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Distribution of Collective Investment Schemes in Switzerland to Qualified Investors

I. INTRODUCTION

Switzerland is commonly known to be an attractive location for distribution investment funds. According to the 2021 annual report of SFAMA, the total volume of assets managed by asset managers in Switzerland reached a new record level of CHF 2,787 billion at the end of 2020, which corresponds to an exceptionally strong year-on-year growth of 10.6%. Discretionary mandates for Swiss and foreign institutional clients accounted for CHF 1,129 billion of this amount, with collective investment schemes (**CIS**) under Swiss and foreign law making up the remaining CHF 1,658 billion. Furthermore, the Swiss asset management industry's total revenue is estimated at CHF 15.67 billion in 2021, its earnings at around CHF 4.1 billion.

However, the Swiss regulatory framework governing the distribution and placement of CIS in Switzerland remains very complex. After providing an overview of the latter (*infra*, II.) and defining the concept of 'distribution' (*infra*, III.), this bulletin aims to provide a comprehensive guide of the regulatory requirements applicable to the distribution of CIS in Switzerland, with a particular focus on the distribution of foreign CIS to qualified investors (*infra*, IV.).

II. SWISS REGULATORY FRAMEWORK

The Swiss regulatory framework applicable to the distribution of CIS essentially consists of (i) the Swiss Financial Services Act (**FinSA**) and its implementing ordinance (**FinSO**), (ii) the Swiss Financial Institutions Act (**FinIA**) together with its implementing ordinance (**FinIO**) as well as (iii) the Swiss Collective Investment Schemes Act (**CISA**) and its implementing ordinance (**CISO**); all of which aim to align, to a certain extent, the Swiss regulatory environment to that of the European Union, in particular the Markets in Financial Instruments Directive 2004/39/EC (**MiFID II**).

FinSA sets out the requirements for honesty, diligence and transparency in the provision of financial services and governs the offering of financial instruments[1]. It applies to financial service providers (**FSPs**), client advisers as well as producers and providers of financial instruments, irrespective of their legal form[2]. FSPs are persons who provide financial services on a commercial basis in Switzerland or for clients in Switzerland, with the criterion of a commercial basis being satisfied if there is an independent economic activity pursued on a permanent, for-profit basis[3]. Client advisers, on the other hand, are individuals who perform financial services on behalf of a FSP or in their own capacity as FSPs[4]. Of note is that there are

1 Art. 1 para. 2 FinSA.
2 Art. 2 para. 1 FinSA.
3 Art. 3 let. d FinSA and art. 2 para. 1 FinSO.
4 Art. 3 let. e FinSA.

two notable exceptions to FinSA' scope of application, namely the 'no point-of-sale' exemption (*infra*, V.A.) and the reverse solicitation exemption (*infra*, V.B.).

III. CONCEPT OF 'DISTRIBUTION'

A. Preliminary remarks

Swiss law does no longer use the concept of 'distribution', but rather distinguishes between three independent concepts: 'financial services', 'offer' and 'advertising'. Accordingly, the distribution of CIS in Switzerland may trigger different requirements depending on the segment of investors targeted and the distribution activity performed, it being specified that such activity may fall under one or several of these concepts depending on its scope.

B. Distribution as a 'financial service'

The concept of 'financial services' within the meaning of FinSA includes (a) acquisition and disposal of financial instruments, (b) receipt and transmission of orders in relation to financial instruments, (c) administration of financial instruments (portfolio management), (d) provision of personal recommendations on transactions with financial instruments (investment advice) and (e) granting of loans to finance transactions with financial instruments[5].

Any activity addressed directly at a specific end-investor[6] in Switzerland that is aimed at the acquisition or disposal of shares or units of CIS characterizes as a 'financial service'[7], regardless of whether an effective purchase or sale of financial instruments occurs. Such a definition therefore also includes interactions of FSPs with specific investors, such as marketing activities, which, based on an assessment of the circumstances, shall be considered, potentially or actually, as an important element for taking a specific investment decision.

C. Distribution as an 'offer' of financial instruments

Any invitation to acquire shares or units of a CIS that (i) contains sufficient information on the terms thereof and on the CIS itself and (ii) is customarily intended to draw attention to the CIS and to sell the shares and units of the latter is deemed to constitute an 'offer'[8].

