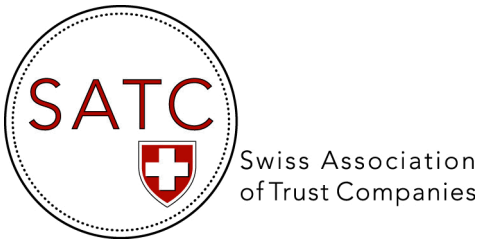

Swiss Association of Trust Companies

White Paper on the Regulation of Trustees in Switzerland

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CONTENTS

I. INTRODUCTION: THE REMIT OF THIS PAPER

This paper has been prepared at the request of the members of the Swiss Association of Trust Companies (hereinafter referred to as "**SATC**") and approved in the Annual General Meeting of SATC on May 31, 2012.

SATC was formed in 2007 and is a Swiss association including many of Switzerland's largest trust companies. At the inception of SATC, its membership had the combined intentions that the body should become the main representative body of the Swiss 'trust industry' and that it should promote the reputation of the Swiss 'trust industry' by ensuring that an appropriate standard of professionalism exists against which professional trustees in Switzerland may be judged.

Any discussions in respect of the proposed regulation of the Swiss 'trust industry' are seen by SATC as an opportunity to participate and contribute to the characteristics of the Swiss 'trust industry'. Through this paper, SATC wishes to contribute to such discussions. SATC sees regulation as one of the main paths to promote the credibility and standing of Swiss trustees and the Swiss 'trust industry' in the international wealth management arena.

Since it was formed SATC has been reviewing and developing its stance on regulation. This paper represents the agreed position of the SATC membership.

In producing this paper, existing regulatory regimes of many trust jurisdictions throughout the world have been considered and this position paper draws on these regimes and the views of experts in the trust field, including all members of the SATC Advisory Board[1]. SATC has also taken note of the suggestions made and positions taken by various interested bodies, most notably the Society of Trust and Estate Practitioners ("**STEP**"), the Offshore Group of Banking Supervisors ("**OGBS**") and the OECD-administered Financial Action Task Force ("**FATF**")[2].

II. THE 'KEY QUESTIONS' TO BE ADDRESSED IN THE PROCESS OF CONSIDERING A REGULATORY REGIME

SATC has investigated and answered the following five "key questions". In SATC's view, the resolution of these questions is central in reaching a position on the proposals for a regulatory regime of the Swiss 'trust industry'.

1. **What should the aim or aims of a proposed regime be?** (See Section V for discussion.)
2. **To what activities and entities should a regulatory regime apply?** (See Section VI below for discussion.)

[1] Richard Pease, Verena Kubitz, Edgar H. Paltzer, Stephanie Jarrett and Prof. Dr. Dominique Jakob.

[2] However, this paper and the conclusions to which it comes are not made in collaboration or conjunction with these or any other groups or bodies. SATC welcomes comments and contributions that this paper may encourage. Please send these to SATC email: info@satc.ch

3. **How should a regulatory regime interact with existing regulation** (for example, anti-money laundering regulation and/or banking regulation)**?** (See Section VII below for discussion.)

4. **Should a Swiss law in respect of trusts be enacted?** (See Section VII below for discussion.)

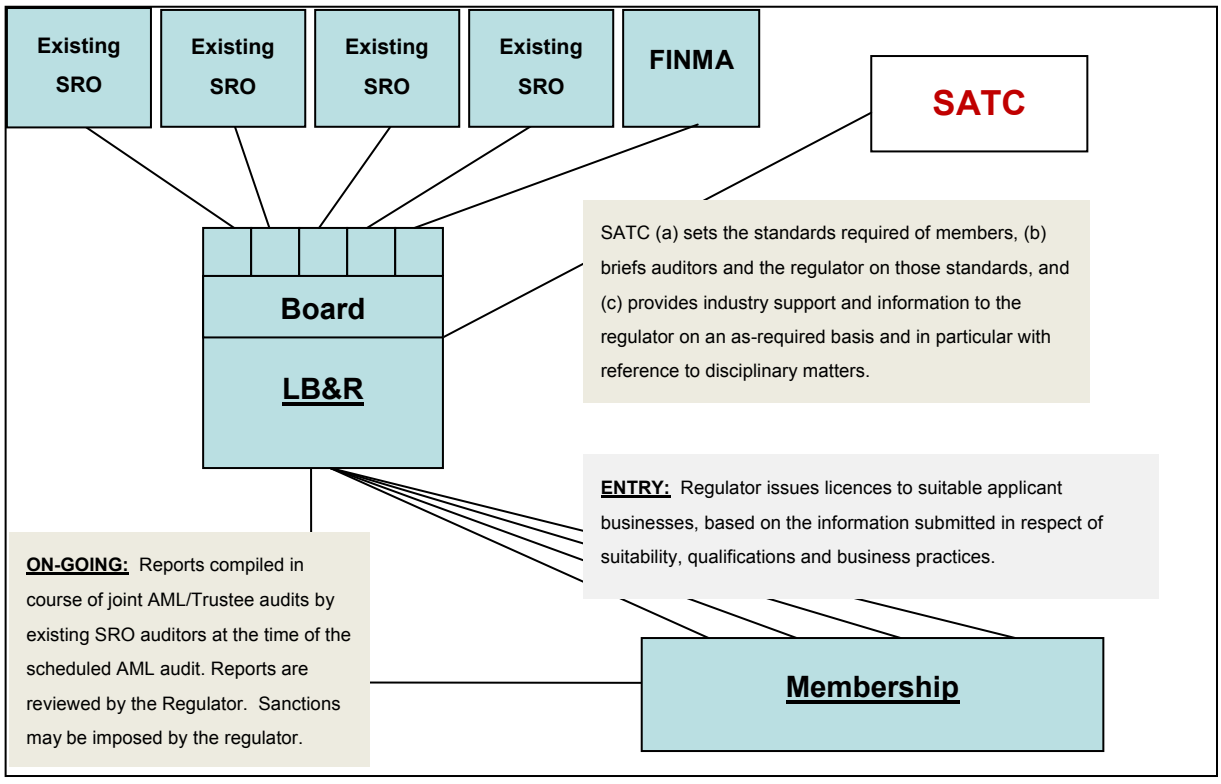
5. **Who should be the licensing body and regulator ("LB&R")?** (See Section VIII below for discussion.)

