

Case C-352/20

Summary of the request for a preliminary ruling pursuant to Article 98(1) of the Rules of Procedure of the Court of Justice

Date lodged:

31 July 2020

Referring court:

Kúria (Supreme Court, Hungary)

Date of the decision to refer:

2 July 2020

Applicant and appellant in the appeal on a point of law:

HOLD Alapkezelő Befektetési Alapkezelő Zrt.

Defendant and respondent in the appeal on a point of law:

Magyar Nemzeti Bank

Subject matter of the main proceedings

Appeal on a point of law brought against a judgment of the court of first instance dismissing an action for the annulment of certain findings set out in a decision adopted by the Magyar Nemzeti Bank in its capacity as supervisory authority.

Subject matter and legal basis of the request for a preliminary ruling

Undertakings for collective investment in transferable securities – Remuneration policy and practice – Dividends paid to members of the board of directors, portfolio managers and investment managers who are simultaneously employees and shareholders of those undertakings – Dividends that may represent an incentive to take on risks allegedly incompatible with the risk profile of the management funds managed (as a fund manager) by the investment undertaking and with the interests of investors.

Legal basis: Article 267 TFEU.

Questions referred for a preliminary ruling

Do dividends distributed to [the directors concerned]

- (a) directly by virtue of their status as holders of preference shares with preferential rights to dividends in the investment fund manager, and
- (b) through single-member companies owned by the [directors concerned], which hold preference shares with preferential rights to dividends in that fund manager

remain subject to the remuneration policies of investment fund managers?

Provisions of EU law relied on

- Directive 2009/65/EC of the European Council and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ 2009 L 302, p. 32), Article 14, Article 14a and Article 14b.
- Article 14 relates to the rules of conduct which each Member State must lay down and which management companies authorised in that Member State must observe at all times. Member States must ensure that management companies discharge the obligations laid down in those rules. Article 14a defines the purpose to be served by the remuneration policies and practices defined by management companies. Article 14b lists the principles to be observed by management companies when defining their remuneration policies.
- Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (OJ 2011 L 174, p. 1), recital 28, Article 13(1) and Annex II, points 1 and 2.
- The provisions cited define the principles that must govern the remuneration policies established and applied by alternative investment fund managers. The list of principles is largely the same as that contained in Article 14b of Directive 2009/65.
- Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive [(OJ 2017 L 87, p. 1)], Article 2(5).
- The provision cited defines the meaning of ‘remuneration’ for the purposes of that regulation.

- Paragraph II.5 of the guidelines issued by the European Securities and Markets Authority on the basis of Article 16 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ 2010 L 331, p. 84).
- The provision cited also defines the concept of ‘remuneration’.

Provisions of national law relied on

- A kollektív befektetési formákról és kezelőikről, valamint egyes pénzügyi tárgyú törvények módosításáról szóló 2014. évi XVI. törvény (Law XVI of 2014 on the detailed rules governing collective investments and managers of collective investments, and amending certain laws in the financial sphere; ‘Law XVI of 2014’), Article 33 and Annex 13.
- The provisions cited govern the principles to be observed by investment fund managers when defining and applying their overall remuneration policy. The list contained in Annex 13 is largely the same as that contained in Article 14b of Directive 2009/65 and Annex II to Directive 2011/61. As regards Annex 13, the referring court cites separately the provisions that were in force prior to 18 March 2016 and those in force thereafter.
- A Polgári Törvénykönyvről szóló 2013. évi V. törvény (Law V of 2013 adopting the Civil Code; ‘the Civil Code’), Paragraphs 3:230, 3:231 and 3:253.
- The provisions cited relate to preference shares, preference shares with preferential rights to dividends and the equality of shareholders.
- MNB Recommendation 3/2017 (II.9) on the implementation of remuneration policy, paragraph 11.
- The provision cited governs the requirements to be met when defining remuneration policy in cases where the employees of the organisations to which the remuneration policy is applied also have a majority shareholding in that organisation or in one of its subsidiaries.
- MNB Recommendation 4/2018 (I. 16.) on the remuneration policy applied by alternative investment fund managers, paragraph 8.
- In accordance with the provision cited, the guidelines set out in the recommendation are to apply to dividends or dividend equivalents paid to the owner of an alternative investment fund management organisation where such payments lead in practice to a circumvention of the relevant remuneration rules.

