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| Response Form to the Consultation Paper |
| Guidelines on performance fees in UCITS |

**Responding to this paper**

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

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

ESMA will consider all comments received by **31/10/2019.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input - Consultations’.

**Instructions**

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

1. Insert your responses to the questions in the Consultation Paper in the present response form.
2. Please do not remove tags of the type <ESMA\_QUESTION\_PFG\_1>. Your response to each question has to be framed by the two tags corresponding to the question.
3. If you do not wish to respond to a given question, please do not delete it but simply leave the text “TYPE YOUR TEXT HERE” between the tags.
4. When you have drafted your response, name your response form according to the following convention: ESMA\_PFG\_nameofrespondent\_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA\_PFG\_ABCD\_RESPONSEFORM.
5. Upload the form containing your responses, in Word format, to ESMA’s website ([www.esma.europa.eu](http://www.esma.europa.eu) under the heading “Your input – Open consultations” 🡪 “Consultation on Position limits and position management in commodities derivatives”).

**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](http://www.esma.europa.eu/legal-notice).

**Who should read this paper**

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

**General information about respondent**

|  |  |
| --- | --- |
| Name of the company / organisation | Arthur Cox |
| Activity | Audit/Legal/Individual |
| Are you representing an association? |  |
| Country/Region | Ireland |

**Introduction**

***Please make your introductory comments below, if any***

<ESMA\_COMMENT\_PFG\_1>

Arthur Cox is one of Ireland’s largest law firms. Our Asset Management and Investment Funds Group is a market leader in the field, advising on all aspects of investment management issues and the establishment and ongoing operation of investment funds in Ireland.

We welcome the opportunity to respond to this consultation on Guidelines on performance fees in UCITS.

<ESMA\_COMMENT\_PFG\_1>

**Questions**

1. : Do you agree that greater standardisation in the field of funds’ performance fees is desirable? What should be the goal of standardisation?

<ESMA\_QUESTION\_PFG\_1>

We agree that standardisation of funds’ performance fees is desirable.

Given the current differences in approach across NCAs as regards the permitted use and rules around performance fees, the goal of standardisation should be to promote a common supervisory approach that will ensure clarity, transparency and consistency of practice for both investors and fund providers. Standardisation should provide a level playing field for all providers and ensure that investors have the information they need to compare and make informed decisions about potential investments. A standard approach to performance fees could also improve the marketability of the UCITS brand.

<ESMA\_QUESTION\_PFG\_1>

1. : Are there any obstacles to standardisation that could be removed by regulatory action? Please elaborate.

<ESMA\_QUESTION\_PFG\_2>

The divergences between NCAs on the use and rules around performance fee models could be addressed by standardisation. See Q1 above.

<ESMA\_QUESTION\_PFG\_2>

1. : What should be taken into consideration when assessing consistency between the index used to calculate the performance fees and the investment objectives, strategy and policy of the fund? Are there any specific indicators which should be considered (eg: historical volatility, asset allocation composition, etc.) to ensure this consistency? Please provide examples and give reasons for your answer.

<ESMA\_QUESTION\_PFG\_3>

Where a fund uses a performance fee model that is based on the outperformance of a benchmark index, we agree that there should be consistency between the benchmark index and the fund’s investment objective, policy and strategy. However, we consider that the fund manager is best placed to determine the most appropriate factors that should be considered to ensure this consistency, having regard to the investment objective, policy and strategy of an individual fund. Therefore, we would agree with including a list of non-exhaustive indicators as a form of guidance for managers, but not as an exclusive list of factors that should be considered.

<ESMA\_QUESTION\_PFG\_3>

1. : What is the anticipated impact of the introduction of Guideline 3? Do you agree with setting a minimum crystallisation period of one year? Do you think this could help better aligning the interests of fund managers and investors? Please provide examples.

<ESMA\_QUESTION\_PFG\_4>

We agree that for certain performance fee models an annual crystaillisation frequency is appropriate. In Ireland performance fees are permitted on the basis of the HWM and benchmark outperformance models and an annual crystallisation frequency applies.

However, setting such a minimum frequency may not always be in the best interests of investors and we agree with ESMA that this frequency should not apply to funds that operate a fulcrum fee model.

<ESMA\_QUESTION\_PFG\_4>

1. : Are there any other models or methodologies currently employed that, in your view, should be exempted from this requirement? For example, do you think that the requirement of a minimum crystallisation period of 12 months should also apply to HWM models? Please provide examples on how these models achieve the objectives pursued by Guideline 3.

<ESMA\_QUESTION\_PFG\_5>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_5>

1. : In your view, should performance fees be charged only when the fund has achieved absolute positive performance? What expected financial impact (e.g. increase or decrease of the manager’s remuneration or increase or decrease of the financial return for investors) would the proposed Guideline 4 have for you/the stakeholder(s) you represent? Are there models or methodologies currently employed where the approach set out in Guideline 4 would not be appropriate?

