

L-QIF – Draft Implementing Provisions

On September 23, 2022, the draft revised Collective Investment Scheme Ordinance ("CISO") has been published for consultation. The new provisions mainly implement the rules on the new unregulated fund category for qualified investors, the so-called Limited Qualified Investor Fund ("L-QIF"). The consultation follows the enactment of the revised Collective Investment Schemes Act ("CISA") in December 2021 and is scheduled to last until December 23, 2022.

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1. Introduction

In December 2021, the Swiss Parliament enacted amendments to the CISA in order to introduce the L-QIF, a new category of funds reserved to qualified investors. Provided it is managed by an institution subject to prudential supervision by the Swiss Financial Market Supervisory Authority ("FINMA"), the L-QIF is exempt from any FINMA authorization and supervision. Also, this new fund type will offer significant flexibility in terms of investment rules and restrictions.

With the introduction of the L-QIF, the Swiss legislator aims at increasing the innovative capacity and attractiveness of the Swiss investment fund market, based on the example of foreign jurisdictions such as Luxembourg and its Reserved Alternative Investment Fund ("RAIF").

On September 23, 2022, the draft revised CISO has been published for consultation. It provides

for implementing provisions as regards the L-QIF as well as further amendments. Certain other acts, including the Lex Koller, the Financial Institutions Ordinance and the Investment Foundations Ordinance, are impacted as well.

For an overview of the key issues raised during the legislative process, please refer to our previous newsflashes of September 2019, April 2021 and December 2021

2. Incorporation and restructuring

During the incorporation process, L-QIFs will need to address an official notice to the Federal Finance Department ("FFD"), by which they expressly waive FINMA supervision. As a consequence, we expect the FFD to publish a list of existing L-QIFs.

Authorized collective investment schemes will need FINMA's approval in order to transform into L-QIFs. The conversion of an L-QIF into a supervised collective investment scheme will not be possible

3. Investment rules and infringements

Based on the RAIF model, the draft investment rules offer a wide range of flexibility. L-QIFs in the form of SICAVs and contractual investment funds will be subject to the same requirements as alternative funds, whereas no provision will restrict limited partnerships for collective investments (KmGK; SCmPC). In the absence of legislative investment rules, the fund documents will define investment and risk diversification rules.

Infringements to investment guidelines trigger different consequences depending on the circumstances: (i) passive violations must be resolved within a reasonable period; (ii) active infringements, on the other hand, must be corrected immediately and must be mentioned in the annual report. If a prejudice to investors cannot be ruled out, the L-QIF will separately need to inform the investors and auditor.

4. Real estate open-ended L-QIFs

Open-ended L-QIFs investing in real estate will be subject to specific investment rules. While real estate L-QIFs are expected to serve as a suitable (and innovative) form of investing in real estate, it is worth noting that the debt ratio will be limited to 50%.

The draft CISO broadly defines eligible real estate. It includes unbuilt/undeveloped land, which is not immediately buildable, and minority interests in condominiums. Diversification rules are also flexible as they do not provide for a minimum amount of properties.

Specific rules will apply to real estate transactions with so-called "related persons". In particular, (i) the fund documents must expressly allow such transactions, (ii) a majority (of at least 50%) of investors must give their consent to the transaction and (iii) an independent expert must issue an opinion confirming that the sale price and transaction costs are in line with the market. No transaction with related persons will be possible for construction projects initiated at the request of the fund management company, the SICAV or related persons.

Whereas the CISA provides that "individuals" will be prevented from investing in real estate L-QIFs, the CISO draft does not expand on this notion. While this covers not only individuals, but also their private investment structures, there is a question whether private investment structures with professional treasury operations, i.e. so-called per se professional clients under the Financial Services Act, will also be considered as "individuals" for the purpose of the L-QIF regime.

5. Compliance and audit

The prudentially supervised institution in charge of managing the L-QIF will be responsible for the compliance with legal provisions. In light of comparable structures abroad, it is expected that this responsibility will be construed strictly in practice and that FINMA will set high standards. As such, it must namely inform the investors and the audit firm in case of infringement to regulatory rules, and ensure remedy and compliance within an appropriate period of time.

The requirements applicable to the management company are intended to compensate the lack of FINMA supervision of the L-QIFs itself and safeguard the investors' interests.

Within this framework, the draft CISO foresees two types of audit: (i) a review of the annual accounts, based on the requirements applicable to supervised collective investment funds, and (ii) a complementary audit, verifying the compliance with other important requirements relating specifically to L-QIFs. Significant deficiencies are to be included in the audit report, so that FINMA is ultimately informed thereof.

6. Other CISO amendments

The draft CISO includes certain other amendments, some of which are indirectly linked to the L-QIF, while others are not, and most of which reflect established FINMA practice:

- (i) the specification of the legal definition of a collective investment scheme, with an express obligation of the entity in charge of the operation of the collective investment scheme (art. 7 CISA) to monitor at all times that these legal conditions are met;
- (ii) the reinstatement of a legal distinction between collective investment schemes and structured products, which will imply updating the product documentation;
- (iii) provisions on liquidity management, based on EU law: decision-making and operational bodies will need to implement corresponding measures, including stress tests, with a particular relevance for less liquid portfolios, including real estate or private equity funds;
- (iv) the creation of side pockets, subject to FINMA's approval: whereas the draft concedes a sufficient legal basis exists for that purpose, the key element will most likely be the measure's speed of implementation (in particular the obligation to require FINMA's prior approval and to notify investors and the audit firm);
- (v) long-awaited rules on Exchange Traded Funds ("ETF"): the new legal definition expressly allows for so-called "mixed funds", i.e. funds including ETF and non-ETF share classes; and
- (vi) an updated list of fees, which can be charged to open-ended funds: by contrast to the expectations of a large part of the industry, this list is still exhaustive.

7. Next steps and timeline

The consultation procedure is scheduled to end on December 23, 2022. The draft CISO thus remains subject to changes. The revised CISA and CISO are currently expected to enter into effect in August 2023 at the earliest.

8. Conclusions

The introduction in Switzerland of the L-QIF as a new form for collective investment schemes, without authorization and oversight of FINMA, is a long-awaited measure to increase the competitiveness and attractiveness of Switzerland as a financial center. The success of this new form of collective investments will, however, largely depend on how this new structure is implemented in practice in order to attract a number of not only institutional, but also private investors, who are qualified investors under CISA. Time will tell whether the L-QIF, and in particular the provisions of the proposed draft CISO ordinance, will provide sufficient flexibility to satisfy the investors' needs. It is expected that, in the course of the consultation procedure, certain provisions will be challenged by the industry with a view to keep the flexibility of the L-QIF (also bearing in mind the current tax treatment in Switzerland of collective investment schemes, which will apply mutatis mutandis to L-QIFs).

Please do not hesitate to contact us in case of any questions.

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