

FMA Circular on  
Articles 17a to 17c InvFG 2011 and Article 11 AIFMG

Principles of Remuneration Policies and Practices

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# 1 INTRODUCTION

- (1) This Austrian Financial Market Authority (FMA) Circular is addressed to management companies pursuant to Article 5 para. 1 of the Investment Fund Act 2011 (InvFG 2011; Investmentfondsgesetz 2011) in conjunction with Article 1 para. 1 no. 13 of the Austrian Banking Act (BWG; Bankwesengesetz) and alternative investment fund managers pursuant to Article 4 para. 1 of the Alternative Investment Fund Managers Act (AIFMG; Alternative Investmentfonds Manager-Gesetz).
- (2) It is intended to serve as guidance in drawing up and correctly applying appropriate remuneration policy and practices. Such a policy and practices are necessary to counteract potentially harmful effects of poorly designed remuneration structures on a sound risk management and checking the risk appetite of individual persons. This circular therefore reflects the FMA's legal opinions for this purpose. This circular therefore also takes into account the ESMA Guidelines on sound remuneration policies under the UCITS Directive<sup>1</sup> as well as the AIFMD<sup>2</sup>, upon which the FMA's supervisory practices are based.
- (3) This circular does not constitute a legal regulation. The legal basis in any case remains unaffected by this FMA circular. No rights and obligations extending over and above the provisions of the law can be derived from this circular.
- (4) This circular has not been updated based a change in the material legislative situation. The supervisor assumes in the case of management companies and AIFMs that any changes to be made to the remuneration policy are evaluated during the course of the remuneration policy's annual review and are duly implemented within an appropriate timeframe.
- (5) This circular explains a selection of issues regarding the application of remuneration provisions: the basic scope of application of provisions in the case of management companies and alternative investment fund managers (AIFMs), the definition of fixed and variable remuneration, the ban on circumventing legal provisions, the definition of particular categories of staff, the principle of proportionality, the applicability of Article 17c para. 1 nos. 11 to 14 InvFG 2011 as well as point 1 lits. m, n or both of Annex 2 to Article 11 AIFMG, as well as the ex post consideration of risk in variable remuneration and the criteria for measuring performance. Based on these statements, the management companies and

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<sup>1</sup> Guidelines on sound remuneration policies under the UCITS Directive (ESMA/2016/575)

<sup>2</sup> Guidelines on sound remuneration policies under the AIFMD (ESMA/2013/232) taking into consideration the Amendment of the AIFMD Remuneration Guidelines by ESMA/2016/579-EN.

AIFMs' independent assessment should be facilitated regarding how and in what manner the principles on remuneration pursuant to Article 17c para. 1 InvFG 2011 as well as point 1 of Annex 2 to Article 11 AIFMG are to be implemented.

- (6) Pursuant to Article 16 (3) of Regulation (EU) No. 1095/2010, the FMA is required in the enforcement of the AIFMG and the InvFG 2011 to apply the Guidelines, Recommendations and Standards issued by the European Securities and Markets Authority (ESMA) and to apply them pursuant to Article 54 para. 1 AIFMG as a decision-making guidance. Furthermore, the FMA may base its specific remarks about the remuneration policy on them as European practices pursuant to Article 17c InvFG 2011. ESMA comprehensively explains the remuneration provisions in Directive 2009/65/EC in the “ESMA Guidelines on sound remuneration policies under the UCITS Directive” published on 14.10.2016 (ESMA/2016/575).<sup>3</sup> Pursuant to Article 16 (3) of Regulation (EU) No 1095/2010 (the ESMA Regulation), financial market participants are required to take all necessary endeavours to comply with the ESMA Guidelines. The ESMA Guidelines on sound remuneration policies under the UCITS Directive (ESMA/2016/575) as well as the ESMA Guidelines on sound remuneration policies under the AIFMD (ESMA/2013/232)<sup>4</sup> are therefore also to be applied by the financial market participants as an interpretative aid.
- (7) Where designations used refer to natural persons, the formulation used applies to both genders.

## 2 LEGAL BASES

- (8) Articles 17a to 17c InvFG 2011 as well as Article 11 AIFMG including its annex form the legal bases for designing remuneration policies and practices in management companies and AIFMs. The cited provisions are respectively transposed into Austrian law by Article 13 in conjunction with Annex II AIFMD on “remuneration policies” and Articles 14a and 14b of the UCITS Directive.
- (9) Pursuant to Article 10 para. 1 no. 3 InvFG 2011 and point c of Article 57 (1) of Delegated Regulation (EU) No 231/2013, management companies and AIFMs are required to maintain appropriate internal control mechanisms to secure compliance with decisions and procedures on an ongoing basis. The risk management function is responsible for the

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<sup>3</sup> Similarly, ESMA has also comprehensively explained the remuneration provisions in Directive 2011/61/EU in the Guidelines on sound remuneration policies under Directive 2011/61/EU.

