear and verifiable mechanism for measuring performance, with risk adjustment applied thereafter in a clear and transparent manner.</p> <p>A firm's risk-adjustment approach must reflect both ex-ante adjustment (which adjusts remuneration for intrinsic risks that are inherent in its business activities) and ex-post adjustment (which adjusts remuneration for crystallisation of specific risks events).</p>	SYSC 19C.3.27 <p>A firm must ensure that its total variable remuneration is generally considerably contracted where subdued or negative financial performance of the firm occurs, taking into account both current remuneration and reductions in payouts of amounts previously earned.</p>			

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
Remuneration Principle 9: Pensions policy SYSC 19A.3.29 / SYSC 19D.3.31 / SYSC 19C.3.29 A firm must ensure that its pension policy is in line with its business strategy, objectives, values and long-term interests, that when an employee leaves the firm before retirement, any discretionary pension benefits are held by the firm for a period of five years in the form of instruments referred to in Remuneration Principle 12(f), and that, when an employee reaches retirement, discretionary pension benefits are paid to the employee in the form of instruments referred to in Remuneration Principle 12(f) and subject to a five-year retention period.			AIFM Remuneration Principle 7: Pension policy SYSC 19B.1.22 An AIFM must ensure that its pension policy is in line with its business strategy, objectives, values and long-term interests of the AIFs it manages, that when an employee leaves the firm before retirement, any discretionary pension benefits are held by the firm for a period of five years in the form of instruments in Remuneration Principle 5(e), and that, in the case of an employee reaching retirement, discretionary pension benefits are paid to the employee in the form of instruments referred to in Remuneration Principle 5(e) and subject to a five-year retention period.	UCITS Remuneration Principle 7: Pension policy SYSC 19E.2.25 A management company must ensure that its pension policy is in line with the business strategy, objectives, values and long-term interests of the management company, and the UCITS it manages, that when an employee leaves the management company before retirement, any discretionary pension benefits are held by the management company for a period of five years in the form of the instruments referred to in Remuneration Principle 5(e), and that, for an employee reaching retirement, discretionary pension benefits are paid to the employee in the form of instruments referred to in Remuneration Principle 5(e), and subject to a five-year retention period.	The IFPRU, Dual-Regulated firms and BIPRU Remuneration Codes are focused on the policies of the firm, whereas the AIFM requirements focus on the funds managed. UCITS Remuneration Code firms are obliged to consider both. The instruments referred to in Remuneration Principles 12(f) and 5(e) are detailed below.
Remuneration Principle 10: Personal investment strategies SYSC 19A.3.30 / SYSC 19D.3.32 / SYSC 19C.3.30 A firm must ensure that its employees undertake not to use personal hedging strategies or remuneration- or liability- related contracts of insurance to undermine the risk alignment effects embedded in their remuneration arrangements. A firm must maintain effective arrangements designed to ensure that employees comply with their undertaking.			AIFM Remuneration Principle 8: Personal investment strategies SYSC 19B.1.23 An AIFM must ensure that its employees undertake not to use personal hedging strategies or remuneration- and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements.	UCITS Remuneration Principle 8: Personal investment strategies SYSC 19E.2.26 A management company must ensure that its employees undertake not to use any of the following to undermine the risk alignment effects embedded in their remuneration arrangements: personal hedging strategies, remuneration-related insurance, or liability-related insurance.	The IFPRU, Dual-Regulated firms and BIPRU Remuneration Codes place an obligation on the firm to maintain effective arrangements to ensure employees comply with undertakings given.
Remuneration Principle 11: Non-compliance with the Remuneration Code SYSC 19A.3.32 / SYSC 19D.3.34 A firm must ensure that variable remuneration is not paid through vehicles or methods that facilitate non-compliance with the Remuneration Code [the EU CRR or the CRD]*. <i>* Words in square brackets not applicable in the IFPRU Remuneration Code.</i>	Remuneration Principle 11: Avoidance of the Remuneration Code SYSC 19C.3.32 A firm must ensure that variable remuneration is not paid through vehicles or methods that facilitate the avoidance of the BIPRU Remuneration Code.		AIFM/UCITS Remuneration Principle 9: Avoidance of the Remuneration Code SYSC 19B.1.24 / SYSC 19E.2.27 An AIFM/management company must ensure that variable remuneration is not paid through vehicles or methods that facilitate the avoidance of the requirements of the AIFM/UCITS Remuneration Code.		The IFPRU and Dual-Regulated firms Remuneration Codes prohibit "non-compliance" whereas the BIPRU, AIFM and UCITS Remuneration Codes prohibit "avoidance". The difference between "avoiding" and "non-compliance" is slight – arguably non-compliance is more difficult to prove. Dual-Regulated firms must also ensure the EU CRR and CRD are complied with.
Remuneration Principle 12: Remuneration structures – introduction SYSC 19A.3.34 / SYSC D.3.35 / SYSC 19C.3.34 <i>Note guidance:</i> Taking account of the remuneration principles proportionality rule, the appropriate regulator does not generally consider it necessary for a firm to apply the rules referred to below where, in relation to an individual, his variable remuneration is no more than 33% of total remuneration and his total remuneration is no more than £500,000. The rules referred to above are those relating to: guaranteed variable remuneration (Remuneration Principle 12(c)), retained shares or other instruments (Remuneration Principle 12(f)), deferral (Remuneration Principle 12(g)) and performance adjustment (Remuneration Principle 12(h)).			No equivalent provision.	No equivalent provision.	The instruments referred to in Remuneration Principles 12(c), (f), (g) and (h) are detailed below.

