Unity Small Finance Bank Limited (USFBL)

Compensation Policy

Contents

1. Overview

The philosophy behind USFBL's compensation policy is to create a compensation framework that supports the Bank's mission and values in full compliance to applicable Regulations. We believe our compensation program is a management tool that when aligned with an effective communication plan is designed to support, reinforce, and align our values, business strategy, operational & financial needs with a goal of growth and profitability.

This Compensation policy seeks to document the practices and procedures to be followed by the Bank for payment of remuneration to Directors (Including WTD and CEO), Key Managerial Personnel, Senior Managerial Personnel, Material Risk Takers, Control Function staff and other employees.

2. Terms and References

In this Policy, the following terms shall have the following meanings:

a. "**Director**" means a director appointed to the Board of a Bank.

b. "**Key Managerial Personnel**" (KMP) means:

   (i) the Chief Executive Officer or the managing director or the manager;

   (ii) the Company Secretary;

   (iii) the Whole-time Director;

   (iv) the Chief Financial Officer;

   (v) such other officer as may be prescribed under the Companies Act, 2013

c. **Senior Management Personnels** (SMPs):

   Members of the Senior Management of the Bank one level below Chief Executive Officer / Managing Director / Whole time Director / Manager and shall specifically include Company Secretary and Chief Financial Officer of the Bank. For the purpose of clarity, it is hereby submitted that all members of Executive Committee (EXCO) and Company Secretary shall be considered as SMPs of the Bank.

d. Share-linked Instruments:

   Share-linked Instruments consisting of ESOPs or other linked instruments which shall be forming part of variable pay.

e. Substantial: Substantial with reference remuneration shall mean at least 40% variable pay.

3. Material Risk Takers (MRTs)

MRTs are employees whose actions have a material impact on the risk exposure of the bank, and who satisfy the qualitative and any one of the quantitative criteria given below:

a. Standard Qualitative criteria: Relate to the role and decision-making power of designated leader having jointly or individually, the authority to commit significantly to risk exposures, etc.
b. Standard Quantitative Criteria:
   i. total remuneration exceeds a certain threshold or
   ii. Included among the 0.3% of staff with the highest remuneration in the Bank
   iii. Remuneration is equal to or greater than the lowest total remuneration of senior management and other risk-takers

Given that USFBL's limited business during first year of operations, USFBL will classify only the position of MD/CEO as MRT. As the Bank goes into commercial launch and the business model gathers momentum, through multiple business streams, Nomination and Remuneration Committee (NRC) of the Bank will re-evaluate other positions for the classification of MRTs.

4. Components of the Policy

USFBL's compensation policy is designed to attract, motivate, and retain talented employees who drive the company's success. The compensation structure and practices shall be in accordance with the generally accepted global principles and practices, thereby ensuing inter alia appropriate balance between fixed and variable pay, adequate deferrals incorporated in the variable component and cost/ income ratio supports the remuneration package consistent with maintenance of a sound capital adequacy ratio.

USFBL shall ensure that compensation of employees is adjusted for all types of risk, compensation outcomes are symmetric with risk outcomes, compensation pay-outs are sensitive to the time horizon of the risk, and a mix of cash, equity and other forms of compensation are consistent with risk alignment Further, in adherence to the FSB (Financial Stability Board) for Sound Compensation Practices, USFB intends to reduce incentives towards excessive risk taking that may arise from the structure of compensation schemes.

There are 4 broad components of this policy:

4.1 Fixed Compensation: While in most cases, we offer market aligned compensation for specific roles (at or around market 50th percentile), we are cognizant of the fact that we operate in a hyper-competitive talent segment and therefore, for relevant experience and niche Fintech/ Banking domain skills, we would operate at or around Market Upper Quartile to attract the right talent during our build stage.

