



April 2016

## ESMA Guidelines on Sound Remuneration Policies under the UCITS Directive and AIFMD

On 31 March, 2016 the European Securities and Markets Authority (“**ESMA**”) published its final Guidelines on sound remuneration policies under the UCITS Directive and AIFMD (the “[Guidelines](#)”). The Guidelines provide clarity on the requirements under the UCITS V Directive (Directive 2014/91/EU) (“**UCITS V**”) for management companies when establishing and implementing a remuneration policy for certain staff as well as clarifying a number of matters with respect to the application of the remuneration rules under AIFMD. UCITS V was transposed into Irish law on 21 March, 2016 by way of the European Union (UCITS) (Amendment) Regulations 2016. ESMA also recently issued a UCITS Q&A to address certain questions relating to this implementation of UCITS V.

The Guidelines will apply from 1 January, 2017.

### The Key Elements of the Guidelines

#### Proportionality for UCITS Management Companies

Article 14(b)(i) of UCITS V provides that: “*When establishing and applying the remuneration policy referred in Article 14(a), 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 ....*”

For further information on any of the issues discussed in this article please contact:



**Cillian Bredin**

DD: + 353 (0)1 673 1889

[cillian.bredin@dilloneustace.ie](mailto:cillian.bredin@dilloneustace.ie)

As was discussed in the ESMA Consultation Paper in respect of the Guidelines, there has been a lack of consensus between different European Regulatory Authorities as regards how the principle of proportionality should be applied to the remuneration rules.

ESMA's AIFMD Remuneration Guidelines (the "**AIFMD Guidelines**") indicate that an AIFM could apply the proportionality principle in a way that results in certain remuneration principles being dis-applied entirely. The European Banking Association ("**EBA**"), however, suggests that, when applying the principle of proportionality to a remuneration policy under Directive 2013/36/EU ("**CRD IV**"), none of the remuneration principles can be dis-applied in full.

The UCITS Directive prescribes that proportionality shall apply to the full set of remuneration principles set out under this Directive. However, the Guidelines do not include guidance on the possibility of dis-applying certain specific requirements on the 'pay-out process' (i.e. the requirements on variable remuneration in instruments, retention, deferral and ex post incorporation of risk for variable remuneration).

This position calls into question the current understanding that the proportionality provisions as set out under the UCITS Directive and AIFMD may lead to a result where:

- under specific circumstances, the requirements on the pay-out process are not applied; or
- it is possible to apply lower thresholds whenever minimum quantitative thresholds are set for the pay-out requirements e.g. the requirement to defer at least 40% of variable remuneration.

In its Press Release accompanying the Guidelines, ESMA states that it considers that these scenarios should remain possible in certain situations and it also says that it believes that it would be inappropriate for certain management companies to be subject in all circumstances to the requirements of the 'pay-out process', such as:

- smaller fund managers (in terms of balance sheet or size of AUM);
- fund managers with simpler internal organisation or nature of activities; or
- fund managers whose scope and complexity of activities is more limited.

In light of this continuing ambiguity, ESMA has written to the European Commission, the Council and the European Parliament to seek further legal clarity on the proportionality principle.

## AIFMD Remuneration Guidelines

The amendment to the AIFMD Guidelines relates to the application of the remuneration rules in a group context and is intended to acknowledge the potential outreach of CRD IV in a banking group.

Pending clarification on the application of proportionality principle from the European institutions, the current AIFMD Guidelines will not be amended to bring them in line with the UCITS Remuneration Guidelines.

## Next Steps

As noted above, the Guidelines will apply **1 January, 2017**. As such, affected management companies (and self-managed investment companies) should undertake a full review of the remuneration policies and procedures currently in place in order to ensure full compliance with the Guidelines as of this date.

If you would like us to assist you with any such review please get in touch with your usual contact at Dillon Eustace.

**Dillon Eustace**

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## DILLON EUSTACE

### **Dublin**

33 Sir John Rogerson's Quay, Dublin 2, Ireland. Tel: +353 1 667 0022 Fax: +353 1 667 0042.

### **Cayman Islands**

Landmark Square, West Bay Road, PO Box 775, Grand Cayman KY1-9006, Cayman Islands. Tel: +1 345 949 0022 Fax: +1 345 945 0042.

### **New York**

245 Park Avenue, 39th Floor, New York, NY 10167, U.S.A. Tel: +1 212 792 4166 Fax: +1 212 792 4167.

### **Tokyo**

12th Floor, Yurakucho Itocia Building, 2-7-1 Yurakucho, Chiyoda-ku, Tokyo 100-0006, Japan. Tel: +813 6860 4885 Fax: +813 6860 4501.

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