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BVI response to ESMA's Consultation paper on Guidelines on remuneration policies and practices (MiFID)

BVI[1] gladly takes the opportunity to express its views on the proposed approach for ESMA guidelines on remuneration policies and practices under the MiFID.

General remarks

1. Consistent Standards

First of all, we will focus particularly on the point that the asset management industry is subject to different remuneration requirements:

- AIF managers will fall under the AIFMD and under the proposed ESMA guidelines on sound remuneration policies under the AIFMD.
- UCITS managers will fall under the future UCITS V Directive. The UCITS V proposal also stipulates that ESMA has to establish remuneration principles under the UCITS Directive.
- UCITS management companies or AIFM providing MiFID services such as portfolio management would be required to comply also with the MiFID remuneration rules and the proposed ESMA guidelines on remuneration policies and practices (MiFID).
- UCITS managers and AIFM belonging to financial groups must also observe remuneration standards for the banking or insurance sector applicable at group level.

Moreover, UCITS management companies and AIFM are bound by law to implement conflict of interest policies including the remuneration of control functions such as compliance or risk management func-

[1] BVI represents the interests of the German investment fund and asset management industry. Its 80 members currently handle assets of EUR 2.0 trillion in both investment funds and mandates. BVI enforces improvements for fund-investors and promotes equal treatment for all investors in the financial markets. BVI`s investor education programmes support students and citizens to improve their financial knowledge. BVI`s members directly and indirectly manage the capital of 50 million private clients in 21 million households. BVI's ID number in the EU register of interest representatives is 96816064173-47. For more information, please visit www.bvi.de.

tions. In developing remuneration practices on management company level it will be much more difficult to set remuneration guidelines which take these diverse remuneration regulations into account. This is made even more difficult by the fact that the wording of each remuneration regulation varies from the other. These sets of remuneration guidelines will also have to be implemented at different times, further increasing the complexity.

Furthermore, particular emphasis of the proposed ESMA remuneration guidelines under the MiFID will be placed on the remuneration of sales forces and the structure of incentives for the distribution of financial products. These activities are regularly provided by MiFID firms or other persons who market financial instruments. This is not the main field of UCITS managers' or AIFMs' activities.

Therefore and in order to facilitate the effective and consistent application of the remuneration requirements and to avoid contradictions, we propose allowing exceptions to ESMA's remuneration guidelines in cases where the investment firms are UCITS management companies or AIFM which provide MiFID-relevant services in addition to the management of UCITS or AIF. Hence, it is essential that the proliferation of remuneration regimes be stopped and consistent standards applied at least to the EU asset management industry. In light of the different remuneration requirements, ESMA should analyze in an interdepartmental manner how remuneration guidelines and practices on the investment management company level (UCITS and AIFM) could converge. This would lead to legal certainty, effective regulation and supervisory practices. Such measurement would also reduce costs for double or triple implementation of different remuneration requirements with different implementation deadlines.

2. Outsourcing arrangements (paragraph 10)

We strongly disagree with ESMA's proposal that the remuneration provided by firms to the outsourced entity is also regarded as remuneration for the purposes of these guidelines. We also do not agree with the notion that in such cases the firm has to ensure that the outsourced entity has equally effective remuneration policies and practices in place. These proposals run counter proven and tested EU regulation in the area of remuneration and are especially not feasible in the area of delegation of fund management.

The provisions of the AIFMD and the draft UCITS V Directive limit the scope of the principles of remuneration to payments made by the management company to the benefit of certain categories of staff of the management company. Therefore, any outsourcing activities by the UCITS management company or AIFM do not fall under the scope of AIFMD or UCITS remuneration regulation. A different approach by the guidelines on remuneration under MiFID is in particular a problem for UCITS and AIFM managers since they would face the challenge of diverse and partially contradicting requirements for remuneration. It is worthwhile mentioning that CRD IV follows the same approach.

Payments or benefits for outsourcing activities by MiFID firms to outsourced entities have no impact on the remuneration of the MiFID firm's staff. They are payments between two independent entities for services rendered. The fees paid by a firm to an outsourced entity contain various elements of compensation and reimbursements and cannot realistically be approached at equal terms with the salary of an individual.

Moreover, specific remuneration regulation generally applies for staff members of entities to which an activity has been delegated by the MiFID firm (e.g. because they are MiFID firms themselves or other

asset manager outside Europe). The MiFID firm has no means of influencing the remuneration policy or practice of the other entity.

Given that UCITS or AIF management companies are already subject to a consistent framework for remuneration (or shortly will be after implementation of UCITS V), there is no need to comprise these entities in the scope of the proposed regulation even if they provide MiFID services within the limited boundaries given by the UCITS or AIFM Directives, respectively. In addition, the relevant payments are already disclosed to potential and existing investors in the prospectus or offering documentation as well as the financial report of the AIFs or UCITS.

Therefore, we propose exceptions to ESMA's remuneration guidelines in cases where the outsourcing activities are in connection with the management of UCITS or AIFs. We would also appreciate clarification that not all persons performing any service on the basis of outsourcing arrangements are covered by the guidelines (for example: outsourced maintenance services, IT services, bookkeeping and accounting and similar services).

