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To: Banks, Securities Traders, Financial and Insurance Groups and
Conglomerates, and Insurers subject to FINMA Supervision

Reference: FINMA Newsletter 20 (2011)

Contact: Institutions are requested to contact their regular FINMA supervisory team

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FINMA Newsletter 20 (2011)

Remuneration Systems of Financial Institutions

Guidance for Institutions Subject to FINMA Circular 2010/01 on Disclosures under Principle 9 of the Circular

Guidance for these Institutions and their External Auditors regarding Report due to FINMA 30 April 2011

Ladies and Gentlemen:

Each institution subject to FINMA Circular 2010/1 Remuneration (the "Circular") by virtue of Margin No. 6 or 7 is required under Principle 9 to provide certain disclosures regarding remuneration in its annual report. Margin No. 75 of the Circular also requires each such institution to submit to FINMA by April 30, 2011 a report on its own assessment of its implementation of the Circular's principles and its compliance therewith. This report is to be certified by the institution's external auditor.

In the Appendix is guidance in respect of the above disclosures and report, including guidance for the external auditors. Institutions subject to the Circular by virtue of Margin No. 6 or 7 of the Circular are asked to review carefully the entire Appendix. Those institutions not directly subject to the Circular are reminded that pursuant to Margin No. 8 of the Circular it is recommended that they "take into account the principles of the Circular for their remuneration schemes as best practice guidelines".

Reference:

Swiss Financial Market Supervisory Authority FINMA
Banks, Insurances

Mark Branson

Dr. René Schnieper

Gabe Shawn Varges

Enclosure: Appendix:
Guidance for Institutions subject to the Circular under Margin No. 6 or 7
Guidance for the External Auditor

Archive

Reference:

APPENDIX

1 Guidance for Institutions subject to the Circular under Margin No. 6 or 7

1.1 Disclosures under Principle 9 of the Circular

Margin No. 62 of the Circular requires an institution to prepare a remuneration report as part of its annual report. FINMA strongly recommends institutions to use tables and other graphic means where appropriate to make the required disclosures as clear as possible, particularly in respect of the disclosures under Margin Nos. 64-67 and 69-70.

FINMA requests institutions to provide where available comparative information so as to clearly show changes over the previous year. For example, for the recommended tables or charts the data should be presented both for reporting years 2010 and 2009 in the institution's first disclosure, and correspondingly in subsequent years.

If for any matter a firm expects to make use of the comply-or-explain provision under Margin No. 73, FINMA expects the disclosure to have a reasoned explanation and an indication as to whether the indicated non-compliance will be corrected in respect of remuneration for the year 2011 and, if not, for the year 2012.

1.2 General Guidance in Respect of Reports due under Margin No. 75

Margin No. 75 specifies that each institution is "to assess its implementation of this Circular and compliance therewith" and report this to FINMA by April 30, 2011.

FINMA is principally interested in knowing if:

- I. The institution has, in the context of the provisions of the Circular and the interactions it may have had with FINMA bilaterally, undertaken a robust review of its remuneration system¹ as it existed prior to the issuance of the Circular.
- II. This review and the actions resulting from it have been led or supervised by the Board of Directors with appropriate involvement by the Risk Management function and other control functions.
- III. All steps necessary to address identified gaps and improvement needs of the institution's remuneration system in light of the Circular have been completed and implemented or, where this is not yet the case, a clear time table has been set for this by the Board of Directors.

¹ By remuneration system we mean the totality of the remuneration approach, policy, instruments, and practices at the institution.

Reference:

In addition, FINMA requests certain information with regard to levels of pay made in 2009 and 2010 in the form indicated under 1.4 below.