Brief presentation of the facts and the main proceedings

- 1 The applicant in the main proceedings, HOLD Alapkezelő Befektetési Alapkezelő Zrt. ('the Fund Manager'), is a company which manages alternative investment funds and forms of collective investment in transferable securities. The Fund Manager carries on that lawful economic activity pursuant to an authorisation issued by the Magyar Nemzeti Bank (National Bank of Hungary, 'the MNB'), the defendant in the main proceedings.
- 2 From 20 March 2014 and, subsequently, from 19 July 2017, the Fund Manager established a remuneration policy applicable to certain categories of its staff.
- 3 Those categories of employee include four senior managers ('the directors concerned'), the first of whom is the managing director (member of the board of directors), the second is a portfolio manager, the third is an investment manager (member of the board of directors) and the fourth is also a portfolio manager (member of the board of directors). They all have an employment relationship with the Fund Manager.
- 4 The directors concerned are linked to the Fund Manager not only through their employment relationship but also because they are shareholders in the Fund. Their interest is both direct and indirect. On the one hand, the portfolio manager, the investment manager (member of the board of directors) and the [other] portfolio manager (member of the board of directors) are direct holders of preference shares with preferential rights to dividends in the Fund Manager. On the other hand, the portfolio manager (member of the board of directors) and the managing director (member of the board of directors) are the sole members of — unlisted — limited companies operating within a closed setting which have preference shares with preferential rights to dividends in the Fund Manager.
- 5 The Fund Manager distributed annual dividends on the organisation's after-tax results for the financial years 2015 to 2018 to the directors concerned and to those single-member companies.
- 6 From 1 January 2016, the MNB, in its capacity as supervisory authority, conducted an inspection of the Fund Manager. Following that inspection, the MNB adopted a decision on 11 April 2019 ('the decision of the MNB') in which it called on the Fund Manager, gradually but within a period of ninety days from receipt of the decision, to take the steps necessary in its business to ensure that the definition of its remuneration policy and practices complies with the relevant legislative provisions. The MNB also adopted other measures and imposed a penalty on the Fund Manager as part of its supervisory activities.
- 7 The Fund Manager brought an administrative-law action against the decision of the MNB. In its action, it sought an order declaring certain findings contained in that decision to be invalid and requiring the MNB to start new proceedings.

- 8 The court of first instance dismissed the Fund Manager's action. The Fund Manager brought an appeal on a point of law against that judgment before the referring court, which has submitted a request for a preliminary ruling to the Court of Justice.

Essential arguments of the parties to the main proceedings

- 9 The MNB takes the view that the dividend paid directly or indirectly by the Fund Manager to the directors concerned may have resulted in those directors' having an interest in the Fund Manager making short-term profits and, to that end, in them taking on risks incompatible with the risk profile of the funds managed by the Fund Manager, with the Fund Manager's management rules and with the interests of the participants. The MNB considers that, in distributing the dividend, the Fund Manager circumvented the rules on deferred payment of performance-based remuneration and infringed the provisions of Law XVI of 2014.
- 10 In the light of the foregoing, the MNB considered it irrelevant that the Fund Manager had a volume of own funds higher than that required by law, that the directors concerned had obtained their shares prior to the entry into force of Law XVI of 2014 and that it was in the interests of those directors, as owners of the Fund Manager, for the Fund Manager to post good results in the long term as well. According to the MNB, both the Civil Code and Law XVI of 2014 are jointly applicable to the distribution of dividends, and the decision of the MNB is also in line with Commission Recommendation 2009/384/EC of 30 April 2009 on remuneration policies in the financial services sector (OJ 2009 L 120, p. 22).
- 11 The Fund Manager argues that the decision of the MNB is, first and foremost, unlawful because the dividend distributed to the directors concerned is not considered to be 'variable remuneration' and does not therefore fall within the scope of remuneration policy. It argues that, for the purposes of the legal instruments of the European Union and the national rules cited, 'variable remuneration' must be understood as being the sums paid to an employee for discharging his or her occupational activity in accordance with performance criteria. The directors concerned, on the other hand, received the dividend in their capacity as shareholders and irrespective of their performance in the context of their employment relationship. In the opinion of the Fund Manager, the decision of the MNB is also discriminatory, since it infringes the provisions of the Civil Code relating to the equality of shareholders. The Fund Manager also regards as unlawful the fact that the decision of the MNB included the single-member companies of the directors concerned within the scope of remuneration policy, despite the fact that those single-member companies are legal persons independent of their owners. According to the information on the balance sheet, there is no correlation between the dividend distributed to those limited companies and the dividend later distributed by those companies to the directors concerned. Similarly, the Fund Manager regards as a purely subjective supposition the

proposition that the dividend distributed to the directors concerned may represent an incentive to obtain short-term profits.

