

# **Symposium for Portfolio Managers and Trustees**

17 February 2022

# Programme

## **Welcome**

Tobias Lux, FINMA spokesperson

## **Introductory remarks**

Philip Hinsén, provisional Head of Asset Management division, FINMA

## **Framework for the authorisation process**

Kenneth Ukoh, Asset Management division, FINMA

## **Findings and challenges on the path to the authorisation**

Paolo Ader, Asset Management division, FINMA

## **Q&A session**

Host: Tobias Lux, FINMA spokesperson

## **Suitability aspects in portfolio management**

Simone Tobler, Markets division, FINMA

## **Focal points for trustees**

Dorothee Ignatz, Asset Management division, FINMA

## **Q&A session**

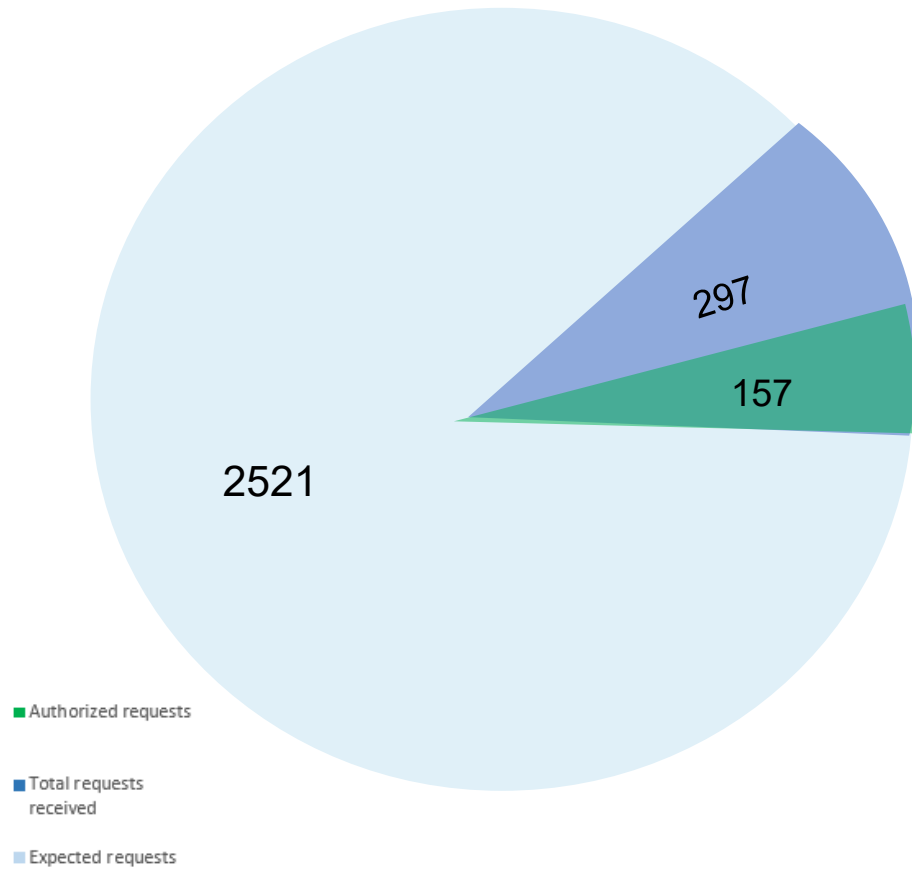
Host: Tobias Lux, FINMA spokesperson



# Introduction

Philip Hinsén

## Starting point: where are we now?



Data as of 31 January 2022



Source: Nirmal Purja /<https://www.nzz.ch/panorama/bilderverbot-am-mount-everest>



