

Newsletter No.

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## Recent Financial Market Regulation Developments

With entry into force of the Financial Institutions Act (FinIA) and Financial Services Act (FinSA) and the implementing ordinances, especially active asset managers and Swiss and non-Swiss financial service providers must cope with various new affiliation and registration deadlines. Given the authorities now have set the framework, the financial institutions have to take action within the next couple of months.

Additionally, the impact of the Swiss Federal Supreme Court's most recent decision on retrocessions on the new duties imposed under FinSA requires thorough consideration for asset managers and financial service providers. Finally, financial market participants are well advised to keep track with the European Commission's Sustainable Action Plan. This newsletter addresses these latest developments in Swiss asset management regulation.

The Swiss Financial Market Supervisory Authority (FINMA) authorized the first supervisory authorities in charge for the supervision of asset managers and the first registration body for client advisers under FinSA. Additionally, the Federal Department of Finance admitted a few ombudsman's offices. Even the law provides for certain transitional periods to register or affiliate with the mentioned bodies, respective financial market participants have to take action within the close future. Also, asset managers of collective investment schemes and fund management companies already authorized before entry into force of the FinIA have only limited time available to fully comply with the licensing requirements set out in FinIA.

Furthermore the Federal Supreme Court's decision on retrocessions deserves attention within financial service providers FinSA compliance framework, essentially with respect to the FinSA duties on conflicts of interest.

### Authorization of Supervisory Organizations

The Swiss Financial Institutions Act (FinIA) introduces a new two-tiered supervisory regime applicable to Swiss asset managers. Swiss asset managers must first obtain a license from the Swiss Financial Market Supervisory Authority (FINMA) but will subsequently be supervised by a Supervisory Organization (SO) which in turn is licensed and supervised by the FINMA. With effect of 6 July 2020, FINMA authorized the first two supervisory bodies. As of today, the following SOs have been authorized:

- Organisme de Surveillance des Instituts Financiers (OSIF);
- Organisation de Surveillance Financière (OSFIN) ; and
- Organisme de Surveillance pour Intermédiaires Financiers & Trustées en formation (SO-FIT).

For an up to date list, please visit: <https://www.finma.ch/en/authorisation/aufsichtsorganisationen/>.

FINMA's authorization of the SO's triggers licensing deadlines for Swiss asset managers, depending on their status.

**Swiss asset managers active before 1 January 2020** and affiliated with a self-regulatory organization for anti-money laundering purposes (SRO) must comply with the licensing requirement imposed by FinIA and file an application with FIN-

MA before 31 December 2022 only. These existing asset managers are thus not affected by the authorization of the SOs.

### Swiss asset managers, established between 1 January and 31 December 2020

have to affiliate with an SRO and report to FINMA prior of commencement of their business activities. Still, the law provides a timeline until 6 July 2021 to submit their licensing request to FINMA.

Swiss asset managers established after 31 December 2020 have to file a request to FINMA prior to commencement of their business activities and will, upon granting of the license, be immediately supervised by the selected SO. Swiss asset managers established after 31 December 2020 will no longer benefit from grandfathering provisions or transitional periods.

### Admission of Client Adviser Register by FINMA

Under the Swiss Financial Services Act (FinSA) client advisers of Swiss financial service providers which are not supervised by FINMA such as banks or asset managers must register with a client adviser register. Client advisers are natural persons which provide tailored advisory services to clients without holding a power of attorney to execute trades for their clients themselves. Client advisers of non-Swiss financial service providers servicing Swiss clients have to sign up to a Swiss adviser register as well provided

that the non-Swiss financial service provider is not subject to prudential supervision in its country of origin, or if the financial services are also offered to Swiss retail clients.

With effect of 20 July 2020 FINMA admitted with BX Swiss AG ([www.regservices.ch](http://www.regservices.ch)) the first registration body of a client advisor registry. Later on, FINMA has admitted with Association Romande des Intermédiaires Financiers (ARIF) ([www.arif.ch](http://www.arif.ch)) another registration body. Additional approvals are not precluded.

