

Initial experiences with the licensing process for portfolio managers and trustees

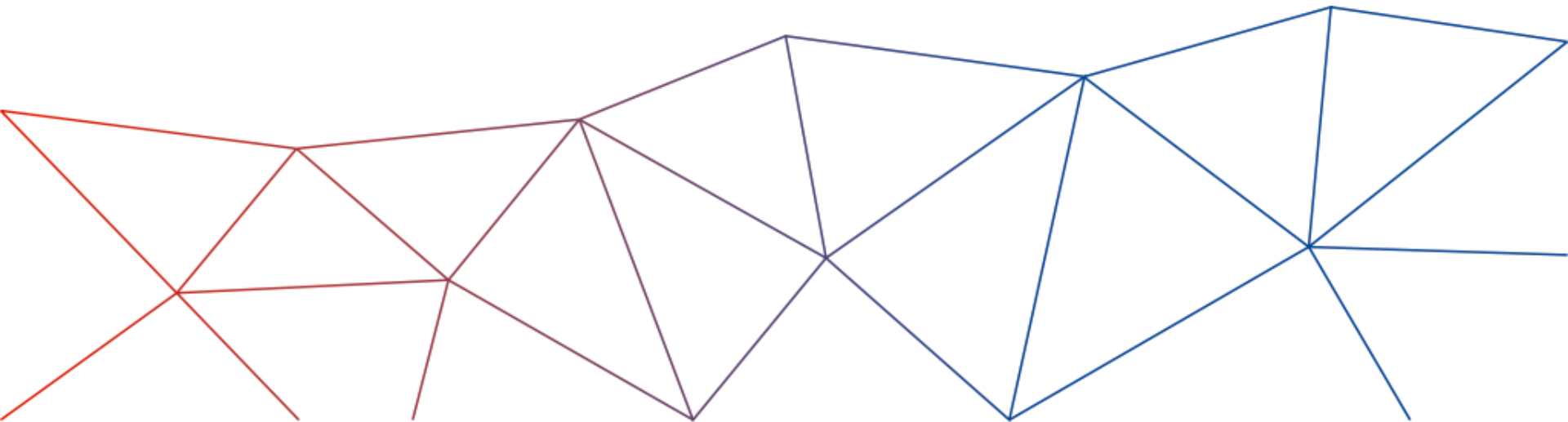
Thomas Hirschi / Kenneth Ukoh

2021

Agenda

- I. Introduction
- II. Risk-based approach to licensing
- III. High-risk business models
- IV. Refresh: licensing process
- V. Questions

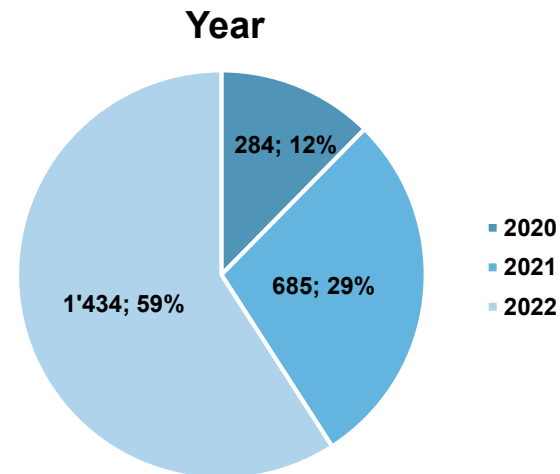
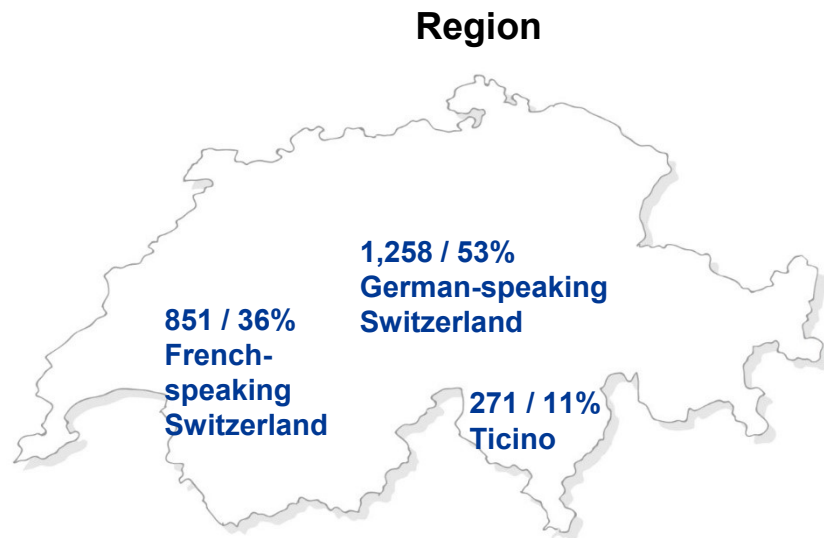
I. Introduction