# Framework for the authorisation process

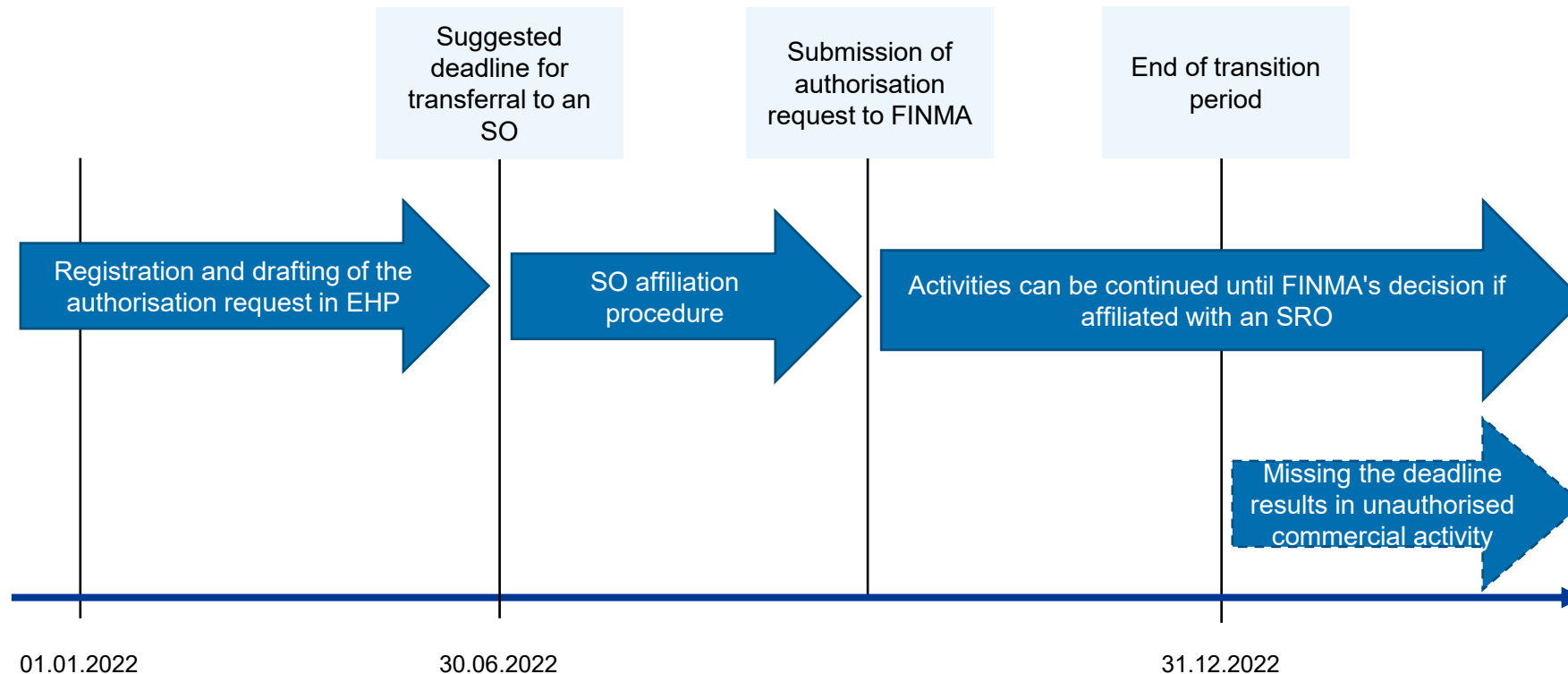
Kenneth Ukoh

## Transition period and timeline

**31 December 2022**

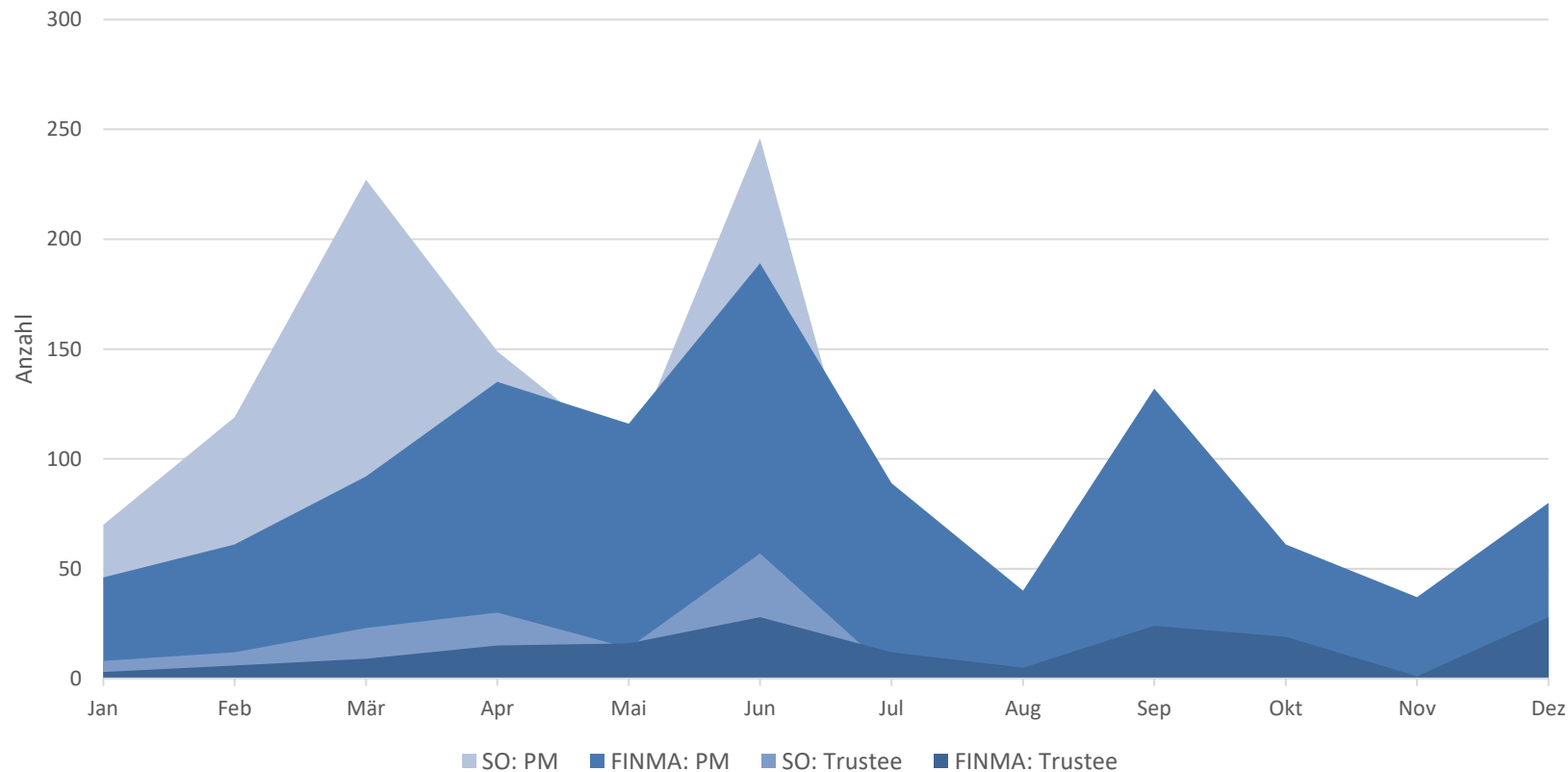
Financial institutions which are newly subject to an authorisation duty must fulfil the requirements of the FinIA and must submit an authorisation request to FINMA (Art. 74 para. 2 FinIA)

