

RETROCESSIONS IN THE FOCUS OF THE REGULATOR**Swiss Federal Banking Commission ("FBC") communicate their position in letter to fund management companies, custodians and Swiss representatives of foreign funds**

Referring to the recent "**late-trading**"-scandal in the U.S. the FBC state that such practices would violate the duty of loyalty stipulated in the Swiss Investment Fund Act ("IFA") as well as the principle of "forward pricing" which is to be adhered to pursuant to the "Guidelines on the calculation of net asset values and the handling of valuation errors in the case of securities funds" by the Swiss Funds Association.

The FBC take the occasion to set out their interpretation of the IFA and the Code of conduct for the Swiss fund industry ("Code of Conduct") in relation to **retrocessions to distributors or investors paid out of the management fee or the subscription/redemption fee**:

➤ Key points of the FBC's interpretation:

- ① If a part of the **management fee** is used to remunerate distributors, **disclosure** must be made in the prospectus/fund regulations.
- ② **Subscription/redemption fees** may be used to remunerate distributors. Different rates may be applied for subscription/redemption fees charged to different investors/different "groups" of investors. The criteria for applying such different rates must be **disclosed** in the prospectus/fund regulations.
- ③ **Retrocessions** are necessarily to be defined as remuneration for distribution activities. Thus they **may not be paid to end-investors**. The FBC fears that the possibility of fee arrangements with large end-investors could lead to dependence from such major investors which might in turn abuse their position.
- ④ Whereas the FBC admit that the interpretation in their letter concerns provisions of the IFA which are only applicable to Swiss fund management companies and Swiss custodians, they say that Swiss representatives of foreign funds must adhere to the rules described above in order to comply with the Code of Conduct.

➤ Our view:

- We *recommend* to review prospectuses/fund regulations and to **implement disclosures** according to ① and ② above also in the case of foreign funds where possible.
- We *disagree* with the FBC's analysis under point ③. The qualification as a distributor or an end-investor cannot be the decisive element when determining whether retrocessions may be paid or not. Major investors may gain influence irrespective of their status as distributor or end-investor. Therefore, the FBC seems to apply the wrong criteria while trying to achieve a legitimate goal. We do not believe that everything has been said in this respect.
- We *disagree* with point ④ above and in particular think that the Code of Conduct does not provide the basis for the interpretation made by the FBC.

For more information feel free to contact any of our investment fund specialists (<http://www.nastra.ch/>).