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
<p>Remuneration Principle 12(a): Remuneration structures – general requirement SYSC 19A.3.35 / SYSC 19D.3.36 / SYSC 19B.3.35</p> <p>A firm must ensure that the structure of an employee's remuneration is consistent with and promotes effective risk management.</p> <p>SYSC 19A.3.35A-35B / SYSC 19D.3.37-38</p> <p>A firm must ensure that the remuneration policy makes a clear distinction between criteria for setting basic fixed remuneration that primarily reflects an employee's professional experience and organisational responsibility as set out in the employee's job description and terms of employment, and setting variable remuneration that reflects performance in excess of that required to fulfil the employee's job description and terms of employment and that is subject to performance adjustment in accordance with the Remuneration Code.</p> <p>[A firm must not award variable remuneration to a non-executive director acting as such.]*</p> <p><i>* Words in square brackets not applicable in the IFPRU Remuneration Code.</i></p>	<p>No equivalent provision.</p>	<p>AIFM Remuneration Principle 1: Risk management SYSC 19B.1.5</p> <p>An AIFM must ensure that its remuneration policy is consistent with, and promotes, sound and effective risk management and does not encourage risk-taking which is inconsistent with the risk profiles of the instrument constituting the fund of the AIFs it manages.</p>	<p>UCITS Remuneration Principle 1: Risk management SYSC 19E.2.5</p> <p>A management company must ensure that its remuneration policy is consistent with, and promotes sound and effective risk management and does not encourage risk taking which is inconsistent with the risk profiles or the instrument constituting the fund of the UCITS it manages.</p>	<p>The IFPRU and Dual-Regulated firms Remuneration Codes add details of how remuneration is to be split between fixed remuneration and variable remuneration. There is no direct equivalent provision in the AIFM and UCITS Remuneration Codes but a similar requirement can be found in Remuneration Principle 1.</p> <p>Only the Dual-Regulated firms Remuneration Code specifies that non-executive directors should not be awarded variable remuneration.</p>	
<p>Remuneration Principle 12(b): Remuneration structures – assessment of performance SYSC 19A.3.36-38 / SYSC 19D.3.39-43 / SYSC 19C.3.36-38</p> <p>A firm must ensure that where remuneration is performance-related: the total amount of remuneration is based on a combination of the assessment of the performance of the individual, the business unit concerned and the overall results of the firm. When assessing individual performance, financial as well as non-financial criteria are taken into account.</p> <p>A firm must ensure that the assessment of performance is set in a multi-year framework in order to ensure that the assessment process is based on longer-term performance and that the actual payment of performance-based components of remuneration is spread over a period which takes account of the underlying business cycle of the firm and its business risks.</p> <p>[A firm must clearly explain the performance assessment process above to relevant employees.]*</p> <p><i>* Words in square brackets not applicable in the IFPRU or BIPRU Remuneration Codes.