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# Board Walk

Briefing for Remuneration Committees

SPECIAL EDITION FOR ALTERNATIVE FUND MANAGEMENT FIRMS – APRIL 2014

**This edition of Board Walk includes:**



## AIFMD Remuneration Code – who gets caught?

***Nigel Mills and Damien Knight review the action that firms need to be taking to comply with the pending Code***

UK alternative investment managers (AIFMs) - private equity and venture capital houses and hedge fund managers - are currently wrestling with the wide-ranging requirements of the Alternative Investment Fund Managers Directive (AIFMD) central to which is the need to apply to the FCA for authorisation (re-registration as an AIFM) by 22 July of this year if they wish to continue marketing their AIFs and investing funds.

Provided they apply for this variation of permission in time, firms will be able to continue in business pending receipt of authorisation provided they comply with the Directive as enshrined in the UK Alternative Investment Fund Managers Regulations (Statutory Instrument 2013 No. 1773). Not least of their problems will be compliance with the remuneration requirements of the Directive which are now separately contained in the AIFM Remuneration Code (the Code) issued by the FCA last July and with which UK full-scope AIFMs (ie AIFMs not exempt on account of their size) must comply as soon as they are authorised, both in the management of their own staff and in their management of any firms to which they have delegated fund management functions. The Code has imported directly the requirements listed in the Directive and requires full compliance with the associated AIFMD Guidelines on Sound Remuneration Policies published by the European Securities and Market Authority (ESMA) last July (The ESMA Guidelines).

The cutting edge of the Code is concerned with the structure of variable pay for "Code Staff" (ie senior managers and other staff with a high risk impact on the firm and its funds). The Code potentially imposes drastic constraints on the range of plan measures and on the timing, form and adjustment of variable pay received (the so-called "pay-out process"). It requires a large proportion to be paid in units of the funds managed (if practicable), deferred over 3-5 years and subject to 'malus'. These restrictions will apply from the first financial year following authorisation, so most firms will certainly have to consider the performance measures (and plan rules) in time for January 2015 and will be required to defer a large proportion of bonus payments after January 2016. But the application for authorisation due in by July itself requires a statement of policy that will need to be compliant with the Code so there is a need for much earlier attention to future policy intentions.

**PULSE SURVEY –**

**FIND OUT WHAT OTHER FIRMS ARE UP TO**

Please take a few minutes to complete our PRIVATE EQUITY AND VENTURE CAPITAL PULSE SURVEY which covers:

- Latest pay review levels and changes in bonus pools
- Priorities and factors in bonus allocation
- Planned changes in staff numbers
- Planned remuneration package changes
- Responses of firms to the AIFMD Remuneration Code
- Responses of LLPs to new "disguised salary" rules

Click on this link to go to the survey questionnaire. Those completing the questionnaire will receive a copy of the survey findings report at the end of April. Do not forget to add your e-mail address.

### Avoiding the restrictions

What are the chances of avoiding the worst of these restrictions? Most firms will hope to be able to apply proportionality on the grounds of size. The FCA's additional Guidance (FCA Guidance) issued in January (see inset panel on Page 2) offers a threshold of size as a starting presumption – assets under management below £1bn in leveraged funds (or £5bn for unleveraged funds with a 5 year investor lock-up) but it makes it clear that a decision to disapply the Code Staff pay-out process (the only part of the Code that can be disapplied) should also take into account other factors that might increase or decrease the risks to the firm or funds. It is down to the firm to ensure its remuneration is aligned with the sound management of these risks.

## The FCA Guidance

This January, the FCA published its own Guidance which clarified certain areas of the Directive and ESMA Guidelines, notably:

- The timing of transition to the new requirements
- How proportionality should be applied to firms and to their individual Code Staff – which helps firms decide when they might disapply some of the Code requirements
- How payments to partners in an AIFM constituted as an LLP should be treated (see article by JD Ghosh on Page 4 for other remuneration concerns affecting partnerships)
- The practical application of the requirement in the Directive to pay 50% of Code Staff variable remuneration in "instruments" ie units in the managed funds or similar
- What "retention" might mean in practice. The Directive and ESMA Guidelines distinguish between retention and deferral, the individual having ownership of the award (but being restricted from selling) in the first case and not yet having received the award in the latter.