<ESMA\_QUESTION\_PFG\_6>

In our view there may be circumstances where performance fees could be charged, nothwithstanding that an absolute positive performance has not been achieved. For example, the approach proposed in Guideline 4 may not be appropriate where a fund operates a hurdle (rather than a HWM) model, which provides for the payment of a performance fee where there has been negative performance, but outperformance of the hurdle is achieved.

The proposed approach may also be inappropriate where a benchmark model is used, in that, the fund could achieve positive performance as against its benchmark, nothwithstanding that the net asset value may have declined in relative terms (relative positive performance), or in absolute terms (absolute positive performance).

<ESMA\_QUESTION\_PFG\_6>

1. : If the performance fee model that you currently use provides for performance fees to be payable in times of negative returns, is a prominent warning on this provided to investors in the legal and marketing documents of the fund? If not, should this be provided? Please give examples for your answer and details on how the best interests of investors are safeguarded.

<ESMA\_QUESTION\_PFG\_7>

We agree that such a risk warning should be included in the Prospectus.

<ESMA\_QUESTION\_PFG\_7>

1. : What are your views on setting a performance reference period for the purpose of resetting the HWM? What should be taken into account when setting the performance reference period? Should this period be defined, for example, based on the whole life of the fund (starting from the fund’s inception date), the recommended holding period of the investor or the investment horizon as stated in the prospectus? Please provide examples and reasons for your answer.

<ESMA\_QUESTION\_PFG\_8>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_8>

1. : Alternatively, would it be possible to envisage predefined time horizons for the purpose of resetting the HWM, such as 3 or 5 years? Please provide examples and details on what you think would be the best practice in order to better align the interests of fund managers and investors.

<ESMA\_QUESTION\_PFG\_9>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_9>

1. : How long do you think the performance reference period should be for performance fee models based on a benchmark index? What should be taken into account when setting the performance reference period for a performance fee benchmark model? Would it be possible to envisage predefined time horizons for the purpose of resetting the performance fee based on a benchmark, such as 3 or 5 years? Please provide examples and details on what you think would be the best practice in order to better align the interests of fund managers and investors.

<ESMA\_QUESTION\_PFG\_10>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_10>

1. : Alternatively, do you think the performance reference period should coincide with the minimum crystallisation period or should it be longer/shorter? Please provide examples and reasons for your answer.

<ESMA\_QUESTION\_PFG\_11>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_11>

1. : What are your views on when the Guidelines should become applicable? How much time would managers require to adapt existing fee mechanisms to comply with the requirements of these Guidelines?

<ESMA\_QUESTION\_PFG\_12>

Given the nature of the operational adjustments and the fact that investor notifications may be required where funds have to adjust their performance fee models, we are of the view that managers may need more time than currently proposed to comply with the Guidelines. Therefore, we would suggest a minimum transitional period of 24 months to allow any adjustments to be carried out over a full financial year.

<ESMA\_QUESTION\_PFG\_12>

1. : Do you consider that the principles set out in the Guidelines should be applied also to AIFs marketed to retail investors in order to ensure equivalent standards in retail investor protection? Please provide reasons.

<ESMA\_QUESTION\_PFG\_13>

We agree that in the interests of investor protection that there should be a level of standardisation across retail products and agree in principle with performance fee guidance for retail AIFs. However, having regard to the specifc characteristics of these funds it may be more appropriate to issue direct guidance to these funds, rather than applying the UCITS Guidelines to AIFs.

<ESMA\_QUESTION\_PFG\_13>

1. : Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits as regards the consistency between the performance fees model and the fund’s investment objective? What other types of costs or benefits would you consider in this context? Please provide quantitative figures, where available.

<ESMA\_QUESTION\_PFG\_14>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_14>

1. : In relation to Guideline 2, do you think that models of performance fee without a hurdle rate, or with a hurdle rate not linked to the investment objective (but clearly stated in the offering documents), should be permissible? For example, do you think that equity funds with a performance fee linked to EONIA, or a performance fee which is accrued as long as there are positive returns, should be allowed? Please give examples and reasons for your answer.

<ESMA\_QUESTION\_PFG\_15>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_15>

1. : What additional costs and benefits would compliance with the proposed Guideline bring to you/the stakeholder(s) you represent? Please provide quantitative figures, where available.

<ESMA\_QUESTION\_PFG\_16>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_16>

1. : What is the anticipated impact from the introduction of this proposed Guideline? Are there models or methodologies currently employed where this Guideline would not be appropriate? If so, please provide examples of these and details of how the best interests of investors are safeguarded.

<ESMA\_QUESTION\_PFG\_17>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_17>

1. : What additional costs and benefits would compliance with the proposed Guideline bring to the stakeholder(s) you represent? Please provide quantitative figures, where available.

<ESMA\_QUESTION\_PFG\_18>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_18>

1. : Which other types of costs or benefits would you consider in the disclosure of the performance fees model? Please provide quantitative figures, where available.

<ESMA\_QUESTION\_PFG\_19>

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<ESMA\_QUESTION\_PFG\_19>