</i></p>		<p>AIFM/UCITS Remuneration Principle 5(a): Remuneration structures - assessment of performance SYSC 19B.1.12 / SYSC 19E.2.12</p> <p>An AIFM/management company must ensure that, where remuneration is performance related, the total amount of remuneration is based on a combination of the assessment of the performance of the individual, of the business unit or AIF/UCITS concerned and of the overall results of the AIFM/management company. When assessing individual performance, financial and non-financial criteria are taken into account.</p>		<p>Performance assessment under AIFMD must be done in the multi-framework appropriate to the AIF's life cycle and performance payments made over a period that takes account of the AIF's redemption policy, whereas for UCITS this must be done in the multi-framework appropriate to the holding period recommended to the investors.</p>	
		<p>SYSC 19B.1.13</p> <p>An AIFM must ensure that the assessment of performance is set in a multi-year framework appropriate to the life-cycle of the AIFs managed by the AIFM to ensure that the assessment process is based on longer term performance and the actual payment of performance-based components of remuneration is spread over a period which takes account of the redemption policy of the AIFs it manages and their investment risks.</p>	<p>SYSC 19E.2.13</p> <p>A management company must ensure that the assessment of performance is set in a multi-year framework appropriate to any holding period recommended to the investors of the UCITS to ensure that the assessment process is based on the long-term performance of the UCITS and its investment risks and actual payment of the performance-based components of remuneration is spread over the same period.</p>	<p>Only Dual-Regulated firms are required to explain the performance assessment process to their employees.</p>	
<p>Remuneration Principle 12(c): Remuneration structures – guaranteed variable remuneration SYSC 19A.3.40-40A / SYSC 19D.3.44-45</p> <p>A firm must ensure that guaranteed variable remuneration is not part of prospective remuneration plans. A firm must not award, pay or provide guaranteed variable remuneration unless it is exceptional, it occurs in the context of hiring new Remuneration Code staff, the firm has a sound and strong capital base, and it is limited to the first year of service.</p> <p>A firm must ensure that remuneration packages relating to compensation for, or buy out from, an employee's contracts in previous employment align with the long-term interests of the firm and are subject to appropriate retention, deferral and performance and clawback arrangements.</p>	<p>Remuneration Principle 12(c): Remuneration structures – guaranteed variable remuneration SYSC 19C.3.40</p> <p>A firm must not award, pay or provide guaranteed variable remuneration unless it is exceptional, occurs in the context of hiring new BIPRU Remuneration Code staff, and is limited to the first year of service.</p>	<p>AIFM/UCITS Remuneration Principle 5(b): Remuneration structures – guaranteed variable remuneration SYSC 19B.1.14 / SYSC 19E.2.14</p> <p>An AIFM/management company must not award, pay or provide guaranteed variable remuneration unless it is exceptional, occurs only in the context of hiring new staff, and is limited to the first year of service/engagement.</p>		<p>Only the IFPRU and Dual-Regulated firms Remuneration Codes refer to an additional requirement on firms to have a sound and strong capital base and to aligning compensation or buy out (of an employee's previous contract) with the firm's long term interests. They are also the only codes to require retention, deferral and clawback arrangements in relation to such buy-outs.</p>	

