CapLaw

SWISS CAPITAL MARKETS LAW

No. 4/2011

Securities

Regulatory

Takeover

Deals & Cases

Events

FINMA Opened Consultation on the Draft FINMA Stock Exchange Ordinance

Reference: CapLaw-2011-32

The Swiss Federal Market Supervisory Authority FINMA has opened the consultation for the partial revision of its ordinance on stock exchanges and securities trading (SESTO-FINMA). The revision focuses primarily on the rules regarding disclosure requirements for foreign collective investment schemes. Other aspects of the revision include clarifications with respect to exact thresholds being reached and the publication of notifications. The consultation period ended on 5 September 2011.

By Petra Ginter

1) Introduction

The SESTO-FINMA entered into force on 1 January 2009. The application of the provisions on the duty to disclose shareholdings (third chapter) has shown some practical problems which should be eliminated or reduced with the proposed new rules.

2) Duty to Disclose Shareholdings in Case of an Exact Threshold being Reached

According to article 20 (1) of the Stock Exchange Act, whoever directly, indirectly or in concert with third parties acquires or sells for its own account shares or purchase or sale rights relating to shares in a company incorporated in Switzerland which are listed in whole or in part in Switzerland and thereby *attains, falls below or exceeds* certain threshold percentages of voting rights whether or not such rights may be exercised, must notify the company and the respective stock exchanges. Lately, there have been some cases where investors acquired or sold equity instruments thereby reaching an exact threshold which they have disclosed accordingly. In this respect the question arose whether a subsequent acquisition or disposal of equity instruments thereby abandoning the exact threshold value would trigger a new disclosure duty. Neither the statute nor the respective FINMA ordinance, as currently in force, provide for a clear answer whether the investor is subject to a "double" disclosure duty, *i.e.* whether it needs to disclose the reaching of an exact threshold value as well as the subsequent falling below or exceeding of the respective threshold value. Therefore, in view of the threatened sanction in case of a breach of the disclosure duties, a clarification seems to be in the interest of all market participants.

FINMA is of the view that the threshold value system as implemented by the legislator presumes that it is always clear in which margin (between two threshold values) the participation of an investor is moving. It is therefore not required—and from a transparency perspective not necessary—that an additional notification must be submitted if a previous notification clearly indicates in which margin the investor is moving. In other words, it is sufficient that it can be assumed from a notification of exactly 5% that subsequently the shareholding of the investor may be moving between 5 and 10% without a new notification becoming necessary.

The proposed new article 11 (3) SESTO-FINMA is based on the understanding that the threshold value should be counted to the respective upper margin (until the next higher threshold). *I.e.,* if an investor reaches an exact threshold value and discloses such event it must not submit a new notification if it subsequently moves away from this threshold value towards the next higher threshold value. This holds of course only true until such next higher threshold value is reached or exceeded. In the opposite case, if an investor moves away from the exact threshold value as notified in the direction of the next lower threshold value, a new notification becomes necessary. If an investor has notified a shareholding between two threshold values and subsequently reaches exactly the lower of the two thresholds values it is not required to submit a new notification.

3) Duty to Disclose Shareholdings of Collective Investment Schemes

The current article 17 SESTO-FINMA comprises a special provision. On the one hand, it contains in paragraph 1 an independent definition of the subject that is required to notify the shareholding. For licensed collective investment schemes under the Collective Investment Scheme Act (CISA) the "licensee" is required to disclose the shareholding. This means that the subject that is required to disclose the shareholding is not determined according to the general rule of article 9 (beneficial owner) but according to the special provision of article 17 (1) SESTO-FINMA. Further, article 17 (4), as currently in force, sets forth that information on the identity of investors in the fund is not necessary. *I.e.*, article 17 SESTO-FINMA does not only determine the licensee of the collective investment scheme as the subject that is required to disclose the shareholding, but also excludes other persons (investors) explicitly from the duty to disclose their shareholdings. This exemption is based on the fact that—under the CISA—investors of contractual collective investment schemes must not have any influence on the licensee, *i.e.* the fund management company which is required to disclose the shareholding.

Further, article 17 (2) (b) SESTO-FINMA sets forth that fund management companies within a group of companies are not obliged to consolidate their holdings with those of the group companies. This is to be understood as an exemption from article 10 (2) (c) SESTO-FINMA (and article 9 (3) SESTO-FINMA respectively) pursuant to which shareholdings within a group of companies must in principle be disclosed on a consolidated basis. The rationale is that the licensees within the meaning of article 17 SESTO-FINMA (primarily fund management companies) are with respect to their investment activities fully independent from the rest of the group companies (accordingly, compliance with the independence requirement with respect to the exercise of membership and creditors rights according to article 23 (1) CISA is one of the key aspects of the regulatory reviews of licensees under the CISA, and the supervision has been tightened in this respect). Therefore, and also with a view to the European Law which applies a privilege for collective investment funds, the current concept will be maintained for licensees under the CISA.

Should—despite the legally required independence according to article 23 SESTO-FINMA—an investor have an influence on the exercise of voting rights of the shareholdings of the collective investment scheme, article 9 (3) (d) SESTO-FINMA can be used as fallback provision. In such case, an investor will be required to disclose the shareholding directly because the controlling influence of the respective investor on the collective investment scheme must be considered as indirect holding of the equity instruments that are held by the collective investment scheme.

