

Game changer for Swiss trustees: new licensing obligation from 2020

19 December 2019 | Contributed by [LALIVE](#)

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Introduction

From 1 January 2020, the Swiss Financial Institutions Act (FinIA) and the Swiss Financial Services Act (FinSA) will become law and introduce a regulatory regime for trustees operating in Switzerland, obliging them to obtain an authorisation to carry out their activities. The new regime should reinforce the general reputation and competitiveness of Switzerland as a financial centre and boost the Swiss trust industry's quality, integrity and accountability.

The objectives of the FinIA and FinSA are twofold:

- to create a uniform competitive landscape for financial intermediaries; and
- to improve client protection.

The FinIA sets out the basic obligations for acting as a financial institution in or from Switzerland, whereas the FinSA outlines the basic requirements for providing financial services and governs the offering of financial instruments. Although not initially included, the Swiss government finally decided to include trustees in the definition of 'financial institutions' provided under the FinIA. This development marks an important move towards regulating the Swiss trust industry.

On 6 November 2019 the Swiss government published the final versions of both ordinances implementing the FinIA and FinSA – respectively, the Swiss Financial Institutions Ordinance (FinIO) and the Swiss Financial Services Ordinance (FinSO). These implementing ordinances will also become law on 1 January 2020. The final drafting of both ordinances has been significantly amended from the initial proposed drafts issued by the Federal Financial Department on 24 October 2018 and takes into consideration input provided by the industry.

Definition of 'trustee' and scope

As construed under the FinIA, a Swiss 'trustee' is defined as a person who manages or disposes of a separate fund on a professional basis for the benefit of a beneficiary or for specified purposes based on an instrument creating a trust within the meaning of the Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on their Recognition.

Of particular importance for practitioners, the FinIO identifies how to interpret the seemingly vague definition of 'on a professional basis'. It would include persons who have:

- a gross annual turnover of Sfr50,000;
- business relationships with more than 20 contracting parties; or
- the power to dispose of third-party assets of more than Sfr5 million at any given time, provided that the power is not time limited.

Notably, the final draft of the FinIO no longer mentions a specific transactional valuation threshold

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as a determining prerequisite. Of equal importance, as confirmed by the Department of Federal Finances' official commentary on the new legislation (in particular, FinIO and FinSO) dated 6 November 2019, Swiss trustees will not be subject to the FinSA and the FinSO since their activity does not comprise asset management.

Licensing process

Under the new regime, trustees will be supervised by the Swiss Financial Market Supervisory Authority (FINMA), which will delegate the day-to-day supervision to separate supervisory organisations that have yet to be created and that must receive prior authorisation from FINMA to act in the envisaged supervisory capacity.

The main deadlines to consider are:

- 30 June 2020 – deadline for trustees to inform FINMA of their intention to apply for a licence;
- 30 June 2020 – deadline for existing representative offices of foreign trustees to notify FINMA of their existence;
- 31 December 2020 – deadline for trustees to affiliate themselves with a supervisory organisation, comply with statutory requirements and file an application to FINMA to obtain a trustee licence; and
- 31 December 2022 – deadline to register with a supervisory organisation, comply with statutory requirements and apply for a licence from FINMA.

During this three-year transitional period, existing trustees will be able to continue their activities on the condition that they remain affiliated to self-regulatory organisations for anti-money laundering compliance purposes.

Licensing exemptions

Under the FinIA, certain trustees may benefit from specific exemptions obtained from FINMA and thus need not obtain a licence to carry out their activities in Switzerland.

These exemptions may be obtained by:

- trustees exclusively managing or holding assets of persons with whom they have family ties (the family ties exemption). This rule specifically caters for family offices and private trust companies (PTCs) and has been extended in the final draft of the FinIO to include not only relatives in a collateral line up to the third degree, but also relatives in a collateral line up to the fourth degree (ie, including cousins). This rule also applies to trustees administering assets for a family if the said assets are directly or indirectly controlled by a trust or foundation that was created by a member of the same family. The family ties exemption will also apply if the beneficiary is a charity; and
- PTCs construed as companies with the sole purpose of operating as trustees for a specific trust or group of trusts belonging to the same settlor or a pre-determined circle of beneficiaries.

