

MACFARLANES

REMINDER: IMPENDING IMPLEMENTATION OF NEW RULES RELATING TO THE DISTRIBUTION OF FUNDS IN SWITZERLAND

INVESTMENT FUNDS

On 1 March 2015, the new rules (the Rules) relating to the distribution of funds in Switzerland take effect in full. This note summarises the main issues for non-Swiss managers. The Rules aim to harmonise pre-existing marketing rules for Swiss and non-Swiss funds, and promote transparency and the “proper functioning” of the market for funds in Switzerland. The Rules are introduced under the Swiss Federal Act on Collective Investment Schemes (CISA), and supplementary provisions in the Collective Investment Scheme Ordinance.

Under the Rules, there are now three categories of investors in Switzerland, namely:

- ◆ Unregulated Qualified Investors;
- ◆ Regulated Qualified Investors; and
- ◆ Non-Qualified Investors (i.e. retail investors).

Unsurprisingly, the Rules relating to the distribution of funds to retail investors are relatively onerous. However, the Rules relating to non-retail investors allow widespread distribution within Switzerland. The most widely known of the new Rules relates to the appointment of a Swiss representative and a paying agent.

This note focuses on the Rules relating to the distribution of funds to non-retail investors, so-called “Qualified Investors” only.

QUALIFIED INVESTORS

The Rules divide non-retail investors into two types: Regulated Qualified Investors and Unregulated Qualified Investors. Broadly speaking, Qualified Investors are professional or institutional investors.

Unregulated Qualified Investors

Unregulated Qualified Investors include publicly listed companies; pension funds and entities with professional treasury operations (which may include certain family offices); and those who opt to be Unregulated Qualified Investors (as further explained below). An investor is deemed to operate a professional treasury service if it has at least one qualified expert whom it entrusts with the “continuous management of its financial assets”.

Certain individual investors, who would otherwise be categorised as Regulated Qualified Investors or Non-Qualified Investors, have the right to either opt-in or opt-out as Unregulated Qualified Investors. Those who can exercise such an option are:

- ◆ investors who have concluded a written management agreement with a recognised independent asset manager¹ or a regulated financial institution² (such investors are deemed to be Qualified Investors unless they opt-out); and
- ◆ high-net-worth individuals who declare in writing they wish to be treated as Qualified Investors (thereby opting-in).

To opt-in, a high-net-worth individual should certify that he or she:

- ◆ can demonstrate the knowledge necessary to understand the risks in connection with the investment and has bankable assets of at least CHF500,000; and
- ◆ has financial assets in an amount exceeding CHF5m.

Regulated Qualified Investors

Regulated Qualified Investors include banks authorised and supervised by the Swiss Financial Market Supervisory Authority (FINMA) under the Swiss Federal Act on Banks and Savings Banks; the Swiss central bank; securities dealers authorised and supervised by FINMA under the Swiss Federal Act on Stock Exchanges and Securities Trading; fund managers or asset managers of collective investment schemes authorised and supervised by FINMA under CISA; and insurance companies authorised and supervised by FINMA under the Swiss Federal Act on the Supervision of Insurance Companies.

Given the nature of such entities, the distribution of a fund to a Qualified Investor is broadly free from additional regulation under the Rules.

TYPES OF FUNDS

The Rules deal with the distribution of all types of fund, whether open or closed-ended, including, but not limited to:

- ◆ alternative, UCITS and offshore funds;
- ◆ hedge funds;
- ◆ private equity funds; and
- ◆ real estate funds.

This range of funds is similar to that prescribed under the Alternative Investment Fund Managers Directive (AIFMD), save that the AIFMD specifically excludes UCITS (as the distribution of such funds is governed by the separate UCITS Directive).

¹ A fund manager subject to the Swiss laws on anti-money laundering and the recognised conduct of business rules of an organisation in the Swiss financial sector.

² A bank, securities dealer, fund management company, fund asset manager or central bank.

DISTRIBUTION OF FUNDS

Unlike the AIFMD, which governs the “marketing” of funds, the Swiss regime governs the, subtly different, “distribution” of funds.

