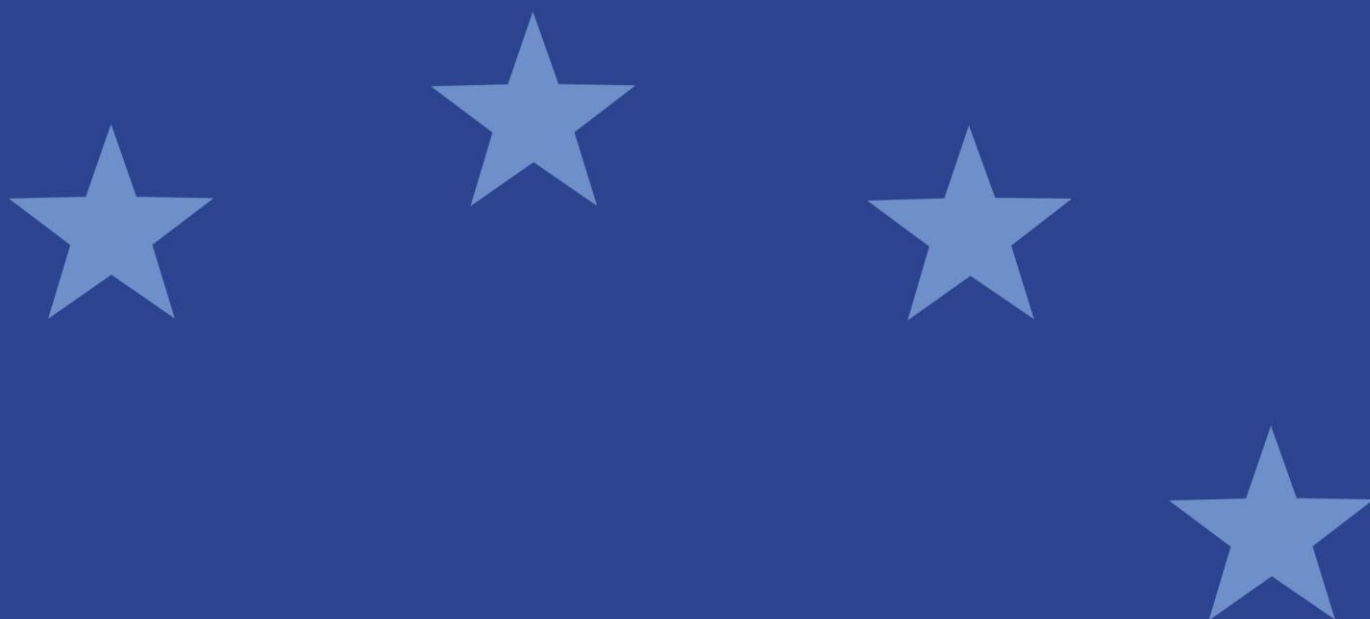


# Consultation Paper

**Guidelines on sound remuneration policies under the UCITS Directive  
and AIFMD**



## **Responding to this paper**

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex II. Comments are most helpful if they:

1. respond to the question stated;
2. indicate the specific question to which the comment relates;
3. contain a clear rationale; and
4. describe any alternatives ESMA should consider.

ESMA will consider all comments received by 23 October 2015.

Responses to this consultation paper can be sent using the response form, via [the ESMA website](#), under the heading ‘Your input/Consultations’.

### **Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

### **Data protection**

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading [Legal Notice](#).

### **Who should read this paper**

This document will be of interest to asset management companies managing UCITS funds and AIFMs managing AIFs and their trade associations, as well as institutional and retail investors investing into such funds and their associations.

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# 1 Executive Summary

## Reasons for publication

Article 14a(4) of Directive 2009/65/EC (“UCITS Directive”), as amended by Directive 2014/91/EU (“UCITS V Directive”) provides that ESMA shall issue guidelines addressed to competent authorities or financial market participants concerning the application of the remuneration principles set out under Article 14b of the UCITS Directive (“UCITS Remuneration Guidelines”). This consultation paper represents the first step in the development of the guidelines on remuneration policies required by the UCITS V Directive and sets out ESMA’s formal proposals for these guidelines. This consultation paper also proposes a targeted revision of the Guidelines on sound remuneration policies under the AIFMD (ESMA/2013/232) (“AIFMD Remuneration Guidelines”), which were published on 3 July 2013.

## Contents

Section 2 explains the background to this document, while Section 3 explains the working method followed by ESMA while developing the draft guidelines. Sections 4 to 7 provide an overview of the content of the draft guidelines focusing on the main areas of difference between the requirements on remuneration under Directive 2011/61/EU (“AIFMD”) and UCITS V Directive.

Annex I provides for a comparison table where the relevant UCITS V provisions on remuneration are marked up against the AIFMD provisions. Annex II sets out the list of questions contained in this paper. Annex III includes the draft cost-benefit analysis for the guidelines, while Annex IV sets out the text of the draft UCITS Remuneration guidelines and Annex V sets out the proposed amendment to the AIFMD Remuneration Guidelines.

## Next Steps

ESMA will consider the feedback it receives to this consultation with a view to finalising the UCITS Remuneration Guidelines and publishing a final report by early Q1 2016, ahead of the transposition deadline for the UCITS V Directive (i.e. 18 March 2016). The final report is expected to also include the revision of the AIFMD Remuneration Guidelines which is proposed in the present paper.

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## 2 Background

1. Article 14a(4) of the UCITS Directive provides that ESMA shall issue guidelines addressed to competent authorities or financial market participants concerning the application of the remuneration principles set out under Article 14b of the UCITS Directive (“UCITS V Remuneration Guidelines”).
2. Article 14a(4) of the UCITS V Directive sets out the following requirements:
  - ESMA shall take into account the principles on sound remuneration policies set out in Recommendation 2009/384/EC (“Recommendation”);
  - ESMA shall take into account proportionality (*“the size of the management company and the size of the UCITS that [the relevant persons] manage, their internal organisation, and the nature, scope and complexity of their activities”*); and
  - ESMA shall cooperate closely with EBA.

## 3 Working method

3. Both the above mentioned requirements and the UCITS V remuneration principles themselves (i.e. the principles under Article 14b of the UCITS Directive) broadly reflect the provisions on remuneration under the AIFMD. For this reason ESMA decided to take the Guidelines on sound remuneration policies under the AIFMD<sup>1</sup> (“AIFMD Remuneration Guidelines”) as a starting point for developing the UCITS V Remuneration Guidelines and depart from them only if and when strictly necessary.
4. This is in line with and justified by the approach envisaged by the co-legislators according to the Level 1 text. Indeed, recital 9 of the UCITS V Directive states that *“ESMA’s guidelines on remuneration policies and practices should, where appropriate, be aligned, to the extent possible, with those for funds regulated under Directive 2011/61/EU of the European Parliament and of the Council”*.
5. Therefore, when developing the proposed draft guidelines, ESMA started from the text of the AIFMD Remuneration Guidelines and adapted it to the specificities of the UCITS framework, also taking into account the differences between the AIFMD and UCITS V Level 1 texts (see the following sections for more details). In order to facilitate the comparison between the provisions on remuneration under the AIFMD and UCITS Directive, ESMA has set out an illustrative comparison table where the UCITS V text is marked up against the AIFMD text (Annex I).
6. The main areas of difference between the requirements on remuneration under the AIFMD Remuneration Guidelines and UCITS Remuneration Guidelines are described in

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<sup>1</sup> [ESMA/2013/232](#)

the following sections. These relate to areas where the UCITS V Level 1 provisions are either different from those under the AIFMD or set out some additional guidance to ESMA on the way the UCITS Remuneration Guidelines should be drafted, i.e. for the guidance on the application of different sectoral rules (Section 9 of the draft guidelines). Notwithstanding the fact that the proposed approach on proportionality is aligned with that of the AIFMD Remuneration Guidelines, there is commentary in the following section on that topic in order to elicit stakeholders' feedback on it.

7. Given that the provisions of the UCITS V Directive require close cooperation with EBA as regards the UCITS Remuneration Guidelines, in developing the present consultation paper, ESMA also considered the provisions of the EBA consultation paper published on 4 March 2015 (EBA/CP/2015/03) ("EBA CP")<sup>2</sup>, as further detailed below.

## 4 Proportionality

8. As set out in paragraph 4 above, recital 9 of the UCITS Directive states that ESMA's UCITS Remuneration Guidelines should, where appropriate, be aligned, to the extent possible, with the AIFMD Remuneration Guidelines. With respect to proportionality, the AIFMD Remuneration Guidelines permit the disapplication of certain specific remuneration requirements under specific circumstances and conditions.<sup>3</sup> In the interests of ensuring consistency between the UCITS Remuneration Guidelines and the AIFMD Remuneration Guidelines, therefore, ESMA considers it appropriate to make provision for a similar approach to disapplication in the draft guidelines.
9. In reaching this conclusion, ESMA also took into account the reading of the CRD IV provisions recently followed by EBA. The EBA CP does not foresee the possibility to disapply any of the remuneration principles under the CRD IV.<sup>4</sup> EBA mentioned that "[...] *the preliminary assessment of the EBA is that a full waiver of the application of even a limited set of remuneration principles for smaller and non-complex institutions would not be in line with the CRD. Therefore, the application of the principle of proportionality needs to be interpreted in a way that, of the possible manners and degrees to apply the corresponding CRD remuneration principle, the most appropriate according to the institution's size, internal organization and nature, scope and complexity of their activities, as required by Article 92 (2) CRD, should be applied. However, the principle itself cannot be disapplied*".
10. Notwithstanding the above, ESMA is of the view that an alternative legal reading of the equivalent provisions of the UCITS V Directive could also be envisaged. In particular, the

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<sup>2</sup> The consultation paper on Draft Guidelines on sound remuneration policies under Article 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013 is available at the following address: <http://www.eba.europa.eu/documents/10180/1002374/EBA-CP-2015-03+%28CP+on+GLs+on+Sound+Remuneration+Policies%29.pdf>.

<sup>3</sup> See Section VII.I of the AIFMD Remuneration Guidelines.

<sup>4</sup> The EBA consultation paper is available at the following address: <http://www.eba.europa.eu/documents/10180/1002374/EBA-CP-2015-03+%28CP+on+GLs+on+Sound+Remuneration+Policies%29.pdf>.



following wording of Article 14b of the UCITS V Directive could be considered (emphasis added):

*When establishing and applying the remuneration policies referred to in Article 14a, management companies shall comply with the following principles in a way and to the extent that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities*

11. A possible reading of this wording is that the co-legislators envisaged the possibility that the application of proportionality could lead a UCITS to disapply certain of the remuneration principles.
12. Moreover, the reading followed by the EBA in the context of the CRD relates to a different sector of the financial services industry. ESMA considers that the different nature of UCITS compared to credit institutions, and the relatively diverse nature of the UCITS sector, could justify a different approach to proportionality.
13. Finally, in developing its proposal ESMA has considered the possible impact that an alternative approach to proportionality might have on the UCITS sector. This relates both to the costs of applying in full all of the principles set out in the UCITS V Directive, and to those arising from the fact that management companies managing both UCITS and AIFs would have to apply different approaches (since the AIFMD Remuneration Guidelines allow disapplication of certain of the principles).

**Q1: In this consultation paper ESMA proposes an approach on proportionality which is in line with the AIFMD Remuneration Guidelines and allows for the disapplication of certain requirements on an exceptional basis and taking into account specific facts. Notwithstanding this, ESMA is interested in assessing the impact from a general perspective and more precisely in terms of costs and administrative burden that a different approach would have on management companies. For this reason, management companies are invited to provide ESMA with information and data on the following aspects:**

- 1) All management companies (i.e. those that hold a separate AIFMD licence and those that do not) are invited to provide details on the following:
  - a) compliance impacts and costs (one-off and ongoing costs, encompassing technological/ IT costs and human resources), and
  - b) any type of practical difficulties in applying in any circumstances the remuneration principles that could otherwise be disapplied according to the provisions under Section 7.1 of the draft UCITS Remuneration Guidelines (Annex IV to this consultation paper).
- 2) Management companies that also hold an AIFMD licence and benefit from the disapplication of certain of the remuneration rules under the AIFMD

**Remuneration Guidelines are asked to provide an estimate of the compliance costs in absolute and relative terms and to identify impediments resulting from their nature, including their legal form, if they were required to apply, for the variable remuneration of identified staff:**

- a) deferral arrangements (in particular, a minimum *deferral period* of three years);**
- b) retention;**
- c) the pay out in instruments; and**
- d) malus (with respect to the deferred variable remuneration).**

**Wherever possible, the estimated impact and costs of these changes should be quantified, supported by a short explanation of the methodology applied for their estimation and provided separately, if possible, for the four listed aspects.**

## **5 Management companies being part of a group**

14. The proposed draft guidelines mirror the provisions of the AIFMD Remuneration Guidelines on the rules applicable to management companies that are part of a group to the extent that the UCITS Remuneration Guidelines also provide that they apply in any case to any management company (see paragraph 30 of the draft UCITS Remuneration Guidelines).
15. However, new wording has been introduced in the UCITS Remuneration Guidelines (see paragraph 31 of the draft guidelines) to clarify that in a group context, non-UCITS sectoral prudential supervisors of group entities may deem certain staff of the UCITS management company which is part of that group to be 'identified staff' for the purpose of their sectoral remuneration rules. This issue relates to the CRD IV provisions which state that the application of the remuneration rules shall be ensured by competent authorities for institutions at group, parent company and subsidiary levels.<sup>5</sup> In this context, it is worth noting that the EBA CP includes additional guidance for subsidiaries within a group which are not subject to the CRD IV.<sup>6</sup>
16. For this reason, ESMA decided not only to insert the wording set out in paragraph 31 of the draft UCITS Remuneration Guidelines, but also to propose a similar amendment to paragraph 33 of the AIFMD Remuneration Guidelines and thereby, in the light of the EBA CP, avoid any interference with the application of the CRD IV provisions<sup>7</sup>.

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<sup>5</sup> See Article 92(1) of the CRD IV.

<sup>6</sup> See, in particular Section 7 (Remuneration policies and group context) of the EBA CP.

<sup>7</sup> The current version of paragraph 33 of the AIFMD Remuneration Guidelines states: *Compliance with these sectoral remuneration principles by AIFMs which belong to banking, insurance, investment groups or financial conglomerates should be*

## 6 Specificities of the UCITS V remuneration rules

17. Notwithstanding the fact that the remuneration rules under the UCITS V Directive are broadly in line with those of the AIFMD, the present section highlights the main specificities which were taken into account by ESMA for the purpose of the proposed UCITS Remuneration Guidelines.

### 6.1 Definitions

#### 6.1.1 Definition of ‘performance fees’

18. Article 14b(3) of the UCITS V Directive specifically includes “performance fees” among the categories of payment that fall within the scope of the remuneration principles.

19. This reference mirrors the AIFMD provisions that explicitly capture “carried interest” under the scope of the AIFMD remuneration rules. Indeed, Annex 2, paragraph 2 of the AIFMD states that “*The principles set out in paragraph 1 shall apply to remuneration of any type paid by the AIFM, to any amount paid directly by the AIF itself, including carried interest, [...] made to the benefits of those categories of staff [...] whose professional activities have a material impact on their risk profile or the risk profiles of the AIF that they manage*” (emphasis added). However, while the AIFMD provides for a definition of “carried interest” (Article 4(1)(d) AIFMD) – which is supplemented by the guidance provided by the AIFMD Remuneration Guidelines<sup>8</sup> – the UCITS Directive does not provide a definition of “performance fee”.

20. ESMA considers appropriate to set out a common definition of “performance fees” in order to ensure a consistent approach across Europe on the scope of application of the UCITS remuneration rules.

21. The proposed definition is based on the one provided in the IOSCO Final report on elements of international regulatory standards on fees and expenses of investment funds (November 2004).<sup>9</sup>

**Q2: Do you agree with the proposal to set out a definition of “performance fees” and with the proposed definition? If not, please explain the reasons why and provide an alternative definition supported by a justification.**

#### 6.1.2 Definition of ‘supervisory function’

22. Article 2(1)(s) UCITS Directive (introduced by the UCITS V Directive) provides for a definition of ‘management body’ which is as follows:

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*considered as ensuring the respect by such a group of the remuneration principles applicable to the group with specific regard to the AIFM.*

<sup>8</sup> See, in particular paragraph 13, of the AIFMD Remuneration Guidelines.

<sup>9</sup> Available at the following website: <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD178.pdf>.

(s) ‘management body’ means the body with ultimate decision-making authority in a management company, investment company or depositary, comprising the supervisory and the managerial functions, or only the managerial function if the two functions are separated. Where, according to national law, the management company, investment company or depositary has in place different bodies with specific functions, the requirements laid down in this Directive directed at the management body or at the management body in its supervisory function shall also, or shall instead, apply to those members of other bodies of the management company, investment company or depositary to whom the applicable national law assigns the respective responsibility;

23. As there is no definition of ‘management body’ under the AIFMD, the AIFMD Remuneration Guidelines provide for a definition of ‘management body’ and refer to the governing body of an AIFM<sup>10</sup>. As compared to the AIFMD Remuneration Guidelines, the definition of ‘management body’ is not included in the list of definitions of the draft guidelines, given that the relevant Level 1 definition applies in any event.

24. However, a definition of ‘supervisory function’ is included in the draft guidelines<sup>11</sup> and mirrors the equivalent definition included in the AIFMD Remuneration Guidelines. Feedback from stakeholders is sought on whether there is any overlap between the proposed definition of ‘supervisory function’ in the UCITS Remuneration Guidelines and the definition of ‘management body’ in the UCITS V Level 1 text (Article 2(1)(s) of the UCITS Directive).

**Q3: Do you see any overlap between the proposed definition of ‘supervisory function’ in the UCITS Remuneration Guidelines and the definition of ‘management body’ in the UCITS V Level 1 text? If yes, please provide details and suggest how the definition of ‘supervisory function’ should be amended in the UCITS Remuneration Guidelines.**

## 6.2 Remuneration covered by the UCITS guidelines

25. Article 14b(3) of the UCITS Directive states that “*The principles set out in paragraph 1 shall apply to any benefit of any type paid by the management company [...]*” while Annex 2, paragraph 2 of the AIFMD states that “*The principles set out in paragraph 1 shall apply to remuneration of any type paid by the AIFM [...]*” (emphasis added). ESMA considers that the different language used in the UCITS Directive does not imply any material consequence for the purpose of the UCITS Remuneration Guidelines as the

<sup>10</sup> The ‘governing body’ is defined in turn under Article 1(4) of Commission Delegated Regulation (EU) No 231/2013 which states the following: “‘governing body’ means the body with ultimate decision making authority in an AIFM, comprising the supervisory and the managerial functions, or only the managerial function if the two functions are separated.”

<sup>11</sup> The proposed definition of ‘supervisory function’ is as follows: “the relevant persons or body or bodies responsible for the supervision of the management company’s senior management and for the assessment and periodical review of the adequacy and effectiveness of the risk management process and of the policies, arrangements and procedures put in place to comply with the obligations under the UCITS Directive. For those management companies that, given their size, internal organisation and the nature, scope and complexity of their activities or their legal structure, do not have a separate supervisory function, the supervisory function should be understood as the member or members of the management body responsible for these functions”.

scope of the payments covered by these Guidelines (which mirrors that of the AIFMD Remuneration Guidelines on this point) is such that also ‘any benefit’ paid by the management company should be covered.<sup>12</sup>

### 6.3 Application of different sectoral rules

26. Article 14b(2), second sub-paragraph of the UCITS V Directive states that “*ESMA shall, in close cooperation with EBA, include in its guidelines on remuneration policies provisions on how different sectoral remuneration principles, such as those set out in [the AIFMD] and in [the CRD IV], are to be applied where employees or other categories of personnel perform services subject to different sectoral remuneration principles*”.

27. This is an important cross-sectoral element of the future guidelines. While the situation described in the Level 1 text may be more common for asset managers being part of a banking group, the relevant issue goes beyond the application of the remuneration rules in a group context as it seems to cover situations where a staff member performs activities subject to different sectoral legislation (e.g. even in cases where the staff member of an asset manager does not have an impact on the risk profile of the parent credit institution). Moreover, there may be circumstances where, for instance, a UCITS management company is the parent company of an investment firm and a staff member performs activities falling under both the UCITS V Directive and the CRD IV remuneration rules.

28. ESMA approached this issue by setting out two alternative solutions that could be followed in case some personnel of management companies perform activities covered by different sectoral legislation. In such a case it should be possible to opt for paying the personnel either:

- a) by applying the remuneration principles in the sectoral legislation (CRD, AIFMD and UCITS Directive) on a pro rata basis based on objective criteria such as the time spent on each service, or
- b) by applying the sectoral remuneration principles which are deemed more effective for achieving the outcomes of discouraging excessive risk taking and aligning the interest of the relevant individuals with those of the investors in the funds they manage.

29. In line with the approach followed under the EBA CP in the context of the guidance provided on the application of the CRD rules in a group context<sup>13</sup>, ESMA clarifies that whenever the option under b) in the previous paragraph is chosen, this should be without prejudice to the application of the specific sectoral legislation covering the relevant services whenever it conflicts with the sectoral remuneration principles that are deemed more effective (e.g. the rules on the payment of variable remuneration in AIF or UCITS

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<sup>12</sup> See paragraph 11 of the Draft guidelines under Annex IV.

<sup>13</sup> See section 7, paragraph 63 of the EBA CP.

instruments should in any case prevail over the CRD rules on the payment of variable remuneration in CRD instruments).