III. APPROACHES TAKEN BY OTHER 'TRUST INDUSTRY' JURISDICTIONS

"Annex A" hereto sets out a summary of the regulatory systems of seven trust jurisdictions with trust industries that might provide some indicators for Switzerland (Cayman Islands, Isle of Man, Guernsey, Jersey, New Zealand, Singapore and the United Kingdom), and provides an analysis of the methods and extents of regulation in each case. In responding to these questions consideration has been given to the characteristics of each of these regimes and the potential for similar regulatory requirements to be adopted in the Swiss 'trust industry'.

IV. THE PROPOSED INITIAL REGIME FOR THE REGULATION OF THE SWISS 'TRUST INDUSTRY'

The following diagram outlines the initial regulatory regime of the Swiss 'trust industry' that is proposed by SATC.



SATC proposes that all entities covered by the proposed regulatory regime in Switzerland be required to obtain a licence from the regulatory body.

This White Paper describes more fully this proposal and this Section IV now provides a summary of it.

- Upon a trust company's initial application for a licence to conduct regulated activities in Switzerland, information contained in the licence application and its supporting documents would be reviewed with a view to issuing a Swiss Trustee Licence (hereinafter referred to as a "**Trustee Licence**"). The Trustee Licence will confirm that, on the basis of the information supplied, the licence holder satisfies certain standards (hereinafter referred to as "**Standards**") at the date of the issue of the Trustee Licence[3].

- On or before the second anniversary of the issue of a Trustee Licence, a licence holder would be subject to its first audit (concurrent with its usual anti-money laundering ("**AML**") audit) by an existing SRO acting in conjunction with the LB&R. The purpose of such audit shall be to confirm that the licence holder has maintained the Standards required for the issue of a Trustee Licence. If the first audit shows that a licence holder has failed to maintain the required standards, the LB&R may impose sanctions.

- Licence holders shall be subject to further LB&R audits at a frequency to be fixed by the LB&R, initially, SATC would suggest, at the same frequency and to coincide with the scheduled AML audit. If such an audit finds that the standards with which a licence holder provides regulated activities has fallen below the Standards the LB&R may impose sanctions.

- The framework and content of the LB&R audits as well as the scale of sanctions will be one of the first tasks of the LB&R after its formation. It is contemplated that sanctions might include the imposition of further or more frequent audits, suspension of the Trustee Licence, and, in the most serious cases, withdrawal of the Trustee Licence.

SATC proposes that the extent of the sanctions available to the LB&R and the circumstances should be such that they provide the necessary incentives and motivation for trustees operating in or from Switzerland to maintain high standards consistent with the SATC code of conduct.

V. KEY QUESTION 1: OBJECTIVES OF A REGULATORY REGIME

SATC considers that, in order to consider the key questions set out above and to provide answers, it is important to be mindful of the objectives of the proposed regulatory regime. It is SATC's position that any regime regulating trustees in Switzerland must focus on three primary objectives:

- First, by ensuring that trustee activities are carried on only by fit and proper persons having due regard to the applicable laws of, and the interests of all appropriate parties to, each trust under such persons' trusteeship and in accordance with industry standards, creating a secure framework for the protection of beneficiaries and thereby the reputation of the Swiss 'trust industry' as a whole. As a key element of the overall

[3] Such MSs are more particularly described in Annex B hereof

Swiss wealth management offering, this is of vital interest for Switzerland's Financial and Banking Services sector.

- Second, the maintenance by trustees of appropriate records for the purposes of trustee regulation, satisfaction of existing anti-money laundering requirements and the protection of beneficiaries, whilst all the while protecting individuals' legitimate expectations of confidentiality in respect of their financial affairs.

- Third, the harmonisation of regulation with existing regulatory requirements (for example, AML requirements and the regulation of banks) so as to ensure a full and credible regulatory regime whilst not adding to the burden of the Swiss 'trust industry' unnecessarily.

In respect of the first objective (protection and standards), SATC would propose that this may only satisfactorily be achieved by implementing a trustee-licensing system, under which trustees would be subject to appraisals by the regulatory body in respect of personal suitability (i.e. 'fit and proper'), appropriate qualifications and satisfactory business practices.

In respect of the second objective (record-keeping), SATC would propose that this may only be effectively regulated by the introduction of an audit-type review. SATC would propose that the honouring of confidentiality expectations should persuade against a South African-type 'register' model, in which the information in respect of beneficial ownership, trust assets and settlors etc. is publicly available.

In respect of the third objective (harmonisation), SATC would propose that no overlap in AML procedures should exist, and that trustee regulators should rely on the existing AML regime for such matters. SATC would suggest the LB&R as an appropriate vehicle to develop and promote the LB&R audit, carried out by the existing SRO at the time of its AML audit, as a coordinated and non-duplicative procedure. This should address any concerns about additional audits in the already heavily regulated wealth management sector in Switzerland.

VI. KEY QUESTION 2: PROPOSALS IN RESPECT OF THE SCOPE AND REACH OF A REGULATORY REGIME

One of the key questions to be decided is the scope of any regulatory regime. Which participants in the Swiss 'trust industry' should be included? Which activities of those participants are to be regulated?

The Swiss 'trust industry' incorporates more parties than merely those entities whose business is acting in the capacity of professional trustee. For example, the business of the professional trustee in Switzerland is often linked with the businesses of corporate formation, corporate services provision and nominee share and asset holding. In addition, Switzerland is naturally exposed to a number of 'alternative' estate planning entities or arrangements, which may be used as alternatives or in addition to trusts in wealth and estate planning[4].

[4] For example, Foundations, Treuhand, Fiducie, Fideicomisos, Trust regs, Partnerships, Private funds

FATF included a useful definition of "Trust and Company Service Providers" in the glossary to its "*40 recommendations*" in respect of anti-money laundering control:

> "*Trust and Company Service Providers refers to all persons or businesses that are not covered elsewhere under these Recommendations, and which as a business, provide any of the following services to third parties:*
> - *acting as a formation agent of legal persons;*
> - *acting as (or arranging for another person to act as) a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons;*
> - *providing a registered office; business address or accommodation, correspondence or administrative address for a company, a partnership or any other legal person or arrangement;*
> - *acting as (or arranging for another person to act as) a trustee of an express trust;*
> - *acting as (or arranging for another person to act as) a nominee shareholder for another person.*"

This has become a central notion in AML regulations and there would be some harmony in adopting the same cornerstone for the regulation of trustees in Switzerland. It would follow then that the services that may be regulated under the above definition are trustee services and the additional services naturally included in the FATF definition of "Trust and Company Service Providers".

Although this definition encompasses the business areas comprised in or frequently linked with the 'trust industry' in Switzerland, for the initial development of a regulatory regime, SATC considers that the applicable definition should be narrowed to exclude corporate services. Therefore, SATC proposes to adopt the expression "Trust Service Providers" (hereinafter referred to as "**TSPs**") throughout this paper.