FINMA has realised that the possibility as set forth in article 17 (3) SESTO-FINMA for foreign collective investment schemes which are not authorised for public distribution in Switzerland to provide an independence proof in order to benefit from the exemption of the duty to disclose the shareholding on a consolidated basis, has not been used in practice. The reason for this was that the foreign regulators did usually not wish to provide respective confirmations. Considering this issue, FINMA proposes the following amendment to article 17 SESTO-FINMA: With the new article 17 (3) an independent "disclosure law" definition of the required independence should be added to the ordinance for foreign collective investment schemes which are not authorised for public distribution in Switzerland. This should solve the problem of the *de facto* exclusion of the current article 17 (3) SESTO-FINMA, as discussed above. The proposed definition of the required independence shifts the focus to the exercise of the voting rights which is crucial for the disclosure law. In article 17 (3) (a) (personal independence) and article 17 (3) (b) SESTO-FINMA (organisational independence) the independence requirements will be substantiated. If the licensee met both conditions and confirmed this vis-à-vis the SIX Disclosure Office according to article 17 (3^{bis}) SESTO-FINMA, it would be eligible to notify the shareholdings on a segregated basis. If the respective conditions were not met, a consolidated disclosure of the group would be necessary. The new article 21 (2) (f) SESTO-FINMA intends to make sure that it is apparent from the notification whether the foreign collective investment scheme which is not authorised for public distribution in Switzerland discloses on a segregated or consolidated basis.

4) Procedural Amendments

Finally, the proposed draft includes some procedural amendments to the SESTO-FINMA, including the following:

Notice period for changes of the notified information (article 21 (4) and article 22 (1)): The current article 21 (4) on the notification period for changes of the notified information will be deleted as in practice the notification of an amendment follows the "normal" notification periods according to article 22. This will be clarified by an explicit statement in article 22 (1).

Clearly represented table of the different notifications of a company on the electronic disclosure platform (article 23 (1)): This will include a general overview showing the actual shareholdings of all investors (transparent and actual presentation of the "important shareholders").

Procedures in Disclosure Matters (article 26 (6) and (7)): The current article 26 (6) sets forth that the applicant may substantiate the refusal of a recommendation within five trading days with a written submission to the SIX Disclosure Office. The SIX Disclosure Office can extend such term. With the refusal of a recommendation the authority on the proceeding shifts to the FINMA (article 26 (4) (b)). Therefore, the proposed draft stipulates that a potential refusal of a recommendation will be declared vis-à-vis FINMA and that FINMA may decide on a potential request to extend the term. Further, the proposed new article 26 (6) will state that the refusal of the recommendation needs to be declared in all cases within five trading days and that only the term to substantiate the refusal may be extended by FINMA. Article 26 (7) will set forth that—separately from article 26 (6) as it also applies to other cases than the refusal of the recommendation—the files be provided to FINMA. In addition, it includes the legal basis for the further proceeding.

5) Enactment and Transitional Regime

The new provisions will enter into force on a specific date which is not yet determined (possibly beginning of 2012). The revised article 11 and the new articles 22, 23 and 26 SESTO-FINMA will become effective immediately upon the entering into force of the revised provisions. The new article 17 (3) and (3^{bis}) (and therefore also article 21 (2) (f) SESTO-FINMA will become effective subject to a transitional regime.

Petra Ginter (Petra.Ginter@nkf.ch)

Revision of the Swiss Collective Investment Schemes Act–Initiation of the Consultation Procedure

Reference: CapLaw-2011-33

On behalf of the Federal Council, the Department of Finance has initiated the consultation procedure on 6 July 2011 for the revision of the Collective Investment Schemes Act (CISA). The enactment of the bill would increase the regulatory density for the Swiss funds industry, particularly by submitting asset managers of foreign collective investment schemes (CIS) to mandatory prudential supervision and by tightening custody and distribution provisions.

By Christian Koller / Christin Krüger

1) Background

According to the *Explanatory Report on the Bill regarding the Revision of the Federal Act on Collective Investment Schemes* of 6 July 2011 issued by the Finance Department (Explanatory Report), existing regulatory gaps, harmonization with international standards and international legal developments necessitate the CISA and the Collective Investment Schemes Ordinance (CISO) to be amended. In fact, the EU Directive 2009/65/EC relating to Undertakings for Collective Investments in Transferable Securities (UCITS-D) and the EU Directive on Alternative Investment Fund Managers (AIFM-D) require the Swiss legislator to make legislation compatible with international requirements.

This particularly holds true with regards to the AIFM-D which entered into force this June and shall be transported into the national laws of the EU Member States by 2013. Alternative investment funds (AIF) are considered investment undertakings for which authorization under the UCITS-D is not required, including, amongst others private equity, real estate and hedge funds (Directive 2011/61/EU, OJ L 174, 1.7.2011, p. 1 and 5). The general scope of the AIFM-D is to regulate AIF-managers (AIFM) that are domiciled in the EU, manage AIF registered in the EU or market them in the EU (not covering reverse solicitation, though). The marketing of AIF to retail investors (as opposed to professional investors) is outside the Directive's basic scope. Under the AIFM-D's passporting regime, AIFM will need to apply for an authorization to be issued by the supervisory authorities of the relevant EU Member State; once granted, it will be valid for all EU Member States. The Directive contains operating conditions, transparency requirements as well as rules regarding the management of leveraged AIF and the acquisition of control of non-listed companies by AIF. It also addresses the role and obligations of custodians and limits delegation of AIFM functions to third parties.

In order to allow Swiss AIFM to manage EU AIF or market AIF in the EU, they will need to be regulated by the Swiss Financial Market Supervisory Authority (FINMA) upon the AIFM-D entering into force in 2013. In March 2011, the Federal Council therefore instructed the Department of Finance to prepare a draft for amending the CISA which shall particularly ensure access of Swiss AIFM to the EU funds market. According to the Federal Council, the revised CISA should also provide for greater investor protection and improved asset management quality in Switzerland (cf. media release of the Federal Department of Finance of 11 March 2011).

