



ADVISORY
Industry Information

Performance Fees – Central Bank takes initial steps towards implementing ESMA’s guidelines

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On 3 December 2020, the Central Bank published a [consultation](#) on new Central Bank performance fee guidance for UCITS and certain types of retail AIFs (“CP134”). In issuing the proposed guidance contained in CP134 the Central Bank is taking initial steps to implement the guidelines on performance fees in UCITS and certain types of AIFs (the “Guidelines”) published by the European Securities and Markets Authority (“ESMA”) earlier this year¹.

Introduction

The Guidelines are set to apply in respect of (i) all new UCITS and in scope AIFs²; and (ii) existing UCITS and in scope AIFs that introduce a performance fee from 5 January 2021. UCITS and in scope AIFs with existing performance fees should apply the Guidelines by the beginning of the financial year following 6 months from 5 January 2021, being the next financial year after 5 July 2021. The Central Bank’s suggested approach to the implementation of the Guidelines, as set out in CP134 and detailed below, will result in funds that seek to amend their performance fees being subject to these requirements from the date of amendment.

Acknowledging that the implementation of the Guidelines will involve a degree of complexity, the Central Bank proposes implementing the Guidelines on a phased basis for Irish domiciled UCITS and in scope AIFs, meaning that the Guidelines won’t be fully implemented in Ireland immediately. For a period of time the existing performance fee requirements³ will run in parallel with the requirements set out in the Guidelines once these requirements are implemented. In CP134 the Central Bank states that in the event of any inconsistencies the statutory obligations of the Central Bank UCITS Regulations and the AIF Rulebook will prevail.

Phased Approach

The reason for the Central Bank proposing a phased approach for the implementation of the Guidelines is that, from 5 January 2021, there will be two parallel performance fees frameworks, in the context of UCITS (i) the relevant provisions of the Central Bank UCITS Regulations; and (ii) the Guidelines, that will need to be taken into consideration.

In CP134, the Central Bank notes that it is not possible to implement certain features of the Guidelines with immediate effect for UCITS and the Central Bank proposes to implement those aspects of the Guidelines, which are consistent with the Central Bank UCITS Regulations by way of the proposed guidance detailed in Schedule A of CP134 (the “Proposed Guidance”).

While the Central Bank notes that the Guidelines could be immediately adopted for in scope AIFs this would lead to different approaches being taken to performance fees for UCITS and in scope AIFs and the Central Bank does not proposing adopting such an approach. Instead the Central Bank considers it preferable for the transposition of the Guidelines in respect of in scope AIFs to also apply on a phased basis.

1. ESMA’s final report containing the final version of the Guidelines was published on 3 April 2020 with the official translations of the Guidelines published on 5 November 2020.
2. The Guidelines apply to retail investor AIFs except for: (a) closed-ended AIFs; and (b) open-ended AIFs that are EuVECAs (or other types of venture capital AIFs), EuSEFs, private equity AIFs or real estate AIFs.
3. For UCITS, set out in the Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1)) (Undertakings for Collective Investment in Transferable Securities) Regulations 2019 (the “Central Bank UCITS Regulations”) and for AIFs, set out in the Central Bank’s AIF rulebook (the “AIF Rulebook”).



It is intended that the Proposed Guidance will be effective:

- a. for new UCITS or in-scope AIFs, from the date of establishment of such funds;
- b. for existing UCITS and in-scope AIFs which amend an existing performance fee or introduce a new performance fee, from the date of amendment or introduction of the performance fee; and
- c. for existing UCITS and in-scope AIFs with performance fees, from the beginning of the accounting period, which occurs six months after 5 January 2021 (i.e. the next accounting period commencing after 5 July 2021).⁴ Until that time, these funds must continue to comply with the current applicable performance fees requirements.

The Proposed Guidance

While the Proposed Guidance broadly mirrors the Guidelines and addresses the following topics:

- a. performance fee calculation methodology;
- b. consistency between the performance fee model and the fund's investment objectives, strategy and policy;
- c. frequency of crystallisation of the performance fee;
- d. negative performance recovery; and
- e. disclosure,

there are certain provision of the Guidelines which are inconsistent with the current provisions of the Central Bank UCITS Regulations. As a result of the requirements set out in Regulations 40 and 74 of the Central Bank UCITS Regulations, it is not currently possible for UCITS to provide for:

- a. the possibility of a performance reference period of less than the life of a fund;
- b. crystallisation of performance fees more frequently than annually, for high water mark models with a performance reference period of the life of the fund; or
- c. fulcrum fees⁵.

Conclusion

Despite feedback being welcomed by the Central Bank on CP134 until 15 January 2021, managers of UCITS and in scope AIFs, including self-managed funds, should be mindful of the implementation dates set out above, in particular for existing funds where it is proposed to amend an existing performance fee after 5 January 2021.

CP134 is a first step towards the implementation of the Guidelines in Ireland and clarifies the Central Bank's expectations in terms of compliance with the Guidelines from 5 January 2021. Our previous [advisory](#) published in August 2019 contains a comparison table of the draft Guidelines against the provisions of the Central Bank UCITS Regulations which may be a useful starting point when considering what, if any, amendments will need to be made to: (i) the processes and procedures in place in respect of performance fees being charged in respect of a UCITS or in scope AIF; and/or (ii) the performance fee disclosures. An updated table will be prepared once the Proposed Guidance has been finalised.

4. For example, for existing funds whose financial year ends on 31 December, the Proposed Guidance will apply from the financial period beginning 1 January 2022 and for existing funds whose financial year ends on 30 June, the Proposed Guidance will apply from 1 July 2022.

5. Defined in the Guidelines as "a type of performance fee which provides for the level of the fee to increase or decrease proportionately with the investment performance of the fund over a specified period of time in relation to the investment record of an appropriate reference indicator (including a negative fee deducted from the basic fee charged to the fund)."



Key Contacts

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