

Commentary
on the
Rules of Conduct
of the
Industry Organisation for Asset Management
of the
VQF Financial Services Standards Association
regarding the
Practice of Asset Management

No comment.

Art. 1 Purpose of these Rules of Conduct

No comment.

Art. 2 Form

In view of the obligations which the asset manager enters into towards his client when concluding and fulfilling the asset management agreement, the only possible basis for the agreement is the written form.

Art. 3 Content

Para. 1:

Any **appendices to the asset management agreement** must form an integral part of the agreement.

The **asset management agreement** must define the activities which the asset manager is authorised to undertake. This concerns both activities in the context of asset management as well as those concerning the assets entrusted to the asset manager (especially account income and remittances). In the case of a discretionary mandate, the asset management agreement must specify which financial instruments the asset manager may use.

The assets to be managed, among other items, must also be clearly identified in the asset management agreement (scope of the asset manager's authority; Art. 3 Para. 1 letter b of the Rules of Conduct). This information also includes details of the financial institution(s) with which the assets are deposited and details of the accounts and deposits covered by the asset management agreement. As a client may have several accounts with a financial institution, the full identification numbers of the accounts and deposits covered by the agreement must be given.

The **investment goal** depends on how the client's risk profile is defined. In this respect, the client's risk appetite (subjective) and risk capacity (objective) must be defined first. Once the client's risk profile has been defined, the asset manager then consults with the client to determine the investment goal. Investment policy and resource allocation must both take account of the client's risk profile and also be geared towards the mutually defined investment goal. In the event that the client's specific instructions are not in accordance with his risk profile or the agreed investment goal, the asset manager draws the client's attention to this fact and records it in writing. The asset manager provides effective monitoring of investment policy. This allows the asset manager to guarantee that the investment policy is in accordance with the client's risk profile and investment goal at all times.

The client must take note of the means of communication (meeting, post, account statements etc.) and methods (with or without comparison indices, own system for results measurement etc.) to be used for the asset manager to **render account** to the client of his activities, as well as the time period associated therewith (half-yearly, annually etc.).

The client must be able to understand how the asset manager is compensated and what the amount of **compensation** is compared to the value of the assets which he has entrusted to the asset manager. In like manner, the client is informed about when and in what way the asset manager is entitled to claim his compensation. The asset manager is not permitted to draw his compensation direct from the client's account unless the client expressly authorises him to do so. If the asset manager receives third party benefits in the context of his mandate, the agreement must specify to whom these benefits are due and in what way the asset manager must disclose them (see Section 4 of the Rules of Conduct).

Art. 4 Duty of Guarantee

The Anti-Money Laundering Act also demands such a guarantee (Art. 14 AMLA).

Art. 5 General

No comment.

Art. 6 Prevention of Conflicts of Interest

Para. 1:

The asset manager's organisational structure must allow him to fulfil the obligations arising to him from his mandate – especially as regards his independence. The asset manager must anticipate the areas in which his own interests may conflict with those of his client and adjust his organisational structure accordingly. If the asset manager's organisational structure is not able to prevent such conflicts of interest he must raise this issue with his client accordingly.

Art. 7 Duty of Confidentiality

Duty of confidentiality continues to apply on termination or cancellation of the asset management agreement.

Art. 8 Duty of Investigation, Clarification and Information

Para. 1:

The asset manager's clients are aware of the rules of conduct to which the asset manager is subject. The asset manager must be able to prove that he either issued a copy of the rules of conduct to his clients or made his clients aware of the existence of such rules.

Para. 3:

On the closure of an agreement and on amendment of the investment goal the asset manager informs his clients about the risks of loss associated therewith. This duty of information also depends on the complexity of the financial instruments from which the client's portfolio is assembled. Obviously, therefore, the asset manager must also understand and have command of the financial instruments purchased on behalf of his client. Duty of information towards clients may also be satisfied by issuing standardised explanations.

Para. 4:

It is not necessary to inform clients about insignificant changes. However, the client must be informed about changes which involve important components relating to the closure or continuation of the agreement.

Art. 9 Duty of Accountability

Para. 1:

The nature and periodicity of the rendering of account to clients must be defined in the asset management agreement (see Art. 3 of the VQF Rules of Conduct).

