**contributions**

# Kickbacks and the resulting claims against Swiss asset managers –

# Liability of Liechtenstein entities for omission of assertion of claims

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## 1. Abstract

The following article addresses the obligation of Swiss asset managers to surrender kickbacks to the principal as principal as well as the resulting impact on bodies of legal entities domiciled in Liechtenstein with regard to liability exposure.

With regard to asset management and stock transactions based on mandate agreements for clients (principal) one has to differentiate between three different contractual relationships in terms of contractual duty of care and the fiduciary duty: asset management, investment consulting and a pure account/depot-relationship (*execution only*).[1] Contrary to the investment consulting and the execution only relationship in the asset management relationship the asset manager specifies the investment strategy of assets within his own discretion according to the individually agreed investment structure. The asset manager is subject to an extensive duty to safeguard the client's interests.[2]

The term retrocession fee (also known as kickback or hidden commission) refers to a process between at least three parties, in which a banking institute or a financial intermediary transfers parts of a collected commission to a third party. In particular, in the banking and asset management business such transfers are directed to brokers.[3] Typically, such transfers are executed between a third party and the mandated asset manager since the latter carries out certain actions or arrangements within the range of his contractual mandate which leads to financial advantages in the sphere of the third party.[4]

These resulting kickbacks which are paid to the asset manager belong to the client or the principal, on whose risk and based upon whose mandate the asset management agreement has been entered into.

One of the fundamental problems regarding kickbacks lies in the potential conflict of interest of the asset manager. As agent an asset manager may only represent the interests of the client towards the service providers. However, in case the asset manager receives contributions of

[1] cf *Thalmann* in Festschrift für *Jean Nicolas Druey*, Von der vorvertraglichen Aufklärungspflicht der Bank zur börsengesetzlichen Informationspflicht des Effektenhändlers, p 974 et seq.
[2] Federal Supreme Court of Switzerland (BGE) 133 III 97 E 7.1, p 102.
[3] cf the definition in *Boemle/Gsell* et al, Geld-, Bank- und Finanzmarkt-Lexikon der Schweiz, Zurich 2002, p 903.
[4] *Roth*, Anlageberatung und Vermögensverwaltung in a nutshell, Zurich, St. Gallen 2013, p 67.

these service providers, the risk remains that the interests of the client may no longer be represented properly. If in addition the asset manager withholds kickbacks and refrains from transferring them to the entitled principal, but instead keeps them for his own benefit, he can be held liable by the principal for violation of the mandate agreement (Art. 400 para. 1 of the Swiss Code of Obligations, OR).

External asset managers are very valuable business partners for banks in terms of generating income, since not only they provide administration, supervision and acquisition services but also provide distribution channels in respect of the products or services offered by the banking establishment. This is mainly related to transactions such as stock exchange and foreign exchange trades or the brokering of Lombard loans, which generate costs such as charges or other fees.

The amount of kickbacks resulting from these fees may vary considerably but on average they account for 25 to 60 % of the fee charged to the client.

For clients of asset managers the question arises, whether retrocession fees may be reclaimed and if so, for which time period and in which amount. These questions also play an important role with regard to Liechtenstein legal entities and their respective beneficial owners whereby special consideration has to be given to the reciprocal relationships of the parties involved.

## 2. Kickbacks – legal basis in Switzerland

The Federal Supreme Court of Switzerland found in a major decision in 2006[5] that kickbacks distributed to external asset managers belong to the client and therefore have to be forwarded to them.

The Swiss regulations which are governing the rights and duties related to mandates, which are mainly articles 394 et seq OR, applies to asset management agreements.[6] According to Art. 400 para. 1 OR the asset manager as agent is obliged to disclose to the principal any and all information regarding his management at any time at the principal´s request. As a consequence has to forward any benefits resulting from such activities to the principal.

Subject to such accountability according to article 400 para. 1 OR is everything that is connected to the management in the name of the principal, even internal documents such as notes, drafts or other records.[7]

Disclosure by the agent has to be made even when the compilation of the required files involves great expenditure.[8]

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[5] BGE 132 II 460 ff.
[6] BGE 124 III 155 E 2b p 161; 115 II 62 E 1.
[7] BGE 139 III 49 E 4.1.3, p 54; cp the list of *Zellweger-Gutknecht* in, Anlegerschutz im Finanzmarktrecht, Zur Annahme und Herausgabe von Retrozessionen und anderen Drittvergütungen, in: *Sethe/Hens/von der Crone/Weber* (Hrsg) Zurich 2013, p 226.
[8] Ibidem E 4.4.2, p 58 et seq.

Thus the disclosure embodies an instrument, enabling the principal to exercise a certain control over the activities of the asset manager as agent.[9]

By now it is beyond dispute that the principal may request report to be given regarding the received kickbacks and the asset manager has to comply based on a mandatary's disclosure obligation.[10] The mere report of a lump sum, which makes it impossible to determine the composition of the kickbacks, is not transparent and consequently cannot be sufficient in terms of compliance of accountability pursuant to Art. 400 para. 1 OR[11] – regarding a similar matter in another case the Federal Supreme Court of Switzerland ruled as follows: *the extent of the accountability in management is limited to matters regarding the mandate agreement whereby the mandatary has to completely and truthfully inform the principal and present to him all documents that relate to the business dealings performed to his benefit.*[12]

Furthermore, in this context it is important to note that the obligation of accountability exists irrespective of the fact whether or not kickbacks have to be surrendered.[13] Even if asset managers argue that kickbacks – for whichever reasons – shall not be surrendered to the principaly, they must nonetheless make report on the receipt of kickbacks.

The duty to surrender not only applies to the assets entrusted to investments regarding the asset management agreement but further applies to direct or indirect contributions, which have been received by the agent from a third party in the course of executing of the asset management agreement.