For an up to date list please visit: <https://www.finma.ch/en/authorisation/registrierungsstelle/>.

FINMA's approval triggers a deadline to register with BX Swiss AG or ARIF (or a yet to approved additional registration body) no later than 19 January 2021 (e.g., within six months since 20 July 2020).

### Recognition of Ombudsman's Offices by the Federal Department of Finance

In order to further protect the interest of the clients and to allow for cost efficient dispute resolution, FinSA has introduced ombudsman's offices for the financial sector. Swiss financial service providers and non-Swiss financial service providers offering financial services to Swiss clients (including asset managers) must affiliate with an ombudsman's office. With effect of 24 June 2020, the Federal Department of Finance (FDF) has recognized the first ombudsman's

offices, however, is handling further pending applications on an on-going basis. As of the date of this newsletter the FDF has recognized seven ombudsman's offices. However, an affiliation with Swiss Banking Ombudsman Foundation is restricted to members of the Swiss Bankers Association.

For an up to date list please visit: <https://www.efd.admin.ch/efd/en/home/das-efd/ombudstelle-nach-fidleg.html>.

Swiss financial service providers and non-Swiss financial service providers serving Swiss clients have to affiliate with a Swiss ombudsman's office no later than 24 December 2020. As the affiliation with an ombudsman's office is a requirement for a successful registration with a client adviser register, client advisers are required to affiliate with an ombudsman's office first.

The law maker has realized that the obligation for non-Swiss financial service providers which serve institutional and professional Swiss clients but no retail clients to register with an ombudsman's office overshoots the target. A reform bill intends to drop this requirement. However, it is likely that the reform bill will be implemented after 24 December 2020 only. Consequently, non-Swiss financial service providers will have to affiliate with a Swiss ombudsman's office before 24 December 2020 and may cancel the affiliation during the course of 2021 after the said reform bill will be enacted. Prudent financial service providers likely to be eligible to rely on aforementioned exemption are well advised not to rush into an affiliation with an ombudsman's office instead to await further developments and hold back an affiliation application for the time being.

### **Approaching FinIA Compliance Deadline for Asset Managers of Collective Investment Schemes and Fund Management Companies**

In addition to the general affiliation with an ombudsman's office until 24 December 2020, asset managers of collective investment schemes and fund management companies authorized by FINMA already before entry into force of FinIA must fully comply with the licensing requirements imposed by FinIA no later than 31 December 2020. The scope of action relates mainly to the streamlining and updating of the internal documents with the new terminologies and legal references, inter alia the articles of association and organizational regulations. Whereas the changes purely related to the licensing requirements are rather minimal, the impact of the conduct duties, now regulated under FinSA and to a certain extent under the Collective Investment Schemes Act, seems to be more of a challenge.

### **Retrocessions under FinSA and Impact of a new Swiss Federal Supreme Court Decision on this Issue**

Retrocessions and other distribution fees paid to asset managers and banks have been subject to several decisions of the Swiss Federal Supreme Court. Case law emerged the practice of asset managers entitlement to retain retrocessions and other distribution fees by way of a client's waiver based on informed consent. In brief under this practice an asset manager's disclosure requires information on the parameters of the amount of retrocessions received, including at least the range of the expected retrocessions indicated in a percentage figure in relation to the specific financial instrument. Additionally, the client must be informed of the risk associated with conflicts of interests linked to retrocession payments and the mitigating measures in place.

With enactment of FinSA and FinSO these general principles under Swiss contractual law have been codified mainly under the provisions dealing with conflict of interests and by view of a bigger picture under the transparency provisions.

In the most recent decision on retrocessions, the Swiss Federal Supreme Court shed some light to its understanding on the level of detail with respect to the information required enabling a client to determine expected retrocessions received by her or his asset manager. In its decision 4A\_355/2019 of 13 May 2020 the Swiss Federal Supreme Court dealt with a signed client notification, inter alia stating and confirming that the asset manager may receive retrocessions for certain financial instruments, such as collective investment schemes or structured products, ranging between 0% and 1% of the volume invested.

