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6) Next Steps

In line with the revised ISO, FINMA will continuously develop and communicate its supervisory practice. While a number of FINMA circulars will be adjusted, new circulars will also be drafted until 1 January 2017.

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The Rise of Actively Managed Certificates

Reference: CapLaw-2015-19

Actively Managed Certificates (AMCs) have become more and more popular in recent years. Unlike most other structured products, AMCs have special features which enable the active selection and adjustment of the components of their underlying strategy. The fast growth of the AMC market emphasizes the importance of the applicable regulatory and contractual framework. In addition to the general rules that apply to all structured products, AMCs are subject to specific regulatory and contractual requirements. This article provides some insights on these characteristics.

By Luca Bianchi

1) Introduction

Traditionally, structured products were qualified as “passive” financial products. However, there has been a shift to a new breed of “active” product solutions. So-called “Actively Managed Certificates” (AMCs) have grown and continue to grow at an astonishing rate. AMCs are structured products whose underlying strategy, respectively, strategy-components are adjusted over the course of their term at the discretion of a strategy-sponsor. The strategy's performance is tracked by calculating the value of a synthetical strategy-basket (or tailor-made index) that consists of individual notional strategy-components which are actively selected and adjusted in compliance with the parameters of the specific product idea.

This article aims to provide a high level overview on selected features of the regulatory and contractual framework that is applicable to AMCs which are issued or distributed in Switzerland.

2) Regulatory Framework

a) General Rules for Structured Products

AMCs are subject to the general rules for structured products. Structured products may only be distributed to non-qualified investors in or from Switzerland if (i) they are

issued, guaranteed or equivalently secured by a Swiss bank, insurance company or securities dealer (or a foreign institute that stands under equivalent prudential supervision) and (ii) a simplified prospectus is published.

The general content requirements of a simplified prospectus for structured products are set out in the Swiss Banking Guidelines on informing investors about structured products of September 2014, p. 1 et seq.

However, the publication of a simplified prospectus is not mandatory if a structured product is listed on a Swiss exchange which ensures the relevant transparency that would otherwise be provided by a simplified prospectus (*i.e.* in the final terms of a product). Further exceptions from the duty to publish a simplified prospectus may apply in the scenario of a distribution which is made *exclusively from* Switzerland (but not *within* Switzerland). Nevertheless, many issuers choose to publish a simplified prospectus on an optional basis for marketing purposes.

Furthermore, the FINMA-FAQ “Structured products” of 10 September 2014 should be taken into consideration. They contain specific guidance on various issues that are related to the offering and distribution of structured products.

It is worth highlighting that foreign issuers of structured products that are not listed in Switzerland are required to have a Swiss branch if distribution to non-qualified investors into, in or from Switzerland is targeted. The term “Swiss branch” comprises a representative office, a branch office, a subsidiary, a sister company or a group company; provided that such “Swiss branch” stands under consolidated supervision at the group level.

The concept of regulated “distribution” applies to any offering or advertising which is not directed exclusively to qualified investors. The scope of this definition is explained in a detailed manner in the FINMA-Circular 2013/9 “Distribution of collective investment schemes” of 1 October 2013 that applies *mutatis mutandis* to structured products (where appropriate).

Generally, the SIX Swiss Exchange (SIX) Listing Rules are also applicable to structured products that will be listed and traded on the SIX Structured Products exchange platform. In particular, the Additional Rules Derivatives (ARD), the Scheme F, the Directive on Procedures for Debt Securities (DPDS), and the Directive on Debt Securities with Specific Structures (DDSS) are applicable.

In addition to this high level overview on the general rules applicable to structured products, the specific requirements that apply for AMCs shall be briefly addressed in the following section.

b) Specific Requirements for AMCs

i. Selected Regulatory Features

The description of AMCs in a simplified prospectus must include information on the basic parameters of the strategy. In particular, the following information should be stated therein: (i) criteria for the selection of strategy-components, (ii) information on the handling of the income of such underlying values, (iii) strategy-guidelines, (iv) the relevant strategy-universe, (v) the strategy-sponsor, (vi) the applicable compensation of the strategy-sponsor, and (vii) notes on where information on the strategy and its current composition are accessible.

Furthermore, AMCs need to be clearly distinguished from collective investment schemes. In practical terms, a general disclaimer must be inserted in a prominent position in the simplified prospectus. This differentiation from collective investment schemes is particularly important because AMCs are, like any other structured products, subject to the issuer risk (whereas this is generally not the case for collective investment schemes). It should be noted that any risk of deception or confusion must strictly be avoided (especially, with respect to the description of the product in the final terms and/or the simplified prospectus).

In addition, AMCs must be marked as dynamic, discretionary managed products in bold letters on the first page of the simplified prospectus. Further regulations may be applicable for specific, innovative AMCs. Potentially applicable restrictions should be evaluated and implemented on a case by case basis; e.g. if collective investment schemes shall represent an eligible strategy-component. However, AMCs must not be confused with fund-linked notes (which are subject to special regulatory requirements).

Similar rules apply in case of listed AMCs. For example, SIX can demand that issuers disclose the current composition of the underlying strategy. The SIX may also request the history of the adjustments made to the relevant AMC from the issuer. Moreover, issuers of listed AMCs have to conclude a market making agreement with SIX and are subject to certain reporting requirements (e.g. in case of mistrades).

ii. Strategy-Sponsor Agreements and Rule Books

Apart from the general structured products documentation (i.e. the base prospectus, the final terms, and distribution agreements) a number of other documents have become market standard for the issuance of AMCs. In particular, issuers conclude so-called “strategy-sponsor agreements” in order to regulate the rights and duties of the strategy-sponsor.

Typically, strategy-sponsor agreements contain sections on (i) the objects of the agreements, (ii) the rights and duties of the parties, (iii) a description of the strategy,

(iv) the administration of the strategy (including guidelines and restrictions for the selection of strategy-components), (v) fees, (vi) liabilities, (vii) term, (viii) sub-delegation, (ix) assignments, (x) notices, and (xi) other standard contract terms.

Potentially, the strategy-sponsor agreements may refer to additional, technical rule books. These documents contain detailed guidelines and restrictions for the selection of and adjustments to the strategy-components. Rule books have become more elaborate in recent practice and continue to become more and more sophisticated. They are recommended in case of complex AMCs.

3) Conclusion and Outlook

Today, AMCs are considered to be a very popular product solution for issuers and for external asset managers. The excellent “time-to-market” of the issuing process as well as the high flexibility in terms of product design seem to be convincing arguments for the selection of these products. It is expected that the trend for more diverse and complex AMCs will continue in the coming years.

Issuers and strategy-sponsors should note that the proposed new rules of the FIDLEG, the FINIG, and the FINFRAG may, presumably, affect production, management, distribution, and trading of AMCs (cp. CapLaw-2014-5 and NKF Banking, Finance & Regulatory Team, Switzerland's New Financial Market Architecture, www.nkf.ch/en/publikationen_suche/fachgebiete.php).

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UBS Group AG Issued Write-Down Notes

Reference: CapLaw-2015-20

On February 19, 2015, UBS Group AG, the new top holding company of UBS group, completed the inaugural issuance of USD 1.25 billion 7.125% Additional Tier 1 write-down notes, USD 1.25 billion 7.00% Additional Tier 1 write-down notes and EUR 1.00 billion 5.75% Additional Tier 1 write-down notes.