The Finance Department took this opportunity to propose rather substantial amendments to the CISA. Without claiming to be complete, the following shall highlight some major innovations:

2) Major Innovations

a) Asset Management

At present, managers of Swiss CIS need an authorization from FINMA to carry out their business (article 13 (2) (f) CISA). Managers of foreign CIS are granted the option to become FINMA supervised if specific restrictive prerequisites are met (article 13 (4) CISA). In response to the AIFM-D, the bill regarding the revision of the CISA (Bill or b-CISA) introduces a general authorization and supervision requirement for asset managers of (Swiss and) foreign CIS (article 2 (1) (a) and (b) b-CISA). Note that the AIFM-D provides for a *regime light* with regards to AIFM managing one or several AIF with (i) total assets not exceeding EUR 100 million or (ii) total assets not exceeding EUR 500 million. The latter must not be leveraged and have no redemption rights exercisable during a period of five years following the date of the initial investment in each AIF. These "small" AIFM must basically register with the competent authorities of the relevant EU Member State and provide them with limited information such as their investment strategy, mainly traded instruments and principal exposures which should help the authorities to monitor systemic risks. Otherwise, they do not have to comply with the directive. The EU Member States are however allowed to impose stricter rules.

In contrast, the Bill does not differentiate between small and large AIFM. Furthermore, Swiss asset managers of foreign CIS shall be subject to authorization and prudential supervision even if there is no relation to the EU at all (*i.e.* if the foreign CIS is neither registered nor intended for marketing in the EU) and access of Swiss asset managers to the EU market is thus not at stake. The lack of differentiation should "exclude the danger" of foreign fund managers, who are not willing to be prudentially supervised, to relocate to Switzerland (Explanatory Report, p. 8); further, such regulation would adopt the recommendations promulgated by the International Organization of Securities Commissions (Explanatory Report, p. 14). The Bill measuring all Swiss asset managers of foreign collective investment schemes by the same yardstick is in our view not fully convincing. For the further course of the consultation procedure we therefore expect that more flexible approaches for asset managers of foreign CIS, which are not required to be prudentially supervised under foreign law, will be put up for discussion.

The new article 18a b-CISA defines the tasks of an asset manager (portfolio and/or risk management) and limits the scope of services which may additionally be performed. Delegation of such tasks shall be permissible if appropriate and to qualified service providers only (article 18b (1) and (2) b-CISA). Investment decisions may only be delegated to institutions that are subject to prudential supervision and—in view of a delegation abroad—if FINMA and the relevant foreign supervisory authority/ies have entered into cooperation and exchange of information agreements (article 18 (b) (3) b-CISA).

b) Custody

To date, CISA requires closed-ended CIS to appoint a custodian and a paying agent (article 102 (1) (j) CISA) which are—unlike custodian banks pursuant to the Banking Act—not subject to prudential supervision. The Bill now obliges closed-ended investment companies with fixed capital (SICAF) to appoint custodian banks, too (article 114 b-CISA). This duty shall however not apply to limited partnerships for collective investments, the second type of closed-ended CIS, as they exclusively address qualified investors (Explanatory Report, p. 11). Investment companies with variable capital (SICAV) shall on the contrary be entitled to request an exemption from the general duty of open-ended CIS to appoint a custodian bank if certain prerequisites, such as their limitation to qualified investors, are fulfilled (article 44a (2) b-CISA).

According to article 72 (1) b-CISA, custodian banks will have to implement *appropriate organizational structures* regarding their custody activities; the Bill authorizes the Federal Council to stipulate additional requirements (article 73 (1) and (4) b-CISA), allowing flexible adaptions to the “constantly evolving international standards” (Explanatory Report, p. 12). In addition, the Bill tightens the liability of custodian banks delegating their tasks to third parties and allows delegation of safekeeping functions to prudentially supervised depositaries only.

c) Distribution

i. New Rules regarding Representatives of Foreign CIS

To date, foreign CIS publicly distributed in or from Switzerland must appoint a Swiss representative. Since the distribution to qualified investors is not deemed public, foreign CIS exclusively directed at such investors are not regulated (article 120 (1) and article 3 CISA). Pursuant to the Bill, foreign CIS will always be obliged to appoint a Swiss representative (article 123 (1) (b) b-CISA) so that also qualified investors may rely on a point of contact in Switzerland (Explanatory Report, p. 29). The Bill further obliges a representative to ensure that a foreign fund’s asset management and custody correspond to the provisions of the CISA in terms of organization and investor rights (article 124 (3) (a) b-CISA). This would justify the investment scheme’s relevant documents not being subject to authorization as it is the case for CIS addressing non-qualified investors (article 120 (1) CISA; Explanatory Report, p. 13). However, since such strict requirements may materially impede the distribution of various foreign products that are currently distributed to qualified investors, we expect this proposed new provision to provoke opposition from the funds industry.

ii. New Concept for Distribution

There are several CISA-related registration and authorization duties linked to the *public* marketing of financial products in Switzerland. Notably, the public offering and distribution of units of CIS is subject to authorization, a foreign fund publicly marketed in Switzerland needs FINMA approval, and persons publicly promoting domestic or foreign collective investment schemes are required to obtain the respective permissions; furthermore, the CISA governs the public offering of structured products and prohibits public advertising in respect of in-house funds of banks and securities dealers.

Based on article 3 (1) CISA stating that advertising is not deemed public if limited to qualified investors, FINMA has considered advertising to be public if addressed to non-qualified investors. The Swiss Supreme Court, however, rejected such restrictive view in its decision 2C_89/2010, 2C_106/2010 of 10 February 2011. It stated that contrary to FINMA's perception public advertising for collective investment schemes is not to be assumed simply because fund units are marketed to non-qualified private investors; instead, advertising to the public would require that more than only a closely circumscribed group of investors is addressed.

FINMA's interpretation of the term *public* reflected its desire for a clearer differentiation between qualified and non-qualified investors. In view of the Supreme Court's decision, however, the terms *public advertising* and *public* prove to be ill suited with regards to the segmentation of investors. Accordingly, the Bill proposes to eliminate the concept of *public advertising* and replaces it with the concept of *distribution* which includes all offering of and advertising for a CIS, regardless of it being public or private (article 3 b-CISA). The specific provisions of the revised CISA would thus directly distinguish between qualified and non-qualified investors, setting different standards for investor information and protection in view of *distribution*. This would result in a segmentation of investors as envisaged by FINMA under the existing law.