Apart from a mandatary's fees the mandatary shall neither bear profit nor loss from the mandate agreement. Consequently, all assets received by the agent from the principal or third parties, which can be linked to the mandate agreement, must be forwarded to the principal. The asset manager may only keep contributions which he received by a third party during the execution of the mandate agreement if such contributions cannot be linked to the agreement.[14]

Indirect contributions, which have to be surrendered, also include *exempli gratia*, bribes, discounts, commissions et al.[15] It is thus beyond irrelevance whether or not the contributions shall only be to the benefit of the agent according to the will of a third party, since the duty to surrender concerns remuneration of all kinds.[16] Along with kickbacks, finder's fees[17] have to be surrendered as well, since the mandatary has set certain management acts based on the

[9] BG 4A_144/2012 of 11.09.2012 E 3.2.2.
[10] BGE 132 II 460 E 4.6, p 469; cp *Roth*, Das Dreiecksverhältnis Kunde – Bank – Vermögensverwalter, Zurich/St.Gallen 2013, recital 209; *Zellweger-Gutknecht*, ibid, p 227.
[11] cp decision of the commercial court of Zurich dated 26.06.2007 ZR 107/208, p 129, 132: „[…] the principal [must] be wholly and truthfully informed about the arising kickbacks[…]" *Fellmann*, Berner Kommentar, recitals 20, 27, 35 and 58.
[12] BGE 139 III 49, E 4.1.3., p 54.
[13] BGE 139 III 49, E 4.1.3., p 55 et seq.
[14] *Fellmann*, Berner Kommentar, recitals 115, 117 and 127 re Art. 400 of the Swiss Code of Obligations (OR); *Weber*, Basler Kommentar, recital 12 re Art. 400 OR.
[15] *Fellmann*, ibid, recital 128 and 132 re Art. 400 OR; *Weber*, ibid, recital 14 re Art. 400 OR.
[16] *Fellmann*, ibid, recital 131 reAart. 400 OR; Federal Supreme Court of Switzerland, 4C.125/2002 dated 27.09.22, E. 3.1.
[17] Finder's fees are one-time commissions resulting from successful client acquisition.

mandate agreement in the name and in the interest of the principal. Consequently, finder fees are also subject to the handover obligation pursuant to Art. 400 OR.[18]

### 3. Waiver of claims regarding kickbacks

A general waiver regarding the surrender of kickbacks is problematic because of the potential conflict of interest resulting therefrom, which Art. 400 para. 1 OR aims to prevent. A waiver in such an agreement regarding the surrender of kickbacks, would have to ensure that the principal has been sufficiently informed about potential kickbacks. As long as the principal is aware of the calculation basis as well as the full extent of kickbacks and agrees in full knowledge of the inherent interest of conflict relating to this type of asset management model, the prerequisites of the altruistic nature of the mandate agreement are met.[19]

Without the awareness of potential kickbacks it is not possible for the principal to identify the cost structure or possible conflicts of interest of the asset manager. Therefore, the principal has to be informed, if and to what extent the management acts are influenced by agreements with third parties.[20]

A waiver regarding these substantial information, which is granted in advance, is not legally valid, since such a waiver would in turn be the same as an absolute waiver of the handover obligation - depending on no conditions whatsoever.[21]

Consequently, a waiver of kickbacks may only enter into effect if the principal is fully aware of all parameters, which are required to quantify the kickbacks and simultaneously allow a comparison with the assets manager's compensation. In case of a waiver granted in advance an accurate quantification regarding the frequency and the amount of the transactions resp. the resulting kickbacks thereof is not possible as the managed assets continuously change.[22] However, the client must at least be able to determine the scale of the kickbacks which will incur - these must be specifiable in a percent value corresponding to the managed assets. As a consequence it would be possible for the principal to reliably estimate the overall costs of the asset management and assess potential conflicts of interest between the asset manager and third party service providers.[23]

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[18] Jörg/*Alter*, Herausgabe- und Rechenschaftspflicht des unabhängigen Vermögensverwalters, Der Schweizer Treuhänder, 2004, p 297 et seq; *Watter*, Über die Pflicht der Bank bei externer Vermögensverwaltung, AJP 1998 p 1177 recital 87; *Hess*, Zur Stellung des externen Vermögensverwalters im Finanzmarktrecht, AJP 1999, p 1432.
[19] BGE 137 III 393, E 2.4, p 398.
[20] *Nänni/Von der Crone*, Rückvergütungen im Recht der unabhängigen Vermögensverwaltung, SZW 2006, p 383.
[21] BGE 137 III 393, E 2.4, p 399, cp *Roth*, Das Dreiecksverhältnis Kunde – Bank – Vermögensverwalter, 2007, recital 182.
[22] *Abegglen*, Der Verzicht auf Ablieferung von Retrozessionen – Einordnung und Anforderungen, recht 25/2007 p 195; *Emmenegger* in Anlagerecht, Anlagekosten: Retrozessionen im Lichte der bundesgerichtlichen Rechtsprechung, Emmenegger (editor), 2007, p 84.
[23] *Hsu/Stupp*, Retrozessionen sind grundsätzlich dem Kunden abzuliefern, Gesellschafts- und Kapitalmarktrecht (GesKR) 2006, p 206; *Schmid*, Retrozessionen an externe Vermögensverwalter, 2009, p 189.

It has to be determined on a case-by-base basis if the prerequisites for an effective waiver of kickbacks have been met – it also has to be taken into account whether or not the principal is well versed in this kind of business.[24]

An inexperienced resp. uninformed client has to be informed comprehensively and comprehensibly especially with respect to the possible conflict of interests. Whereas with more business-savvy clients with experience in such financial matters it is sufficient to inform them of the heads of terms of the agreements with third parties regarding kickbacks, including but not limited to the expected kickbacks and anticipated volume of transactions.[25]

This information, is not subject to any formal requirements. In proceedings, the burden of proof lies with the agent when it comes to the matter whether he has complied with his information obligation or reporting requirements and consequently, whether or not the waiver has been agreed upon in a legally binding way pursuant to Art. 8 of the Swiss Civil Code (ZGB). General notes, which only indicates that the asset manager could possibly receive kickbacks, are not sufficient to comply with the mandatary's duty to provide full information to the principal – such general information is not adequate in illustrating the consequences of a waiver (compare section 3.1).[26]

A client's absence of response may not indicate a (implied) waiver regarding retrocession fees.[27]

At this point a waiver granted by a body of a legal entity has to be further examined, since it is in the interest of legal entities to enforce recoverable claims as described in detail under section 5.1. Unless such waiver can be justified in accordance with the Business Judgement Rule (confer section 5.2), this may generally lead to liability of the executive body as such a waiver hardly represents the interests of a legal entity.