On request, FINMA also may dispense exemptions if:

- supervision and ownership of the trustee (a trust company) is carried out by a trustee which already holds an authorisation granted by FINMA to act as a trustee; or
- the activity of a trustee is exclusively limited to acting as a trustee of trusts that have been created by the same person or for the benefit of the same family.

New regulatory obligations

Trustees falling within the scope of the FinIA will be subject to regulatory supervision and must be authorised to carry out their activities in addition to complying with the following structural, organisational, business conduct and audit requirements:

- Structure – a trustee can take the form of sole proprietorship, commercial enterprise or cooperative, and can be registered in the commercial register only once authorised. There is a minimum requirement of paid capital of Sfr100,000, with the obligation to maintain adequate financial coverage or professional liability insurance.
- Organisation – a trustee's management must be exercised in principle by at least two 'qualified directors', defined in the FinIA as persons who have at least five years' experience and have

received relevant training of at least 40 hours in the trusts field. In addition, a trustee must have an appropriate corporate and management organisation, risk management and adequate internal control systems. The final draft of the FinIO also imposes that if the trust company employs more than 10 employees full-time or if its annual revenues exceed Sfr5 million, the trustee must have a board of directors in place composed of members that are mainly independent from the entity's management. Finally, the effective place of management must be located in Switzerland.

- Business conduct – trustees and persons responsible for trust administration and management must be fit and proper, uphold a good reputation and attain the necessary professional qualifications.
- Internal audit and risk management – if the entity employs five or more employees full-time or if the annual gross revenue exceeds Sfr2 million, internal control, audit and risk management must be monitored independently (ie, by a different employee) from the activities which generate revenue. Should these thresholds not be reached, the aforementioned tasks could be assigned to two directors (ie, one in charge of the client follow-up, risk monitoring and control execution and the other in control of the portfolio monitoring and anti-money laundering and cross-border activity compliance).
- Audit – trustees are subject to an annual audit that may be conducted by the designated supervisory organisation or, if no such organisation is in place, by an external auditor and which may be extended to once every four years, with the obligation to submit an annual report on the conformity of their activities during the years when no annual audit is conducted.

Trustee's professional qualifications

One of the main and most important consequences of the new legislation for Swiss trustees is the necessity to meet certain criteria in order to obtain a licence from FINMA to practise in Switzerland.

The latest draft legislation of the FinIO has lowered the experience and qualifications required. However, it does impose the following alternative minimal conditions to be considered as a qualified director under the FinIA:

- the person must have at least five years' experience in the trust industry; and
- the person must have followed a training course for at least 40 hours which related to trusts (during or after working in the trusts field).

Under special circumstances and on a case-by-case basis, FINMA may grant exemptions for persons who do not meet these requirements. The rule remains that meeting these prerequisites will become essential in order to be granted a licence by FINMA from 2020.

Swiss versus foreign trustees

The FinIA and the FinIO provide clarity as to how FINMA will distinguish Swiss trustees from foreign trustees. The main test will be to determine the place of effective management (ie, whether the geographical location where the entity carries out its management activities is exclusively or predominantly in Switzerland or from Switzerland). If these criteria are met, the entity will have to be organised in accordance with Swiss legislation and will be subject to the FinIA and FinIO rules governing foreign financial institutions.

Therefore, one of the key practical issues arising from the new legislation will be determining how existing multi-jurisdictional financial setups will be construed under the new law, especially in light of the location of the predominant management activities test and how the Swiss authorities (in particular, FINMA) will distinguish genuinely foreign trustees from those that will thus be entirely regulated.

This issue will have foreseeably significant practical consequences, as trustee structures commonly operate with a foreign and sometimes predominant component and will no doubt be at the centre of many existing trustees' concerns and future planning.

Comment

The new financial legal framework represents a novel legislative era for trustees operating in or from Switzerland and, with it, brings considerable regulatory and administrative challenges, but also opportunities which may bring the Swiss trust industry to the next level.

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