As our operations mature, we would strive to provide fixed salary that meets the market median when employees are fully proficient and meeting expectations. The data for arriving at median would be from our applicant database. As the Bank achieves threshold levels of performance, we will conduct formal compensation benchmark survey and realign the base salaries appropriately. We believe that employees consistently performing above expectations and are proficient in the role should be rewarded with a higher fixed pay. Employees who are new to their role and/or not meeting expectations would be paid below the target (50th percentile). All the fixed items of compensation, including the perquisites, will be treated as part of fixed pay. It may be noted that all perquisites that are reimbursable should also be included in the fixed pay so long as there are monetary ceilings on these reimbursements. Contributions towards superannuation/retiral benefits will be treated as part of fixed pay.

4.2 Variable pay / Performance linked incentive (PLI): In addition to base salary, USFBL will utilize incentive or variable pay to meet the strategic goals of the company. PLI will be applicable for selective set of employees of the bank and will be based on individual goals that relate to the Bank's objectives as well as overall performance of the Bank.

In alignment with our Bank's culture, we will strive to communicate openly about the goals of the Bank and the design of the Variable pay plan. The objective is to keep the plan design fair and simple yet comprehensive so that all employees and Managers understand the goals and collectively work towards achieving the USFB Bank objectives. There are 3 components of Variable Pay:

a) ***Performance Assessment and PLI for Whole Time Directors / MD & CEO Material Risk Takers****:*

I. For MD & CEO, a substantial portion of compensation i.e., at least 50%, should be variable and paid on the basis of individual, business-unit and firm-wide measures that adequately measure performance. The total variable pay shall be limited to a maximum of 300% of the fixed pay (for the relative performance measurement period).

II. In case variable pay is up to 200% of the fixed pay, a minimum of 50% of the variable pay; and in case variable pay is above 200%, a minimum of 67% of the variable pay should be via non-cash instruments. The non- cash instrument for variable pay for MD & CEO would be via Share Linked Instrument which also includes Stock Appreciation Rights.

III. In the event that an executive is barred by statute or regulation from grant of share-linked instruments, his/her variable pay will be capped at 150% of the fixed pay but shall not be less than 50% of the fixed pay.

IV. Performance of the MD & CEO would be evaluated by the Nomination & Remuneration Committee of the Board on the basis Performance Metric which would be pre-approved.

V. The percentage of Performance linked payout would be recommended by the Nomination & Remuneration Committee to the Board for its approval on basis the achievement on Performance Metric and the business performance during the year

VI. The pre-approved performance metric to ensure that

(a) compensation is adjusted for all types of risks,

(b) compensation outcomes are symmetric with risk outcomes,

(c) compensation payouts are sensitive to the time horizon of the risks, and
(d) the mix of cash, equity and other forms of compensation are consistent with risk alignment.

A wide variety of measures of credit, market, liquidity and various other risks have been taken into consideration by the bank in implementation of risk adjustment.

b) ***Performance Assessment and PLI for Finance/Risk and Control Functions/ MRTs:***

I. Members of Financial and Risk control functions would be governed by the comprehensive performance assessment process as part of the Human Resources Policy of the Bank. However, to ensure independence from business, the performance assessment for Chief Compliance Officer(CCO) of the Bank would not be on the basis of any business outcome and will be based on regulatory compliance only. Furthermore, performance appraisal of the CCO will be reviewed by the Nomination & Remuneration Committee of the Board.

II. Members of staff engaged in Financial and Risk control, including Internal Audit, should be compensated in a manner that is independent of the business areas they oversee and commensurate with their key role in the bank. Effective independence and appropriate authority of such staff are necessary to preserve the integrity of financial and risk management's influence on incentive compensation. Back office and risk control employees play a key role in ensuring the integrity of risk measures. The mix of fixed and variable compensation for control function personnel should be weighted in favour of fixed compensation. However, a reasonable proportion of compensation has to be in the form of variable pay, so that exercising the options of malus and/or clawback, when warranted, is not rendered infructuous. To comply with this advisory the variable pay for all leaders and senior staff in Finance/Risk and control function has been proposed at an optimum level, as per the grid in clause 4.2 (c) I.

c) Performance Assessment and PLI for Other Employees including other KMPs and SMPs.