The FCA allows itself the right to require firms to report their payout process and justify it, although there is no mandatory annual remuneration statement such as must be submitted by Tiers 1 and 2 under the Banking and Financial Services (CRD III) Remuneration Code. Firms are invited to publish a remuneration statement for stakeholders at large but the only mandatory reporting requirement is within the annual reports of the individual alternative investment funds (AIFs) that are being managed, where aggregates of fixed and variable remuneration paid for the AIFM and for categories of Code Staff have to be provided. The Directive requires each AIF to have a single AIFM .

How many firms are likely to be caught? MM&K reviewed the assets under management of the firms covered by the two private equity remuneration surveys we ran in 2013. Half of the total of 45 firms participating are above the presumptive threshold, although most of these are in the large or large mid-market category. Some of these firms have already identified themselves as Tier 3 under the CRD Remuneration Code and under that code are disapplying the rules for retained instruments, deferral and performance adjustment. Although the AIFMD Code recognises its sister code as applying equally rigorous risk alignment to remuneration, firms should not assume that their disapplication under the earlier code will apply under the AIFMD regime, not least because the proportionality thresholds are lower in the latter.

Secondly, private equity and venture capital firms at least are hoping they can argue disapplication of the pay-out rules when they are operating long-term carry plans. The characteristic of these plans is that they pay out on cash realisations after the Limited Partners (external investors) have recovered all their investment plus a hurdle. They are therefore, it is argued, inherently risk aligned. ESMA Guidelines Paragraph 159 expressly provides a basis for arguing this disapplication.

Most hedge fund managers will not have this argument to fall back on, although, given the very wide spread of investment strategies and remuneration models in the hedge fund industry, it is possible that some may.

**Carry plans are risk-aligned, but are they inherently compliant with the rules?**

In private equity/venture capital firms, will the variable payouts under carry plans really stand up to scrutiny from the FCA? The ESMA Guideline tests for a carry plan that is 'risk compliant' are:

- Limited Partners receive back all investment plus the agreed hurdle rate, before any carry is paid
- Code Staff compensation (bonus plus carry) is subject to clawback until the liquidation of the relevant AIF.

We would expect any normally-designed carry plan to pass these tests. Moreover the management fee from which any bonus is paid often also has ultimately to come out of the carry pot for the firm.

We decided to look at the data in our main private equity survey to see if typical carry plans would in any case satisfy the payout process rules for Code Staff. These rules require that:

1. 50% of variable remuneration is paid in fund units
2. 40% of the payout (60% for variable remuner-ation which is more than £500,000) should be

deferred over 3-5 years following the end of the performance measurement period

3. Awards should be risk adjusted 'ex ante' and 'ex post' (ie by malus).

The payout process rules in the Directive and Code appear to have been written with annual bonus pools in mind. There is no provision for running a multi-year measurement period concurrently with the multi-year deferral period, even though the desired risk adjustment is being achieved automatically because of the longer measurement period – usually more than 5 years with carry plans. So, although, prima facie, a carry plan does not comply with Requirement 2 above, we have ignored this in our analysis.

We had to decide how to value allocations of carry as remuneration. Of course it has historically been essential to the capital gains tax treatment of carry that it was not seen as remuneration but as a return on an investment. However, the Code is quite explicit that it is to be counted as variable remuneration for the purposes of compliance with the Directive. (It remains to be seen if this provides any grounds for the tax treatment to be changed.)

We decided it would be totally impracticable to attempt to demonstrate (to the FCA or otherwise) the value of carry as variable remuneration on the basis of amounts actually paid out from the carry plan. The figures are too variable and intermittent. Instead we felt the analysis should centre on the expected or fair value of carry allocation at grant. We have treated allocations of carry as though they are grants of full price share options with an exercise hurdle representing a share price growth of 8% (a typical hurdle rate). Because of the normally long period before 'exercise', the growth target and lack of a liquid market for the shares (an exit has to be found) we have assumed a conservative fair value factor of 15% of the initial value of the carry allocation.

Table 1 below shows the results of this analysis for the average compensation packages and carry at work for the large buyout/large mid-market firms (those likely to be above the proportionality threshold) and venture capital firms (which are more likely to be able to disapply the process rules anyway on the grounds of size).

