

# Update

## Newsflash July 2017

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### **Claims by clients for restitution of retrocessions received by financial intermediaries: the Swiss Federal Supreme Court rules in a leading case on the highly disputed question of the applicable statute of limitations.**

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#### **Introduction**

The issue of the status of retrocessions and similar financial arrangements perceived by financial intermediaries, e.g., banks, broker-dealers, portfolio managers, fund managers or distributors of financial products, gave rise to major legal controversies and significant court decisions during the last decade in Switzerland. In a series of well-known decisions starting as of 2006, the Supreme Court held that retrocessions paid to a financial intermediary acting as agent in connection with clients' assets were subject to a statutory restitution duty, meaning in practical terms that such retrocessions are, as a matter of principle, due to the client. The Supreme Court ruled that this restitution duty which derives from the existence of a mandate relationship between the parties is not mandatory and may be varied by the parties, provided, however, that certain conditions are fulfilled. In two subsequent decisions issued in 2011 and 2012, the Supreme Court further defined the requirements, in particular regarding the disclosure of the amount of the retrocessions, that are to be complied with in order for the

client to validly waive its right to restitution.

The principles defined by the Supreme Court, unlike a new legislative act – which would have applied only for future situations –, is an interpretation of the existing law which was accordingly of immediate and "retroactive" application. These decisions of the Supreme Court led banks and other financial intermediaries to adapt the terms governing their relationships with clients, be it for the future or to settle the past.

In that respect, the practical question that arose in situations where the right to restitution was not validly waived was for how many years back the client could claim the restitution of retrocessions received. From a legal standpoint, this raised two distinct questions: the duration of the applicable statute of limitations – five or ten years – and its starting date – the end of the mandate relationship or the reception of each payment. These two questions were left unresolved by the prior decisions of the Supreme Court which opened the door to abundant speculations and scholarly contributions.

The decision 4A\_508/2016 of 16 June 2017 which was published on the Supreme Court's website on 3<sup>rd</sup> July 2017 now answers these questions.

### **The Supreme Court Decision**

Between 1994 and 1995, an association mandated a brokerage firm for the purposes of developing and organizing an insurance system for its members. The brokerage firm concluded various contracts with insurance companies on behalf of the association.

In 2005, the association realized that the brokerage firm received undisclosed commissions from these insurance companies. The association immediately challenged their legitimacy and terminated the brokerage contract.

In 2007, the association filed a suit against the brokerage firm and claimed for the payment to it of the undisclosed commissions as a restitution of retrocessions. The Geneva judicial authorities considered that a ten years statute of limitations should apply to such claim and that the starting date was the termination of the contract. Therefore, the Geneva judicial authorities considered that the association's claim was not time-barred and ruled entirely into its favor.

On the brokerage firm's appeal, the Supreme Court had to determine (i) the applicable statute of limitations to a claim for the restitution of retrocessions as well as (ii) its starting point.

The Supreme Court had to determine first whether the retrocessions have to be considered as periodical fees or not. Indeed, periodical fees are subject to a five years statute of limitations whereas the ordinary statute of limitations is ten years. The Supreme Court held that retrocessions do not arise from a contract of duration and cannot be considered as periodical fees. Therefore, the claim for restitution of retrocessions is subject to a ten years statute of limitations. To that extent, the Supreme Court confirmed the Geneva judicial authorities' decision and disregarded numerous scholars' contributions supporting the opposite view.

The Supreme Court then considered the question whether the starting point of the statute of limitations corresponded to the termination of the brokerage contract (in the present case 2005) or to each individual payment received by the brokerage firm (in the present case between 1994 and 2005). The Supreme Court referred to Article 130 of the Swiss Code of Obligations according to which the limitation period commences as soon as an obligation falls due. It then held that the obligation of the agent to pass on the commissions to the principal fell due at the date of each individual payment of a retrocession to the brokerage firm. In this respect, the Supreme Court concluded that the statute of limitations started for each individual retrocession when received by the brokerage firm and not upon the termination of the contract only. Therefore, on this second issue, the Supreme Court partially granted the brokerage firm's appeal and overruled the Geneva judicial authorities' decision.

### **Comments**

As indicated above, the question of the applicable statute of limitations was hotly disputed and created significant legal uncertainties. The Supreme Court's decision puts an end to this controversy by holding that the longer ten years statute of limitations applies, but that the limitation period of the restitution claim for each individual retrocession starts when it was received by the agent, and not as of the termination of the mandate agreement.

Whereas the prior decisions of the Federal Supreme Court had a major impact and led numerous actors in the financial sector to significantly adapt their business model in terms of remuneration, this latest development is not expected to have the same impact. Because of the large publicity that was given to the prior decisions on the subject – including by the Swiss regulator FINMA – it can be assumed that banks and other financial intermediaries have by now adapted their approaches, either by renouncing to any form of retrocessions or by complying with the disclosure obligations imposed by the Supreme Court's precedents.

This notwithstanding, the decision of the Federal judges in favor of the ordinary ten years statute of limitations may be a source of concern for those actors in the financial sector that had not anticipated the legal developments deriving from the 2011 and 2012 decisions and only acted upon these decisions to make the necessary adaptations thereafter. To the extent that the Supreme Court has now held that claims for restitution of retrocessions are subject to a ten-year statute of limitations, this means that claims related to retrocessions received between July 2007 and such time as a client validly renounced to the restitution of retrocessions are not time-barred (as of today).

One question that arises is whether clients having accepted the revised regime as of the moment it was implemented should be deemed to have renounced to their claims for the prior period and which are not yet time-barred.

Due to the large publicity that was reserved to the prior decisions, it can be expected that the clients with the most significant potential claims have already asserted their rights at the time the new regime was being implemented. As regards clients who accepted to settle the past, even where assuming that a five-year statute of limitations would govern their claims, they should not be in a position to challenge such settlements and renegotiate their terms to the extent that the legal uncertainty was known to all parties and accepted by them.

Finally, it is to be noted that contrary to the MIFIDII regime, the forthcoming Swiss Federal Financial Services Act does allow for retrocessions, provided specific and detailed transparency and consent requirements deriving from the Swiss jurisprudence are met.

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

**Legal Note:** The information contained in this UPDATE Newsflash is of general nature and does not constitute legal advice. In case of particular queries, please contact us for specific advice.

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