

Employment in Financial Services

Contributing Editor

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02. Are there particular pre-screening measures that need to be taken when engaging a financial services employee? Does this vary depending on seniority or type of role? In particular, is there any form of regulator-specified reference that has to be provided by previous employers in the financial services industry?

India

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The pre-screening measures, when employing a financial service employee, are carried out in compliance with the frameworks laid down by the respective industry regulators. For instance, the Reserve Bank of India (RBI), the central banking sector regulator in India, periodically issues certain guidelines for banking and non-banking employers to conduct mandatory employee background checks. These regulators also recognise certain “Self-Regulatory Organisations” (SROs), who then play the primary role in conducting grassroots verifications. SROs conduct character and antecedent verification of employees registered with them as per the standards set by the regulator. Strict police verification of at least the last two addresses is usually mandated and verifications are periodically updated and shared on a common database at an industry level. For instance, the Finance Industry Development Council is an SRO of Non-Banking Finance Companies (NBFCs) and is registered with the RBI.

A financial services employer should be sensitive to the data being used for pre-screening measures as India protects individual privacy. Hence, both the employer and the service provider engaged by the employer should obtain prior consent from the prospective employee before pre-screening. If the pre-screening measures include the collection of “sensitive personal data information^[1]”, then an employer must seek the individual’s consent, which would also help mitigate risks for any claims concerning the invasion of an employee’s privacy. Employers should ideally ensure that pre-screening is complete before the employee is hired. A comprehensive pre-screening will include verification of educational qualifications, checks with past employers, verification of residential addresses, police records, and passport status. Usually, with seniority of the role, checks with past employers happen more rigorously, while for entry-level employees, checks with academic institutions about educational qualifications may be done more rigorously. Similar standards must be met by contract employees empanelled by the service providers.

There is no regulator-specified reference that must be provided by previous employers in the financial services industry. However, in practice, most public sector banks (eg, Bank of India) and many central public sector undertakings in financial services (eg, Life Insurance Corporation of India (LIC)), as per their selection or onboarding protocols, require at least two "Character Certificates", one of which should be from the head of the educational institution last attended or the present employer and the other should be from gazetted officers^[2] or bank officers, without any familial ties to the employee.

^[1] Information Technology Act, 2000 & Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules 2011.

^[2] A 'gazetted officer' is a high rank government official working as an officer for the government of India or any state government whose name and credentials are published in the Gazette of India.

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Ireland

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RFSPs must satisfy themselves that all CF and PCF candidates or employees comply with the F&P Standards. Pre-employment due diligence must be performed, including asking the candidate to certify they will comply with the F&P Standards and notify the RFSP immediately of any change in circumstance that may mean they no longer comply. Employers must continue to ensure that in scope employees comply with the F&P Standards and must complete an annual declaration to this effect. This means that due diligence must continue throughout the employment relationship and not just at the recruitment stage.

Candidates for PCF roles must complete an online individual questionnaire, which is submitted to the CBI in advance of appointment to the role through the Central Bank portal. The CBI must grant its approval for the PCF appointment before a candidate can take up the role. Any PCF offer of employment must be conditional on that approval being obtained. The CBI may request applicants attend an interview as part of the approval process.

Employers should take all reasonable steps to secure references from previous employers in order to due diligence the candidate's compliance with the F&P Standards and their suitability for the role. However, an employer is not obliged to issue a reference in respect of a former employee which means that a prospective employer may not be able to secure a reference from a previous employer. The CBI does not oblige employers to either issue or obtain a reference as part of screening checks, however employers must make good efforts to do so.

There are material obstacles from a data privacy and practical perspective to employers conducting criminal background checks in relation to prospective employees. Data relating to criminal convictions is special category data under the GDPR. Employers would need to satisfy both Article 6 and Article 9 requirements under the GDPR to justify the processing of this data. In terms of Article 9, this means employers would need to show reasons of substantial public interest or that they are carrying out their legal obligations in processing the data. In terms of Article 6 the employer will need to show that the processing is necessary to comply with a legal obligation to which the employer is subject or the processing is necessary for the employer's legitimate interests for example to ensure the suitability and honesty of its employees and to protect its reputation. Employers are also prevented from asking candidates about "spent convictions" which are usually minor criminal offences dating back over seven years.

