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The Launch of the Real Estate Investment Foundation

Reference: CapLaw-2015-41

While Swiss investment foundations have been used quite often for indirect real estate investments of Swiss pension plans in the past, recently, more market participants have been using the real estate investment foundation as an attractive real estate offering for their eligible clients. In addition to the general regulatory and civil law framework that applies to all Swiss investment foundations, some specific requirements must be observed for the launch of real estate investment foundations. This article aims to provide a brief overview on the applicable general and specific requirements.

By Sandro Abegglen / Luca Bianchi / Thomas Hochstrasser

1) Introduction

The tax efficient Swiss (real estate) investment foundation was created in order to serve as a regulated and collective investment structure for Swiss pension funds. Despite its major commercial relevance, it had previously not been subject to a dedicated, specific set of regulations. The structural reform with respect to pension fund regulation introduced a new, specific regulatory framework for the Swiss investment foundation which has had a major impact on its structuring and issuance process. In addition, investment foundations with a particular focus on real estate investments are subject to some specific requirements that one should be aware of when structuring such an investment vehicle.

This article aims to provide an overview of selected features of the legal framework (including documentation) to be observed in connection with the launch of Swiss real estate investment foundations.

2) Statutory Basis of Swiss Investment Foundations

Swiss investment foundations are regulated by articles 53g et seqq. of the Occupational Retirement, Survivors' and Disability Pension Plans Act (OPA). Detailed provisions solely applicable to investment foundations are set out in the Ordinance on Investment Foundations (IFO). Furthermore, the Ordinance on the Supervision of the Occupational Retirement, Survivors' and Disability Pension Plans (OPO 1) contains provisions that are relevant for the establishment of an investment foundation and the applicable regulatory approval process. In addition, the Ordinance on the Occupational Retirement, Survivors' and Disability Pension Plans (OPO 2) must be taken into consideration with respect to provisions regarding conflicts of interests and transactions with related parties that may apply by analogy. Notably, the rules governing (common) civil law foundations are subsidiary applicable. They are set forth in articles 80 et seqq. of the Civil Code (CC). Investment foundations are subject to direct supervision and must be (pre-)approved by the Occupational Pension Supervisory Commission (OPSC).

3) Aspects to be Considered for the Launch of a Real Estate Investment Foundation

a) General Aspects

The most crucial and time-consuming aspect of the creation and launch of an investment foundation is the designing of its internal organization. In practical terms, this means that a broad range of documents have to be produced (and pre-approved by OPSC), including, but not limited to, the foundation regulations, articles, organizational and other regulations, organization chart, description of activities and financial situation, business plan, management agreements, asset management agreements in the case of delegation of asset management to a third party and outsourcing agreements. The external asset manager of an investment foundation requires a regulatory asset management registration with OPSC (which should be distinguished from the regulatory product approval process concerning the investment foundation) or another accepted regulated status (*e.g.*, of a FINMA licensed bank, securities dealer, fund management company, or CISA asset manager).

In its approval process, the OPSC examines whether the irreproachable business conduct of the investment foundation can be granted. In particular, the members of the foundation board and the directors of the investment foundation must establish their know-how, expertise and integrity based on their CVs, their criminal and debt enforcement records, declarations regarding qualified shareholdings and pending proceedings as well as personal references. Not more than one third of the members of the foundation board may consist of persons that are entrusted with the management, administration or asset management of the investment foundation (respectively, their employees).

Investment foundations regularly launch a number of investment groups with different investment strategies. Each investment group is economically independent and managed autonomously. In the extremely unlikely event of the investment foundation's bankruptcy, the assets of each investment group would be segregated in favor of the investors of such investment group. The launch of an additional investment group can be executed much faster than the initial structuring of the entire investment foundation, respectively, the first investment group (subject to a pre-approval of the investment guidelines by OPSC in the event the investment group is involved in alternative investments or foreign real estate).

The circle of potential investors of an investment foundation is limited to tax-exempt occupational pension schemes with their domicile in Switzerland and collective investment schemes which are subject to supervision of the Swiss financial market supervisory authority FINMA, of which the investors' eligibility is restricted to occupational pension schemes. As a result, the investment foundation benefits from the same tax treatment as their investing pension schemes (which should be ensured by a tax ruling from the competent tax authorities).

Once the investment foundation and their investment group(s), respectively, are approved by OPSC and registered in the commercial register, the fundraising period begins. For this stage, the production of a road show presentation, a specific term sheet for each investment group and respective subscription forms or capital commitment agreements comprise the market standard in terms of documents that are used for the fundraising.

b) Aspects Specific to Real Estate Investment Foundations

i) Selected Regulatory Features

The formation of each investment group of a real estate investment foundation is subject to a regulatory prospectus duty. The real estate investment foundation is obliged to publish a prospectus before the subscription period for the relevant real estate investment group begins. Based on the OPSC-accepted market standard, such a prospectus is considerably shorter than, for instance, a prospectus of a FINMA-approved collective investment scheme. The prospectus must be filed with OPSC.

