

Regulatory Regime under FINIA

FinControl Informationsveranstaltung (Webinar)

30. November 2021



Timetable

- 10:30 Welcome
- 10:35 Goals of the Workshop
- 10:40 Corporate Governance
- 10:45 Risk Management, Internal Controls and Compliance
- 11:00 Organisational Scenarios
- 11:05 Organisational Hot Topics
- 11:15 End

Welcome



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Marc is the founder of Alithis. He is a Swiss attorney who has over 10 years of experience in the wealth planning, trustee and corporate services business working for independent and bank-owned trustees. As a board member and in-house counsel of different organisations, Marc has also gained relevant experience in the non-profit and sports sector.

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Focus Areas

Financial market regulations (emphasis on trustees and portfolio managers) – AML, FATCA, CRS – Cross border – Governance and outsourcings – Data protection – Internal and regulatory investigations – Contentious trusts and trust litigation – Trusts and other private wealth structures – Foundations, non-profit organisations and social enterprises – Associations and other sports organisations

Goals of this Workshop



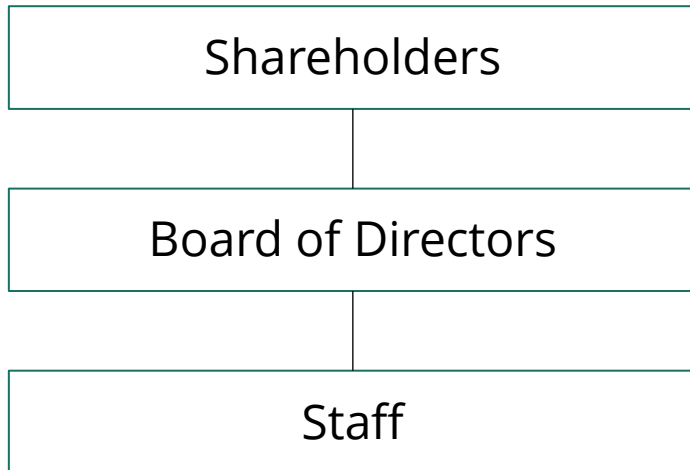
What do we want to achieve today?

- Understand what is expected by the regulator in terms of corporate governance
- Understand what is risk management, internal controls and compliance
- Outline organizational scenarios
- Hot Topics (One-Man Management, Cross Border)

Expectations re Corporate Governance

Default Corporate Setup

Swiss Corporate Law (Company Limited by Shares, “AG”)