## 3.1 General Terms and Conditions in Switzerland

For general terms and conditions (T&Cs) to enter into legal force in Switzerland the following prerequisites must be met: Firstly, the T&Cs have to be announced and/or published in a way which enables any potential contracting party to become aware of the T&Cs, secondly, they must be brought to the attention of the client before the actual conclusion of a contract, lastly, the client must consent to the validity of the T&Cs. The T&Cs come into force if the first two prerequisites apply, since the consent of the client regarding the T&Cs is implicitly assumed in

[24] *Von Büren/Walter*, Die wirtschaftliche Rechtsprechung des Bundesgerichts im Jahr 2006, ZBJV 143/2007, p 449 et seq.
[25] cp *Von Büren/Walter*, ibid, p 499 et seq.
[26] *Emmenegger* in Anlagerecht, Anlagekosten: Retrozessionen im Lichte der bundesgerichtlichen Rechtsprechung, 2007, p 83.
[27] BGE 132 III 460 E 4.5, p 469.

such case. The party which would benefit of the terms and conditions – in this case the drafter of the T&Cs - has the burden of proof regarding the validity of the same.

The validity and consequently the applicability of the T&Cs is based on the general principle of trust, according to which all circumstances connected to the conclusion of the contract have to be taken into account. Subsequently, within the scope of the so-called "*Geltungskontrolle*" ("control of validity") it has to be examined whether any clause is unusual in terms of the so-called "rule of the unusual" ("*Ungewöhnlichkeitsregel*"). This is the case if and only if a global adoption of the T&Cs occurred. A global adoption of T&Cs refers to approval of the same without having read or understood them and their consequences.[28] It has to be assessed on a case-by-case basis whether a global adoption of T&Cs has taken place.

According to the doctrine and jurisprudence the T&Cs will not come into effect at all in case of a global adoption and if they are unusual in terms of the aforementioned principle of trust since they would not reflect the parties' mutual consensus. Unusual in this sense are surprising clauses which may not be anticipated by a contracting party – the client – with regard to a specific type of agreement.[29] According to the Federal Supreme Court of Switzerland the criteria mentioned hereafter must be fulfilled in order to deem a clause unusual: The clause to be assessed must be unusual in subjective and objective terms, in other words it has to be surprising (subjective element) and unrelated to common business practice (objective element).[30]

If clauses about kickbacks are unusual from a subjective point of view they must be assessed on a case-by-case basis, since it depends on individual experiences of each client. A clause is more likely to be assumed unusual for a layperson rather than experts or institutional investors.

An objective unusual nature may be seen in the waiver of Art. 400 para. 1 OR in favour of banking institutions, which is intrinsic to the legal nature of mandate agreements and therefore posing an uncommon business practice.

Furthermore, unconscionable or unethical T&Cs are unfair in terms of Art. 8 of the Unfair Competition Act (UWG). Unfairness is assumed if the provisions of the T&Cs result in a significant and unwarranted imbalance between the contractual rights and obligations of the involved parties. Such clauses are deemed invalid. Irrespective of this, according to the decision BGE 137 III 393 dated August 29, 2011, the requirements for a binding waiver are rather strict. These requirements have to be taken into account, additionally, to the other

[28] Decision of the Federal Supreme Court of Switzerland BGer 4C.282/2003, E 3.1.
[29] *Gauch/Schluep/Schmid/Rey*, Schweizerisches Obligationenrecht, 8. Auflage, Zürich/Basel/Genf 2003, recital 1141 et seq.
[30] BGE 109 II 213, 216 et seq, E 2a; BGE 109 II 452, 456 et seq; BGer decision 5P.115/2005, E 1.1.

regulations regarding T&Cs, like the previously mentioned control of validity and control of content.

Hereafter you may find an overview of the requirements of a waiver:

- The principal has to be correctly, completely and truthfully informed about the expectable kickbacks and the asset manager has to disclose the heads of terms of existing agreements. Future potential retrocession fees may be specified within a percent value of the managed assets. This enables the principal to wholly grasp the cost structure of the asset management agreement. On this basis it is possible for him to understand the spectrum of commissions – kickbacks, in particular – which the asset manager receives next to his mandatary's fees.
- The principal must be aware of the inherent conflict of interest of the asset manager in connection with kickbacks. The risk remains, that investments are not made based on the highest prospective yield but rather based on transactions that yield the most kickbacks.
- With knowledge of aforementioned aspects, the principal may agree to a waiver regarding prospective kickbacks.

The asset manager has the duty to inform the principal (without prior request from the latter) about received kickbacks. The asset manager has to prove that he informed the principal adequately.

Therefore *Emenegger*[31] already correctly advocated in 2007 that: «*A legally binding and valid waiver of the handover obligation is only possible if the waiver is made in a separate declaration. However, this means that the waiver is no longer part of the T&Cs. In conclusion, a valid waiver regarding the obligation to surrender cannot be agreed upon in the T&Cs.*»

## 4. Prescription of claims based on kickbacks according to Swiss Law

In connection with the question of prescription, the contractual prescription period must be considered with regard to the asset manager.

In certain constellations, however, the question of prescription may be twofold. On the one hand, as mentioned above, the limitation of claims regarding retrocession fees against the asset manager has to be assessed according to the law of Switzerland because of the fact that the place of business of the asset manager is generally in Switzerland. On the other hand, a liability of a body of a legal entity exists, which is assessed - within the framework of the present paper - according to the law of Liechtenstein (for further details see section 6. et seq).

[31] *Emmenegger* in Anlagerecht, Anlagekosten: Retrozessionen im Lichte der bundesgerichtlichen Rechtsprechung, 2007, p 86.