What happened so far...

- The institutional and regulatory framework for implementing the FinSA/FinIA has been established:
 - ✓ **5 supervisory organisations (SOs)** licensed for the supervision of portfolio managers and trustees
 - ✓ **Regulation implementing** the FinSA/FinIA adopted (FinIO-FINMA, Circ. on market conduct)
 - ✓ The processes are in place and applications can be submitted entirely digitally via the electronic **EHP platform**
- So far FINMA has received **95 applications** and licensed **36 portfolio managers**; no applications have been rejected so far
- FINMA is in close contact with various associations, custodian banks as well as the supervisory organisations

Key figures for reports made



Intended applications as per reports made under Article 74 FinIA (as at 31.12.2020)	Reports made under paragraph 2	Reports made under paragraph 3
Portfolio managers	2,041	83
Trustees	353	34
Branches of foreign portfolio managers	4	n/a
Branches of foreign trustees	5	1
Total		2,521

Findings

- Very significant and heterogeneous supervisory population
- Applications are being submitted later than reported
- Majority of applications will be processed in 2023
- Challenge of process duration: dependent on quality and complexity of the application
- Some “first movers” despite long transitional period

New licensing regime

- New prudential authorisation conditions
 - Financial, personal and organisational requirements
 - Applicants may need to adapt their structure and business model
 - Some institutions will either not submit an application or will not automatically be granted a licence with their existing structures

- Heterogeneous supervised population
 - Ensuring a level playing field is key
 - Risk-based review of licence applications to ensure uniform quality standards
 - Complexity and risk exposure of business model are crucial

- A FINMA licence is an opportunity / seal of quality

- The industry and Switzerland as a centre for wealth management will become more attractive and competitive as well as gaining international recognition

Expectations and challenges

Expectations of applicants...

- Critical self-assessment with regard to the new requirements and the risk exposure of their own business model
- Willingness to make the changes required for eligibility for licensing e.g. with regard to organisation, processes, resources etc.
- Submission of a high-quality licence application via the correct process (particularly prior affiliation to an SO)