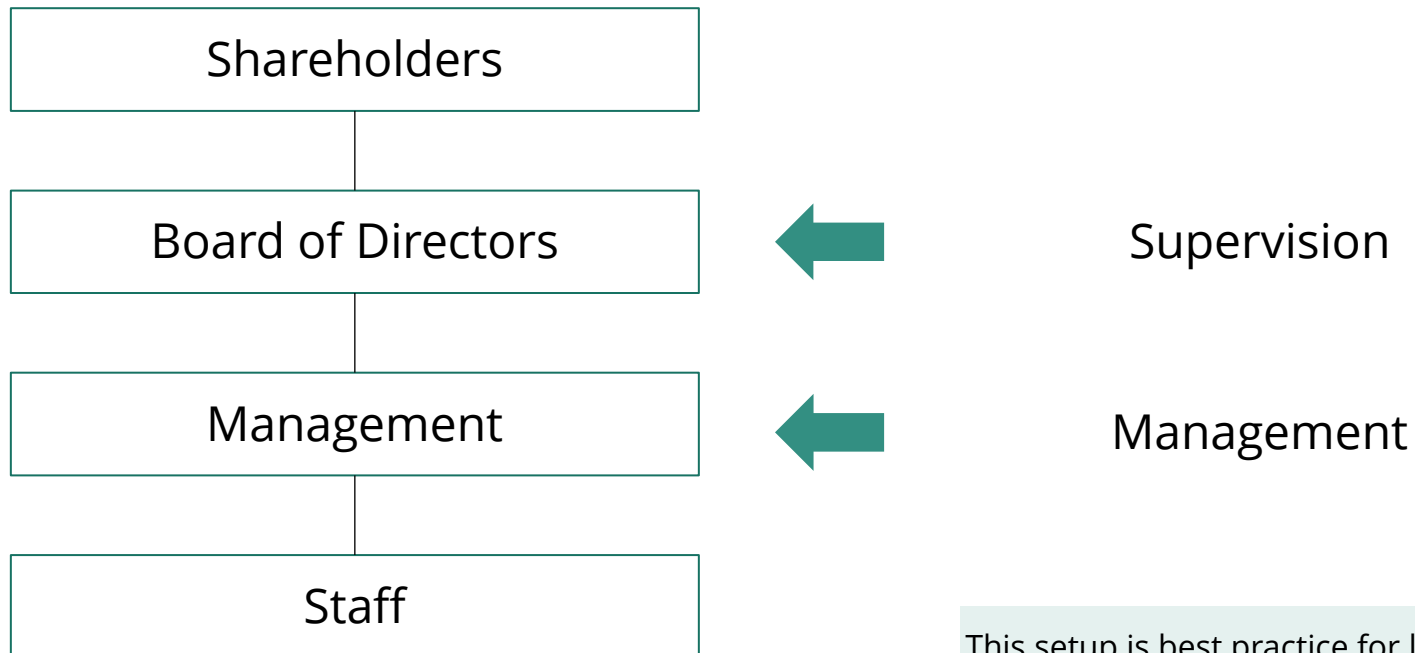


Management + Supervision

- BoD **can** delegate the management to a single person («Geschäftsführer» or «Delegierter»); or
- BoD **can** delegate management to an executive committee («Geschäftsleitung»).
- If it does not do so, it is the BoD is responsible for the management

Corporate Setup – with delegated management responsibility

Swiss Corporate Law, Company Limited by Shares, “AG”)



This setup is best practice for listed and bigger companies

Organisational Expectations of FINIA

1	Supervisory Body	Art. 23 sect. 3 FINIO
2	Management	Art 20 FINIA Art. 25 FINIO
3	Risk Management	Art. 26 sect. 2 FINIO
4	Internal Controls	Art. 26 sect. 2 FINIO
5	Internal Audit	Art. 26 sect. 4 FINIO

Management (“Geschäftsführung”)

(Art 20 FINIA i.V.m. Art. 25 FINIO)

- Generally, **Management** must consist of **two qualified persons**
- **May consist of only one person**, if
 - it is demonstrated that **orderly continuation of business** is guaranteed

(Art. 25 Abs. 4 FINIO)

- Managers must take precautionary measures to **ensure business continuity** in case they are unavailable or passed away.
- If **third parties** are engaged for that purpose
 - Clients must be informed
 - Art. 14 FINIA is to be adhered with

Separate and independent supervisory body (“Aufsichtsorgan”)?

(Art. 23 Abs. 3 FINIO)

- FINMA **can** request the creation of a **supervisory body**
- The **majority** of members of such body are **not part of management**, if
 - **10+ FTE or 5+ mil CHF gross revenue** p.a.; **and**
 - **Type and scope of the business activity** make it necessary

Separate independent risk management and internal control function?

(Art 26 Abs. 2 FINIO)

- **Risk management and internal control functions must NOT be independent from revenue generating activities, if**

- **5 or less FTE or less than 2 mil CHF gross revenue p.a.; and**
- **The business model is without increased risks**

Internal audit

(Art 26 Abs. 4 FINIO)

- FINMA **can** request the creation of an **internal audit function** which is **independent** from the management, if
 - Type and **scope of the business activities** of the portfolio manager or trustee require it
 - The portfolio manager or trustee has a **separate supervisory body** pursuant to Art. 23 Abs. 3 FINIO, **and**
 - an **annual gross revenue of 10+ mil CHF**

Conclusion Corporate Governance



The **board and management** of trustees can consist of **the same persons**



These senior persons are **“multi-hatted”**



Board and management can even consist **of one person only**



EAMs and Trustees which are **not «low risk»** require separate and **independent risk management and internal control functions**



Internal audit is usually **not required.**

What is Risk Management / ICS?