30. As for the MiFID ancillary services, ESMA considers that the performance of ancillary services under Article 6(3) of the UCITS Directive or under Article 6(4) of the AIFMD by personnel of a management company or an AIFM should be subject to the remuneration principles under the UCITS Directive or AIFMD, as applicable.

**Q4: Please explain how services subject to different sectoral remuneration principles are performed in practice. E.g. is there a common trading desk/an investment firm providing portfolio management services to UCITS, AIFs and/or individual portfolios of investments? Please provide details on how these services are operated.**

**Q5: Do you consider that the proposed 'pro rata' approach would raise any operational difficulties? If yes, please explain why and provide an alternative solution.**

**Q6: Do you favour also the proposed alternative approach according to which management companies could decide to voluntarily opt for the sectoral remuneration rules which are deemed more effective in terms of avoiding excessive risk taking and ensuring risk alignment and apply them to all the staff performing services subject to different sectoral remuneration rules? Please explain the reasons behind your answer.**

**Q7: Do you agree that the performance of ancillary services under Article 6(3) of the UCITS Directive or under Article 6(4) of the AIFMD by personnel of a management company or an AIFM should be subject to the remuneration principles under the UCITS Directive or AIFMD, as applicable? Or do you consider that that MiFID ancillary services do not represent portfolio/risk management types of activities (Annex I of the AIFMD) nor investment management activities (Annex II of the UCITS Directive) and should not be covered by the rules under Article 14b of the UCITS Directive and Annex II of the AIFMD which specifically refer to the UCITS/AIFs that a UCITS/AIFM manages? Please explain the reasons of your response.**

## 6.4 Application of the rules to delegates

31. Recital 2 of the UCITS V Directive states that

*"[...] remuneration policies and practices should apply, in a proportionate manner, to any third party which takes investment decisions that affect the risk profile of the UCITS because of functions which have been delegated in accordance with Article 13 of Directive 2009/65/EC"* (emphasis added).



32. While explaining the core legal text of the UCITS V Directive, these provisions can be understood as seeking to achieve the same outcome as the approach on delegates followed under paragraph 18 of the AIFMD Remuneration Guidelines.<sup>14</sup> Therefore, ESMA took the latter provisions as a starting point for the guidance to be provided on delegates in the UCITS Remuneration Guidelines.
33. ESMA considers that management companies should not circumvent the remuneration rules through the delegation of activities to external service providers. Therefore, in line with the approach followed under the AIFMD Remuneration Guidelines, when delegating investment management activities according to Article 13 of the UCITS Directive, where the remuneration rules would otherwise be circumvented, management companies should ensure that
- a) the entities to which investment management activities have been delegated are subject to regulatory requirements on remuneration that are equally as effective as those applicable under these guidelines; or
  - b) appropriate contractual arrangements are put in place with entities to which investment management activities have been delegated.
34. Following the approach set out under the Q&A on the application of the AIFMD<sup>15</sup>, ESMA sees merit in also introducing a system of equivalence between the AIFMD, CRD IV and UCITS V remuneration rules. For instance, whenever portfolio management is delegated by a UCITS management company to an AIFM and the staff of the AIFM who are *identified staff* for the purpose of these guidelines are subject to the AIFMD rules, the AIFMD remuneration rules should be considered equivalent and no material compliance with the UCITS V rules should be required (and vice versa).

## 6.5 Payment in instruments

35. Article 14b(1)(m) of the UCITS Directive provides that

*“(m) subject to the legal structure of the UCITS and its fund rules or instruments of incorporation, a substantial portion, and in any event at least 50 %, of any variable remuneration component consists of units of the UCITS concerned, equivalent*

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<sup>14</sup> “When delegating portfolio management or risk management activities according to Article 20 of the AIFMD and its implementing measures, AIFM should ensure that:

a) the entities to which portfolio management or risk management activities have been delegated are subject to regulatory requirements on remuneration that are equally as effective as those applicable under these guidelines; or

b) appropriate contractual arrangements are put in place with entities to which portfolio management or risk management activities have been delegated in order to ensure that there is no circumvention of the remuneration rules set out in the present guidelines; these contractual arrangements should cover any payments made to the delegates’ identified staff as compensation for the performance of portfolio or risk management activities on behalf of the AIFM”.

<sup>15</sup> Q&A 4 states the following: “Question 4 [last update 17 February 2014]: In a delegation arrangement where the delegate is subject to the CRD rules, can the delegate be considered to be subject to regulatory requirements on remuneration that are equally as effective as those applicable under the Remuneration Guidelines?

Answer 4 : Provided that the staff of these entities who are identified staff for the purpose of the Remuneration Guidelines are subject to the CRD rules, these entities are subject to regulatory requirements on remuneration that are equally as effective as those applicable under the Guidelines”.

*ownership interests, or share-linked instruments or equivalent non-cash instruments with equally effective incentives as any of the instruments referred to in this point, unless the management of the UCITS accounts for less than 50 % of the total portfolio managed by the management company, in which case the minimum of 50 % does not apply. [...]"*

36. Based on the experience gained in the implementation of the equivalent AIFMD rules, ESMA sees merit in providing additional guidance on how to comply with the rules on the payment of variable remuneration in instruments under the UCITS Directive. In particular, ESMA analysed the following issues:

- 1) whether in relation to the size of the funds being less than 50% of the total portfolio, the provisions refer to the individual UCITS in question or all the UCITS managed by the management company; and
- 2) what is the total portfolio managed by the management company (AIF + UCITS + individual portfolios; only the UCITS; or only AIF+UCITS).

37. ESMA considers that for the issue under 1) above, reference should be made to the individual UCITS, while for the issue under 2), reference should be made to the portfolios managed under the UCITS authorisation. Therefore, it is proposed to clarify that for the purposes of the requirement to pay at least 50% of variable remuneration in instruments unless the management of the UCITS accounts for less than 50% of the total portfolio managed by the management company, the 50% threshold should be based on the net asset value of the individual UCITS managed by the management company. For the purposes of the same requirement, the total portfolio managed by the management company should be the portfolios managed by the management company under its authorisation under the UCITS Directive (i.e. the portfolios managed under its authorisation under the AIFMD, if any, should not be taken into account).

38. The above approach may be explained through the following example. A management company manages 5 UCITS under its UCITS authorisation, for a total of 100 million EUR of assets under management (AuM). The net asset value of each of the 5 UCITS is as follows:

- UCITS 1: 5 million EUR (5% of the total AuM);
- UCITS 2: 5 million EUR (5% of the total AuM);
- UCITS 3: 10 million EUR (10% of the total AuM);
- UCITS 4: 15 million EUR (15% of the total AuM);
- UCITS 5: 65 million EUR (65% of the total AuM).

39. The requirement to pay at least 50% of variable remuneration in instruments would apply only in relation to UCITS 5 (i.e. the only one whose net asset value represents more than



50% of the total AuM managed by the management company under its UCITS authorisation).

**Q8: Do you agree with the proposal to look at individual entities for the purpose of the payment in instruments of at least 50% of the variable remuneration or consider that it would risk favouring the asset managers with a bigger portfolio of UCITS assets under management? Should you disagree, please propose an alternative approach and provide an appropriate justification.**

## **7 Date of application of the guidelines**

40. The UCITS V Directive does not impose a specific deadline for the finalisation of the UCITS Remuneration Guidelines. However, considering the transposition deadline for the UCITS V Directive (i.e. 18 March 2016) and the time necessary to both competent authorities and market participants to adapt to the provisions of the future guidelines, ESMA aims to finalise the UCITS Remuneration Guidelines in Q4 2015.

41. ESMA considers that the UCITS Remuneration Guidelines should then start to apply as from the transposition deadline of the UCITS V Directive.

**Q9: Do you consider that there is any specific need to include some transitional provisions relating to the date of application of the UCITS Remuneration Guidelines? If yes, please provide details on which sections of the guidelines would deserve any transitional provisions and explain the reasons why, also highlighting the additional costs implied by the proposed date of application. Please be as precise as possible in your answer in order for ESMA to assess the merit of your needs.**

## 8 Annexes

### 8.1 Annex I

#### Comparison table UCITS V vs. AIFMD texts on remuneration

Art. 14b(1)(a) UCITS Directive vs. Par. (1)(a) Annex II AIFMD	<u>the remuneration policy is consistent</u> with and promotes sound and effective risk management and does not encourage risk-taking which is inconsistent with the risk profiles, rules or instruments of incorporation of the <u>UCITS AIFs</u> <del>they</del> <u>that the management company manages</u> ;
Art. 14b(1)(b) UCITS Directive vs. Par. (1)(b) Annex II AIFMD	the remuneration policy is in line with the business strategy, objectives, values and interests of the <u>AIFM management company</u> and the <u>UCITS AIFs that it manages</u> <del>or</del> <u>and of the investors of in such UCITS AIFs</u> , and includes measures to avoid conflicts of interest;
Art. 14b(1)(c) UCITS Directive vs. Par. (1)(c) Annex II AIFMD	the remuneration policy is adopted by the management body of the <u>AIFM management company</u> , in its supervisory function, <u>and that body adopts, and and periodically reviews at least annually</u> , the general principles of the remuneration policy and is responsible for, <u>and oversees, its their implementation</u> ; <u>the tasks referred to in this point shall be undertaken only by members of the management body who do not perform any executive functions in the management company concerned and who have expertise in risk management and remuneration</u> ;
Art. 14b(1)(d) UCITS Directive vs. Par. (1)(d) Annex II AIFMD	the implementation of the remuneration policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for remuneration adopted by the management body in its supervisory function;
Art. 14b(1)(e) UCITS Directive vs. Par. (1)(e) Annex II AIFMD	staff engaged in control functions are compensated in accordance with the achievement of the objectives linked to their functions, independently of the performance of the business areas <u>that they control</u> ;
Art. 14b(1)(f) UCITS Directive vs. Par. (1)(f) Annex II AIFMD	the remuneration of the senior officers in the risk management and compliance functions is directly overseen by the remuneration committee, <u>where such a committee exists</u> ;
Art. 14b(1)(g) UCITS Directive vs. Par. (1)(g) Annex II AIFMD	where remuneration is <del>performance</del> <u>performance-related</u> , the total amount of remuneration is based on a combination of the assessment <del>of as to</del> <u>the performance of the individual and of the</u>

	business unit or <u>UCITSAIF</u> concerned and <del>of as to their risks and of</del> the overall results of the <del>AIFM</del> management company, and when assessing individual performance, <u>taking into account</u> financial as well as <del>and</del> non-financial criteria <del>are taken into account</del> ;
Art. 14b(1)(h) UCITS Directive vs. Par. (1)(h) Annex II AIFMD	<del>the assessment of performance is set in a multi-year framework appropriate to the life-cycle</del> holding period recommended to the <u>investors</u> of the <u>UCITSAIFs</u> managed by the <del>AIFM</del> management company in order to ensure that the assessment process is based on <u>the longer-longer-term</u> performance of the UCITS and its investment risks and that the actual payment of performance-based components of remuneration is spread over <del>a the same period which takes account of the redemption policy of the AIFs it manages and their investment risks</del> ;
Art. 14b(1)(i) UCITS Directive vs. Par. (1)(i) Annex II AIFMD	guaranteed variable remuneration is exceptional, occurs only in the context of hiring new staff and is limited to the first year <u>of engagement</u> ;
Art. 14b(1)(j) UCITS Directive vs. Par. (1)(j) Annex II AIFMD	fixed and variable components of total remuneration are appropriately balanced and the fixed component represents a sufficiently high proportion of the total remuneration to allow the operation of a fully flexible policy; on variable remuneration components, including the possibility to pay no variable remuneration component;
Art. 14b(1)(k) UCITS Directive vs. Par. (1)(k) Annex II AIFMD	payments related to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure;
Art. 14b(1)(l) UCITS Directive vs. Par. (1)(l) Annex II AIFMD	the measurement of performance used to calculate variable remuneration components or pools of variable remuneration components includes a comprehensive adjustment mechanism to integrate all relevant types of current and future risks;
Art. 14b(1)(m) UCITS Directive vs. Par. (1)(m) Annex II AIFMD	subject to the legal structure of the <u>UCITSAIF</u> and its <u>fund rules</u> or instruments of incorporation, a substantial portion, and in any event at least 50 %, of any variable remuneration <u>component</u> consists of units <del>or shares</del> of the <u>UCITSAIF</u> concerned, <del>or</del> equivalent ownership interests, or share-linked instruments or equivalent non-cash instruments <u>with equally effective incentives as any of the instruments referred to in this point</u> , unless the management of <u>the UCITSAIFs</u> accounts for less than 50 % of the total portfolio managed by the <del>AIFM</del> management company, in which case the

	<p>minimum of 50 % does not apply.</p> <p>The instruments referred to in this point shall be subject to an appropriate retention policy designed to align incentives with the interests of the <u>AIFM management company</u> and the <u>UCITS AIFs</u> that it manages and the investors of such <u>UCITS AIFs</u>. Member States or their competent authorities may place restrictions on the types and designs of those instruments or ban certain instruments as appropriate. This point shall be applied to both the portion of the variable remuneration component deferred in line with point (n) and the portion of the variable remuneration component not deferred;</p>
Art. 14b(1)(n) UCITS Directive vs. Par. (1)(n) Annex II AIFMD	<p>a substantial portion, and in any event at least 40 %, of the variable remuneration component, is deferred over a period which is appropriate in view of the <del>life-cycle and redemption policy</del><u>holding period recommended to the investors</u> of the <u>UCITS AIF</u> concerned and is correctly aligned with the nature of the risks of the <u>UCITS AIF</u> in question.</p> <p>The period referred to in this point shall be at least three <del>to 5</del> years <del>unless the life-cycle of the AIF concerned is shorter</del>; remuneration payable under deferral arrangements vests no faster than on a pro-rata basis; in the case of a variable remuneration component of a particularly high amount, at least 60 % of the amount <del>is</del> <u>shall be</u> deferred;</p>
Art. 14b(1)(o) UCITS Directive vs. Par. (1)(o) Annex II AIFMD	<p><u>the</u> variable remuneration, including the deferred portion, is paid or vests only if it is sustainable according to the financial situation of the <u>AIFM management company</u> as a whole, and justified according to the performance of the business unit, the <u>UCITS AIF</u> and the individual concerned.</p> <p>The total variable remuneration shall generally be considerably contracted where subdued or negative financial performance of the <u>AIFM management company</u> or of the <u>AIF-UCITS</u> concerned occurs, taking into account both current compensation and reductions in payouts of amounts previously earned, including through malus or clawback arrangements;</p>
Art. 14b(1)(p) UCITS Directive vs. Par. (1)(p) Annex II AIFMD	<p>the pension policy is in line with the business strategy, objectives, values and long-term interests of the <u>AIFM management company</u> and the <u>UCITS AIFs</u> that it manages.</p> <p>If the employee leaves the <u>AIFM management company</u> before retirement, discretionary pension benefits shall be held by the</p>

	<del>AIFM</del> management company for a period of <del>5</del> -five years in the form of instruments defined in point (m). In the case of an employee reaching retirement, discretionary pension benefits shall be paid to the employee in the form of instruments defined in point (m), subject to a <del>5</del> -five-year retention period;
Art. 14b(1)(q) UCITS Directive vs. Par. (1)(q) Annex II AIFMD	staff are required to undertake not to use personal hedging strategies or remuneration- and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements;
Art. 14b(1)(r) UCITS Directive vs. Par. (1)(r) Annex II AIFMD	variable remuneration is not paid through vehicles or methods that facilitate the avoidance of the requirements <del>of</del> <u>laid down in</u> this Directive.
Art. 14b(2) UCITS Directive (no correspondent under the AIFMD)	<u>In accordance with Article 35 of Regulation (EU) No 1095/2010, ESMA may request information from competent authorities on the remuneration policies and practices referred to in Article 14a of this Directive.</u>  <u>ESMA shall, in close cooperation with EBA, include in its guidelines on remuneration policies provisions on how different sectoral remuneration principles, such as those set out in Directive 2011/61/EU of the European Parliament and of the Council and in Directive 2013/36/EU of the European Parliament and of the Council, are to be applied where employees or other categories of personnel perform services subject to different sectoral remuneration principles.</u>
Art. 14b(3) UCITS Directive vs. Par. (2) Annex II AIFMD	The principles set out in paragraph 1 shall apply to <del>remuneration any benefit</del> of any type paid by the <del>AIFM</del> management company, to any amount paid directly by the <del>UCITS</del> AIF itself, including <del>carried interest</del> performance fees, and to any transfer of units or shares of the <del>UCITS</del> AIF, made <del>to</del> for the benefits of those categories of staff, including senior management, risk takers, control functions and any employee receiving total remuneration that <del>takes them into the same</del> falls into the remuneration bracket <del>as</del> of senior management and risk takers, whose professional activities have a material impact on their risk profile or the risk profiles of the <del>UCITS</del> AIF that they manage.
Art. 14b(4) UCITS Directive vs. Par. (3) Annex II AIFMD	<del>AIFMs</del> Management companies that are significant in terms of their size or <del>of</del> the size of the <del>UCITS</del> AIFs they manage, their internal organisation and the nature, <del>the</del> scope and <del>the</del> complexity of their activities shall establish a remuneration committee. The remuneration committee shall be constituted in a way that enables it

	<p>to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk.</p> <p>The remuneration committee <u>that is, where appropriate, set up in accordance with the ESMA guidelines referred to in Article 14a(4)</u> shall be responsible for the preparation of decisions regarding remuneration, including those which have implications for the risk and risk management of the <u>AIFMmanagement company</u> or the <u>UCITS AIF</u> concerned and which are to be taken by the management body in its supervisory function. The remuneration committee shall be chaired by a member of the management body who does not perform any executive functions in the <u>AIFMmanagement company</u> concerned. The members of the remuneration committee shall be members of the management body who do not perform any executive functions in the <u>AIFMmanagement company</u> concerned.</p> <p><u>If employee representation on the management body is provided for by national law, the remuneration committee shall include one or more employee representatives. When preparing its decisions, the remuneration committee shall take into account the long-term interest of investors and other stakeholders and the public interest.</u></p>
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## 8.2 Annex II

### Summary of questions

**Q1:** In this consultation paper ESMA proposes an approach on proportionality which is in line with the AIFMD Remuneration Guidelines and allows for the disapplication of certain requirements on an exceptional basis and taking into account specific facts. Notwithstanding this, ESMA is interested in assessing the impact from a general perspective and more precisely in terms of costs and administrative burden that a different approach would have on management companies. For this reason, management companies are invited to provide ESMA with information and data on the following aspects:

- 1) All management companies (i.e. those that hold a separate AIFMD licence and those that do not) are invited to provide details on the following:**
  - a) compliance impacts and costs (one-off and ongoing costs, encompassing technological/ IT costs and human resources), and**
  - b) difficulties in applying in any circumstances the remuneration principles that could otherwise be disapplied according to the provisions under Section 7.1 of the draft UCITS Remuneration Guidelines (Annex IV to this consultation paper).**
- 2) Management companies that also hold an AIFMD licence and benefit from the disapplication of certain of the remuneration rules under the AIFMD Remuneration Guidelines are asked to provide an estimate of the compliance costs in absolute and relative terms and to identify impediments resulting from their nature, including their legal form, if they were required to apply, for the variable remuneration of identified staff:**
  - a) deferral arrangements (in particular, a minimum *deferral period* of three years);**
  - b) retention;**
  - c) the pay out in instruments; and**
  - d) malus (with respect to the deferred variable remuneration).**

Wherever possible, the estimated impact and costs should be quantified, supported by a short explanation of the methodology applied for their estimation and provided separately, if possible, for the four listed aspects.