SATC would envisage that an extension to the reach of this definition would later be possible, and may ultimately be necessary to avoid distortions in trust-related services provided in or from Switzerland.

The activities that would potentially require a Trustee Licence would be offering to act as trustee in or from Switzerland. For the purposes of this paper we refer to all such activities as "**TSP Regulated Activities**".

Initially, SATC proposes that a single regulatory regime be adopted for TSPs conducting TSP Regulated Activities in or from Switzerland and that only TSP Regulated Activities are included within the regulation, without however excluding the possibility of later expansion to other services potentially encompassed in the FATF definition of Trust and Company Service Providers.

SATC has identified several areas of uncertainty in respect of the precise applicability of a TSP regulatory regime. In particular the applicability of such a regime to individuals and to family offices. Bearing in mind the third objective (harmonisation), SATC would propose that the scope of the regulatory regime should, at least initially, only extend to TSPs who are "financial intermediaries" within the meaning of Article 2 of the Swiss *Anti-Money Laundering Act*. All such financial intermediaries are subject to AML audit by an existing SRO or the FINMA.

In conclusion then, SATC proposes that any TSP's conducting TSP Regulated Activities who are also financial intermediaries under the Swiss Anti-Money Laundering Act should be required to hold a Trustee Licence if they wish to operate in or from Switzerland.

VII. KEY QUESTIONS 3 and 4: INTERACTION WITH EXISTING REGULATORY REQUIREMENTS

A. Risk v. cost considerations

It has been suggested that most trust jurisdictions support a risk-based approach to regulation – that is, an approach in which the risk posed for various activities is balanced against the cost incurred for regulation[5]. STEP has stated that it too supports this approach[6].

SATC would therefore propose that any regulation of TSPs must be cost effective in so far as it achieves its stated objectives without excessive or inappropriate levels of monitoring on the part of the regulator. The harmonisation of the proposed regulatory regime with the regulation already undertaken in respect of TSPs is a central concern and SATC feels strongly that successful regulation must eliminate any overlaps between the requirements of other regimes (most notably AML and financial services regulation).

B. AML: No changes to existing procedures proposed

At present, TSPs come within the definition of "Financial Intermediaries" for Swiss AML purposes[7]. We would not propose to change the manner in which TSPs are regulated for AML purposes, as current AML procedures are well established and functioning smoothly. The present AML regime covering Swiss TSPs requires audits to be carried out by FINMA or an SRO at varying but regular intervals.

SATC would propose that the continuing satisfaction of AML requirements be incorporated by the LB&R as an ongoing regulatory requirement for TSPs. Satisfaction of this requirement would be measured on the basis of the AML audit report of the relevant AML regulator (FINMA or an existing SRO).

C. Register of Trusts: No proposal to establish a register of trusts in Switzerland

SATC strongly opposes a register of trusts being implemented in Switzerland.

SATC has noted that almost all 'main' trust jurisdictions employ an 'investigative' approach to trust regulation, rather than a 'register' approach. The most notable exception to this rule is South Africa. SATC has noted that the STEP Policy Briefing of October 2010 on trust regulation[8] expressed reservations about the reliability of information contained in South Africa's register of trusts. It is

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[5] Page 7, STEP Policy Briefing of October 2010

[6] Ibid

[7] Article 2[3], *Federal Act on Combating Money Laundering and Terrorist Financing in the Financial Sector 1997*

[8] Page 6, STEP Policy Briefing of October 2010

suggested therein that the legitimate concerns of interested parties in respect of confidentiality and use of information in jurisdictions maintaining registers of trusts are the registration of ambiguous, inaccurate or incomplete information.

The same STEP Policy Briefing quoted FATF's suggestion that "*it matters less who maintains the required information…provided that the information on beneficial ownership exists, that it is complete and up-to-date and that it is available to competent authorities*"[9].

It was further noted in the abovementioned STEP Policy Review that it is likely that "*the costs of ensuring a comprehensive regular audit of registered information would be significant*"[10] and that the monitoring of new and old information entered in the register might be a practical impossibility.

SATC proposes that the present requirements to which TSPs (alongside all other financial intermediaries and banks in Switzerland) are subject in respect of their AML obligations will satisfy in the appropriate situations any need for the provision of up-to-date information on beneficial ownership and sources of funds, without compromising individuals' legitimate expectations of confidentiality in respect of their financial affairs.

D. Introduction of a Swiss law of trusts not proposed

In respect of trust arrangements, Switzerland is unique amongst the significant trust administration jurisdictions in that it has not enacted a law of trusts. The proper administration of trusts in Switzerland therefore relies upon the provisions of the trust laws of other jurisdictions, which are the designated proper laws of trusts administered by Swiss TSPs. In the event that a Swiss TSP breaches the requirements of a settlement's proper law, subject to the terms of the trust deed, action against that TSP may be brought in the Swiss courts or in the courts of the proper law, who would seek to apply the terms of the proper law as appropriate.

SATC does not propose that a Swiss law on trusts is necessary or desirable. SATC would propose that Switzerland may grow its own 'trust industry' by marketing itself as a jurisdiction providing high standards of trusteeship, unparalleled expertise in the field of wealth management, due protection of individuals' rights to confidentiality within the boundaries of international laws and – under these proposals – a unique and effective regime of regulation. In due course, rather than introducing its own law on trusts, it should assist the Swiss 'trust industry' to develop a statutory procedure for resolution of trust disputes, which could include some statutory support for arbitration and/or mediation of trust disputes.

However, SATC does consider that a meaningful regulatory regime must be supported by the force of law. The LB&R, as an intermediate step, is a step in the right direction and should provide the platform to fill any knowledge gap in Swiss institutions concerning trusts and trustee regulation through the combined efforts of existing SROs, FINMA and SATC. Ultimately however SATC believes that a governmental agency, such as the FINMA should be designated or established to oversee the regulatory process in respect of TSP Regulatory Activities and to wield the ultimate regulatory powers and sanctions.

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[9] Ibid, quoting FATF Typologies Study, "*The Misuse of Corporate Vehicles, Including Trust and Company Service Providers*" FATF October 2006

[10] Ibid, page 7

VIII. KEY QUESTION 5: WHO SHOULD REGULATE THE PROPOSED REGIME?

A. Entry level regulation

SATC suggests that, ideally, the body tasked with the examination of applications and the issuance of Trustee Licences should be one that is formed by FINMA specifically for the purpose.