Preliminary remark



FINMA Circular on Corporate Governance provides for the pertinent definitions re risk management and internal controls



The Circular does not apply to Trustees, but the definitions will be relevant nevertheless

Definition of Risk Management



Pursuant to Circular on Corporate Governance, N 3

→ **The highlighted points are addressed through the ICS** (see below)

Definition Risikopolitik and Risk Management Principles

Risikopolitik and Risk Management Principles

The “**Risikopolitik**” and the **Risk Management Principles** govern how substantial risks are dealt with, the risk tolerance and the risk limits that derive from the risk tolerance, in all relevant risk categories

The following aspects need to be considered (applies to the big institutions in category 1-3)

- **Unified categorization of significant risks** to ensure consistency with the risk management targets
- Specification of a **potential loss** arising from risks in these significant risk categories
- Definition and application of the **instruments** as well as the **organizational structures** for the **identification, analysis, assessment, appraisal, management and supervision of the significant risk categories** and the respective reporting
- Design of a **documentation** that allows for an **adequate review** of the risk tolerance as well as the respective risk limits
- Provisions for the **risk data aggregation and reporting**

Pursuant to Circular on Corporate Governance, N 53 to 59

Definition of Internal Control System and Compliance (1/2)

Internal Control System

= The entirety of the **control structures and processes** that form the basis for the **achievement of the business policy objectives** and for the **proper operation of the institute** at all levels.

Includes

- Ex-post controls
- Planning and Steering

Includes, inter alia

- Control activities as part of the daily business procedures (**1st Line of Defense**)
- Adequate risk management and **compliance** procedures
- Control functions (risk-based), in particular independent risk management and **compliance** functions (**2nd Line of Defense**)

Pursuant to Circular on Corporate Governance, N 6 and 7

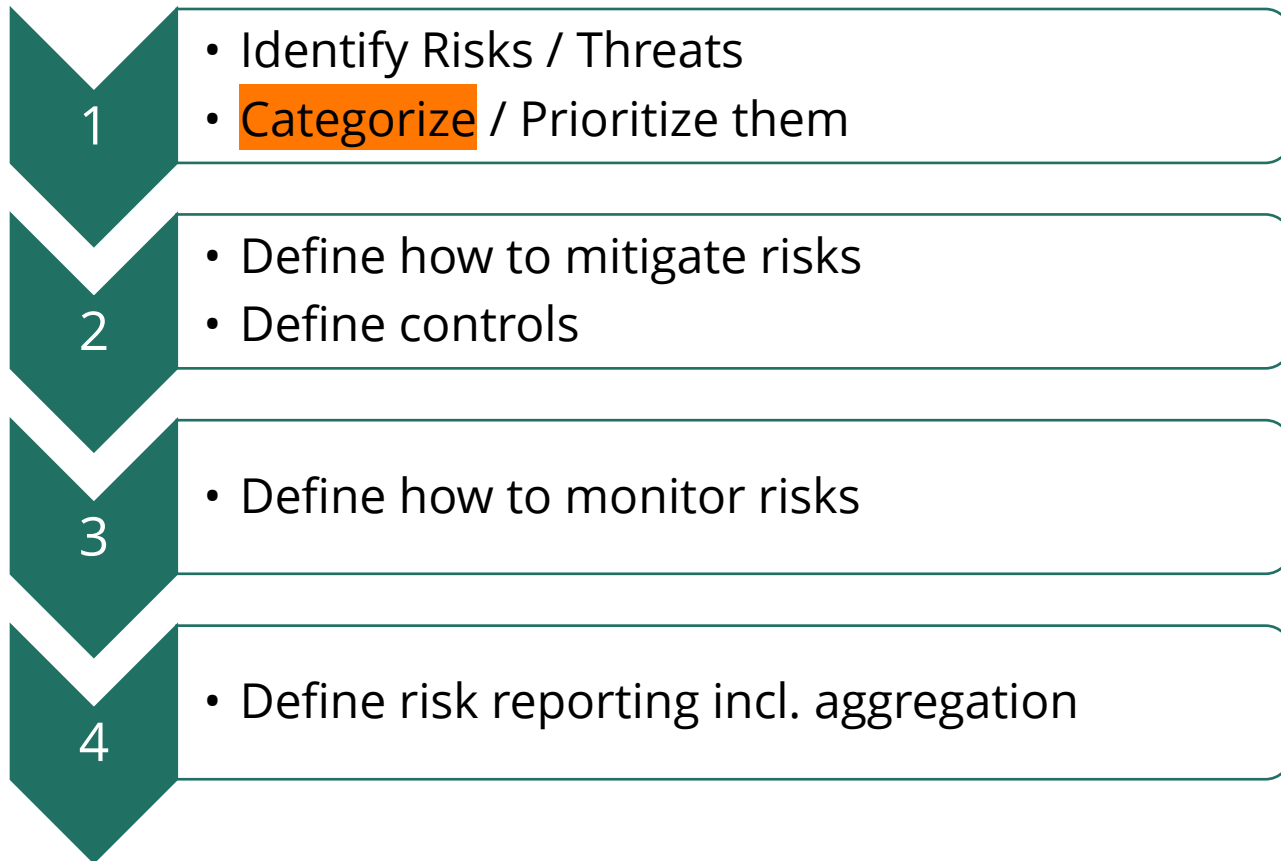
→ **“Compliance Procedures” and “Compliance Functions” are part of the internal control system**