Pre-employment medical checks must also have a clear legal basis justifying the processing of an employee's medical and health information.

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Under Swiss civil law, there is no requirement to apply pre-screening measures. However, while not a statutory requirement under Swiss financial market laws per se, companies subject to these laws apply pre-screening measures to ensure that a prospective financial services employee meets the requirements set forth by these laws. In particular, regulated companies such as banks, securities firms, insurance companies, fund management companies, managers of collective investment schemes and asset managers are required to obtain authorisation from the Swiss Financial Market Supervisory Authority (FINMA) relating to strategic and executive management and each change thereto.

As a general rule, the higher the responsibility or position of a person, the more requirements financial services employees may need to fulfil. Persons holding executive or overall management functions (eg, a member of the board or members of the senior management) are required to fulfil certain requirements set forth by the applicable Swiss financial market regulations. Such requirements may include providing current CVs showing relevant work experience and education as well as excerpts from the debt and criminal register. It may also include providing various declarations (eg, concerning pending and concluded proceedings, qualified participations and other mandates). Furthermore, financial services employees holding certain control functions (eg, compliance officer, risk officer and their deputies) may also be required to prove that they are suitable for the position by providing, for example, a current CV showing relevant work experience and education.

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07. Are there any specific rules relating to compensation payable to financial services employees in your jurisdiction, including, for example, limits on variable compensation, or provisions for deferral, malus and/or clawback of monies paid to employees?

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There are certain rules relating to compensation payable to financial services employees, such as those in the banking, mutual fund or asset management, and insurance industries.

The central bank of India, the RBI, deals with the compensation policy for all private-sector banks and foreign banks operating in India by requiring them to formulate their own compensation policy and annually reviewing it. Banks are not allowed to employ or continue the employment of any person whose remuneration is excessive in the RBI's opinion. For instance, the RBI lays down guidelines on the compensation of "Whole Time Directors ("WTD") / Chief Executive Officers / Material Risk Takers and Control Function Staff"[\[1\]](#), elaborate guidelines encompassing the governance of compensation and its alignment with prudent risk-taking, policies for risk control and compliance staff, the identification of "material risk takers", and disclosure and engagement by stakeholders. It even envisages deferred payments being subjected to malus or clawback arrangements if there was negative performance. For variable pay, it mandates banks to incorporate malus or clawback mechanisms and suggests they specify

periods of malus or clawback application to cover at least deferral and retention periods.[2] It is pertinent to highlight that private sector and foreign banks in India must obtain regulatory approval[3] for the grant of remuneration to WTDs or CEOs.

The RBI also prescribes guidelines around compensation for key managerial personnel (KMP) and senior management in non-banking financial companies (NBFCs)[4]:

- NBFCs are mandated to form “Nomination and Remuneration Committees” (NRCs) as per Section 178 of the Companies Act, 2013, which will then be entrusted with framing, reviewing and implementing the compensation policy to be approved by the board of the company.
- The compensation must align with the risk related to the decision-making process. The compensation package can comprise both fixed and variable pay and may also be a mix of cash, equity or other forms, in line with projected risk factors.
- A bonus has no bearing on the performance of the individual. The bonus is guaranteed based on the fulfilment of certain criteria as may be specified in the compensation policy. A guaranteed bonus should neither be considered part of fixed pay nor variable pay and the same is not payable to KMP and senior management. However, a guaranteed bonus can be paid to new employees as part of a sign-on bonus whereby potential employees can be incentivised to join NBFCs.
- "Deferred compensation may be subject to malus/clawback arrangements." The compensation policy concerning malus or clawback must mandatorily apply for the period equal to at least the deferred retention period.

Despite the aforementioned guidelines being applicable from 1 April 2023, NBFCs must immediately begin aligning their internal procedures to comply with the mandatory guidelines above to assist the transition. Existing remuneration policies being followed by the NBFCs should be reviewed to make the necessary changes to be compliant with the above-mentioned policies.

