Dear Andrew

Deferral of variable remuneration

I refer to the recent discussion in the House of Lords with regards to remuneration under the proposed Amendment 182 to the Financial Services (Banking Reform) Bill and your follow-up request for a statement on the PRA’s proposed implementation of the Parliamentary Commission on Banking Standards (PCBS) recommendations on deferral of variable remuneration.

We are committed to improving the alignment of reward to the maturity of risk, and are confident of our ability to do so under our current regulatory powers and the relevant provisions in the Remuneration Code (Code).

We do not believe it necessary to place the Code or any provisions therein in statute as this would result in unduly rigid requirements which could undermine supervisory judgement.

Our approach

A desire to align risk, performance and reward underpins global, European and national initiatives on remuneration, including the Code. It will also drive our revision of the Code in 2014 to implement the remuneration recommendations in the PCBS report.

In addition to prescribing minimum, non-negotiable deferral periods for Code Staff, the Code already requires the length of the deferral period to be established “in accordance with the business cycle, the nature of the business, its risks and the activities of the employee in question”. The Code’s current requirements reflect the view, set out in EU legislation and guidelines, that “the actual deferral period should be further accommodated to the responsibilities and tasks performed by the staff and expected fluctuations in the economic activity of the institution, which in many cases will imply longer time horizons. At least for members of the management body in its management function (i.e. executive directors) the institution should consider longer deferral periods”.

Deferral periods in future

The PRA agrees with the PCBS’s conclusion that “for the most senior and highest rewarded, it is even more crucial that their remuneration reflects the higher degree of individual responsibility expected of them”.

We will therefore carefully consider the options available to strengthen the current approach to deferral of variable remuneration in our upcoming consultation and bring forward proposals to better align the maturity of risk and reward so as to ensure that the crystallisation of any risks taken in previous years has a measurable impact on the variable remuneration of the individuals responsible.

Our upcoming consultation on deferral will be linked to and influenced by the development of the Senior Persons Regime. The PRA is working with the FCA in developing these policies. In addition, the PRA will be consulting separately in the first half of 2014 on the use of clawback to recover vested variable remuneration. In conjunction with our recent Supervisory Statement setting out our
expectations of firms in the application of malus (the recovery of unvested variable remuneration), which clarified and underscored the contingent nature of deferred remuneration as recommended by the PCBS, mandating the use of clawback in appropriate circumstances will enhance incentives for prudent-risk taking. Promoting remuneration policies, procedures and practices that are consistent with and promote sound and effective risk management is the overarching objective of the PRA's approach to remuneration.

I hope the above clarifies our position and how we are planning to deliver the PCBS recommendations on deferral of variable remuneration.

Yours sincerely,

Andrew Bailey