### 4.1 Period of prescription

In legal literature, a minority of authors[32] argues that kickbacks incur periodically in terms of Art. 128 para. 1 OR and are therefore subject to a five-year prescription period. According to this opinion kickbacks are paid in regular intervals by the provider of the investment product to the asset manager. The Federal Supreme Court of Switzerland considered this compensation to be part of the management fee, which is charged »periodically, usually annually« by the providers of the investment product. Consequently, kickbacks paid by the banks are periodic in terms of Art. 128 para. 1 OR. Since repayment- and compensation claims would generally be subject to the same prescription period as the underlying main claim, the issuance of kickbacks is – as main claim between the provider and the banking institution - a periodic activity – pursuant to this the five-year prescription period would also be applicable to the privity of contract between the bank and their client according to Art. 128 para. 1 OR.[33]

In contrast to this, the prevailing parts of academia as well as the prevalent jurisprudence postulate the applicability of the regular ten-year prescription period pursuant to Art. 127 OR.[34] This is in particular due to the fact that the legal basis for the surrender of kickbacks (Art. 400 para. 1 OR) is simply not designated as a periodic obligation to perform. The mandatary is not obliged to surrender yields periodically to the principal. The nature and extent of the surrender claim depends at which point in time the principal requests the agent to surrender the accrued revenues; ie it depends on whether or not the principal demands the yields during the mandate agreement or after the termination thereof.[35] Furthermore, the surrender claims is linked to an ancillary duty for which the same prescription period applies as for the main duty (cf Art. 133 OR). The main obligation is *in casu* the proper asset management, for which the ten-year prescription period applies in accordance with Art. 127 OR.[36]

It should be noted that the question of the prescription period for retrocession fees to be refunded has not yet been finally decided by the Federal Supreme Court of Switzerland and is therefore handled differently in each Canton. For example, a decision of the Court of Appeal of Bern has been rendered, which declares the prescription period of five years to be

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[32] *Beat/Vito*, Wann verjähren Bestandespflegekommissionen? in: Jusletter dated November 19, 2012, recital 9 et seq.; *Nobel* – Das Bundesgericht zu den Bestandespflegekommissionen, in: Jusletter dated November 19, 2012, recital 14; *Romerio/Bazzani*, Verjährung des Anspruchs auf Herausgabe von Bestandespflegekommissionen, in: GesKR 2013, p 49 et seq.
[33] *Romerio/Bazzani*, ibid, p 53.
[34] *Emmenegger* in Anlagerecht, Anlagekosten: Retrozessionen im Lichte der bundesgerichtlichen Rechtsprechung, Basel 2007, p 87 seq.; *Neuman/Von der Crone*, Herausgabepflicht für Bestandespflegekommissionen im Auftragsrecht, in SZW 2013, p 110; *Roth*, Anlageberatung und Vermögensverwaltung in a nutshell, Zürich/St. Gallen 2013, p 68; *Schaller*, Retrozessionen, Nochmals zur Verjährungsfrage, in Jusletter dated December 3, 2012, recital 3 et seq.; *Weber*, in Basler Kommentar zum Obligationenrecht I, *Honsell/Vogt/Wiegend* (Hrsg), Basel 2011, Art. 400 recital 24; *Zellweger* in Anlegerschutz im Finanzmarktrecht, Zur Annahme und Herausgabe von Retrozessionen und anderen Drittvergütungen, *Sethe/Hens/Von der Crone/Weber* (Hrsg), Zürich 2013, p 213 et seq.
[35] *Schaller*, ibid, recital 5 et seq.; cf *Roth*, ibid., p 68.
[36] *Schaller*, ibid., recital 7.

applicable. The court states in its ruling that retrocession fees are to be qualified as periodic and as such will be subject to the five-year prescription period.[37]

Contrary to this, the Court of Appeal of Zurich applied the ten-year prescription period in one of its rulings, according to which the sum of all kickbacks which have incurred can be claimed together with the main claim within a period of ten years from the date of termination of the contract.[38] In addition, the duty to surrender returns is indirectly limited by the banking establishment's retention of information and documents requirement, which is ten years.[39]

### 4.2 Commencement of the limitation period

In principle, the limitation period starts upon maturity of the claim (Art. 130 OR). This means upon arising of the claim (art. 75 OR). Relating to kickbacks it is argued by some of the authors of the legal literature that the maturity occurs at that point in time, at which the bank *(note: as asset manager)* received the kickbacks.[40] This is especially the case since one has to consider that the claim to surrender the kickbacks has to be seen independently from the claim to return the managed assets.[41] Furthermore, this view is based on a decision of the Federal Supreme Court of Switzerland (*Bundesgericht*), which stated that the asset manager has to hand over all assets, which he does not need for the fulfilment of the contract, immediately after acquisition, unless it has been agreed otherwise.[42]

On the other hand, other authors argue that an artificial separation between kickbacks and other asset inflows of third parties does not seem to be appropriate. Kickbacks, similarly to dividend payments, repayments of receivables or sales revenues, should rather be attributed to the original assets, since the purpose of asset management is not to simply hold the net assets but to increase the total return by means of reinvestments.[43] This total amount would have to be issued as such upon termination of the mandate contract.[44] It would arise therefrom that kickbacks become due only by termination of the contract and that the limitation period commences only at this point in time. The Court of Appeal of the Canton of Zurich decided in correspondence with the latter line of thought.[45]

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[37] Decision of the first criminal division of the Court of Appeal of Bern, SK 2012, 218 dated July 4, 2013.
[38] Decision of the Court of Appeal of Zurich LB090076 dated January 13, 2012, E 3.D 2.1.
[39] Art. 962 OR; cp *Emmenegger*, Anlagekosten: Retrozessionen im Lichte der bundesgerichtlichen Rechtsprechung, 2007, p 88 et seq.
[40] *Beat/Vito*, ibid, recital 21 et seq; *Neuman/Von der Crone*, ibid, p 111 *Romerio/ Bazzani*, ibid, p 55 et seq.
[41] *Romerio/Bazzani*, ibid, p 56.
[42] Decision of BGer 4C.125/2002 dated 27.09.2002 E 3.1.
[43] *Emmenegger*, ibid, p 89 et seq; *Schaller*, ibid, recital10
[44] BGE 91 II 442 E 5b, p 451 et seq
[45] Decision of the Court of Appeal Zurich LB090076 dated 13.1.2012, E 3.D 2.1.

However, only a decision of the Supreme Court will provide final certainty on this issue with regard to kickbacks.