A. Guidance in respect of I and II above

In support of the answers to I and II above FINMA does not require extensive documentation but a brief summary (e.g. two to four pages) of the specific efforts the institution has undertaken from the date of FINMA's issuance of the Circular (October 21, 2009) to the date on which the institution submits its report to FINMA. This summary should include information about:

1. The nature of the review conducted of the existing remuneration system.²
2. Board of Director meetings, Remuneration Committee meetings, and other relevant board committees' meetings (e.g. Risk, Audit) at which the existing remuneration system was discussed with the aim of bringing it into compliance with the Circular.
3. The involvement on remuneration by (i) the Risk Management function, including in conducting risk analyses of the existing remuneration system and any proposed changes thereto and (ii) other control functions (e.g. Internal Audit, Compliance).
4. Such other relevant efforts the institution undertook to implement the principles of the Circular and comply therewith. If the institution has also had to consider the remuneration requirements of other jurisdictions, an indication should be provided of which jurisdictions these are and whether the institution has met, discussed, or exchanged correspondence between 2009 and 2011 with the authorities of these jurisdictions in reference to remuneration.

B. Guidance in respect of III above

In support of its answers to III above, the institution should provide FINMA (where possible, in table form) the following:

1. A brief description of the gaps and improvement needs that the institution identified through the review process as described under I and II above, including without limitation any relating to
 - (i) the governance and controls behind remuneration, including the existence of appropriate remuneration rules,
 - (ii) the incorporation of remuneration costs into capital and liquidity planning,
 - (iii) the reflection of cost of capital and risk in bonus pool funding and in the allocation therefrom to business units and to individual employees,
 - (iv) the alignment of performance evaluations made of employees to actual remuneration decisions made about those employees (including the Members of the Management Board or similar),
 - (v) the mix between fixed and variable remuneration and between cash and equity,

² If the review of the remuneration system was carried out in the form of a formal project, the institution should provide a description of the project goals and indicate who was project sponsor and project head (with titles). If it was not conducted as a formal project, the institution should provide a brief description of how the work was planned and carried out.

Reference:

- (vi) whether sufficient remuneration is deferred and deferred for a sufficiently long period of time, including whether there is any excessive proportion or amount of immediate non-deferred cash,
 - (vii) the performance indicators and metrics used for determining payouts under the various remuneration instruments,
 - (viii) the financial and conduct conditions (clawbacks) upon which the vesting of deferred amounts depend in order to promote risk alignment and risk symmetry,
 - (ix) sign-on payments, guaranteed bonuses, severance payments, special remuneration packages or arrangements,
 - (x) the identification of those managers and Key Risk Takers for which higher levels of remuneration governance and risk alignment should apply by virtue of the higher responsibility they have or higher risk they represent,
 - (xi) other relevant matters in respect of the Circular.
2. A brief description of the steps that the institution determined necessary to address the identified gaps and improvement needs³.
 3. A description of (a) which of these steps are now completed and fully implemented and (b) which have not yet been completed or fully implemented.
 4. A description of the time plan for completing and fully implementing remaining steps.
 5. An overall self-assessment by the institution using the scale below, indicating as follows: “With the steps our institution has completed and implemented as of the date hereof, we believe our institution’s remuneration system is consistent with the Circular:
 - (1) in few respects
 - (2) in some respects
 - (3) in many respects
 - (4) in many respects including most material respects
 - (5) in many respects including all material respects
 - (6) in all respects

1.3 Specific Considerations in Conducting the Self-Assessment and Submitting the Report to FINMA

In conducting its self-assessment each institution is asked to consider the items set out in Attachment I and Attachment II, as well as such other matters as the institution deems relevant for determining its level of implementation of the principles of the Circular and its compliance therewith.

The items in Attachment I and Attachment II are intended neither as a mandatory list of steps for all institutions to take nor as a safe haven for determining successful implementation of the principles of

³ If any gap or improvement need was identified but no step was determined necessary to address it, this should be also be included along with an explanation of why it was felt no action was needed.

Reference:

the Circular or compliance therewith. Many are illustrative in nature and reflect good practice from the marketplace.

The self-assessment and the content of the entire report to FINMA should be discussed and approved by the Board of Directors. The report to FINMA should be signed by the Chair of the Board of Directors or the Chair of the Remuneration Committee of the Board of Directors.

The report must be submitted to FINMA in electronic form (in both PDF and Word formats) by close of business April 30, 2011. It should be addressed to the institution's regular contact person from the FINMA supervisory team responsible for the institution.