<sup>4</sup> Taking into consideration the Amendment of the AIFMD Remuneration Guidelines in ESMA/2016/579.

implementation of risk management policies and procedures. Article 17a para. 1 InvFG 2011 and Article 11 para. 1 AIFMG both stipulate that the remuneration policy and practice are compatible with a sound and effective risk management and conducive for this and should neither encourage them to take risks that are incompatible with the risk profiles or fund rules of the UCITS that they manage, nor should they prevent the management company or the AIFM from their obligation to act in the best interest of the UCITS or AIF.

- (10) False incentives in the remuneration structure of a management company or an AIFM may undermine an efficient and sound risk management. If the realisation of profits in the short-term is rewards and if employees are induced to continue to pursue activities that are associated with unreasonably high risks, then both the management companies as well as the funds that they manage are exposed to higher potential risks in the long-term as a result. The design of remuneration systems should be compatible with the risk profiles, the contractual conditions or articles of association of the UCITS or AIF that is managed by the management company and the objectives of the management company and the UCITS or AIFs it manages that are defined in the strategies.
- (11) Essentially, as is apparent from the remuneration provisions of the InvFG 2011 and the AIFMG, the granting and payment<sup>5</sup> of variable remuneration (boni, incentives, performance-related fees, etc.) at management companies and the AIFM are linked to two fundamental conditions in addition to risk policy aspects (see MN 9 in this Circular): variable remuneration must always be based on a sustainable performance, the amount of which must be tenable for the institution(s) concerned in accordance with the management company's or the AIFM's financial situation (see 7. Personal Performance and Company Success).
- (12) The principles for the remuneration policy are specified in Article 17c para. 1 InvFG 2011 as well as in point 1 of Annex 2 to Article 11 AIFMG. When determining and applying the remuneration policies and practice, the institutions shall, having taken the principle of proportionality into account, apply the principles for the remuneration policy in such a manner and such an extent that are appropriate for their size, internal organisation as well as the nature, scale and complexity of their activities.
- (13) The remuneration provisions in the InvFG 2011 or the AIFMG therefore oblige management companies and AIFMs, on the one hand to address the risks arising from remuneration

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<sup>5</sup> Granting means acquiring the general entitlement to variable remuneration. Payment mean the right effectively being paid out. The timing of both aspects may differ from one another, for example in the case that only 60% of the bonus is paid out immediately, and 40% is deferred for 5 years. During the deferral period, the entitlement is initially only conditional (see Section 6. Deferral below)

policies and practices as part of the general controlling of risks pursuant to Article 17a para. 1 InvFG 2011 as well as Article 11 para. 1 AIFMG, while on the other hand also define in Article 17c para. 1 InvFG 2011 as well as in point 1 of Annex 2 to Article 11 AIFMG how remuneration policies and practices are specifically to be designed.

### **SPECIAL TOPIC: REMUNERATION PROVISIONS AND CONTRACT LAW**

- (14) The respective remuneration provisions in the InvFG 2011 and the AIFMG are administrative law provisions rather than civil law ones. The statements set forth in this Circular will not have any influence on existing contracts.
- (15) Management companies or AIFMs are obliged to conclude contracts with their bodies and staff members in such a way in substantive terms that they fulfil the requirements set out in Articles 17a to 17c InvFG 2011 or Article 11 AIFMG including its Annex that the management company or the AIFM is able to act in accordance with the principles on remuneration (e.g. Ex post risk adjustment or clawback). Any remuneration contracts that have been concluded in violation of the law constitute a breach of supervisory law, and therefore incur the corresponding supervisory measures (e.g. A request to restore legal compliance or prohibiting the management of the institution, c.f. Article 148 InvFG 2011, Article 56 AIFMG, Article 70 para. 4 BWG).<sup>6</sup>

## **3 SCOPE OF APPLICATION**

### **3.1 FIXED AND VARIABLE REMUNERATION**

- (16) The remuneration provisions in the InvFG 2011 and the AIFMG cover remuneration policy and practices in management companies and AIFMs in their entirety, and therefore cover in principle all employee remuneration. Variable components in the remuneration policy however require special scrutiny as they could encourage employees to take excessive risks. It therefore also follows from the specific normative content of (most) of the principles on remuneration in Article 17c para. 1 InvFG 2011 as well as point 1 of Annex 2 to Article 11 AIFMG that the provisions focus on the regulation of variable remuneration i.e. remuneration

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<sup>6</sup> In this context, it is necessary to refer to the special case that applies to the remuneration agreements of the members of the management board. As the members of the management board are directly responsible for compliance with the provisions set out in the InvFG 2011, AIFMG and BWG, in the event of unlawful agreements they will not be able to insist on their being fulfilled (e.g. due to a lack of good faith). In any case, claims for damages may need to be looked into by the management company or the AIFM.

that is granted for having achieved a specific performance, and which therefore influences employees risk conduct.<sup>7</sup>

(17) Both the InvFG 2011 as well as the AIFMG define remuneration components as being either fixed or variable, with the consequence that in applying Article 17c para. 1 InvFG 2011 as well as point 1 of Annex 2 to Article 11 AIFMG remuneration is allocated to one of the two respective categories. In particular, it is necessary to take into account that every form of variable remuneration must be identified as being such irrespective of the label that is used for it. Against this background, it is also necessary to refer to the ban on circumventing of legal provisions pursuant to Article 17c para. 1 nos. 19 and 20 InvFG 2011 as well as lits. q and r of point 1 of Annex 2 to Article 11 AIFMG (see 3.4 on the ban on circumventing of legal provisions below).