In contrast, the provision of information upon clients' unsolicited requests (*i.e.*, reverse solicitation; *infra*, V.B.), the reference by name to the CIS, even in conjunction with factual and general information (e.g., net asset values, prices, risk information, price performance or tax figures), the provision of factual information only or the preparation, provision, publication and forwarding of legally or contractually required information and documents to existing clients or financial intermediaries (e.g., corporate action information, invitation to general meetings) are not deemed to constitute an 'offer'[9].

D. Distribution as 'advertising'

Any communication aimed at investors and serving to draw attention to a CIS is deemed to constitute 'advertising'[10]. In contrast, circumstances such as mentioning by name of a CIS, the provision or forwarding of communications from issuers and reports in the trade press do not constitute, in and of themselves alone, 'advertising'[11]. Fundamentally, an 'advertisement' differs from an 'offer' in that it is not specific enough to enable the investor to make an investment decision based thereon.

IV. REGULATORY REQUIREMENTS

A. Client Segmentation

1. Client segmentation under FinSA

First and foremost, FSPs are required to assign the investors they approach to the segment of retail clients, professional clients or institutional clients.

Retail clients are deemed to be clients who are not Professional Clients (together with the Opted-In Professional Clients, the **Retail Clients**)[12].

Professional clients are deemed to be any of the following (together with the Opted-Out Retail Clients and the Opted-In Institutional Clients, the **Professional Clients**)[13]: (a) financial intermediaries subject to prudential supervision pursuant to the Swiss Banking Act, the FinIA and the CISA (the **Swiss Supervised FI**); (b) regulated insurance companies subject to prudential supervision pursuant to the Swiss Insurance Supervision Act; (c) foreign clients subject to an equivalent form of prudential supervision as the entities under letters (a) and (b); (d) central banks; (e) public

5 Art. 3 let. c FinSA.
6 Otherwise, the 'no point-of-sale' exemption applies (*infra*, V.A.).
7 Art. 3 let. c ciph. 1 FinSA and art. 3 para. 2 FinSO.
8 Art. 3 let. g FinSA *cum* art. 3 para. 5 FinSO.
9 Art. 3 para. 6 FinSO.
10 Art. 95 para. 1 FinSO.
11 Art. 95 para. 2 FinSO.
12 Art. 4 para. 2 FinSA.
13 Art. 4 para. 3 let. a-i FinSA.

entities with professional treasury operations (**PTO**), such operations being deemed exist if at least one person qualified and experienced in financial matters is employed to manage financial assets[14]; (f) occupational pension schemes with PTO and other occupational pension institutions providing PTO; (g) companies with PTO; (h) large companies[15]; (i) private investment structures created for high-net-worth individuals (**HNWI**), including family offices, provided that they have PTO.

Institutional clients are deemed to be professional clients defined in letters (a) and (b) above as well as supranational public entities with PTO (together with the Opted-Out Professional Clients, the **Institutional Clients**)[16].

HNWI, and the private investment structures created for them, may 'opt-out' (up) from the Retail Client status by declaring that they wish to be treated as Professional Clients (the **Opted-Out Retail Clients**) if they can make plausible that:

— they hold assets of at least CHF 500,000 (or exchange value in another currency) and they possess the necessary knowledge to understand the risks associated with the investments (a) on the basis of their training, education and professional experience, (b) on the basis of comparable experience in the financial sector or (c) due to the knowledge and experience of their authorized representative; or

— they hold assets of at least CHF 2 million (or exchange value in another currency).

Professional clients defined in letters (e), (f) and (g) above may 'opt-out' (up) from the protection as Professional Client to the status of Institutional Clients, as do the Swiss and foreign CIS and their management companies which are not already deemed to be Institutional Clients (the **Opted-Out Professional Clients**).

Professional Clients who are not Institutional Clients may 'opt-in' (down) from the protection as Professional Client to the status of Retail Clients (the **Opted-In Professional Clients**).

Last but not least, Institutional Clients may 'opt-in' (down) from the protection as Institutional Clients to the status of Professional Clients (the **Opted-In Institutional Clients**).

2. Client segmentation under CISA

After performing the client segmentation under FinSA (*infra* IV.A.1 above), FSPs shall assign the investors they approach to one of the statutory client clients pursuant to the CISA.

Institutional Clients and Professional Clients, including Opted-Out Retail Clients, are deemed to be 'qualified investors' (the **Qualified Investors**, other investors being the **Non-Qualified Investors**)[17], it being specified that Retail Clients under permanent portfolio management or in an investment advisory relationship as well as Opted-In Professional Clients are also considered as Qualified Investors[18].

