

European Securities and Markets Authority Publishes Guidelines for UCITS V Remuneration Policy

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The guidelines, which apply from 1 January 2017, seek to clarify the concepts of disclosure, governance, and risk alignment in respect of remuneration; in advance of this date, non-EU investment managers of UCITS should prepare for discussions with UCITS managers.

On 31 March, the ***European Securities and Markets Authority (ESMA)*** published its report setting out the final guidelines (Guidelines) on sound remuneration policies under the ***Undertakings for Collective Investment in Transferable Securities (UCITS)*** Directive.

The Guidelines clarify the remuneration policy requirements for self-managed UCITS and UCITS management companies (ManCos) to implement for staff whose professional activities have a material impact on the profile of the UCITS (Identified Staff).

Overview

In summary, the Guidelines provide that

- remuneration comprises any benefit (direct or indirect, monetary or non-monetary) paid by a UCITS/ManCo to Identified Staff, including any fixed and variable aspects of salaries and discretionary pensions. The definition specifically includes performance fees and the transfer of units in the UCITS, and detailed rules apply concerning the pay-out process for variable remuneration (“pay-out process rules”). However, payments or benefits that are part of a general, non-discretionary policy of the UCITS and which pose no incentive effects in terms of risk taking can be excluded from the definition of remuneration;
- when establishing and applying the remuneration policies, a UCITS/ManCo must comply with the remuneration requirements “in a way and to the extent that is appropriate to their size, internal organisation and the nature, scope, and complexity of their activities”. Therefore, proportionality may (subject to particular conditions) lead to the disapplication of aspects of the Guidelines if such approach can be reconciled with the risk profile, risk appetite, and strategy of the UCITS, the pay-out process rules, and the need to have a remuneration committee; and

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- a UCITS' prospectus must include either details of the remuneration policy itself, or a summary of the policy and a statement that the policy details are available on an identified website, with paper copies provided free of charge upon request. The Key Investor Information Document (KIID) must include a similar statement. The UCITS' annual report must disclose the aggregate remuneration paid by the UCITS/ManCo to key staff, the number of beneficiaries, and any performance fees paid by the UCITS. The first disclosures need to be included in (i) the first annual report published on or after 18 March 2016 that relates to an accounting period ending after this date; (ii) the prospectus by 30 September 2016; and (iii) the KIID at the time of the next update or otherwise by no later than 18 March 2017.

Delegates

Customarily, a UCITS/ManCo delegates investment management functions to another entity, and the Guidelines will be applied on a "look-through" basis to such delegates. In these instances, the UCITS/ManCo must ensure that

- the entities to which investment management activities have been delegated are subject to equivalent regulatory requirements on remuneration; or
- appropriate contractual arrangements are put in place to ensure that there is no circumvention of the remuneration requirements.

Any contractual arrangements should cover any payments made to a delegate's Identified Staff in respect of compensation for the investment management activities on behalf of the UCITS/ManCo.

Investment management delegates to whom the Markets in Financial Instruments Directive (MiFID)[1] and/or Capital Requirements Directive (CRD) IV[2] apply are considered to be subject to equivalent remuneration rules to the Guidelines. Therefore, delegates within the European Union will satisfy the first condition described above.

Non-EU Investment Managers

Delegates of UCITS/ManCos based outside of the European Union will need, in lieu of an equivalent local regulatory regime on remuneration, to demonstrate contractual compliance with the Guidelines. However, thought should also be given to whether there is scope to dis-apply some of the requirements of the Guidelines based on the specific set of circumstances. For instance, do the activities performed by the non-EU delegate have little/no scope to affect the risk profile of UCITS or, based on the grounds of proportionality discussed above, is it appropriate to dis-apply aspects of the Guidelines such as the pay-out process rules.

[1] Directive 2004/39/EC

[2] Directive 2013/36/EU

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