

L-QIF: New Innovative Swiss Fund Structure – Final Rules Published

On January 31, 2024, the Federal Council has published the final implementing provisions to the Collective Investment Schemes Act ("CISA"). As a result, a new category of funds, reserved for so-called qualified investors under CISA, will be available to the Swiss asset management industry as of March 1, 2024.

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1. Introduction

On January 31, 2024, the Federal Council has published the final implementing provisions to the Collective Investment Schemes Act ("**CISA**"). As a result, a new category of funds, reserved for so-called qualified investors under CISA, will be available to the Swiss asset management industry as of March 1, 2024. As a reminder, the Limited Qualified Investor Fund ("**L-QIF**") is an innovative fund type which is exempt from any authorisation, approval and product supervision by the Swiss Financial Market Supervisory Authority ("**FINMA**"). It offers significant flexibility in terms of investment policy and restrictions. The ultimate goal is to increase the innovative capacity and attractiveness of the Swiss asset management market on the model of similar structures in foreign jurisdictions, such as the Reserved Alternative Investment Fund (RAIF) in Luxembourg.

In parallel, several other key changes have been introduced in the Collective Investment Schemes Ordinance ("**CISO**"), such as more flexible rules for Swiss and foreign Exchange Traded Funds ("**ETF**"), the launch of side pockets in case of illiquid assets or the creation of funds

targeting a limited number of investors.

For an overview of the key issues raised during the entire legislative process and the at times lively debates among Swiss asset managers on certain topics relating to the L-QIF, please refer to our previous Newsflashes of September 2019, April 2021, December 2021 and October 2022.

2. Key features of the L-QIF

- **Concept**

The key elements of a L-QIF are identical to those of any other collective investment scheme under Swiss law pursuant to Art. 7 CISA, with one key difference: no product authorisation or approval is required from FINMA to launch a L-QIF; as a consequence, there is no prudential product supervision by FINMA over L-QIFs. This does not result in the absence of any regulation, as an L-QIF remains subject to the provisions of CISA and CISO unless those are expressly disapplied pursuant to the lists set out in Art. 118d CISA and Art. 126f CISO, which include the waiver of investment restrictions under CISA, as well as any authorisation/approval procedure with FINMA for amendments of the fund regulations.

Similarly, an L-QIF will be subject to the Swiss tax regime applicable to collective investment schemes under Swiss tax laws. Also, the provisions of the Anti-Money Laundering Act ("**AMLA**") as well as, in respect of funds with real estate investments, the provisions regarding the acquisition of real estate by persons abroad (so-called "**Lex Koller**") remain applicable as for any other Swiss fund.

- **Absence of FINMA supervision**

While the L-QIF itself will not be subject to FINMA's prudential supervision, certain provisions of the CISO-FINMA on specific technical details will be relevant for L-QIFs, as explicitly stated in the CISO, such as for derivatives, securities lending or repo transactions as well as for accounting principles. The CISO further expressly states that certain AMAS self-regulation will also apply to L-QIFs, such as the AMAS Code of Conduct and the guidelines on the Total Expense Ratio ("**TER**").

In this context, the obligations of the custodian under Art. 72 CISA, in particular as to the safekeeping of the assets in custody and its control function, remain unchanged as compared to a FINMA supervised fund.

- **Investment restrictions**

The usual risk diversification rules and investment restrictions applicable to a regulated fund under CISA are disapplied for an L-QIF. L-QIFs are however obliged to define in their fund regulations the applicable investment restrictions. Also, Art. 126p CISO imposes specific limitations in terms of leverage, collateral or guarantees as well as in respect of the total exposure of the net assets of the L-QIF. Specific investment techniques, such as the use of derivatives, securities lending, repo or leverage must be set out in detail in the fund regulations. Additional restrictions apply to L-QIFs with real estate investments, namely as regards diversification rules (e.g. minimum number of real estate to be defined), the limitation of leverage to finance the real estate portfolio (max. 50%) as well as transactions with so-called "close persons".

- **L-QIFs for illiquid investments**

L-QIFs might be an appropriate form for alternative or infrastructure portfolios with illiquid investments, although generally not in the form of open-ended structures (i.e. L-QIF as contractual fund or SICAV). For alternative or infrastructure investments, an L-QIF in the form of a limited partnership for collective investments might be the appropriate legal form. Additional provisions will apply to such L-QIFs, such as an explicit risk warning.

- Audit and compliance

Considering the absence of FINMA supervision over L-QIFs, the CISA and in particular Art. 126h CISO imposes on the financial institution in charge of the administration and management of the L-QIF strict legal obligations, including the monitoring of the ongoing compliance with the CISA rules applicable to an L-QIF. In particular, Art. 126h CISO imposes a legal obligation to immediately inform the investors, the custodian (where applicable) as well as the auditors in case any of the legal restrictions applicable to L-QIFs under CISA are not complied with. We expect this to result in increased due diligence requirements to be applied by financial institutions acting as fund management companies or asset managers of L-QIFs, but also on the part of the auditors in case of the launch and operation of a L-QIF.