Definition of Internal Control System and Compliance (2/2)

Internal Control System	
As a minimum, there are at least two instances of control	
<p>Business Units (1st Line of Defense)</p> <ul style="list-style-type: none"> Control activities as part of the daily business procedures Management of risks, direct supervision, steering and reporting of risk 	<p>(Independent) control units (2nd Line of Defense)</p> <ul style="list-style-type: none"> Risk control activities ("Risk Control") Control activities re compliance with legal, regulatory and internal provisions ("Compliance") There must not be any financial incentives leading to conflicts of interest Unlimited rights to access and review information Direct access to the Board
<p>Risk Control</p> <ul style="list-style-type: none"> Ensures systematic monitoring and reporting of specific and aggregated risk positions Monitors risk tolerance and risk limits in accordance with the Risikopolitik and the Risk Management Principles Develops and operates risk monitoring systems Is consulted when new products, services, business areas or markets are developed, and in case of significant or complex transactions Actively participates in the process of setting the risk limits, and ensures that the limits are in line with the risk tolerance Reports to management (at least semi-annually) and to the Board (at least annually) how the risk profile of the institution and its activities are developing Ad-hoc reporting to management and internal audit in case of significant incidents 	<p>Compliance</p> <ul style="list-style-type: none"> Annual assessment of the compliance risk of the business activities, development of risk-based activity plan which is to be approved by the management. Activity plan is also to be provided to internal audit. Ad-Hoc reporting in case of significant changes of the compliance risk Annual reporting to the Board regarding (1) assessment of compliance risk and (2) the activities of the compliance function. Copy to be provided to internal and statutory audit Ad-Hoc reporting to the management and the Board in case of serious violations of compliance or incidence of great significance, support of the management in preparing and implementing the appropriate measures. Internal audit to be notified.