It is the duty of the institution to meet the deadline



# EHP survey – preview of the request wave

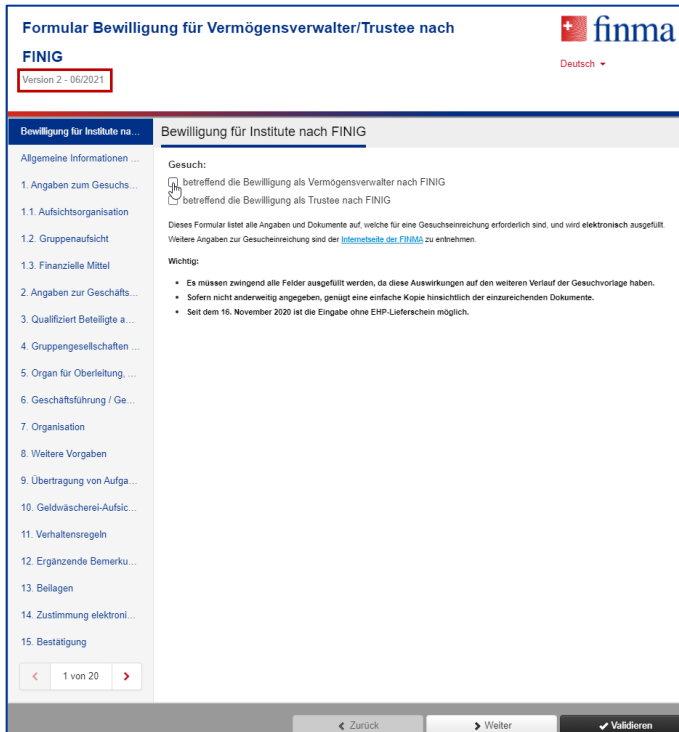
Volume and distribution of requests SO / FINMA



## Key findings

- EHP survey was sent to 2,500 registered institutions
- Return rate 66% (1'645)
- 1'224 / 74% institutions will be submitting their request to the SO by 30 June
- 1'351 / 82% institutions will be submitting a request by 31 December
- 222 / 13% institutions will not be submitting a request
- 72 / 5% institutions did not answer

# Digital requests in the EHP



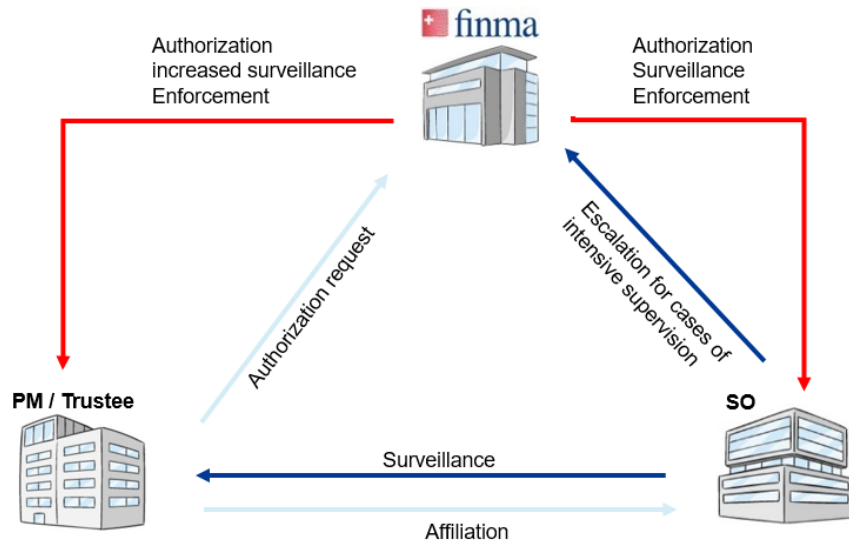
The screenshot shows the 'Formular Bewilligung für Vermögensverwalter/Trustee nach FINIG' (Version 2 - 06/2021) in German. The form is titled 'Bewilligung für Institute nach FINIG'. It includes a table of contents on the left with 15 sections, and the main content area shows the 'Gesuch' (Request) section. The 'Gesuch' section contains two sub-sections: 'betreffend die Bewilligung als Vermögensverwalter nach FINIG' and 'betreffend die Bewilligung als Trustee nach FINIG'. Below these, there is a note stating that the form is for electronic submission and that further information can be found on the FINMA website. A 'Wichtig:' (Important) section follows, with three bullet points: 1. All fields must be filled out as they affect the further course of the application. 2. If not otherwise specified, a simple copy of the original documents is sufficient. 3. Since November 16, 2020, electronic submission without EHP is possible. At the bottom, there are navigation buttons: '< Zurück', '> Weiter', and 'Validieren'.

## Key points

- As of 1 October 2021, you are required to use **authorisation form version 2.0**
- Submission is fully electronic and without signature
- **Paper submissions** will not be accepted
- Original documents must be kept by the institution
- The authorisation request and the corporate documents must be submitted in an **official language**. Other documents can be submitted in English.
- You can find visual aids online: <https://www.finma.ch/en/authorisation/portfolio-managers-and-trustees/bewilligungsprozess/>



# SO affiliation procedure



## Key points

- Early affiliation with an SO of your choice by 30 June 2022 at the latest
- Request needs to be assigned to the SO in the EHP and must not be "submitted".
- The SO will analyse the affiliation based on the authorisation request
- This pre-examination is based on FINMA's requirements
- The **instructions given by the SO** must be followed
- The SOs may not transmit incomplete requests
- Following the analysis, the SO will confirm the affiliation in writing
- Only following receipt of the written confirmation may the authorisation request be submitted to FINMA

# FINMA authorisation procedure I

## Key takeaways regarding the eligibility for approval

- Generally applicants display high willingness to cooperate
- Improvements requested by FINMA lead to some requests being withdrawn
- First authorisations granted to individual and small businesses

