|  |
| --- |
| 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 | Sycomore Asset Management |
| Activity | Investment Services |
| Are you representing an association? |  |
| Country/Region | France |

**Introduction**

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

<ESMA\_COMMENT\_PFG\_1>

Sycomore Asset Management welcomes the ESMA’s consultation on performance fees and sees in a very positive light the introduction of overarching guidelines throughout the Union.

Sycomore AM believes that the Guidelines should aim at creating a fair competitive arena, rather than setting restrictions and limits on the applications of the performance fees (periods and mechanisms). We are therefore more supportive of a flexible approach, which could leave each asset management company free to defining mechanisms, resets, and amounts of performance fees, with ESMA setting general guiding principles. It is very positive that IOSCO principles are taken as reference, as they have long been discussed and represent a well-balanced global guidance.

Sycomore AM believes that clear definitions of the concepts used in the ESMA proposed Guidelines are of paramount importance.

<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 believe that coherence should be set as objective of the Guidelines, as to enable a fair competition among players and ease cross-border distribution of products, preventing regulatory inconsistencies and red-tape, constraints and inefficiencies.

In light of this, we believe that the role of the regulator should be that of setting broad principles and guidelines, but at the same time grant some level of flexibility to managers on the application of the specific elements.

We agree on the importance of full, fair and transparent disclosure of the existence, structure, as well as application of performance fees. However, as we further mention in our document, we do not believe there is a need for prominent remarks and warnings, which could instead disadvantage some players (e.g. active managers), rather than working on the creation of a fair and even competitive field for everyone.

We believe that the Guidelines should also contain a comprehensive Glossary of Terms to clarify the key objects/ definitions of the document, as we have noticed some incongruences in the definitions provided in the Guidelines and those reported in the existing glossary section.

<ESMA\_QUESTION\_PFG\_1>

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

<ESMA\_QUESTION\_PFG\_2>

TYPE YOUR TEXT HERE

<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>

We strongly agree on the requirement of full consistency between the selection and application of performance fees and the fund’s objectives, strategy and policy, as well as the need to grant full transparency on the definition of outperformance to the final client.

However, we would like to clarify that it is the investment objective that determines how a performance fee is suitable, not the other way round. Indeed, to be clear, an absolute/total return fund often uses a money market index as hurdle rate, but this does not mean that the fund is managed in reference to that index.

Lastly, we support the net-of-costs approach to the calculation of performance fees.

To this point we would suggest a further effort in terms of clarity of definition when it comes to the “net-of-cost” calculation, and we believe that the Guidelines should mention that excess performance should be calculated net of management fees and funds’ administrative fees, but gross of those costs related to share classes’ features, such as hedge share class, as well as those costs related to performance fees.

<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 suggest ESMA to provide a clarification of the definition of Crystallization Period, as we notice an inconsistency between that included in the Guidelines and in the Glossary, as to whether it refers to the “virtual accrual/booking” of the fee, or rather to the actual pay-out of it to the management company. On this matter, we embrace the first definition (i.e. accrual and not actual payment) in this document. Moreover, in order to avoid misunderstandings with reference to Performance Reference Period, we suggest to substitute the word Period with the word Frequency (hence adopting the definition “Crystallization Frequency”).

We believe that, while the Crystallization Frequency for the calculation of performance fees should be provided and clearly communicated, the regulator shall grant some flexibility on its definition, especially as far as peculiar situations are concerned.

In particular, we believe that an appropriate Crystallization Frequency should be defined by each asset management company considering its fund’s investment objectives and investment strategy, as well as the company’s performance compensation policies, among other factors.

As such, we do not agree in aligning the period with the investors’ holding period, given the difficulty in ex-ante foreseen and setting such periods.

In the case of a Benchmark or Hurdle Rate performance fee models - shall a fixed or minimum Crystallization Frequency be defined by the regulator, we believe that 1 (one) year would be the most appropriate, as granting the right balance between (i) the need to measure a performance over a relevant and long-enough time period, as well as (ii) the requirement to reward a well-performing portfolio manager in a frequent manner.

<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>

We understand from the current wording of the ESMA consultation paper, that no distinction is provided between Pure HWM model (whereby the performance fee becomes payable when the NAV per share exceeds the highest previous value ever recorded since fund’s inception) and High of High model (whereby the performance fee becomes payable when the NAV per share exceeds the highest previous value at which the last performance fee was accrued and paid out to the fund).

However, both such models are adopted in European jurisdictions, and, as they present inherently different features, they would require a different treatment under the ESMA Guidelines.

In particular, the Pure HWM model, which is widely adopted in Italy, should be exempted from a minimum Crystallization Frequency and reset date.

<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>

The concept of absolute positive performance not only poses a major threat to the rationale of a performance-driven fee structure, but also hampers the alignment of interests with the final client. As illustrated also in Guideline 1, outperformance is defined with respect to a reference indicator. As such, should the manager be able to beat the reference indicator, he/she should be rewarded accordingly.

By requiring a manager not only to outperform his/ her index, but also make up for any negative performance he/she delivered in the case of negative index performance, the regulator is de-facto incentivizing the manager to take on additional risk in order to get back to zero. In addition, such provision creates a misalignment and conflict of interests on the side of the manager, who is not incentivized to manage well the portfolio in circumstances of market downturns.

In turn, paragraph 22 of Guideline 4 is de-facto going against the principle described in the following paragraph (23) of preventing the manager from taking excessive risk.

Lastly, structured in this way, this guideline inherently disadvantages active managers versus passive products.<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 believe that proper information and fair and transparent communication on performance fees is important and should be guaranteed, in order to duly safeguard the interests of investors. This policy should apply also to the performance fee computation methodology.

However, we do not believe that a prominent warning sign or specific highlighting should be included as to the point of performance fees payable in times of negative returns. Such warning, if treated differently from any other information provided in the relevant documentation, would de-facto disadvantage performance fees-based players, thus going against one of the main objectives of the ESMA Guidelines to guarantee a fair and even competitive arena for fund managers.

<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>

We believe that ESMA should not set a predefined timeline for the reference period and leave this to the asset management company’s decision. A one-size fits all reference period setting would wrongly impact asset management fee models with no added benefit.

For High of High models, we strongly support that defining a reference period that is less than the crystallisation frequency (yearly) would not be in favour of a fair treatment of investors. Indeed, generally the performance of funds are looked at on a yearly basis and this ensures that the same outperformance is remunerated only once on this generally accepted horizon. A longer reference period bears the risk of a too high wealth transfer between investors whose investments contributed to the building of the provision and those who have not. Also, it bears the risk of putting pressure on the management company to prefer setting a higher fixed fee model.

We are not in favour of a prescriptive approach as to the reference period for reset. Should a set period be defined by the regulator, we propose the 12 months minimum for Benchmark and Hurdle Rate models.

<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>

Please refer to the answer to question Q8.

<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>

Please refer to the answer to question Q8.

<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>

Please refer to the answer to question Q8.

<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 crystallisation period of at least 12 months, any change in the performance fee model described in the prospectus would take at least 12 months before the performance fees accrued become payable to management company.

With this in mind, and taking into account legal and operational operations needed to adapt existing fee mechanisms, especially in Member States where the IOSCO principles are not yet fully implemented, we believe that at least 24 months are needed to be able to comply with the requirements of these Guidelines.

<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 think that these principles should be applied to UCITS. We would like to recall that AIF share classes generally develop, as the case may be, specific performance fees structures targeted to professional clients to match their specific needs.

<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>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_PFG\_19>