(18) Remuneration components<sup>8</sup> are characterised as follows:

- a. Fixed remuneration components:
  1. Payments or benefits that do not take into account performance criteria
  2. Ancillary payments or benefits that are part of a general, non-discretionary policy at the level of the management company or the AIFM, provided that such ancillary payments do not constitute an incentive with regard to taking risks.
- b. Variable remuneration components:
  1. Additional payments or benefits that are granted based on performance criteria or in specific cases based on other contractual criteria, such as e.g. ESG criteria.

### 3.2 MANAGEMENT COMPANIES AND AIFMS AS PART OF A GROUP

(19) All management companies and AIFMs must draw up principles on remuneration that correspond with legal requirements and the Guidelines. In particular, no exceptions should exist regarding the application of the sector-specific principles on remuneration in accordance with the InvFG 2011, the AIFMG or Guidelines with regard to management companies and AIFMs that are subsidiaries of a credit institution. A remuneration policy that

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<sup>7</sup> Cf. Article 17c para. 1 no. 2 InvFG 2011 and point 1 lit. b of Annex 2 to Article 11 AIFMG, the principle of which also applies to fixed and non-performance related remuneration: For example it is the "long-term interest" that total personal costs (both fixed and variable costs) do not escalate to a level that is likely to undermine sustainable economic development.

<sup>8</sup> Old-age provision benefits are considered as part of a remuneration policy and shall be subject to the categories of remuneration components.

is applied on a group-wide basis is required to fully comply with the requirements set out in the laws and the Guidelines, and must be decided upon by the management company or the AIFM itself.

### **3.3 COMPETENT BODIES IN THE MANAGEMENT COMPANY OR THE AIFM**

- (20) Pursuant to Article 17c para. 1 no. 3 InvFG 2011 or point 1 lit. c of Annex 2 to Article 11 AIFMG the approval of the remuneration policy, as well as reviewing it regularly and the monitoring of its practical implementation shall be the responsibility of the supervisory board of the management company or the management body of the AIFM in its supervisory function. In this way the supervisory board or the management body of the AIFM in its supervisory function is standardised as the primary competent body for the monitoring of observance of the remuneration provisions. Both the legal conformity of the remuneration policy in terms of its content as well as its full and correct implementation in the management company or the AIFM falls under its responsibility. Furthermore, it must also be noted that the supervisory board or the management body of the AIFM in its supervisory function is not only responsible for reviewing the remuneration of the senior management, but is also required to pass resolutions on the issue of remuneration including those that have an impact on risk and risk management.
- (21) Management companies or AIFMs that are of significant relevance due to their size, the size of the funds that they manage, their internal organisation and the nature, scale and complexity of their business activities, shall be required to establish a remuneration committee pursuant to Article 17b para. 1 InvFG 2011 or point 3 of Annex 2 to Article 11 AIFMG. The remuneration committee is responsible for drawing up decisions in relation to remuneration, including those that have an impact on the risk and the risk management of the institution or the respective fund. The supervisory board of the management company or the management body of the AIFM in its supervisory function shall be responsible for the passing of resolutions.
- (22) Where a remuneration committee has been established pursuant to Article 17b InvFG 2011 at a management company, and where the decision-making powers of the supervisory board have been conferred to the remuneration committee, then the state commissioner and their deputy are required to be invited to the remuneration committee's meetings pursuant to Article 76 para. 4 BWG.

- (23) In the event that the remuneration committee has not been granted decision-making powers, its reports or draft decisions for subsequent supervisory board decisions must be subject to material discussions that allow the state commissioner attending the supervisory board's meetings to be aware of their content and to be able to issue a statement.

### **3.4 BAN ON CIRCUMVENTING OF LEGAL PROVISIONS**

- (24) Any (legal) construction is not allowed, which help to avoid that a remuneration provision is complied with, even though they would have to be applied in accordance with the principle of proportionality and the affected category of staff. Pursuant to Article 17c para. 1 nos. 19 and 20 as well as no. 1 lits. q and r of Annex 2 to Article 11 AIFMG, a variable remuneration is not allowed to be paid using instruments or processes that allow the requirements set out in the InvFG 2011 and the AIFMG to be circumvented. The cited provision standardises a general ban on circumventing legal provisions. The expression by means of “instruments or procedures” in Article 17c para. 1 no. 20 InvFG 2011 or in point 1 lit. r of Annex 2 to Article 11 AIFMG is to be understood in a broad sense.
- (25) In particular when transferring portfolio management or risk management activities it should be ensured that appropriate contractual arrangements exist with the establishments to which portfolio management or risk management activities are transferred, in order to ensure that it is not possible in accordance with these provisions to circumvent remuneration provisions.