In this context, note that the Bill remains yet unclear as to which exact activities will be considered *distribution,* especially in view of advisory or discretionary asset management services. Further, every distribution of CIS shall require authorization regardless of whether qualified or non-qualified investors are addressed (article 13 (1) b-CISA). We assume that the authorization as a representative of a foreign CIS will continue to include a distribution license (article 8 (3) CISO).

iii. Changed Definition of Qualified Investors

According to the Bill, an individual holding financial assets of less than CHF 2 million shall no longer be deemed a qualified investor due to a discretionary asset management agreement with a supervised financial institution or an independent asset manager which is a member of a FINMA approved industry organization. As the current provision (article 10 (3) (f) CISA) does not comply with international standards, its deletion aims to consistently distinguish between retail and qualified investors (Explanatory Report, p. 18). The proposed change will influence the regulatory concept of independent asset managers since they will assumedly (except for anti-money laundering purposes) no longer be obliged to affiliate with a FINMA-approved industry organization to "convert" their non high net-worth individuals into qualified investors. On the other hand, one could speculate that *distribution* according to article 3 b-CISA also includes the acquisition of fund units based on discretionary asset management agreements which would factually require independent asset managers to apply for authorization and submit themselves to prudential supervision (article 13 (1) b-CISA/article 14 CISA). In our view, such extensive and very general regulation of independent asset managers would however contradict FINMA's deliberations published in its discussion paper on the *Regulation of the production and distribution of financial products to retail clients—status, shortcomings and courses of action* of October 2010 where more flexible approaches were proposed.

Considering that high net-worth individuals are not necessarily sufficiently knowledgeable in financial matters, the Bill authorizes the Federal Council to postulate additional conditions for the suitability of persons who, in accordance to the CISA, are deemed qualified investors (article 10 (4) b-CISA).

3) Process and Timing

The consultation regarding the revision of the CISA is open until 7 October 2011. The legislative process shall be terminated by mid-2012. Subsequently, market participants will be given relatively short adjustment periods in order to become compliant with the new law.

The revision project has a comprehensive scope and would significantly increase the regulatory density for specific members of the funds industry. Some of the proposed amendments are clearly necessary in order to assure continuing international market access for Swiss players. On the other hand, the adequacy and the commensurability of various proposals seem questionable.

Christian Koller (chkoller@gloor-sieger.ch)
Christin Krüger (ckrueger@gloor-sieger.ch)

Federal Supreme Court (Criminal Division) Judges on the Question Whether a Distributor Must Pass on Distribution Fees to its Client (judgment 6B_223/2010)

Reference: CapLaw-2011-34

Whether distribution fees for the distribution of structured products (or of funds) belong to the distributing custodian bank or whether they are to be treated like retrocessions and must, in principle, be passed on by the custodian bank to its client has been highly controversial after the Federal Supreme Court (FSC) judgment 132 III 460. It was the criminal division of the FSC that now—as a preliminary civil law question to its judgment of 13 January 2011—decided that distribution fees belong to the custodian bank and not to its client. This article points out the remarkable facts that the criminal division of the FSC supports its considerations only by reference to one single article and that it is uncertain or at least unknown to the public whether the FSC consulted its civil law divisions before rendering its decision on the controversial preliminary civil law issue.

By Peter Ch. Hsu / Andrea Boog

1) Summary

The criminal division of the Federal Supreme Court (FSC) in its decision of 13 January 2011 (Federal Supreme Court, judgment 6B_223/2010, dated 13 January 2011) held that distribution fees paid by an issuer of structured products (or by a fund management company as the case may be) to a custodian bank acting as a distributor of structured products (or of funds respectively) are being paid for the (distribution) services in relation to these financial products rendered to the issuer of the structured products (or the fund management company respectively). Conversely, it considered that they are not being paid on the ground of (or in any legally relevant connection with) a contractual relationship between the client and its custodian bank. It argued that distribution fees must be distinguished from retrocessions and came to the conclusion that in contrast to retrocessions which according to FSC judgment 132 III 460, in principle, must be passed on to the client unless a valid waiver has been obtained from the client, distribution fees need not be passed on by the custodian bank to its client on the basis of the contractual relationship with the client. Accordingly, it found that such distribution fees belong to the custodian bank and not to its client.

In its decision, the FSC's criminal division had to decide on the criminal matter whether the accused was guilty of criminal mismanagement in the meaning of art. 158 Penal Code (PC). However, as a preliminary question it had to decide on the private law issue whether distribution fees belong to the distributor (that at the same time acts as custodian bank of the client) or whether they must be passed on by the custodian bank to the client. This question has been highly controversial after the FSC judgment 132 III 460. One might speculate whether the criminal division of the FSC was fully aware of the importance of its decision on this point—this will probably remain unknown to the public.

In a brief analysis of the civil procedure aspects, we explore the consultation requirements between the various divisions of the FSC, in particular between the criminal division and the civil law divisions. Furthermore, we discuss whether a precedent decided by the criminal division of the FSC as a preliminary civil law question in the course of a proceeding on a criminal matter is binding for the civil law (and other) divisions of the FSC and/or courts at lower levels.

2) Summary of the Facts of the Case

The facts of the case may be summarized as follows: The employee X of the custodian bank Y had, without authorization by the custodian bank Y and for the purpose of personal enrichment, instructed issuers of structured products to pay the "arranger fees" or commission payments (*i.e.* distribution fees) paid for the placement of their structured products with investors (*i.e.* customers of the custodian bank Y) to his own accounts instead of having them paid to the custodian bank Y.