**Q2: Do you agree with the proposal to set out a definition of “performance fees” and with the proposed definition? If not, please explain the reasons why and provide an alternative definition supported by a justification.**

**Q3: Do you see any overlap between the proposed definition of ‘supervisory function’ in the UCITS Remuneration Guidelines and the definition of ‘management body’ in the UCITS V Level 1 text? If yes, please provide details and suggest how the definition of ‘supervisory function’ should be amended in the UCITS V Guidelines.**

**Q4: Please explain how services subject to different sectoral remuneration principles are performed in practice. E.g. is there a common trading desk/an investment firm providing portfolio management services to UCITS, AIFs and/or individual portfolios of investments? Please provide details on how these services are operated.**

**Q5: Do you consider that the proposed ‘pro rata’ approach would raise any operational difficulties? If yes, please explain why and provide an alternative solution.**

**Q6: Do you favour also the proposed alternative approach according to which management companies could decide to voluntarily opt for the sectoral remuneration rules which are deemed more effective in terms of avoiding excessive risk taking and ensuring risk alignment and apply them to all the staff performing services subject to different sectoral remuneration rules? Please explain the reasons behind your answer.**

**Q7: Do you agree that the performance of ancillary services under Article 6(3) of the UCITS Directive or under Article 6(4) of the AIFMD by personnel of a management company or an AIFM should be subject to the remuneration principles under the UCITS Directive or AIFMD, as applicable? Or do you consider that that MiFID ancillary services do not represent portfolio/risk management types of activities (Annex I of the AIFMD) nor investment management activities (Annex II of the UCITS Directive) and should not be covered by the rules under Article 14b of the UCITS Directive and Annex II of the AIFMD which specifically refer to the UCITS/AIFs that a UCITS/AIFM manages? Please explain the reasons of your response.**

**Q8: Do you agree with the proposal to look at individual entities for the purpose of the payment in instruments of at least 50% of the variable remuneration or consider that it would risk favouring the asset managers with a bigger portfolio of UCITS assets under management? Should you disagree, please propose an alternative approach and provide an appropriate justification.**

**Q9: Do you consider that there is any specific need to include some transitional provisions relating to the date of application of the UCITS Remuneration**



**Guidelines? If yes, please provide details on which sections of the guidelines would deserve any transitional provisions and explain the reasons why, also highlighting the additional costs implied by the proposed date of application. Please be as precise as possible in your answer in order for ESMA to assess the merit of your needs.**

**Q10: Do you agree with the assessment of costs and benefits above for the proposal on proportionality? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs that the proposal would imply.**

**Q11: Do you agree with the assessment of costs and benefits above for the proposal on the application of different sectoral rules to staff? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs that the proposal would imply.**

## 8.3 Annex III

### Cost-benefit analysis

#### 1. Introduction

1. The UCITS Directive and its implementing measures set out a comprehensive framework for the regulation of UCITS within Europe. The UCITS Directive was amended most recently by the UCITS V Directive which introduced new rules on UCITS depositaries, remuneration and sanctions.
2. Following that amendment, Article 14a(4) of the UCITS Directive provides that ESMA shall issue guidelines addressed to competent authorities or financial market participants concerning the application of the remuneration principles set out under Article 14b of the UCITS Directive.
3. The remuneration principles set out under the UCITS Directive are broadly in line with those under the AIFMD on which ESMA already issued guidelines (AIFMD Remuneration Guidelines). Therefore, when developing the proposed draft guidelines under the UCITS Directive, ESMA started from the text of the AIFMD Remuneration Guidelines and adapted it to the specificities of the UCITS framework, also taking into account the differences between the AIFMD and UCITS V Level 1 texts.
4. This consultation paper sets out proposals for the guidelines required under the UCITS V Directive which relate to the remuneration principles set out under Article 14b of the UCITS Directive. These principles cover topics such as: (i) the governance of remuneration, (ii) requirements on risk alignment and (iii) disclosure of remuneration.
5. In preparing this consultation paper, ESMA consulted with the Consultative Working Group (CWG) of ESMA's Investment Management Standing Committee (IMSC), in particular on the proportionate application of the remuneration rules. The input provided by the CWG was useful for the purpose of this draft cost-benefit analysis (CBA) as it allowed, inter alia, views to be gathered on the various approaches that may be envisaged when applying the relevant provisions of the UCITS Directive.
6. For the purposes of this draft CBA ESMA carried out a mapping exercise among national competent authorities (NCAs) to gather data on the approaches proposed on (i) proportionality and (ii) the application of different sectoral rules to staff (see sections 7 and 8 below).
7. This draft CBA is mostly qualitative in nature. However, ad hoc questions have been introduced in the text below in order to elicit market participants' input on the quantitative impact of the proposals. Should relevant data be received through the consultation process, ESMA will take it into account when finalising its UCITS Remuneration Guidelines and will include it in the CBA accompanying the final report.

## **2. Policy objective**

8. The UCITS remuneration rules are intended to protect the interests of UCITS investors by ensuring that the remuneration of risk takers within management companies are subject to appropriate governance requirements and the interests of these risk takers are aligned with those of the management companies and the UCITS they manage. These rules should be applied consistently across Europe.
9. The UCITS Remuneration Guidelines aim to promote the objectives of the UCITS Directive and, by extension, those of the Commission Recommendation of 2009. They should contribute to the creation of a level playing field across Member States, which will help ensure that the risks tackled by the guidelines are done so in a harmonised way and there is reduced scope for regulatory arbitrage (e.g. a management company choosing to move its activities to a jurisdiction with a more flexible approach) which could hamper the key objectives of the UCITS Directive.

## **3. Baseline scenario**

10. The baseline scenario for this CBA would be the application of the requirements in the Level 1 Directive (i.e. the provisions in Article 14b of the UCITS Directive) without any further guidance. This would in effect be more of a principles-based approach, leaving discretion to management companies to determine how best to apply the high-level requirements to their businesses. This could lead to a lack of harmonisation in the application of the provisions of the Level 1 Directive across the UCITS industry.

## **4. Technical options**

11. The following options were identified and analysed by ESMA to address the policy objectives referred to above and provide guidance on the application of the rules under Article 14b of the UCITS Directive.
12. In identifying the options set out below and choosing the preferred ones, ESMA was guided by the relevant UCITS Directive rules.
13. To the extent that, in line with the steer given to ESMA by the co-legislators under recital 9 of the UCITS V Directive<sup>16</sup>, the UCITS Remuneration Guidelines should broadly reflect the content of the AIFMD Remuneration Guidelines, this section focuses on the options that were available on the two major issues on which ESMA either had to provide additional guidance as compared to the AIFMD Remuneration Guidelines (Guidelines on the application of different sectoral rules – Section 9 of the draft UCITS Remuneration Guidelines) or considered a possible departure from the

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<sup>16</sup> Recital 9 of the UCITS V Directive states that “ESMA’s guidelines on remuneration policies and practices should, where appropriate, be aligned, to the extent possible, with those for funds regulated under Directive 2011/61/EU of the European Parliament and of the Council”.

content of the AIFMD Remuneration Guidelines (Guidelines on proportionality – Section 7 of the draft UCITS Remuneration Guidelines).

#### 4.1. Proportionality

<b>Policy Objective</b>	According to Article 14b of the UCITS Directive, the remuneration principles are to be applied taking into account the size, internal organisation and the nature, scope and complexity of the management companies' activities.
<b>Baseline scenario</b>	No further guidance would be provided through the guidelines on how to apply the proportionality principle spelled out under the "Policy Objective" above.
<b>Option 1</b>	<p>The UCITS Remuneration Guidelines would provide that remuneration principles are applicable to all management companies and proportionality may not lead to any disapplication of any of the requirements. This means that the specific minima set out in Article 14b of the UCITS Directive (e.g. the minimum deferral of 40 to 60% of variable remuneration) should never be disapplied. Management companies should in any case apply at least the minima criteria set out therein and, where appropriate, apply more strict criteria.</p> <p>The AIFMD Remuneration Guidelines – which currently provide for the possibility to disapply certain of the AIFMD remuneration principles under the specific conditions – would be amended in order to align them with the UCITS Remuneration Guidelines and provide that proportionality may not lead to any disapplication of any of the remuneration requirements.</p>
<b>Option 2</b>	The UCITS Remuneration Guidelines would provide that – in line with the approach followed under the AIFMD Remuneration Guidelines – proportionality may lead, on an exceptional basis and taking into account specific facts, to the disapplication of some requirements under certain specific conditions and limits.
<b>Option 3</b>	The UCITS Remuneration Guidelines would provide that remuneration principles are applicable to all management companies and proportionality may not lead to any disapplication of any of the requirements. This means that the specific minima set out in Article 14b of the UCITS Directive (e.g. the minimum deferral of 40 to 60% of variable remuneration) should never be disapplied. Management companies should in any case apply at least the minima criteria set out therein and, where appropriate,

	<p>apply more strict criteria.</p> <p>Disapplication of certain of the AIFMD remuneration principles would continue to be allowed under the specific conditions spelled out under the AIFMD Remuneration Guidelines.</p>
<b>Preferred Option</b>	<p>ESMA decided to consult on option 2 and discarded options 1 and 3. The baseline scenario was also discarded as it would not have provided any harmonisation on how to apply proportionality in relation to the remuneration principles. This could have led to an inconsistent level of investor protection across Europe.</p> <p>Option 3 was discarded as it would have introduced a misalignment of rules across the asset management sector which would have been problematic for the application of the rules and also contrary to the desire of the co-legislators to ensure an alignment of the remuneration rules applicable to UCITS and AIFMs.</p> <p>ESMA preferred option 2 as it is in line with the approach followed under the AIFMD Remuneration Guidelines. Thus, option 2 is the option which would ensure the lesser impact on both asset managers and supervisory authorities which could leverage on the experience gained under the AIFMD framework on the application of proportionality. Indeed, based on the outcome of the mapping of the data available at national level on proportionality (see section 7 of this draft CBA), it appears that in those jurisdictions where data are available on the use of the possibility to disapply certain remuneration rules under the AIFMD Remuneration Guidelines, most UCITS management companies also holding an AIFM licence did rely on the possibility to disapply certain rules under the AIFMD. Therefore, prohibiting the possibility to disapply any of the rules would create potentially considerable impacts on AIFMs, including those holding a separate UCITS licence which would be prohibited from disapplying any of the requirements also under UCITS Remuneration Guidelines.</p>

#### 4.2. Application of different sectoral rules

<b>Policy Objective</b>	The UCITS Directive requests that ESMA include in its guidelines on remuneration policies guidance on how different sectoral remuneration principles are to be applied where staff performs
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services subject to different sectoral remuneration principles.	
<b>Baseline scenario</b>	No further guidance would be provided through the guidelines on how different sectoral remuneration principles are to be applied where staff performs services subject to different sectoral remuneration principles.
<b>Option 1</b>	The sectoral remuneration principles (CRD IV, AIFMD and UCITS Directive) would have to be applied to staff on a pro rata basis based on objective criteria.
<b>Option 2</b>	The pro rata criterion described under option 1 would be accompanied by an alternative option under which it would be allowed to apply to staff performing services subject to different sectoral principles those principles which are deemed more effective for achieving the outcomes of discouraging excessive risk taking and aligning the interest of the relevant individuals with those of the investors in the funds they manage.
<b>Preferred Option</b>	<p>ESMA decided to consult on option 2 and discarded option 1. The baseline scenario was also discarded as it would not have complied with the explicit mandate granted to ESMA under the Level 1 provisions on the topics to be covered in the UCITS Remuneration Guidelines. Moreover, this would have led to inconsistent approaches across Europe in relation to staff performing services subject to different sectoral remuneration principles.</p> <p>ESMA preferred option 2 as it provides some flexibility by setting out two alternative approaches, while at the same time ensuring an appropriate level of investor protection to the extent that the approach which is additional in option 2 (as compared to option 1) requires that the rules which are more effective in discouraging excessive risk taking are applied. Option 1 would have been less cost effective as it would have set a fixed rule, while the alternative approach set out under option 2 may save implementation costs for those firms that already voluntarily follow this approach in practice.</p> <p>In elaborating the two options, ESMA informed its views also by taking into account the outcome of the mapping of the data available at national level on staff subject to different sectoral rules (see section 7 of this draft CBA).</p>

## 5. Assessment of the impact of the various options

### 5.1. Proportionality

Option 1	Qualitative description
<b>Benefits</b>	<p>Clarifications that proportionality cannot lead to the disapplication of any of the rules on remuneration under the UCITS Directive or the AIFMD would set appropriate standards in terms of investor protection (including retail investors as regards UCITS). Indeed, the application of the minimum standards set out under the UCITS Directive and the AIFMD would ensure a better alignment of the interests of risk takers with those of the managers for which they act and, ultimately, with those of the investors in the relevant funds that they manage.</p> <p>This option would ensure an alignment between the provisions under the AIFMD Remuneration Guidelines and the UCITS Remuneration Guidelines.</p>
<b>Costs to regulator and compliance costs</b>	<p>While no detailed data are available at this stage<sup>17</sup>, one-off and ongoing costs to certain competent authorities and asset managers are expected to arise from the prohibition to disapply any of the remuneration requirements under both the UCITS Directive and the AIFMD. This is particularly the case for those UCITS management companies (and their supervisors) also holding a separate AIFMD licence which are allowed to disapply certain of these rules in line with the provisions of the AIFMD Remuneration Guidelines.<sup>18</sup> Moreover, these costs may be more relevant to those AIFMs currently disapplying all of the requirements that may be disapplied according to the AIFMD Remuneration Guidelines.<sup>19</sup></p> <p>The costs under this option are expected to be substantially higher than those under options 2 and 3.</p>

Option 2	Qualitative description
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<sup>17</sup> See tables 5 and 6 under section 7 below.

<sup>18</sup> See table 2 under section 7 below.

<sup>19</sup> See table 4 under section 7 below.

<b>Benefits</b>	<p>The benefits in terms of investor protection highlighted above under option 1 are not expected from this option.</p> <p>This option would ensure an alignment between the provisions under the AIFMD Remuneration Guidelines and the UCITS Remuneration Guidelines and help foster a harmonised approach throughout Europe.</p>
<b>Costs to regulator and compliance costs</b>	<p>To the extent that this option would mirror the approach followed under the AIFMD Remuneration Guidelines, no one-off and ongoing compliance costs to both competent authorities and asset managers are expected to arise from it.</p>

Option 3		Qualitative description
<b>Benefits</b>		<p>Clarifications that proportionality cannot lead to the disapplication of any of the rules on remuneration under the UCITS Directive would set appropriate standards in terms of protection of retail investors. However, contrary to option 1, the same outcome would not be achieved for investors investing into funds falling under the AIFMD.</p> <p>Moreover, contrary to options 1 and 2, this option would introduce a misalignment between the provisions under the AIFMD Remuneration Guidelines and the UCITS Remuneration Guidelines.</p>
<b>Costs to regulator and compliance costs</b>		<p>To the extent that this option would not change the approach followed under the AIFMD Remuneration Guidelines, no one-off and ongoing costs to both competent authorities and AIFMs are expected to arise from it. However, certain one-off and ongoing costs to certain competent authorities and UCITS management companies are expected to arise from the prohibition to disapply any of the remuneration requirements under the UCITS Directive.</p> <p>Such costs are expected to be higher than costs under option 2, but lower than costs under option 1, even if the misalignment between the requirements under the UCITS Remuneration Guidelines and the AIFMD Remuneration Guidelines might in itself create additional compliance costs.</p>



**Q10: Do you agree with the assessment of costs and benefits above for the proposal on proportionality? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs that the proposal would imply.**

## 5.2. Application of different sectoral rules

Option 1	Qualitative description
<b>Benefits</b>	The pro rata criterion has the advantage of being based on simple and objective elements such as the time spent on the performance of the different services to which different rules apply. By applying the different rules based on the activities performed, the relevant level of investor protection targeted under each piece of applicable legislation would be ensured.
<b>Costs to regulator and compliance costs</b>	<p>Limited one-off and ongoing compliance costs are expected to arise from the application of the pro rata criterion. Indeed, even in the absence of such a provision being clearly spelled out, firms are expected to apply remuneration rules based on the activities performed by each relevant staff member. Therefore, they should already be in a position to determine which activities are performed under each sectoral rules.</p> <p>Additional one-off and ongoing monitoring costs are more likely to arise for supervisors who are not necessarily supervising this element for the time being in the context of their supervision of asset managers, credit institutions and investment firms.</p>

Option 2	Qualitative description
<b>Benefits</b>	The same benefits highlighted above for option 1 are expected from this option. Moreover, the possibility under this option to adopt a criterion which is alternative to the 'pro rata' one should introduce more flexibility while at the same time ensuring an equivalent level of investor protection.
<b>Costs to regulator and compliance costs</b>	One-off and ongoing costs are expected to be less relevant than under option 1 for both supervisors and supervised entities. This is linked to the fact that supervised entities could voluntarily decide to apply – for instance – CRD IV rules to staff performing activities subject to different sectoral legislation, thus reducing compliance costs within entities such as those that are part of a

group.

**Q11: Do you agree with the assessment of costs and benefits above for the proposal on the application of different sectoral rules to staff? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs that the proposal would imply.**

## **6. Mapping of data available at national level in relation to the possible approaches on proportionality**

14. In order to inform its decision on the approach to take on proportionality under the UCITS and AIFMD Remuneration Guidelines, ESMA submitted a number of questions to NCAs in order to gather data available at national level.

15. The relevant questions are set out in the tables below which include the data received from the relevant NCA for each Member State. Unless stated otherwise, the data reflect the situation as at 30 March 2015.

Table 1

<b>Question 1</b>			<i>How many UCITS management companies out of those authorised in your jurisdiction also hold a separate AIFMD licence?</i>
	<i>Authorised UCITS management companies</i>		<i>Holding a separate AIFMD licence</i>
<b>Estonia</b>	5*		None <sup>20</sup>
<b>Sweden</b>	43*		18
<b>Spain</b>	79		55 <sup>21</sup>
<b>Croatia</b>	18		11
<b>Greece</b>	16*		2
<b>Portugal</b>	21*		11

<sup>20</sup> 1 was in the process of authorization for an additional AIFM licence.

<sup>21</sup> 55 management companies also manage non-UCITS funds. AIFMD was transposed into Spanish law on November 2014. An additional provision states that AIFM were required to provide a declaration of compliance with the Spanish law to the national authority (CNMV) within 3 months. Declarations have to get approved in order to grant the license to AIFM and include them into the national register. As of the closing date of the mapping exercise (30 March 2015) declarations received were being reviewed and no licenses were granted yet. Therefore, figures included in the table above for Spain were obtained based on the distinction between 'UCITS' and 'non-UCITS' funds.

<b>Denmark</b>	13*	10
<b>Latvia</b>	12*	4
<b>Luxembourg<sup>22</sup></b>	206	111
<b>Germany</b>	52*	32
<b>Belgium</b>	7	5
<b>Austria</b>	25*	19
<b>Ireland</b>	78	24
<b>Czech Republic</b>	8*	8
<b>United Kingdom</b>	159*	Circa 90
<b>France</b>	316*	142
<b>Malta</b>	14*	5 <sup>23</sup>
<b><u>TOTAL:</u></b>	<b>1,072</b>	<b>547</b>

\*Source: data available as at 5 June 2015 in the UCITS management companies register available at the ESMA website.

*Table 2*

<b>Question 2</b>	<i>Among the UCITS management companies also holding an AIFMD licence, how many of them avail themselves of the possibility to disapply (some of) the remuneration requirements as foreseen under the AIFMD Guidelines?</i>
<b>Estonia</b>	N/A
<b>Sweden</b>	None <sup>24</sup>
<b>Spain</b>	N/A <sup>25</sup>

<sup>22</sup> Data as of 31/12/2014.

<sup>23</sup> Data as at 1 June 2015.

<sup>24</sup> 2 applications were under process as of 30 March 2015.

<sup>25</sup> Information not available as at 30 March 2015 (see footnote 21).

<b>Croatia</b>	All of them (11)
<b>Greece</b>	None
<b>Portugal</b>	N/A
<b>Denmark</b>	No data available
<b>Latvia</b>	None
<b>Luxembourg</b>	N/A – no data available
<b>Germany</b>	None
<b>Belgium</b>	4 <sup>26</sup>
<b>Austria</b>	11
<b>Ireland</b>	No data available
<b>Czech Republic</b>	7
<b>United Kingdom</b>	No data available <sup>27</sup>
<b>France</b>	73
<b>Malta</b>	All of them (5)
<b><u>TOTAL:</u></b>	<b>111</b>

*Table 3*

<b>Question 3</b>	<i>If in your jurisdiction the possibility to disapply any of the remuneration requirements under the AIFMD Guidelines is based on quantitative thresholds, please provide details.</i>
<b>Estonia</b>	No quantitative thresholds
<b>Sweden</b>	N/A

<sup>26</sup> These management companies avail themselves of the exemption from the obligation to set up a remuneration committee whenever such a committee is set up at group level pursuant to the Guidelines on sound remuneration policies under the AIFMD.

<sup>27</sup> This NCA issued specific guidance on the application of the AIFMD remuneration rules. This guidance covers the circumstances under which AIFMs might be able to apply proportionality to the remuneration provisions and it sets out certain quantitative thresholds.

<b>Spain</b>	No quantitative thresholds
<b>Croatia</b>	No quantitative thresholds <sup>28</sup>
<b>Greece</b>	N/A
<b>Portugal</b>	No quantitative thresholds
<b>Denmark</b>	The Danish remuneration regulation applicable to AIFMD-companies contains a de minimis threshold of up to DKK 100.000. According to this quantitative threshold smaller amounts of variable remuneration (of up to DKK 100.000) which does not encourage employees to excessive risk taking can be exempted from instrument, retention and deferral requirements if the management function in its supervisory function or the senior management assesses that exemption is appropriate. The threshold is absolute and cannot be exceeded. If an employee is remunerated more than DKK 100.000 in variable remuneration during the financial year all the remuneration requirements of the AIFMD have to be applied to the total variable remuneration. The Danish AIFMD remuneration regulation does not contain other possibilities to disapply remuneration requirements. On request, the companies should be able to demonstrate to the relevant NCA that the exempted smaller amounts of remuneration does not encourage the employees to excessive risk taking and that disapplication of instrument, retention and deferral requirements are appropriate.
<b>Latvia</b>	The use of instruments is required only in cases where the variable part of the remuneration is significant (i.e. >60% of the total annual remuneration).
<b>Luxembourg</b>	No quantitative thresholds
<b>Germany</b>	No quantitative thresholds
<b>Belgium</b>	<p>The relevant NCA could apply – by analogy – the quantitative thresholds that exist pursuant to article 62, § 2ter of the Belgian law on the legal status and supervision of investment firms.<sup>29</sup></p> <p>Pursuant to this article, a “small” investment firm (due to its internal organisation or due to the nature, the scope and the complexity of its activities) is exempted from setting up a remuneration committee if at</p>

<sup>28</sup> All the Croatian AIFMs are below the threshold stipulated in the AIFMD Remuneration Guidelines for the purpose of the establishment of a remuneration committee – their AuM is below EUR 1.25 billion and they have less than 50 employees, including those dedicated to the management of UCITS and providing investment services under Article 6(4) of the AIFMD

<sup>29</sup> As at 30 March 2015 these provisions were not applied to any specific case.