**Table 1: How the average investment manager's remuneration complies with the Pay-out Process Rules**

| | Test A: Total remuneration exceeds 500k? | Test B: Variable remuneration exceeds 33% total rem | Disapply on Tests A and B combined? | Fair value of carry/total variable rem* | > 50% in units? | > 40% (60%) deferred? | Compliant? |
|---|---|---|---|---|---|---|---|
| **Large buyout/midmarket** | | | | | | | |
| Managing Partner | Yes | Yes | No | 82% | Yes | Yes | Yes |
| Senior Partner | Yes | Yes | No | 73% | Yes | Yes | Yes |
| Partner/MD | Yes | Yes | No | 57% | Yes | No | No |
| Principal/VP | No | Yes | No | 52% | Yes | Yes | Yes |
| Senior Associate | No | Yes | No | 46% | No | Yes | No |
| Associate | No | Yes | No | 27% | No | No | No |
| | | | | | | | |
| **Venture capital** | | | | | No | | |
| Managing Partner | Yes | Yes | No | 51% | Yes | No | No |
| Senior Partner | No | Yes | No | 51% | Yes | Yes | Yes |
| Partner/MD | No | Yes | No | 58% | Yes | Yes | Yes |
| Principal/VP | No | Yes | No | 55% | Yes | Yes | Yes |
| Sen Associate | No | No | Yes | 0% | No | No | No |
| Associate | No | No | Yes | 0% | No | No | No |

** Carry represents both the portion of variable paid in 'instruments and the portion deferred.*
*Source: MM&K/Holt/Thomson Reuters European PE/VC Compensation Report 2013*

There are a number of conclusions we can form from this analysis.

- The carry model is inherently capable of satisfying the deferral and payment in 'instruments' requirements of the payout process rules
- The balance of carry and bonus for some less senior partners may need to be adjusted to ensure a sufficient amount is deferred
- The way the carry element is valued is critical to the calculation

- Pay for junior investment staff is likely not to be compliant because of the lower allocation of carry in relation to bonus payments. In the smaller firms this will not be a problem as they will be excluded on the grounds of proportionality (even if the firm as a whole is not). But in the larger firms it is possible they will be caught unless the firms consider that their impact on risk is too low for them to be considered Code Staff.

Finally, we draw readers' attention to the requirement in the Code to conduct an independent review of remuneration policy every year. If you would like help in developing a compliant policy, putting the case for the risk alignment of your current policy or conducting future reviews, MM&K would be pleased to help and our database will provide a resource in supporting your arguments.

For further information contact Nigel.Mills@mm-k.com or Damien.Knight@mm-k.com.

**AIFMs operating through partnerships**

AIFMs and other investment managers operating through partnerships (including limited liability partnerships) which are subject to the AIFMD Remuneration Code may be required to defer payment of certain profits to the partners/members, as discussed above.

This causes problems for AIFMs operating through partnerships as partners/members are taxed on their share of profits as they arise even though they will not have access to the deferred part of their profit share until a later date.

Finance Bill 2014 will, with effect from 6 April 2014, introduce new rules by which a partner of an AIFM partnership may elect to allocate to the partnership all or part of his 'restricted profit' (i.e. deferred remuneration within the AIFMD Remuneration Code and other remuneration in the form of instruments that need to be retained for at least six months). If such an allocation is made, the partnership will pay tax at the additional rate of income tax (currently 45%) with no reliefs or allowances as if the partnership was an individual. When the 'restricted profits' vest, the allocating partner will be treated as receiving a taxable income with a credit for the tax paid initially. If the 'restricted profits' do not vest, the payment would be treated like any other partnership distribution with no additional tax liability or credit.

The new rules will allow deferral on a 'net of tax' basis and from the tax year 2014/15, partners/members of AIFM partnerships who elect to allocate the 'restricted profits' to the partnership will no longer be required to fund the income tax liability on the 'restricted profits'. **For further information contact** JD.Ghosh@mm-k.com

## Partnership taxation changes

### *JD Ghosh explains the proposals in the Finance Bill 2014*

#### 1. LLPs and 'salaried members'

The Finance Act 2014 introduces new rules, effective from 6 April 2014, to determine whether an individual member of a UK limited liability partnership ('LLP') will be regarded as self-employed or an employee (a 'salaried member'), for tax purposes.

These new tax rules only apply to UK LLPs, not to general partnerships, limited partnerships or non-UK partnerships. Moreover, these rules apply to individual members of an LLP only. They do not apply to corporate members, retired members or sleeping partners.

If the tests in the new rules are met by a member of an LLP, the member will be regarded as a 'salaried member'. Remuneration paid to him will be subject to income tax and NICs under PAYE. The new rules are designed to remove the presumption that a registered member of an LLP is self-employed.

Financially, this will mean that there will be an additional cost of employer's Class 1 NICs (currently 13.8%). Moreover, there will be an adverse cash flow effect because the tax on the remuneration of the 'salaried members' will be payable under PAYE.

