Fondbolagens förening
SWEDISH INVESTMENT FUND ASSOCIATION

EBA/ESMA

2024-09-03

Response to EBAs and ESMAs Call for advice on the investment firms prudential framework

Q24. Do you have any views on the possible ways forward discussed above concerning the provision of MiFID ancillary services by UCITS management companies and AIFMs?

The Swedish Investment Fund Association (SIFA) believes it is imperative that a limitation of fund management companies possibility to manage individual portfolios is not introduced.

Today, in accordance with the UCITS Directive and AIFMD, fund management companies may provide management of portfolios of investments, including those owned by pensions funds (individual portfolio management). There is no indication in the legal texts that the management of such portfolios is in any way restricted. On the contrary, the wording only states that management companies "may provide" such services, with no reference to "ancillary" or "non-core" services (Article 6[3] of the UCITS Directive and Article 6[4] of AIFMD). When it comes to investment advice and safe-keeping of fund units, those services are listed as "non-core services", which indicate that they should be seen as ancillary, however, not necessarily as a limitation of the amount of provided services. In practice, fund management companies today manage individual portfolios without any limitations as to the amount of such services. There is no evidence that the combined provision of services of collective and individual portfolio management has given rise to any problems. On the contrary, the combined service is requested by clients and provides for economies of scale and cost-efficiency which will benefit the clients.

Nevertheless, if the two options (point 212 in the Discussion Paper) were to be considered, SIFA believes that limiting the amount of provided individual portfolio management would distort competition and give rise to unnecessary administrative burdens to the detriment of clients. SIFA believes this option is not feasible without large negative effects to the market.

Limiting the amount of provided individual portfolio management would mean that larger mandates from e.g. pension funds cannot be accepted by fund management companies, despite obvious synergy effects with the management company's collective

portfolio management. It would ultimately be to the detriment of investors if such economies of scale were reduced.

It would distort competition if fund management companies were not able to provide individual portfolio management on equal terms with investment firms that perform the same service. It would ultimately make it impossible to provide management on an individual basis to clients which request such services. Since there are no alternative licences or company forms that allow both individual and collective portfolio management within the same unit, a management company that wishes to continue providing individual portfolio management would be forced to set up a separate investment firm. This would make the service more expensive to clients while creating an excessive administrative burden to fund managers. Authorisation to manage individual portfolios provides an opportunity to meet the needs of clients and retain clients even in cases where the fund management company is not part of a group with an investment firm.

When it comes to capital requirements they should, as a starting point, be the same for companies providing the same services. Notably, capital requirements for fund management companies and investment firms are very similar. The initial capital requirements are higher for fund management companies than for investment firms that provide similar services. Fund management companies should hold additional capital depending on the size of the collective portfolios and should as a minimum requirement hold capital of 25 % of fixed overheads. As far as SIFA has experienced, the capital requirement for a fund management company often ends up at the minimum requirement of 25% of fixed overheads. Additional capital requirements in relation to assets under management would in practice have little effect but increase the complexity of the regulation.

If the inclusion of a capital requirement relating to the management of individual portfolios should nevertheless be considered, it should be constructed as simple as possible in order to not increase the regulatory burden. For example, the assets managed in individual portfolios could be added to those of the collective portfolios (i.e. a capital requirements equal to 0.02 % of the assets exceeding EUR 250 million subject to a limit of EUR 10 million).

Regardless of the method chosen, it is important that portfolios managed under delegation received from other institutions that are subject to capital requirements based on the assets are deducted from the assets under management. One example is portfolios managed on behalf of an insurance company. Capital requirements for the same capital both at the firm delegating the management and the firm managing the assets under a delegation agreement, would make it financially impossible to delegate such management.

Q27. Is the different scope of application of remuneration requirements a concern for firms regarding the level playing field between different investment firms (class 1 minus and class 2), UCITS management companies and AIFMs, e.g. in terms of the application of the remuneration provisions, the ability to recruit and retain talent or with regard to the costs for the application of the requirements?