A “distribution” is defined as “any offer or advertisement for collective investment schemes which is not exclusively addressed to regulated financial intermediaries”. And “offering” or “advertising” include any type of activity which aims to encourage the acquisition of units of funds by an investor. Therefore, any reference to a fund in or through, for example, a marketing meeting; presentation; website; cold call; or monthly distribution list, will be considered a distribution where the target or recipient is resident in Switzerland.

Unlike the AIFMD, the Rules also catch the offering, promotion or advertising of managed accounts. Managed accounts would be caught by the Rules on the basis that their economic effect is comparable to a fund of funds or an asset allocation fund and thus for these purposes they are regarded as collective investment schemes.

Note also that, again unlike the AIFMD, there is no distinction between “pre-marketing” and “marketing”. If the activity falls under the definition of distribution, the Rules apply. There is no ability, therefore, to provide general marketing material relating to a fund to Unregulated Qualified Investors without triggering the requirement to appoint a Swiss representative or paying agent. In addition, as distribution is defined to include public distributions and private placement activities, the existing Swiss private placement rules will no longer apply.

Internet-based distribution to qualified investors in Switzerland.

In 2013, FINMA published a revision of a 2008 circular entitled “Public advertising – collective investment schemes”. This circular gave guidance on, amongst other things, the use of websites to attract Qualified Investors. In particular:

- ◆ *Disclaimer on the website.* A disclaimer must be included to inform Swiss investors that the website is for Qualified Investors only. If the website refers to funds for which there is no Swiss representative and/or paying agent (i.e. if it is aimed at Regulated Qualified Investors), the website must also display a disclaimer informing investors that such funds may not be distributed in Switzerland other than to such investors.
- ◆ *Restricted access to the website.* The website must limit access based on the category of investor and interested investors must first answer all of the control questions before they are granted access to the website.

Unregulated Qualified Investors should only be able to access areas of the website which contain indications of funds for which a FINMA-authorized representative and/or paying agent has been appointed. Non-Qualified Investors should not be given access.

- ◆ *Distribution license.* Any person domiciled in Switzerland who is responsible for maintaining a website attracting Qualified Investors must hold the appropriate distribution license in Switzerland. If the website is operated by a non-Swiss distributor e.g. the investment manager of the fund, then such entity must be authorised to distribute funds in its own country of incorporation and comply with the appropriate Swiss Rules.

Distributing Funds to Unregulated Qualified Investors and Regulated Qualified Investors

Regulated Qualified Investors. Where a non-Swiss fund wishes to distribute exclusively to Regulated Qualified Investors, there is no requirement to seek authorisation or approval. Nor are there additional regulatory requirements to be adopted in order to distribute funds. It is advisable to review the wording of Swiss marketing legends contained in the fund's offering material making it clear that the fund is only being distributed in Switzerland to Regulated Qualified Investors. Although there is no obligation to include this wording, its inclusion will assist in demonstrating the fund's limited distribution in Switzerland.

Unregulated Qualified Investors. There is no notification, registration or approval requirement for distributing a non-Swiss fund to Unregulated Qualified Investors in Switzerland. However, prior to distribution, the fund must:

- ◆ appoint a licensed Swiss representative;
- ◆ appoint a Swiss paying agent;
- ◆ ensure that the relevant distributor/investment manager, enters into a distribution agreement, subject to Swiss law, with the Swiss representative of the fund;
- ◆ ensure that the distributor/investment manager is authorised in its home jurisdiction to carry out marketing activities and is supervised by its home regulator (those regulated under the AIFMD, or by the SEC, will be appropriately authorised);

- ◆ ensure that the distributor/investment manager is fully compliant with Guidelines on Duties Regarding the Charging and Use of Fees and Costs (the Transparency Guidelines) issued by the Swiss Funds and Asset Management Association (SFAMA) as outlined below; and
- ◆ ensure that all marketing and offering materials available to Qualified Investors specify:
 - the country of domicile of the fund;
 - the name and address of the Swiss representative;
 - the name and address of the paying agent; and
 - the location where fund documents can be found.

ACTIVITIES OUTSIDE THE SCOPE OF THE RULES

According to the Rules, a distribution does not include:

- ◆ reverse solicitation (also referred to as reverse enquiry) where an investor invests in a fund on its own initiative;
- ◆ the publication of prices, net asset values and tax data by regulated financial intermediaries, provided that such publication does not contain any contact information; and
- ◆ a distribution aimed exclusively at a regulated financial intermediary.