The real estate investment foundation has to establish investment guidelines which define the investment focus, the eligible investments, and the investment restrictions in a complete and coherent manner for each investment group. To the extent the investment focus of an investment group so permits, the investments must be diversified by regions, locations, and types of usages.

Generally, a maximum of 30 % of the assets of an investment group may be invested in real estate developments such as construction projects, construction land, unfinished construction buildings, and buildings subject to reconstruction. However, this threshold does not apply for investment groups that invest exclusively in such real estate projects. Real estate investment foundations are only permitted to purchase undeveloped properties if they are made accessible and the prerequisites for an immediate development are fulfilled.

The articles and regulations of a real estate investment foundation may provide for capital commitments from investors. Thereby, it can ensure that the real estate investment foundation can carry out capital calls at a point in time in the future when the capital will be required.

In principle, a leverage of up to one third of the total market value of the real estate portfolio of the real estate investment foundation is permitted (although it may be increased temporarily under certain conditions).

Transactions with related parties must be concluded at arm's length terms and disclosed to the auditor in connection with the annual audit. The auditor shall examine whether the interests of the investors have been safeguarded with respect to such transactions. In connection therewith, specific restrictions on transactions with related parties may be suggested by OPSC.

ii) Code of Conduct and Transaction Handbook

In addition to the above described documentation of an investment foundation, a number of further documents are regularly established. For instance, a code of conduct may be necessary in order to deal with conflicts of interest. Typically, a code of conduct contains sections on (i) general rules of conduct, (ii) the applicable laws and regulations (specifically, with respect to the rules of conduct), (iii) conflicts of interests (and particular means and methods to avoid them or to exclude that they adversely affect the interests of the investors), (iv) transactions with related parties, (v) further organizational rules, and (vi) rules on market conduct (including own-account/employee transactions). An elaborate code of conduct may not only be a regulatory requirement, but also protects the responsible directors and officers against accusations of having acted under conflict to the detriment of the investment foundation and its investors.

Furthermore, so-called "transaction handbooks" may be created in order to deal with specific issues of proposed types of real estate acquisitions or disposals. The transaction handbook sets out additional and more detailed rules when compared with those included in the general investment process description of the real estate investment foundation. Typically, a transaction handbook contains detailed guidelines and restrictions for the selection of target investments (including, the regulatory and civil law requirements to be observed, the due diligence and evaluation process as well as the settlement and timeline of the transaction). Transaction handbooks are used frequently for large real estate transactions and may become quite sophisticated in case of regulated parties and/or complex package transactions.

4) Conclusion and Outlook

The considerable flexibility in structuring real estate investment foundations, in particular when compared with other regulated investment structures, make them an attractive offering for pension plans seeking exposure to and yield from the real estate market. This, nevertheless, remains true despite the structural reforms that have led to a more detailed regulatory regime. The familiarity of institutional investors with the investment foundation and its oversight by a recognized, Swiss supervisory authority increase the attractiveness of the real estate investment foundations, not only for investors, but also for product providers/asset managers. Finally, the relatively fast approval process, contingent upon the quality of the application by the respective applicants, also speaks in favor of this investment vehicle from a time-to-market perspective. For these reasons, and due to the ever more urgent economic need to allocate capital in the real estate segment, we may see a significant number of new launches of real estate investment foundations/investment groups in the near future.

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EU Recognises Swiss (Re)Insurance Supervision as Equivalent

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On 5 June 2015, the European Commission recognised the Swiss (re)insurance supervision system as being fully equivalent with the Solvency II Directive. The European Commission recognised in particular the equivalence of the Swiss system in three areas, such as reinsurance, solvency calculation and insurance group supervision.

By Petra Ginter

1) Introduction

The European Insurance and Occupational Pensions Authority (EIOPA) has conducted a detailed assessment on the equivalence of the Swiss (re)insurance supervision system with the Solvency II Directive (Directive 2009/138/EC, as modified by the "Omnibus II" Directive 2014/51/EU) which will be fully applied from 1 January 2016. The Solvency II Directive will introduce a modernised risk-based prudential and supervisory regime for (re)insurance undertakings in the European Union.

Switzerland is the only third country whose insurance regulation the European Commission has recognised as equivalent in full and for an indefinite period. It appears that the EU has positively recognised the regulatory framework and (re)insurance supervision in Switzerland, and in particular the changes that have been introduced with the revision of the Swiss Insurance Supervision Ordinance (ISO). The EU recognition of the equivalence of the Swiss (re)insurance supervision system enhances the reputation and competitiveness of Switzerland as a global financial centre.

The decision of the European Commission shall enter into force on the twentieth day following its publication in the Official Journal of the European Union.