However, SATC understands that, for the time being, FINMA is unlikely to be willing to put such a body in place for these purposes. If this is so, SATC would propose to establish an alternative regulatory body, together with the existing anti-money laundering SROs regulating Swiss based trustees and, so far as possible, the involvement and/or support of FINMA.

SATC believes that this may, in any event, be a sensible intermediate step, to help bridge the perceived knowledge gap in Swiss institutions concerning trusts and trustee regulation. It should also help in meeting the coordination objective through cooperation with existing SROs (should they agree to participate; SATC notes that only a number of existing SROs are likely to be interested in participating, in particular those with regulatory functions across a range of sectors including the TSP sector). The ultimate goal however, should be to preserve, so far as possible in the present circumstances, a credible degree of independence and neutrality.

The LB&R would be an SRO formed specifically for the purpose of issuing licences and supervising licensees with the authority and support of FINMA.

The involvement of FINMA should provide an immediate credibility to the regulatory regime and would raise the profile of the Swiss 'trust industry' in the international wealth management arena. SATC considers that material direct government involvement of any kind would be invaluable for these purposes.

In practical terms SATC intends to approach FINMA and the existing SROs with TSP members with the intention of creating the LB&R. The LB&R would have the existing SROs and possibly FINMA as members, as well as SATC. The members would be invited to participate in the board of the LB&R. It would also be canvassed whether a FINMA representative might join the board either as board member or observer. As such it would be an intermediate body which would become permanent or move under the full control of FINMA after an intermediate phase. The Existing SROs would be asked, as a condition of membership, to add a layer of TSP regulation, as devised by the LB&R, to the AML audits that they presently undertake.

Initially, the LB&R would have a key role consulting with Existing SROs, FINMA, SATC and its members and other interested parties to develop and agree the framework and content of the application for a trustee licence, the framework and content of the LB&R audit and the system and content of sanctions.

After the initial development phase the role of the LB&R would be restricted to

- granting Trustee Licenses;

- liaising with the existing SROs in connection with the grant of Licences and the conduct of LB&R audits;
- undertaking the supervision of TSPs (including the review of audit reports) and enhancement of the procedures developed during the initial phase;
- conducting any investigations and/or disciplinary procedures;
- determining the content and management of information services to TSPs and generally concerning Swiss trustee regulation.

At least during the initial phase, it is contemplated that SATC and its members will have an important role in supporting the LB&R with input and assistance concerning the Swiss 'trust industry' and trusts and trustee regulation.

B. The process of ongoing regulation

It is proposed that SATC should have a role in the ongoing regulation of the Swiss 'trust industry' and that such role should be in the setting and review of standards and in the education of the auditors given the task of reviewing TSP businesses (the TSP part of the LB&R audit).

SATC is in a unique position to understand the services and the reputation that the Swiss 'trust industry' seeks to cultivate within the international marketplace and it is the most appropriate body to understand the ongoing regulation of its own members and to set the minimum standards that Swiss trustee regulation should accept.

However, SATC considers it essential to the overall credibility of the regulation that regulatory power should remain with LB&R, which will be aided and influenced also by the Existing SROs and possibly, depending on its involvement, FINMA.

The model of regulation of an industry through licensing with FINMA involvement (or through an SRO overseen by FINMA), with the requisite industry standards being set by an appropriate industry representative body, is a model already known in Switzerland. A similar model is employed in the banking sector, in which FINMA licences and supervises banks, although the Banking Association sets the industry standards that are to be complied with. As mentioned earlier in this paper, it remains SATC's preferred position that LB&R would ultimately be under government control, for example, as part of FINMA.

C. Extraordinary/disciplinary regulatory activity

SATC holds that LB&R should have absolute discretion in respect of the suspension or withdrawal of Trustee Licences. SATC proposes, however, that LB&R should not act in an active investigatory capacity in this respect, but should instead rely upon the results and advice of the Existing SROs in respect of suspected occurrences of malpractice as determined by LB&R audits.

SATC further proposes that the LB&R should have power to act in respect of TSP Regulated Activities being conducted by non-licensed entities. However this would require statutory support empowering the LB&R to impose sanctions and is therefore unlikely, at least during the initial phase, and probably until there is some political support for LB&R as the industry regulator.

IX. APPROACH TO REGULATION: MAINTENANCE OF STANDARDS

A. Regulation Step 1: "Entry Licensing Process"

1. The regulating body: LB&R

As anticipated above, SATC would propose that the LB&R should oversee the initial process of reviewing applications and issuing Trustee Licences to suitable applicant businesses.

2. The process of Regulation Step 1 / Entry Licensing Process

SATC proposes that no entity would be permitted to conduct or to market itself in respect of any TSP Regulated Activities before it has been issued with a Trustee Licence by LB&R.

Initially, the LB&R's role will depend on voluntary submission by market participants. In due course, it is SATC's hope that this would be given force of law requiring all financial intermediaries providing TSP Regulated Activities to hold a Trustee Licence.

SATC proposes that Trustee Licence applications are made by lodging a standard application form with LB&R. The application form would require specified information on the entity, its owners, its management, its activities and its AML regulatory procedures and supporting documentation. In effect, the form for applying for SATC membership probably only needs minor adaptations for use as the standard application form. The analysis of the information in these forms would be carried out by the Existing SRO of the relevant applicant acting under delegation from the LB&R in respect of the licence application.

The current entry requirements for SATC membership provide a good starting point when considering the standards that TSPs in Switzerland should be expected to maintain. Switzerland's financial services industry has a strong reputation for professionalism in the international community, and the SATC entry requirements were drafted to reflect this. As mentioned earlier, SATC would accept the role of standard setter and reviewer for LB&R on an ongoing basis.

The present requirements include (a) entity registration in Switzerland, (b) the maintenance of operative offices within Switzerland, (c) minimum capitalisation of CHF 100,000, (d) a minimum of three employees carrying out their employment within Switzerland and having appropriate experience, (e) observance of the "four eyes" principle, (f) appropriate insurance cover, and (g) a clean AML record.

SATC would propose that all existing SATC members would automatically be granted a Trustee Licence. If material additional requirements are added to the application, rather than following the present SATC forms, these Trustee Licences could be issued under a simplified procedure requiring existing members to demonstrate the additional requirements, if any. Such an approach would have the merit of speeding up the launch of the new regime and lightening the burden of the new LB&R in the initial phase. Such licence holders would however be subject to the LB&R audit and supervision.

B. Regulation Step 2: Continuing regulation requirements after entry: The first audit

1. The regulating body

LB&R would oversee the scheduling and conduct of LB&R audits. The review of the audit reports would be a key competence of the LB&R board.