### **3.5 CATEGORIES OF STAFF**

#### **3.5.1 GENERAL AND SPECIFIC PRINCIPLES OF THE REMUNERATION POLICY**

- (26) A distinction shall be made between general and specific principles of the remuneration policy with regard to the principles of the remuneration policy pursuant to Article 17c para. 1 InvFG 2011 as well as point 1 of Annex 2 to Article 11 AIFMG. While the general principles apply respectively for the entire management company or the entire AIFM and all staff members, the special principles only apply to particular categories of staff (also known as “identified staff” pursuant to ESMA/2016/575 or ESMA/2013/232). However, it is explicitly recommended to extend the scope of application of the special principles to the whole management company or the whole AIFM and all staff members.
- (27) Identified staff members are ones whose activities have a significant impact on the risk profile of the management company or the AIFM (see also point 3.5.2) and upon the variable

remuneration of which the more detailed special principles on remuneration shall also be applied.

(28) The following general principles in Article 17c para. 1 InvFG 2011 or point 1 of Annex 2 to Article 11 AIFMG (ESMA/2016/575 or ESMA/2013/232 Annex II) shall apply for the entire institution and all staff members:

- Article 17c para. 1 nos. 2, 3, 4, 5, 8, 20 InvFG 2011
- Point 1 lits. b, c, d, e, f, i, r of Annex 2 to Article 11 AIFMG

(29) In addition, the special principles for Article 17c para. 1 InvFG 2011 or point 1 of Annex 2 to Article 11 AIFMG (ESMA/2016/575 or ESMA/2013/232 Annex II) shall only apply for the identified staff:

- Article 17c para. 1 nos. 1, 6, 7, 9, 9a, 10 to 19 InvFG 2011
- Point 1 lits. a, g, h, j, k, l, m, n, o, p, q of Annex 2 to Article 11 AIFMG

### 3.5.2 DEFINITION OF THE CATEGORIES OF STAFF

(30) It is primarily the responsibility of the management company or the AIFM to define the categories of staff in the remuneration policy in such a way that this leads to an appropriate orientation of risks. Management companies and AIFMs should be in a position to provide the competent authorities with the proof about how they have evaluated and selected the categories of staff. Pursuant to Article 17a para. 1 InvFG 2011 or Article 11 para. 1 AIFMG, the following (although not exclusively) in any case shall belong to the categories of staff, whose activity has a significant impact on the risk profile on the management company, the AIFM or the funds that they manage:

- (1) the directors, authorised signatories and supervisory board members,
- (2) staff members that head investment management, administration, marketing, human resources, portfolio managers<sup>9</sup>
- (3) staff members with control functions
- (4) staff members that on the basis of the total remuneration that they receive are in the same income bracket as the managerial staff and risk-takers
- (5) other risk takers, whose professional activities have a significant impact on the risk profile of the management company or the AIFM or one of the UCITS or AIFs that they manage.

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<sup>9</sup> Provided they have significant influence on the AIFM's risk profile. The management of a portfolio is always to be considered as a significant influence.

### **3.5.3 ALLOCATION OF STAFF MEMBERS**

(31) The management companies and AIFMs shall allocate members of staff to the category of identified staff based on the categories of staff in the remuneration policy. The decision making process regarding the determining of the identified staff must be appropriately documented by management companies or the AIFM, so that the necessary proof may be furnished towards the competent authorities, about how the identified staff are assessed and selected.

## **4 PRINCIPLE OF PROPORTIONALITY**

### **4.1 GENERAL**

(32) Pursuant to Article 17c para. 1 InvFG 2011 or point 1 of Annex 2 to Article 11 AIFMG management companies and AIFMs shall apply the principles of remuneration policy and practices proportionately in accordance with their size, their internal organisation and the nature, scale and complexity of their activities. The principle of proportionality should also apply for the categories of staff members within a management company or an AIFM. A few specific requirements shall apply for identified staff that are not necessarily required to apply for the entire workforce.

(33) The principle of proportionality contained in Article 17c para. 1 InvFG 2011 or point 1 of Annex 2 to Article 11 AIFMG applied to both the general and specific principles. In so doing, the principle of proportionality works both ways: a few institutions will be required to the establish more demanding standards due to their size and increased complexity or for their staff members that are most relevant in terms of risk, while other companies will be able to prescribe more simple rules on the basis of their less large or complex nature, or for their less relevant staff members in terms of risk, or even both. The manner and extent of the application of the remuneration principles must always adequate for the individual risk situation.

### **4.2 PROPORTIONALITY BETWEEN INSTITUTIONS AND BETWEEN CATEGORIES OF STAFF**

(34) According to the wording of Article 17c para. 1 InvFG 2011 or point 1 of Annex 2 to Article 11 AIFMG, it is necessary to distinguish between the institution-based proportionality between the management companies and the AIFM (size; internal organisation; and the nature, scale

and complexity of their activities), and proportionality between the staff members (categories of staff, the type and amount of remuneration, as well as the activity's impact on risk profile). Management companies and AIFMs that are of significant relevance in terms of risk policy, must in particular be identified.