***The 3 statutory conditions***

An individual member of an LLP will be treated as a partner for tax purposes (hence self-employed) and not a 'salaried member' (like an employee) if the member does not meet any of the following three conditions:

(a) Condition A - there is a reasonable expectation that the amounts payable by the LLP to the member will be wholly or substantially (i.e. at least 80 per cent) 'disguised salary';

(b) Condition B - the mutual rights and duties of the members and the LLP do not give the member significant influence over the affairs of the LLP;

(c) Condition C - the individual member's capital contribution to the LLP is less than 25 per cent of the 'disguised salary' payable to him by the LLP in the tax year.

**JD Ghosh** has recently joined the MM&K team. He specialises in the design and tax structuring aspects of UK and European based private equity funds and AIFM entities. He has advised extensively on the UK taxation aspects on fund formation and formation of AIFM and management entities (such as LLPs) and on management incentives (including carry and co-investment) and employee benefit trusts. He has also assisted management teams on 'exit'. In addition he has expertise in advising non-UK domiciled individuals (in particular AIFM managers and employees) on their personal taxation aspects (including trusts).

Prior to joining MM&K, JD worked in a Big Four accountancy practice for five years and before that with an international law firm. Before being enrolled as a solicitor, JD qualified as a barrister.

### *Condition A*

This condition is intended to identify those members of an LLP who are working for the LLP on terms that are like those of employees and are being paid for their services substantially without reference to the overall profitability of the LLP, viewed realistically.

What Condition A appears to state is that more than 20% of the total reward package of an individual member must represent a share of the overall profits of the LLP. Any arrangement, however complicated, where more than 20% of remuneration is related to the overall profits of the LLP should fail Condition A.

A 'disguised salary' is an amount which:

(a) is fixed; or

(b) if variable, is varied without reference to the overall profits or losses of the LLP; or

(c) is not, in practice, affected by the overall profits of the LLP.

A distinction is drawn between an amount which is a share of the LLP's profits and amounts which are fixed or which are intended to remunerate individual performance and will include non-refundable drawings, guaranteed payments, amounts payable purely based on the member's personal performance or performance of a team, piece work or turnover or on performance of a division of a business, without reference to the overall profits of the LLP.

In assessing this condition, it is necessary to consider all facts and circumstances, which include documents, agreements, understandings, schemes and transactions (whether legally binding or not) business plans etc. and a 'realistic' view needs to be taken (i.e. what is the actual position, not just what the written agreements reveal).

This condition is applied on a forward-looking basis. Once an arrangement is made and a view taken, that view remains valid until a new arrangement is brought in.

### *Condition B*

This condition is intended to identify those members of an LLP who do not have a real say in the affairs of the LLP and whether they are truly 'carrying on a business in common with a view to profits' as partners do in a partnership.

By 'significant influence over the affairs of the LLP', HMRC mean that the member must be involved in the management of the business as a whole, or be a senior member of a large LLP who may not be involved in day to day management, but whose role and rights mean that he or she is able to exert significant influence over the business of the LLP as a whole.

The meaning of 'significant influence' for the purpose of this condition is different from the 'significant influence' function test for the purposes of the Financial Services and Markets Act 2000. While HMRC will accept that a member who has CF3 (chief executive) or CF8 (apportionment and oversight) functions is likely to have significant influence for the purposes of failing Condition B, having a CF4 (partner) function will not of itself be sufficient to fail condition B unless he significantly contributes to the firm's major (management, strategic or investment) decisions.

Condition B will be failed by members who have a real say in the business and management of the business. While it may be clear in straightforward situations, it may be difficult to ascertain the precise scope of the application of this condition in many cases especially given that “the test is applied on the basis of a realistic view of facts”.

### *Condition C*

This condition is intended to identify those members of an LLP who have not made sufficient capital contribution to the LLP and so do not have a real risk resting on the success or failure of the business.

This condition comes into play after the determination of the ‘disguised salary’ amount in the first condition. The test is whether the capital contribution of the member to the LLP is more than 25% of his ‘disguised salary’ expected to be payable for the relevant tax year. If the member’s contribution is more than 25%, he will not be regarded as a ‘salaried member’.

A member’s capital contribution is based on the amount that he has invested as capital (‘permanent endowment’) in the LLP in accordance with the terms of the LLP. Such contribution cannot be varied by the member alone, any variation must be by agreement of the members.

### *Start of the rules and frequency of testing*

The conditions will need to be tested for each individual member on 6 April 2014. For individuals who become members after 6 April 2014, the conditions will need to be tested on the date the individual becomes a member of the LLP.