	<p>least two of the three following criteria are satisfied:</p> <ul style="list-style-type: none"> <li>- the average number of employees lower than 250 people over the full year concerned;</li> <li>- the balance sheet total equal or lower than 43.000.000 euros;</li> <li>- the net annual turnover equal or lower than 50.000.000 euros.</li> </ul>
<b>Austria</b>	Quantitative thresholds are either based on the size of the company (AIF assets under management, number of AIF managed, number of employees, number of delegations etc versus the respective industry median numbers) and/or the size of the bonus itself: EUR 30.000 or 25% of fixed remuneration serve as materiality threshold and are considered as too small for application of the pay-out requirements under section XII.IV of the AIFMD Remuneration Guidelines.
<b>Ireland</b>	No quantitative thresholds
<b>Czech Republic</b>	No quantitative thresholds
<b>United Kingdom</b>	<p>The relevant NCA has provided some guidance to AIFMs on how to interpret the application of the principle of proportionality. This guidance includes the following quantitative thresholds for the disapplication of certain remuneration rules:</p> <ul style="list-style-type: none"> <li>– <i>AIFMs which manage portfolios of AIFs that are unleveraged and have no redemption rights exercisable during a period of 5 years following the date of initial investment in each AIF: it is appropriate to disapply ‘Pay-out Process Rules’ if their assets under management (AuM) are <u>less than £5 billion</u>;</i></li> <li>– <i>AIFMs which manage portfolios of AIFs in other cases, including any assets acquired through the use of leverage: it is appropriate to disapply ‘Pay-out Process Rules’ if their assets under management (AuM) are <u>less than £1 billion</u>.<sup>30</sup></i></li> </ul>
<b>France</b>	The possibility to disapply some of the rules is based on an overall case-by-case analysis, which is based on the following criteria:

<sup>30</sup> The relevant guidance is available at the following address (see p. 5 ff.): <https://www.fca.org.uk/static/documents/finalised-guidance/fg14-02.pdf>.

	<ul style="list-style-type: none"><li>– size (e.g. less than 500 million EUR AuM),</li><li>– internal organization (e.g. 2/3 of the salary is fixed and maximum 1/3 of the salary is variable) and</li><li>– the nature, scope (e.g. less than 10% of AuM are AIFs) and</li><li>– complexity of their activities (e.g. applied investment strategies: index management, formula management, management linked to employee saving plans).</li></ul>																					
Malta	<p>The relevant NCA has established different thresholds for AIFMs whose portfolio of AIFs includes assets acquired through use of leverage and AIFMs whose portfolio of AIFs does not include leveraged assets. These thresholds are as follows:</p> <ul style="list-style-type: none"><li>– <i>Leveraged assets</i></li></ul> <table><tr><th>Value of Portfolio of AIFs</th><th>Pay-Out Process Rules</th><th>Remuneration Committee</th></tr><tr><td>Less than €100 million</td><td>Disapplied</td><td>Disapplied</td></tr><tr><td>Between €100 million and €1.25 billion</td><td>Disapplication could be considered on the grounds of proportionality</td><td>Disapplication could be considered on the grounds of proportionality</td></tr><tr><td>Over €1.25 billion</td><td>Full application of the ESMA Guidelines</td><td>Full application of the ESMA Guidelines</td></tr></table> <ul style="list-style-type: none"><li>– <i>Unleveraged assets</i></li></ul> <table><tr><th>Value of Portfolio of AIFs</th><th>Pay-Out Process Rules</th><th>Remuneration Committee</th></tr><tr><td>Less than €500 million</td><td>Disapplied</td><td>Disapplied</td></tr><tr><td>Between €500 million and €6 billion</td><td>Disapplication could be considered on the grounds of</td><td>Disapplication could be considered on the grounds of</td></tr></table>	Value of Portfolio of AIFs	Pay-Out Process Rules	Remuneration Committee	Less than €100 million	Disapplied	Disapplied	Between €100 million and €1.25 billion	Disapplication could be considered on the grounds of proportionality	Disapplication could be considered on the grounds of proportionality	Over €1.25 billion	Full application of the ESMA Guidelines	Full application of the ESMA Guidelines	Value of Portfolio of AIFs	Pay-Out Process Rules	Remuneration Committee	Less than €500 million	Disapplied	Disapplied	Between €500 million and €6 billion	Disapplication could be considered on the grounds of	Disapplication could be considered on the grounds of
Value of Portfolio of AIFs	Pay-Out Process Rules	Remuneration Committee																				
Less than €100 million	Disapplied	Disapplied																				
Between €100 million and €1.25 billion	Disapplication could be considered on the grounds of proportionality	Disapplication could be considered on the grounds of proportionality																				
Over €1.25 billion	Full application of the ESMA Guidelines	Full application of the ESMA Guidelines																				
Value of Portfolio of AIFs	Pay-Out Process Rules	Remuneration Committee																				
Less than €500 million	Disapplied	Disapplied																				
Between €500 million and €6 billion	Disapplication could be considered on the grounds of	Disapplication could be considered on the grounds of																				

		proportionality	proportionality
	<b>Over €6 billion</b>	Full application of the ESMA Guidelines	Full application of the ESMA Guidelines

Table 4

<b>Question 4</b>	<p><i>Among the UCITS management companies referred to under Q2, please provide:</i></p> <p>(i) <i>the number of those disapplying all the remuneration requirements that may be disappplied according to the AIFMD Guidelines (i.e. those under Section XII.IV of the Guidelines [variable remuneration in instruments, retention, deferral, ex post incorporation of risk for variable remuneration]), and [...]</i></p>		
<b>Estonia</b>	None		
<b>Sweden</b>	None		
<b>Spain</b>	N/A		
<b>Croatia</b>	All of them (11)		
<b>Greece</b>	N/A		
<b>Portugal</b>	N/A		
<b>Denmark</b>	No data available		
<b>Latvia</b>	N/A		
<b>Luxembourg</b>	N/A		
<b>Germany</b>	None		
<b>Belgium</b>	None		
<b>Austria</b>	<p>Most of the management companies either apply all requirements of Section XII.IV of the AIFMD Remuneration Guidelines or none. Currently 8 out of the 19 AIFM/UCITS management companies fully apply all requirements.</p>		



<b>Ireland</b>	N/A
<b>Czech Republic</b>	7
<b>United Kingdom</b>	No data available
<b>France</b>	Five requirements can be disapplied (four are linked to the pay-out process and one concerns the establishment of a remuneration committee). The 72 management companies mentioned in the response to question 2 disapply all these five requirements. <sup>31</sup>
<b>Malta</b>	All of them (5)
	<p><i>Among the UCITS management companies referred to under Q2, please provide:</i></p> <p>[...]</p> <p>(ii) <i>the number of those disapplying only some of these requirements</i></p>
<b>Estonia</b>	None
<b>Sweden</b>	None
<b>Spain</b>	N/A
<b>Croatia</b>	None
<b>Greece</b>	N/A
<b>Portugal</b>	N/A
<b>Denmark</b>	No data available
<b>Latvia</b>	N/A
<b>Luxembourg</b>	N/A
<b>Germany</b>	None
<b>Belgium</b>	None

<sup>31</sup> Beyond that, and only as far as individuals are not identified as risk takers, a partial disapplication can be granted on an individual basis (an additional evaluation needs to be undertaken).

<b>Austria</b>	Some companies - even though they would have qualified as small and non-complex - apply the deferral requirement on a voluntary basis.
<b>Ireland</b>	N/A
<b>Czech Republic</b>	None
<b>United Kingdom</b>	No data available
<b>France</b>	N/A
<b>Malta</b>	None

Table 5

<b>Question 5</b>	<i>Based on the data provided in your answer to Q2, please provide an estimate of the direct costs to your competent authority arising from the prohibition to disapply any of the remuneration rules under the UCITS Directive. Please provide details on their one-off or ongoing component.</i>
<b>Estonia</b>	N/A
<b>Sweden</b>	Approximately 600 EUR for a one-off assessment, the ongoing costs may vary considerably depending on the number of applications.
<b>Spain</b>	No data available
<b>Croatia</b>	N/A
<b>Greece</b>	No data available
<b>Portugal</b>	N/A
<b>Denmark</b>	No data available
<b>Latvia</b>	N/A
<b>Luxembourg</b>	N/A
<b>Germany</b>	N/A
<b>Belgium</b>	None

<b>Austria</b>	N/A
<b>Ireland</b>	N/A
<b>Czech Republic</b>	The prohibition to disapply any of the remuneration rules under the UCITS Directive would generate extra costs for the relevant NCA (as a result of additional staff requirements). One-off costs would be related to necessary legislative changes (an amendment of the Act No. 240/2013 on Investment Companies and Investment Funds and relating decrees) whereas ongoing costs would have to be allocated on introduction of new internal rules, on-site and off-site supervision and enforcement.
<b>United Kingdom</b>	No data available
<b>France</b>	If a prohibition of disapplication called into question the hundreds of AIFM authorisation granted, a team of the relevant NCA consisting of approximately 40 persons would need to work at least 15 days per person for the review of the authorisation process. Additional costs would also appear due to the revision and disclosure of material recently issued in relation to the AIFMD Remuneration Guidelines.
<b>Malta</b>	The main cost to the relevant NCA arising from the prohibition to disapply any of the remuneration rules would be the additional human resources and man hours required to examine the setups and ensure that these remain compliant at all times. It is not envisaged that one off and ongoing supervisory costs would be significant, although one has to bear in mind that this would be an additional task for supervisory resources.

Table 6

<b>Question 6</b>	<i>Based on the AIFMD experience (i.e. data gathered in that context, if any), which is the estimated implementation cost (one-off and ongoing) by an investment manager to implement the remuneration rules under the UCITS Directive? To what extent can these costs be reduced by applying the principle of proportionality?</i>
<b>Estonia</b>	No data available. The relevant NCA does not expect these costs to be unreasonable or significant for the management company.
<b>Sweden</b>	No data available

<b>Spain</b>	No data available
<b>Croatia</b>	N/A
<b>Greece</b>	No data available
<b>Portugal</b>	N/A
<b>Denmark</b>	N/A
<b>Latvia</b>	N/A
<b>Luxembourg</b>	N/A
<b>Germany</b>	No data available
<b>Belgium</b>	No data available
<b>Austria</b>	No data available. The relevant NCA would expect both costs and efforts to be disproportionately high for the majority of the UCITS management companies because of their small size and small bonuses (on average).
<b>Ireland</b>	No data available
<b>Czech Republic</b>	Currently, every UCITS management company in the Czech Republic holds also an AIFMD licence (there is no management company holding UCITS license only). As a consequence all UCITS management companies apply the same remuneration rules as those required under the AIFMD and, therefore, a joint system of remuneration is applied to all relevant employees within one management company (no matter under which Directive (UCITS or AIFMD)). Excluding UCITS management companies from the possibility to apply the proportionality approach (and thus to adopt different remuneration systems within one company) would cause in particular implementation costs.
<b>United Kingdom</b>	The below estimates of costs for AIFMs from applying the AIFMD remuneration rules were prepared by the relevant NCA when consulting on the implementation of AIFMD:

	<b>Table 10: Costs for investment managers from applying the Remuneration Code</b>		
	<b>Costs</b>	<b>Incremental costs</b>	
		<b>One-off</b>	<b>Ongoing (annual)</b>
	For changing: • the way remuneration policies are set; • systems and controls; • additional data collection; • reporting; and • record keeping requirements.	£0 – £300,000	£0 – £50,000
	Issuing an annual remuneration statement	£0 – £100,000	£0 – £30,000
	Senior management board or committee time	NA	£0 – £24,000
	Enhanced risk management function	NA	£0 – £31,000
	Adjusting remuneration structures	£0 – £47,000	£0 – £50,000
	<b>Average of total costs</b>	<b>£7,000</b>	<b>£4,000</b>
	<b>Median</b>	<b>Minimal costs</b>	<b>Minimal costs</b>
<b>France</b>	If the UCITS Remuneration Guidelines remain close to the AIFMD Remuneration Guidelines, then implementation costs should be acceptable for all players. If the UCITS Remuneration Guidelines deviate strongly from the AIFMD Remuneration Guidelines, important costs will appear for all players (those applying the guidelines totally and those disapplying the allowed number of requirements). The costs are mainly linked to IT implementation/ transformation costs.		
<b>Malta</b>	Currently all the licensed AIFMs have satisfied the proportionality principles and have qualified to be exempt from the relevant requirements (e.g. on remuneration committee and payout process). Maltese UCITS management companies tend to be modest/ small in size. It is difficult for the relevant NCA to estimate the one-off implementation costs although it was mentioned that not distinguishing on the basis of scale, size and complexity would be deleterious on UCITS management companies and UCITS and in a worst case scenario they may tilt the scales to make them uneconomic/ non-viable.		

## 7. Mapping of data available at national level in relation to the possible approaches on the application of different sectoral rules to staff

16. In order to inform its decision on the approach to take on the application of different sectoral rules to staff under the UCITS and AIFMD Remuneration Guidelines, ESMA submitted a number of questions to NCAs in order to gather data available at national level.

17. The relevant questions are set out in the tables below which include the data received from the relevant NCA for each Member State. Unless stated otherwise, the data reflect the situation as at 30 March 2015.

Table 7

<b>Question 7</b> <i>How many asset managers out of those authorised in your jurisdiction are subsidiaries of an entity subject to the CRD? Please distinguish between</i>	
(i) <i>UCITS management companies</i>	
<b>Estonia</b>	5
<b>Sweden</b>	2
<b>Spain</b>	6 (out of 24 UCITS management companies)
<b>Croatia</b>	6
<b>Greece</b>	8 <sup>32</sup>
<b>Portugal</b>	3
<b>Denmark</b>	4
<b>Latvia</b>	9
<b>Luxembourg<sup>33</sup></b>	34
<b>Germany</b>	None
<b>Belgium</b>	2
<b>Austria</b>	23
<b>Ireland</b>	No data available
<b>Czech Republic</b>	None
<b>United Kingdom</b>	Circa 70 (including AIFMs) <sup>34</sup>

<sup>32</sup> 2 of them were under liquidation as at 30 March 2015.

<sup>33</sup> Data as at 31/12/2014.

<sup>34</sup> There are circa 70 AIFMs or UCITS management companies which are part of a group with at least an entity subject to CRD IV requirements within it.

<b>France</b>	56
<b>Malta</b>	1
<b><u>TOTAL:</u></b>	<b>159<sup>35</sup></b>
	<i>How many asset managers out of those authorised in your jurisdiction are subsidiaries of an entity subject to the CRD? Please distinguish between [...]</i>
	<i>(ii) AIFMs</i>
<b>Estonia</b>	None
<b>Sweden</b>	None
<b>Spain</b>	2 (out of 10 non-UCITS managers)
<b>Croatia</b>	None
<b>Greece</b>	None
<b>Portugal</b>	4
<b>Denmark</b>	None
<b>Latvia</b>	1
<b>Luxembourg<sup>36</sup></b>	9
<b>Germany</b>	27
<b>Belgium</b>	None
<b>Austria</b>	24
<b>Ireland</b>	No data available
<b>Czech Republic</b>	None
<b>United Kingdom</b>	Circa 70 (including UCITS management companies)
<b>France</b>	94

<sup>35</sup> Please note that the total does not include the United Kingdom as figures for this jurisdiction were provided in aggregate taking into account AIFMs and UCITS management companies.

<sup>36</sup> Data as at 31/12/2014.

<b>Malta</b>	None
<b><u>TOTAL:</u></b>	<b>161<sup>37</sup></b>
	<p><i>How many asset managers out of those authorised in your jurisdiction are subsidiaries of an entity subject to the CRD? Please distinguish between [...]</i></p> <p><i>(iii) entities authorised under both the UCITS Directive and AIFMD</i></p>
<b>Estonia</b>	None
<b>Sweden</b>	6
<b>Spain</b>	41 (out of 55 management companies also managing non-UCITS funds) <sup>38</sup>
<b>Croatia</b>	None
<b>Greece</b>	1
<b>Portugal</b>	9
<b>Denmark</b>	4
<b>Latvia</b>	1
<b>Luxembourg<sup>39</sup></b>	44
<b>Germany</b>	10
<b>Belgium</b>	3
<b>Austria</b>	19
<b>Ireland</b>	No data available
<b>Czech Republic</b>	5
<b>United Kingdom</b>	Circa 70 (including AIFMs or UCITS management companies)
<b>France</b>	53

<sup>37</sup> See comment under footnote 35 above.

<sup>38</sup> See footnote 27 above for an explanation on the reference to 'non-UCITS funds'.

<sup>39</sup> Data as at 31/12/2014.



<b>Malta</b>	None
<b><u>TOTAL:</u></b>	<b>196<sup>40</sup></b>

*Table 8*

<b>Question 8</b>	<i>How many asset managers have employees or other categories of personnel performing services subject to different sectoral remuneration principles (UCITS and/or AIFMD and/or CRD)? Please distinguish between</i>
	<i>(i) UCITS management companies [...]</i>
<b>Estonia</b>	7
<b>Sweden</b>	26
<b>Spain</b>	No data available
<b>Croatia</b>	11
<b>Greece</b>	No data available
<b>Portugal</b>	12
<b>Denmark</b>	4
<b>Latvia</b>	No data available
<b>Luxembourg</b>	No data available
<b>Germany</b>	No data available
<b>Belgium</b>	None
<b>Austria</b>	No data available
<b>Ireland</b>	No data available
<b>Czech Republic</b>	8
<b>United Kingdom</b>	No data available <sup>41</sup>

<sup>40</sup> See comment under footnote 35 above.

<b>France</b>	No data available
<b>Malta</b>	No data available
<b><u>TOTAL:</u></b>	<b>68</b>
	<i>How many asset managers have employees or other categories of personnel performing services subject to different sectoral remuneration principles (UCITS and/or AIFMD and/or CRD)? Please distinguish between [...]</i>
	<i>(ii) AIFMs</i>
<b>Estonia</b>	None
<b>Sweden</b>	18
<b>Spain</b>	Not available
<b>Croatia</b>	11
<b>Greece</b>	None
<b>Portugal</b>	4
<b>Denmark</b>	None
<b>Latvia</b>	No data available
<b>Luxembourg</b>	No data available
<b>Germany</b>	No data available
<b>Belgium</b>	No data available
<b>Austria</b>	No data available
<b>Ireland</b>	No data available
<b>Czech Republic</b>	8
<b>United Kingdom</b>	No data available <sup>42</sup>

<sup>41</sup> While the requested information was not available, the relevant NCA mentioned that there are 320 firms carrying out ancillary services under either AIFMD or UCITS Directive.

<sup>42</sup> See footnote 41 above.

<b>France</b>	No data available
<b>Malta</b>	No data available
<b><u>TOTAL:</u></b>	<b>41</b>

*Table 9*

<b>Question 9</b>	<i>How many entities perform investment management activities under delegation from a UCITS according to Article 13 of the UCITS Directive? Please distinguish between</i>
	<i>(i) AIFMs [...]</i>
<b>Estonia</b>	None
<b>Sweden</b>	4
<b>Spain</b>	1 <sup>43</sup>
<b>Croatia</b>	None <sup>44</sup>
<b>Greece</b>	No data available
<b>Portugal</b>	8
<b>Denmark</b>	None
<b>Latvia</b>	N/A
<b>Luxembourg</b>	No data available
<b>Germany</b>	No data available
<b>Belgium</b>	No data available
<b>Austria</b>	None <sup>45</sup>
<b>Ireland</b>	No data available

<sup>43</sup> See footnote 21 above.

<sup>44</sup> 6 UCITS management companies have delegated the function of internal audit on credit institutions. In all cases, credit institutions that perform the function of internal audit under delegation are within the same group as UCITS management companies.

<sup>45</sup> There are a few management delegations of UCITS to AIFMs, but only to those AIFM with an additional UCITS authorisation, so this should rather be seen as a delegation to a UCITS management company.

<b>Czech Republic</b>	None
<b>United Kingdom</b>	No data available
<b>France</b>	No data available
<b>Malta</b>	No data available
<b><u>TOTAL:</u></b>	<b>13</b>
	<i>How many entities perform investment management activities under delegation from a UCITS according to Article 13 of the UCITS Directive? Please distinguish between [...]</i>
	<i>(ii) entities subject to the CRD</i>
<b>Estonia</b>	2
<b>Sweden</b>	11
<b>Spain</b>	5
<b>Croatia</b>	None
<b>Greece</b>	4
<b>Portugal</b>	8
<b>Denmark</b>	None
<b>Latvia</b>	N/A
<b>Luxembourg</b>	No data available
<b>Germany</b>	No data available
<b>Belgium</b>	No data available
<b>Austria</b>	16 <sup>46</sup>
<b>Ireland</b>	No data available
<b>Czech Republic</b>	2

<sup>46</sup> This figure covers Austrian CRD entities only. The total amount of delegations is higher because there are some delegations to foreign CRD entities.

<b>United Kingdom</b>	No data available
<b>France</b>	No data available
<b>Malta</b>	No data available
<b><u>TOTAL:</u></b>	<b>48</b>

## 8.4 Annex IV

### Draft guidelines (UCITS Remuneration Guidelines)

## 1 Scope

### Who?

1. These guidelines apply to management companies as defined under Article 2(1)(b) of the UCITS Directive and competent authorities. They also apply to investment companies that have not designated a management company authorised pursuant to the UCITS Directive.<sup>47</sup>
2. UCITS having designated a management company authorised pursuant to the UCITS Directive are not subject to the remuneration principles established in the UCITS Directive, nor to these guidelines. However, the remuneration principles set out in the *Recommendation* are relevant to those UCITS, to the extent that they fall within the definition of 'financial undertaking' provided in paragraph 2.1 of the *Recommendation*. Annex I of these guidelines provides for a correlation table highlighting those principles of the *Recommendation* which are reflected in the UCITS Directive.