1.4 Other Information to be Submitted with the Self-Assessment

FINMA requests institutions to also provide in their report to FINMA the following information:

A table or similar showing each of the variable remuneration instruments the institution used for remunerating employees for year 2010 and those expected to be used for 2011, in each case describing their different features so their similarities and differences can be easily perceived and compared. Among the features to display in this manner are:

- a) whether it is a cash or equity instrument,
- b) for which level or type of employees the instrument is available,
- c) how many employees receive or will receive compensation under this instrument,
- d) how much was paid in total under such instrument for 2010 and, if known, an estimate of how much is expected to be paid in 2011,
- e) the performance indicators or metrics upon which such instrument depends,
- f) the length and nature of deferral that applies to such instrument and the percentage that vests each year,
- g) the conditions and factors that apply to such instrument during the deferral which allow the institution to *upwardly* adjust the awarded remuneration prior to vesting (e.g. an upward post-award adjustment possibility, including any leverage) and how much of the non-vested amount can so be adjusted,
- h) the conditions and factors that apply to such instrument during the deferral which allow the institution to *downwardly* adjust or cancel the awarded remuneration prior to vesting (e.g. a downward post-award adjustment possibility allowing for a reduction or total forfeiture of the award, also known as a clawback) and how much of the non-vested amount can so be adjusted, and
- i) such other features as the institution considers relevant.

In addition, each institution is asked to include the following information on remuneration paid for years 2009 and 2010 for each of (a) the entire Management Board (or similar) and (b) the group of employees the institution has defined as Key Risk Takers ("KRT"). The information should be presented

Reference:

separately for each of the Management Board (as a whole) and the KRT group (as a whole, but excluding the Management Board). The information should include in respect of each year:

- a) percent of Total Remuneration that is Variable Remuneration⁴,
- b) percent of Total Remuneration that is cash (e.g. fixed salary plus the cash portion of Variable Remuneration, including immediate and deferred cash)
- c) percent of Variable Remuneration that is cash (immediate and deferred cash) and percent that is equity,
- d) percent of Variable Remuneration that is immediate cash (this includes any portion of deferred cash that vests in the same year it is awarded),
- e) percent of Variable Remuneration that is immediate equity (this includes any portion of deferred equity that vests in the same year it is awarded),
- f) percent of Variable Remuneration that is deferred (this includes only any cash or equity award that vests *after* the first year it is awarded, i.e. the difference between total Variable Remuneration minus the amounts in reference to d) and e) immediately above),
- g) percent of the deferred Variable Remuneration that is subject to a *downward* financial or conduct post-award adjustment possibility prior to vesting, e.g. a clawback,⁵
- h) such other information as the institution considers relevant.

Hypothetical example for the Group Management Board or similar of an institution. A similar separate presentation should be made for the institution's KRT group.

	2010	2009
a. % of Total Remuneration that is Variable Remuneration	70%	55%
b. % of Total Remuneration that is cash (fixed salary plus cash portion of Variable Remuneration)	58%	78%
c. % of Variable Remuneration that is cash (immediate and deferred cash) and % that is equity	40% cash, 60% equity	60% cash, 40% equity
d. % of Variable Remuneration that is immediate cash	30%	50%
e. % of Variable Remuneration that is immediate equity	0%	15%
f. % of Variable Remuneration that is deferred	70%	35%
g. % of deferred Variable Remuneration subject to a <i>downward</i> financial or conduct post-award adjustment possibility	100%	25%

⁴ Capitalized terms used herein are used as defined in FINMA Circular 2010/01.

⁵ To be included here are only those portion of the Variable Remuneration which the institution may reduce in part or in full prior to vesting due to the non-attainment of given financial goals or other expectations, such as relating to risk or compliance conduct by an unit or individual. If an instrument's value is tied to the price of the institution's shares or an index of shares, this will not be considered by itself by FINMA to be a sufficient downward post-award adjustment possibility and should not be reflected here.