B. Rules of conduct

FSPs are exempt from observing the rules of conduct set out in art. 7-19 FinSA with respect to Institutional Clients[19].

With respect to Professional Clients, the above rules of conduct shall be observed by FSPs, unless the former have expressly released the latter from applying the rules of conduct set out in art. 8, 9, 15 and 16 FinSA[20], in which case only the rules on the appropriateness and suitability review set out in art. 10-14 FinSA shall be observed.

In contrast, all of the rules of conduct set out in art. 7-19 FinSA shall be observed with respect to Retail Clients[21].

It should be specified that the rules on the appropriateness and suitability review set out in art. 10-14 FinSA are not relevant with respect to activities that do not constitute neither an 'investment advice' nor a 'portfolio management service' withing the meaning of the FinSA.

C. Organizational rules

Regardless of the nature of financial services provided and the segment of the clients targeted, FSPs shall implement the organizational measures set out in art. 21-27 FinSA, in proportion to the size and complexity of such services and the risks arising thereof. It should also be noted that these obligations do not apply to fund management activities if they are performed outside Switzerland.

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14 Art. 3 para. 8 FinSO.

15 Large companies are those exceeding two of the following parameters: (a) CHF 20 million balance sheet total; (b) CHF 40 million annual gross revenues; (c) CHF 2 million equity.

16 Art. 4 para. 4 FinSA.

17 Art. 10 para. 3 CISA.

18 Art. 10 para. 3ter CISA, resp. art. 10 para. 3 CISA.

19 Art. 20 para. 1 FinSA.

20 Art. 20 para. 1 FinSA.

21 Art. 20 para. 1 FinSA *a contrario*.

1. *Appropriate organization*

FSPs shall ensure that they fulfil their duties under FinSA by defining internal guidelines, which shall be appropriate to their size, complexity and legal form and the services offered and commensurate with the associated risks[22].

2. *Qualification of employees and third parties*

FSPs shall ensure that their employees possess the necessary skills, knowledge and experience to perform their work by carefully selecting staff and ensuring that they receive basic training and continuing professional development in respect of the code of conduct and the specific specialized knowledge which they require to perform their concrete tasks[23].

FSPs may appoint third parties for the provision of financial services, provided that such persons possess the necessary skills, knowledge and experience, have the required authorizations and register entries and that they are carefully instructed and supervised[24].

FSPs do not have the duty to ensure that only persons registered in the register of advisers act as client advisers for them insofar as they provide financial services exclusively to Institutional Clients and/or Professional Clients other than Opted-Out Retail Clients (*infra*, IV.D.)[25].

3. *Conflicts of interests*

FSPs and their employees shall act in the best interests of the clients. They shall endeavor to act at all times in a professional and independent manner and take all reasonable steps to identify and prevent conflicts of interest that could arise through the provision of financial services as well as any disadvantages for clients as a result of conflicts of interest[26]. FSPs must take the risk-adequate precautions set forth in art. 25 FinSO to the extent that they are appropriate to their size, complexity and legal form as well as to the financial services provided[27].

If the above precautions cannot prevent disadvantages for clients or only with a disproportionate amount of effort, FSPs shall disclose this to the clients concerned in an appropriate manner[28]. The conflicts of interest arising shall be described, in particular, by explaining, in general terms, the circumstances behind them, the resultant risks for the clients and the precautions taken to reduce these risks[29].

Specific attention should be given to the FinSA rules on retrocessions, which differ from those of MiFID II. FSPs may accept compensation from third parties in association with the provision of financial services (e.g., brokerage fees, commissions, discounts or other financial benefits) only if they (a) have expressly informed the clients of such compensation in advance and the latter relinquish it or (b) passed it on to the clients in full. The information on the type and scope of such compensation must be given to the clients before provision of a financial service or conclusion of a contract. If the amount of compensation cannot be determined in advance, the clients shall be informed of the calculation parameters and ranges (e.g., a percentage of the amount that the client will acquire). Upon the client's request, the amounts effectively received shall be disclosed. Compensation from third parties which by its very nature cannot be passed on to clients must be disclosed as a conflict of interest.[30]

Furthermore, FSPs shall take measures to prevent their employees[31] from misusing for own-account transactions any information made available to them only by virtue of their function[32], respectively from engaging in impermissible forms of conduct set forth in art. 27 FinSO.

D. Registration of client advisors

Client advisers of a Swiss FSP may carry out their activity in Switzerland only if they are entered in a register of advisers, unless such FSP is subject to prudential supervision pursuant to art. 3 of the Swiss Financial Market Supervision Act (FINMASA)[33].