- 12 According to the court of first instance, while it is true that dividends are not technically distributed for the discharge of occupational activity against performance criteria, they must nonetheless be regarded as remuneration in the light of their actual effect. It takes the view that dividends are an alternative channel of pay which may indeed represent an incentive for the directors concerned to obtain short-term profits, to take on risks contrary to the interests of investors and to circumvent the principles of remuneration policy.
- 13 What is more, there was no balance in the Fund Manager between the fixed remuneration of the directors concerned and the dividend distributed to them. Thus, while their fixed remuneration amounted to a few million forints per year, the amount of the dividend was in the hundreds of millions of forints. For that reason, payment of at least 40% of the dividends should have been deferred for at least three years, in line with the life cycle of the investment funds managed and the redemption of investment fund shares.
- 14 As regards dividends distributed to the single-member companies, the court of first instance took the view that these too represented an economic benefit for the directors concerned. For that reason, the form in which those directors subsequently decide to distribute dividends through the single-member companies has no bearing on the fact that the foregoing considerations are also applicable to those dividends.
- 15 On appeal on a point of law, the Fund Manager claimed that the court of first instance had committed an error in applying to it legislative provisions that are in fact aimed at investment funds. It states that dividends are not a form of variable remuneration because the right to receive them is independent of the occupational performance of the directors concerned. According to the Fund Manager, it has not been demonstrated either in the proceedings pursued by the MNB or in the proceedings before the court of first instance that it infringed the principles of remuneration policy. The Fund Manager also denies that the distribution of dividends has any additional content, over and above the rights derived from ownership of the shares, aimed at remunerating the work of the directors concerned.
- 16 The MNB contends that the judgment at first instance should be upheld. It contends that the dividend distributed by the Fund Manager may exceptionally be regarded as remuneration.

Brief presentation of the reasons for the request for a preliminary ruling

- 17 The referring court must determine whether the dividends which the directors concerned receive directly and indirectly through the limited companies they own fall within the scope of remuneration policy.

- 18 The directors concerned not only work for the Fund Manager but also own it. This is an important consideration for the purposes of remuneration practice, since the directors concerned, in their capacity as shareholders, may take decisions which determine the economic results of the Fund Manager and, therefore, the subsequent distribution of dividends on shares. At the same time, however, those directors, in their capacity as employees of the Fund Manager, are involved in defining and supervising the Fund Manager's remuneration policy, since these are matters falling within their responsibility. In the light of the 'dual' legal status which the directors concerned thus enjoy, the uncertainty arises as to whether the amounts obtained by those directors through their employment relationship and the amounts they receive both directly and indirectly by virtue of their status as shareholders must also be examined from the point of view of the application of the principles of remuneration policy.
- 19 When the rules on remuneration policy were laid down, account was taken principally of the economic receipts arising from the employment relationship of the employees. Recital 28 of Directive 2011/61 states that the provisions on remuneration are to be without prejudice to, *inter alia*, applicable legislation regarding shareholders' rights. The Commission considered it necessary to define the concept of 'remuneration' in Delegated Regulation 2017/565 (see recital 40).
- 20 As regards Hungarian law, Law XVI of 2014 does not define the concept of remuneration, while the a javadalmazási politikának a hitelintézet és a befektetési vállalkozás mérete, tevékenységének jellege, köre és jogi formájából eredő sajátossága figyelembevételével történő alkalmazásáról szóló 131/2011. (VII. 18.) Korm. rendelet (Government Decree No 131/2011 of 18 July 2011 on the application of remuneration according to the size, nature and content of the activities of credit institutions and investment service undertakings and the particularities arising from their legal form) is not applicable to the Fund Manager.
- 21 The definitions contained in Delegated Regulation 2017/565 and in the guidelines issued by the European Securities and Markets Authority are not sufficiently unequivocal to make it possible to determine whether the dividend paid directly or indirectly to the directors concerned, not by virtue of their relationship with the Fund Manager as its employees but by virtue of their relationship with it as its owners, must be regarded as an economic receipt subject to remuneration policy.
- 22 Given that Annex 13 to Law XVI of 2014 corresponds to Directive 2009/65 and Directive 2011/61, the referring court considers that the dispute before it calls for an interpretation of the provisions of EU law cited in the order for reference.