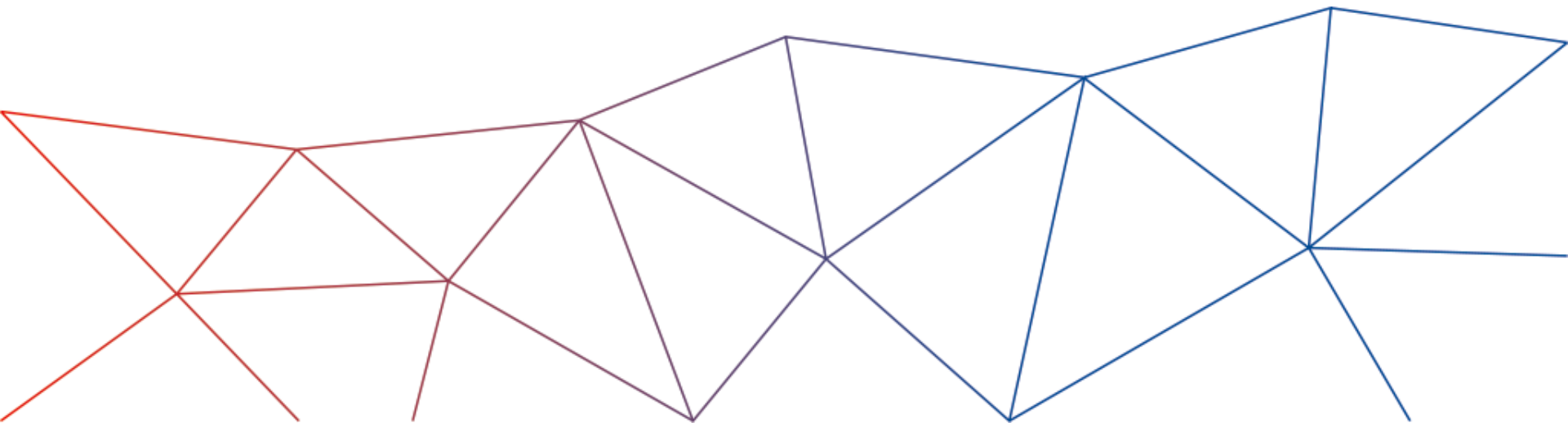
Expectations of FINMA...

- Transparent and clear communication regarding its expectations
- Ensure a level playing field
- Efficient processing of applications

Expectations of the SOs...

- Establish their systems and processes
- High-quality preliminary checks
- Risk-oriented supervision of its members in accordance with FINMA's criteria

II. Risk-based approach to licensing



Risk-based approach to licensing

- No “one size fits all” approach, but instead risk-based review of licence applications to ensure uniform quality standards
- Simple applications/business models should be processed in a standardised way, whereas complex and risky models are examined in depth
- Institutions with risky business models must take appropriate risk-mitigating measures
- Eligibility for licensing is conditional upon the inherent risks being adequately limited and monitored
- No licence without the necessary adjustments being made (resources built up, separation of risk and compliance, outsourcing with the involvement of third parties, etc.)