I. A transparent and comprehensive performance assessment exercise shall be instituted as part of human capital management practices. The factors taken into consideration include clear key performance/result areas, a holistic performance evaluation framework which includes, feedback mechanism, ensuring adequate performance differentiation between employees and suitable reward and recognition. In USFBL, every year the performance management process shall start with defining accountabilities, objectives, key result areas, enablers to do the job and development needs, which are assessed by the supervisor through continuous conversations. The year-end review shall be conducted to assess performance against defined goals. In order to maintain transparency, flexibility and efficiency efforts shall be put to automate the entire appraisal process.

USFBL will use variable pay as a financial incentive for performance-based goals. These targets are used to establish the amount of incentive an employee is eligible to receive for outstanding performance. The payout shall happen based on 2 parameters:

a) Organization Performance (Based on AOP);
b) Individual Performance (Based on goals planning at the beginning of the year)

The weight of both the parameters shall be decided every year based on business priorities and external environment influencing the business. For USFB, we will follow the following Pay-mix guidelines while determining variable pay:

Band	Variable Pay (as % of Fixed Pay)
Level 5	20% - 25%
Level 4	10% - 20%
Level 3	5% – 10%
Level 2 & Below	0%-5%

II. Any exception would be approved by MD/CEO and reported to NRC at its next meeting. Variable pay over and above 40% is considered to be substantial and 60% of total variable pay in such case shall be subject to deferment for a period of 3 years, implying that employee will receive 60% of eligible deferred pay in 3 equal installments starting from the end of next review cycle. This is to ensure there is adequate risk adjustment in the variable pay mix.

III. In addition to this, certain critical employees will be eligible for an Employee deferred pay, in the form of Long-Term Incentive Plan payable over a period of 4 years, payable at the end of each year. Total amount paid over 4 years under such deferred pay Long Term Scheme cannot exceed more than 100% of the fixed CTC.

IV. The employee shall be eligible for vested variable pay only, implying unvested pay shall expire once employee leaves the organization or otherwise gets terminated. Such deferred pay shall be subject to Malus or Clawback as MD/ CEO and NRC deem fit and shall be agreed with the employee at the time of assignment of such variable pay. Additional short-term incentive schemes for frontline sales or service personnel shall be announced subject to MD / CEO approval.

d) Guidelines on Deferral of Variable Pay:

For WTDs, MD/CEO and other employees who are MRTs in adherence to FSB Implementation Standards and extant Regulatory Guidelines, deferral arrangements must invariably exist for the variable pay, regardless of the quantum of pay. For such executives of the bank, a minimum of 60% of the total variable pay must invariably be under deferral arrangements. Further, if cash component is part of variable pay, at least 50% of the cash bonus should also be deferred. However, in cases where the cash component of variable pay is under Rs.25 lakh, deferral requirements would not be necessary, as follows:

I. **Period of Deferral arrangement**: The deferral period should be a minimum of three years. This would be applicable to both the cash and non-cash components of the variable pay.

II. **Vesting**: Deferred remuneration should either vest fully at the end of the deferral period or be spread out over the course of the deferral period. The first such vesting should be not before one year from the commencement of the deferral period. The vesting should be no faster than on a pro rata basis Additionally, vesting should not take place more frequently than on a yearly basis to ensure a proper assessment of risks before the application of ex post adjustment.

4.3 Long-term Wealth Creation through Equity linked compensation program

USFB tends to attract a large part of its talent pool from broadly 3 industries – a) Retail Banking, b)FinTech & Payments companies and c) Consulting Organizations, both in strategy and technology consulting space

Stock related compensation practices, especially Employee Stock Option Plan (ESOP) are very prevalent in two of the aforesaid three segments - Retail Banks and Payments Companies. To be able to attract top talent from these sectors and to create a long-term Retention strategy, we plan to create an Employee Stock Options Plan (ESOP) for employees of USFB. ESOP scheme shall be in accordance with applicable guidelines and will be over and above the variable pay.

The objective of the ESOP scheme will be to cover a select set of Management members and employees having niche skills and will also be used to attract talent for buying out the existing Equity related compensation obligation for select set of senior recruitments.

The Bank currently does not have any share linked instruments. However, in future if bank decides to include such instruments as a component of variable pay, the same would be framed by the bank in conformity with relevant statutory provisions. Share-linked instruments would be fair valued on the date of grant by the bank using Black-Scholes model.

