

# UK Investment Firms Prudential Regime - New Remuneration Requirements for UK Firms

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Investment firms in the United Kingdom (“**UK**”) that are authorised to carry on investment services or activities under the Markets in Financial Instruments Directive (“**MiFID**”) (EU/2014/65) (including alternative investment fund managers (“**AIFMs**”) with a MiFID “top-up” permission) will be subject to the new Investment Firms Prudential Regime (“**IFPR**”), which will become effective from 1 January 2022. This note provides an overview of the new remuneration requirements that are proposed under the IFPR.

## Background

While a key focus of the FCA’s IFPR proposals has been on the impact that the IFPR will have on UK investment firms’ capital requirements, there are also proposed new rules in relation to remuneration and associated guidance which are summarised in further detail below.

The FCA considers remuneration as the key driver of behaviour for all firms and individuals, noting that the objectives of its approach are:

- to promote effective risk management in the long-term interests of the firm and its customers;
- to ensure alignment between risk and individual reward;
- to support positive behaviours and healthy firm cultures; and

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- to discourage behaviours that can lead to misconduct and poor customer outcomes.

The proposed remuneration rules will be set out in a new single remuneration code, called the MIFIDPRU Remuneration Code (the “**Remuneration Code**”). The Remuneration Code will be contained in SYSC 19G of the FCA Handbook.

## Which firms are in-scope of the Remuneration Code?

### Classification into SNI firms, non-SNI firms and larger non-SNI firms

The IFPR regime distinguishes between “small and non-interconnected investment firms” (“**SNI**” firms) and non-SNI firms. SNI firms are defined in MIFIDPRU 1 and include, broadly, some investment firms that fall within certain size tests, which do not hold client money or assets and are not permitted to deal on their own account. All other firms will be classified as “non-SNI”.

A firm will be considered as a “larger non-SNI” if: (i) the value of its on and off-balance sheet assets over the preceding four-year period is a rolling average of more than £300 million; or (ii) the value of its on and off-balance sheet assets over the preceding four-year period is a rolling average of more than £100 million (but less than £300 million), and it has a trading book business of over £150 million, and/a derivatives business of over £100 million.

### Application to CPMI firms

Collective portfolio management investment firms (“**CPMI firms**”) are UK firms which are authorised as full-scope AIFMs or UCITs management firms and which also provide certain investment services that would usually require authorisation under MIFID. Currently, these firms comply with the AIFM Remuneration Code or the UCITs Remuneration Code (as the case may be) and are not subject to a separate code applicable to their “MiFID business”.

However, under the new IFPR regime, all CPMIs would need to apply the MIFIDPRU Remuneration Code to their MiFID “top-up” business. This means that CPMIs will now need to apply either of two different remuneration codes, as their non-MiFID business will continue to be subject to the AIFM or UCITS Remuneration Codes, and therefore bringing a wider pool of staff into scope of the remuneration rules.

## What are the key requirements of the Remuneration Code?

The FCA proposes to create three different levels of remuneration requirements depending on the classification and size of the firms: basic, standard and enhanced requirements.

### Basic remuneration requirements

The basic remuneration requirements will be principles-based and apply to all investment firms with respect to all staff. SNI firms will only have to comply with basic requirements.

It is expected that every firm should have proper remuneration documentation and governance in place that is proportionate to the firm’s structure and activities. As a result, all firms will be expected to have a remuneration policy that complies with the minimum requirements and covers all essential components of the proposed Remuneration Code, which includes the central policy objective to align

staff rewards with risk, as well as ensuring that the remuneration policy is gender-neutral.

### **Standard remuneration requirements**

Non-SNI firms will have to comply with the standard requirements in addition to the basic requirements. These firms will have to identify material risk takers (“**MRTs**”) amongst its staff on an annual basis and set an appropriate ratio between variable and fixed remuneration. Variable remuneration will have to include mechanisms to make risk adjustments (malus and clawback). The term “staff” will be interpreted broadly and will also include partners or members (in the case of partnership structures) and employees of other entities in the group, so it will be important to consider all types of roles that may have material impact on the firm or its assets. Firms should therefore take steps to determine which of their staff are identifiable as MRTs and review their existing remuneration terms and conditions.

The FCA does propose, however, to exempt certain MRTs who earn below certain thresholds from some remuneration requirements which are broadly aligned with current approach under the existing codes. The proposals exempt those MRTs which have variable remuneration of £167,000 or less and have variable remuneration which makes up one-third or less of their total remuneration.

### **Extended remuneration requirements**

Only large non-SNI firms (estimated to be 101 UK firms in total) will be subject to extended remuneration requirements, including requirements relating to deferral and payout of variable remuneration in instruments and the treatment of discretionary pension benefits. These firms would also need to establish a remuneration committee.

### **Timing and what’s next?**

The FCA’s remuneration proposals under the IFPR would enter into force from 1 January 2022. Firms will be expected to apply the new rules from the start of their next performance year beginning on or after this date.

Firms which are currently in scope of the IFPRU or BIPRU Remuneration Codes should continue to apply the requirements under these codes until 1 January 2022, or the beginning of their next performance year after that date, whichever is later. The FCA is also expected to consult on public disclosure of remuneration information in its next IFPR consultation, which is set to be published later this year.

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National Law Review, Volume XI, Number 190

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