Reference:

1.5 Information to provide to the External Auditor

Along with a copy of the report the institution is submitting to FINMA, each institution is requested to provide the external auditor with access to those documents which the institution found were material for its preparation of the report.

2 Guidance for the External Auditor

Margin No. 75 of the Circular requires the institution's report submitted to FINMA pursuant thereto to be "certified by the firm's external auditor". FINMA is not requesting an audit or review of the institution's remuneration system at this time but a statement of the view of the external auditor in respect of the matters set out in Attachment III hereto. This should be based on the external auditor's review of such documents as the institution has identified to the external auditor as having been material for the institution's preparation of its report to FINMA.

The external auditor should provide its certification to FINMA by May 30, 2011 in a letter substantially in the form of Attachment III hereto.

Reference:

ATTACHMENT I

This table is not for submission to FINMA but it is for consideration by the institution in conducting its own self-assessment.

Leadership and Supervision by the Board of Directors (the "Board")		
Points for consideration	Yes/No	Comments
1. The governance documents of the institution define the authority and responsibility of the entire Board for remuneration in a way that allows the Board to fulfill its obligations consistent with the Circular and, if not, such documents have been correspondingly amended.		
2. The charters or similar documents of the Remuneration Committee, Risk Committee and other relevant Board committees have been reviewed to determine if they require any amendment in light of the Circular and/or any decisions taken by the Board relating to the Circular, including the remuneration rules referred in Margin No. 18 of the Circular.		
3. The Board or the Remuneration Committee has ensured that responsibilities within the institution in respect of remuneration in general are properly defined and documented, are allocated in a manner that avoids conflicts of interest, and are subject to appropriate checks-and-balances and controls.		
4. The Board and the Remuneration and other relevant committees have met sufficiently and have otherwise devoted appropriate time for reviewing, determining and supervising necessary steps in respect of the institution's remuneration system in light of the Circular.		
5. To the extent that the Board has delegated responsibilities to the Remuneration Committee in respect of the Circular, the Remuneration Committee has kept the Board appropriately informed of its work relating to the Circular and of any risks identified with the institution's remuneration system and has referred to the Board those decisions requiring decision by the full Board.		

Reference:

<p>6. The Board or Remuneration Committee has ensured that the review of the institution's remuneration system and the implementation steps undertaken sufficiently cover all entities of the institution subject to the Circular and all relevant areas of business.</p>		
<p>7. The Board has ensured that the institution has defined Key Risk Takers in a way that does not omit anyone who may have a significant influence on the firm's risk profile or anyone whose total or variable remuneration is higher than that of any member of the Management Board or similar.</p>		
<p>8. The Board has reviewed and approved the remuneration rules required under Margin No. 18 of the Circular and has taken note of the expectations of FINMA in this regard and in regard to any exceptions, as set out in Attachment II hereto.</p>		
<p>9. The Board has ensured that the institution's work to implement the principles of the Circular and comply therewith has included reviewing and revising existing employment contracts where needed as well generally updating contractual practices and compensation plan descriptions to ensure consistency with the principles of the Circular and the institution's remuneration rules.</p>		
<p>10. The Board's approval of the remuneration of members of the institution's Management Board or similar is based on an appropriate review by the Board of the performance and accomplishments of each such member, and the Board has access to and receives from management such information as it deems necessary for this purpose.</p>		
<p>Control Functions and Controls</p>		
<p>1. The charters or similar documents of the Risk Management, Internal Audit and other relevant control functions are defined in a way as to allow these functions to carry out their respective responsibilities consistent with the Circular and the institution's remuneration rules and, if not, corresponding amendments have been made.</p>		
<p>2. The risk policy, code of conduct, compliance rules, employee handbook and/or other appropriate institution policies, directives, and manuals have been reviewed to determine if they require any amendment in light of the Circular and the institution's remuneration rules, and</p>		

Reference:

<p>any needed changes have been made. In the case of the risk policy, the risk of any part of the institution using inappropriate performance goals or incentives has been appropriately reflected.</p>		
<p>3. The Risk Management function has undertaken such steps as it, in its independent judgment, has deemed necessary to fulfill its responsibilities in a manner consistent with the Circular, including conducting risk analyses of existing and proposed remuneration practices and instruments and reporting thereon to the Board of Directors or a committee thereof, whether as part of the regular risk report or separately.</p>		
<p>4. The remuneration structure for the control functions, including any variable remuneration, has been reviewed and adjusted where necessary to ensure it does not create any conflicts of interest, compromise their independence, or incent any conduct inconsistent with their responsibilities.</p>		
<p>5. The Internal Audit function, under the supervision of the Board of Directors, has incorporated in its multi-year audit plan the carrying out of audits or reviews of the institution's remuneration system consistent with Margin No. 29 of the Circular, or the Board of Directors has determined alternative means for fulfilling the requirements of Margin No. 29.</p>		
<p>6. An appropriate system has been set up for the Risk Management function, Compliance function, and other relevant functions to feed information regarding the risk and compliance performance of employees (particularly senior management and Key Risk Takers) into the annual employee performance evaluation and remuneration decision making processes of the institution.</p>		
<p>7. A review has been done to ensure that remuneration decisions about individuals employees, including members of the Management Board or similar, are properly documented and are properly supported by the actual performance of these individuals as reflected in the annual or other periodic performance evaluation of such individuals.</p>		
<p>8. There has been an inventory and review of any special pay arrangements, custom packages, out-of-cycle payments, and the like (including any local remuneration plans) and these have been terminated or changed if not consistent</p>		

Reference:

with the remuneration rules or the Circular.		
9. There has been an inventory and assessment of the processes and controls that apply to the remuneration system on its own and in the context of the internal controls system of the institution and any necessary improvements have been undertaken.		
Nature, Structure, Level of and Conditions to the Remuneration		
1. The remuneration system has been reviewed to ensure sustainability and a long-term orientation and where needed adjustments have been made.		
2. As part of the above review, the institution's current and prospective a) profits, b) capital and liquidity position, c) risks, and d) other appropriate and relevant factors have been considered.		
3. Remuneration costs have been incorporated into mid- and long-term capital and liquidity planning.		
4. Past and prospective fixed and variable remuneration costs have been analysed and compared with the development of other major areas of the institution's costs.		
5. The remuneration system, as well as specific features of individual remuneration instruments, has been reviewed from the perspective of avoiding incentives that may lead to inappropriate risk taking, including any breach of internal risk limits, code of conduct prescriptions, or legal or regulatory obligations.		
6. The performance indicators and other metrics used for determining the funding of the remuneration pools, and the allocation therefrom to business units or divisions, have been reviewed to ensure they are linked to long-term performance, reflect risks and cost of capital, and allow for reduction or total elimination of the pool when there are poor results.		
7. In connection with the above, consideration has been given to the appropriate balance between business unit or division performance indicators versus group-wide indicators.		
8. The process for determining the nature, structure and level of remuneration for specific employees or category of employees has been reviewed to ensure that capital usage and the risks that such individuals take or are responsible for are appropriately taken into account.		

Reference:

<p>9. For the highest paid individuals, the maximum future upside that a particular pay package could represent (taking into account the financial metrics on which it depends and any leverage) has been tested from the perspective of affordability for the institution, proportionality, overall reasonableness, and the avoidance of reputational or other risks and, where needed, appropriate limits or other measures have been applied.</p>		
<p>10. The mix between fixed and variable remuneration and between cash and equity has been reviewed to ensure, among other things, appropriate risk alignment and long-term orientation.</p>		
<p>11. The percentage and length of deferral, as well as the vesting schedule, of variable remuneration have been reviewed, including to avoid any excessive proportion or amounts of immediate cash and to ensure that a sufficient amount of variable remuneration is at risk in the last year of vesting.</p>		
<p>12. Deferred remuneration has been structured and conditioned in a way that allows the institution to substantially reduce or eliminate an award not yet vested in the event of negative (a) financial or (b) conduct developments that make such award no longer appropriate.</p>		
<p>13. The financial indicators and the tables, grids and other tools used for determining specific payouts and vesting under the remuneration instruments have been reviewed to ensure these support a long-term orientation, include some peer or comparative performance criteria, do not depend only on share price fluctuations, avoid any inappropriate leverage, and balance any upside potential with a symmetrical downside potential.</p>		
<p>14. The conduct conditions that allow for a reduction or cancellation of unvested amounts have been defined so that they apply not just in the case of termination of the employee but also in situations where the risk, compliance and other relevant performance by the individual has been below expectations even if not sufficiently so to support termination of the individual for cause.</p>		