The Swiss Federal Supreme Court held that a signed client notification, indicating the expected retrocessions solely based on the range of the volume invested would be invalid. In its reasoning the Swiss Federal Supreme Court stressed that given the signed client notification allowed the calculation only on future investments, the client would not be able to determine the amount of the expected retrocessions in advance. The volume invested can only be determined in the future, at the time the asset manager decides on the investments.

When putting this recent decision of the Swiss Federal Supreme Court in context with the new FinSA and its implementing ordinance, we are of the view that this decision provides for further interpretation guidance on article 26 para. 2 FinSA even though the decision deals with the regulatory framework in place before entry into force of FinSA. Article 26 para 2 FinSA merely repeats the Swiss Federal Supreme Court's general practice already in place before its abovementioned

tioned decision and requires the asset manager to inform clients of the calculation parameters and the ranges in case the amount of compensation cannot be assessed in advance. Both, neither the dispatch nor the explanatory report to FinIA/FinSA take position or provide for any further guidance on interpretation of article 26 para 2 FinSA. As a consequence, the Swiss Federal Supreme Court's decision 4A\_355/2019 of 13 May 2020 is of paramount importance. Asset managers keen to receive and keep retrocessions must, therefore, ensure to inform clients on the range of the expected retrocessions indicated in a percentage figure in relation to the assets under management rather than in relation to any undetermined future investments. However, it is worthwhile mentioning, that indication of a percentage figure in relation to the assets under management in full seems barely practical and to the detriment of the clients. Retrocessions vary depending on the type of the investment products, in addition the exact asset allocation cannot be determined beforehand and varies during the asset management mandate. Thus, in case the asset manager within the investment strategy considers different investment products, the range of the expected retrocessions broadens, with the consequence that a client has to agree to a more broadened and indefinite range of expected retrocessions. A result, which in our view, is to the detriment of both the client and the asset manager.

### ESG Disclosure and its Impact on Swiss Financial Institutions

With the UN Sustainable Development Goals (SDGs) and the 2015 Paris Climate Convention, sustainable finance has become key in financial markets and more specifically in asset management. With a consequence that Environmental, Social and Governance (ESG) considerations have become increasingly important.

Whereas the Swiss regulations with the Sustainable Asset Management Recommendations of the Swiss Funds and Asset Management Association (SFAMA) and the Guideline for the integration of ESG considerations into the advisory process for private clients of the Swiss Bankers Association (SBA) only provide for recommendations, the European Commission's Sustainable Action Plan provides for a broad range of envisaged regulatory measures. Most recently, on 12 July 2020 the Taxonomy Regulation entered into force. The Taxonomy Regulation provides for an EU-wide classification standard for ESG activities, setting out the criteria for determining a product's or an activities' qualification as environmentally sustainable. Furthermore, on 10 March 2021 most of the obligations under the Disclosure Regulation (also known as the ESG Regulation) will come into force, which essentially require financial institutions, on a firm and a product level, to establish and disclose strategies with respect to ESG. Given the additional EU regulation in the pipeline under the European Commission's Sustainable Action Plan, (Swiss) financial market participants active in the EU markets should keep track with these regulations and developments.

### Conclusion

With FINMA's and the FDF's approval and recognition, respectively, of the newly to be implemented bodies under the FinSA/FinIA, the Supervisory Organization, the client adviser register, the ombudsman's office (and the prospectus offices) the respective lapses of all transition periods have been set now. Consequently, implementation of the various requirements, including client documentation taking account of the Swiss Federal Supreme Court's decision on retrocessions must now be tackled by asset managers. Asset managers of collective investment schemes and fund management companies must in addition to the affiliation with an ombudsman's office, comply with

the general licensing requirements imposed by FinIA at the latest as of 31 December 2020. Additionally, financial institutions should keep track with the further ESG regulations and developments.

The Walder Wyss Newsletter provides comments on new developments and significant issues of Swiss law. These comments are not intended to provide legal advice. Before taking action or relying on the comments and the information given, addressees of this Newsletter should seek specific advice on the matters which concern them.

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