## 5. Liability of bodies of Liechtenstein legal entities

Of course, the above described relationship between clients, Swiss asset managers and banks resp. financial intermediaries applies also for Liechtenstein clients, although a special constellation arises in relationship to Liechtenstein. After all, the management of the clients' assets is often conducted by Liechtenstein legal entities. Consequently, the bodies of these entities may be responsible for reclaiming the kickbacks and an omission to do so may result in them becoming liable. In particular for Liechtenstein financial intermediaries, especially Fiduciaries, a major part of their success in business has been closely linked to the cooperation with Swiss banks. One can assume that the two major Swiss banks UBS and Crédit Suisse established several thousand structures in recent decades - primarily foundations for their bank clients - via Liechtenstein trust companies. It goes without saying that the reason behind this mandate by Swiss banks was the fact that the assets transferred to the Liechtenstein structures were subsequently managed by the same banks.

It therefore is necessary to further examine whether the bodies were and are obliged to reclaim the withheld kickbacks from asset managers pursuant to corporate due diligence obligations in favour of the administered entities and whether liability claims may arise, in case they failed to assert these claims contrary to their duty.

### 5.1 Responsible bodies of Liechtenstein legal entities

The body authorized to manage and administer the entity is the executive board. The board has the duty and right of management and representation of the entity.

The responsibility of bodies is regulated by the articles 218 et seq. of the Liechtenstein Person and Company Law (PGR) and the liability of persons responsible according to Art. 218 et seq PGR is covered by the regulations regarding the contractual liability according to Art. 226 PGR.

To be able to go into detail regarding the civil liability, it is necessary to explain the rights and obligations of the administrative bodies.

Art. 182 PGR regulates the rights and obligations of the management, which has all the rights and obligations that have not been transferred to another body. In the course of the amendment of the foundation law of April 01, 2009, the *business judgement rule* (BJF), which

by then had already been accepted by the jurisprudence for years, was codified in Art. 182 para. 2 PGR. Pursuant to the BJR, bodies have to take appropriate and diligent business decisions otherwise becoming liable for failures to act accordingly.

Consequently, corporate executives may be held liable for any breach of the principles of diligent administration and representation. In order to comply with the BJR, members of the board must not breach any one of the triads of their fiduciary duty – good faith, loyalty or due care. This means they must not pursue interests that go against the legal entity which they are representing and must act in the best interest of the entity based on reasonable and appropriate information.

In the course of these due diligence obligations, the bodies have to safeguard the interests of the entity. This also includes the verification and if needed the assertion of any existing claim. If such claims, contrary to the given duty, are not asserted the bodies may be held responsible for causing damage by said breach of duty by omission.

In other words, this means that the executive board has to assert the claims resulting from kickbacks against the mandated asset managers, since it is in the interest of the entity to assert existing claims. The same applies for structures according to trust law.

### 5.2 Safe Harbour pursuant to the Business Judgement Rule

This liability has to be further examined under the context of the Business Judgement Rule (BJR) as stipulated in Art. 182 para. 2 PGR. The BJR originates from the American corporate law and its purpose is to create an exemption from liability (so-called *safe harbour*) for bodies, who act in good faith, act in the best interests of the legal entity, act on an informed basis, are not wasteful and do not involve self-interest (duty of loyalty). In other words, decisions must be plausibly justified, well prepared, in good faith, from an ex ante point of view reasonable, sound and rational as well as responsible and in the best interest of the legal entity.[46]

Accordingly, the board would have been obliged to conduct detailed clarifications after the judgement of the Federal Supreme Court of Switzerland in BGE 132 III 460 on the obligation to surrender kickbacks, which has already been delivered in spring of 2006, (naturally, taking into consideration an appropriate course in time to take note of the ruling). Such clarifications would at least have been necessary regarding the respective contractual partners, which were commissioned with the asset management, as well as the amount of the kickbacks. These procedures would have enabled the concerned bodies to evaluate whether legal proceedings

[46] *Jakob*, die liechtensteinische Stiftung, Vaduz, 2009, recital 343 et seq.

were justifiable considering the litigation risks in case of denial of surrender of the kickbacks. However, a total failure to act cannot - even from an *ex-ante* perspective - lead to a safe harbour, since the omission of any action or inquiry towards the banking institutions cannot be seen as an action, which serves the interests of the legal entity.

Moreover, such a decision would have to be sufficiently well documented in order to be able to deduce the decision-making process based on the relevant motives and interests as laid out on these documents.

### 5.3 Awareness of the Swiss court rulings and consequences thereof

The first legal precedent has been rendered on March 22, 2006[47]. This precedent has been further specified by the Commercial Court of Zurich on June 26, 2007[48]. With regard to the jurisprudence of the Federal Supreme Court of Switzerland (BGE), the Commercial Court has stated that solely the awareness of the disbursement of retrocession fees is insufficient for a waiver of the same. In fact, it is required, that the principal is capable of estimating the amount of these kickbacks, in order to put in a legally binding disclaimer. This decision was reaffirmed and further elaborated in a key decision of August 29, 2011.[49] Lastly, a crucial ruling has been rendered on October 30, 2012[50], according to which an investor with an asset management mandate is not only entitled to such kickbacks, which the bank has received from external asset managers, but also to retrocession fees generated by internal asset managers (portfolio and management commissions, “trail” fees).

In the decision of May 27, 1986[51], the Supreme Court of Liechtenstein had already stated that the standard of liability of the respective body must not be organized excessively and that the duty of care must not be interpreted in an unpredictable, unrealizable and therefore unreasonable way. Nevertheless, the Supreme Court also held that the liability of the bodies, which are entrusted with the asset management goes beyond the *diligentia quam in suis rebus* – the diligence that a body exerts in its own business. A violation of this diligence takes place in particular, in cases, in which an effective control is neglected and replaced by mere trust.

[47] Federal Supreme Court of Switzerland (BGE) 132 III 460.
[48] ZR 107/2008 p 129. Further decisions of the BGE: BGE 6B_233/2010 on January 13, 2011; OG ZH LB090076 on January 13, 2012; BGE 4A_155/2011 on January 10, 2012; BGE 137 III 393 (4A_266/2010 on August 29, 2011). Cf. the FMA in Liechtenstein, regulation 2011/1 item 30: «In cases in which an asset manager receives contributions by a third party for the management of clients’ assets (reimbursements, commission fees portfolio commissions, credit notes etc.), the utilization of these contributions has to be contractually agreed with the client. The contributions belong to the asset manager if he or she informs the customer about them and if there is an improvement of the services related to the contributions or if the client signs a disclaimer.»
[49] BGE 4A_266/2010 – Prerequisites of an effective waiver: Clear and unambiguous intention to waive the claims based on complete and truthful information. *In conclusio* the basic parameters of the retrocession agreement of the mandatary with a third party as well as the scale of the reimbursements which may be expected must be obvious.
[50] BGE 138 III 755.
[51] 01 C 7/75-127, LES 1988,60.