3) Distribution Fees Belong to the Distributor Not to its Client

Under art. 158 section 1 PC *"[a]ny person who by law, an official order, legal transaction or authorization granted to him, has been entrusted with the management of the property of another or the supervision of such management, and in the course of and in breach of his duties causes or permits that other person to sustain financial loss shall be liable […]"* for criminal mismanagement. The delinquent must violate the property interests of the principal. In the present case, the FSC had thus *inter alia* to assess whether bank Y or its clients have sustained a financial loss (*i.e.* have been directly damaged). Accordingly, the criminal division of the FSC had to decide as a preliminary question under civil law whether the distribution fees belong a) to the bank Y or b) to the clients of the custodian bank Y.

Pursuant to the decision of the lower court, the provision on criminal mismanagement (art. 158 section 1 PC) was not fulfilled based on the argument that the distribution fees did not belong to the custodian bank Y (but instead to the clients of the custodian bank Y) and therefore the custodian bank Y's property interests were not violated—as the lower court found that only the client was directly damaged, it considered that the elements of misappropriation (art. 138 PC) rather than criminal mismanagement should have been investigated (in our view, it is doubtful whether commissions are "entrusted" to the recipient in the meaning of the criminal provision and therefore whether (wrongly) failing to pass on commissions potentially fulfils the offence of misappropriation in the meaning of art. 138 PC; see Peter Ch. Hsu, Retrozessionen, Provisionen und Finder's Fees, Basle/Geneva/Munich 2006 [=ZSR Beiheft 45], p. 44 et seq.;

Peter Ch. Hsu, Finder's Fee, Commissions and Similar Arrangements, in: Eric Stupp/Nedim Peter Vogt (eds.), Swiss Banking & Private Wealth Management, Vol. 1, Basle/Geneva/Munich 2007, p. 42 et seq.). The FSC overruled this decision of the lower court. It held that as the distribution fees belong to the custodian bank Y, the employee X violated his fiduciary duties as an employee and violated the property interest of the principal (*i.e.* the custodian bank Y).

The FSC considered that the arranger or distribution fees paid by the issuer of structured products to the custodian bank of the client that acts as a distributor for the distribution of the financial products are being paid for the distribution of the financial products. The FSC further reasoned that there was no legally relevant connection between the mandate of the client to purchase structured products and the distribution fees received by its custodian bank. The FSC pointed out that this was the decisive difference between a) distribution fees received by a distributor (even if it also acts as custodian bank) and b) retrocessions received by an independent asset manager from the banks. As a result of these considerations, the FSC found that the custodian bank Y received the distribution fees not on the basis of (or in any legally relevant connection with) its contractual relationship with the client (*i.e.* the mandate between the customer and the custodian bank) but for the (distribution) services connected with the structured products and rendered to the issuer of these products. For these reasons, the FSC concluded that the distribution fees received by the custodian bank in connection with the placement of the structured products (or placement of funds) belong to the custodian bank Y. Consequently, the distribution fees are in the view of the FSC not within the scope of the precedence on retrocessions of FSC judgment 132 III 460.

The FSC makes reference to several authors in support of its consideration that FSC judgment 132 III 460 referred to the obligation of an independent external asset manager to pass on the received retrocessions to its customer. However, this question has not been controversial. In contrast, the FSC supports its considerations on the decision that distribution fees are to be treated differently from retrocessions only by reference to one single article of Raphael Jäger/Thomas Hautle (Retrozessionen vs. Bestandespflegekommissionen im Vermögensverwaltungsgeschäft, Anwaltsrevue 2008, p. 438 et seqq.). This is surprising as the question whether distribution fees shall be treated similarly to retrocessions and thus be subject to the obligation to pass them on to the client (*i.e.* principal) has been controversial in Swiss legal literature: Several Swiss legal authors pointed out that it is necessary to distinguish between retrocessions and distribution fees (see Sandro Abegglen, Retrozession ist nicht gleich Retrozession: Zur Anwendbarkeit von Art. 400 Abs. 1 OR auf Entschädigungen, die an Banken geleistet werden, insbesondere im Fondsvertrieb, SZW 2007, p. 122 et seqq., 128 et seqq.; Thomas Jutzi, Der öffentliche Vertrieb von kollektiven Kapitalanlagen—Illustration am Beispiel des vertraglichen Anlagefonds, recht 2011, p. 60 et seqq., 75; Philippe Meyer, Retrozessionen, Finder's Fees und Vertriebsentschädigungen im Schweizerischen

Bankgeschäft—Status aus zivilrechtlicher und aufsichtsrechtlicher Optik 5 Jahre nach BGE 132 III 460, SZW 2011, p. 184 et seqq., 188; Peter Nobel/Isabel Stirnimann, Zur Behandlung von Entschädigungen im Vertrieb von Anlagefonds und strukturierten Produkten durch Banken, SZW 2007, p. 343 et seqq., 348; Raphael Preisig, Der Vertrieb von Anlagefonds durch Banken, Diss. Zurich 2010, p. 159 et seq.; Simon Schären, Retrozessionskontroverse—Bringt das Handelsgericht Zürich Licht in die Sache?, Jusletter dated 20 October 2008, p. 4). One of their key arguments is that the distribution services of a distributor of financial products would remain uncompensated if he had to pass on the distribution fees to the client since the fees obtained from the client for the services rendered to the client would not compensate these distribution services (see the communication of the Swiss Funds Association SFA to its members including a list of services provided by the distributors of funds, communication no. 22/06 dated 5 December 2006, p. 3). Several other authors suggest that distribution fees paid by the issuers of structured products or fund management companies shall be treated similarly to retrocessions (see Susan Emmenegger, Anlagekosten: Retrozessionen im Lichte der bundesgerichtlichen Rechtsprechung, in: Susan Emmenegger (ed.), Anlagerecht, Basle 2007, p. 59 et seqq., 79; Christoph Peter Gutzwiller, Rechtsfragen der Vermögensverwaltung, Zurich 2008, p. 205 et seqq.; Monika Roth, Das Dreiecksverhältnis Kunde—Bank—Vermögensverwalter, Zürich 2007, p. 62 et seqq.; Fabian Schmid, Retrozessionen und Anlagefonds, Zur Problematik der Retrozessionen im Anlagefondsgeschäft nach dem Grundsatzentscheid des Bundesgerichts und dem Inkrafttreten des Kollektivanlagegesetzes, Jusletter dated 21 May 2007, p. 14 et seqq.). In light of the lack of such references in the reasons of the FSC's decision, one may dare to call into question whether the FSC was fully aware of the existing controversy in literature and the importance the civil law matter it had to decide as a preliminary question to the judgment has for the financial industry. It would certainly have provided more comfort if the FSC had supported its reasoning with a more detailed analysis and further references.