## Authorisation requirements

### Authorisation

- ✓ Complete request including SO affiliation
- ✓ Proof that authorisation requirements will be met
- ✓ Appropriate limitation and control of inherent risks
- ✓ Information and cooperation in the procedure

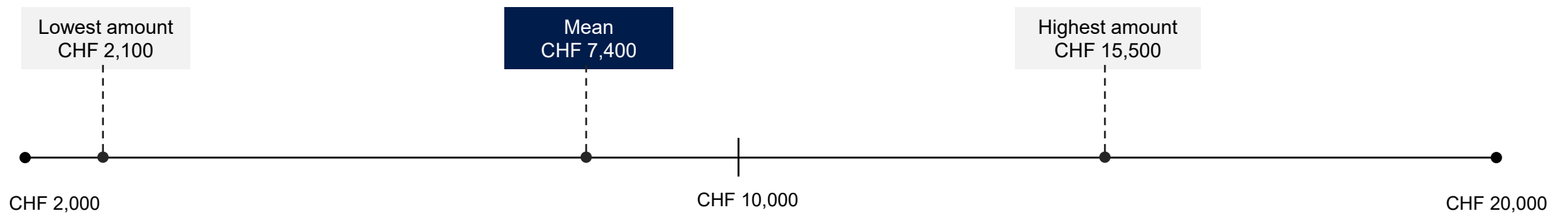
### No authorisation

- × Poor application quality / incomplete and inconsistent information
- × Authorisation requirements not met
- × No adequate risk management
- × Violation of the duty to provide information and to cooperate

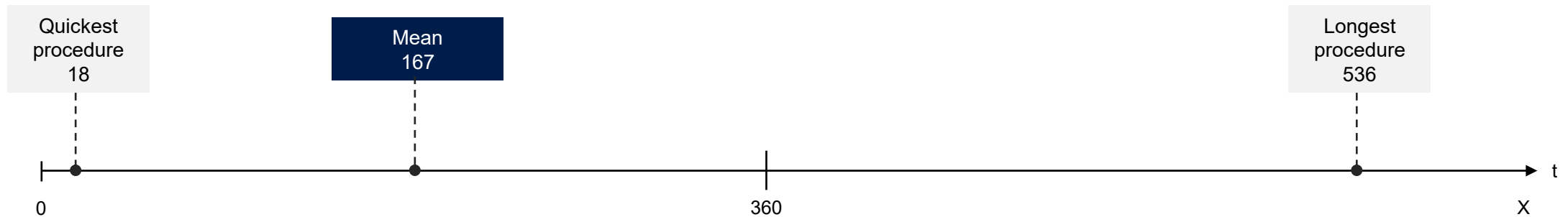
# FINMA authorisation procedure II

**Quality of the request as the determining factor for duration and cost**

## Costs



## Duration of procedure (days)



# Findings and challenges on the path to the authorisation

Paolo Ader

## FINMA's goals in the authorisation procedure

- FINMA creates an **efficient, transparent and risk-oriented** authorisation procedure while ensuring a level playing field
- In doing so, FINMA applies a **rigorous but fair assessment standard** and thus contributes to **portfolio managers' and trustees' respectful treatment of their clients**
- The **authorisation** functions as a **seal of approval**

## Proportionality of the risk-based authorisation procedure

### Complex business model with high risks

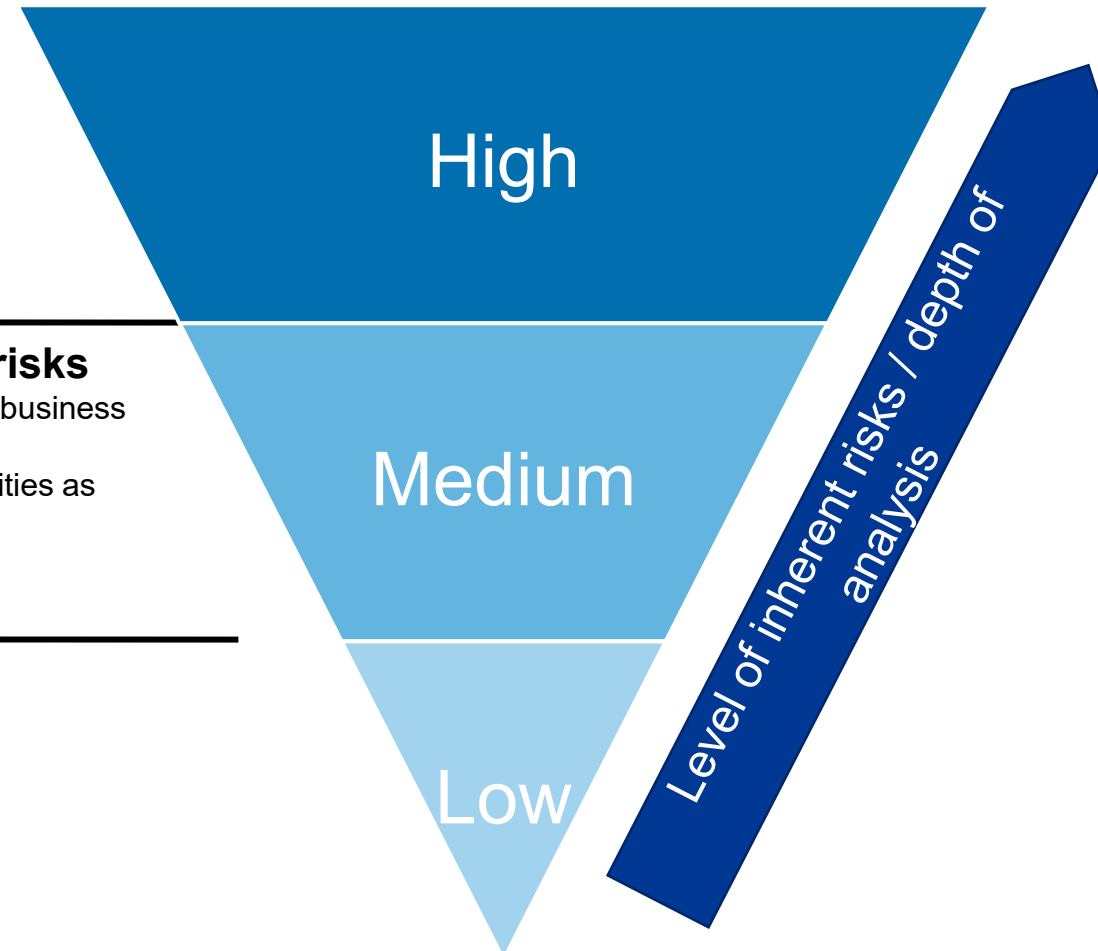
- Largely independent senior management body
- Increased requirements for professional qualifications as well as adequacy of the organisation