Authorisation conditions

Risk management

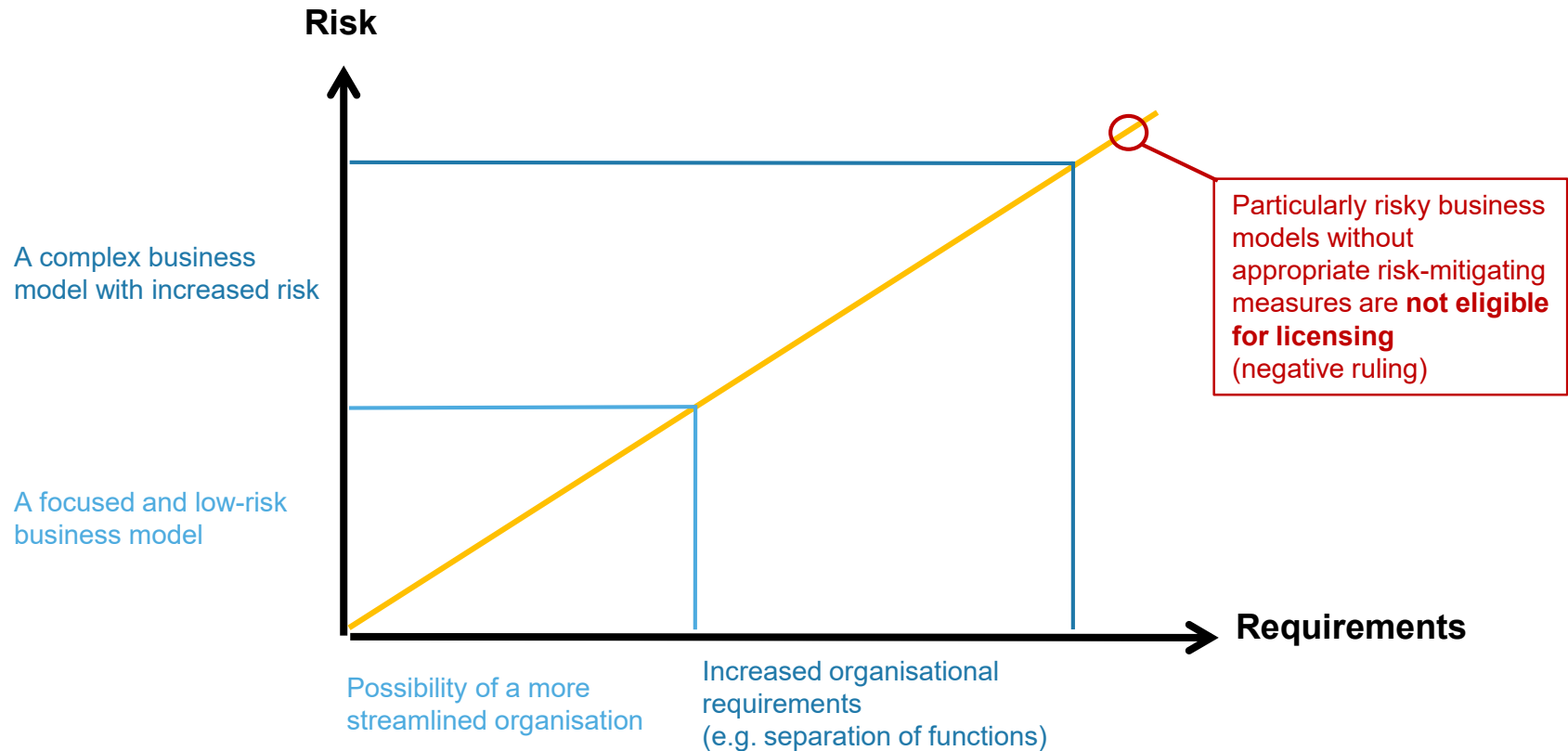
Basic principles

- Must have adequate risk management in place
- Effective internal controls are in place
- Ensures that statutory and internal provisions are complied with
- Sets out the basic principles of risk management and defines risk tolerance
- All business activities are covered
- All material risks must be
 - identified
 - assessed
 - controlled
 - monitored

Organisation

- Can be carried out by qualified managers, qualified employees or delegated to a qualified external body
- Persons who perform risk management tasks must not be involved in the performance of activities they monitor
- Risk management and the internal controls are not required to be independent of revenue-based activities if the portfolio manager or trustee:
 - a. is a company which has five or fewer full-time positions or annual gross earnings of less than CHF 2 million; and
 - b. adheres to a non-high-risk business model