This effective control must already be exercised upon acceptance of a customer's assets in the course of the asset management.

This means, that regarding the monitoring of the business practices, bodies of legal entities which manage bank accounts at Swiss banks, were obliged to acquire the knowledge of an average Swiss trustee, this even more so since they must have become aware of the Swiss jurisprudence - which by the way received major feedback in media[52] - by 2007/08 at the latest.

After becoming aware of aforementioned judgements, which must be assumed at the point in time at which banks implemented the waiver provisions in the terms and conditions, it would have been the next consistent step of the respective executive boards to verify potential retrocession fee claims. In order to receive information about the scale of the kickbacks, it would at first seem expedient to send an inquiry letter to the bank. Consequently, the retrocession fees should be demanded from the bank. If the banking establishment refuses to surrender the retained kickbacks – for example based on a potential waiver or other reasons – a decision according to the business judgement rule would be necessary to evaluate whether or not it would make sense to assert these claims (cost-benefit-consideration). The result of such a decision would depend on the expected amount of retrocession fees and the risks of such an enforcement. In any event, this decision will have to be substantiated and recorded. Failure to act at all is certainly insufficient.

A waiver regarding the reclaiming of kickbacks from a body of a legal entity towards an asset manager may basically be considered as an damage causing act. Therefore, any type of (retrospective) waiver regarding existing and future claims without justification has to be considered as a damage causing behaviour.

In respect to the assertion of these claims against the provider of the relevant business relations in Liechtenstein in terms of fiduciary mandates conflicts of interests might possibly arise. Regarding the establishment and the management of legal entities in Liechtenstein, the Swiss banks have actually been and still are acting as intermediaries. Since there are claims of considerable amounts to be enforced against the proverbial *«feeding hand»,* there exists the possibility of conflicts of interests and as a consequence, the interests of the represented legal entity may be put on hold and therefore adversely affected.

[52] In extracts: NZZ on June 22, 2006, Wem gehören Retrozessionen?; *Charlotte Jacquemart* in NZZ am Sonntag, Bundesgericht, 07.10.2007; Die Anleger müssen mehr Druck machen, 28.10.2007; Retrozessionen: Ein zweites Gerichtsurteil muss her, 06.07.2008; *Franco Tonozzi* in Saldo No. 16, Banken behalten Geld, das Kunden gehört, 11.10.2006; *Christof Moser* in Sonntagsblick, Diese Milliarden gehören den Kunden, 22.06.2008; *Michael Rasch* in NZZ, Banken brauchen Druck von Kunden, 20.10.2007; *Clifford Padevit* in Finanz und Wirtschaft, Retrozessionen gehören nicht immer den Kunden, 19.07.2006; *Thomas Müller* in Handelszeitung No. 8, Wem die Provision eigentlich gehören würde, 19.02.2008; *Rudolf Strahm* in Berner Zeitung, Kickbacks stören die Vertrauensbasis, 03.12.2008; *Eugénie Hollinger-Hagmann*, November 2007; *Werner Grundlehner* in NZZ, Mehr Transparenz für Bankkunden, 02.11.2012; *Grundlehner/Ferber* in NZZ, Banken spielen bei Retrozessionen auf Zeit, 24.10.2013.

If decisions are not being substantiated and recorded according to the business judgement rule or if the interests of the company were not properly protected, the actions of the bodies of the legal entity will be subject to liability claims for breach of professional responsibilities – for further information regarding this subject see section 6.4 (case study).

### 5.4 Capacity to sue

According to the assertion of the compensation of damages, the legal entity itself is primarily entitled and therefore owner of the capacity to sue. The bodies of the legal entity are liable towards the legal entity for any type of fault, thus negligence and intent.

If the legal entity does not have any claim for damages (in case of a direct damage of a member of the entity) or if malicious damage is caused by one of the bodies against a member, the bodies bear liability for every single member (Art. 218 para. 2 in conjunction with Art. 222 para. PGR).

The term *member* is used in different ways in the PGR and describes members of the administration, on the one hand, and members of the legal entity, on the other hand.

The subject regarding the capacity to sue is especially relevant in matters of liquidated legal entities. In order to assert claims of legal entities which have already been liquidated, the appointment of a curator is necessary (see below in section 6.3). In this context it is of importance, that possible exemptions from liability by members of the legal entity, cannot comprise the executive body (foundation board or executive board) of the legal entity, because such an exemption from liability granted to oneself cannot be legally agreed upon from the outset.

## 6. Limitation of liability claims against Liechtenstein corporate bodies

As mentioned above, the ruling of the Swiss Federal Supreme Court regarding retrocession fees has already been issued in spring 2006. This was the first possible date to enforce the claims. Assuming a limitation period of ten years, the first possible date to claim the kickbacks would have been in 1996/1997. Assuming a limitation period of only five years, assertion of the claims regarding kickbacks still would have been possible back to 2001/2002.

There are two elements regarding the question of the prescription period, as mentioned before under section 4. On the one hand there is the question of the limitation period of claims resulting from kickbacks against the asset manager. This claim has to be assessed according to Swiss law, since the registered office of the banking establishments respectively of the

financial intermediaries is situated in Switzerland. On the other hand there is the limitation period regarding liability claims against the bodies of the legal entities registered in Liechtenstein. The consequences are, that even if the claims against the asset manager are already prescribed, there is still the possibility to file a liability claim against the executive board - provided there has been a breach of duty of care.

As provided by the first indent of the first paragraph of Art. 226 PGR liability claims against board members prescribe within three years, whereby the limitation commences with the awareness of the damage and the damaging party.

However, if wrong information was given knowingly or deliberate damages were caused, the liability claim will prescribe only after ten years after becoming aware of the damage and the damaging party (Art 226 para. 1 second indent PGR).

The Liechtenstein Supreme Court (OGH) postulated that the prescription of liability claims of a legal entity against its body may not commence as long as said body represents the entity. Correspondingly, the same applies for liquidated legal persons (for details see section 6.3).