### Standard business model with significant risks

- Appropriate and appropriately qualified personnel for the business activity
- Business model must correspond to the financial possibilities as well as the operational organisation
- Principle of separation of risk control functions

### Simple, low-risk business model

- Possibility of single-member companies
- Lean instruction and control system

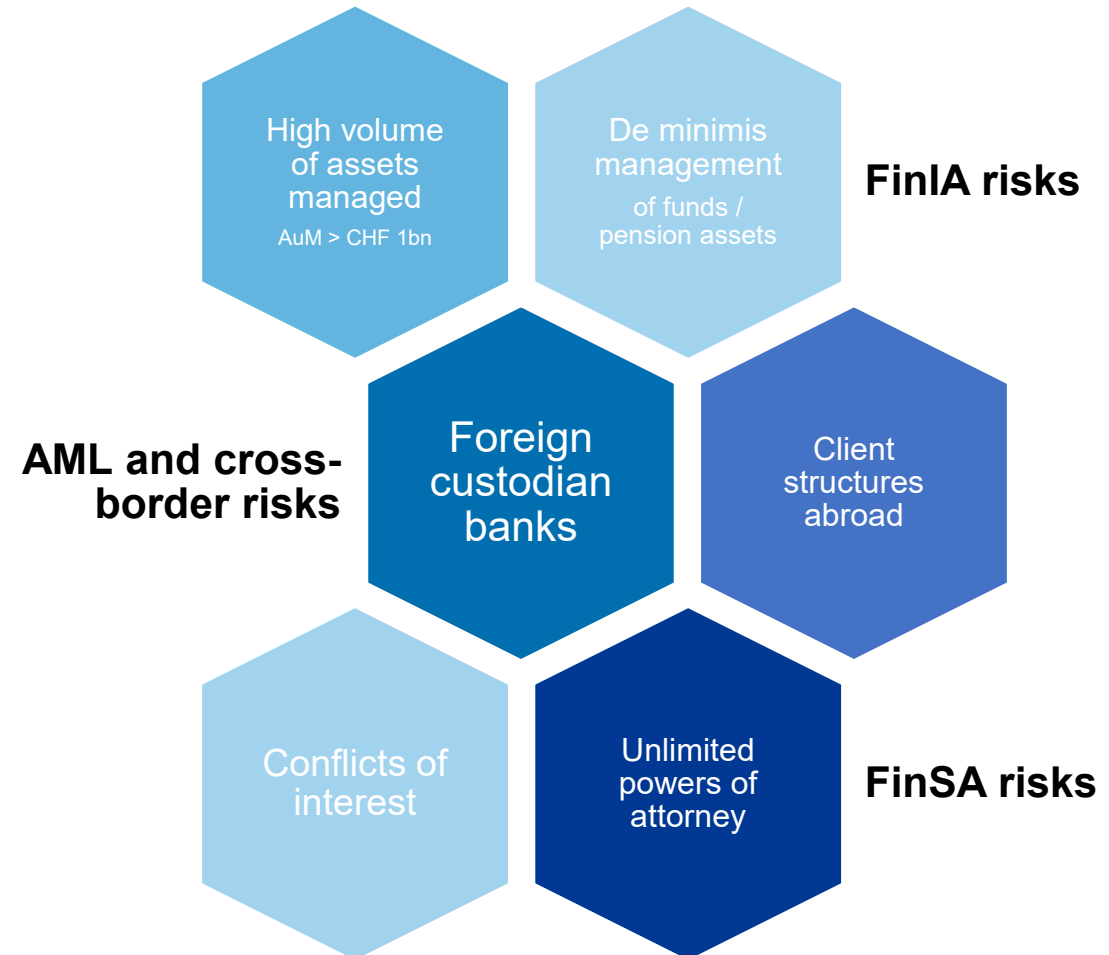


## High-risk business models

It is up to FINMA to define the term "*high-risk business models*"

The following circumstances are considered risky, even if they are below the threshold of Article 26 para. 2 FinIO

**In principle, separation of the control functions from the operating units**



## Findings pertaining to authorisation requests

### Internal documentation

- The **internal documentation** of financial institutions must be adapted to the effective organisation of the institution and the associated business models
- **Professional qualifications**: not only at the level of the executive board but also at the level of the governing body, the control functions and the other key functions (compliance and risk management)
- **Independence of the control functions** (especially compliance and risk management): if provided for or necessary, must be effectively implemented and also ensured in the case of deputies