Another open question is whether or not the criminal division of the FSC consulted the civil law divisions of the FSC before it decided on the preliminary civil law question. It is in this context of interest to examine whether and to what degree a decision of the criminal division of the FSC on a preliminary civil law question is binding for the civil law (and other) divisions of the FSC and/or any court at lower level.

4) Precedent on Civil Law Issue Established by Unilateral Decision of the FSC's Criminal Division on a Preliminary Question

Pursuant to the wording art. 23 section 2 of the Federal Supreme Court Act (FSCA), a division of the FSC having to decide on a question of law that concerns more than one division seeks the consent of the assembly of all divisions affected, if it considers this appropriate with view to the development of law or the unity of jurisdiction.

That the consent of other divisions be obtained is not an individual right of the parties, but is basically left to the discretion of the competent division of the FSC (Hansjörg Seiler/Nicolas von Werdt/Andreas Güngerich, Bundesgerichtsgesetz (BGG), Berne 2007, N 12 to Art. 23; Martin Beyeler, Angebot oder Nichtangebot? Anmerkungen zu BGr. 2D_64/2008, recht 2009, p. 34 et seqq., 40; cf., however, the interesting discussion of Giovanni Biaggini/Stephan Haag, in: BSK BGG, Basle 2008, N 25-29 to Art. 23, about whether the purpose of art. 23 section 2 FSCA would actually prohibit a fully discretionary decision of the FSC division concerned). Even though a previous consultation according to art. 23 section 2 FSCA seems thus not mandatory (let alone enforceable), it would in the case at hand with view to the far-reaching implications of this precedent have been desirable if the criminal division of the FSC had consulted the civil law divisions before taking its decision on the preliminary private law question. The actual purpose of art. 23 section 2 FSCA is not only or primarily the development of judicial law or the unity of jurisdiction, but this provision also aims to achieve or secure a certain stability and continuity of judicial law. It constitutes a preventative mean to avoid contradictory judgments and a frequent change of the FSC's jurisdiction respectively. It should not be left on chance which division of the FSC enjoys the privilege to establish a precedent which will limit the freedom of decision of other divisions being faced with the same legal issue at a later point in time (Giovanni Biaggini/Stephan Haag, l.c., N 23, 26 to Art. 23; cf. also FSC judgment 126 I 81 D. 2c p. 84 under the former law).

Admittedly, the judgment remains silent on the question whether the criminal division actually consulted the civil law divisions of the FSC. In previous judgments, however, the FSC used to explicitly point out if the consent of other divisions was obtained, which at least suggests that this was not the case in respect of the judgment at hand (*cf. e.g.* FSC judgment 137 III 47 D. 1.2.3. p. 48; FSC judgment 136 V 7 D. 2.2.2.2. p. 14; FSC judgment 135 V 124 D. 4.3.3. p. 133).

Notwithstanding the above, *i.e.* the manifest circumstance that the criminal division failed to consult the civil law divisions of the FSC before rendering its decision of 13 January 2011, the precedent established by the FSC's criminal division on the preliminary question under civil law will be binding for the civil law (and other) divisions of the FSC for the following reasons:

Pursuant to art. 23 section 1 FSCA, a division of the FSC may only deviate from a previous decision of one or several other divisions if the assembly of all affected divisions gives its respective consent. This procedure is—in contrast to the one stated in section 2 of art. 23 FSCA—mandatory, and it is in the terms of art. 23 section 1 sufficient in order to commit a "modification of practice", if a division of the FSC intends to deviate from one single precedent ruling over the identical question of law. However, the notion of the "modification of practice" has to be held apart from a sole clarification or further development of existing jurisprudence, which do not fall within the scope of art. 23

section 1 FSCA. The wording of art. 23 section 1 FSCA does not provide, and the purpose of the provision does not allow, for any distinction between decisions on preliminary and principal questions, as long as the preliminary decision was still relevant for the outcome of the judgment and constituted a so called *ratio decidendi* (Giovanni Biaggini/Stephan Haag, l.c., N 6, 8-10 to Art. 23; Hansjörg Seiler/Nicolas von Werdt/Andreas Güngerich, l.c., N 3, 6 to Art. 23; Hans Dubs, Richterrecht und Rechtssicherheit, in: SJZ 1991, p. 293 et seqq., p. 295; see also Jean-François Poudret, l.c., N 3 to Art. 16, referring to the former law; cf. also FSC judgment 90 II 274 D. 5 p. 281 and FSC judgment 96 I 425 D. 1b p. 428, both relating to the former law).

This means that the civil law (and other) divisions will basically be bound by the criminal division's preliminary decision on the private law issue and must not deviate from it unless the conditions of art. 23 section 1 FSCA are met. Although another division of the FSC would thus be required to follow the procedure under this provision if it subsequently intended to modify the practice, it can, as a matter of fact, not be ruled out that such division of the FSC simply disregards the criminal division's precedent and deviates from it without respecting the formal requirements of art. 23 section 1 FSCA. The FSCA does not sanction such unjustified deviation from a precedent (in particular, such deviation does not give reason for a revision of the decision; cf. Giovanni Biaggini/Stephan Haag, l.c., N 38 to Art. 23; Hansjörg Seiler/Nicolas von Werdt/Andreas Güngerich, l.c., N 11 to Art. 23; Jean-François Poudret, l.c., N 6 to Art. 16, referring to the former law). As regards lower civil courts, they are not legally bound by precedents of higher courts—not even of the FSC (FSC judgment 71 I 225 D. 2 p. 229). As a matter of fact, however, lower courts usually follow the FSC's jurisdiction (Hans Dubs, l.c., p. 295; Fabienne Hohl, Procédure civile, Tome II, Berne 2010, § 1 N 16; Karl Spühler/Annette Dolge/Myriam Gehri, Schweizerisches Zivilprozessrecht und Grundzüge des internationalen Zivilprozessrechts, Berne 2010, § 13 N 18).