For Conditions A and B, once the test is applied, they do not need to be re-tested again unless there is a change in the arrangements between the member and the LLP.

However, for Condition C, the test is applied each year on 6 April unless there is a change in the year, in which case the test is re-applied on the change.

**MOST URGENTLY:** For existing members, the required capital contribution has had to be made by 6 April 2014, or by that date there must have been an unconditional requirement for the member to provide the capital and the capital must be contributed within the following 3 months. For new members, the required capital contribution will need to be made at the time of his becoming a member or at the time he becomes a member there must be an unconditional requirement for the member to provide the capital and the capital must be contributed within 2 months of becoming a member.

### *Anti-avoidance*

There are anti-avoidance provisions which, if applied, will effectively negate any artificial arrangement, the main purpose or one of the main purposes of which is to secure that an individual member is not regarded as a ‘salaried member’. These provisions will also catch the use of intermediaries by individuals to avoid being a ‘salaried member’.

Although widely drafted, HMRC seem to confirm that the anti-avoidance rules have been put in place to deter the use of artificial structures to circumvent the new rules and will not be applied to situations where genuine changes with real commercial effects are made. In particular, a genuine increase in capital contribution by a member which is intended to be enduring and giving rise to a real risk to him, or a genuine third party loan arrangement to enable the member to contribute increased capital to the LLP, even if the loan is arranged by the LLP, should be acceptable to HMRC as long as the real risk and liabilities in respect of the debt remains with the member.

## 2. Mixed partnerships and profit allocation

As profits of a partnership can be allocated to any partner/member without any reference to the partner’s/member’s contributions, efforts or capital to the partnership, the Consultation document on Partnership published on 20 May 2013 sought to address the profit and loss allocation arrangements adopted by some mixed partnerships (usually individual and company partners) whereby profits and losses could be diverted to reduce taxation liabilities. For example, an individual’s partner’s profit share which is taxable at 45% (current rate) could be allocated to a company partner which will be taxed at a lower rate of 21% (current corporation tax rate).

New rules are coming into force (effective from 5 December 2013) with regard to profits earned from 6 April 2014 whereby HMRC will have the power to reallocate ‘excess’ profits allocated to a non-individual partner to an individual partner on a just and reasonable basis. However, the legislation will prevent double taxation.

The following conditions would need to be met before HMRC can invoke its powers of reallocation of profits:

(a) a non-individual member has a share of the partnership’s profits;

(b) an individual member has the power to enjoy the non-individual partner's share or there are deferred profit arrangements in place;

(c) the non-individual partner's share is excessive; and

(d) it is reasonable to suppose that the individual partner's profit share is lower than it would be had the individual partner not been able to enjoy the profits allocated to the non-individual member.

Profits allocated to the non-individual member would be regarded as 'excessive' if it exceeds an 'appropriate notional return' on the capital or assets contributed by non-individual member or it exceeds an 'appropriate notional consideration' for the services that it provides to the partnership, judged on an arm's length basis.

Similar rules will also be introduced to counter avoidance of tax by diverting partnership losses (from trade or property business) to individual members from a non-individual member to enable the individual member to enjoy certain loss relief or increased loss relief.

### 3. Asset disposal through partnerships

Finance Bill 2014 will also introduce legislation to counteract certain schemes, effective from 6 April 2014, where a taxpayer uses a partnership to reduce or eliminate tax (income tax or corporation tax) arising on the disposal of an asset or an income stream. For example, a corporate partner introducing capital to a trading partnership for an income profit share. If this legislation applies, the individual partner of the partnership will be regarded as selling a part of his/her income stream in return for capital.

This legislation will apply where there is an arrangement by the use of a partnership whereby, directly or indirectly, there is a disposal of an asset or an income stream by a member (or a connected person) to another member and one of the main purposes of the arrangement is to obtain an income tax or corporation tax advantage.

Where this legislation applies, the person disposing of the asset or the income stream will be liable to income tax/corporation tax on the consideration given or market value of the asset disposed.

These new rules do not apply where the transferor and transferee are spouses, civil partners or relatives.

### 4. Negating compensating adjustments

Many partnerships, mainly professional partnerships/LLPs have a service company which provides services (staff etc.) to the partnership/LLP. If the transfer pricing legislation applies to the service company, it will be taxed on a mark up over costs at the corporation tax rate. However, legislation also allows the partnership to claim a compensating adjustment. Such compensating adjustment also reduces the tax liability of the individual partners/members at a higher rate (as the rate of corporation tax is lower than individual tax rate).