### International clients and cross-border risks

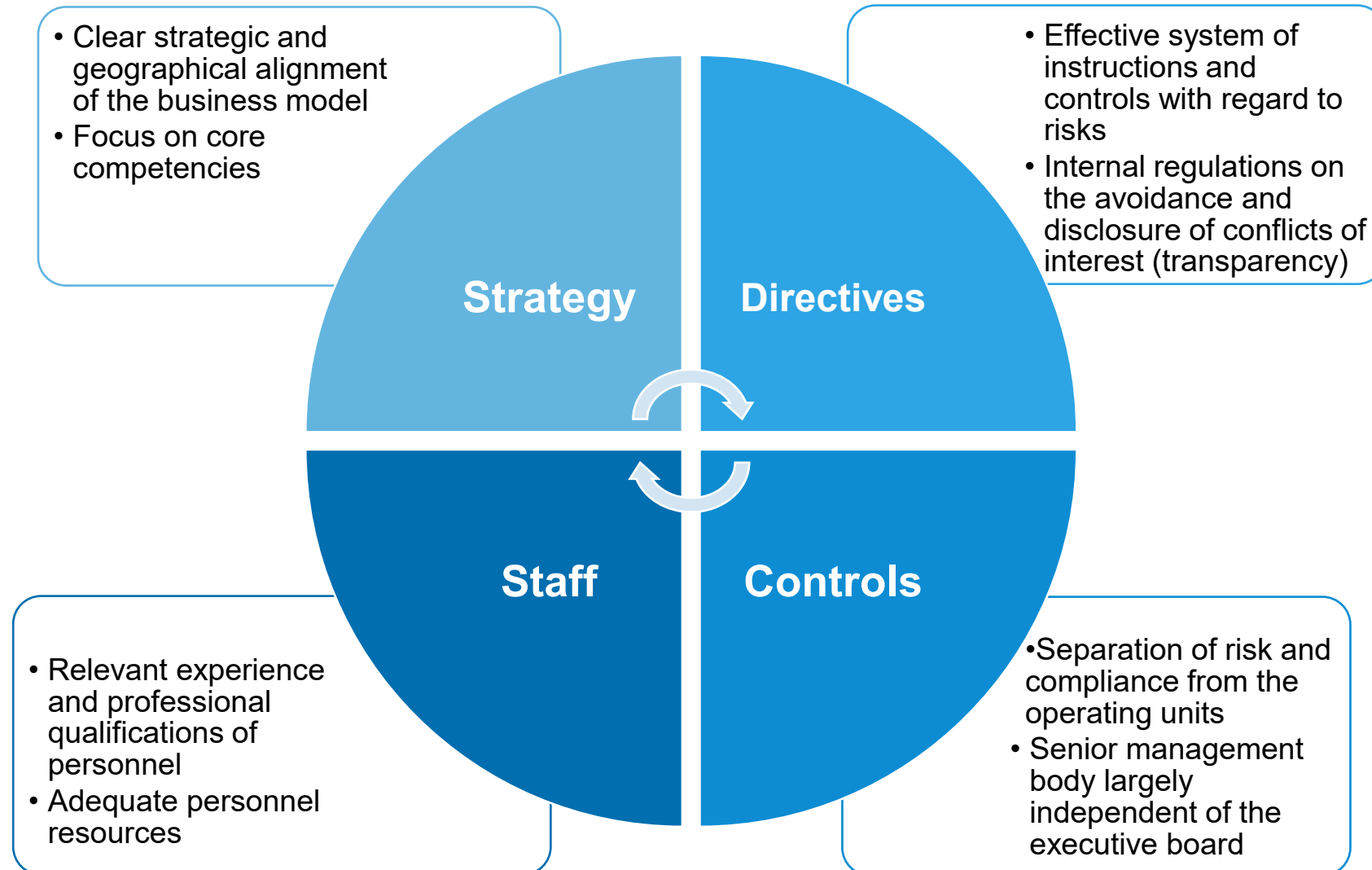
- Understanding of **risks associated with cross-border activities** and adequacy of internal policies
- **Fragmented customer base** could lead to in-depth clarifications and comprehensive documentation being expected

### Financial guarantees

- **Detailed and precise calculation** of the financial guarantees based on the last balance sheet (if available, otherwise business plan)