Para. 3:

The asset manager's report to his client must allow the client to determine whether the investment goal was achieved. Where applicable, the method of calculation employed must be compatible with the chosen reporting period. If the asset manager uses comparison indices (benchmarks), these must be meaningful in relation to the transacted investments. In the context of his duty of accountability, the asset manager may also make use of client-related performance reports issued by the deposit bank which are relevant to the respective client, provided that such reports satisfy the standards prevalent in the asset management industry (e.g. global investment performance standards) and allow the client to determine whether the investment goal was achieved.

Art. 10 Handling the Client's Instructions

No comment.

Art. 11 Investments and Transactions

Paras. 1 and 2:

The transactions carried out by the asset manager are open to financial scrutiny. The relationship between received commissions and managed client assets must be reasonable. The asset manager may not use the knowledge gained from the orders received from his clients for his own purposes if by doing so he would be in breach of his duty of trust or the principle of good faith. The same principle applies accordingly to both securities dealers and asset managers (See SFBC Circular 08/1 concerning supervisory regulations regarding market behaviour for securities dealers).

Art. 12 Choice of Depositary Location

No comment.

Art. 13 Choice of Counterparty

No comment.

Art. 14 Organisational Measures

Paras. 1 - 3:

The asset manager must adjust his organisational structure in accordance with the value of the assets assigned to him. The asset manager uses financial products of whose risks he is fully cognizant. He adjusts his organisational structure accordingly – and indeed in such a way that he is always in a position to check whether the risks correspond to the investment policy agreed with the client. For asset managers of Swiss collective capital investment schemes the same obligation arises from Art. 20 Para. 1 letter b of the Swiss Collective Capital Investment Act (KAG): “They take the organisational measures which are required for impeccable business management.”

Art. 15 Measures relating to the Execution of the Asset Management Order

Paras. 3 - 4:

The definition of the client’s risk profile forms the basis for the proper fulfilment of the asset management mandate. In this respect, the client’s risk appetite (subjective) and risk capacity (objective) must first be defined. Once the client’s risk profile has been defined, the asset manager then consults with the client to determine the investment goal.

The asset manager provides effective monitoring of investment policy. Temporary variance of the investment policy from the investment goal agreed with the client due to fluctuations in the financial markets is permitted. The situation must be discussed with the client if such variance persists. In the event that the client’s specific instructions are not in accordance with his risk profile or the agreed investment goal, the asset manager draws the client’s attention to this fact and records it in writing. The client’s risk profile and investment policy must be checked regularly for compliance with the client’s changing situation - especially his financial situation.

Art. 16 Acceptance of Assets and the Management of Assets deposited at Banks

Only banks and securities dealers approved by the SFBC may accept deposits from the public on a commercial basis. However, no interest must be paid in respect of such deposits with securities dealers (Art. 1 Para. 2 Swiss Banking Act [BankG] and Art. 3a Swiss Banking Ordinance [BankV]). The asset manager may arrange for the assets which he manages to be transferred via his own accounts.

Art. 17 Delegation of Asset Management Duties

No comment.

Art. 18 Content of Compensation

The client must be able to understand how the asset manager is compensated and what the amount of compensation is compared to the value of the assets which he has entrusted to the asset manager. The client is also aware of when and in what way the asset manager is entitled to claim his compensation.

Art. 19 Third Party Benefits

Para. 1:

The asset management agreement must define the legal assignment of all benefits which the asset manager receives from third parties in the context of his mandate. These benefits include both those benefits which are associated with the mandate in their own right and those which relate to benefits that were directly or indirectly conferred by the said third parties in favour of the asset manager. However, in practice it is often difficult to differentiate between benefits associated with the mandate in their own right and those which are only received on execution of the mandate.

Para. 2:

In accordance with current practice and jurisdiction (Federal Court Rulings 132 III 460 et seq.).

Para. 3:

The member must inform his client accordingly if the acceptance of third party benefits leads to a conflict of interest, or the possibility of such a conflict.

Para. 4:

The asset manager openly provides his client with the necessary information about what benefits he might receive in accordance with the selected product type. The principle of client information likewise applies in the case of benefits which are not directly associated with a specific product type, such as those that depend exclusively on the deposit value.