Therefore, *in concretu* one must assume that a negligent breach of duty will lead to a prescription period of three years. However, the commencement of this period is a wholly different issue.

### 6.1 Factual extension of the liability period

The result of the different claims and different prescription periods is a *de facto* extension of the limitation period. So, on the one hand claims against Swiss banks prescribe after ten years (respectively five years according to the opinion held by a minority), however, on the other hand, the respective body would have been responsible to assert the claims after the precedent in 2006 as laid out before. Upon failure to act accordingly the body may be held liable. As mentioned before the prescription period of three years regarding liability claims commences upon awareness of the damage and the damaging party pursuant to Art. 226 para. 1 first indent PGR. Nonetheless, the prescription period may not commence before a neutral body has been appointed (concerning this see under section 6.3), since it would be unrealistic to assume that a body will assert claims against itself.

As a result it comes to the factual extension of the prescription period as referred to at the outset, since the executive board of a legal entity may be held liable for claims regarding kickbacks as far back as 1996/97, considering that they were able to take note of the mentioned ruling of the Federal Supreme Court of Switzerland in 2006/07.

Hence, it is possible to enforce liability claims regarding kickbacks against executive boards even after the ten year limitation period has passed, for failure of said board to assert the

claims against the Swiss banks. In other words, even though a claim against a bank or an asset manager may already have been prescribed, it is feasible to assert these claims – based on differing legal grounds – against the responsible body of the entity, ie its executive board.

Thus, one has to closely examine the retention obligation of banking institutions and consequences resulting thereof. The pressing matter at hand is the possible lack of proof concerning the amount of kickbacks which accrued more than ten years ago.

In the event of a bank destroying its documents after ten years of storing, problems regarding the provability of the amount of kickbacks as well as their enforceability may arise.

However, it is safe to assume that kickbacks on transactions exist - considering they can be fairly easily quantified within the ten-year period of the retention requirement – retrocession fees must accrue even before that period as well. If need be, an expert witness would have to estimate the figures based on the invested capital and the type of investment.

Even this might be dispensable, considering the claim itself is determined in terms of reason, just not in terms of amount - which leads to a discretionary assessment of evidence (*ex aequo et bono*) pursuant to Art. 273 of the Liechtenstein Code of Civil Procedure (ZPO). If it is evident that compensation for damages (*damnum emergans* – the actual damage as well as *lucrum cessans* – loss of profit) has to be payed - it is however, unfeasible to determine or only possible due to disproportionate effort to determine the exact amount of the damages, then the court may *ex officio* or upon application determine the amount in its free and discretionary opinion based on the facts of the case.

In this case, where the claim itself is determined in terms of reason, no dismissal of the claim with regard to the burden of proof is possible. Pursuant to *legis citatae*, in such a case the judge is obligated to determine the amount of the claim - if it is impossible to quantify the damages the judge has to undertake a discretionary estimation based on all the facts of the case, including but not limited to expert opinions.[53]

Hence, a determination of damages by the judge is necessary and as a result retrocession fees may be enforceable even after the ten-year prescription period has passed; a doubt regarding the enforceability cannot arise since the contractual basis is proof enough of the asset management mandate. Even when talking about liquidated entities the required documentation should be accessible via the records of the respective file.

[53] *Rechberger* in Fasching/Konecny, 2. Edition, § 273 ZPO, recital 4, 9.

## 6.2 Excursus: "Absolute" period of prescription

In Liechtenstein the legal provisions regarding contractual relations between a principal and a mandatary are codified in §§ 1002 et seq of the Austrian Civil Code (ABGB). According to § 1009 ABGB the mandatary is obligated to diligently and candidly execute the mandate pursuant to the authority granted to him or her as well as to surrender to the principal any benefit arising from the mandate. The claim to surrender cannot be qualified as a claim for damages, but as a claim for performance and therefore is subject to the prescription period of 30 years according to § 1478 ABGB.[54]

In case of the omission of the enforcement of retrocession fees, it is not feasible to demand their surrender based on the provisions stipulating unjustified enrichment. The relationship between a legal entity and its executive board does not constitute a mandate agreement, but much rather a contractually regulated mandate *sui generis* between the legal entity and its body.

As indicated above, the liability pursuant to Article 226 PGR is applicable with regard to claims concerning professional responsibility. This statutory provision is classified as *lex specialis* in relation to § 1489 ABGB, but it does not provide an "*absolute" period of limitation*, whereas § 1489 ABGB establishes such an absolute period of prescription of 30 years for compensation claims.

*In concretu*, it is necessary to establish whether this "*long" period of limitation* gets reduced to ten years by the legal provision of § 1489a ABGB. In pursuance of this provision, every claim for compensation in connection with the financial services businesses of a financial intermediary licensed by the FMA becomes statute-barred within three years from the awareness of the damage and the damaging party, at all events, however, time-barring occurs in ten years from the conclusion of contract. Consequently, any and all claims for damages would already have been prescribed after ten years. There are, however, several reasons why § 1489a ABGB, in particular its stipulated absolute period of limitation, is not applicable in cases discussed in this article.

§ 1489a ABGB was enacted in order to reduce the period of limitation to ten years for very specific damage claims. This legal provision includes damage claims associated with the financial services business.[55] It came into force on November 11, 2007.[56] Pursuant to § 5 ABGB, laws do not have retroactive effect and therefore do not influence actions or rights which have been set or acquired prior to the effective date of the respective law. In accordance

[54] *Strasser* in *Rummel*, 3rd Edition, § 1009 recital 21 et seq.
[55] Parliamentary report and motion 2007 Nr. 65, p 17 et seq.
[56] LGBl 2007 Nr. 272.

with settled case law, in cases in which the prescription period has already commenced, the prior statute is applicable instead of the posterior act. Nevertheless, in case of enactment of a shorter period of limitation, in absence of legal provisions that state otherwise, this shorter limitation period is applicable. Nonetheless, this shortened limitation period may commence only after the new right has been enacted and has come into force.[57] Even if one would affirm the applicability of § 1489a ABGB, the limitation may only commence successively from November 01, 2017 onwards.