As mentioned earlier, SATC would assist through training of AML auditors given the additional task of reviewing TSP business in an LB&R audit.

2. The process of Regulation Step 2 / The first audit

(1) Management of Existing SRO auditors

SATC would have a role in assisting the Existing SROs in respect of this new regulation of TSPs and the required standards.

To this end SATC would develop a program of education in conjunction with Existing SROs.

SATC might also provide ongoing support and advice to Existing SROs in respect of questions that may arise in the course of audits, at least in the early stages.

(2) The first audit of a TSP

On or before the second anniversary of a TSP's being granted its Trustee Licence, an Existing SRO will undertake the first LB&R audit at the same time as the scheduled AML audit. The purpose of such an audit would be to confirm that the TSP has maintained the Standards as required by the conditions of issue of the Trustee Licence.

Provided that a TSP is able to satisfy the requirements of the Standards at the first audit, it will thereupon, if not already a member, be entitled to apply for automatic membership of SATC. Nothing would however prevent the TSP from applying for SATC membership in the ordinary way. Whether or not it decides to take up such automatic SATC membership, the TSP will subsequently be subject to further LB&R audits at a frequency determined by the LB&R.

If a first audit shows that a TSP has not maintained the Standards, there should be due process under the auspices of the LB&R, which may result in sanctions being imposed (for example, additional auditing requirements).

C. Regulation Step 3: Continuing regulation requirements after entry

1. The regulating body

The same bodies would oversee the continuing regulatory process. LB&R would arrange and oversee the auditing process through Existing SROs. SATC would have the task of further standard setting and assisting Existing SROs to understand the required standards and LB&R the responsibility for assessing the audit results and subsequent action.

2. The process of Regulation Step 3 / regular audits

After the first audit, SATC proposes that TSPs should be subject to further audits by an Existing SRO at regular intervals, for example, each time there is a scheduled AML audit by the TSPs Existing SRO.

X. APPROACH TO REGULATION: ADVISORY AND SUPPORT

A. Advisory and support role of SATC

In addition to its role as standard setter, SATC would have the important function of providing advice and support to TSPs in respect of Trustee Licence applications and, understanding and compliance with this new form of regulation in Switzerland.

B. No pre-clearance

However SATC would not seek to offer any form of pre-clearance service which SATC believes is beyond the remit and powers of SATC.

XI. APPROACH TO REGULATION: DISCIPLINARY PROCEDURES

A. Regulating body

As mentioned earlier in this paper, LB&R should have absolute discretion in respect of sanctions, including in the most serious cases, the withdrawal of Trustee Licences.

B. The process of Discipline Procedures

1. Investigation of a complaint: LB&R

LB&R should be the nominated body for the purposes of receiving complaints in respect of any licensed trustee. Such complaints may arise out consideration of the LB&R audit or from third parties.

When LB&R receives a complaint it should first conduct an analysis of that complaint with reference to the SATC Code of Conduct and the Standards and reach its decision. In so going, LB&R might rely on the support and guidance of SATC in determining accepted practice under the SATC Code of Conduct. In the case of a third party complaint, any decision may be suspended to a further LB&R audit, if the LB&R finds this to be necessary.

2. Referral of a report to SATC and imposition of sanctions: LB&R

Should LB&R refer to SATC for confirmation of the correct application of the SATC Code of Conduct, it should be on the basis that it is not bound to follow any recommendations of SATC. LB&R should however explain its reasons for not doing so to SATC, so that SATC can consider such cases when considering enhancement of the SATC Code of Conduct.

3. Appeals against decisions of the Regulator

Annex C contains appeal and arbitration procedures that might be implemented to afford due process to a TSP who disagrees with a decision of the LB&R.

XII. CONCLUDING STATEMENTS

A. On the concept of regulation

- A regime of regulation of the 'trust industry' in Switzerland would be to the advantage of Switzerland and its TSPs.
- Any regime implemented must include sanctions if it is to be credible in the international wealth management arena.
- The use of SROs as a common form of regulation in Switzerland has proven successful and should be used as a template for the regulation of the Swiss 'trust industry'.
- A system of compulsory licensing provides the regulator with a simple method of sanctioning poorly performing TSPs, whilst also benefiting TSPs by providing them with evidence that they meet the required standards in their conduct as TSPs. If ultimately the regulation of TSPs in Switzerland is considered to meet international standards, this may assist Swiss-based TSPs in obtaining licences elsewhere on the basis that there is comparable regulation in both jurisdictions.
- Ongoing regulation is necessary to maintain the credibility and effect of the Licensing process.

B. On the form of regulation

SATC believes that the regulatory regime outlined by this paper would achieve the stated objectives.

C. On the body or bodies to regulate

SATC would prefer a regulatory system which is developed and implemented under the auspices of the Swiss financial regulator, FINMA. Further to SATC's consultation of interested parties it appears likely that there will not be the political appetite for such an approach for the time being. However SATC is firmly of the view that delaying regulation will only be negative for the Swiss trust industry. Foreign counterparts and the trust market expect and require regulation of trustees. SATC believes that there are also legitimate concerns about how to regulate trustees given the absence of the trust as an institution in Swiss law. Bearing this in mind as well as the further particularity of the Swiss regulatory landscape which is to rely on Self-Regulatory Organisations, SATC is proposing the LB&R, a hybrid SRO and regulatory framework pitched somewhere in between the SRO system historically embraced by many of Switzerland's financial and professional industries and the governmental system used by many other jurisdictions.

Such a hybrid system would present a regulatory process that was understandable, manageable and practical in the present environment of Swiss professional and financial industries whilst giving a suitable degree of credibility and gravitas to the system in the eyes of foreign jurisdictions and markets.

* * *

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ANNEX A: Existing regulation in selected jurisdictions: A comparison of perceived strengths and weakness

Part 1

Existing regulation in selected jurisdictions: A comparison of perceived strengths and weakness[11]

Cayman Islands

The Cayman Islands introduced the *Banks and Trust Companies Law 1995*, which imposed a regime of licensing for companies providing trust services. This statute was subsequently amended in 2001 and again in 2003, and was then revised in 2007. Consequently, the provision of trust services is a regulated activity in the Cayman Islands, and is subject to corporate due diligence and record-keeping requirements amongst others. TSPs in the Cayman Islands are therefore required to be licensed to carry on such business, and 278 trust and corporate services providers were so licensed as at October 2010[12].

There now exists three categories of trustee licence, which are as follows:

- "Trust Licences", which cover the provision of trust services both within and outside of the Cayman Islands, subject always to any conditions that may be imposed by the Cayman Islands Monetary Authority.

