

FINIA – Organisational requirements for Trustees

FINIA, The Swiss Financial Institutions Act, which came into force on the 1st January 2020, places Trustees under prudential regulation in Switzerland for the first time. Trustees are required to register with and obtain a license to operate from the Swiss Financial Market Supervisory Authority (FINMA). One provision, which from our experience so far, seems to be causing concern is Article 9 relating to the FINIA organisational requirements, whereby *‘the financial institution must establish appropriate corporate management rules and be organised in such a way that it can fulfil its statutory duties.’*¹

In essence, this Article is focussing on adequate internal control systems and governance for professional trustees. The Federal Council will be responsible for setting the minimum requirements to be satisfied by financial institutions, but at the time of writing these have not yet been determined.

In order to seek some guidance on what we could expect, we, and presumably FINMA and the Federal Council, can look at other centres having a longer history of trust and trustee regulation. Jersey, in the Channel Islands, has had a Financial Services Act since 1998, which also governs Trustees and Trust Companies. Being a major centre for trust and asset management business for decades, it can be looked at as a best-practice example to provide some guidance for the direction Switzerland may follow in implementation of the new FINIA organisational requirements.

In a recent publication from the Jersey Financial Services Commission (JFSC) the commission imposed a significant penalty on Equity Trust (Jersey) Limited where a number of breaches were identified. One major failing was that Equity Trust were deemed to have negligently breached certain paragraphs of The Conduct Of Business Code (TCB Code²), notably that; *‘a registered person must organise and control its affairs effectively for the performance of its business activities and be able to demonstrate the existence of adequate risk management systems.’*

Specifically, Equity’s compliance function came in for criticism as it was deemed not to have sufficient independence to devote sufficient time and have sufficient resources to effectively discharge the responsibilities of the function, as set out in the TCB Code; An example of the importance of adequate internal control systems and governance in place. The [former] compliance officer of Equity also served as a director on the board of a (non-specified) number of Equity’s companies, which in turn, were appointed as directors to a number of customer entities.

Aside from the obvious conflicts of interest, the customer facing role meant that the compliance function was not clearly defined and there was a lack of discipline with respect to Equity’s three lines of defence, with the second line of defence being significantly eroded. It was noted that Equity failed to operate an independent compliance function as determined by the TCB.

¹ <https://www.admin.ch/opc/en/classified-compilation/20152662/index.html>

² <https://www.jerseyfsc.org/industry/codes-of-practice/trust-company-business-code-of-practice/>

Whilst the Swiss Financial Institutions Act is focussed primarily on asset managers and smaller to medium sized financial institutions, the explicit coverage of trustees under the act means greatly increased scrutiny, rigour of oversight and increased standards of practice for trustees in Switzerland. We fully expect that the organisational requirements for trustees going forward will focus on business functions where there should be clear levels of independence between each of the functions, to avoid or minimise as far as possible, conflicts of interest and implement functions that are able to demonstrate adequate risk management systems.

Ahead of the publication of the minimum requirements, many of the smaller Trust Companies and asset managers are already concerned about how they will implement an organisational structure with limited numbers of employees, not to mention the cost implications. Firms who are concerned about this and who they feel that there may be perceived conflicts of interest, or inadequate independence of risk management functions, could take steps to externalise their compliance function, creating an independent, outsourced function that remains separate from the day to day business. FINMA has foreseen and allowed for the need for financial institutions to outsource certain functions and set out guidelines in the circular from September 2017: [Circular 2018/3 - Outsourcing – banks and insurers](#). FINMA has since stated that the provisions in this circular can be applied to trustees and asset managers.

In order to demonstrate independence at board level it could be that we see an increase in the use of non-executive directors, where they are brought in to provide industry experience and can act with prudence where required.

Whilst we can only provide informed commentary at this early stage, it is clear that the impact of the Act for trustees should not be underestimated and Aviolo is watching developments closely. As the full implications of the FINIA organisational requirements for trustees become clearer, we will be advising our clients on how to comply with them in a pragmatic, timely and cost-effective manner.