Reference:

15. There has been a review of the institution's policy and practices in respect of any bonus guarantees, formulaic bonus arrangements, severance pay, "golden parachutes" (including any post-employment consulting arrangements that are not at arm's-length), and these have been changed if not consistent with the remuneration rules or the Circular.		
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Reference:

ATTACHMENT II

1. Remuneration Rules

FINMA expects that the remuneration rules pursuant to Line 18 of the Circular, among other things, will

- a) make it easy for employees to understand the institution's remuneration strategy and how the remuneration plans work, including how specific instruments under these plans function and are funded;
- b) clearly set out for employees the financial and non-financial performance factors (at the institution, business unit and individual level) upon which these instruments, the awards thereunder (including the vesting of amounts deferred) depend; examples of non-financial performance include the extent of fulfilling the institution's expectations of employees relating to risk, compliance, and ethical decision-making;
- c) provide guidance to managers and others making performance and remuneration decisions regarding any employee on what their duties are in this respect and what they need to consider in making such decisions and in setting or approving performance goals for such employee; this would include ensuring that no such performance goals, nor the incentives behind them, incite the taking of any inappropriate risks;
- d) create generally a clear enough roadmap on how remuneration is determined at your institution such as to allow adequate verifiability.

FINMA expects that the above rules will be properly communicated internally and that appropriate training will be held as necessary. They should be reviewed by all relevant control functions, including Risk Management, and discussed and approved by the Board of Directors before implementation. It is FINMA's expectation that remuneration decisions will be made pursuant to the rules and will be properly documented.

2. Special Arrangements or Exceptions

FINMA expects that any special remuneration arrangements (whether for sign-on payments, out-of-pattern severance payments, post-termination consulting arrangements, or otherwise) or material exceptions in respect of any senior manager or Key Risk Taker will be reviewed and approved by the Remuneration Committee or the full Board of Directors and tested against the remuneration policy.

Reference:

ATTACHMENT III

[Date]

To the Swiss Financial Market Supervisory Authority FINMA

We serve as [the external auditors] to _____ (the "Institution").

We refer to the requirement under Margin No. 75 of FINMA Circular 2010/01 (the "Circular") for an external auditor certification of the report submitted by an institution to FINMA pursuant thereto (the "Report") and to the FINMA Communication 20 of January 19, 2011. In accordance with the latter, the external auditor may base its certification solely on a review of those documents which the institution has identified to it as having been material for its preparation of the Report (the "Documents").

The Institution is responsible for the statements made in the Report. Our responsibility is to review the Documents and assess whether there are indications that would suggest that there are any material inconsistencies as between the statements made in the Report and the Documents.

The Institution has identified to us the Documents listed in the Appendix hereto as having been material for its preparation of the Report.

Accordingly, and based solely on a review of the Documents without conducting any additional specific audit procedures, we certify that[, other as qualified below,] we have no indication that would suggest any material inconsistency as between the statements made in the Report and the Documents.

Please note that these limited procedures do not either constitute an audit or a review of the statements made in the Report pursuant to the Swiss Auditing Standards. Had we performed an audit or a review of the statements made in the Report in accordance with Swiss Auditing Standards, other matters might have come to our attention that would have been reported to you. Furthermore, with this certification we do not express an opinion as to whether the Institution's remuneration system is in line with the FINMA Circular 2010/1.

Our report is solely for your information and is not to be distributed to any other party other than the Institution and such other parties as may be necessary in the fulfilment of your supervisory responsibilities or as may be legally required.

Sincerely,

Name and Signature of Audit Firm