- "Restricted Trust Licences", which cover the provision of trust services but subject always to the restriction that the licensee may not undertake trust business for persons other than those listed in any undertaking accompanying the application for the licence;

- "Nominee (Trust) Licences", which cover the provision of trust services under a Trust Licence to a licensee which is a wholly-owned subsidiary of another licensee and where the sole purpose of that subsidiary is to act as its nominee.

All categories of trustee licence have minimum capital requirements: The Trust Licences require a minimum net worth of USD400,000, whereas Restricted Trust Licences and Nominee (Trust) Licences require a minimum net worth of only USD20,000. In the latter case, the parent of a nominee trust company must provide a guarantee of not less than USD200,000.

There is no requirement for licensees to be Cayman companies, but foreign licensees may expect to provide a 'head office guarantee'. However, all companies holding any type of trustee licence must have a place of business in the Cayman Islands (approved by the Cayman Islands Monetary Authority), and must have two individuals resident or a body corporate incorporated (again approved by the Cayman Islands Monetary Authority) in the Cayman Islands. Any trust licensee incorporated in the Cayman Islands must submit annual audited accounts to the Cayman Islands Monetary Authority.

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[11] As found by the STEP Policy Briefing, "*Trust Reporting Systems – An International Comparison*" STEP October 2010

[12] Page 60 (Annex, Table 2), "*Money Laundering Using Trust and Company Service Providers*" FAFT/OECD and CFAFT October 2010

TSPs are subject to ongoing monitoring and supervision by the Cayman Islands Monetary Authority. Such ongoing monitoring includes prudential and AML reviews, onsite and offsite audits and reviews of audited financial statements.

The broad approach to trust monitoring in respect of AML matters in the Cayman Islands is based upon the investigative powers of the local authorities, using information provided by regulated trust service providers. Trust service providers are provided with guidance in respect of the due diligence required of them in respect of settlors, settled assets and beneficiaries. The local regulatory and law enforcement authorities are able to access information on trusts that are maintained by licensed trust service providers. In November 2007, a FATF-coordinated peer review of the Cayman Islands found that the jurisdiction was "compliant" in respect of AML and anti-terrorist funding procedures recommended by FATF[13].

Isle of Man

Since 2005, trustees have been licensed and supervised (in respect of services other than business in investment, banking or insurance, which were licensed activities previously) by the Isle of Man's Financial Supervision Commission. Most trust providers are required to be licensed, although an exception is made where trust service providers act as a trustee for less than ten legal arrangements.

The *Fiduciary Services Act 2005*, added to the *Corporate Service Providers Act* 2000 so as to require persons to hold a fiduciary licence if they conduct a business providing certain services to trusts and partnerships or act as nominee holders of units in unit trusts. The initial application for a licence will invite the Isle of Man's Financial Supervision Commission to examine whether the applicant is a "fit and proper" person to hold such a licence. This adjudication will be monitored on an ongoing basis. The assessment is carried out in respect of controllers (that is, beneficial owners), directors and key personnel (which includes managers and other persons who appear to have significant powers and responsibilities).

In order to assess the competence of the trust company, individuals in the business are required to hold appropriate levels of qualification and/or appropriate experience. Any doubts of the Isle of Man Financial Supervision Commission in respect of an individual's competence may result in a meeting in order to test that individual.

A licence holder is also generally expected to be able to meet the "four eyes" principle.

Alongside the *Fiduciary Services Act 2005*, the Isle of Man's Financial Supervision Commission updated its Fiduciary Services Regulatory Codes. By way of a program of simplification of the licensing system, the *Fiduciary Services Acts 2001* and *2005* have subsequently been consolidated into the *Financial Services Act 2008*.

A beneficiary of a trust with Isle of Man trustees may apply to the court to stop a trustee from dealing with trust assets in an unauthorised manner. Loss as a result of unauthorised conduct will result in the trustee being responsible for making the loss good. The asset value of the trustee is therefore an important consideration.

[13] "*40 Recommendations*" FATF October 2003, and "*9 Special Recommendations*" FATF October 2001

Where a breach of trust is committed by a corporate trustee, every person who at the time of breach was a director of the trustee may be deemed, in certain circumstances, to be guarantor of the trustee (i.e. personally liable) in respect of damages awarded by the court. Principles of constructive trusteeship also apply.

The broad approach to trust monitoring in respect of AML matters in the Isle of Man is also based upon the investigative powers of the local authorities. Some concerns exist that measures do not exist in respect of the requirements for AML purposes of trust service providers that are exempted from licensing. The September 2009 FATF peer review of the Isle of Man found the jurisdiction to be "largely compliant".

Jersey

Under the *Financial Services (Jersey) Law 1998*, all professional trustees (wherever incorporated) are required to register with the Jersey Financial Services Commission, upon which they will be issued with a licence provided they are deemed to be compliant with the requirements laid down by the Jersey Financial Services Commission. As at October 2010, 182 TSPs were registered in Jersey[14].

'Principal persons' are required to provide evidence on a "fit and proper" appraisal, and the Jersey Financial Services Commission will assess whether the 'principal persons' satisfy the qualification and experience criteria set out in the *Trust Company Business Codes of Practice*.

TSPs in Jersey are subject to ongoing monitoring and supervision by the Jersey Financial Services Commission, such monitoring including prudential and AML reviews, onsite and offsite audits and reviews of annual submissions. The Jersey Financial Services Commission carries on 'desk-based' monitoring (including risk assessments of regulated businesses) as well as onsite compliance visits.

The broad approach to trust monitoring in respect of AML matters in Jersey is similarly based upon the investigative powers of the local authorities, who have wide powers in order to access information and documentation held by registered trust service providers. The August 2009 FATF peer review of Jersey found it to be "largely compliant".

Guernsey

The *Regulation of Fiduciaries and Administration Businesses (Bailiwick of Guernsey) Bill 2000* - known as the Fiduciary Law - came into effect on April 1, 2001. Under this legislation, anyone (including companies, wherever registered) who, by way of business, carries on regulated fiduciary activities in or from within Guernsey requires a fiduciary licence granted by the Guernsey Financial Services Commission. As at October 2010, 197 TSPs were registered in Guernsey[15].

There are two categories of fiduciary licence:

- 'Full Fiduciary Licence', which will only be granted to a company or a partnership. This authorises all regulated fiduciary activities.