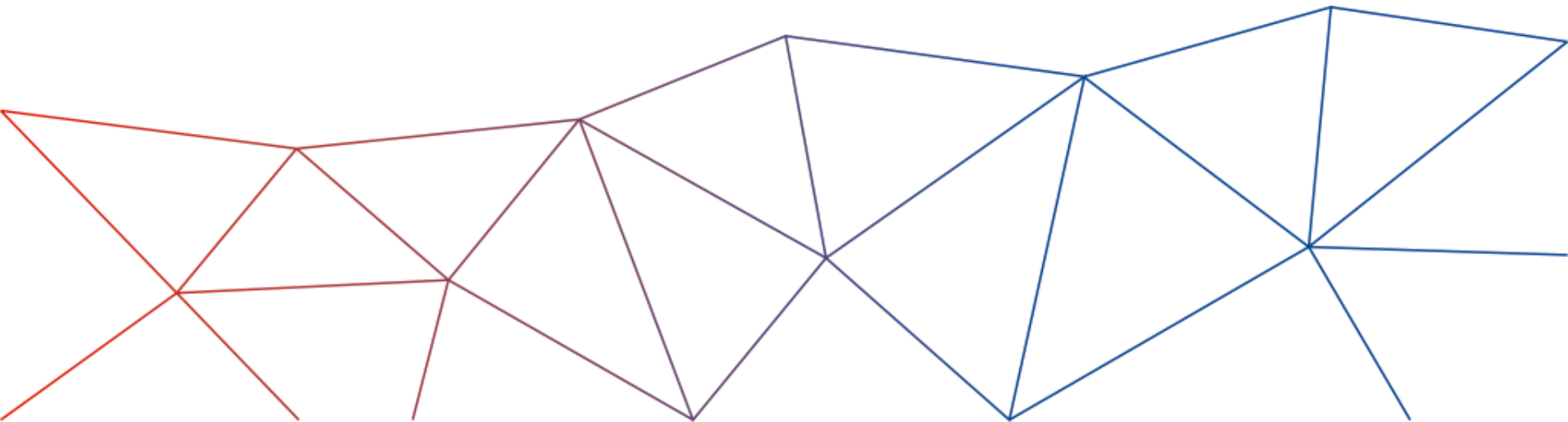
Appropriateness of risk management



The higher the risks inherent in a business model, the higher the requirements for its eligibility for licensing

inter alia with regard to appropriate organisation, internal processes, policies/directives, training requirements, risk control functions, risk management and compliance etc.

III. High-risk business models



General expectations

- Appropriate business organisation
- Appropriate policies/directives (particularly with regard to FinSA, AMLA, cross-border, market conduct etc.)
- Appropriate recording and addressing of the inherent risks
- Independence of risk management and the internal controls from revenue-based activities (Art. 26 para. 2 FinIO), unless:
 - company size \leq 5 full-time positions or annual gross earnings $<$ 2m and
 - non-high-risk business model
- Independent board of directors if (Art. 23 para. 3 FinIO)
 - $10 \geq$ full-time positions or annual gross earnings $>$ CHF 5m and
 - nature and scope of activities or risky business model
- Qualified managers with sufficient professional experience and appropriate training (Art. 25 FinIO)
- Appropriately and suitably qualified personnel (Art. 12 para. 3 FinIO)
- Description of area of business in factually and geographically precise terms in the principal documents

High-risk business model in accordance with Article 26 para. 2 FinIO

It is up to FINMA to interpret the expression “high-risk business model”.

In particular, the following circumstances – even below the thresholds in accordance with Article 26 para. 2 FinIO – are deemed to be risky:

- De minimis management of occupational pension scheme assets or funds;
- Involvement of foreign custodian banks;
- Certain heterogeneous structure of foreign client base or client base with a focus on a particular region abroad;
- Use of investment instruments with potential conflicts of interests;
- Applicant holds unrestricted power of attorney;
- High volume of assets under management: AuM > CHF 1bn

→ In principle operational separation of risk control is required

Initial experiences

Risky business models:

- Involvement of foreign custodian banks
- Foreign client bases
- Use of investment instruments with potential conflicts of interests
- Compensation from third parties (retrocessions etc.)

Depending on the business model and scope, as well as the type of risks, FINMA expects to see evidence of the requisite expertise and any necessary adjustments to the organisation

Foreign custodian banks

Risks

- Increased money laundering risk (including tax offences)
- No equivalent supervision or no equivalent AMLA standard
- Risk of letterbox banks (shell banks)
- Instruction and monitoring more difficult

Expectations

- ✓ Involvement of foreign custodian banks fits with the strategic orientation of the business model, makes sense in isolated cases / can be explained
- ✓ Policies/directives and controls address the risks associated with foreign custodian banks
- ✓ Separation of risk and compliance from the operational units

Structure of foreign client base

Risks

- Market access (legal and liability risks)
- Heterogeneous structure of client base or serving a large number of different countries
- Focus on a particular foreign region with increased money laundering risks (e.g. corruption etc.)

Expectations

- ✓ Policies/directives address the risks associated with cross-border financial services (particularly country manuals, AMLA directive)
- ✓ Relevant experience and professional qualifications of client advisers (inter alia knowledge of the country, language and culture, geopolitics, legal and financial system)
- ✓ Adequate personnel resources
- ✓ Periodic training on country-specific knowledge
- ✓ Possible reason for separation of risk and compliance from the operational units

Use of investment instruments with potential conflicts of interests

Risks

- Lack of disclosure of conflicts of interests to clients when own investment instruments are used (e.g. funds, AMCs) within the scope of asset management, investment advice or structuring
- Lack of transparency regarding multiple billing of fees (“double dip”)
- Risk of fraud

Expectations

- ✓ Internal regulations concerning the avoidance and disclosure of conflicts of interests
- ✓ Percentage cap on own investment instruments in line with the investment strategy
- ✓ Handling and disclosure of multiple billing
- ✓ Separation of risk and compliance from the operational units

Compensation from third parties (retrocessions etc.)