These registration duties also apply to client advisers of foreign FSPs[34], with a notable exception: client advisers of FSPs prudentially supervised abroad are exempted from the duty to register, provided that the financial services they provide in Switzerland are exclusively aimed at Professional Clients and/or Institutional Clients, to the exclusion of

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22 Art. 21 FinSA and art. 23 para. 1 let. a FinSO.
23 Art. 22 para. 1 FinSA and art. 23 para. 1 let. b FinSO.
24 Art. 23 FinSA.
25 Art. 22 para. 2 FinSA *a contrario*.
26 Art. 25 para. 1 FinSA.
27 Art. 25 let. a–g FinSO.
28 Art. 25 para. 2 FinSA and art. 26 para. 1 FinSO.
29 Art. 26 para. 2 FinSO.
30 Art. 26 FinSA and 29 FinSO.
31 These include members of the body responsible for governance, supervision and control, the body responsible for management, partners with unlimited liability as well as persons with comparable functions (art. 30 FinSO).
32 Art. 27 FinSA.
33 Art. 28 para. 1 FinSA.
34 Art. 28 para. 1 FinSA.

Retail Clients[35]. Legal scholars are of the opinion that this exemption shall also apply in case the financial services they provide in Switzerland are exclusively aimed at Opted-Out Retail Clients; however, as this question is debatable, we recommend, by precaution, to assume the contrary.

The requirements of the above exemption from the duty to register must be fulfilled at the level of the individual client advisor, not with respect to the entire client base of the FSP. Moreover, this exemption generally does not apply to client advisers of Swiss based companies of the same group.

E. Affiliation with an ombudsman

FSPs that intend to provide financial services to Opted-Out Retail Clients (and/or Retail Clients) must affiliate to an ombudsman at the latest on commencing their activity[36] and inform their clients of the possibility of initiating mediation proceedings before such ombudsman[37]. It follows that FSPs are exempted from the duty to affiliate to an ombudsman should they provide financial services exclusively to Institutional Clients and/or Professional Clients other than Opted-Out Retail Clients.

F. Requirements specific to advertising

Regardless of the segment of the targeted client, advertising must be clearly indicated as such[38]

Furthermore, the publications and marketing materials related to a CIS, should it be offered to Opted-Out Retail Clients (or to Non-Qualified Investors), shall indicate the country of domicile of the CIS, the Swiss representative, the Swiss paying agent as well as the location where the fund documents and the annual and semi-annual report may be obtained for free[39]. If the CIS is an alternative investment (*i.e.*, if it is an open-ended CIS whose investments, structure, investment techniques and investment restrictions exhibit a risk profile that is typical for alternative investments), related advertising materials shall make reference to the special risks involved in alternative investments[40].

G. Appointment of Swiss representative and paying agent

A Swiss representative is a local point of contact for Swiss investors and the Swiss Financial Market Supervisory Authority (**FINMA**)[41], whereas a Swiss paying agent is a Swiss banking institution that a Swiss investor could use as intermediary to invest or receive proceeds from a CIS[42].

FSPs intending to offer, respectively to advertise, a CIS to Opted-Out Retail Clients shall ensure that both a Swiss representative and a Swiss paying agent have been appointed[43]. It follows that this requirement does not apply should a CIS be offered, respectively advertised, exclusively to Qualified Investors other than Opted-Out Retail Clients.

H. FINMA's approval

When offered, respectively advertised, to exclusively to Qualified Investors, CIS do not require a prior approval by FINMA[44].

Foreign FSPs, on the other hand, require authorization from FINMA if they wish to have a 'physical presence' in Switzerland or, in other terms, to employ persons in Switzerland who will work for them on a professional and permanent basis in Switzerland or from Switzerland. Specifically, they require a branch license if such persons can conclude transactions on behalf of the foreign FSP or perform, in the name of the foreign FSP, asset management or trustee activities, portfolio management for CIS or occupational pension schemes, securities trading or client account management[45]. Where such persons perform, in the name of the foreign FSP, activities other than those listed above, specifically if they forward client orders to foreign FSPs (introducing brokers) or represent them for marketing or other purposes, such FSPs require a representative office license from FINMA[46]. In our opinion, nevertheless, this does not hold true if the activities performed are limited to the distribution of a CIS. The representation office is designed for foreign FSPs carrying out activities in Switzerland, which tend to foster the core activities of an asset manager; the distribution not being considered as such.