4.4 Malus/Clawback

The Variable Pay for WTD/CEO, Risk Control & Compliance Staff and other MRTs would also be governed by Malus and Clawback arrangements which will be applicable in the event of subdued or negative financial performance of the bank and/or the relevant line of business in any year. Following are the set of representative situations in which Malus and Clawback can be invoked:

a. When an individual has personally acted frequently, dishonestly, or in a manner that adversely affects the Bank's reputation, or which is characterized as a gross misconduct.

b. When an individual is involved in directing an employee, contractor, or advisor to act frequently, dishonestly or to undertake other misconduct
c. When an individual breach their material obligation through error, omission or negligence.
d. When an individual has received a short term or long-term payout because of fraud, dishonesty or a breach of obligation committed by another person
e. Where significant financial or reputation loss is suffered by the Bank owing to conduct or decisions of an individual
f. When it is proven that bank has suffered financial or reputation loss due to lack of due diligence on part of a decision maker
g. When it is established that an individual has taken a decision on behalf of the Bank as per a quid pro quo arrangement
h. Wherever the assessed divergence in bank's provisioning for Non-Performing Assets (NPAs) or asset classification exceeds the prescribed threshold for public disclosure, the bank will not pay the unvested portion of the variable compensation for the assessment year.

5. Compensation for non-executive Directors (excluding the part- time non-executive Chairman)

The bank shall pay sitting fees to the non-executive directors and reimburse their expenses for participation in the Board and other Committee meetings, subject to compliance with the provisions of the Companies Act, 2013, the Banking Regulation Act, 1949, RBI guidelines issued from time to time and Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations,2015, as amended from time to time.

In addition to sitting fees and expenses related to attending meetings of the board and its committees as per extant statutory norms/ practices, the bank may provide for payment of compensation to NEDs in the form of a fixed remuneration commensurate with an individual director's responsibilities and demands on time and which are considered sufficient to attract qualified competent individuals. However, such fixed remuneration for an NED, other than the Chair of the board, shall not exceed ₹20 lakh per annum.

In case of any Non-Executive Director of the Bank, who is re-appointed or resigns or retires during the financial year, he/she would be paid commission on pro-rata to the number of days he/ she was a director during the said financial year, subject to the outcome of his performance evaluation and compliance of other conditions.

Additionally, all non-executive Directors would be entitled to reimbursement of expenses for attending Board/Committee meetings, official visits and participation in various forums on behalf of the Bank.

6. Compensation for part-time non-executive Chairman

The remuneration payable to the part-time non-executive Chairman would be governed by the provisions of Banking Regulation Act, 1949, RBI guidelines issued from time to time and the provisions of Companies Act, 2013 & related rules to the extent it is not inconsistent with the provisions of the Banking Regulation Act, 1949/RBI guidelines. Considering the above, the permitted modes of remuneration for the part-time non-executive Chairman would be:

- Fixed payments at such periodicity as may be recommended by the Nomination and Remuneration Committee, and approved by the Board and shareholders of the Bank.
- Sitting fee for attending each of the Board and other Committee meetings, as approved by the Board from time to time within the limits as provided under Companies Act, 2013 and related rules.

The part-time non-executive Chairman would be entitled to reimbursement of expenses for attending Board/Committee meetings, official visits and participation in various forums on behalf of the Bank

In line with regulatory guidelines, bank shall obtain prior approval of RBI for the Part-Time Nonexecutive Chairman under Section 10B(1A) (i) and 35B of the Banking Regulation Act, 1949.

7. Nomination and Remuneration Committee

Nomination and Remuneration Committee is the committee constituted by USFBL Board in accordance with the provisions of Section 178 of the Companies Act, 2013, RBI guidelines and the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations,2015.