THE ROLE OF SWISS REPRESENTATIVES AND PAYING AGENTS

Swiss representatives

The role of the Swiss representative is to:

- ◆ establish a permanent local presence for the fund in Switzerland;
- ◆ ensure a Swiss paying agent is appointed;
- ◆ inform and update the distributor on Swiss legislation and standards;
- ◆ ensure distribution material is fully compliant with SFAMA's Guidelines on Distribution of Collective Investment Schemes (the Distribution Guidelines);
- ◆ enter into a distribution agreement with the fund manager;
- ◆ represent the fund and be a point of contact for both Qualified Investors and FINMA, in the case of requests for information, claims or regulatory issues;

- ◆ receive from the distributor annual written confirmation of compliance with the Distribution Guidelines and Transparency Guidelines; and
- ◆ provide investors with the fund's governing documents and annual reports.

Swiss investors must be able to call the Swiss representative with any queries on the fund and request the relevant documents, although this does not prevent the fund from contacting the Swiss investor directly.

Swiss paying agents

The role of the Swiss paying agent is to enable investors to have the option to subscribe, redeem and receive pay-outs from the fund through a Swiss bank. The Swiss paying agent does little in the context of a closed-ended fund, so the administrator of the fund can still interact with the investor and send out all drawdown notices and distributions. However, this limited role does not rule out the obligation to have a paying agent.

THE TRANSPARENCY GUIDELINES

The Transparency Guidelines contain a general duty to disclose information in the fund's documentation (such as its offering memorandum or other marketing material) regarding:

- ◆ fees and costs;
- ◆ commissions or finder's fees paid for (usually) by fund managers (so-called retrocessions); and
- ◆ rebates.

Retrocessions. A person who pays retrocessions has a duty to disclose in the fund documentation that such retrocessions are paid, and for which services. While the names of the recipients need not be disclosed, a person who received retrocessions must inform Swiss investors about the amount of the compensation they may receive for distribution. Lastly, if retrocessions imply possible conflicts of interests, such conflicts and their nature should be disclosed to investors by the recipient of the retrocessions.

Rebates. Rebates are payments which result in a reduction of the fee or cost attributable to the fund. Rebates are permitted provided that they are granted on objective criteria i.e. the amount of fees generated by investors. Criteria and conditions upon which rebates are granted must be disclosed in the fund documentation. The names and beneficiaries of rebates need not be disclosed.

Generally, these disclosures will be made in a fund's existing fund offering document and we do not envisage additional changes. However we are aware of Swiss Representatives demanding additional clarification language prior to accepting an appointment.

CONTACT DETAILS

If you would like further information or specific advice please contact:

SIMON THOMAS

DD: +44 (0)20 7849 2444

simon.thomas@macfarlanes.com

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RECORDS

The Swiss Bankers Association has previously issued guidelines on the duty to keep records of a distributor's interaction with investors and parties in Switzerland. These guidelines, while more suited to private wealth managers, also apply to distributions to Qualified Investors, although may be limited in practice to queries as to suitability raised by the fund's existing subscription documents. The guidelines state that the following information should be kept on record (if known):

- ◆ the investment objectives and an indication of the investor's risk profile; and
- ◆ the reasons for the investor's subscription to a fund.

PENALTIES AND REMEDIES FOR NON-COMPLIANCE

The deadline for compliance with the Rules is 1 March 2015. Non-compliance with the new distribution and marketing regulations by the distributor (Swiss or foreign) may incur criminal sanctions. While non-compliance will not render the contract between the fund and the investor unenforceable, a Qualified Investor could bring a claim for damages under Swiss law if it can be shown that the investor had been improperly solicited and the investor's investment has declined in value.

MACFARLANES LLP

20 CURSITOR STREET LONDON EC4A 1LT

T: +44 (0)20 7831 9222 F: +44 (0)20 7831 9607 DX 138 Chancery Lane www.macfarlanes.com

This note is intended to provide general information about some recent and anticipated developments which may be of interest. It is not intended to be comprehensive nor to provide any specific legal advice and should not be acted or relied upon as doing so. Professional advice appropriate to the specific situation should always be obtained.

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