### What?

3. These guidelines apply in relation to the remuneration policies and practices for management companies and their identified staff. Annex II of these guidelines provides details on which guidelines apply to management companies as a whole and which apply to their identified staff only.

### When?

4. These guidelines apply from 18 March 2016.

## 2 Definitions

Unless otherwise specified, terms used in the Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) have the same meaning in these guidelines. In addition, the following definitions apply for the purposes of these guidelines:

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<sup>47</sup> The remuneration principles in Article 14a and 14b of the UCITS Directive apply *mutatis mutandis* to these investment companies, based on the provisions of Article 30 of the UCITS Directive.

<i>Recommendation</i>	Commission Recommendation 2009/384/EC of 30 April 2009 on remuneration policies in the financial services sector. <sup>48</sup>
<i>performance fees</i>	<p>a variable fee linked to the “performance of the UCITS”.</p> <p>The “performance of the UCITS” includes capital appreciation as well as any income linked to the UCITS’s assets (e.g. dividends). It may be assessed with reference to a target ‘performance’.</p> <p>A performance fee can be based on elements such as a share of the capital gains or the capital appreciation of the UCITS’ net asset value or any portion of the UCITS’ net asset value as compared to an appropriate index of securities or other measure of investment performance.</p> <p><i>Performance fees</i> are payments made directly by the management company or the UCITS itself for the benefit of <i>identified staff</i>.</p>
<i>identified staff</i>	categories of staff, including senior management, risk takers, <i>control functions</i> and any employee receiving total remuneration that falls into the <i>remuneration bracket</i> of senior management and risk takers, whose professional activities have a material impact on the management company’s risk profile or the risk profiles of the UCITS that it manages and categories of staff of the entity(ies) to which investment management activities have been delegated by the management company, whose professional activities have a material impact on the risk profiles of the UCITS that the management company manages.
<i>control functions</i>	staff (other than senior management) responsible for risk management, compliance, internal audit and similar functions within a management company (e.g. the CFO to the extent that he/she is responsible for the preparation of the financial statements).
<i>remuneration bracket</i>	the range of the total remuneration of each of the staff members in the senior manager and risk taker categories – from the highest paid to the lowest paid in these categories.
<i>instruments</i>	units or shares of the UCITS managed by the management company, equivalent ownership interests (including – for UCITS issuing only units – unit-linked instruments), subject to the legal structure of the UCITS concerned and its fund rules or instruments of incorporation, or share-linked instruments or equivalent non-cash instruments with equally effective incentives as any of the instruments referred to in this

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<sup>48</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:120:0022:0027:EN:PDF>.

definition.

<i>malus</i>	arrangement that permits the management company to prevent the vesting of all or part of the amount of a deferred remuneration award in relation to risk outcomes or performances of the management company as a whole, the business unit, the UCITS and, where possible, the staff member. Malus is a form of ex-post risk adjustment.
<i>clawback</i>	contractual agreement in which the staff member agrees to return ownership of an amount of remuneration to the management company under certain circumstances. This can be applied to both upfront and deferred variable remuneration. When related to risk outcomes, clawback is a form of ex-post risk adjustment.
<i>supervisory function</i>	the relevant persons or body or bodies responsible for the supervision of the management company's senior management and for the assessment and periodical review of the adequacy and effectiveness of the risk management process and of the policies, arrangements and procedures put in place to comply with the obligations under the UCITS Directive. For those management companies that, given their size, internal organisation and the nature, scope and complexity of their activities or their legal structure, do not have a separate supervisory function, the supervisory function should be understood as the member or members of the management body responsible for these functions.
<i>retention period</i>	period of time during which variable remuneration that has already vested and paid out in the form of <i>instruments</i> cannot be sold.
<i>accrual period</i>	period during which the performance of the staff member is assessed and measured for the purposes of determining his or her remuneration.
<i>deferral period</i>	the deferral period is the period during which variable remuneration is withheld following the end of the <i>accrual period</i> .
<i>vesting point</i>	an amount of remuneration vests when the staff member receives payment and becomes the legal owner of the remuneration. Once the remuneration vests, no explicit ex-post adjustments can occur apart from <i>clawback</i> clauses.



### 3 Purpose

5. The purpose of these guidelines is to ensure common, uniform and consistent application of the provisions on remuneration in Articles 14a and 14b of the UCITS Directive.

## 4 Compliance and reporting obligations

### 4.1 Status of the guidelines

6. This document contains guidelines issued under Article 16 of the ESMA Regulation. In accordance with Article 16(3) of the ESMA Regulation competent authorities and financial market participants must make every effort to comply with guidelines and recommendations.
7. Competent authorities to whom the guidelines apply should comply by incorporating them into their supervisory practices, including where particular guidelines within the document are directed primarily at financial market participants.

### 4.2 Reporting requirements

8. Competent authorities to which these guidelines apply must notify ESMA whether they comply or intend to comply with the guidelines, with reasons for non-compliance, within two months of the date of publication by ESMA. In the absence of a response by this deadline, competent authorities will be considered as non-compliant. A template for notifications is available from the ESMA website.
9. Management companies are not required to report to ESMA whether they comply with these guidelines.

## 5 Guidelines on which remuneration is covered by these guidelines

10. Solely for the purposes of the guidelines and Article 14b of the UCITS Directive, remuneration consists of
  - (i) all forms of payments or benefits paid by the management company,
  - (ii) any amount paid by the UCITS itself, including *performance fees*, and
  - (iii) any transfer of units or shares of the UCITS,in exchange for professional services rendered by the management company's *identified staff*.

For the purpose of item (ii) of this paragraph, whenever payments, excluding reimbursements of costs and expenses, are made directly by the UCITS to the management company for the benefit of the relevant categories of staff of the management company for professional services rendered, which may otherwise result in a circumvention of the relevant remuneration rules, they should be considered remuneration for the purpose of the guidelines and Article 14b of the UCITS Directive.

11. All remuneration can be divided into either fixed remuneration (payments or benefits without consideration of any performance criteria) or variable remuneration (additional payments or benefits depending on performance or, in certain cases, other contractual criteria). Both components of remuneration (fixed and variable) may include monetary payments or benefits (such as cash, shares, options, cancellation of loans to staff members at dismissal, pension contributions) or non (directly) monetary benefits (such as, discounts, fringe benefits or special allowances for car, mobile phone, etc.). Ancillary payments or benefits that are part of a general, non-discretionary, management company-wide policy and pose no incentive effects in terms of risk assumption can be excluded from this definition of remuneration for the purposes of the risk alignment remuneration requirements that are specific to the UCITS Directive.
12. A "retention bonus" is a form of variable remuneration and can only be allowed to the extent that risk alignment provisions are properly applied.
13. Management companies should ensure that variable remuneration is not paid through vehicles or that methods are employed which aim at artificially evading the provisions of the UCITS Directive and these guidelines. The management body of each management company has the primary responsibility for ensuring that the ultimate goal of having sound and prudent remuneration policies and structures is not improperly circumvented. Circumstances and situations that may pose a greater risk under this perspective may be: the conversion of parts of the variable remuneration into benefits that normally pose no incentive effect in respect of risk positions; the outsourcing of professional services to firms that fall outside the scope of the UCITS Directive (unless these firms are subject to regulatory requirements on remuneration that are equally as effective as those applicable under these guidelines, according to the provisions of paragraph 15); the use of tied agents or other persons not considered "employees" from a legal point of view; transactions between the management companies and third parties in which the risk takers have material interests; the setting up of structures or methods through which remuneration is paid in the form of dividends or similar pay outs and non-monetary material benefits awarded as incentive mechanisms linked to the performance.
14. Consideration should also be given to the position of partnerships and similar structures. Dividends or similar distributions that partners receive as owners of a management company are not covered by these guidelines, unless the material outcome of the payment of such dividends results in a circumvention of the relevant remuneration rules, any intention to circumvent such rules being irrelevant for such purpose.

15. When delegating investment management activities according to Article 13 of the UCITS Directive, where the remuneration rules would otherwise be circumvented, management companies should ensure that:

- a) the entities to which investment management activities have been delegated are subject to regulatory requirements on remuneration that are equally as effective as those applicable under these guidelines; or
- b) appropriate contractual arrangements are put in place with entities to which investment management activities have been delegated in order to ensure that there is no circumvention of the remuneration rules set out in the present guidelines; these contractual arrangements should cover any payments made to the delegates' *identified staff* as compensation for the performance of investment management activities on behalf of the management company.

16. For the purpose of letter a) under the previous paragraph, an entity can be considered subject to regulatory requirements on remuneration that are equally as effective as those applicable under these guidelines, *inter alia*, where the following conditions are met:

- i) the entity with whom the delegation arrangement is concluded is subject to the remuneration rules under either Directive 2013/36/EU (CRD IV) or Directive 2011/61/EU (AIFMD), and
- ii) the staff of the entity who are *identified staff* for the purpose of these guidelines are subject to the CRD IV or AIFMD rules.

## **6 Guidelines on how to identify the categories of staff covered by these guidelines**

17. Management companies should identify the identified staff, according to these guidelines and any other guidance or criteria provided by competent authorities. Management companies should be able to demonstrate to competent authorities how they have assessed and selected identified staff.

18. The following categories of staff, unless it is demonstrated that they have no material impact on the management company's risk profile or on an AIF it manages, should be included as the identified staff:

- Executive and non-executive members of the management body of the management company, depending on the local legal structure of the management company, such as: directors, the chief executive officer and executive and non-executive partners.
- Senior management

- Control functions
- Staff responsible for heading the investment management, administration, marketing, human resources
- Other risk takers such as: staff members, whose professional activities – either individually or collectively, as members of a group (e.g. a unit or part of a department) – can exert material influence on the management company's risk profile or on a UCITS it manages, including persons capable of entering into contracts/positions and taking decisions that materially affect the risk positions of the management company or of a UCITS it manages. Such staff can include, for instance, sales persons, individual traders and specific trading desks.

When assessing the materiality of influence on a management company's risk profile or on a UCITS it manages, management companies should define what constitutes materiality within the context of their management companies and the UCITS they manage. Criteria that management companies may follow to check whether they are capturing the correct staff members include an assessment of staff members or a group, whose activities could potentially have a significant impact on the management company's results and/or balance sheet and/or on the performance of the UCITS they manage.

An analysis of job functions and responsibilities at the management company should be undertaken for a proper assessment of those roles that could materially affect the risk profile of the management company or of the UCITS it manages. There could be cases where a staff member does not earn a high amount of total remuneration but could have a material impact on the risk profile of the management company or of the UCITS it manages given the individual's particular job function or responsibilities.

Staff members such as administrative or logistical support staff that, given the nature of their job functions, clearly do not have any connection with the risk profile of the management company or the UCITS, should not be considered risk takers. However, such exclusion only applies to support staff whereas, as mentioned in the fourth bullet point in the present paragraph, staff heading the administration should be included as the *identified staff*.

19. Additionally, if they have a material impact on the risk profile of the management company or of the UCITS it manages, other employees/persons, whose total remuneration falls into the remuneration bracket of senior managers and risk takers should be included as the *identified staff*, such as: high-earning staff members who are not already in the above categories and who have a material impact on the risk profile of the management company or of the UCITS it manages. It is likely that in some cases, those staff members whose remuneration is as high as or higher than senior executives and risk takers will be exerting material influence in some way on the risk profile of the

management company or of the UCITS it manages. In other management companies, this may not be the case.

20. The examples mentioned in paragraphs 18 and 19 above are not definitive. The greater the assumption that there may be risk-takers in certain business units, the more in-depth the risk analysis must be to assess whether a person is to be considered a material risk-taker or not.

## 7 Guidelines on proportionality

### 7.1 Proportionality in general

21. According to the Recommendation, when taking measures to implement remuneration principles Member States should take account of the size, nature and scope of financial undertakings' activities. In taking measures to comply with the remuneration principles management companies should comply in a way and to the extent that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities. In this way Article 14b of the UCITS Directive and the Recommendation envisage that provisions should operate in a way to enable a management company to take a proportionate approach to compliance with a remuneration principle.
22. Not all management companies should have to give substance to the remuneration requirements in the same way and to the same extent. Proportionality should operate both ways: some management companies will need to apply more sophisticated policies or practices in fulfilling the requirements; other management companies can meet the requirements of the UCITS Directive in a simpler or less burdensome way.
23. Although the remuneration principles in Article 14b of the UCITS Directive are applicable to all management companies, proportionality may lead, on an exceptional basis and taking into account specific facts, to the disapplication of some requirements if this is reconcilable with the risk profile, risk appetite and the strategy of the management company and the UCITS it manages and within the limits set by the present guidelines. If management companies deem a disapplication for these requirements appropriate for their type of management company or *identified staff*, they should be able to explain to competent authorities, if requested, the rationale for every single requirement that is disappplied. Disapplication should never be automatically triggered on the basis of these guidelines alone: management companies should perform an assessment for each of the remuneration requirements that may be disappplied according to the following paragraph and determine whether proportionality allows them not to apply each individual requirement; if management companies come to the conclusion that no disapplication is possible for any of the disapplicable requirements, there should be no variation to the general application of such requirements to them.
24. The following are the only requirements that may be disappplied and then only if it is proportionate to do so:

- the requirements on the pay-out process for which guidelines are given below under Section 13.4 (Payout process). This means that some management companies, either for the total of their *identified staff* or for some categories within their *identified staff*, may decide not to apply the requirements on:
  - variable remuneration in *instruments*;
  - retention;
  - deferral;
  - ex post incorporation of risk for variable remuneration;
- the requirement to establish a remuneration committee for which guidelines are given below in Section 11.2 (Remuneration committee).

25. The specific numerical criteria set out in Article 14b of the UCITS Directive – for example, the minimum deferral period of three years, the minimum portion of 40 to 60% of variable remuneration that should be deferred (Article 14b(1)(n) of the UCITS Directive) and the minimum portion of 50% of variable remuneration that should be paid in instruments (Article 14b(1)(m) of the UCITS Directive) – if disapplied, may only be disapplied in their entirety. It should not be possible to apply, within a management company, lower thresholds based on proportionality. For instance, when justified by its size, internal organisation and nature, scope and complexity of its activities, a management company may decide not to defer any of the variable remuneration component, but may not decide to apply a 20% deferral of variable remuneration i.e. if the management company does not pass the proportionality test for the disapplication of the requirement, it has to apply at least a 40% deferral, or a 60% deferral in the case of a variable remuneration component of a particularly high amount.

26. It is primarily the responsibility of the management company to assess its own characteristics and to develop and implement remuneration policies and practices which appropriately align the risks faced and provide adequate and effective incentives to its staff. Competent authorities should review the ways management companies actually implement proportionality, taking into account the achievement of regulatory objectives and the need to preserve a level playing field among different management companies and jurisdictions.

## 7.2 Proportionality with respect to the different characteristics of management companies

27. The different risk profiles and characteristics among management companies justify a proportionate implementation of the remuneration principles. Criteria relevant to the application of proportionality are the size of the management company and of the UCITS it manages, its internal organization and the nature, scope and complexity of its activities.

- a) Size: the size criterion can relate to the value of the management company capital and to the value of the assets under management (including any assets acquired through the use of leverage) of the UCITS that the management company manages; liabilities or risks exposure of the management company and of the UCITS that it manages; as well as the number of staff, branches or subsidiaries of a management company. The size of a management company and of the UCITS it manages should not be considered in isolation when applying proportionality. A management company might be considered “small” in terms of number of staff or subsidiaries, but be engaged in a high level of risk taking. A management company should adhere strictly to the remuneration principles where the aggregate set of UCITS that it manages - each of them considered “small” - becomes potentially systemically important (e.g. in terms of total assets under management) or leads to complex investment management activities.

The general obligation to have sound remuneration policies and practices applies to all management companies, regardless of their size or systemic importance.

- b) Internal organization: this can relate to the legal structure of the management company or the UCITS it manages, the complexity of the internal governance structure of the management company, the listing on regulated markets of the management company or the UCITS it manages.

This criterion should be assessed having regard to the entire organisation of the management company including all the UCITS it manages, meaning that for instance the listing of one UCITS should not by itself be sufficient for considering the management company as having a complex internal organisation.

- c) Nature, scope and complexity of the activities: in considering this criterion, the underlying risk profiles of the business activities that are carried out, should be taken into account. Relevant elements can be:
- the type of authorized activity (collective portfolio management of UCITS only or also the additional services listed in Article 6(3) of the UCITS Directive);
  - the type of investment policies and strategies of the UCITS the management company manages;
  - the national or cross-border nature of the business activities (management company managing and/or marketing UCITS in one or more EU or non-EU jurisdictions); and
  - the additional management of AIFs.

28. In assessing what is proportionate, the focus should be on the combination of all the mentioned criteria (size, internal organization and the nature, scope and complexity of the activities) and, as this is not an exhaustive list, of any other relevant criteria. For instance,



a management company's business may well be small-scale but could still include complex risk-profiles because of the nature of its activities or the complexity of the managed UCITS.

### **7.3 Proportionality with respect of the different categories of staff**

29. Proportionality should also operate within a management company for some of the specific requirements. The categories of staff whose professional activities have a material impact on their risk profile should comply with specific requirements which aim to manage the risks their activities entail. The same criteria of size, internal organisation and the nature, scope and complexity of the activities should apply. In addition, the following non-exhaustive elements should be taken into account, where relevant:

- The size of the obligations into which a risk taker may enter on behalf of the management company;
- The size of the group of persons, who have only collectively a material impact on the risk profile of the management company;
- The structure of the remuneration of the staff members (e.g. fixed salary with a variable remuneration vs. profit sharing arrangements), in particular, the following elements:
  - the amount of variable remuneration;
  - the percentage of variable remuneration over the fixed remuneration.

## **8 Guidelines for management companies being part of a group**

30. These guidelines apply in any case to any management company. In particular, there should be no exception to the application to any of the management companies which are subsidiaries of a credit institution of the sector-specific remuneration principles set out in the UCITS Directive and in the present guidelines.

31. It may be the case that in a group context, non-UCITS sectoral prudential supervisors of group entities may deem certain staff of the UCITS management company which is part of that group to be 'identified staff' for the purpose of their sectoral remuneration rules.



## 9 Guidelines on the application of different sectoral rules

### 9.1 General guidelines

32. Where some employees or other categories of personnel of management companies perform services subject to different sectoral remuneration principles, they should be remunerated either:
- a) based on the activities carried out and on a pro rata basis; or
  - b) when there is a conflict between different sectoral remuneration principles, and without prejudice to the guidance in paragraphs 30 and 31 above, by applying the sectoral remuneration principles which are deemed more effective for achieving the outcomes of discouraging excessive risk taking and aligning the interest of the relevant individuals with those of the investors in the funds they manage.
33. The approach under item a) of paragraph 32 means that, for instance, the remuneration of an individual which performs services subject to the UCITS Directive and services subject to CRD IV and/or the AIFMD, should be determined applying the remuneration principles under the UCITS Directive, CRD IV and AIFMD on a pro rata basis based on objective criteria such as the time spent on each service.
34. The approach under item b) of paragraph 32 means that, for instance, where the remuneration of an individual which performs services for various entities (including management companies and/or AIFMs) that are subsidiaries of a parent company that is subject to the CRD IV, is determined – on a voluntary basis – in compliance with all the remuneration principles under the CRD IV for all the services performed by such an individual, this should be deemed to also satisfy the requirements on remuneration under the UCITS Directive and AIFMD. However, where specific CRD requirements – such as those relating to the payment of variable remuneration in *instruments* – conflict with the requirements under the AIFMD or UCITS Directive, the remuneration of the individual concerned should in any event follow the relevant specific sectoral legislation conflicting with the CRD requirements. This means that, for instance, for individuals performing services subject to the AIFMD or UCITS Directive the variable remuneration should always be paid in the AIF *instruments* or UCITS *instruments* (Annex II (1) (m) of AIFMD and Article 14(b)(m) of UCITS V).
35. For the avoidance of doubt, the guidance under paragraphs 32 to 34 above applies to employees or other categories of personnel of management companies (including, for instance, secondees from parent undertakings subject to different sectoral remuneration rules such as CRD IV). Whenever employees or other categories of personnel of other entities perform investment management activities under delegation according to Article 13 of the UCITS Directive, the guidance under paragraphs 15 and 16 above should apply.

36. For management companies engaging in activities covered by the AIFMD (subject to authorisation under the AIFMD), compliance with the sectoral remuneration principles applying firm-wide – based on the relevant sectoral guidelines issued under the AIFMD and UCITS Directive – should be sufficient to consider that at individual level each of the sectoral remuneration principles are complied with. For example, compliance with the requirement under Article 14b(1)(e) of the UCITS Directive – which applies firm-wide – should at the same time satisfy the equivalent requirement under paragraph 1(e) of Annex II of the AIFMD for management companies engaging in activities covered by the AIFMD.

## 9.2 Specific guidelines on ancillary services

37. For the performance of ancillary services under Article 6(3) of the UCITS Directive or under Article 6(4) of the AIFMD, personnel of a management company or an AIFM should be subject to (i) the remuneration principles under the UCITS Directive or AIFMD, as applicable and (ii) the relevant MiFID rules, including the ESMA Guidelines on remuneration policies and practices (MiFID) (ESMA/2013/606).

## 10 Guidelines on the financial situation of the management company

38. In order to guarantee ongoing compliance with the requirements of Article 7(1) of the UCITS Directive, management companies should ensure that they maintain a prudent balance between sound financial situation and the award, pay out or vesting of variable remuneration.

39. The management company should ensure that its financial situation will not be adversely affected by:

- 1) the overall pool of variable remuneration that will be awarded for that year; and
- 2) the amount of variable remuneration that will be paid or vested in that year.