3. Group level (paragraph 12)

We suggest a clarification that the parent enterprise within a group structure shall only ensure that subsidiaries for which other special remuneration requirements under supervisory law apply comply with these specific requirements under supervisory law concerning remuneration systems. For example, if the parent undertaking is an investment firm such a bank and the subsidiary is an AIFM, the bank must ensure that the AIFM complies with the special remuneration requirements for the asset management industry, but not extend the CRD principles also to the AIFM.

4. Stigmatization of certain financial instrument caused by examples of poor practices

We consider the way of presenting examples for good and poor practices inappropriate to handle the complex questions with regard to remuneration requirements. This is especially the case since certain financial instruments such as new fund products are described as examples of poor practices (e.g. **paragraph 26**). We feel that the selection of examples lacks balance and recommend equal treatment for all financial instruments in order to avoid stigmatization of certain financial instruments in connection with poor practices. It should be clear that the described good or poor practices are examples for all kind of financial instruments.

5. Level playing field

We understand that the ESMA Guidelines aim at preventing miss-selling of financial products and services and avoiding remuneration or practices which could be detrimental for clients. To ensure a level playing field, guidelines should not only apply to MiFID firms selling saving products. BVI would welcome if relevant guidelines would already comprise the concept of PRIPs and thus be applicable to the sale of any substitute financial product to retail clients.

Specific comments

We would like to provide the following responses to selected questions for consultation:

Q1: Do you agree that firm's remuneration policies and practices should be aligned with effective conflicts of interest management duties and conduct of business risk management obligations so as not to create incentives that may lead relevant persons to favour their own interest, or the firm's interests, to the potential detriment of clients? Please also state the reasons for your answer.

Yes, we agree.

Q2: Do you agree that, when designing remuneration policies and practices, firms should take into account factors such as the role performed by relevant persons, the type of products offered, and the methods of distribution? Please also state the reasons for your answer.

The used definition of 'relevant persons' is different from the definition of 'relevant persons' of MiFID Level 2 (Commission Directive 2006/73, Article 1). This creates legal uncertainty which should be avoided. Therefore, we propose replacing the term 'relevant persons' with another wording in the context of the guidelines in order to prevent conflicting definitions.

However, we agree with the proposal that firms should take into account factors such as the role performed by relevant persons, the type of products offered, and the methods of distribution, when designing remuneration policies and practices. We welcome this as an application of the proportionality principle.

However, we understand the criterion 'type of products offered' as only one factor in the process of assessing the overall risk structure as a precondition for designing a remuneration policy.

In our view, the method of distribution is only of minor influence. At this point, it should be clarified that the method of distribution does not mean any inducements.

Q3: Do you agree that when designing remuneration policies and practices firms should ensure that the fixed and variable components of the total remuneration are appropriately balanced?

Yes, we agree. For each firm, this should be possible as the remuneration policies and principles will be designed by each firm in application of the proportionality principle according to the nature, scale and complexity of their business and taking into account factors such as the role performed by the relevant persons, the type of products offered and the methods of distribution.

Q4: Do you agree that the ratio between the fixed and variable components of remuneration should therefore be appropriate in order to take into account the interests of the clients of the firm? Please also state the reasons for your answer.

In our view, a universal link between the interest of the clients of the firm and the ratio between fixed and variable components cannot be established. Therefore, it should be clarified that the interests of the clients of the firm is only one criterion which should be taken into account in an appropriate manner.

Q11: Do you agree that firms should set up controls on the implementation of their remuneration policies and practices to ensure compliance with the MiFID conflicts of interest and conduct of business requirements, and that these controls should include assessing the quality of the service provided to the client? Please also state the reasons for your answer.

Evidence as described in paragraph 65 does not necessarily mean low quality has been delivered to the client. Suitability and quality of the provided service need to be assessed based on common standards.

Q12: Do you agree that the compliance function should be involved in the design process of remuneration policies and practices before they are applied to relevant staff? Please also state the reasons for your answer.

We disagree. Remuneration policies should be designed by HR taking business needs into account. Depending on legal restrictions (i.e. individual and collective labour laws), compliance in terms of compensation may need to be done by a dedicated entity, e.g. by an “HR Compliance Team”. This team should be assessed by the Remuneration Committee/Compensation Committee. Compliance should design and assess any policies for conflicts of interest.

Q13: Do you agree that it is difficult for a firm, in the situations illustrated above in Annex I, to demonstrate compliance with the relevant MiFID rules?

Q14: If you think some of these features may be compatible with MiFID rules, please describe for each of (a), (b), (c) and (d) in Annex I above which specific requirements (i.e. stronger controls, etc) they should be subject to.

The way the examples in annex 1 are worded is highly suggestive since they use terms with a clearly negative connotation (“push”, “unnecessary”, “unsuitable” and the like). We do not deem such examples helpful for developing criteria for sound remuneration principles.

We hope that our comments prove helpful for reconsidering and refining ESMA’s MiFID guidelines on remuneration policies. Please do not hesitate to contact us, should you have any questions or see the need for further discussion.

Yours sincerely,

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