#### **4.2.1 PROPORTIONALITY BETWEEN INSTITUTIONS**

(35) The management company or the AIFM shall be primarily responsible for reviewing their own characteristics and for drawing up and implementing remuneration policies and practices that lead to an appropriate alignment of risks and create an appropriate and effective incentive for employees. In addition to the institution-specific risk alignment, this review also covers the risk alignment relative to the national and international market as a whole.

(36) Management companies and AIFMs that are of significant relevance due to their size, the size of the funds that they manage, their internal organisation and the nature, scale and complexity of their business activities, shall be required to establish a remuneration committee pursuant to Article 17b para. 1 InvFG 2011 or point 3 of Annex 2 to Article 11 AIFMG (see also MN 21 of this Circular). Accordingly, the management company or the AIFMs must make an allocation about whether or not the activities are of significant relevance overall. In contrast, for less or non-complex institutions, while the establishment of a remuneration committee is not mandatory, it is nevertheless recommended.

(37) To aid understanding the concept of proportionality between institutions is explained below in a very schematic form:

- Complex management companies and AIFMs:
  - Comprehensive and detailed application of the principles on remuneration
- Less or non-complex management companies and AIFMs:
  - Partial simplified application of the principles on remuneration
  - Where applicable the non-application of the principles on payment with instruments, deferral and ex post consideration of risk in variable remuneration (Article 17c para. 1 nos. 11 to 14 InvFG 2011 or point 1 lits. m, n or both of Annex 2 to Article 11 AIFMG).

(38) The requirement to perform a separate, detailed assessment of the size, internal organisation as well as the nature, scale and complexity of the activities in every

management company or every AIFM naturally remains unaffected by the aforementioned overview-like delineation. The criteria below in particular indicate increased complexity:<sup>10</sup>

Size: respectively in relation to the national market:

- Value of the capital of the management company
- Value of the managed asset items including leveraged financing
- Number of employees
- Number of branches or subsidiaries
- Number of managed funds

Internal organisation:

- Legal structure of the management company, the AIFM or the funds managed
- Complexity of the internal governance structure (e.g. a multi-level organisation)
- Whether the management company, the AIFM or the funds managed are exchange-listed

Nature, scale and complexity of business activities:

- The type of authorised business (whether exclusively collective portfolio management or also other ancillary services requiring a licence);
- The type of investment policies and strategies of the managed funds;
- The national or cross-border nature of the business
- Management of both UCITS as well as AIFs

(39) The aforementioned criteria should be viewed holistically within a flexible system rather than individually. If however a specific criterion is particularly exaggerated (e.g. size), then this may be assigned a greater or even decisive weighting in the overview.

#### **4.2.2 PROPORTIONALITY BETWEEN CATEGORIES OF STAFF**

(40) Following the proportionality test for the management company or the AIFM ("complex" or "less or non-complex"), in a second subsequent stage a proportionality test is conducted within the institution among the staff members. Pursuant to Article 17a InvFG 2011 of Annex 2 to Article 11 AIFMG, all principles for the remuneration policy apply to certain categories of staff, while simplified provisions may apply for the remaining categories.

(41) It also applies regarding proportionality between employees that such proportionality may lead to a simplified application of some or all principles on remuneration, but that the

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<sup>10</sup> Cf. ESMA/2016/575 para. 25 et seq. and ESMA/2013/232 para. 29 et seq regarding the criteria.

minimum requirements prescribed under law must nevertheless still be fulfilled (see the following provisions regarding exemptions regarding complete non-application).

### **SPECIAL TOPIC: SIGNIFICANCE THRESHOLD AND NEUTRALISATION OF CERTAIN PRINCIPLES ON REMUNERATION (ANALOGUE TO ARTICLE 39B BWG)**

- (42) Following the principle of proportionality in point 13 of the Annex to Article 39b BWG, the legislator has created an explicit exemption for credit institutions from applying the special principles on remuneration in point 11 (payment using instruments and with a retention period), point 12 introductory part (deferral and therefore to a large extent<sup>11</sup> the ex post risk adjustment), as well as point 12 lit. b second and third sentences (voluntary pension contribution payments) for “small” credit institutions or “small” boni.
- (43) To date, the legislator has not followed suit in relation to these explicit exceptions to the rules under banking law in either the InvFG 20211 or the AIFMG. However, the principle of proportionality allows certain possibilities in not applying certain principles to variable remuneration of small amounts, where there is no risk whatsoever of the respective staff members being encouraged to take on risk or otherwise not to act in accordance with the obligation to act in the best interests of the unit-holders or investors.
- (44) Provided that the management company or the AIFM documents in a transparent, comprehensible and detailed manner about why neutralising certain principles does not negatively impact the management company, the AIFM or the managed funds, the following principles may be neutralised:
- Article 17c para. 1 nos. 11 to 14 InvFG 2011
  - Point 1 lits. m, n, or both of Annex 2 to Article 11 AIFMG as well as
  - Ex-post consideration of risk in variable remuneration.
- (45) Analogously to point 13 of the Annex to Article 39b BWG, such a neutralisation may only be made use of by non-complex management companies or AIFMs. In addition, the above principles, analogously to point 13 lit. b of the Annex to Article 39b BWG, must not be applied to employees, regardless of whether in whether in complex or non-complex management companies or AIFMs, where annual variable remuneration does not exceed EUR 50,000 and does not amount to more than one third of the total annual remuneration (50% of the fixed remuneration) of the respective employee.