40. The fact that a management company is or risks becoming unable to maintain a sound financial situation, should be a trigger for, inter alia: a) reducing the variable remuneration pool for that year and b) the application of performance adjustment measures (i.e. *malus* or *clawback*) in that financial year<sup>49</sup>. Instead of awarding, paying out the variable remuneration or allowing it to vest, the net profit of the management company for that year and potentially for subsequent years should be used to strengthen its financial situation. The management company should not compensate for this at a later date by awarding, paying out or vesting a greater amount of variable remuneration than it

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<sup>49</sup> See also Section XII (Guidelines on the specific requirements on risk alignment).

otherwise would have done, unless it becomes evident in subsequent years that the management company's financial results justify such actions.

## 11 Guidelines on governance of remuneration

41. The general requirements on governance of remuneration should apply to the management company as a whole.

### 11.1 Management body

#### 11.1.1 Design, approval and oversight of the remuneration policy

42. A management company's remuneration policy should encourage the alignment of the risks taken by its staff with those of the UCITS it manages, the investors of such UCITS and the management company itself; in particular, the remuneration policy should duly take into consideration the need to align risks in terms of risk management and exposure to risk.

43. The *supervisory function* should be responsible for approving and maintaining the remuneration policy of the management company, and overseeing its implementation. The remuneration policy should not be controlled by any executive members of the *supervisory function*. The *supervisory function* should also approve any subsequent material exemptions or changes to the remuneration policy and carefully consider and monitor their effects. Procedures to determine remuneration should be clear, well-documented and internally transparent. For example, proper documentation should be provided on the decision-making process, the determination of the *identified staff*, the measures used to avoid conflicts of interest, the risk-adjustment mechanisms used etc.

44. In the design and oversight of the management company's remuneration policies, the *supervisory function* should take into account the inputs provided by all competent corporate functions (i.e. risk management, compliance, human resources, strategic planning, etc.). As a result, those functions should be properly involved in the design of the remuneration policy of the management company.

45. Ultimately, the *supervisory function* should ensure that a management company's remuneration policy is consistent with and promotes sound and effective risk management. The remuneration policy should:

- be in line with the business strategy, objectives, values and interests of the management company,
- not encourage excessive risk taking as compared to the investment policy of the UCITS the management company manages, and

- enable the management company to align the interests of the UCITS and their investors with those of the *identified staff* that manages such UCITS, and to achieve and maintain a sound financial situation.

46. The *supervisory function* should ensure that the management company's overall corporate governance principles and structures, as well as their interactions with the remuneration system are considered within the design and implementation of a management company's remuneration policies and practices. The *supervisory function* should ensure that the following elements are taken into account: the clear distinction between operating and *control functions*, the skills and independence requirements of members of the *management body*, the role performed by internal committees, including the remuneration committee, the safeguards for preventing conflicts of interests and the internal reporting system and the related parties' transactions rules.

#### 11.1.2 Remuneration of members of the management body and supervisory function

47. The remuneration of the members of the *management body* should be consistent with their powers, tasks, expertise and responsibilities.
48. Where appropriate considering the size of the management company, its internal organisation and the nature, scope and complexity of its activities, the *management body* should not determine its own remuneration. The *supervisory function* should determine and oversee the remuneration of the members of the *management body*. To the extent compatible with national law, the *supervisory function* should also specifically approve and oversee the remuneration of senior executives and staff members who receive the highest amounts of total remuneration within the management company.
49. For management companies which have a separate *supervisory function*, in order to properly address conflicts of interests, it may be more appropriate for members of the *supervisory function* to be compensated only with fixed remuneration. When incentive-based mechanisms are in place, they should be strictly tailored to the assigned monitoring and control tasks, reflecting the individual's capabilities and the achieved results. If *instruments* are granted, appropriate measures should be taken, such as *retention periods* until the end of the mandate, in order to preserve the independence of judgment of those members of the *management body*. For those management companies that given their size, internal organisation and the nature, scope and complexity of their activities do not have a separate *supervisory function*, the principle according to which members of the *supervisory function* may more appropriately be compensated only with fixed remuneration should apply only to the non-executive members of the *management body* that perform the tasks of the *supervisory function*.

### 11.1.3 Shareholders' involvement

50. The approval of a management company's remuneration policy and decisions relating to the remuneration of members of the *management body*, may be assigned to the meeting of the shareholders of the management company, depending on the management company's characteristics or on the national rules in the jurisdiction in which the management company is established. The shareholders' vote may be either consultative or binding. To this end, shareholders should be provided with adequate information in order that they can make informed decisions.
51. The *supervisory function* remains responsible for the proposals submitted to the meeting of the shareholders of the management company, as well as for the actual implementation and oversight of any changes to the remuneration policies and practices.

### 11.1.4 Review of the remuneration policy and its implementation

52. The *supervisory function* should ensure that the remuneration policy of the management company and its implementation will be reviewed on an annual basis at a minimum. Such central and independent reviews should assess whether the overall remuneration system:
- operates as intended (in particular, that all agreed plans/programs are being covered; that the remuneration payouts are appropriate, and that the risk profile, long-term objectives and goals of the management company are adequately reflected); and
  - is compliant with national and international regulations, principles and standards.
53. The relevant internal *control functions* (i.e. internal audit, risk management, compliance functions, etc.) as well as other key *supervisory function* committees (i.e. audit, risk, and nominations committees) should be closely involved in reviewing the remuneration system of the management company.
54. Where periodic reviews reveal that the remuneration system does not operate as intended or prescribed, the *supervisory function* should ensure that a timely remedial plan is put in place.
55. The periodic review of the implementation of the remuneration policies and practices may be, partially or totally, externally commissioned when appropriate according to proportionality. Larger and more complex management companies should have sufficient resources to conduct the review internally, though external consultants may complement and support the management company in carrying out such tasks where appropriate. In line with proportionality, smaller and less complex management companies may decide to outsource the entire review. In all cases, the *supervisory function* should remain responsible for the review of remuneration policies and practices and for ensuring that

the results of the review are followed up; moreover, the relevant *control functions* should be closely involved.

## 11.2 Remuneration committee

### 11.2.1 Setting up a remuneration committee

56. The setting up of a remuneration committee should be considered, as a matter of good practice, even by those management companies that are not obliged to set up such a committee under Article 14b(4) of the UCITS Directive.

57. In order to identify whether a remuneration committee is expected to be set up, the factors mentioned in Section 7 (Guidelines on proportionality) need to be considered. When assessing whether or not a management company is significant, a management company should consider the cumulative presence of all the three factors (i.e. its size or the size of the UCITS it manages, its internal organisation and the nature, scope and complexity of its activities). A management company which is significant only with respect to one or two of the three above factors should not be required to set up a remuneration committee.

58. Without prejudice to the previous paragraph, specific (non-exhaustive) elements to be taken into account when determining whether or not to establish a remuneration committee are:

- whether the management company is listed or not;
- the legal structure of the management company;
- the number of employees of the management company;
- the management company's assets under management;
- whether the management company is also an AIFM;
- the provision of the services mentioned under Article 6(3) of the UCITS Directive.

59. Taking into account the above principles and having regard to all circumstances, the following are examples of management companies which may not need to establish a remuneration committee:

- management companies for which the value of the portfolios of UCITS that they manage does not exceed EUR 1.25 billion and not having more than 50 employees, including those dedicated to the management of AIFs and the provision of the services mentioned under Article 6(3) of the UCITS Directive;

- management companies which are part of banking, insurance, investment groups or financial conglomerates within which an entity is obliged to set up a remuneration committee which performs its tasks and duties for the whole group, provided that the rules governing such remuneration committee's composition, role and competences are equivalent to the ones set out in these guidelines and the existing remuneration committee takes responsibility for checking the compliance of the management company with the rules set out in these guidelines.

60. It should also be understood as mentioned above under paragraph 56 that management companies falling within the examples set out above may choose to set up a remuneration committee at their own initiative as a matter of good practice.

61. Management companies that fall outside the above examples should not be automatically required to set up a remuneration committee. For this purpose, management companies that are above the thresholds set out in paragraph 59 should be considered significant in terms of their size or the size of the UCITS they manage; in order to decide whether or not they need to set up a remuneration committee, however, such management companies should still assess whether or not they are significant in terms of their internal organisation and the nature, the scope and the complexity of their activities.

#### 11.2.2 Composition of the remuneration committee

62. In order to operate independently from senior executives, the remuneration committee should comprise members of the *supervisory function* who do not perform executive functions, at least the majority of whom qualify as independent.

63. The chairperson of the remuneration committee should be an independent, non-executive member.

64. An appropriate number of the members of the remuneration committee should have sufficient expertise and professional experience concerning risk management and control activities, namely with regard to the mechanism for aligning the remuneration structure to management companies' risk and capital profiles.

65. The remuneration committee should be encouraged to seek expert advice internally (e.g. from risk management) and externally. The chief executive officer should not take part in the remuneration committee meetings which discuss and decide on his/her remuneration.

#### 11.2.3 Role of the remuneration committee

66. The remuneration committee should:

- be responsible for the preparation of recommendations to the *supervisory function*, regarding the remuneration of the members of the *management body* as well as of the highest paid staff members in the management company;



- provide its support and advice to the *supervisory function* on the design of the management company's overall remuneration policy;
- have access to advice, internal and external, that is independent of advice provided by or to senior management;
- review the appointment of external remuneration consultants that the *supervisory function*, may decide to engage for advice or support;
- support the *supervisory function* in overseeing the remuneration system's design and operation on behalf of the *supervisory function*;
- devote specific attention to the assessment of the mechanisms adopted to ensure that:
  - the remuneration system properly takes into account all types of risks and liquidity and assets under management levels, and
  - the overall remuneration policy is consistent with the business strategy, objectives, values and interests of the management company and the UCITS it manages and the investors of such UCITS; and
- formally review a number of possible scenarios to test how the remuneration system will react to future external and internal events, and back test it as well.

67. The remuneration committee itself may be in charge of overseeing the central and independent review of the implementation of the remuneration policies and practices.

#### 11.2.4 Process and reporting lines of the remuneration committee

68. The remuneration committee should:

- have unfettered access to all data and information concerning the decision-making process of the *supervisory function*, on the remuneration system's design and implementation;
- have unfettered access to all information and data from risk management and *control functions*. Such access should not hinder the management company's ordinary activities;
- ensure the proper involvement of the internal control and other competent functions (e.g. human resources and strategic planning). The remuneration committee should collaborate with other board committees whose activities may have an impact on the design and proper functioning of remuneration policy and practices (e.g. risk audit, and nomination committees); and



- provide adequate information to the *supervisory function*, and, where appropriate, to the management company's shareholders' meeting about the activities performed.

## 11.3 Control functions

### 11.3.1 Roles of control functions

69. Management companies should ensure that *control functions* have an active role in the design, ongoing oversight and review of the remuneration policies for other business areas.
70. Working closely with the remuneration committee and the *supervisory function* and *management body*, the *control functions* should assist in determining the overall remuneration strategy applicable to the management company, having regard to the promotion of effective risk management.
71. The risk management function should assess how the variable remuneration structure affects the risk profile of the management company. It is good practice for the risk management function to validate and assess risk adjustment data, and to attend a meeting of the remuneration committee for this purpose.
72. The compliance function should analyse how the remuneration structure affects the management company's compliance with legislation, regulations and internal policies.
73. The internal audit function should periodically carry out an independent audit of the design, implementation and effects of the management company's remuneration policies.

### 11.3.2 Remuneration of control functions

74. The remuneration level of staff in the *control functions* should allow the management company to employ qualified and experienced personnel in these functions.
75. If staff in *control functions* receives variable remuneration, it should be based on function-specific objectives and should not be determined solely by the management company-wide performance criteria.
76. The remuneration structure of *control functions* personnel should not compromise their independence or create conflicts of interest in their advisory role to the remuneration committee, *supervisory function* and/or *management body*. If remuneration of the *control functions* includes a component based on management company-wide performance criteria, the risk of conflicts of interest increases and, therefore, should be properly addressed.
77. For management companies which are required to have a remuneration committee, the remuneration of the senior staff responsible for heading the *control functions* should not

be solely left to the *supervisory function*, but should be directly overseen by the remuneration committee. The remuneration of those staff members in compliance and risk management functions must be designed in a way that avoids conflict of interests related to the business unit they are overseeing and, therefore, should be appraised and determined independently. The remuneration committee should make recommendations to the *management body* on the remuneration to be paid to the senior officers in the risk management and compliance functions.

78. For management companies which are not required to have a remuneration committee, the remuneration of the senior staff responsible for heading the *control functions* should be overseen by the *supervisory function*.
79. Conflicts of interest which might arise if other business areas had undue influence over the remuneration of staff within *control functions* should be adequately managed. The need to avoid undue influence is particularly important where staff members from the *control functions* are embedded in other business areas. However, the views of other business areas should be sought as an appropriate part of the assessment process.
80. *Control functions* should not be placed in a position where, for example, approving a transaction, making decisions or giving advice on risk and financial control matters could be directly linked to an increase or decrease in their performance-based remuneration.

## 12 Guidelines on the general requirements on risk alignment

81. The general requirements on risk alignment should be applied by management companies only to the individual remuneration packages of the *identified staff*, but a voluntary management company-wide application is strongly recommended as indicated in Annex II. Management companies should make an assessment on whether these requirements should be applied to the management company as a whole and, if required, be able to demonstrate to competent authorities why they have applied these requirements to the *identified staff* only.

### 12.1 The general remuneration policy, including the pension policy

82. The long-term strategy of the management company should include the overall business strategy and quantified risk tolerance levels with a multi-year horizon, as well as other corporate values such as compliance culture, ethics, behaviour towards investors of the UCITS it manages, measures to mitigate conflicts of interest etc. The design of the remuneration systems should be consistent with the risk profiles, rules or instruments of incorporation of the UCITS the management company manages and with the objectives set out in the strategies of the management company and the UCITS it manages and changes that could be decided in the strategies must be taken into account. Management companies should, therefore, ensure that their remuneration systems are well designed

and implemented. This includes, in particular, a proper balance of variable to fixed remuneration, the measurement of performance as well as the structure and, where appropriate, the risk-adjustment of the variable remuneration. Even a smaller or less sophisticated management company should ensure it makes the best possible attempt to align its remuneration policy with its interests and the interests of the UCITS it manages and their investors.

83. When developing their remuneration policy, management companies should give due consideration to how remuneration contributes to the prevention of excessive risk-taking, the efficiency of the management company and the UCITS it manages and the consistency of the remuneration policy with effective risk management.
84. Managers should consider conservative valuation policies and should not ignore concentration risks and risk factors, such as liquidity risk and concentration risk that could place the UCITS that the management company manages under stress at some point in the future. There are strong incentives not to follow such obligations if the variable part of the remuneration consists predominantly of *instruments* that are paid out immediately, without any deferral or ex post risk adjustment mechanisms (*malus* or *clawback*), and/or are based on a formula that links variable remuneration to current year revenues rather than risk-adjusted profit.
85. In order to counterbalance the dangers mentioned, risk management elements should be connected to the remuneration policy. When properly structured and implemented, variable remuneration can be an efficient tool to align the staff's interests with the interests of the UCITS that the management company manages. Having regard to the nature, scale and complexity of a management company, alternative approaches exist for connecting risk management elements to a remuneration policy.

## 12.2 Discretionary pension benefits

86. Remuneration policy should cover all aspects of remuneration including fixed components, variable components, pension terms and other similar specific benefits. The pension policy (the fixed as well as the variable pension payments) should be aligned with the long term interests of the management company and the UCITS it manages.
87. In case of discretionary pension benefits, as part of the variable remuneration, a staff member should not retire or leave the management company with such benefits vested, with no consideration of the economic situation of the UCITS that the management company manages or risks that have been taken by the staff member in the long term.
88. In order to align this specific kind of pension benefits with the economic situation of the UCITS that the management company manages, discretionary pension benefits, where legally possible according to the relevant pension legislation, should be paid in the form of *instruments*.

89. In the context of a retirement, the discretionary pension benefits vested to the staff member should be subject to a five years *retention period*.
90. Where a staff member leaves the management company before retirement, the discretionary pension benefits should not be vested before a period of five years and should be subject to performance assessment and ex post risk adjustment before pay out.

### 12.3 Severance pay

91. "Golden parachute" arrangements for staff members who are leaving the management company and which generate large payouts without any performance and risk adjustment should be considered inconsistent with the principle in Article 14b(1)(k) of the UCITS Directive. Any such payments should be related to performance achieved over time and designed in a way that does not reward failure. This should not preclude termination payments in situations such as early termination of the contract due to changes in the strategy of the management company or of the UCITS it manages, or in merger and/or takeover situations.
92. Management companies should set up a framework in which severance pay is determined and approved, in line with the management company's general governance structures for employment. The framework should ensure that there is no reward for failure.
93. Management companies should be able to explain to competent authorities the criteria they use to determine the amount of severance pay. It is good practice to defer any outstanding variable payments or long-term incentive plans and for these to mirror the original deferral schemes.

### 12.4 Personal hedging

94. Staff could be considered to have hedged away the risk of a downward adjustment in remuneration if the staff member enters into a contract with a third party which requires the third party to make payments directly or indirectly to the staff member that are linked to or commensurate with the amounts by which the staff member's variable remuneration has been reduced. The contract could for instance take the form of an option or any other derivative contract or other form of contract which provides any type of hedging for the staff member's variable remuneration.
95. In order to ensure the effectiveness of risk alignment, staff members should not buy an insurance contract which compensates them in the event of a downward adjustment in remuneration. As a general rule, however, this would not prohibit insurance designed to cover personal payments such as healthcare and mortgage instalments (provided that the mortgage coverage concerns health-related circumstances that would render the staff

member unable to work in an equivalent position), although each case should be judged on its merits.

96. The requirement not to use personal hedging strategies or insurance to undermine the risk alignment effects embedded in their remuneration arrangements should apply to deferred and retained variable remuneration. Management companies should maintain effective arrangements to ensure that the staff member complies with this requirement.

## **13 Guidelines on the specific requirements on risk alignment**

97. The specific requirements on risk alignment should be applied by management companies only to the individual remuneration packages of the *identified staff*, but management companies may always consider an management company-wide application (or, at least, a “broader than strictly necessary” application) of all or some of the specific requirements. Annex II indicates the specific requirements for which this voluntary management company-wide application is strongly recommended.

### **13.1 Fully flexible policy on variable remuneration**

98. Having a fully-flexible policy on variable remuneration implies not only that variable remuneration should decrease as a result of negative performance but also, that it can go down to zero in some cases. For its practical implementation, it also implies that the fixed remuneration should be sufficiently high to remunerate the professional services rendered, in line with the level of education, the degree of seniority, the level of expertise and skills required, the constraints and job experience, the relevant business sector and region. Individual levels of fixed remuneration should be indirectly impacted by the basic principle on risk alignment.

### **13.2 Risk alignment of variable remuneration**

#### **13.2.1 Risk alignment process**

99. To limit excessive risk taking, variable remuneration should be performance-based and risk adjusted. To achieve this aim, an management company should ensure that incentives to take risks are constrained by incentives to manage risk. A remuneration system should be consistent with effective risk management and governance processes within the management company.

#### **13.2.1.1 Performance and risk measurement process**

100. Setting up a remuneration system should start by defining the objectives of the management company, the unit, as well the staff and the investment strategy of the UCITS concerned. These objectives should be derived from the business plan of the

management company, if any, and should be in line with the risk appetite of the management company and the investment strategy of the UCITS concerned. The performance criteria, which should be used to assess the staff member's achievement of his/her objectives during the *accrual period*, can be directly derived from these objectives. The right to receive the variable remuneration is earned ("awarded") at the end of the *accrual period* or during the *accrual period*, which should be at least one year, but it may be longer. In some cases different *accrual periods* may overlap. If properly designed, the performance assessment links the remuneration with the achievement of the investment strategy of the UCITS concerned and the business plan, if any, or the objectives of the management company. On the contrary, performance criteria which are badly designed can be an incentive for taking too much risk. When assessing performance, only the effective results should be taken into account. Risk alignment during performance measurement can be achieved by using risk adjusted performance criteria or by adjusting performance measures for risk afterwards. The risk adjustment may differ according to the activity of the staff member and the business line or UCITS concerned.

#### 13.2.1.2 Award process

101. After the *accrual period*, the management company should use a specified award process in order to translate performance assessment into the variable remuneration component for each staff member. This should usually be carried out through so-called "pools" of variable remuneration that are first determined and later on allocated. As not all performance and risk measures are suitable to be applied at the level of the management company, the business unit and the staff member, the management company should identify the risks at each level and ensure that a risk correction adequately captures the magnitude and the duration of the risk at each level. This so-called "ex-ante risk adjustment" should adjust remuneration for potential adverse developments in the future.

#### 13.2.1.3 Payout process

102. In order to align the actual payment of remuneration to the holding period recommended to the investors of the UCITS managed by the management company and their investment risks, the variable remuneration should partly be paid upfront (short-term) and partly deferred (long-term). The short-term component should be paid directly after the award and rewards staff for performance delivered in the *accrual period*. The long-term component should be awarded to staff during and after the *deferral period*. It should reward staff for the sustainability of the performance in the long term, which is the result of decisions taken in the past. Before paying out the deferred part, a reassessment of the performance and, if necessary, a risk adjustment should be required in order to align variable remuneration to risks and errors in the performance and risk assessments that have appeared since the staff members were awarded their variable remuneration component. This so-called ex post risk adjustment should always be necessary, because at the time remuneration is awarded, the ultimate performance cannot be assessed with certainty.