When it comes to regulations on an “employee stock option plan” (ESOP) for financial services employees, regulators may impose industry-specific guidelines. For instance, as per the SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021[5], the employee stock option scheme should be drafted in a manner that no such employee violates SEBI (Insider Trading) Regulations, 1992 and SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations, 1995. ESOPs issued to managerial staff and for non-cash consideration shall be treated as part of managerial remuneration. In another development, the RBI has directed that ESOPs should be at a fair value, shooting up costs and creating the cascading effect of replacing ESOPs with deferred bonus payments for senior managerial personnel.

[1] Guidelines on Compensation of Whole Time Directors/Chief Executive Officers/Material Risk Takers and Control Function staff, November 4, 2019, available at <<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/NOTI898C120D41D0E3465B8552E5467EDD7A56.PDF>>

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[3] Section 35B, Banking Regulation Act 1949.

[4] Guidelines on Compensation for Key Managerial Personnel (KMP) and Senior Management in non-banking financial companies (NBFCs), April 29, 2022, available at <<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/KMPNBFCs962EC76438C845A6846A5BD59BC7513D.PDF>>

[5] Securities and Exchange Board of India (Share Based Employee Benefits and Sweat Equity) Regulations 2021, August 13, 2021, available at <https://www.sebi.gov.in/legal/regulations/aug-2021/securities-and-exchange-board-of-india-share-based-employee-benefits-and-sweat-equity-regulations-2021_51889.html>

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There are prescriptive, sector-specific requirements, which apply to the remuneration of specified categories of employees or directors, and which apply in the asset management, investment services, banking, and insurance sectors.

Employers in these sectors are tasked with ensuring that the remuneration paid to material risk takers (individuals whose professional activities have a material impact on an RFSP's risk profile) or identified staff align with the RFSP risk profile.

There are detailed rules with technical guidance (emanating from EU law) specific to each sector, but at a high level they (to differing degrees) set out rules on; variable remuneration composition, ratios or other metrics to compare variable to fixed remuneration to ensure it is appropriate; malus requirements, which would allow the RFSP to cancel or reduce the employee's variable remuneration before it is paid out; and clawback provisions which allow RFSPs to recover variable remuneration after it has been awarded. It is important to ensure that employees' contracts of employment acknowledge that any variable remuneration will be subject to all regulatory restrictions and rules and may be clawed back in certain circumstances.

The CBI's 2014 Guidelines on Variable Remuneration Arrangements for Sales Staff also emphasise the importance of remuneration structures to have sufficient deterrents built into them (such as malus and clawback mechanisms) to avoid incentivising undesirable/risky behaviours from sales staff in the banking, insurance and investment services sectors.

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Switzerland

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Swiss civil law provides for special rules that govern the compensation of current and former members of inter alia the board and executive committee (Ordinance against Excessive Compensation) of Swiss companies limited by shares that are listed on a Swiss or foreign stock exchange. In addition, there are disclosure provisions listed companies need to follow concerning remuneration under stock exchange regulations.

In addition to the above, FINMA has formulated ten principles regarding remuneration that banks, securities firms, financial groups and conglomerates, insurance companies, insurance groups and conglomerates are required to implement. The principles serve as minimum standards for the design, implementation and disclosure of remuneration schemes.

These schemes should not incentivise to take inappropriate risks and thereby potentially damage the stability of financial institutions.

One of the focal points of the principles is variable remuneration that depends on business performance and risk. In particular, all variable remuneration must have been earned by the company over the long term. Consequently, remuneration is dependent on performance, taking into account the sustainability of such performance as well as the risks. That said, FINMA's principles do not limit the amount of variable remuneration. However, FINMA aims to prevent the granting of high remuneration based on large risks and the generation of short-term, unsustainable earnings. Furthermore, persons who have significant responsibility relating to the risk or receive a high total remuneration, must receive a significant part of the variable remuneration on a deferred basis and consequently, in a way that is linked to the current risk. Under the FINMA principles, "clawback" and "malus" arrangements are permitted.

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