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
<p>Remuneration Principle 12(d): Remuneration structures – ratios between fixed and variable component <i>SYSC 19A.3.44 / SYSC 19D.3.48 / SYSC 19C.3.44</i></p> <p>A firm must set appropriate ratios between the fixed and variable components of total remuneration and ensure that fixed and variable components of total remuneration are appropriately balanced and that the fixed component represents a sufficiently high proportion of the total remuneration to allow the operation of a fully flexible policy on variable remuneration components, including the possibility to pay no variable remuneration component.</p> <p><i>SYSC 19A.3.44-44E / SYSC 19D.3.48-53</i></p> <p>Subject to the below, the level of the variable component of total remuneration must not exceed 100% of the fixed component of total remuneration.</p> <p>A firm may set a higher maximum level of the ratio between the fixed and variable components of total remuneration provided the overall level of the variable component does not exceed 200% of the fixed component of the total remuneration for each Remuneration Code staff and is approved by the shareholders or owners or members of the firm in accordance with the following provision [which sets out a procedure for approval and notification of such approval not reproduced here].</p> <p>A firm may apply a discount rate to a maximum of 25% of an employee's total variable remuneration provided it is paid in instruments that are deferred for a period of not less than five years. In doing so, a firm must apply the EBA Guidelines on the applicable notional discount rate for variable remuneration published on 27 March 2014.</p>		<p>No equivalent provision.</p>	<p>AIFM/UCITS Remuneration Principle 5(c): Remuneration structures - fixed and variable components of total remuneration <i>SYSC 19B.1.15 / SYSC 19E.2.15</i></p> <p>An AIFM/management company must ensure that fixed and variable components of total remuneration are appropriately balanced and that the fixed component represents a sufficiently high proportion of the total remuneration to allow the operation of a fully flexible policy on variable remuneration components, including the possibility to pay no variable remuneration component.</p>		<p>The IFPRU and Dual-Regulated firms Remuneration Codes add that the ratio between fixed and variable remuneration must be set at 1:1. The ratio can be set at 1:2 where shareholder approval permits it</p> <p>The IFPRU and Dual-Regulated firms Remuneration Codes permit the use of a discount rate, which is not referred to in the BIPRU Remuneration Code.</p>
<p>Remuneration Principle 12(e): Remuneration Structures – payments related to early termination <i>SYSC 19A.3.45 / SYSC 19D.3.54</i></p> <p>A firm must ensure that payments relating to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure or misconduct.</p>		<p>Remuneration Principle 12(e): Remuneration Structures – payments related to early termination <i>SYSC 19C.3.45</i></p> <p>A firm must ensure that payments related to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure.</p>	<p>AIFM/UCITS Remuneration Principle 5(d): Remuneration structures – payments related to early termination <i>SYSC 19B.1.16 / SYSC 19E.2.16</i></p> <p>An AIFM/management company must ensure that payments related to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure.</p>		<p>The IFPRU and Dual-Regulated firms Remuneration Codes alone contain the additional requirement to avoid rewarding misconduct.</p>