Para. 5:

If requested to do so, members must inform their client of the total amount of the effective benefits received from third parties in the context of their mandate, provided that the member is technically able to quantify these benefits. Asset managers are expected to have a structure which allows them, in particular, to calculate the benefits received from banks and securities dealers individually for each of their clients. With regard to banks, this concerns benefits which originate from deposit commissions on their clients' assets. In the case of securities dealers, this refers to benefits that originate from brokers' commissions which are generated from the execution of client orders.

Although Art. 26 of the Markets in Financial Instruments Directive (MiFID - European Union regulation) specifies that the respective data must be provided immediately, before the investment service is transacted, the situation is different in this case. The client must only be informed immediately about the margin on the services received by product type. Once the asset manager has received third party benefits the client may demand additional information on the specific amount of those benefits. The asset manager establishes a suitable structure which allows him to meet his clients' demands for further information, provided that it is possible to allocate the benefits received from third parties to individual client relationships.

Art. 20 Severability Clause

No comment.

Art. 21 Entry into Force

No comment.

Art. 22 Temporary Arrangements

Introductory comments:

- a. **Voluntary subordination:** "Independent" asset managers (e.g. financial intermediaries pursuant to Art. 2 Para. 3 AMLA) who do not offer collective capital investment schemes to their clients can voluntarily become subordinate to the rules of conduct of an industry organisation (e.g. VQF IOAM) which are recognised by FINMA. Such voluntary subordination makes sense because, as a necessary prerequisite for the granting of mandates relating to client accounts, an increasing number of **banks** require their external asset managers to be members of an industry organisation for asset management in addition to holding membership of a self-regulatory organisation (SRO) pursuant to the AMLA, thus ensuring that investor protection is also supervised (compliance with rules of professional conduct for asset managers). By doing so, banks aim to prevent any threats to their reputation and risks of liability. An increasing number of **clients** likewise desire that asset managers independent of banks should also be supervised with regard to investor protection.
- b. **Compulsory subordination:** Insofar as in the context of their asset management or other activities independent asset managers offer collective capital investment schemes to **non-qualified investors**, in view of FINMA Circular 2008/8 Public Advertising of Collective Capital Investment Schemes such subordination to officially recognised rules of conduct (e.g. VQF IOAM membership) is indeed **compulsory** with effect from

30. September 2009

(see detailed explanation in the VQF letter to members dated 18 September 2009, which can be viewed at www.vqf.ch, "IOAM" heading, sub-heading "Duty of Subordination"), provided that the asset manager does not intend to offer collective capital investment schemes to high net worth private individuals (or otherwise qualified investors) as the client after 30 September 2009. Further information on duty of subordination is available on our website (www.vqf.ch, "IOAM" heading, sub-heading "Duty of Subordination").

Comment on Art. 22 Paras. 1 - 3:

Apart from the above mentioned deadline of 30 September 2009 concerning subjection to supervision by the VQF IOAM, the following additional **transitional regulations** apply with regard to compliance with the provisions on public advertising contained in the KAG:

- a. With regard to **business relationships (asset management agreements) entered into after 30 September 2009**, full compliance is required with the provisions of the rules of conduct (Art. 22 Para. 1 of the Rules of Conduct).
- b. The following transitional regulation exists with regard to **business relationships (asset management agreements) entered into before 30 September 2009** (and still in existence on 30 September 2009): in Art. 22 Para. 2 of the rules of conduct, the VQF provides for a transitional period of grace until **31 December 2010** for the formal adjustment of existing asset management agreements. However, compliance with the material duties contained in the rules of conduct in accordance with Art. 22 Para. 3 thereof is required with effect from 30 September 2009 for agreements entered into prior to this date.

Other comments:

For the purpose of supporting members when entering into agreements with new clients as from 30 September 2009, the VQF IOAM provides members with a **sample asset management agreement** with examples for the formulation of contractual clauses in accordance with the VQF IOAM rules of professional conduct (see enclosure to the VQF letter to members dated 18 September 2009; or the protected members' area on the VQF website, www.vqf.ch). Members can use this sample asset management agreement or adjust this in line with their individual needs – provided that they maintain compliance with the rules of professional conduct.