Pursuant to Circular on Corporate Governance, N 60 to 81

Preventive Risk Management



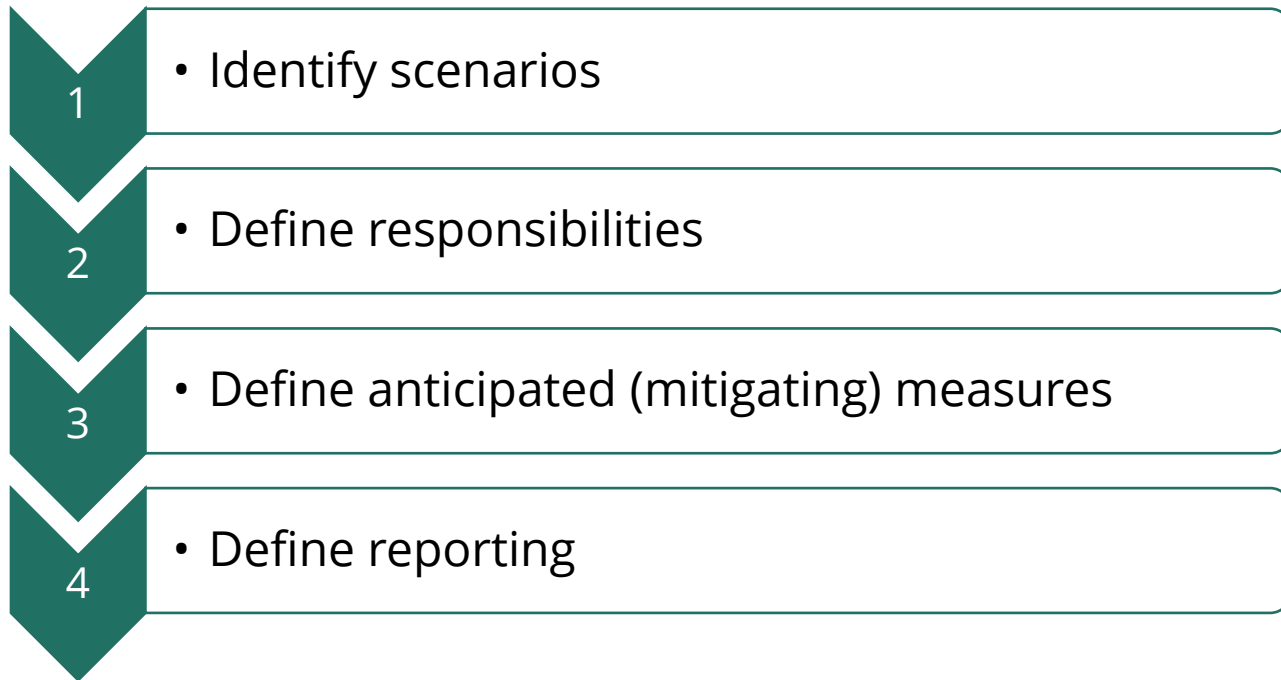
Risk Categories

Collated from FINMA Circulars

- 1 Operational Risk
- 2 ML / TF Risk
- 3 Market Conduct
- 4 Financial Risk
- 5 Reputational Risk
- 6 Strategic Risk

Reactive Risk Management

Handling of Incidents



Risk Management – Management Responsibilities

Risk Management related tasks of the Management

- Operational risk steering, including balance sheet and liquidity management
- Adoption of **policies and procedures** regarding the operative business activities
- Design and maintenance of an appropriate **management information system** and an **internal control system**, as well as a suitable technology infrastructure
- Drafting of the **Risikopolitik** and the **Risk Management Principles**, that are adopted by the Board

Pursuant to Circular on Corporate Governance, N 10 to 14

Risk Management – Board Responsibilities

Risk Strategy Tasks of the Board (“Risikopolitik”)	<ul style="list-style-type: none">• Adopts Guiding Principles re corporate culture• Adopts risk policy (“Risikopolitik”) and the basic principles of risk management for the entire institution (“Risk Management Principles”)• Is responsible for the regulation, implementation and supervision of an effective risk management• Is responsible for the steering of the overall risks
Organisational Tasks of the Board	<ul style="list-style-type: none">• Responsible to implement an appropriate organization• Adopts the necessary regulations / policies
Finance Tasks of the Board	<ul style="list-style-type: none">• Ultimately responsible for the financial state and development of the institution• Approves or adopts the capital and liquidity planning,• Approves the annual report, annual budget, intermediary financial accounts and the annual financial targets
Human and other Resources Tasks of the Board	<ul style="list-style-type: none">• Appropriate infrastructure / IT• Selection and appointment of board committee members, members of management, including the CEO, Chief Risk Officer (CRO) and the Head of Internal Audit (as far as applicable)
Supervision and Control Tasks Board	<ul style="list-style-type: none">• Responsible for suitable risk and control framework within the institution• Ensures an effective internal control system (ICS)• Appoints and supervises internal audit (if applicable)• Appoints the regulatory auditor and assesses their reports

Pursuant to Circular on Corporate Governance, N 10 to 14

Organisational Scenarios

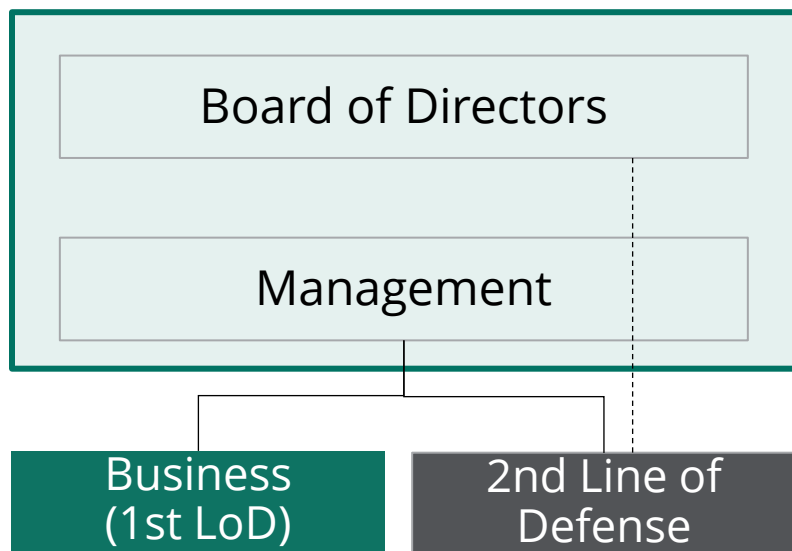
Option 1: Very small and low risk



Very small size and low risk
Less than 5 FTE and 2 mil CHF revenue

- No separation of board from management
- No independent risk management and control functions
- No internal audit