<p>Remuneration Principle 12(f): Remuneration Structures – retained shares or other instruments <i>SYSC 19A.3.47</i></p> <p>A firm must ensure that a substantial portion, which is at least 50%, of any variable remuneration consists of an appropriate balance of shares or equivalent ownership interests, subject to the legal structure of the firm concerned, or share-linked instruments or equivalent non-cash instruments in the case of a non-listed firm, and, where possible, other instruments which are eligible as Additional Tier 1 instruments or are eligible as Tier 2 instruments or other instruments that can be fully converted to Common Equity Tier 1 instruments or written down, that in each case adequately reflect the credit quality of the firm as a going concern and are appropriate for use as variable remuneration.</p>	<p>Remuneration Principle 12(f): Remuneration Structures – retained shares or other instruments <i>SYSC 19D.3.56</i></p> <p>A firm must ensure that a substantial portion, which is at least 50%, of any variable remuneration consists of an appropriate balance of shares or equivalent ownership interests, subject to the legal structure of the firm concerned, or share-linked instruments or equivalent non-cash instruments in the case of a non-listed firm, and, where possible, other instruments that in each case adequately reflect the credit quality of the firm as a going concern and are appropriate for use as variable remuneration, such as those which are eligible as additional tier 1 instruments or tier 2 instruments, or those that can be fully converted to common equity tier 1 instruments or written down.</p>	<p>Remuneration Principle 12(f): Remuneration Structures – retained shares or other instruments <i>SYSC 19C.3.47</i></p> <p>A firm must ensure that a substantial portion, at least 50%, of any variable remuneration consists of an appropriate balance of shares or equivalent ownership interests, subject to the legal structure of the firm concerned, or share-linked instruments or equivalent non-cash instruments for a non-listed firm, and, where appropriate, capital instruments which are eligible for inclusion at stage B1 of the calculation in the capital resources table, where applicable, adequately reflect the credit quality of the firm as a going concern.</p>	<p>AIFM Remuneration Principle 5(e): Remuneration structures – retained units, shares or other instruments <i>SYSC 19B.1.17</i></p> <p>Subject to the legal structure of the AIF and the instrument constituting the fund, an AIFM must ensure that a substantial portion, and in any event at least 50% of any variable remuneration, consists of units or shares of the AIF concerned, or equivalent ownership interests, or share-linked instruments or equivalent non-cash instruments. However, if the management of AIFs accounts for less than 50% of the total portfolio managed by the AIFM, the minimum of 50% does not apply.</p> <p>The instruments above must be subject to an appropriate retention policy designed to align incentives with the long-term interests of the AIFM and the AIFs it manages and the investors of such AIFs.</p>	<p>UCITS Remuneration Principle 5(e): Remuneration structures – retained units, shares or other instruments <i>SYSC 19E.2.18</i></p> <p>Subject to the legal structure of the UCITS and the instrument constituting the fund, a management company must ensure that a substantial portion, and in any event at least 50%, of any variable remuneration component consists of units or shares of the UCITS concerned, equivalent ownership interests in the UCITS concerned, share-linked instruments relating to the UCITS concerned, or equivalent non-cash instruments relating to the UCITS concerned with incentives that are equally as effective as any of the instruments referred to above. However, if the management of UCITS accounts for less than 50% of the total portfolio managed by the management company, the minimum of 50% does not</p>	<p>There are differences between the Codes relating to which instruments are eligible for the purposes of calculating variable remuneration.</p> <p>IFPRU and Dual-Regulated Remuneration Code firms may include Additional Tier 1 instruments, Tier 2 instruments or other instruments that can be fully converted to Common Equity Tier 1 instruments or written down.</p> <p>The requirements for BIPRU Remuneration Code firms are more tailored and differ according to the type of firm in question, in accordance with the capital resources table in the FCA Handbook.</p> <p>AIFM and UCITS Remuneration Code firms may include units/shares in the fund itself or equivalent ownership interests. For these firms the 50% variable remuneration minimum will not</p>