Finance Bill 2014 introduces new rules, effective from 25 October 2013 which would prevent persons (other than companies) liable to income tax from claiming such transfer pricing compensating adjustments. The service company must nevertheless continue to make the transfer pricing adjustments.

To learn more about the new rules, or to take advice on their application to your firm, contact JD Ghosh on JD.Ghosh@mm-k.com

## Findings from 2013 PE and VC Survey

***Dedar Mahal runs through the headlines of the MM&K private equity survey***

In November, MM&K published its annual PE/VC Compensation Report, a reward and HR practice survey covering 38 European Private Equity and Venture Capital houses and published in association with Holt (who produce a North American sister survey) and Thomson Reuters. In this article, Dedar Mahal, who runs the European survey, reports the summary findings.

The 38 participating firms were spread between larger mid-market buy-out (12 firms), smaller mid-market and growth capital (19 firms) and early stage, venture and technology (11 firms). Four firms spanned two categories. This article outlines the findings of the report.

For different categories of employee and for different types of firms, the pattern of remuneration change is quite varied. Overall, the figures suggest that there has been a limited degree of growth in remuneration across the industry.

Looking first at investment professionals, on average across all types of firms, both CEOs/managing partners and senior partners received no base salary increase. For other investment levels, salaries did go up especially at associate level where the median increase was nearly 7%. Turning to total cash (salary plus annual bonus) there seem to have been significant increases across the industry. The largest increases, of over 20%, were seen at the associate and senior analyst levels. Breaking this down by type of firm, the largest increases in the total cash figure were seen in the larger mid-market group, although there were also some significant increases seen in the lower mid-market grouping. As was the case last year, the more senior the investment professional the less the increase in total cash. In fact, on average, those at the managing partner/CEO and partner levels received virtually zero increases. These trends are similar for non-investment professionals. Base salary increases have been widespread, but on the whole, modest, while increases in total cash have been more significant but varied. The Chief Legal Counsel role provided the stand out data with its median base salary increasing by 10%. Other roles that stand out as having done particularly well include secretary/administrator, head of marketing, compliance officer, head of HR and head of IT.

For senior investment professionals, carry has a large weighting in their total remuneration package. Generally, carry at work for most recent funds and all active funds increased marginally in line with industry expectations. This would appear to be the case for senior investment individuals. The median percentage carry for the most recent fund across all firms for CEO/managing partner was 3.9% of the fund which is an increase on last year's 2.9%. A similar increase in the median carry for the most recent fund across all firms was seen at senior partner level (2.2% this year, an increase on last year's 0.8%). From our survey, it is also apparent that the median percentage carry for the most recent fund increased for most investment professionals. Venture Capital firms have seen a larger increase in their carry relative to the larger firms in this industry. VC firms typically have fewer individuals to share the carry and already tended to be remunerated well in this area of their total remuneration package. This tendency appears to be increasing.

With both fundraising and exit levels in 2013 reaching their highest figures for some years, a balanced flow of capital is powering the steady stabilization of the PE industry after the financial crisis that rocked global economies. The outlook for 2014 is positive with investors appearing to show an increase in confidence to invest in an industry which is moving away from its classification as 'alternative' into more of a mainstream asset class. A large majority of firms (78%) are confident about the future and expect to increase salaries in the year to come. Most are expecting to see a modest increase, mainly between 2% and 3% and 22% of respondents are expecting to see increases of above 8%. The general consensus (over half of respondents) is that bonuses will remain at the same sort of level as they were for 2012. This partly explains how it would appear that the balance between carry and bonuses paid is shifting more so towards carry.

As downward pressure from investors on management and transaction fees charged by fund managers continues and fund raising remains difficult, competitive and resource demanding, the medium term future for Private Equity remains challenging. Although funds with a strong track record and good investor relations are prevailing, the number of funds that find themselves on the fringes may well increase. Those that do continue to operate in the market will have to face the prospect of increasing remuneration demands from those below partner level and of decreasing revenues.

Dedar Mahal manages the MM&K European PE and VC survey.

If you wish to purchase our 2013 private equity compensation report, priced at £2,500 (+VAT as appropriate) or to **take part in the 2014 private equity compensation survey**, please contact Dedar Mahal at Dedar.Mahal@mm-k.com

In addition, you can read more about our **2014 private equity compensation survey** and **download the questionnaire** here: www.mm-k.com/pay-salary-surveys/private-equity-hedge-funds/participating.aspx