Option 2: Small or increased risk

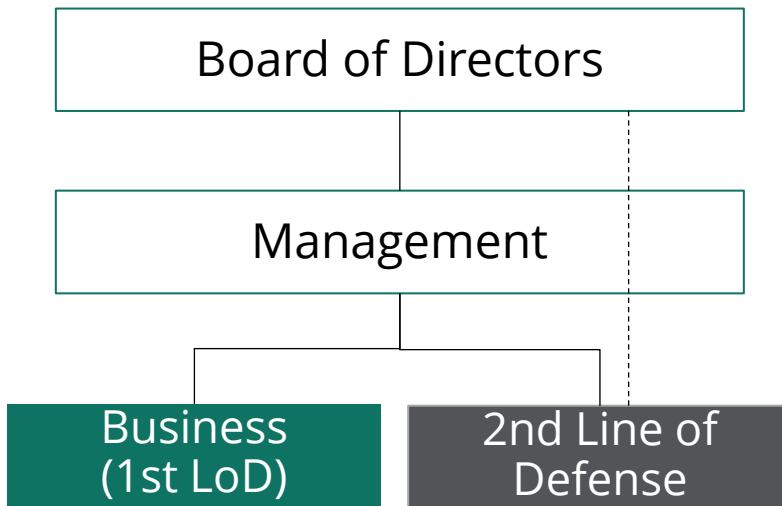


Small size or increased risk

Less than 10 FTE and 5 mil CHF revenue

- No separation of board from management
- independent risk management and control functions required
- No internal audit

Option 3: Medium

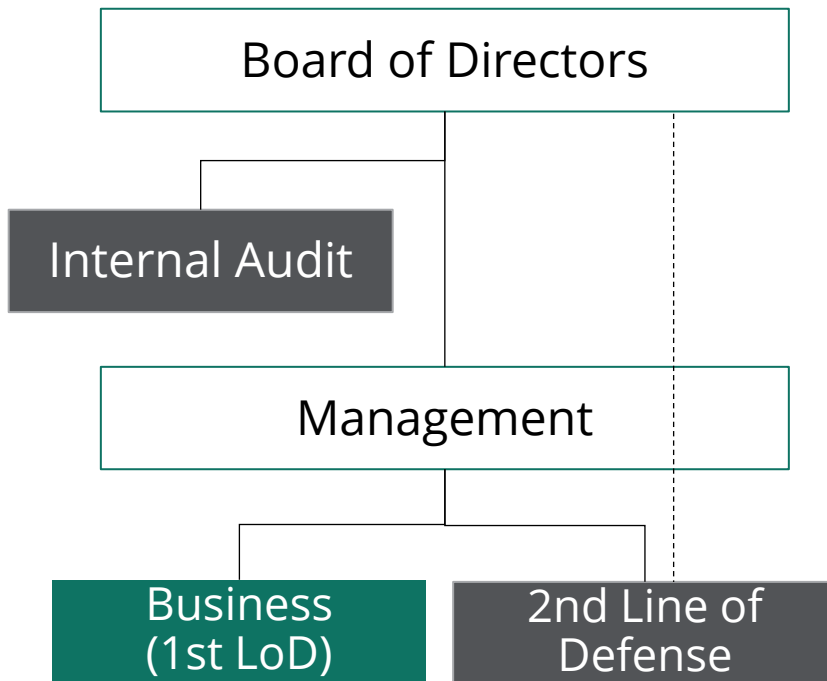


Medium size

From 10 FTE and 5 mil CHF revenue

- separation of board from management
- independent risk management and control functions required
- No internal audit

Option 4: Big



Big size
From 10mil CHF revenue

- separation of board from management
- independent risk management and control functions required
- internal audit

