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Eidgenössische Bankenkommission
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Swiss Federal Banking Commission

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Collective investments: the SFBC listens to the market

The Banking Commission's legal framework and approach with regard to investment funds underwent a number of developments and changes in 2005. The main changes were the partial revision of the Banking Commission's Ordinance on Investment Funds (IFO-FBC), the extension of the scope of supervision to include independent Swiss managers of euro-compatible foreign funds, the Swiss Funds Association's (SFA) guidelines on transparency with regard to management fees, the new exemptions granted to funds for institutional investors and the liberalisation of public advertisement practices.

These examples demonstrate that the Banking Commission is committed to combating over-regulation while still respecting the legislator's desire to protect investors, and that it is keen to respond to international demands and safeguard the interests of the Swiss financial sector.[1]

Extremely strong growth in the Swiss market

The Swiss market enjoyed strong growth in 2005, as evidenced by the following figures:

- Number of Swiss funds authorised for sale as at 31 December 2005: 954 versus 735 as at 31 December 2004.

- Number of foreign funds authorised for sale and distributed in Switzerland as at 31 December 2005: 3,980 versus 3,605 as at 31 December 2004.

- Assets of Swiss funds as at 31 December 2005: 275.5 billion, versus 186.6 billion as at 31 December 2004.

[1] More details on the topics covered in the rest of the speech can be found in the Annual Report, p. 134ff. (German) or p. 136 ss (French)

Switzerland on the international stage

The Ordinance of the Swiss Federal Council on Investment Funds (IFO) was partially revised in 2004 to adapt it to two new UCITS directives adopted by the European Union in 2001. As part of this partial revision, the Federal Council introduced a simplified prospectus for securities funds. The supervisory authority was charged with defining the content of the prospectus information in line with European law. Due to delays in this process, the partial revision of the Banking Commission's Ordinance on Investment Funds (IFO-FBC) could not enter into force until 31 December 2005. The two chapters in Part 2 have been joined by a third chapter entitled "Simplified prospectus for securities funds" which integrates the EU recommendations in a binding manner.

To ensure that Swiss funds remain euro-compatible, the future Collective Investment Act (CIA) and its implementing ordinances will integrate all the provisions of the two UCITS directives, in particular the Investment Services Directive, which was only partly integrated into the partial revision of the IFO as it necessitates a complete overhaul of the current legal framework.

SFBC initiatives to support Swiss intermediaries

The Banking Commission has decided, based on a pragmatic interpretation of the Federal Act on Stock Exchanges and Securities Trading, to grant authorised securities dealer status on request to independent Swiss managers who manage euro-compatible foreign funds. This solution protects these managers from a possible loss of market share or even total exclusion from the European investment fund market as a result of European investment fund legislation, which requires that managers of euro-compatible UCITS be subject to state supervision in their country of origin.

The Banking Commission has developed this approach to avoid the need for new regulation and to provide a solution that does not require the creation of a new category of securities dealer.

Partnership with the Swiss Funds Association

The Banking Commission promotes self-regulation wherever possible and recognises the standards of the Swiss Funds Association as minimum standards based on SFBC Circular 04/2 "Self-Regulation Recognised by the Swiss Federal Banking Commission as Minimum Standard", in conjunction with Art. 56 para. 4 of the IFO and Arts. 22 para. 3 and 56 para. 3 of the IFO. Examples of recently recognised self-regulation standards include the guidelines for the calculation and publication of fund performance issued on 27 July 2004 and the guidelines for the calculation and publication of the "total expense ratio" (TER) issued on 13 June 2003.

The Banking Commission has held a number of discussions with the Swiss Funds Association on the problem of the costs of investment funds. The latter has agreed to address this issue within the framework of self-regulation, and has issued guidelines on transparency with regard to management fees that the Banking Commission has rec-

ognised as minimum supervisory standards. The purpose of these guidelines is twofold: firstly, to enable investors to form an objective opinion of the envisaged use of the management fees debited from a fund before they purchase units in that fund; and secondly, to promote equal treatment for all types of investor, both ordinary and institutional.

With this in mind, the simplified prospectus for structured products will also be governed by self-regulation (see below).

Self-regulation can only function if fund managers demonstrate irreproachable conduct. The Banking Commission therefore attaches huge importance to this aspect, and is currently conducting an inquiry into compliance with due diligence obligations.

Deregulation initiatives

If the fund manager proves that only institutional investors with professional treasury are authorised to invest in the fund, the Banking Commission may, on a case-by-case basis, waive certain provisions of the Investment Fund Act in accordance with Art. 2 para. 2 of the IFO. It has established a well-developed approach in this area, and in addition to the exemptions to the Investment Fund Act which have now become common currency, such as the waiver of the obligation to issue and redeem units in cash, the Banking Commission has announced three new decisions which round off its practice: it has authorised the first mortgage fund under Swiss law and has announced decisions regarding the delegation of investment decisions for single-investor funds and the eligibility of minority investments in real estate funds.