IFPRU Remuneration Code Provision	Dual-regulated firms Remuneration Code Provision	BIPRU Remuneration Code Provision	AIFMD Remuneration Code Provision	UCITS Remuneration Code Provision	Comments on Differences
<p>The instruments above must be subject to an appropriate retention policy designed to align incentives with the longer-term interests of the firm.</p> <p>This rule applies to both the portion of the variable remuneration component deferred in accordance with Remuneration Principle 12(g) and the portion not deferred.</p>			<p>This rule applies to the portion of the variable remuneration component deferred in line with Remuneration Principle 5(f) and the portion not deferred.</p>	<p>apply.</p> <p>The instruments above must be subject to an appropriate retention policy designed to align incentives for the UCITS Remuneration Code staff with the long-term interests of the management company, the UCITS it manages, and the investors of such UCITS.</p> <p>This rule applies to the portion of the variable remuneration component deferred in line with Remuneration Principle 5(f) and the portion not deferred.</p>	<p>apply if the AIF/UCITS accounts for less than 50% of the total portfolio under management.</p>
<p>Remuneration Principle 12(g): Remuneration Structures – deferral SYSC 19A.3.49</p> <p>A firm must not award, pay or provide a variable remuneration component unless a substantial portion of it, which is at least 40%, is deferred over a period which is not less than three to five years.</p> <p>Remuneration must vest no faster than on a pro-rata basis.</p> <p>In the case of a variable remuneration component of a particularly high amount, or payable to an executive director of a firm that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities, at least 60% of the amount must be deferred.</p> <p>The length of the deferral period must be established in accordance with the business cycle, the nature of the business, its risks and the activities of the employee in question.</p> <p>£500,000 is a particularly high amount for the purpose the above, without prejudice to the possibility of lower sums being considered a particularly high amount.</p>	<p>Remuneration Principle 12(g): Remuneration Structures – deferral SYSC 19D.3.59</p> <p>A firm must not award, pay or provide a variable remuneration component unless a substantial portion of it, which is at least 40%, is deferred over a period which is not less than three to five years, with no vesting taking place until one year after the award, and vesting no faster than on a pro-rata basis (for staff who do not perform a PRA-designated senior management function); or seven years, with no vesting taking place until three years after the award, and vesting no faster than on a pro-rata basis (for staff who perform a PRA-designated senior management function).</p> <p>In the case of a variable remuneration component of £500,000 or more, or payable to a director of a firm that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities, at least 60% of the amount must be deferred on the basis set out above.</p> <p>The length of the deferral period must be established in accordance with the business cycle, the nature of the business, its risks and the activities of the employee in question.</p>	<p>Remuneration Principle 12(g): Remuneration Structures – deferral SYSC 19C.3.49</p> <p>A firm must not award, pay or provide a variable remuneration component unless a substantial portion of it, which is at least 40%, is deferred over a period which is not less than three to five years.</p> <p>Remuneration must vest no faster than on a pro-rata basis.</p> <p>In the case of a variable remuneration component of a particularly high amount, or payable to an executive director of a firm that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities, at least 60% of the amount must be deferred.</p> <p>The length of the deferral period must be established in accordance with the business cycle, the nature of the business, its risks and the activities of the employee in question.</p> <p>£500,000 is a particularly high amount for the purpose the above, without prejudice to the possibility of lower sums being considered a particularly high amount.</p>	<p>AIFM Remuneration Principle 5(f): Remuneration structures – deferral SYSC 19B.1.18-18A</p> <p>An AIFM must not award, pay or provide a variable remuneration component unless a substantial portion, and in any event at least 40%, of the variable remuneration component, is deferred over a period which is appropriate in view of the life cycle and redemption policy of the AIF concerned and is correctly aligned with the nature of the risks of the AIF in question.</p> <p>The period referred to must be at least three to five years, unless the life cycle of the AIF concerned is shorter.</p> <p>Remuneration payable must vest no faster than on a pro-rata basis.</p> <p>In the case of a variable remuneration component of a particularly high amount, at least 60% of the amount must be deferred.</p> <p><i>Note guidance:</i></p> <p>£500,000 is a particularly high amount for the purpose the above, without prejudice to the possibility of lower sums being considered a particularly high amount.</p>	<p>UCITS Remuneration Principle 5(f): Remuneration structures – deferral SYSC 19E.2.20-21</p> <p>A management company must not award, pay or provide a variable remuneration component unless a substantial portion, and in any event at least 40%, of the variable remuneration component, is deferred over a period which is appropriate in view of any holding period recommended to the investors of the UCITS concerned and correctly aligned with the nature of the risks of the UCITS in question.</p> <p>The period referred to must be at least three years.</p> <p>Remuneration payable must vest no faster than on a pro-rata basis.</p> <p>For a variable remuneration component of a particularly high amount, at least 60% of the amount must be deferred.</p> <p><i>Note guidance:</i></p> <p>£500,000 should be considered a particularly high amount for the purpose of the above.</p> <p>Management companies should also consider whether lesser amounts should be considered to be 'particularly high'.</p>	<p>The 60% deferral rule in the IFPRU and BIPRU Remuneration Codes does not apply to non-executive directors of significant firms.</p> <p>The 40% deferral period for Dual-Regulated firms is higher (seven years, vesting after three years) for firms that perform a PRA-designated senior management function) than those that do not (three-five years, vesting after one year).</p> <p>Deferral of variable remuneration under AIFMD must be over a period appropriate to the AIFs' life cycle and redemption policy, whereas for UCITS the period must be appropriate to the holding period recommended to investors.</p> <p>The deferral period must be at least three years for UCITS, but AIFs have a longer period of three-five years (unless the AIF's life cycle is shorter).</p>