## Risk management measures



# Q&A

Tobias Lux, FINMA spokesperson





# Suitability aspects in portfolio management

Simone Tobler

# FINMA on-site inspections and benchmarking

Suitability	Internal control system	Contractual relations	Risk profiles	Product classification	Diversification	Own investment funds	Risk information and inventory	Retrosessions	Training and development
<ul style="list-style-type: none"> <li>• Strategy</li> <li>• Guidelines, instructions</li> <li>• Management involvement</li> <li>• Management reporting</li> </ul>	<ul style="list-style-type: none"> <li>• Point of sale Controls</li> <li>• Downstream controls</li> <li>• Compliance &amp; risk control integration</li> <li>• Reports</li> </ul>	<ul style="list-style-type: none"> <li>• Asset management</li> <li>• Investment advice</li> <li>• Execution only</li> </ul>	<ul style="list-style-type: none"> <li>• Existence</li> <li>• Content</li> <li>• Regular updating</li> <li>• Control of deviations</li> </ul>	<ul style="list-style-type: none"> <li>• Method</li> <li>• Risk aggregation</li> </ul>	<ul style="list-style-type: none"> <li>• Requirements</li> <li>• Control</li> </ul>	<ul style="list-style-type: none"> <li>• Own volumes of PM, IA and EX-O funds</li> </ul>	<ul style="list-style-type: none"> <li>• Process</li> <li>• Documentation</li> <li>• Control</li> </ul>	<ul style="list-style-type: none"> <li>• Disclosure</li> <li>• Waiver</li> <li>• IA, PM, EX-O</li> </ul>	<ul style="list-style-type: none"> <li>• Specialist knowledge</li> <li>• Behavioural requirements</li> <li>• Internal processes and systems</li> </ul>
<p><i>Institution's suitability strategy, design of overall suitability processes and assessment of whether they are appropriate for risk reduction. Is management involvement adequate? Existence of appropriate management reporting?</i></p>	<p><i>How is the control system designed and what controls are performed at what intervals at the point of sale or downstream? Pending item management and escalation processes. Integration of independent risk functions. Reporting.</i></p>	<p><i>Contractual separation of PM, IA and EX-O clients. Systematic or ad hoc investment advice to EX-O clients? Compliance with due diligence obligations for these clients.</i></p>	<p><i>Appropriate content for the assessment of risk capacity and readiness? Consideration of knowledge and experience. Regular checking of the currency and the discrepancies between the risk profile and the content of the deposits?</i></p>	<p><i>What method (e.g. volatility, asset class, combination of indicators, liquidity) is applied to calculate product risks? How is risk aggregation performed at the portfolio level?</i></p>	<p><i>Are there any diversification requirements applied to PM and IA and how is compliance ensured? Regular monitoring of risk concentrations. Processes for handling and reporting to clients.</i></p>	<p><i>What volume for own investment funds in PM and IA? Process for reducing conflicts of interest (e.g. in PM).</i></p>	<p><i>When and how is risk information communicated? What standardised processes and instruments are used? Is the documentation appropriate? Compliance with the inventory obligation CISA Art. 24 para. 3.</i></p>	<p><i>Retrosessions waived or disclosed. Adequate transparency regarding calculation parameters. Differences between PM, IA and EX-O.</i></p>	<p><i>Do front office staff and portfolio managers have the necessary specialist knowledge? How and how often are employees trained in behavioral requirements/systems and internal guidelines/processes?</i></p>

## Contractual relationships (1/2)

### ➤ Topics:

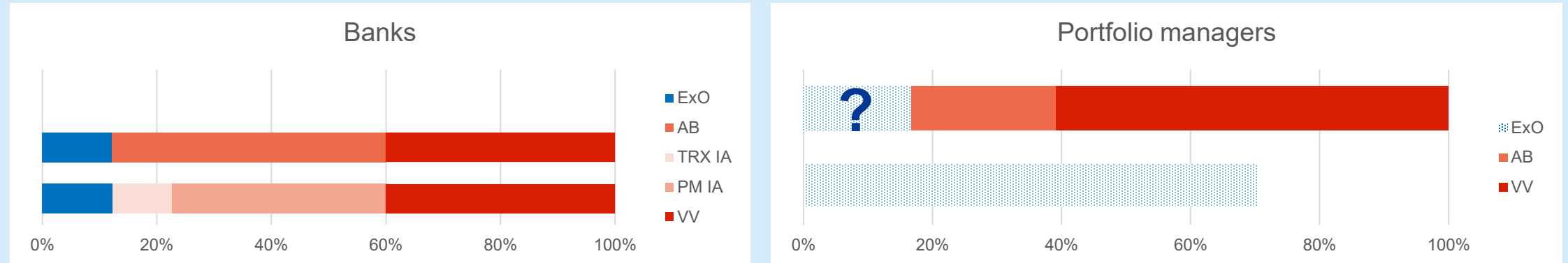
- Separation of asset management, investment advisory and execution-only clients
- Compliance with the respective duties of conduct for these clients

### ➤ Findings:

- Need for action regarding suitability obligations, especially for **investment advice** (e.g. risk profiles, internal control system)
- **Demarcation between execution only and investment advice** not yet fully implemented

## Contractual relationships (2/2)

Example 1: *Distribution of financial service types by custody value for asset managers and banks:*



Example 2: *"Contact notes are not documented in such a way that it can be traced whether execution only or advice has been given and the client advisers have fulfilled the respective suitability obligations, especially if clients hold several custody accounts."*

## Use of in-house products (1/2)

### ➤ Topics:

- Volume of in-house investment products in asset management and investment advisory services
- Minimisation and disclosure of conflicts of interest

### ➤ Findings:

- In particular, there is a need for an **objectified selection process** for proprietary vs. third-party products, the right remuneration incentives, separation of functions between product management and sales
- Clients must be able to see the **extent** to which proprietary products are taken into account
- All (potential) **conflicts of interest**, including their causes, must be disclosed

## Use of in-house products (2/2)

### ➤ Examples:

Example 1: *"The conflict of interest fact sheet does not disclose that certain investment solutions are limited to in-house products."*

Example 2: *" The administration contract provides for the possibility of investing part of the discretionary mandate funds in collective investments managed by (...). However, our random sampling identified cases where the entire assets of the business relationship were invested in in-house funds."*

Example 3: *"In the basic contract documentation, reference is made to information on the institution's website for the disclosure of conflicts of interest."*

Example 4: The reason for conflicts of interest is not disclosed (e.g. that the institution manages financial instruments and receives a management fee for this, which is charged directly to the financial instrument).



## Retrocessions (1/2)

### ➤ Topics:

- Retention of third-party compensation (brokerage fees, discounts, etc.)
- Minimum content and medium of advance information on third-party compensation

### ➤ Findings:

- Many institutions continue to retain retros despite declining trend
- Transparent information on ranges is "key" for valid advance waiver
- In the case of asset management and portfolio-related advice, retros must be disclosed as a percentage/range of custody assets (see [Federal Supreme Court decision 4A\\_355/2019 of May 13 2020](#))

## Retrocessions (2/2)

### ➤ Examples:

Example 1: Based on a table with different percentages for individual asset classes (e.g. funds, structured products), clients cannot correctly assess the amount of third-party compensation and compare it with the amount of the management fee.

