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Retrocessions: New case law of the Swiss Federal Supreme Court

Judgment of 13 May 2020 (4A_355/2019)

Swiss Federal Court, https://www.bger.ch/index.htm, last visited on 07.10.2020

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Requirements for a waiver of retrocession (previous case law)

Extract from BGE 137 III 393 ("retro decision"):

[…] In order for an advance waiver to be valid, the client must therefore know the parameters necessary to calculate the total amount of retrocessions and allow a comparison with the agreed asset management fee. It is not possible to give an exact figure in the case of a prior waiver because the total amount of the assets under management is constantly changing and the exact number or volume of transactions to be carried out is unknown at the time of the waiver. In order for the client to be able to assess the scope of the expected retrocessions and compare them with the agreed fee, he must at least know the key figures of the existing retrocession agreements with third parties as well as the scale of the expected reimbursements. The latter requirement is satisfied in the case of advance waivers if the amount of expected refunds is expressed as a percentage range of the assets under management. The interaction of these two elements enables the client to assess the total costs of asset management and to identify the conflicts of interest existing at the asset manager due to the concrete incentive structures. […]

- key figures of the existing retrocession agreements with third parties («Eckwerte»)
- scale of the expected reimbursements («Grössenordnung»)

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Scale of the expected reimbursements

Extract from BGE 137 III 393 (retro decision):

[…] In order for an advance waiver to be valid, the client must therefore know the parameters necessary to calculate the total amount of retrocessions and allow a comparison with the agreed asset management fee. It is not possible to give an exact figure in the case of a prior waiver because the total amount of the assets under management is constantly changing and the exact number or volume of transactions to be carried out is unknown at the time of the waiver. In order for the client to be able to assess the scope of the expected retrocessions and compare them with the agreed fee, he must at least know the key figures of the existing retrocession agreements with third parties as well as the scale of the expected reimbursements. The latter requirement is satisfied in the case of advance waivers if the amount of expected refunds is expressed as a percentage range of the assets under management. The interaction of these two elements enables the client to assess the total costs of asset management and to identify the conflicts of interest existing at the asset manager due to the concrete incentive structures. […]

- Scale can be estimated by indicating percentage ranges ("Prozentbandbreiten")
- The reference value of the percentage ranges must be the assets under management

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Clarification by Judgment of 13 May 2020 (4A_355/2019)

- *The reference value of the percentage ranges must not be the invested assets, but the assets under management*
- *Reason: The scale of expected retrocessions must be determined or determinable at the time of the waiver*
- *Future investment volume is not yet known at the time of waiver, only the size of the assets under management*
- *Reference to invested assets is not permitted → no legal waiver*

Conclusion and outlook

- No change in practice by new judgement of 13 May 2020 (4A_355/2019), but clarification of previous case law.
- In practice, there are numerous waivers which refer to the invested assets rather than the assets under management as the reference value for the percentage ranges. These retrocessions have not been validly waived.
- It is still unclear what the Swiss Federal Supreme Court exactly means by "key figures of the existing retrocession agreements" ("Eckwerte")? In practice, there are no waivers where retrocession agreements with third parties are mentioned.

Consequences: Advance waivers of retrocessions are most likely always invalid

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Retrocessions: First case law of Liechtenstein Supreme Court

Judgment of 4 September 2020 (02 CG.2019.58)

Liechtenstein Courts, https://www.volksblatt.li/nachrichten/liechtenstein/Vermischtes/vb/257723/betrunkene-spritztour-endete-vor-gericht, last visited on 07.10.2020

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First Decision of Supreme Court in Liechtenstein on the topic of retrocessions

(OGH 09/04/2020, 02 CG.2019.58)

The Supreme Court confirmed the bank's obligation to return all retrocessions to the customer, irrespective of whether the customer concluded an advisory agreement with the bank or whether the relationship with the bank was an execution-only business relationship. In both cases, the Bank is obliged under contract law to return to the customer the benefits received from third parties.

In comparison, the Swiss federal Court did not yet confirm the obligation of the bank to surrender retrocessions in connection with execution-only relationships.

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Statute of limitations – 30 years!

(OGH 09/04/2020, 02 CG.2019.58)

Although the defendant did not raise questions pertaining to the statute of limitations (strategic decision), the Supreme court explained, obiter dictum, that the customer's claims for the surrender of retrocessions become time-barred only after 30 years.

In comparison, the Swiss federal Court ruled that such claims become time-barred after 10 years.

Requirements for advance waivers of retrocession (Pre-MiFID)

(OGH 09/04/2020, 02 CG.2019.58)

[…] „In both cases, a waiver requires certainty or at least sufficient determinability. If the waiver is so vague that the legal relationships to which it refers are not clear in advance and therefore the risks cannot be foreseen and calculated, it must be deemed invalid."[…]

The Supreme Court applied these principles to the case at hand and held that the Bank's clause was inadmissible because it was not clear whether the Bank was actually receiving any retrocessions and because there was also no information with regard to expected amount of retrocessions.

The waiver stemmed from 2004 and it remains to be seen as to whether the Supreme Court will apply the same principles to clauses which were implemented after MiFID I came into force.

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Requirements for advance waivers of retrocession (Post-MiFID) - new case: Submission to the EFTA Court

(OGH 04.09.2020, 09 CG.2018.166)

New case where Supreme Court has to decide on the admissibility of two advance waiver clauses under MiFID I regime.

Supreme Court referred the case to the EFTA Court for a legal opinion on art. 26 of Directive 2006/73/EC which requires financial service providers to disclose retrocessions to their costumers in advance.

The EFTA Court will now decide, inter alia, on the following questions:

- Does Directive 2006/73/EC allow for retrocessions to be disclosed in general terms and conditions or must the disclosure be individual for each client?
- What does a sufficient disclosure of retrocessions look like ("existence, nature and amount")?
- Can bank customers directly derive individual right from art. 26 of the Directive 2006/73/EC?

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Thank you for your attention!

Dr. Helmut Schwärzler MM