Outsourcing

Delegation of Tasks

Art. 14 Abs. 1 FINIA
i. V. m. Art. 19 FINIA und Art. 15 Abs. 1
FINIO

No provision in the FINIA, contractual / fiduciary duties
pursuant to Art. 394 Code of Obligations or applicable trust law
i. V. m Art. 55 OR

Independently and
permanently

Significant tasks

Not independent

Not permanent

Not significant

→ **Outsourcing AML Unit / AML Officer: See also AMLA (e.g. Art. 25 sect. 4)**

Outsourcing - Examples of significant and not significant tasks

Art 15 FINIO

Significant tasks

- Management of portfolios or trust assets pursuant to Art. 19 FINIA
- Delegation of management of client assets pursuant to Art. 19 FINIA
- Delegation of significant activities in the area of trust or fund administration
- **Performance of compliance or risk management tasks**
- Outsourcing of IT-Systems and infrastructure including client data
- Safekeeping of business files in premises of third parties
- Trust Accounting

Not significant tasks

- Outsourcing of proprietary accounting
- Engagement of experts for the wealth structuring and in the area of estate and tax planning
- Use of IT-Systems with custodian banks or securities firms
- Hosting of websites without client data
- Maintenance (incl. Remote) of internal IT-Systems

see Erl FINIV zu Art. 15, S. 89

Outsourcing - What tasks cannot be outsourced?

FINIA	Circular Outsourcing
<p>Tasks, which must be part of the responsibilities and decisions of the management or supervisory bodies</p> <p>(Art. 16 Abs. 1 FINIO)</p>	<ul style="list-style-type: none"> • Supervisory body • Supervision and controls by the supervisory body • Central leadership functions of the management body
<p>Responsibility for the performance of regulatory duties</p> <p>(Art. 17 Abs. 1 FINIO)</p>	<ul style="list-style-type: none"> • Functions which include the taking of strategic decisions, including decision regarding acceptance or continuation of business relationships
<p>Delegation of tasks must not result in the licensed entity or affiliated companies to become empty shell.</p> <p>(Erläuterungen, S. 90)</p>	<ul style="list-style-type: none"> • Outsourcing of control functions is permitted to a limited extent (see N 9 RS) • Administrators of collective investments must at least have one collective investment plan that they manage themselves. (N 13.2 Rundschreiben)

Organisational Hot Topics



“One Man” Management

Art. 20 FINIA and Art. 25 FINIO

Currently, the SOs / FINMA offer three solutions to “demonstrate that orderly continuation of business is guaranteed”

1) Internal Solution	<ul style="list-style-type: none">• Qualifications same as for the sole manager (5 year experience and 40hrs training)• Employment agreement required
2) Cooperation Route (External)	<ul style="list-style-type: none">• Cooperation Partner must be licensed to professionally act as a trustee• Qualifications of responsible person same as for the sole manager• Written contract• [!] Agreement to take over trusts [!]• Regular communication / exchange between Trustee and cooperation partner [!]• Information of clients [!]
3) Liquidation Route (External)	<ul style="list-style-type: none">• Liquidator can be qualified individual (attorney, trust specialist etc.)• Written contract• Information of clients at the latest when Liquidator is starting to perform his role

- ➔ **Trustee specific issue: Transfer of client book is more tricky, as it is usually not in the power of the trustee to appoint a successor trustee**
- ➔ **Liquidation route: Must mandate be limited to liquidation? Could it include finding a buyer for the entity (share deal) or even recruiting a suitable qualified manager to continue?**

Cross Border

Trust Law

FINMA position: trustee specific risks arising from a business model involving a **large number of different trust jurisdictions and / or domiciles of settlors and beneficiaries**

Risks

- Trust laws are diverging, i.e., specific knowledge is needed for each trust jurisdiction
- Trustees always have to act in the interest of the beneficiaries, i.e., tax implications when making distributions

Organisational Expectations (FINMA)

- ➔ Trustee must have **access to specialists** from the relevant trust jurisdictions as well as to tax experts
- ➔ Separate of risk management and internal controls function

Cross Border

Foreign regulation / AML

FINMA position: trustee specific risks arising from a business model involving a **large number of different trust jurisdictions and / or domiciles of settlors and beneficiaries**

Risks

- Market Access (Legal Risks, Liabilities)
- Diverse Client Structure, i.e., servicing a large number of jurisdictions / markets
- Focus on a specific foreign region with increased money-laundering risks

Organisational Expectations (FINMA)

- ➔ Policies address the risks inherent to cross border services (i.e. country manuals, AML policy)
- ➔ Specific experience and qualifications of relationship managers
- ➔ Appropriately staffed institution
- ➔ Periodic trainings re country specific know-how
- ➔ Separate and independent risk and compliance functions

Cross Border

Foreign regulation / AML

Any activity performed by a **CFE** in relation to a prospect or **client outside of Switzerland**, or **from Switzerland into a different country** abroad, are **potentially subject to local regulation and licensing of the respective foreign jurisdiction.**

➔ Risks for the trustee, including financial losses due to fines, reputational damage and regulatory action by SO / FINMA.