Example 2: *"A mere reference to the website with the overview of compensation in the investment business does not ensure [sufficient information about the scope of retrocessions]."*

Example 3: The ranges must be defined in such a way that clients can make a meaningful assessment of the compensation. A generic bandwidth of 0-3% is not suitable for this purpose.

Example 4: *"The Bank retains the commission without prior agreement with the client, or without having drawn the client's attention to such a particular clause in the contract."*

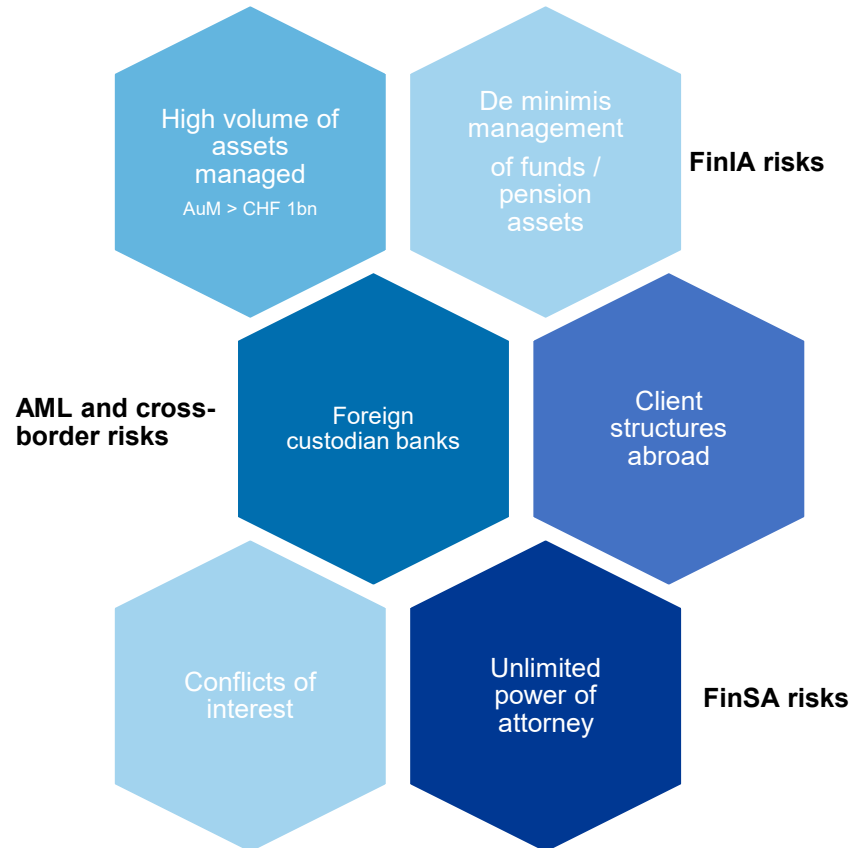
# Focus topics for trustees

Dorothee Ignatz

## Introduction

- Activity as trustee is newly subject to **prudential licensing and supervision**
- FINMA's **risk-based authorisation approach** also takes into account the specifics of trustees
- **Definition of trustee-specific business models** with increased risks as well as expectations for appropriate risk management
- **Clarification of the authorisation requirements** for trustees on core aspects such as minimum substance, organisational requirements as well as due diligence and fiduciary duties

## Business models with increased risks: trustee-specific risks



### Trustee-specific risks



**Responsibility for corporate decisions or maintenance of non-bankable assets.** Trustee can be sued for breach of trust

**Trust laws vary.** Furthermore, trustees must consider **legal implications for beneficiaries** when making **distributions**

## Business models with increased risks: expectations of trustees

**Specific knowledge** in the management of assets or **transfer to qualified third parties**

**Access to specialists** from the relevant jurisdictions

**Recording the risks** in the risk analysis and **formalising the controls** in the ICS

Fundamental **independence of risk management** and operational activities

## Requirements for minimum substance

### Empty structures are not eligible for authorisation

- At least **one qualified managing director** - in the case of extended management, all members must be **employed on the basis of an employment contract**.
- **The role of qualified managing director cannot be delegated**. However, it is possible for a qualified managing director to work for several financial institutions (conflicts of interest must be adequately considered)
- Financial institutions must have **staff that are appropriate to their business** and appropriately qualified
- **No umbrella authorisation**, authorisation can only be granted at the institution level

### Outsourcing requirements with regard to the minimum substance

- **Essential tasks may be delegated** if this **does not affect the appropriateness** of the company's organisation
- Essential tasks that are typically delegated: **asset management** and **trust accounting**

## Trustee-related duties of care and loyalty

### Retention of due diligence and fiduciary duties in the internal directives

(Art. 24 para. 4 FinIO)

- **Written** trust instrument
- **Preservation** of value and earmarked use of the trust assets
- Investment of the trust assets in **accordance with the applicable trust law** and in accordance with the provisions of the deed of creation
- Act exclusively in the interest of the **beneficiaries** and **avoid conflicts of interest** in accordance with the applicable trust law
- In **accordance with the applicable trust law** and the **provisions of the instrument of incorporation**, to act impartially towards beneficiaries



## Trustee-related organisational requirements

### Specification of organisational requirements in the internal directives

(Art. 24 para. 4 FinIO)

- **Separation of the trust assets**
- **Access to specialists** (lawyers specialising in trusts, tax experts, asset managers, accountants)
- Ensuring that, in accordance with the applicable trust law and the provisions of the deed of creation, entitled parties can be **provided with information on trust assets, business activities and claims / entitlements** (in principle, **trust accounting** is required)
- **Availability of current contact details of parties involved** (settlor, beneficiaries, protector, etc.)

# Q&A

Tobias Lux, FINMA spokesperson



Should you have further questions regarding the topics discussed at the symposium, you can contact [assetmanagement@finma.ch](mailto:assetmanagement@finma.ch)