However, § 1489a ABGB only covers matters regarding financial services businesses – including businesses in connection with investment services in the securities field – and other banking services as well as their ancillary services. These types of transactions do not include administrative activities of bodies of corporate entities which are undertaken for the benefit of the latter as a result of the position as the executive body. Consequently, § 1489a ABGB is not applicable to claims regarding the professional responsibility of legal persons. § 1489a ABGB was enacted in the interests of banks, asset management companies and investment firms, but not to discharge administrative bodies of legal entities of their responsibilities.[58]

The fiduciary *»exertion of a contractually regulated mandate at a domiciliary company by a trustee does not embody a finance services business between the trustee and the legal entity. Furthermore, concerning the absolute limitation of possible claims regarding the professional responsibility pursuant to the Articles 218 et seq PGR, it cannot be assumed that the legislator prefers trustees, who are acting as bodies of legal entities, over <conventional> bodies of <operating entities> […]. There are no factual grounds to build such an unequal treatment upon.«* [59]

It can ultimately be stated that the absolute limitation period of § 1489a ABGB is not applicable in cases discussed in this article. In fact, the "relative" limitation period of three years according to § 1489 ABGB respectively the limitation period of ten years according to Article 226 para. 1, second indent PGR is applicable in such cases.

### 6.3 Liquidated structures

As discussed below (section 6.4), the intermediate liquidation of the foundation or the corporate entity in general represents a special case of limitation. According to consistent case-law, the awareness of the executive body representing the entity is crucial for the commencing of the prescription period. The awareness of a person as the body of an entity, who has committed a

[57] *Kodek* in *Rummel/Lukas*, ABGB[4] § 5 recital 40; RIS-Justiz RS0008705, RS0008685.
[58] Parliamentary report and motion 2007, Nr. 65, p 117 et seq.
[59] Liechtenstein High Court (OG), 08 CG.2015.133.

harmful act or caused damage by omitting the necessary action, does not trigger the beginning of the limitation period. The reason for this is that the body, who committed a breach of duty in exercise of its executive role, would not assert claims of professional responsibility against itself on behalf of the corporate entity.[60]

In cases, in which the legal entity has already been liquidated, there is no existing body, which is authorized to represent the legal entity. As a consequence, the prescription period of the liability claims cannot commence at all.[61] In order to assert any claims it is necessary to first appoint a curator for the liquidated entity pursuant to Art 141 para. 1 PGR, who can represent the liquidated entity in proceedings and has to be registered in the register of companies.

The intent and purpose of the appointment of a curator for a liquidated legal entity is that a *pro forma* liquidated legal entity, which is still in possession of assets, cannot be considered as an entirely liquidated entity and therefore still has legal capacity while lacking any bodies to properly represent or act on behalf of it. Thus, in accordance with Art. 141 para. 1 PGR the liquidated regains its ability to act by the appointment of a curator.[62] The appointment may enter into force via application by a concerned party.

As already mentioned, the legal entity has capacity to sue in respect of claims regarding professional responsibility. Therefore, it is the curator's duty – as its body– to assert the claims to the benefit of the legal entity.

### 6.4 Case Study

The premise of this case study is as follows: A legal entity was established in the year 1995 with CHF 1.000.000,-- being invested; in 2012 the entity has been liquidated. On average, kickbacks in the amount of CHF 5.000,-- to CHF 10.000.-- incur per annum. The amount of kickbacks aggregating within the 17 years totals to CHF 85.000,-- to CHF 170.000,--.

The first decision of the Federal Supreme Court of Switzerland was issued in March 2006 with further clarifications being rendered by the ruling of the Commercial Court of Zürich in June 2007. Taking this into account, it is safe to assume that one must have become aware of the kickbacks-issue in 2007/08, which in turn means that it would be possible to assert kickbacks going back as far as 1997/98 (regarding the explanations on prescription pursuant to Swiss Law see under section 4.). Let us presume that awareness of the decisions occurs in 2008 at the latest, this would result in kickbacks being enforceable against Swiss banks as far back as 1998. The relevant period of time for reclaimable kickbacks amounts to 14 years in total, from

[60] Liechtenstein Supreme Court (OGH) April 5th, 2001, 01 C 1998.586, p 29.
[61] Last confirmed by the High Court in OG 08 CG.2015.33, p 53 et seq, in reference to OGH 1 C 586/98.
[62] OGH March 6th, 2015, 05 CG.2013.525.

1998 until the liquidation of the entity in 2012. Under aforementioned assumption regarding the amount of the kickbacks this would result in a total value of CHF 70.000,00 to CHF 140.000,00 in 14 years.

Now, the prescription period of liability claims against the executive board is three years (see in detail section 6.). However, the prescription period may not start for an entity that has already been liquidated (as mentioned under section 6.3). The starting point of the limitation period principally arises with awareness of the damage and the infringing party. Notwithstanding the above, the prescription period does not start when a person in its function as a member of a body of the entity, who committed the damaging act or omission themselves, becomes aware. It may only start with appointment of another, neutral body with the power of external representation.

As a result, with regard to the interaction of the two different periods of limitation and their different starting and ending points it is possible to assert claims of kickbacks not only within the last ten years, but also over a much longer time frame by means of liability claims against the body of a legal entity – in the case at hand – regarding the time period between 1998 to 2012, this would mean at least an extension of four years, totaling in a new prescription period of 14 years; with even longer periods being possible of course.

## 7. Conclusio

Regarding the assessment of kickbacks from Swiss banks it has to be distinguished between asset management agreements and investment consultancy agreements. If an asset management agreement between a client and a bank or an asset manager exists it is imperative to examine potential claims based on wrongfully withheld kickbacks.

Apart from claims against asset managers, in case of an involvement of an entity administered in Liechtenstein which is entitled to kickbacks, it is also possible to assert liability claims against the bodies of the entity based on omission of enforcement of said claims. This leads to a *de facto* prolongation of the limitation period for wrongfully retained kickbacks, since the negligence of the bodies as of the date at which they become aware of circumstances which require certain actions – in this case the reclamation of kickbacks – makes the bodies liable to their respective entity; this liability is subject to an individual prescription period.

*Reference:*

Regarding the liability of bodies of legal entities see *Schwärzler/Wagner*, Verantwortlichkeit im liechtensteinischen Gesellschaftsrecht, 2nd Edition 2012; regarding kickbacks see also *Plüss*, Streit um Retrozessionen, liechtenstein-journal, 2009, 70 et seq.