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<p>Remuneration Principle 12(h): Remuneration Structures – performance adjustment SYSC 19A.3.51 / SYSC 19D.3.61 / SYSC 19C.3.51</p> <p>A firm must ensure that any variable remuneration, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the firm as a whole, and justified on the basis of the performance of the firm, the business unit and the individual concerned.</p>			<p>AIFM Remuneration Principle 5(g): Remuneration structures – performance adjustment SYSC 19B.1.19-20</p> <p>An AIFM must ensure that any variable remuneration, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the AIFM as a whole and justified according to the performance of the AIF, the business unit and the individual concerned.</p>	<p>UCITS Remuneration Principle 5(g): Remuneration structures – performance adjustment SYSC 19E.2.22</p> <p>A management company must ensure that any variable remuneration, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the management company as a whole, and justified according to the performance of the UCITS, the business unit, and the individual concerned.</p>	<p>Only the BIPRU Remuneration Code does not refer to provisions in place for malus or clawback arrangements.</p>
<p>SYSC 19A.3.51-51A / SYSC 19D.3.62</p> <p>A firm must ensure that any variable remuneration is subject to clawback, such that it is not awarded save where an amount corresponding to it can be recovered from the individual by the firm if the recovery is justified on the basis of the circumstances described below, and that variable remuneration is subject to clawback for a period of at least seven years from the date on which it is awarded.</p> <p>A firm must set specific criteria for the application of malus and clawback, and ensure that the criteria for the application of malus and clawback in particular cover situations where the employee participated in or was responsible for conduct which resulted in significant losses to the firm, or failed to meet appropriate standards of fitness and propriety.</p> <p>No equivalent provision.</p>	<p>No equivalent provision.</p> <p>SYSC 19D.3.61(4)</p> <p>A firm must ensure that for staff who perform a PRA-designated senior management function, it can, by notice to the employee to be given no later than seven years after the variable remuneration was awarded, extend the period during which variable remuneration is subject to clawback to at least ten years from the date on which the variable remuneration is awarded, where the firm has commenced an investigation into facts or events which it considers could potentially lead to the application of clawback were it not for the expiry of the clawback period, or where the firm has been notified by a regulatory authority (including an overseas regulatory authority) that an investigation has been commenced into facts or events which the firm considers could potentially lead to the application of clawback by the firm were it not for the expiry of the clawback period.</p> <p>A firm must ensure it considers to us this power an ongoing basis.</p>		<p><i>Note guidance:</i></p> <p>The total variable remuneration should generally be considerably contracted where subdued or negative financial performance of the AIFM or of the AIF concerned occurs, taking into account both current compensation and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.</p>	<p><i>Note guidance:</i></p> <p>The total variable remuneration should generally be considerably contracted where subdued or negative financial performance of the management company or of the UCITS concerned occurs. Management companies should take into account both current compensation and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.</p>	<p>Only the Dual-Regulated firms Remuneration Code contains the power to extend the clawback period from seven to ten years.</p> <p>The IFPRU and Dual-Regulated firms Remuneration Codes detail how provisions of agreements that contravene specified provisions of the Code related to clawback can be rendered void.</p>

Contacts



Nicholas Thompsell

Partner - London

E: nicholas.thompsell@fieldfisher.com

T: +44 (0)20 7861 4292



Kirstene Baillie

Partner - London

E: Kirstene.Baillie@fieldfisher.com

T: +44 (0)20 7861 4289



John Dooley

Associate - London

E: John.Dooley@fieldfisher.com

T: +44 (0)20 7861 4086

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