CFE “Client Facing Employee”. Employee of the trust services provider who is directly engaging with prospects or existing clients. “Directly engaging” includes meeting, video calls, emails and any other form of communication or correspondence **in or into a foreign country.**

Client Includes settlor(s), beneficiaries and, rarely, a protector. Not included are, in general, persons or entities providing services to the trust structures, or persons or entities representing an underlying company or other trust asset

Cross Border

Examples of potentially regulated activities abroad

Services to Prospects (not exhaustive)

- pro-actively providing general information / marketing material on Services
- pro-actively soliciting services
- Providing specific information re trust services, at request
- Negotiation of engagement of trust services provider
- Referral to bank
- Referral to third party provider (e.g. lawyers, tax advisors)
- Roadshows, workshops etc.

Services to Existing Clients (not exhaustive)

- pro-actively providing general information / marketing material on Services
- pro-actively soliciting services
- Providing specific information re trust services, at request
- Providing to the client documentation for services undertaken (reporting)
- pro-actively providing services to the Client

Q&A



End



Appendix



Sources

Zitierweise	Quelle
Circular Corporate Governance	FINMA Rundschreiben 2017/1 Corporate Governance, Risikomanagement und interne Kontrollen bei Banken vom 1. Juli 2017 (letzte Änderung 31. Oktober 2019) https://www.finma.ch/de/~media/finma/dokumente/dokumentencenter/myfinma/rundschreiben/finma-rs-2017-01-20200101.pdf?la=de
Circular Market Conduct	FINMA Rundschreiben 2013/8 Marktverhaltensregeln vom 1. Oktober 2013 (letzte Änderung 4. November 2020)
Circular Operational Risks	FINMA Rundschreiben 2007/21 Operationelle Risiken – Banken vom 20. November 2008 (letzte Änderung 31. Oktober 2019)
Circular Outsourcing	FINMA Rundschreiben 2018/3 Outsourcing vom 1. April 2018 (Letzte Änderung 4 November 2020)
ERV	Verordnung über die Eigenmittel und Risikoverteilung der Banken und Wertpapierhäuser https://www.fedlex.admin.ch/eli/cc/2012/629/de
Erl FINIV	Erläuterungen FIDLEV, FINIV, AOV vom 6. November 2019
ErlB AB FINMA FINIG	Erläuterungsbericht für die Anhörung zu den Ausführungsbestimmungen der FINMA zu FIDLEG und FINIG vom 7. Februar 2020
ErlB GwV-FINMA	Erläuterungsbericht zur Teilrevision der Geldwäschereiverordnung-FINMA (GwV-FINMA) vom 4. September 2017 https://www.finma.ch/de/~media/finma/dokumente/dokumentencenter/anhoerungen/laufende-anhoerungen/rs-gwv/20170904-eb-gwv-finma.pdf?la=de
NRA	National report on risks of money laundering and terrorist financing of the interdepartmental coordinating group on combating money laundering established by the Swiss Federal Council («CGMF») published in June 2015

Laws and Regulations

Zitierweise	Quelle
DSG	https://www.fedlex.admin.ch/eli/cc/1993/1945_1945_1945/de
GwG	https://www.fedlex.admin.ch/eli/cc/1998/892_892_892/de
GwV	https://www.fedlex.admin.ch/eli/cc/2015/791/de
GwV-FINMA	https://www.fedlex.admin.ch/eli/cc/2015/390/de
FINIG	https://www.fedlex.admin.ch/eli/cc/2018/801/de
FINIV	https://www.fedlex.admin.ch/eli/cc/2019/763/de
FINIV-FINMA	https://www.fedlex.admin.ch/eli/cc/2020/922/de
VSB 20	https://www.swissbanking.ch/de/downloads

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