It is a serious concern that the requirements are not the same. It is important that the derogations introduced for investment firms are also introduced for fund managers. The different scope has led to an uneven playing field.

Due to the ambiguities of the remuneration requirements for UCITS management companies and AIFMs, competition is distorted not only between fund management companies and other financial institutions, but also between fund management companies established in different Member States. While some Member States have introduced different types of derogations for fund managers with reference to the principle of proportionality, others perceive that the rules do not allow such derogations. In Sweden, the supervisory authority has communicated that, in light of the absence of explicit derogations in the UCITS Directive and AIFMD and what has previously been communicated by the Commission, it is not possible to introduce derogations equivalent to those that apply to investment firms, even if such derogations would be desirable (Letter from Finansinspektionen to the Ministry of Finance on the need to revise the remuneration requirements in the UCITS Directive and the AIFMD, 2021-06-01, FI dnr 21-14621).

Hence Swedish fund management companies may not benefit from any derogations to the provisions on variable remuneration, but are obliged to apply the provisions on deferral and pay out in instruments regardless of the size of the remuneration and the size of the company. As has already been established for investments firms, such application is not proportionate. It is associated with disproportionate costs to apply these rules to smaller amounts of variable remuneration.

This means that fund management companies have to bear costs that other financial institutions do not have, which creates an unlevel-playing-field. In many cases the administrative burden has led to the removal of variable remuneration. This, of course, has a negative effect on the ability to recruit and retain staff. To compensate, the fixed salaries have to be raised, which is problematic from a competition point of view but also to the clients. When fund management companies have to refrain from variable remuneration, there is no longer the link between remuneration and result that many investors find desirable. It also, in general, increases the fixed overheads, which is a disadvantage.

The different provisions also cause problems when fund management companies delegate management to an investment firm. The ESMA guidelines on sound remuneration policies under the UCITS Directive and AIFMD state that the provisions must not be circumvented in the event of delegation and that this must be ensured through agreements. The fund management company must therefore require the investment firm to comply with the stricter requirements that apply to the fund management company, which creates an obstacle to delegation.

Consequently, it is urgent that the provisions on remuneration policies applicable to fund management companies be revised to achieve a level-playing-field with investment firms.

Q29. Are the different provisions, criteria and thresholds regarding the application of derogations to the provisions on variable remuneration, and that they apply to all investment firms equally without consideration of their specific business model, a concern to firms regarding the level playing field between different investment firms (class 1 minus under CRD and class 2 under IFD), UCITS management companies and AIFMs, e.g. in terms of the application of the remuneration provisions, the ability to recruit and retain talent or with regard to the costs for applying the deferral and pay out in instruments requirements? Please provide a reasoning for your position and if possible, quantify the impact on costs and numbers of identifies staff to whom remuneration provisions regarding deferral and pay out in instruments need to be applied.

As stated in our answer to Q 27 it is important that the same explicit derogations to the deferral and pay out in instruments requirements as in the IFD are introduced in the UCITS Directive and the AIFMD.

This would provide legal certainty to fund managers, reduce unproportionate costs for smaller companies and lower remunerations, and ensure a level-playing-field.

In Sweden applying the deferral and pay out in instruments requirements are, due to legal uncertainty, mandatory to all remuneration to identified staff, regardless of how small the remuneration is. Administrative costs consist of IT systems, human resources and consulting, which are estimated at between €100,000 and €500,000 as one-off costs, and between €50,000 and €200,000 in annual costs. The fact that smaller fund management companies must bear theses costs that other financial institutions do not have creates an unlevel-playing-field.

In many cases smaller companies will not be able to take those costs but will have to remove the variable remuneration. This will have a negative effect on their ability to recruit and retain staff compared to other financial institutions that may benefit from derogations. A raise of the fixed salaries to compensate is also problematic from a competition point of view since it will increase fixed overheads. It is often not desirable to clients that the link between remuneration and result is removed, why the removal of variable remuneration in itself could be a competitive disadvantage for fund managers.

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