## 13.2.2 Common requirements for the risk alignment process

### 13.2.2.1 Time horizon

103. Management companies, when assessing risk and performance, should take into account both current and future risks that are taken by the staff member, the business unit, the UCITS concerned or the management company as a whole. For this exercise, management companies should examine what the impact of the staff member's activities could be on the UCITS they manage and management company's short and long term success. To be able to do so, the management company should align the horizon of risk and performance measurement with the holding period recommended to the investors of the UCITS managed by the management company and their investment risks. The requirement of a management company to assess the performance of its staff in a multi-year framework appropriate to the holding period recommended to the investors of the UCITS managed by the management company implies the *accrual period* and the payout period for short-term and long-term remuneration covering an appropriate period in total.

104. The right balance between accrual and payout periods should depend on the type of UCITS managed by the management company and on the type of business and activity developed by the staff member. However, the use of multi-year *accrual periods* is more prudent since the assessment of the performance can take into account with certainty more risks that have materialized since the beginning of the *accrual period*.

### 13.2.2.2 Levels of risk and performance measurement

105. Performance-related remuneration should include parameters linked to the risks and performance of the UCITS concerned and of the business unit of the management company in addition to the risks and performance of the individual activities. Thus, the amount of variable remuneration a staff member is eligible for should be determined by his/her individual performance, the performance of his/her business line or the UCITS concerned and the performance of the management company. The relative importance of each level of the performance criteria should be determined beforehand and adequately balanced to take into account the position or responsibilities held by the staff member.

106. To have the greatest impact on staff behaviour, the variables used to measure risk and performance should be linked as closely as possible to the level of the decisions made by the staff member that is subject to the risk adjustment. Performance criteria should include achievable objectives and measures on which the staff member has some direct influence. For example, for senior executives, management companies may design the remuneration policies to include financial measures based on the performance of all the UCITS managed by the management company or the entire management company, or for performance and risks of units, or decisions that were determined by senior executive strategy. In contrast, variables for the manager of a business unit ideally would be for performance and risk of that unit.



#### 13.2.2.3 Quantitative and qualitative measures

107. The risk alignment process should use a mix of quantitative and qualitative approaches (e.g. measurement of performance or risk; setting of the pool and adjustment to risks).

108. Quantitative measures may have some advantages in terms of transparency if they are pre-defined. They can, therefore, influence the behaviour of staff more directly. However, quantitative measures or criteria are not sufficient to measure all risk or performance or to risk adjust remuneration. To complete the measurement and adjustment of risk or performance, management companies should also rely on qualitative approaches.

#### 13.2.2.4 Judgemental measures

109. Whenever judgement is used for a risk and performance measurement or risk adjustment, there should be:

- a clearly written policy outlining parameters and key considerations on which the judgement will be based;
- clear and complete documentation of the final decision regarding risk and performance measurement or risk adjustment;
- involvement of relevant *control functions* experts;
- appropriate levels of approval obtained, e.g. of the *management body* or *supervisory function*, or of the remuneration committee; and
- consideration of the personal incentives of the manager making the judgement, e.g. by using scorecards.

110. For both quantitative and qualitative measures, management companies should be prepared to disclose and reproduce any judgmental elements incorporated into their risk alignment process. Management companies should also provide detailed information to the competent authority if the final outcome after applying judgmental measures is significantly different from the initial outcome using pre-defined measures.

#### 13.2.3 Risk measurement

111. Management companies should take into account all risks, whether on or off balance sheet, differentiating amongst risks affecting the management company, the UCITS it manages, business units and individuals. Risk identification and quantification at the UCITS level can be found in the risk management policy that the management company is required to establish, implement and maintain and which identifies all the relevant risks to which the UCITS they manage are or might be exposed to. Management companies



should also determine whether measures they are using for risk adjustment include 'difficult-to-measure' risks, such as reputational and operational risk.

112. In order to take into account all material risks, management companies should use the same risk measurement methods as used in the risk management policy established for the UCITS managed by the management company. Furthermore, management companies should also take into account the risks arising from the additional management of AIFs and from the services provided under Article 6(3) of the UCITS Directive.

113. Taking proportionality into account, the risk management calculations should be transparent and the management companies should be able to demonstrate how the risk calculations can be broken down by UCITS and related to the management company's business units and different types of risk positions throughout the organisation. The quality of methods and models used should influence the extent to which a management company should implement a more sophisticated variable remuneration policy based on performance measurements.

#### 13.2.4 Performance measurement

##### 13.2.4.1 Qualitative/Quantitative measures

114. Management companies should use both quantitative (financial) as well as qualitative (non-financial) criteria for assessing individual performance.

115. The appropriate mix of quantitative and qualitative criteria should depend on the tasks and responsibilities of the staff member. In all cases, the quantitative and qualitative criteria and the balance between them should be specified and clearly documented for each level and category of staff.

116. Quantitative measures should cover a period which is long enough to properly capture the risk of the staff member's actions. Examples of quantitative performance measures used in the asset management sector which fulfil the abovementioned provisions are the internal rate of return (IRR), earnings before interest, taxes, depreciation and amortization (EBITDA), Alpha Ratio, absolute and relative returns, Sharpe Ratio and assets raised.

117. In addition to quantitative performance measures, variable remuneration awards should also be sensitive to the staff's performance with respect to qualitative (non-financial) measures. Examples are the achievement of strategic targets, investor satisfaction, adherence to risk management policy, compliance with internal and external rules, leadership, management, team work, creativity, motivation and cooperation with others business units and with *control functions*. Such determined qualitative criteria could rely on compliance with risk control measures such as limits and audit results. Negative non-financial performance, in particular unethical or non-compliant behaviour,

should override any good financial performance generated by a staff member and should diminish the staff member's variable remuneration.

#### 13.2.4.2 Relative/absolute and internal/external measures

118. Absolute performance measures are measures set by the management company on the basis of its own strategy, which includes the risk profile and risk appetite of the management company and of the UCITS it manages, as further developed down through the chain of business levels. Such measures help to minimize the risk that remuneration is awarded that is not justifiable by the management company's or UCITS' performance. They also tend to create long term incentives. However, it may be difficult to calibrate absolute performance measures, especially for new entrants or for new kinds of financial activities (with difficult-to-measure risks) linked to the management of UCITS.
119. Relative performance measures are measures that compare performance with peers, either 'internal' peers (i.e. within the organization) or 'external' (similar management companies). Relative performance measures are easier to set because the benchmark is readily available. However, such measures pose the risk that variable remuneration that is not supported by long-term success of the business unit or the management company or the UCITS it manages will be paid out anyway. In a period of sector wide positive financial performances, it could lead to 'raising the bid' and/or 'herd' mentality, providing incentives to take on excessive risk. In a downturn economic cycle where most management companies and UCITS may perform poorly, relative measures may nonetheless lead to positive outcomes (and thus to an insufficient contraction of the management company's total variable remuneration) even if absolute performance has deteriorated compared to previous periods.
120. Internal (e.g. profits) and external (e.g. share price) variables come with both advantages and disadvantages that should be balanced carefully. Internal performance measures are able to generate more involvement of the staff members if they can influence the outcome by their own behaviour. This is especially true if the performance measures are fixed at the level of the business unit (rather than on the management company-wide level). Furthermore, it is easier to introduce risk adjustment features for internal measures, because the link with in-house risk management techniques is more readily available. On the other hand, such measures can be manipulated and can create distorted outcomes on a short-term basis. External performance measures are less subject to this danger of manipulation, although attempts to artificially increase the stock price (probably only relevant for top executives) may still occur.

## 13.3 Award process

### 13.3.1 Setting and allocation of pools

121. Management companies should adopt a documented policy for the award process and ensure that records of the determination of the overall variable remuneration pool are maintained.

### 13.3.2 The risk adjustment in the award process

122. In determining remuneration pools or individual awards, management companies should consider the full range of current and potential (unexpected) risks associated with the activities undertaken. Performance measures used in setting the remuneration pool may not fully or adequately capture risks undertaken, thus, ex-ante adjustments should be applied to ensure that the variable remuneration is fully aligned with the risks undertaken. Management companies should establish whether the risk adjustment criteria they are using take into consideration severe risks or stressed conditions.
123. Management companies should determine to what level they are able to risk adjust their variable remuneration calculations quantitatively – whether to the business unit level or further down the line such as to a trading desk level, if any, or even to an individual level. Management companies should determine the level of granularity that is suitable for each level.

#### 13.3.2.1 Quantitative ex ante risk adjustment

124. In order to have a sound and effective remuneration scheme, management companies should use a number of different quantitative measures for their risk adjustment process. Normally, these measures should be based on an overarching risk adjustment framework.
125. When measuring the profitability of the management company and its business units as well as the UCITS it manages, the measurement should be based on net revenue where all direct and indirect costs related to the activity are included. Management companies should not exclude IT costs, research costs, legal fees, marketing costs, and costs for outsourced activities. Management companies should make sure that remuneration pools are not being “back-fitted” to meet remuneration demands.
126. The quantitative ex-ante risk adjustments made by management companies should largely rely on existing measures within the management companies, generally used for other risk management purposes. As a result, the limitations and potential issues related to these measures should also be relevant for the remuneration process. The risk adjustments used should benefit from the experience gained when dealing with these risks in other contexts and should be challenged like any other component of the risk management process.

#### 13.3.2.2 Qualitative measures for ex-ante risk adjustment

127. Qualitative risk elements should be considered by management companies. Qualitative ex-ante adjustments could take place while setting management company-wide and business unit remuneration pools or when determining or allocating individuals' remuneration. Qualitative ex-ante risk adjustments are common at pool and individual levels, contrary to quantitative adjustments which tend to be mostly observed only at the pool level.

128. Management companies make qualitative risk adjustments when allocating/determining individuals' remuneration through assessments that may explicitly include risk and control considerations such as compliance breaches, risk limit breaches and internal control breakdowns (e.g. based on internal audit results).

### 13.4 Pay-out process

#### 13.4.1 Non-deferred and deferred remuneration

129. Although remuneration is aligned through ex-ante risk adjustments, due to uncertainty, ex-post risk adjustments should be put in place to keep incentives fully aligned. This can only be done if part of the remuneration has been deferred.

130. A deferral schedule is defined by different components: (a) the time horizon of the deferral, (b) the proportion of the variable remuneration that is being deferred, (c) the speed at which the deferred remuneration vests (*vesting point*), (d) the time span from accrual until the payment of the first deferred amount and (e) the form of the deferred variable remuneration. Management companies can differentiate their deferral schedules by varying these five components. A stricter than necessary application for one component may influence the supervisory scrutiny for another component. In any case, the way in which a management company combines these components should lead to a meaningful deferral schedule, in which the long-term risk alignment incentives are clear.

##### 13.4.1.1 Time horizon and vesting

131. The *deferral period* always starts at the moment the upfront part of the variable remuneration is paid out and can be coupled either to cash variable remuneration or variable remuneration in *instruments*. It ends when the last variable remuneration has vested. The minimum *deferral period* is three years. Management companies should set the *deferral period* which should be calculated on the basis of the holding period recommended to the investors of the UCITS and depending on the potential impact of the staff on the risk profile of the UCITS. The actual *deferral period* should be further tailored to the responsibilities and tasks performed by the staff and expected fluctuations in the value of the assets of the UCITS, which in many cases will imply longer time horizons. The management company should consider longer *deferral periods* for at least members of the *management body*.

#### 13.4.1.2 Vesting point

132. Pro rata vesting (or payment) means that for a *deferral period* of, for example, three years one-third of the deferred remuneration vests at the end of each of the years  $n+1$ ,  $n+2$  and  $n+3$ , where 'n' is the moment at which performance is measured to determine the variable remuneration. Annex III includes a diagram showing an example of a pro rata spreading for a deferral scheme in which 60% of the variable remuneration is deferred (first diagram).

133. In any case, vesting should not take place more frequently than on a yearly basis (e.g. not every six months).

#### 13.4.1.3 Proportion to be deferred

134. The proportion of the variable remuneration that should be deferred ranges from 40 to 60 %, depending on the impact the staff member (or category of staff) can have on the risk profile of the UCITS managed by the management company and the responsibilities and tasks performed, and depending on the amount of variable remuneration. If management companies decide to determine the proportion that is being deferred by a cascade of absolute amounts (rather than percentages of the total variable remuneration - e.g. part between 0 and 100: 100% upfront, part between 100 and 200: 50% upfront and rest is deferred, part above 200: 25% upfront and rest is deferred ...), on an average weighted basis, such management companies should respect the 40 to 60 % threshold.

#### 13.4.1.4 Time span between end of accrual and vesting of deferred amount

135. In order to ensure a proper assessment of the performance outcome and, thus, to undertake a proper ex-post risk adjustment, the first deferred portion should not be paid out too soon after the *accrual period*. For the deferral to be really effective with regard to the staff's incentives, the first amount should not vest sooner than 12 months after the accrual.

### 13.4.2 Cash vs. instruments

#### 13.4.2.1 Types of instruments

136. Staff should only be remunerated using *instruments* if it does not trigger interest misalignment or encourage risk-taking which is inconsistent with the risk profiles, rules or instruments of incorporation of the relevant UCITS. A misalignment of interests might arise in relation to *identified staff* that are not directly involved in investment management. Rewarding those individuals with *instruments* of UCITS might represent a conflict of interest with their duty to perform independently their functions relating to those UCITS.

137. For management companies managing several UCITS, in order to align the interests of the *identified staff* with those of the relevant UCITS, when possible according to the

organisation of the management company and the legal structure of the managed UCITS, the *identified staff* should receive *instruments* related mainly to the UCITS in relation to which they perform their activities, provided that no excessive concentration in the holding of the *instruments* – facilitating an excessive risk-taking by the *identified staff* – is created. E.g. if one member of the staff of a management company which manages three UCITS (x, y and z) performs his/her activities for UCITS x only, in principle that member of the staff should receive *instruments* related mainly to UCITS x; however, should the application of such principle lead to a situation where the *identified staff* has too strong an interest in the UCITS for which they perform their activities, the management company should consider enlarging the spectrum of *instruments* paid in order to prevent an excessive risk-taking from the *identified staff* in relation to the relevant UCITS.

138. The availability of *instruments* is dependent on the legal structure of the UCITS concerned and their fund rules or instruments of incorporation. For UCITS in the legal form of a corporate fund, shares or share-linked instruments should be able to align the interests of the shareholders and staff. Share-linked instruments are those whose value is based on a market value appreciation of the stock and that have the share price as a reference point, e.g. stock appreciation rights, types of synthetic shares.

139. For UCITS which are common funds, *instruments* should consist of units of the UCITS concerned, or equivalent ownership interests; for many of these UCITS, share-linked instruments are not an option due to their legal form.

140. Neither dividends nor interest should be paid on *instruments* before vesting.

#### 13.4.2.2 Retention policy

141. A retention policy should be determined by the management company in the remuneration policy. The management company should be able to explain how the retention policy relates to other risk alignment measures in the total remuneration policy and should explain whether and how they differentiate between *instruments* paid upfront and deferred *instruments*.

142. *Retention periods*, as the most important element of the retention policy, should be coupled with the vesting of *instruments*. The *retention period* is independent from the *deferral period*. This means that, in order to meet the requirement of a minimum *deferral period* of three years, the *retention period* counts for nothing. The *retention period* can last for a shorter or longer period than the *deferral period* applied to the *instruments* that are not paid up front.

143. In the case of upfront *instruments*, *retention periods* are the only mechanism available to emphasize the difference between cash paid upfront and *instruments* awarded upfront in order to align incentives with the longer-term interests of the management company and the UCITS it manages and the investors of such UCITS.

144. In the case of deferred *instruments*, the *retention periods* come after every vested portion (the second diagram in Annex III illustrates these concepts). Competent authorities may determine whether the *retention periods* proposed by the management company are sufficient and appropriate.
145. The minimum *retention period* should be sufficient to align incentives with the longer term interests of the management company, of the UCITS it manages and of their investors. Different factors may tend to suggest that this period could be longer or shorter. Longer *retention periods* should be applied for staff with the most material impact on the risk profile of the management company and the UCITS it manages.
146. It is possible that a *retention period* lasts for a shorter period than the *deferral period* applied to the *instruments* that are not paid up front. However, as an example of proportionality, for their most senior staff, large and complex management companies should consider the use of a *retention period* for upfront paid *instruments* that goes beyond the *deferral period* for the deferred *instruments*.
147. *Instruments* should be valued on the date of the award (at the end of the *accrual period*) of these *instruments*. This value is the basis for the determination of the initial number of *instruments* and for later ex-post adjustments to the number of *instruments*.
148. The upfront payment of *instruments*, even with a minimum *retention period* of, for example, three years, is not equivalent to deferred *instruments*. Deferred *instruments* are subject to an ex-post risk adjustment due to the back-testing of the underlying performance, possibly leading to a reduction in the number of *instruments* that will eventually be paid out (second diagram in Annex III).

#### 13.4.2.3 Minimum portion of instruments and their distribution over time

149. The requirement in Article 14b(1)(m) of the UCITS Directive to apply the minimum of 50% (where applicable) to both the portion of the variable remuneration component that is deferred and the portion of the variable remuneration component not deferred means that the 50% minimum threshold for *instruments* should be applied equally to the non-deferred and the deferred part; in other words, management companies should apply the same chosen ratio between *instruments* and cash for their total variable remuneration to both the upfront and deferred part.

#### Examples:

- Good practice: For a certain category within its *identified staff*, a management company establishes a 50 *instruments* / 50 cash ratio for the variable remuneration, combined with a 60% deferral schedule (that is, 40% is non-deferred variable remuneration). This results in an upfront payment in *instruments* of 20 (i.e. 50% of 40) and 20 in cash. The deferred part consists of 30 in *instruments* and 30 in cash.



- Good practice: For a certain category within its *identified staff*, a management company establishes a 70 *instruments* / 30 cash ratio for the variable remuneration, combined with a 40% deferral schedule (that is, 60% is non-deferred variable remuneration). This results in an upfront payment in *instruments* of 42 (i.e. 70% of 60) and 18 in cash. The deferred part consists of 28 in *instruments* and 12 in cash.
- Poor practice: If for a certain category within its *identified staff*, a management company were to establish a 50 *instruments* / 50 cash ratio for the variable remuneration, combined with a 40 % deferral scheme, the management company cannot decide to pay 50 in cash up front and 10 in *instruments*, leading to a deferred pay out of 40 in *instruments*.
- Poor practice: If for a certain category within its *identified staff*, a management company were to establish a 70 *instruments* / 30 cash ratio for the variable remuneration, combined with a 50% deferral scheme, the management company cannot decide to pay 50 upfront in *instruments* and 0 in cash, leading to a deferred pay out of 20 in *instruments* and 30 in cash.

150. The second diagram in Annex III provides an example of this equal distribution of *instruments* over the non-deferred and deferred parts of remuneration.

151. For the purposes of the requirement to pay at least 50% of variable remuneration in *instruments* unless the management of the UCITS accounts for less than 50% of the total portfolio managed by the management company, the 50% threshold should be based on the net asset value of the individual UCITS managed by the management company. For the purposes of the same requirement, the total portfolio managed by the management company should be the portfolios managed by the management company under its authorisation under the UCITS Directive (i.e. the portfolios managed under its authorisation under the AIFMD, if any, should not be taken into account).

### 13.4.3 Ex post incorporation of risk for variable remuneration

#### 13.4.3.1 Explicit ex-post risk adjustments

152. An “ex-post risk adjustment” should imply that once an initial variable remuneration component has been awarded to the staff member, and an upfront part has already been paid, the management company is still able to adjust, by way of a reduction, the variable remuneration as time goes by and the outcomes of the staff member’s actions materialize.

153. An ex-post risk adjustment is an explicit risk alignment mechanism through which the management company itself adjusts remuneration of the staff member by means of *malus* or *clawback* clauses (e.g. by lowering cash remuneration or by awarding a lower number of *instruments*). Ex-post risk adjustment should always be performance-related: techniques that are, for example, based on the amount of dividends or the evolution of



the share price are not sufficient because the link to the performance of a staff member is not sufficiently direct. Therefore, ex-post risk adjustments are frequently also called “performance adjustments” because they are a response to the actual risk outcomes of the staff member's actions. Performance measures taken at this stage should allow the management company to perform an analysis (similar to back testing) as to whether its initial ex-ante risk adjustment was correct. Management companies should ensure there is a link between the initial performance measurement and the back-testing. Thus, the extent to which an ex-post risk adjustment is needed depends on the quality (accuracy) of the ex-ante risk adjustment.

154. The effect of *maluses* should not be inflated by paying out artificially high interest (above market rates) on the cash deferred parts to the staff member. *Maluses* operate by affecting the *vesting point* and cannot operate after the end of the *deferral period*. Furthermore, *clawback* can be a method for achieving an ex-post risk adjustment on variable remuneration.
155. Management companies may utilize specific criteria whereby *malus* (to both the cash portion and the *instruments* portion of deferred remuneration) and *clawbacks* would apply. Such criteria should, for example, include:
- a. evidence of misbehaviour or serious error by the staff member (e.g. breach of code of conduct, if any, and other internal rules, especially concerning risks);
  - b. whether the UCITS and/or the management company and/or the business unit subsequently suffers a significant downturn in its financial performance (specific indicators should be used);
  - c. whether the UCITS and/or the management company and/or the business unit in which the staff member works suffers a significant failure of risk management;
  - d. significant changes in the management company's overall financial situation.
156. A *clawback* should typically operate in the case of established fraud or misleading information. Where applicable, management companies should include *clawback* clauses in addition to these cases e.g. for remuneration received in breach of the UCITS Directive and/or these guidelines.
157. Ex-post risk adjustment could be based on both quantitative measures and informed judgment.
158. To have the greatest impact on staff's incentives, the variables should measure outcomes as close as possible to the level of the decisions made by the staff member that is subject to the ex-post explicit adjustment. For example, variables for senior

executives probably should be for outcomes for the management company as a whole, or for outcomes of units or decisions that were determined by senior executive strategy. In contrast, variables for the head responsible for a business unit ideally would reflect outcomes of that unit.