The Board has constituted a Nomination and Remuneration Committee (NRC) to oversee the framing, review and implementation of compensation policy of the bank on behalf of the board. The NRC should comprise three or more non-executive directors, out of which not less than one-half should be independent directors and should include at least one member from Risk Management Committee of the board. The majority of members of the NRC will be independent non-executive directors. The NRC will work in close coordination with Risk Management Committee of the bank, in order to achieve effective alignment between remuneration and risks. The NRC will also ensure that the cost/income ratio of the bank supports the remuneration package consistent with maintenance of sound capital adequacy ratio.

8. Approval and Disclosure Requirements -

Compensation of WTDs/ CEO and Part-time non-executive Chairman shall be in accordance with Banking Regulations Act, 1949[1] and other extant Regulatory Guidelines. USFBL shall ensure that

[1] Refer Section 35B for compensation of WTDs/ CEO & Section 10B(1A)(i) and 35B for Part-time non-executive Chairman

RBI approval is obtained for the compensation, or changes thereon, of WTDs/ CEO and Part Time Non-Executive Chairman.

The approval matrix for different roles will be as follows:

Designation	Nomination and Remuneration committee approval Required	Board approval required	Shareholder's approval required	RBI Approval / intimation Required
Part Time Chairman	Yes	Yes	Yes	Yes
Non-Executive Directors (including Independent Directors)	Yes	Yes	Yes	Intimation to be given
Managing Director (MD) & CEO and Whole Time Director(s)	Yes	Yes	Yes	Yes
Key Managerial Personnel (KMP) other than MDs & WTDsas mentioned under Co. Act,2013	Yes	Yes	NA	Intimation to be given
Senior Management Personnel (SMP)	Yes	Only for CCO & HIA	NA	Intimation to be given for CCO, CRO, HIA & CTO
*Material Risk Takers, Risk Control and Compliance Employees	NA	NA	NA	NA
Other Categories of Employees	NA	NA	NA	NA

** In the above categories of employees, the NRC committee may from time to time add / amend the criteria aswell as the list of the officer(s) to be covered under the compensation framework.*

9. Disclosure requirements in the financial statements

USFBL shall disclose remuneration paid to directors in Annual Financial Statements. Additionally, bank shall make qualitative and quantitative disclosure as mandated by RBI in circular dated November 4th 2019 or as amended thereafter. After year 1 , the disclosures of remuneration paid to directors should be disclosed for previous financial year in addition to the current financial year, wherever applicable.

10. Review of policy and updates

The policy will be reviewed annually for necessary amendments and updates, or earlier to incorporate the change in business strategy or amendments in applicable regulations impacting the policy. Any revisions in the policy shall be approved by the Board. Exceptions to these guidelines, if any & as appropriate, will need specific approval from MD/CEO, USFB.

11. Regulatory References

I. This Policy adheres to principles and guidelines as prescribed by the Reserve Bank of India (RBI) in terms of the following circulars as amended time to time:

- Guidelines on Compensation of Whole Time Directors/ Chief Executive Officers/ Material Risk Takers and Control Function staff (Vide Circular no. RBI/2019-20/89 DOR.Appt.BC.No.23/29.67.001/2019-20 dated 4th November 2019) also referred herein as "**Compensation Guidelines**"
- Non-Executive Chairman of a Private Sector Bank (In terms of Section 10B (1A) of the Banking Regulation Act, 1949,)
- Non-Executive Directors (NEDs) (other than Non-Executive Chairman) (Vide Circular DBR. No. BC. 97/29.67.001/ 2014-15 dated 1st June 2015)
- Corporate Governance in Banks - Appointment of Directors and Constitution of Committees of the Board dated April 26, 2021.

II Companies Act, 2013

- Chapter XIII: The Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014
- SCHEDULE IV Code for Independent Directors
- SCHEDULE V Conditions for appointment and payment of remuneration of managerial personnel

III. Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations,2015, SEBI Circular No. SEBI/HO/CFD/CMD/CIR/P/2017/004 dated 5th January 2017 and other related circulars, guidelines in this regard.

IV. Banking Regulation Act, 1949

VERSION CONTROL TABLE

Version No.	Approval Date	Maintained by
1.0	Board- October 14, 2022	HR Department & Secretarial Department
2.0	NRC- May 13, 2022 Board - May 19, 2022	HR Department & Secretarial Department