[14] Page 60 (Annex, Table 2), FAFT/OECD and CFAFT paper of October 2010

[15] Page 62 (Annex, Table 2), FAFT/OECD and CFAFT paper of October 2010

- 'Personal Fiduciary Licence', which will be granted to an individual. This authorises the licensee to carry on a restricted range of fiduciary activities, including acting as a company director, as trustee (but not as a sole trustee) and as executor of a Will or administrator of an estate. The holder of a Personal Fiduciary Licence is prohibited from marketing his or her services by the *Regulation of Fiduciaries (Fiduciary Advertisements and Annual Returns) Regulations 2001*.

Applicants for licences are subject to an adjudication as to whether they are "fit and proper". This applies to the shareholders, beneficial owners, directors and senior managers of a business. This includes an assessment of their professional knowledge and experience, including qualifications of relevance.

Licensees are required to adhere to the "four eyes" principle, as well as standards for capital adequacy and compulsory indemnity insurance.

The law empowers the Guernsey Financial Services Commission to make decisions in respect of the granting, refusal, revocation and application of conditions to fiduciary licences.

The Guernsey Financial Services Commission makes detailed on-site visits to TSPs and monitors licensees through receipt of annual audited financial statements and other reporting requirements.

The broad approach to trust monitoring in respect of AML matters in Guernsey is similarly based upon the investigative powers of the local authorities, who have wide powers in order to access information and documentation held by registered trust service providers.

New Zealand

TSPs in New Zealand are not regulated from a conduct of business perspective: There is therefore no licensing, supervision and/or monitoring process. It is anticipated that some form of licensing and minimum prudential requirements will be proposed[16].

Unlike the examples of the Cayman Islands, , Guernsey, the Isle of Man and Jersey above, New Zealand's approach to regulation of trustees for AML purposes was adjudicated to be "non compliant" by the FATF peer review of November 2009. In common with the above examples, the broad approach of the New Zealand regulatory regime is one of investigative powers of local authorities. However, this is not backed by an obligation on any of the interested parties to gather or maintain records in respect of key information.

Singapore

There is no regulation of professional company formation and administration service providers in Singapore, although the provision of trustee services is regulated under the *Trust Companies Act 2005*, and persons carrying on trust business in or from Singapore are required to be licensed.

"Trust business" constitute the provision of services with respect to the creation of an express trust, acting as trustee in relation to an express trust, arranging for any person to act as a trustee in respect of an express trust, and the provision of trust administration services in relation to an express trust.

[16] Page 223, "*The Regulation of Trust and Company Service Providers*" STEP 2006

However, a licence is not required by bare trustees, trustee-managers of registered business trusts, persons preparing or advising on Wills, and persons acting as the executor or administrator of the estate of a deceased.

Further, the following businesses are all exempted from the requirement to obtain a licence:

- banks and merchant banks regulated by the Monetary Authority of Singapore,
- holders of a capital markets services licence, or persons who are exempt from holding a capital markets services licence for providing fund management or custodial services for securities under the *Securities and Futures* Act ,
- lawyers and accountants,
- private trust companies,
- overseas persons,
- persons engaging in trust business in connection with the issuance of debentures,
- trustees of collective investment schemes approved under the *Securities and Futures Act*, and
- persons carrying out introducing activities.

When considering whether or not to issue a licence, the Monetary Authority of Singapore will consider the following factors, amongst others:

(a) physical presence and management expertise in Singapore;
(b) financial soundness;
(c) ability to meet the minimum financial requirements and professional indemnity insurance requirements;
(d) adequacy of internal compliance systems and processes; and
(e) competence and integrity.

The ongoing monitoring of the entities that do fall within the licensing requirement is limited to the requirement to provide certain financial information and staffing figures on an annual basis.

The regulatory regime of Singapore is also an 'investigative' model, in which certain information is provided by regulated businesses. However, as the scope of the definition of "regulated businesses" is limited, and effectively only applies to trustee companies and trust company service provides, it was the conclusion of the February 2008 FATF peer review that many complex trust arrangements, which are established in Singapore through law firms, are outside the regulatory regime in respect of information gathering for AML purposes. On this basis the regime was graded as only "partially compliant" by that review.

United Kingdom

There is no regulation of TSPs in the United Kingdom.

As with all of the jurisdictions already referred to above, the United Kingdom employs an 'investigative' approach to trust regulation. It is based upon the information provided to the local authorities by regulated businesses and by way of required tax filings. However, on the basis that trust service providers that are not otherwise regulated (that is, they are not lawyers or accountants, both of which are regulated by professional bodies) are essentially not monitored in respect of their AML processes, the November 2009 FATF peer review found the United Kingdom's regulatory regime to be only "partially compliant".

Bermuda

The *Trust Companies Act 1991* of Bermuda imposed a regime of licensing and regulation on trust formation and management companies. It should be noted that private individuals or partnerships managing one or a group of named trusts do not need to register under the *Trust Companies Act 1991*. The *Trusts (Regulation of Trust Business) Act 2001* also helped to establish a new regulatory regime for trust management companies in Bermuda.

Bermuda, like many other offshore jurisdictions, tightened up its regulatory regime in response to pressure from the OECD and FATF. As part of this, the government passed the *Trusts (Regulation of Trust Business) Act 2001*. Much of the *Trusts (Regulation of Trust Business) Act 2001* is based on the recommendations made by the November 2000 KPMG report on financial services regulation in the Overseas Territories, which was commissioned by the UK government.

The Bermuda Monetary Authority is the licensing body in Bermuda, and it may grant or refuse an application for a licence. However, it may not grant a licence unless it is satisfied that the minimum criteria are fulfilled by the applicant. The minimum criteria, which are set out in a schedule to the *Trusts (Regulation of Trust Business) Act 2001*, are as follows:

- All controllers and officers are to be fit and proper persons.
- The business is to be directed by at least two persons: This is effectively a codification of the "four eyes principle".
- The board of directors of the trust business should include as many directors without executive responsibility for the management of the business as the Bermuda Monetary Authority considers to be appropriate.
- The business must be conducted in a prudent manner.
- The position of the entity within a group structure shall be such that it will not obstruct the conduct of the effective consolidated supervision.
- The business will be carried on with integrity and the professional skills appropriate to the nature and scale of its activities.

The Bermuda Monetary Authority conducts ongoing monitoring and supervision, through off-site, desk-based assessment and on-site, compliance monitoring visit assessment. The on-site visits are generally scheduled at tri-yearly intervals. The off-site monitoring consists of reviews of annual financial statements and follow-up discussions.