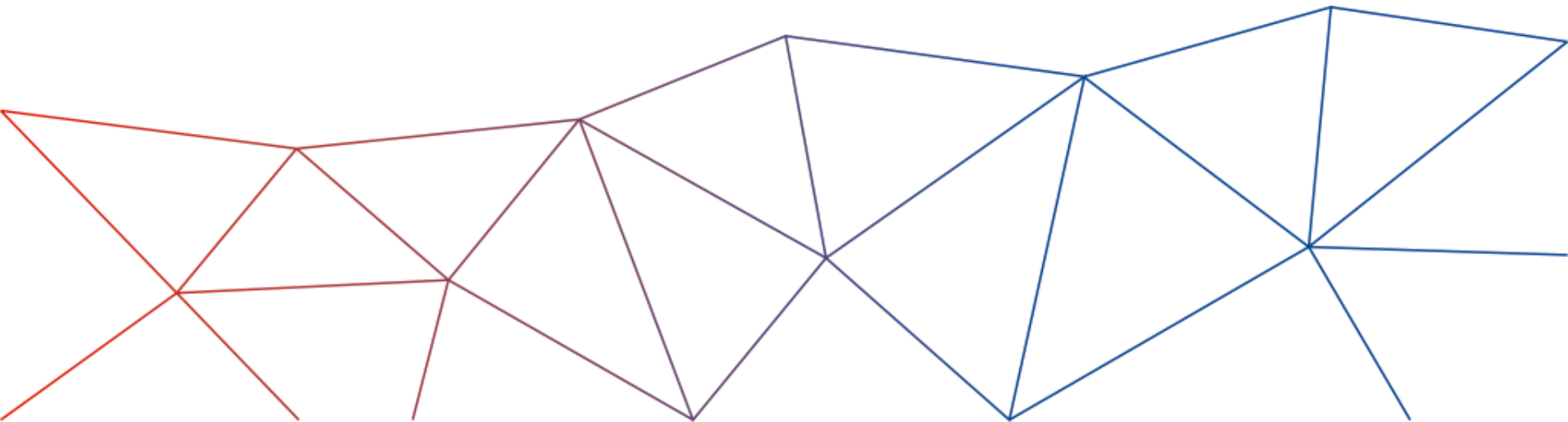
Risks

- Risks under civil and criminal law
- Missing information or no valid waiver by the customer

Expectations

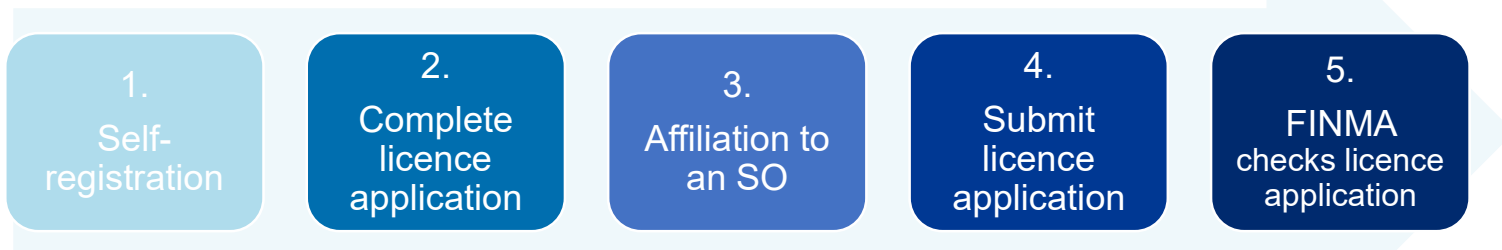
- ✓ Policies/directives address the risks associated with compensation from third parties
- ✓ Duty to provide prior information to clients
- ✓ Observance of Article 26 FinSA