#### 13.4.3.2 Implicit adjustments

159. When the variable remuneration takes the form of *instruments*, the final payout to the staff member will depend partly on market prices due to fluctuations during the *deferral* or *retention period*. This implicit adjustment of remuneration is not related to any explicit decision of the management company, but is inherent to the form that is used for paying out. Under no circumstances should the evolution of the net asset value of the UCITS or, for listed UCITS, the evolution of the share price be considered sufficient as a form of ex-post risk adjustment. There should always be a form of explicit risk adjustment on the initiative of the management company. For non-senior staff in particular, there may be no direct relation between their decisions and the value of the UCITS.

160. A *retention period* on its own can never be sufficient to design an ex-post risk adjustment for *instruments* and should not be a substitute for a longer *deferral period*.

#### 13.4.3.3 Possibility of upward revisions

161. The market price of *instruments* can go up, so implicitly they are subject to movements in their value in both directions.

162. Under no circumstances should the explicit ex- post risk adjustment (both for cash and *instruments*) lead to an increase of the deferred part.

## 14 Guidelines on disclosure

### 14.1 External disclosure

#### 14.1.1 Specific and general requirements on disclosure

163. Management companies should consider the additional disclosure on remuneration required under paragraph (8) of the *Recommendation*, to the extent that the latter may also be relevant to them. Management companies should have the flexibility to disclose the information mentioned in the *Recommendation* through an independent remuneration policy statement, a periodic disclosure in the annual report or any other form. In all cases, however, the management company should ensure that the disclosure is clear and easily understandable and accessible.

164. Without prejudice to confidentiality and applicable data protection legislation, management companies should disclose detailed information regarding their remuneration policies and practices for members of staff whose professional activities

have a material impact on the risk profile of the UCITS the management company manages.

165. The *Recommendation's* remuneration disclosures may be made on a proportionate basis and the overall remuneration proportionality principle will apply to the type and amount of information disclosed. Small or non-complex management companies/UCITS should only be expected to provide some qualitative information and very basic quantitative information where appropriate. In practice, this could mean that such management companies/UCITS are not expected to provide all the information under paragraph (8) of the *Recommendation*. Management companies should disclose how they have applied proportionality.
166. The disclosure should be published on at least an annual basis and as soon as practicable after the information becomes available.

#### 14.1.2 Policy and practices

167. The disclosure report should set out the decision-making process used to determine the remuneration policy for the individuals to which it applies. This may include the governance procedure relating to the development of the remuneration policy and should include information about the bodies (including their composition and mandate), such as the remuneration committee or external consultants, which played a significant role in the development of the remuneration policy. Management companies should outline the role of all relevant stakeholders involved in the determination of the remuneration policy. Additionally, the disclosure should include a description of the regional scope of the management company's remuneration policy, the types of staff considered as material risk takers and the criteria used to determine such staff.
168. The report should include information on how pay and performance are linked. Such information should include a description of the main performance metrics used for: the management company, top-level business lines, and for individuals (i.e. scorecards). Management companies should disclose information relating to the design and structure of remuneration processes, such as the key features and objectives of the remuneration policy and how the management company ensures that staff members in *control functions* are remunerated independently of the businesses they oversee. The report should also include a description of the different forms of variable remuneration used (i.e. cash, equity, options, other capital instruments, and long-term incentive plans) and should include the rationale for using these different forms and for allocating them to different categories of staff. Additionally, the report should include a discussion of the parameters used to allocate deferred and non-deferred remuneration for different staff categories.
169. Disclosure reports should describe how the management company takes into account current and future risks to which they are exposed when implementing remuneration methodologies and what these risks are. Also, management companies should describe the measures used to take account of these risks and the ways in which these measures

affect remuneration. In addition, management companies should disclose the ways in which they seek to adjust remuneration to take account of longer-term performance - as in the management company's policy on deferral, vesting and performance adjustment.

170. The quantitative (financial) as well as qualitative (non-financial) criteria used by management companies for assessing individual performance which are relevant for determining the remuneration policies and practices and are described under Section 13.2.4.1 (Qualitative/Quantitative measures) should also be disclosed in the disclosure reports.

171. The disclosure should be produced and owned by the *management body* that has the ultimate sign-off on remuneration decisions.

## 14.2 Internal disclosure

172. The remuneration policy of a management company should be accessible to all staff members of that management company. Management companies should ensure that the information regarding the remuneration policy disclosed internally reveals at least the details which are disclosed externally. Therefore, according to the size, internal organisation and the nature, scope and complexity of the activities of the management company, the information provided to staff members might contain some of the elements listed in Section III (Disclosure) of the *Recommendation*. The staff members should know in advance the criteria that will be used to determine their remuneration. The appraisal process should be properly documented and should be transparent to the member of staff concerned. Confidential quantitative aspects of the remuneration of staff members should not be subject to internal disclosure.

## Annex I

### Correlation table Recommendation/UCITS Directive

	Recommendation	UCITS Directive
1.	Section II, par. 3.1.	Art. 14b(1)(a)
2.	Section II, par. 3.2. and 6.1.	Art. 14b(1)(b)
3.	Section II, par. 6.2.	Art. 14b(1)(c)
4.	Section II, par. 6.5.	Art. 14b(1)(d)
5.	Section II, par. 6.6.	Art. 14b(1)(e)
6.	Section II, par. 5.1. and 5.4.	Art. 14b(1)(g)
7.	Section II, par. 5.2.	Art. 14b(1)(h)
8.	Section II, par. 4.1. and 4.2.	Art. 14b(1)(j)
9.	Section II, par. 4.5.	Art. 14b(1)(k)
10.	Section II, par. 5.3.	Art. 14b(1)(l)
11.	Section II, par. 4.4.	Art. 14b(1)(m)
12.	Section II, par. 4.3.	Art. 14b(1)(n)
13.	Section II, par. 6.4.	Art. 14b(4)

## Annex II

### Mapping of the remuneration principles included in the UCITS Directive

UCITS Directive requirements - Article 14b		Paragraphs of these Guidelines relating to the relevant requirement	Scope
Art. 14b(1)(a)	the remuneration policy is consistent with and promotes sound and effective risk management and does not encourage risk taking which is inconsistent with the risk profiles, rules or instruments of incorporation of the UCITS that the management company manages;	82 – 85	Only to the <i>identified staff</i> , but management company-wide strongly recommended and management companies, if required, should be able to demonstrate why the applied the requirement to the <i>identified staff</i> only
Art. 14b(1)(b)	the remuneration policy is in line with the business strategy, objectives, values and interests of the management company and the UCITS that it manages and of the investors in such UCITS, and includes measures to avoid conflicts of interest;	82 – 85 42 – 55	Paragraphs 78 – 81 → Only to the <i>identified staff</i> , but management company-wide strongly recommended and management companies, if required, should be able to demonstrate why the applied

			<p>the requirement to the <i>identified staff</i> only</p> <p>Paragraphs 38 51 → management company-wide obligatory</p>
Art. 14b(1)(c)	the remuneration policy is adopted by the management body of the management company in its supervisory function, and that body adopts, and reviews at least annually, the general principles of the remuneration policy and is responsible for, and oversees, their implementation; the tasks referred to in this point shall be undertaken only by members of the management body who do not perform any executive functions in the management company concerned and who have expertise in risk management and remuneration;	42 – 55	Management company-wide obligatory
Art. 14b(1)(d)	the implementation of the remuneration policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for remuneration adopted by the management body in its supervisory function;	52 – 55	Management company-wide obligatory
Art. 14b(1)(e)	staff engaged in control functions are compensated in accordance with the achievement of the objectives linked to their functions, independently of the performance of the business areas that they control;	74 – 80	Management company-wide obligatory

Art. 14b(1)(f)	the remuneration of the senior officers in the risk management and compliance functions is directly overseen by the remuneration committee, where such a committee exists;	74 – 80	Management company-wide obligatory
Art. 14b(1)(g)	where remuneration is performance-related, the total amount of remuneration is based on a combination of the assessment as to the performance of the individual and of the business unit or UCITS concerned and as to their risks and of the overall results of the management company when assessing individual performance, taking into account financial and non-financial criteria;	105 – 110 114 – 117	Only to the <i>identified staff</i> , but management company-wide strongly recommended
Art. 14b(1)(h)	the assessment of performance is set in a multi-year framework appropriate to the holding period recommended to the investors of the UCITS managed by the management company in order to ensure that the assessment process is based on the longer-term performance of the UCITS and its investment risks and that the actual payment of performance-based components of remuneration is spread over the same period ;	103 – 104 131 – 135	Only to the <i>identified staff</i> , but voluntary management company-wide application is always possible
Art. 14b(1)(i)	guaranteed variable remuneration is exceptional, occurs only in the context of hiring new staff and is limited to the first year of engagement;	None	Management company-wide obligatory
Art. 14b(1)(j)	fixed and variable components of total remuneration are appropriately balanced and the fixed component represents a sufficiently high	98	Only to the <i>identified staff</i> , but management



	proportion of the total remuneration to allow the operation of a fully flexible policy on variable remuneration components, including the possibility to pay no variable remuneration component;		company-wide strongly recommended
Art. 14b(1)(k)	payments related to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure;	91 – 93	Only to the <i>identified staff</i> , but management company-wide strongly recommended and management companies, if required, should be able to demonstrate why the applied the requirement to the <i>identified staff</i> only
Art. 14b(1)(l)	the measurement of performance used to calculate variable remuneration components or pools of variable remuneration components includes a comprehensive adjustment mechanism to integrate all relevant types of current and future risks;	111 – 113 121 – 128	Only to the <i>identified staff</i> , but management company-wide strongly recommended
Art. 14b(1)(m)	subject to the legal structure of the UCITS and its fund rules or instruments of incorporation, a substantial portion, and in any event at least 50 %, of any variable remuneration component consists of units of the UCITS concerned, equivalent ownership interests, or share-linked instruments or equivalent non-cash instruments	136 – 151	Only to the <i>identified staff</i> , but voluntary management company-wide application is always possible

	<p>with equally effective incentives as any of the instruments referred to in this point, unless the management of the UCITS accounts for less than 50 % of the total portfolio managed by the management company, in which case the minimum of 50 % does not apply.</p> <p>The instruments referred to in this point shall be subject to an appropriate retention policy designed to align incentives with the interests of the management company and the UCITS that it manages and the investors of such UCITS. Member States or their competent authorities may place restrictions on the types and designs of those instruments or ban certain instruments as appropriate. This point shall be applied to both the portion of the variable remuneration component deferred in line with point (n) and the portion of the variable remuneration component not deferred;</p>		
Art. 14b(1)(n)	<p>a substantial portion, and in any event at least 40 %, of the variable remuneration component, is deferred over a period which is appropriate in view of the holding period recommended to the investors of the UCITS concerned and is correctly aligned with the nature of the risks of the UCITS in question.</p> <p>The period referred to in this point shall be at least three years; remuneration payable under deferral arrangements vests no faster than on a pro-rata basis; in the case of a</p>	129 – 135	Only to the <i>identified staff</i> , but voluntary management company-wide application is always possible

	variable remuneration component of a particularly high amount, at least 60 % of the amount shall be deferred;		
Art. 14b(1)(o)	<p>the variable remuneration, including the deferred portion, is paid or vests only if it is sustainable according to the financial situation of the management company as a whole, and justified according to the performance of the business unit, the UCITS and the individual concerned.</p> <p>The total variable remuneration shall generally be considerably contracted where subdued or negative financial performance of the management company or of the UCITS concerned occurs, taking into account both current compensation and reductions in payouts of amounts previously earned, including through malus or clawback arrangements;</p>	<p>38 – 40</p> <p>121 – 128</p> <p>152 – 162</p>	Only to the <i>identified staff</i> , but voluntary management company-wide application is always possible
Art. 14b(1)(p)	<p>the pension policy is in line with the business strategy, objectives, values and long-term interests of the management company and the UCITS that it manages.</p> <p>If the employee leaves the management company before retirement, discretionary pension benefits shall be held by the management company for a period of five years in the form of instruments defined in point (m). In the case of an employee reaching retirement, discretionary pension benefits shall be paid to the employee in the form of instruments</p>	82 – 90	Only to the <i>identified staff</i> , but management company-wide strongly recommended and management companies, if required, should be able to demonstrate why the applied the requirement to the <i>identified</i>

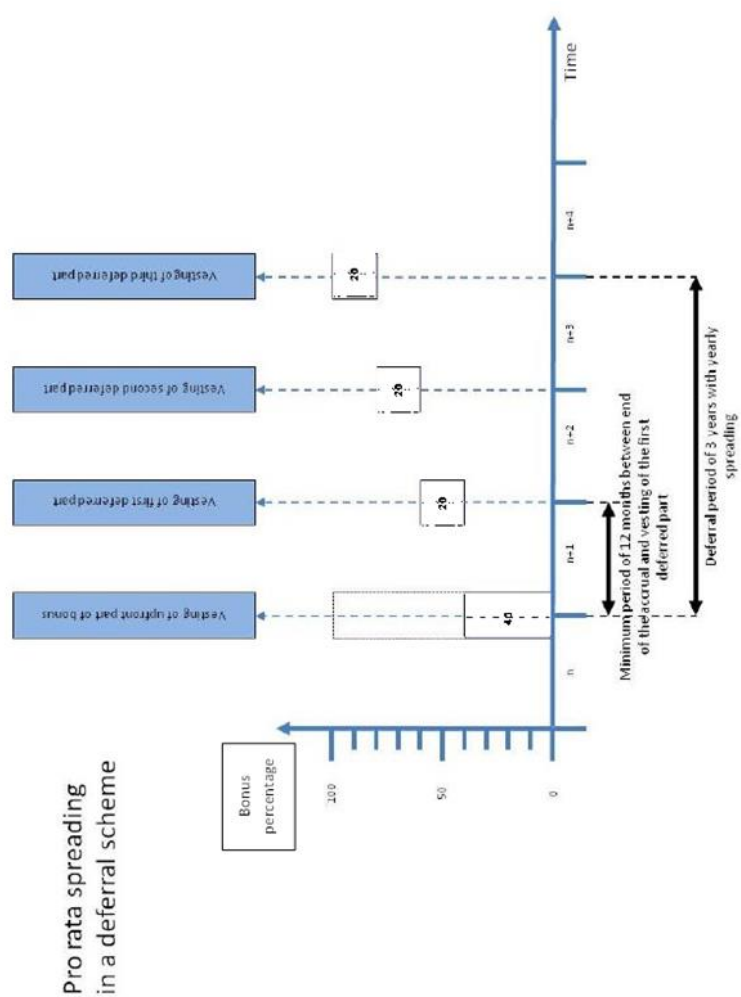
	defined in point (m), subject to a five-year retention period;		<i>staff</i> only
Art. 14b(1)(q)	staff are required to undertake not to use personal hedging strategies or remuneration- and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements;	94 – 96	Only to the <i>identified staff</i> , but management company-wide strongly recommended and management companies, if required, should be able to demonstrate why the applied the requirement to the <i>identified staff</i> only
Art. 14b (1)(r)	variable remuneration is not paid through vehicles or methods that facilitate the avoidance of the requirements laid down in this Directive.	13 – 16	Management company-wide obligatory
Art. 14b(2)	<p>In accordance with Article 35 of Regulation (EU) No 1095/2010, ESMA may request information from competent authorities on the remuneration policies and practices referred to in Article 14a of this Directive.</p> <p>ESMA shall, in close cooperation with EBA, include in its guidelines on remuneration policies provisions on how different sectoral remuneration principles, such as those set out in Directive 2011/61/EU of the European Parliament and of the Council and in Directive 2013/36/EU of the</p>	32 – 36	

	European Parliament and of the Council, are to be applied where employees or other categories of personnel perform services subject to different sectoral remuneration principles.		
Art. 14b(3)	The principles set out in paragraph 1 shall apply to any benefit of any type paid by the management company, to any amount paid directly by the UCITS itself, including performance fees, and to any transfer of units or shares of the UCITS, made for the benefit of those categories of staff, including senior management, risk takers, control functions and any employee receiving total remuneration that falls into the remuneration bracket of senior management and risk takers, whose professional activities have a material impact on their risk profile or the risk profiles of the UCITS that they manage.	10 – 20	Management company-wide obligatory
Art. 14b(4)	<p>Management companies that are significant in terms of their size or of the size of the UCITS they manage, their internal organisation and the nature, scope and complexity of their activities shall establish a remuneration committee. The remuneration committee shall be constituted in a way that enables it to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk.</p> <p>The remuneration committee that is, where appropriate, set up in accordance with the ESMA</p>	56 – 68	management company-wide obligatory

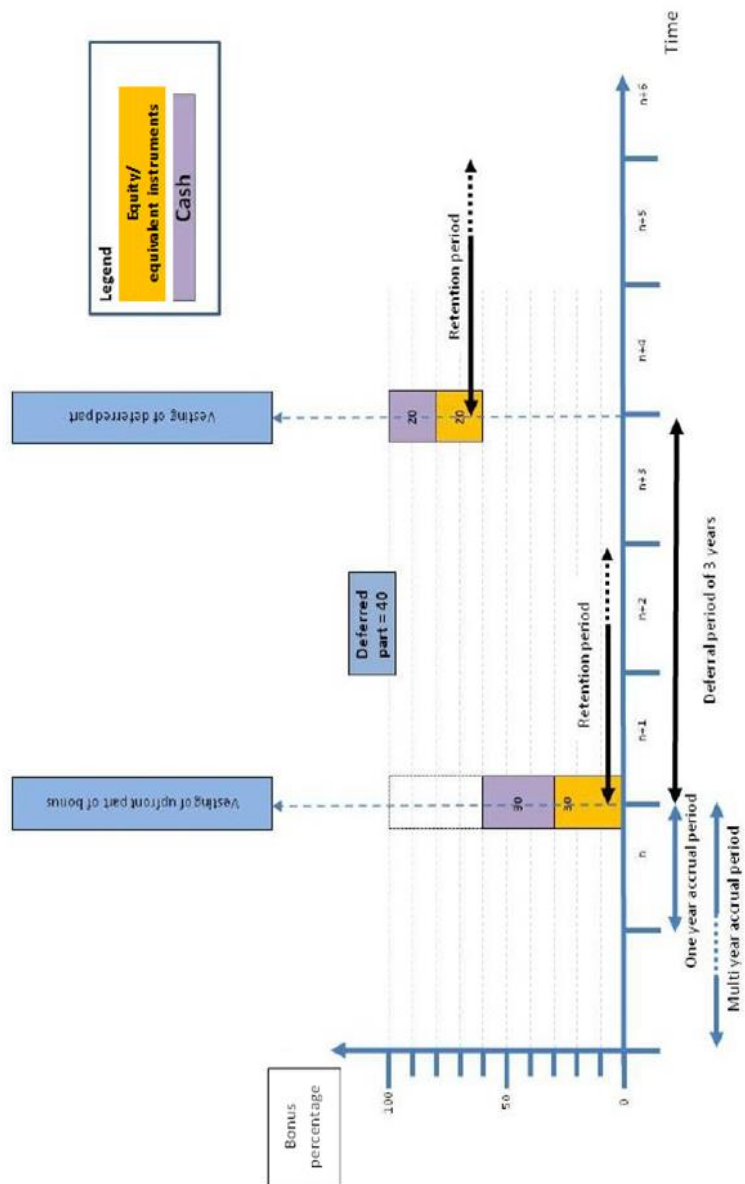
	<p>guidelines referred to in Article 14a(4) shall be responsible for the preparation of decisions regarding remuneration, including those which have implications for the risk and risk management of the management company or the UCITS concerned and which are to be taken by the management body in its supervisory function. The remuneration committee shall be chaired by a member of the management body who does not perform any executive functions in the management company concerned. The members of the remuneration committee shall be members of the management body who do not perform any executive functions in the management company concerned.</p> <p>If employee representation on the management body is provided for by national law, the remuneration committee shall include one or more employee representatives. When preparing its decisions, the remuneration committee shall take into account the long-term interest of investors and other stakeholders and the public interest.</p>		
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## Annex III

### Schematic overview of some deferral mechanisms



## Accrual vs. deferral vs. retention





## 14.5 Annex V

### Draft guidelines (AIFMD Remuneration Guidelines)

#### 1 Scope

**Who?**

**What?**

1. These guidelines amend the Guidelines on sound remuneration policies under the AIFMD (ESMA/2013/232) ('AIFMD Remuneration Guidelines') and have the same scope of application.

**When?**

2. These guidelines apply from two months after the date of publication by ESMA.

#### 2 Guidelines for AIFMs being part of a group

3. Paragraph 33 of the AIFMD Remuneration Guidelines is amended so that Section VIII of such guidelines reads as follows:

***VIII. Guidelines for AIFMs being part of a group***

*32. These guidelines apply in any case to any AIFM. In particular, there should be no exception to the application to any of the AIFMs which are subsidiaries of a credit institution of the sector-specific remuneration principles set out in the AIFMD and in the present guidelines.*

*33. It may be the case that in a group context, non-AIFM sectoral prudential supervisors of group entities may deem certain staff of the AIFM which is part of that group to be 'identified staff' for the purpose of their sectoral remuneration rules.*