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<sup>11</sup> The ex-post risk adjustment does not apply insofar as a variable remuneration that is not deferred can in principle also no longer be reduced ex-post. However, any clawback requirement even after disbursement (“clawback”) is not covered by the provisions on exemptions (see 6.2 on Ex-post risk adjustment below regarding the difference between malus and clawback arrangements).

(46) Without prejudice to the aforementioned legal exemptions and its official power pursuant to Article 17c para. 3 InvFG 2011 and Article 11 para. 3 AIFMG, the FMA recommends that management companies or AIFM should nevertheless consider the application of the special remuneration principles (payment with instruments, vesting period, deferral and ex-post risk adjustment) in the case of high variable remuneration or high-risk transactions in the interest of sustainable governance.

## 5 PAYMENT USING INSTRUMENTS

### 5.1 APPLICABILITY

(47) According to the wording of Article 17c para. 1 no. 11 InvFG 2011 of point 1 lit. m of Annex 2 to Article 11 AIFMG a considerable proportion of the variable remuneration, which is at least 50%, must either consist of units in the UCITS or AIF in question, in comparable shares in associated companies or instruments that are linked with units or comparable non-cash instruments.

(48) The principle on payment using instruments belongs to the special principles on remuneration. Its application is restricted to the categories of staff listed in Article 17a para. 1 InvFG 2011 or Article 11 para. 1 AIFMG. In less or non-complex management companies and in such AIFMs (c.f. 4.2.1 proportionality between institutions) the cited principle shall be applied in accordance with the principle of proportionality. In complex institutions in which the principle is fully applicable, it may suffice to pay only 50% of the variable remuneration with instruments, although a higher proportion may be necessary for more high-ranking risk-takers.

(49) The application of the principle of payment using instruments is subject to relevant instruments having been issued, and their being securitised and transferable. Under this principle, management companies or AIFMs might therefore not issue their own instruments in order to apply the principle. This applies for non-complex and complex institutions alike.

(50) A management company or an AIFM is free to decide whether to assist such capital items or to develop other innovative solutions especially non-cash instruments with incentives (e.g. "phantom plans"). For example management companies or AIFMs might consider the remuneration of staff members by means of representative (umbrella) funds.

(51) In addition, it is noted that a non-application of the principle of paying with instruments, due to a lack of instruments shall not have any influence of the categorisation as a large or

complex management company or a large or complex AIFM. In such instances greater attention is to be paid to the application of the other principles for the remuneration policy.

## 5.2 RETENTION PERIOD<sup>12</sup>

- (52) Where 50% or more of the variable remuneration is paid out in the form of instruments, then the instruments shall be subject to a suitable deferral policy pursuant to Article 17c para. 1 no. 12 InvFG 2011 or point 1 lit. m of Annex 2 to Article 11 AIFMG respectively.
- (53) In accordance with the ESMA Guidelines guidance on deferral should be determined in the remuneration policy of the management company or the AIFM. As the most important element of the guidance on deferral retention periods should be linked to the subscribing to instruments. A retention period is defined as a “period of time during which variable remuneration that has been already vested and paid out in the form of instruments cannot be sold.” It should be noted that the retention period is independent for the deferral period, and therefore the retention period will not be included in the calculation of the minimum deferral period of 3 to 5 years.
- (54) Therefore the deferral policy or retention period are to be distinguished from the term of deferral pursuant to Article 17c para. 1 no. 13 InvFG 2011 or point 1 lit. n of Annex 2 to Article 11 AIFMG (ESMA also defines this as the “deferral period”<sup>13</sup>, which is defined as the period during which variable remuneration is withheld following the end of the accrual period). In the case of deferral pursuant to Article 17c para. 1 no. 13 InvFG 2011 or point 1 lit. n of Annex 2 to Article 11 AIFMG the staff member’s entitlement to the deferred portion of the variable remuneration is only a conditional one: Where the incentivised performance is proven to be non-sustainable, or in the event of a deterioration of the financial and earnings situation, deferred remuneration may be partially or fully cancelled (explicit ex-post risk adjustment). In contrast, during the retention period pursuant to Article 17c para. 1 no. 12 or point 1 lit. m of Annex 2 to Article 11 AIFMG, the employee is already the owner of the instruments, but may not sell them. The staff member continues to participate in the (lack of) success of the entity (implicit ex post risk adjustment).
- (55) The management company or AIFM’s remuneration policy shall draw up guidelines on the retention period in line with the business model and risk profile to be adopted by the competent body. The minimum deferral period must be sufficient to align the incentives

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<sup>12</sup> Cf. paras. 140ff ESMA/2016/575 about retention periods.