V. Refresh: licensing process



Licensing process

- No voluntary licensing → Eligibility for licensing is conditional upon activities that require a licence
- No umbrella licensing → Licensing takes place only at the individual institution level
- No further reports under Article 74 FinIA possible because deadlines expired at the end of 2020
- Only after the confirmation of SO affiliation has been received, the complete application can be sent to FINMA via the EHP by the applicant
- Submission is possible entirely electronically and without a signature



Aids and support

The screenshot shows the FINMA website interface. At the top, there is a navigation bar with links for Home, Media, Jobs, Contact, and Extranet-Login. Below this is the FINMA logo and a menu with categories: Authorisation, Supervision, Enforcement, Documentation, and FINMA. A 'FINMA Public' button is also visible. The main content area features a 'Welcome' section with a 'FinSA and FinIA' article. To the right, there is a sidebar with a 'Favourite links' section. Two links in this section are circled in red: 'Information for portfolio managers and trustees' and 'EHP survey and application platform'. A red arrow points from the 'EHP survey and application platform' link to a video player on the right. The video player shows a video titled 'Bewilligungsprozess für Vermögensverwalter und Trustees' with a play button. On the far right, there is a 'EHP-Support' section with a 'Frequently asked questions' list and 'User manuals' for various documents.

EHP-Support

Frequently asked questions

- Accessing the FINMA survey and application platform (E...
- Surveys in the EHP
- Applications and Reports in the EHP
- EHP Delivery note

User manuals

- Online Help**
EHP survey and application platform
Updated: 03.09.2018 Size: 1,34 MB Language(s): >DE >FR >IT >EN
- Die Rolle des Berechtigungsverantwortlichen**
Updated: 13.07.2020 Size: 1,09 MB Language(s): >DE >FR >IT >EN
- Technische Voraussetzungen zur Erhebungs- und Gesuchplattform der FINMA**
Updated: 05.03.2019 Size: 0,3 MB Language(s): >DE >FR
- Nutzungsmodalitäten zur Erhebungs- und Gesuchplattform der FINMA**
Updated: 27.07.2018 Size: 0,18 MB Language(s): >DE >FR

Explanatory videos

The video player shows a video titled 'Bewilligungsprozess für Vermögensverwalter und Trustees'. The video description includes 'Videoanleitung Bewilligungsge...' and 'Gesuch erstellen'. The player has a play button, a volume icon, and a full screen icon.

IV. Questions

Any questions...

...of a technical nature?

→ FIDLEG-FINIG@finma.ch

...concerning the EHP or IT?

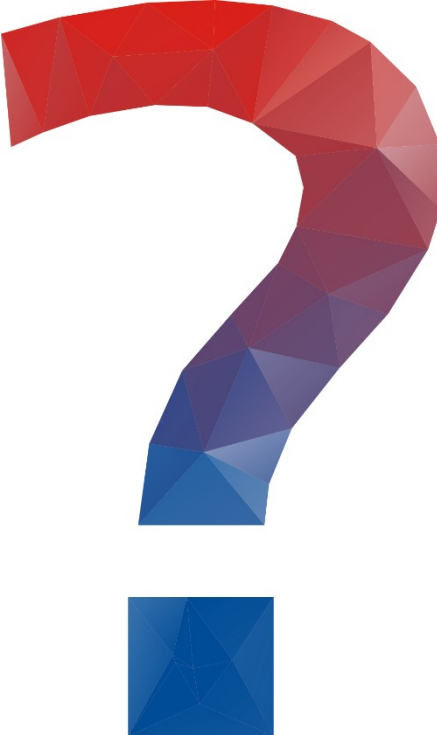
→ www.finma.ch/ehp-support

Swiss Financial Market Supervisory Authority FINMA

Laupenstrasse 27

CH-3003 Bern

www.finma.ch



THANK YOU!