5) Conclusion

To conclude, it may be held that the criminal division with its judgment of 13 January 2011 established a precedent which constitutes for the time being the FSC's jurisdiction in respect of a controversially discussed question which has now been answered: Distribution fees must be distinguished from retrocessions and must not be passed on by the custodian bank to its client. It will be interesting to see whether the civil courts will follow the precedent or whether they will further concretize it, *e.g.,* by considering various types of bank-client relationships.

Summary overview of the court practice regarding retrocessions and distribution fees:	
1.	**Decision of the Federal Supreme Court dated 23 May 2005 (FSC judgment 132 III 460):** The Federal Supreme Court decided that the external asset manager must disclose and pass the received retrocessions on to the client. The client may waive the right to remittance of the retrocessions (even in advance). However, the client must be fully and truthfully informed of the expected amount of retrocessions and the client's intent to waive must be clear and unambiguous. **Conclusion: In general, retrocessions must be passed on to the client. However, a duly informed client may validly waive the right to such remittance even in advance.**
2.	**Decision of the Commercial Court of Zurich dated 26 June 2007 (HG050118/U/ei):** The court followed the judgment of the Federal Supreme Court: The client must be informed fully and truthfully. The client must be in a position to at least estimate the amount of the retrocession or have certain indications about the expected retrocession. **Conclusion: The Commercial Court of Zurich follows the Federal Supreme Court judgment 132 III 460.**
3.	**Decision of the District Court of Zurich dated 26 August 2009 (CG080108/U):** The court decided that distribution fees for the distribution of funds must not be passed on to the clients on the basis of art. 400 para. 1 of the Code of Obligations (CO). The decision is apparently on appeal. **Conclusion: Distribution fees belong to the bank and must not be passed on to the client.**
4.	**Decision of the Federal Supreme Court dated 13 January 2011 (6B_223/2010):** The Federal Supreme Court (criminal division) decided, in examining a preliminary question under civil law, that distribution fees for the distribution of structured products (or of funds) belong to the (custodian) bank and not to the client of the custodian bank. (See more details in this article.) **Conclusion: Distribution fees belong to the bank and must not be passed on to the client.**
5.	**Decision of the Commercial Court of Zurich dated 19 May 2011 (HG090121-O/U/dz; p. 54 et seq.):** The court decided that the custodian bank must disclose any distribution fees, which the bank has received for the sale of structured products (equity yield notes of a third party), to the client, based on the duty of accountability according to art. 400 CO. The court stated that it does not matter, whether the payments were terminologically recorded as retrocessions or distribution fees, how they are to be legally qualified or whether they are subject to an obligation to deliver them up to the client or not. It was further stated that it was not relevant, whether, at the intention of the third party, they shall exclusively be to the benefit of the mandated party. A mandated party shall, upon request, give account on its management exhaustively and truthfully at any time as the client may only assess in this way whether, and if yes in which amount, he/she may claim a refund. In this case, the court did not assess whether distribution fees obtained for the sale of structured products must be passed on to the client. The decision is apparently on appeal. **Conclusion: A custodian bank must disclose the amount of received distribution fees for the sale of structured products (or of funds). In this decision it was not decided on the question whether distribution fees must be passed on to the client.**

Peter Ch. Hsu (peter.hsu@baerkarrer.ch)
Andrea Boog (andrea.boog@baerkarrer.ch)

CAPLAW

SWISS CAPITAL MARKETS LAW

When Is a Concurrent Tender Offer a Competing Tender Offer?

Reference: CapLaw-2011-35

In a recent order the Takeover Board had to rule on whether a partial tender offer published within the initial offer period of a tender offer made for all publicly held shares of the same target company constituted a competing offer within the meaning of Swiss takeover regulation. The decision is of particular interest with regard to timing of the offers and possible implications for the success (or failure) of the offers resulting therefrom. The Takeover Board also commented on the initial offeror's allegation that the publication of the partial offer constituted an abuse of rights.

By Thomas U. Reutter / Daniel Raun

1) Facts and Legal Background

On 7 June 2011, HarbourVest Acquisition GmbH (HarbourVest) submitted a public tender offer (Initial Offer) for all publicly held shares (Absolute Shares) of Absolute Private Equity Ltd (Absolute). The initial offer period started on 23 June 2011 and was supposed to end on 20 July 2011. HarbourVest initially offered USD 17.25 in cash per Absolute Share but increased the offer price to USD 18.50 on 14 July 2011. Simultaneously, the initial offer period was extended by one day until 21 July, and again on 19 July until 26 July.

On 20 July 2011, ACP Acquisition GmbH (ACP) announced a partial public tender offer for 19.32%, or 20% after registration with the commercial register of a share cancellation which had previously been resolved by the Absolute shareholders' meeting, of the publicly held Absolute Shares (Second Offer). ACP offered USD 18.60 in cash per Absolute Share. The offer prospectus for the Second Offer was published on 27 July 2011. After publication of the Second Offer, the Takeover Board (TOB) further extended the offer period for the Initial Offer to 3 August.