<sup>13</sup> See ESMA Guidelines ESMA/2016/575, p. 6 for the definition of this term.

with the longer-term interests of the management company or the AIFM, the UCITS or AIFs that they manage, and their investors. Overall, the retention period and the length of deferral have to be in line with the holding period recommended to the unit-holders of the UCITS or AIF in question. For example, a retention period of three years shall not be considered equivalent to a deferral period of the same length, since it lacks an option for ex-post risk adjustment.

- (56) The legislator does not explicitly stipulate a minimum retention period. In the case of instruments that have been disbursed previously retention periods are the only available mechanism to highlight the difference between an upfront cash payment and pre-granted instruments in order to provide for a longer-term balance of interests between the management company, the AIFM and the funds they manage and the investors of these funds. Accordingly, a retention period of at least one year shall be provided. According to ESMA Guidelines, instruments are valued from the date of these instruments being granted, from when the retention period starts to run.
- (57) The retention period applies for all instruments, both for those that are deferred as well as instruments that are not deferred.

## 6 DEFERRAL

### 6.1 DEFERRAL PERIOD

- (58) Pursuant to to Article 17c para. 1 nos. 13 and 14 InvFG 2011 or point 1 lit. n of Annex 2 to Article 11 AIFMG, at least 40% of the variable remuneration must be deferred over a period of time that is appropriate for the life cycle of the funds in question that is at least three to five years. The deferred remuneration may not be acquired more quickly during this minimum period that is permitted on a pro rata basis, i.e. in the case of a five year deferral, a maximum of one-fifth of the deferred amount may be acquired each year.
- (59) Pursuant to to Article 17c para. 1 nos. 13 and 14 InvFG 2011 or point 1 lit. n of Annex 2 to Article 11 AIFMG, the share of the variable remuneration that should be deferred is between 40% and 60%, depending on the influence of the employee (or employee category) on the risk profile of the funds managed and depending on the responsibilities and tasks performed as well as the amount of the variable remuneration.

## 6.2 EX-POST RISK ADJUSTMENT

- (60) Pursuant to to Article 17c para. 1 no. 10 InvFG 2011 or point 1 lit. l of Annex 2 to Article 11 AIFMG a comprehensive corrective mechanism must be established for performance measurement. Accordingly, the disbursement of variable remuneration, including the deferred portion, shall only take place where viable to do so in light of the financial situation of the management company or the AIFM, and following justification of the performance of the business unit, the fund managed and the person in question (Article 17c para. 1 no. 15 InvFG 2011 or point 1 lit. o of Annex 2 to Article 11 AIFMG).
- (61) During the deferral period, if it emerges that the performance that was being incentivised was either not sustainable (malus), or where a pay-out would not (or no longer) be compatible with the management company or the AIFM's financial situation, the pay-out of the deferred portions should be cancelled (malus arrangement see also Section VII below Personal Performance and Company Success). The management company or the AIFM is required to ensure that organisational and legal frameworks (including the design of contracts) are created in order to ensure that this principle on remuneration is applied effectively.
- (62) Under no circumstances shall the explicit ex-post risk adjustment (for both cash payments as well as for instruments) lead to an increase in the deferred part. In the event that the paying out of (deferred) variable remuneration is cancelled for one or several years due to one of the aforementioned circumstances prevailing, it shall not be permissible to make good the pay-out in later years (e.g. once the institution has recovered financially). A subsequent payment would also contradict the requirements of Article 17c para. 1 no. 15 InvFG 2011 or no. 1 lit. o of Annex 2 to Article 11 AIFMG and thus effectively constitute a circumvention.
- (63) For particularly severe cases of unsustainable performance (in particular fraud as well as intentional or grossly negligent damage to the management company, the AIFM or the managed fund), the possibility of a clawback agreement is to be provided in addition to the malus agreement. The ESMA Guidelines define clawback as a "*contractual agreement in which the staff member agrees to return ownership of an amount of remuneration to the management company under certain circumstances...*". Where the malus agreement is limited to deferred variable remuneration only, i.e. remuneration that has been awarded but not yet transferred, any clawback also covers bonuses and incentives that have already become the property of the employee.

## 7 PERSONAL PERFORMANCE AND COMPANY SUCCESS

### 7.1 GENERAL

- (64) Pursuant to Article 17c para. 1 no. 15 InvFG 2011 or point 1 lit. o of the Annex to Article 11 AIFMG the granting or payment of must on the one hand be justified by the personal and sustained performance of the staff member as well as that the fund, while on the other hand also being viable in terms of the financial situation of the management company or the AIFM. The total variable remuneration is to be significantly limited, in the event of the financial or earnings situation deteriorating. Variable remuneration is therefore conditional on the individual employee's personal performance as well as that of the management company or the AIFM as well as the managed fund (cf. MN 11 of this Circular).
- (65) It should be noted that the conditionality of variable remuneration based on the company's success is standardised in a special principle for remuneration (identified employees, risk-takers in a broad sense) (see above 3.5.1. General and special principles of the remuneration policy). Pursuant to the principle of proportionality, the differentiation into identified staff pursuant to Article 17a InvFG 2011 or Article 11 para. 1 AIFMG and other staff members should be taken into account, in that (negative) changes to the financial and earnings situation in a management company or the AIFM take effect to a greater extent or at an earlier stage on the variable remuneration of identified staff, than on the variable salary components of other staff members. Accordingly, the bonuses and incentives of other staff members shall be reduced or cancelled only in severe cases of financial failures.