It should be noted that foreign fund management companies may not establish representations in Switzerland[47]. However, the legislative revision of the FinIO that came into effect on August 1, 2021 limited this prohibition exclusively to the office's activities in relation to the administration and management of investment funds[48].

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35 Art. 28 para. 2 FinSA *cum* art. 31 FinSO.
36 Art. 77 FinSA.
37 Art. 8 para. 1 let. c FinSA.
38 Art. 68 FinSA.
39 Art. 133 para. 2 CISO.
40 Art. 71 para. 3 CISA.
41 Art. 124 para. 1 CISA.
42 Art. 121 para. 2 CISA.
43 Art. 120 para. 4 CISA, resp. art. 127a CISO.
44 Art. 120 para. 1 CISA, resp. art. 127a CISO.
45 Art. 52 et seq. FinIA.
46 Art. 58 et seq. FinIA.
47 Art. 58 para. 2 FinIA.
48 Art. 82 para. 2 FinIO.

V. EXEMPTIONS

A. No point-of-sale exemption

In contrast to approaching an end-investor directly with the aim to acquire or dispose of shares or units of a CIS, approaching a financial intermediary in Switzerland is not considered as providing a 'financial service' as long as such financial intermediary does not intend to acquire shares or units of the CIS for its own account. In fact, FinSA's remit is to protect the end-investor. Accordingly, in such case, FinSA will only be applicable to the financial intermediary having invested in a CIS for its own clients (e.g., in the frame of a discretionary portfolio or advisory investment mandate) as this constitutes a provision of financial services to end-investors within the meaning of art. 3 FinSA.

It follows that distribution activities related to a CIS may be performed by a given FSP without triggering any regulatory requirements under the FinSA at the level of such FSP insofar as such distribution activities are not made 'at a point-of-sale', which is the case if they target: (a) HNWI, respectively Swiss private investment structures created for HNWI, or Retail Clients other than HNWI, having their place of residence or registered office is Switzerland for which a Swiss Supervised FI or a foreign financial intermediary subject to equivalent prudential supervision provides, under a permanent portfolio management or investment advisory agreement, portfolio management or investment advisory services within the meaning of art. 3 lit. c ciph. 3 and ciphr. 4 FinSA; (b) Swiss Supervised FI acting as nominees on behalf of their own clients.

B. Reverse solicitation exemption

FinSA's territorial scope of application is relatively broad as it covers the provision of financial services by Swiss FSPs to clients in Switzerland (domestic services), by Swiss FSPs to clients abroad (outbound services) and by foreign FSPs to clients in Switzerland (inbound services)[49].

However, the following are not deemed to be provided in Switzerland: (a) financial services provided by foreign FSPs within the scope of a new client relationship (e.g., portfolio management or investment advisory agreement) that has been entered into at the express initiative of a client (inbound reverse solicitation); (b) individual financial services requested at the express initiative of clients from a foreign FSP (outbound reverse solicitation)[50]. Similarly, the provision of information is not deemed to be an 'offer' if it is made at the instigation of the client and is not preceded by 'advertising' by the FSP or an agent of the FSP in relation to the specific financial instrument[51].

Even though FinSA does not further specify the criteria for reverse solicitation, it can generally be held, in our view, that this exemption may only be applicable if (i) the initiative for a financial service or product comes expressly and exclusively from the relevant client, (ii) if it concerns a specific financial service or a specific product or type of products (as opposed to mere general inquiries), (iii) the relevant specific financial service or product has not been advertised or solicited by any other means to the relevant client prior to such client's enquiry and (iv) the financial service provided does not go beyond the scope of the original client's request.

It follows that reverse solicitation is a narrow exemption. Accordingly, it should not serve as a business model. If a client relationship was entered into on client's express initiative, all financial services falling under the requested service are covered by the reverse solicitation exception (e.g., individual advisory services in the case of an advisory relationship, or individual investment decisions and related acts in the case of an asset management relationship, but not the 'recommendation' of an asset management relationship in case of an existing advisory relationship). The extension of financial services beyond those that have been requested by the client is not possible based on the said exemption.

FSPs seeking to rely on reverse solicitation should clearly document the client's own initiative, which shall be examined on a case-by-case basis. It should be noted that a mere *ex post* client's confirmation is generally not sufficient but rather constitutes circumstantial evidence only.

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[49] Art. 3 let. d FinSA.

[50] Art. 2 para. 2 FinSO.

[51] Art. 3 let. g FinSA *a contrario*.

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