In line with the foregoing, the audit rules applicable to an L-QIF expressly provide for two types of audit, namely the review of the annual accounts, based on the usual requirements applicable to Swiss collective investment schemes, and an additional audit for the verification of the compliance with the specific requirements under CISA and CISO applicable to L-QIFs.

3. Other key changes

In parallel to the provisions relating to the L-QIF, the revised CISO introduces a number of material provisions applying to all Swiss collective investment schemes in Switzerland and, to a certain extent, to foreign funds registered for offering to non-qualified investors in Switzerland. The key changes are the following:

- Funds for a limited circle of investors

Following intense debates in the legislative process, the initially proposed restriction for so-called "family funds" has not been introduced. This means that members of the same family could meet the legal requirement of independence. This being said, Art. 5 para. 6 CISO expressly imposes an obligation to verify on an ongoing basis that the legal requirements applicable to a collective investment scheme under Art. 7 CISA are complied with. In this context, the Explanatory Report of the Federal Finance Department states that this includes an obligation to monitor that the requirement of a "collective investment" always be complied with for Swiss funds, including L-QIFs. This would seem to preclude collective investment schemes - whether in the form of an L-QIF or regulated fund - with only one investor, unless the specific conditions for a "single investor fund" are complied with. The requirement of "collective investment" presupposes indeed at least two independent investors. This would be in line with FINMA practice not to allow the launch of funds in circumstances where those are launched only for estate planning purposes or where the investors are organised within an estate.

- Active breaches of investment restrictions

The CISO introduces in Art. 67 para. 2bis a new liability for fund management companies and asset managers in case of active breaches of investment restrictions: In case the fund is not indemnified for the relevant damage, the breach must be immediately notified to the auditors and

has to be published. This new obligation is mitigated to the extent that, by contrast to the previous draft CISO provisions, a publication and notification can be avoided if the fund is indemnified for the loss resulting from such an investment breach.

- ETF

A material flexibility, which is key for the ETF industry in Switzerland, has been introduced. Art. 106 CISO now expressly includes in the definition of "Swiss ETFs" individual ETF shares/units of a fund. This will allow the launch, within Swiss index funds, of specific ETF share classes/units, as long as these share/unit classes are listed on one of the Swiss trading venues with the appointment of a market maker. The use of the name or a reference to the concept of an "exchanged traded fund" or "ETF" is only allowed if those units/shares are listed in Switzerland. Additional requirements apply as to the content of the prospectus for those ETF shares/ units, or for collective investment funds structured as ETF. New requirements will also apply for actively managed ETF.

New flexible rules will also be introduced for the offer of foreign ETFs to non-qualified investors in Switzerland pursuant to Art. 120 CISA. While the offer of those ETFs to non-qualified investors will still have to be approved by FINMA, it will be possible to have within such regular funds, such as index funds, ETF shares/units subject to the duty to list in Switzerland all ETF shares/units intended to be offered to non-qualified investors in Switzerland pursuant to Art. 127b CISO and to appoint a market maker. This will open significant new opportunities for foreign fund promoters, which wish to include within an index fund a number of specific ETF share/unit classes.

- New requirements for the management of the fund's liquidity

In line with international standards, Art. 108a CISO introduces the obligation for Swiss collective investment schemes to implement strict processes for the management of the liquidity of portfolios, including ongoing monitoring obligations, the obligation to proceed with stress tests, and the obligation to prepare for a crisis plan. This new obligation will be relevant, in particular, for less liquid portfolios, including funds with real estate investments.

- Side pockets

Art. 110a CISO introduces, namely as a result of certain recent global events as well as past experiences during the 2008-2007 financial crisis, the possibility to create so-called "side pockets". This will require that the Swiss fund regulations expressly provide in advance for the possibility to issue side pockets for illiquid investments and, once an illiquidity event occurs, that FINMA authorizes the issue of those side pockets with a corresponding publication to the attention of the investors. We expect this new flexibility to be important given that, so far, the launch of side pockets was not possible or subject to very restrictive terms.

4. Conclusion

The introduction of the L-QIF as well as of certain new key provisions in the CISO, such as the flexibility introduced for the offer of ETF in Switzerland, will certainly strengthen Switzerland as one of the leading asset management centres.

We expect the L-QIF to trigger a substantial interest among asset managers, mainly for the launch of alternative investment strategies as well as of infrastructure funds, digital assets portfolios or funds with real estate investment, or as a pooling vehicle for institutional investors with additional

flexibility as compared to regulated funds.

First projects are already being considered by the industry, not only for institutional investors, but also as a vehicle for sophisticated private investors. Time and the practical implementation of the new L-QIF rules will tell in particular for alternative and infrastructure portfolios, if this new form of fund meets the expectations of the industry.

Please do not hesitate to contact us if you have any further questions on this subject.

Legal Note: The information contained in this Smart Insight newsletter is of general nature and does not constitute legal advice.

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