### 7.2 VARIABLE REMUNERATION AND PERSONAL PERFORMANCE

- (66) As defined in Article 17c para. 1 nos. 6 and 15 InvFG 2011 or point 1 lits. g and o of Annex 2 to Article 11 AIFMG, the personal criteria for assessing whether variable remuneration is granted or paid out should be as close as possible to the area of responsibility of the individual employee. A director would be required to consider the result of the entire management company or the AIFM, whereas a head of department should consider the performance of their department, etc.
- (67) From this perspective, variable remuneration is frequently not permitted for members of the management board, heads of divisions or departments, as well as staff members that produce a loss within their area of responsibility. Possible exceptions are group members and organisational units that do not generate (direct) profits (IT, facility management, etc.)

as a matter of principle, as well as where it is consciously taken into account for business policy reasons not to generate a profit (e.g. during the start-up phase or conversely in the orderly exit from a business field). Key performance indicators (KPIs) are to be agreed upon in relation to organisational units that do not generate a direct profit.

- (68) In addition to the personal performance, the success/failure of the respective division or the entire institution must always also be taken into consideration, as well as the performance of the funds managed i.e. factors that are also not dependent on the personal performance of the individual staff member.

### 7.3 VARIABLE REMUNERATION AND COMPANY SUCCESS

- (69) From Article 17c para. 1 nos. 6 and 15 InvFG 2011 and point 1 lits. g and o of Annex 2 to Article 11 AIFMG it follows that an employee's (deferred) variable remuneration must also be reduced or even cancelled if although justified based on their personal performance, but where its granting or payment is precluded by the overall economic situation of the management company or the AIFM.
- (70) Such principles do not generally exclude the granting or payment of variable remuneration those employees who have achieved their performance targets, even though a net loss was generated in a year. Under such provisions, variable remuneration would not be permissible, in the event that a substantial net loss is incurred, or in the case that an adequate capital base no longer exists, or is unable to be sustained.
- (71) From MN 69 and 70 it follows in the event of net losses that the entire variable remuneration, in particular for the special employee categories pursuant to Article 17a InvFG 2011 or Article 11 para. 1 AIFMG ("identified employees" or "risk-takers in a broad sense"), must be significantly reduced or even completely eliminated. In any case, this shall be required to be done where maintaining or attaining minimum own funds requirements required under supervisory law is no longer guaranteed.

## 8 PERFORMANCE CRITERIA

- (72) Variable remuneration shall be granted where targets in this regard (employee performance as well as successes of their department) have been achieved at the management company, or the AIFM, or the managed fund (cf. Article 17c para. 1 nos. 6, 7, 10, 15 and 16 InvFG 2011 or point 1 lits. g, h, l and o of Annex 2 to Article 11 AIFMG).

- (73) Quantitative and qualitative (financial and non-financial) criteria are to be used for the evaluation of performance and success in a multi-year framework (Article 17c para. 1 nos. 6 and 7 InvFG 2011 or point 1 lits. g and h of Annex 2 to Article 11 AIFMG). However, the principle of proportionality also applies in this case.
- (74) Especially in the case of variable remuneration of the members of the management body and the senior management, as well as for high variable remuneration, attention must be paid:
- (1) The performance criteria must be determined for the predominant part of the variable remuneration to a sufficient extent to determine in an objective manner that targets have been achieved.
  - (2) The performance criteria must be determined in advance, i.e. at the latest at the start of the performance period, and documented in a comprehensible manner.
  - (3) As a rule<sup>14</sup>, performance criteria cannot be changed or supplemented afterwards.
  - (4) The process for measuring performance must ultimately also be documented in a comparably plausible manner.
- (75) The aforementioned requirements conclusively follow the wording of the law, on the one hand binds the granting of variable remuneration to performance and to predetermined performance criteria in this regard, while on the other hand also prohibiting any activity whatsoever from circumventing this (cf. Article 17c para. 1 nos. 6, 7, 10, 15 and 20 InvFG 2011 or point 1 lits. g, l, o and r of Annex 2 to Article 11 AIFMG; paras. 11, 14 to 16 and 101 to 160 ESMA/2016/575, or paras. 10, 15, 17, 18, 99 to 158 ESMA/2013/232 respectively).

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<sup>14</sup> In the case of exceptional changes or additions to the performance criteria, their necessity and appropriateness must be justified in a plausible way and duly documented. In any case, it would be inadmissible to reward exceptional performances to overcome a crisis that itself was caused by the beneficiary as a result of previously taken decisions.