ANNEX B: The Standards

For the purposes of assessing the Standards, SATC proposes that the following definitions be used for the categorisation of personnel:

- The term "**TSP Managers**" means the partners, directors and/or officers of a TSP and any other partners and/or employees who are granted by the TSP the authority to make decisions, enter agreements and/or sign off on advice on behalf of the TSP.

- The term "**TSP Administrators**" means employees of a TSP who administer the day-to-day management of trust funds and assets and who are involved in the decision-making process in respect of such day-to-day management, although they are not permitted to execute such management without the sign off of a TSP Manager.

- The term "**TSP Assistants**" means employees of a TSP who conduct an administrative role within the TSP and who are not part of the decision-making process in respect of trust funds or assets (although they may execute certain acts in respect of such trust funds or assets upon the instructions of TSP Managers and/or TSP Administrators).

The LB&R may issue a Licence to a TSP provided that it satisfies the Standards set out below:

(a) Registration in Switzerland

The entity must be suitably registered in Switzerland with the Register of Commerce and with any other appropriate registers for a vehicle and business of its type. The entity should also be able to show that it is in a position to decide freely and objectively on the administration of a trust.

(b) Operative offices within Switzerland

The entity must have fully operative offices within Switzerland from where it will carry on all or most of its activities falling within the TSP Regulated Activity definition. The entity must have a minimum of three Swiss-based employees, all of whom must conduct all or most of their employment from within Switzerland.

For these purposes, "most" shall be given its ordinary meaning and shall apply both to time spent and fees accrued, and work taking place outside Switzerland shall be taken cumulatively. It would be sufficient for a TSP and its Swiss-based employees to conduct a minimum of 51% of its/their business in Switzerland in terms of time spent and fees accrued.

(c) Minimum capitalisation

Upon registration, a TSP must be able to show that it has received paid up share capital to a minimum level of CHF 100,000, or must be able to provide a suitable guarantee from a parent or group company.

(d) Management and staff must satisfy minimum levels of experience/qualifications

The entity must be able to evidence that all management and staff are fit, proper and capable of fulfilling their roles as trust managers or trust administrators.

By way of example, it is suggested that:

- all TSP Managers must have a minimum of eight years of relevant professional experience, or four years of relevant professional experience and be a full member of STEP, and

- all TSP Administrators must have an appropriate education and a minimum of three years relevant professional experience, or be a full member of STEP and have a minimum of two years relevant professional experience, or have a minimum of eight years of relevant professional experience.

TSP Assistants would not have any qualification or experience requirements placed upon them.

TSP Managers and TSP Administrators must not have been convicted in any country of any crime incorporating any element of dishonesty, nor may they have been declared bankrupt at any time within the previous ten years.

(e) Observance of the "four eyes" principle

Registering TSPs must agree that they would always adhere to the "four eyes" principle in respect of the administration of trust funds and other client assets – that is, that sufficient management systems and work procedures be put in place to ensure that all such matters would be checked and signed off by two members of staff, at least one of which must be a TSP Manager.

(f) Confirmation of insurance coverage

Registering entities must demonstrate that they have continuous policies of D&O and professional indemnity (including negligence and errors and omissions and employee dishonesty) insurance in place with appropriate cover for single and aggregate liabilities of at least CHF 2 million.

(g) Confirmation of adherence to appropriate AML procedures

The TSP must be subject to AML regulation by the FINMA or an approved SRO.

(h) Adequate accounting and record-keeping

The Existing SRO conducting the LB&R audit must be satisfied that, on the basis of the information presented to it during an the audit, the accounting and record-keeping practices of a TSP are adequate both for the purposes of fulfilling a TSP's fiduciary

duties to parties interested in assets under the TSP's control and for the purposes of presenting the Existing SRO with sufficiently complete and detailed information upon which it may conduct its LB&R audit.

(i) Adhering to the SATC Code of Conduct: Performing TSP Regulated Activities to a high standard and from within Switzerland

TSPs will be required to show that they perform their TSP Regulated Activities to an appropriately high standard of professionalism and always to a standard befitting the reputation and standing that the Swiss 'trust industry' seeks. SATC proposes that the SATC Code of Conduct be adopted for the purposes of assessing whether the professionalism and processes of the TSP are maintained at an appropriate level.

Each TSP will also be required to show that most of its business is conducted from within Switzerland and that there is good reason on the basis of its business practices to be based in Switzerland.

These matters would be reviewed through the LB&R audit.

(j) Management and staff with appropriate levels of experience/qualifications in order to carry on TSP Regulated Activities to a high standard

SATC proposes that, at the time of each LB&R audit, all TSP Managers and TSP Administrators must either be full members of STEP or must be enrolled as student members of STEP and active in the process of attaining full membership.

TSP Managers and TSP Administrators with (a) a minimum of five years relevant professional experience and (b) a proven track-record of professionalism would be exempted from this requirement provided they fulfil a minimum commitment to professional development on an annual basis. Such a commitment may be satisfied by attending a minimum of 10 hours of appropriate courses and/or conferences per calendar year.

(k) Strong professional reputation and track record

TSPs will be required to disclose to the Existing SRO details of any and all claims made against them within the previous two years, irrespective of the outcome, nature or merits of such claims, and that they also disclose details of any and all settlement payments made by them during that period.

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ANNEX C: Appeal and Arbitration procedures

1. Decisions of the LB&R may be appealed before an arbitral tribunal provided that a statement of appeal is sent by the Licence holder to the LB&R by registered letter within thirty days of receipt of the LB&R's decision.

2. The arbitral tribunal shall be composed of three members. The Licence holder and the LB&R shall each appoint its arbitrator. The Licence holder shall nominate its arbitrator in its statement of appeal and the LB&R shall nominate its arbitrator in its answer to the statement of appeal, which shall be sent by registered letter to the Licence holder within thirty days of receipt of the statement of appeal. The two arbitrators shall appoint a third arbitrator who shall act as the chairman of the arbitral tribunal.

3. The arbitration procedure is initiated by the Licence holder, who must name its chosen arbitrator in its letter requesting an arbitration.

4. If the LB&R does not name its arbitrator within thirty days following receipt of the statement of appeal or if the two arbitrators cannot agree on the nomination of the chairman within thirty days from the appointment of its arbitrator by the LB&R, the LB&R's arbitrator and/or the chairman, as the case may be, shall be appointed by the President of the Swiss Arbitration Association (ASA).

5. The seat of the arbitration tribunal shall be Berne.

6. The language of the arbitration shall be English.

7. The arbitral tribunal shall decide costs and disbursements in its discretion.

8. The arbitral tribunal's award shall be reasoned in writing, be signed at least by a majority of the arbitrators and be sent to the Licence holder by registered mail with return receipt requested.

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