The Banking Commission has also liberalised the investment fund sector through an amendment to SFBC Circular 03/1 “Public advertising within the context of the Investment Funds Act”, which came into force on 1 April 2006.

The Banking Commission has now liberalised and extended the concept of a qualified relationship with advertisers or distributors of investment funds. In the new version of the circular, investment advisory services provided by banks and securities dealers no longer constitute public advertising if there is a written advisory agreement between the institution and the client and the institution verifies that the client has financial assets of at least CHF 5 million. Wealthy private clients, referred to as High Net Worth Individuals (HNWIs), are therefore also considered to have a qualified relationship.

Through this liberalisation, the Banking Commission has partially acceded to the wishes of the fund industry and the banks. It continues the course set by the revision of the Investment Fund Act. In the new Collective Investment Act (CIA) wealthy private clients are to be put in the same category as institutional investors.

The Collective Investment Act

The National Council approved the draft Collective Investment Act during its spring session. The text of the act is currently with the Committee for Economic Affairs and Taxa-

tion of the Council of States, and should be submitted to the latter during its summer session. The bill could then be definitively passed, subject to delays due to possible conciliation procedures between the two parliamentary chambers, and could come into force at the beginning of 2007. The Banking Commission has worked extremely hard right from the outset to support this project, and therefore looks forward to this new instrument for promoting the attractiveness of Switzerland's investment fund industry becoming available as soon as possible.

In terms of content and form, the CIA is based on the draft submitted for consultation in 2004. Some chapters have been amalgamated, while others have been rewritten in extra detail to ensure greater legal certainty. One such example concerns the provisions relating to new types of legal entity (the investment company with variable capital [société d'investissement à capital variable] SICAV and the limited partnership for collective capital investment [société en commandite de placements collectifs]). Investment foundations, meanwhile, whose inclusion had been criticised during the consultation process, no longer fall within the scope of the CIA. The same applies to investment companies with fixed capital [sociétés d'investissement à capital fixe] (SICAF), which the National Council has also decided to remove from the scope of the CIA. At this stage, however, initial discussions within the Committee for Economic Affairs and Taxation of the Council of States (CEAT-S) suggest that the provisions relating to SICAFs are not yet definitive.

The treatment of SICAVs is one of the greatest achievements of the CIA. In contrast to the draft act submitted for consultation, the CIA regulates SICAVs autonomously and only refers to the provisions of the Swiss Code of Obligations relating to joint stock companies for secondary points. In line with the EU Investment Services Directive, the CIA allows for two forms of SICAV – self-managed SICAVs and SICAVs managed by third parties. In the case of self-managed SICAVs, the executive team (a body of the company) is responsible for its management. As for SICAVs managed by third parties, in other words SICAVs who delegate management to an authorised fund manager, they do not have to meet any additional organisational conditions except with regard to legal bodies (board of directors, general meeting, audit company).

The limited partnership for collective capital investment, as a vehicle for venture capital investments, is open solely to qualified investors. Contrary to the provisions of the Swiss Code of Obligations relating to limited partnerships, the unlimited partner may be a joint stock company, which is responsible for management. The limited partners are excluded from the management of the company. They may not decide on certain investments, nor may they block investment decisions. The rights of the parties to the agreement are set out in the partnership agreement.

The CIA takes into account the differing need for protection of the various categories of investor. A distinction is made between ordinary investors and qualified investors. The range of qualified investors includes in particular institutional investors and now affluent private individuals. The CIA provides for a 'simplified' authorisation or approval procedure for collective capital investments designed to facilitate the simple and rapid authorisation of standard funds and funds reserved for qualified investors. Based on the results of the consultation process, the concept of "public advertising" was defined in

the act. In view of the hefty criticism received, the official naming of financial intermediaries guilty of wrongdoing was removed from the draft bill.

As for structured products, the parliamentary debates on the CIA resulted in a solution in the shape of Art 5 of the CIA. Pursuant to this article, structured financial instruments are not subject to the new act apart from the minimum regulation included in the act for reasons of legal certainty. Consequently, only banks and securities dealers as well as foreign institutions subject to equivalent supervision are authorised to advertise structured products to the public. Furthermore, for reasons of transparency these issuers must publish simplified prospectuses containing the principal characteristics, opportunities and risks of the product. The model prospectus will be developed by means of self-regulation. The prospectus must also state that the structured product is not an investment fund and has not been authorised by the Banking Commission.

The prospects for the imminent entry into force of the CIA also present new challenges for the Banking Commission, above all due to the increase in the number of entities subject to supervision (SICAVs, Swiss fund managers, limited partnerships for collective capital investment).