The success of ACP's slightly higher offer hinged on whether holders of Absolute Shares could tender into the Second Offer before expiry of the Initial Offer. This would be the case if the Second Offer was qualified as a competing offer. Swiss takeover law mandates that the initial offer periods of competing offers end on the same date. This rule is designed to grant the recipients of competing offers the ability to freely choose between offers without any timing constraints. Further, if the offer was qualified as a competing offer, Absolute shareholders that had already tendered their Absolute Shares would have a withdrawal right. It does not come as a surprise, therefore, that ACP alleged that its Second Offer was a competing offer in the sense of Swiss takeover law. It is also not surprising that HarbourVest rejected that argument. Nevertheless, HarbourVest agreed to grant Absolute shareholders who had already tendered their Absolute Shares the right to withdraw all or part of their Absolute Shares from the Initial Offer before the end of the initial offer period.

2) Considerations of the Takeover Board

Against that background the TOB had to rule on whether ACP's slightly higher Second Offer was indeed a competing offer even though it was only a partial tender offer for 20% of the Absolute Shares. A level playing field is only provided for competing offers, *i.e.* offers which have the purpose of obtaining control over the target company. Without specifying at what percentage a participation resulting from a public tender offer would constitute control over the target company, the TOB went on to state that whereas HarbourVest in tendering the Initial Offer did in fact seek to acquire a controlling interest in Absolute, ACP did not. Rather, according to the TOB, the purpose of the Second Offer could only be for ACP to be a minority shareholder of Absolute, as the Second Offer merely extended to 20% of the Absolute Shares.

The TOB also took into consideration the fact that the Initial Offer was subject to the condition that until the end of the initial offer period HarbourVest would have received valid acceptances for Absolute Shares representing, when combined with any Absolute Shares held by HarbourVest, at least 50.01% of all Absolute Shares issued. Similarly, the Second Offer was conditional on ACP receiving acceptances for at least 4,358,261 Absolute Shares (equaling half of the Absolute Shares for which the Second Offer was made, *i.e.* 10% of all Absolute Shares issued) by the end of the initial offer period. The TOB concluded that there was the possibility that both offers could be declared successful and that ACP, with respect to its offer and the Initial Offer, was therefore not directly competing with HarbourVest.

3) Considerations of the Takeover Board in Respect of the Validity of the Second Offer

The TOB also commented on HarbourVest's allegation that the Second Offer constituted an abuse of rights. HarbourVest had put forward that both the timing (the Second Offer having been published shortly before the expiration of the initial offer period of the Initial Offer) and the offer price (USD 18.60 in the Second Offer versus USD 18.50 in the Initial Offer, *i.e.* a mere 0.54% difference) were evidence to the fact that ACP's primary intention was to cause confusion among Absolute shareholders and to interfere with the Initial Offer process.

The TOB did not share HarbourVest's reasoning. Without specifically addressing the circumstances of ACP's offer, the TOB contented itself with stating that an offeror generally has the right to publish a partial offer or a competing offer at any time it pleases. In respect of the offer price the TOB pointed out that an offeror is even free to launch a competing offer at a lower price than the price offered in a previously published tender offer. The TOB thus held that the circumstances under which the Second Offer had been published did not constitute an abuse of rights.

Notwithstanding the above view, the TOB ordered the initial offer period of the Second Offer not to start until after the publication of the final interim result of the Initial Offer which suggests that the TOB was not completely unsympathetic to HarbourVest's argument that ACP mainly intended to interfere with the Initial Offer. The TOB based its order on the need of the recipients to have maximum freedom of choice under which offer to tender their Absolute Shares. According to the TOB, this could only be accomplished if the Absolute shareholders knew for certain that the Initial Offer is declared successful.

However, the TOB's argument does not seem to take into account the minimum acceptance threshold of the Initial Offer, *i.e.* the fact that the Initial Offer would only be successful if at least 50.01% of the Absolute Shares were tendered during the initial offer period. Had the majority of Absolute shareholders tried to keep their option to tender under the Second Offer to have actual freedom of choice, this would have resulted in the failure of the Initial Offer and Absolute shareholders would no longer have had the possibility to choose between the two offers. It can be assumed that Absolute shareholders, under these circumstances, opted for the safer option of tendering their Absolute Shares under the Initial Offer instead of running the risk that the Initial Offer is unsuccessful and that they would then only be able to tender a part of their Absolute Shares under the Second Offer. The success rate of the Initial Offer published by HarbourVest on 5 September 2011 of 98.68% supports this assumption.

(TOB Order 477/04 dated 2 August 2011)

Thomas U. Reutter (thomas.reutter@baerkarrer.ch)

Daniel Raun (daniel.raun@baerkarrer.ch)

HarbourVest Acquisition GmbH Announces Final Results of Tender Offer for Absolute Private Equity Ltd

Reference: CapLaw-2011-36

On 5 September 2011, HarbourVest Acquisition GmbH announced the definitive final result of its public tender offer for all publicly held shares in Absolute Private Equity Ltd. Pursuant to the published result, HarbourVest Acquisitoin GmbH held 43,005,846 shares corresponding to 98.68% of the voting rights in Absolute Private Equity Ltd. See also the in-depth article on p. 18 et seqq.

St. Gallen Stock Corporation Law Forum 2011 (St. Galler Aktienrechtsforum 2011)

Friday, 4 November 2011, 09.15 h–17.00 h, Kongresshaus, Zurich

www.eiz.uzh.ch

Capital Market Transactions VII (Kapitalmarkttransaktionen VII)

Wednesday, 23 November 2011, 09.15 h–17.00 h, Kongresshaus, Zurich

www.eiz.uzh.ch

St. Gallen Symposium on Financial Market Regulation (St. Galler Tagung zur Finanzmarktregulierung)

Friday, 2 December 2011, Convention Point, Zurich

www.es.unisg.ch

Developments in Collective Investment Schemes Law VI (Entwicklungen im Recht der kollektiven Kapitalanlagen VI)

Thursday, 8 December 2011, SIX ConventionPoint, Zurich

www.es.unisg.ch