SwissBanking

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Swiss Banking – Roadmap 2015

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Editorial

Dear Reader

Switzerland's financial service providers, with banks leading the way, enjoy a respected position on the international scene. They are among the world's market leaders in many areas and, with a share in the country's overall value added of 15%, represent the most important sector of the Swiss economy, making a key contribution to the country's prosperity and standard of living. In order to ensure that this remains the case in the future, the banks, under the aegis of the Swiss Bankers Association, have carried out a careful analysis of individual areas of business that are particularly important for the future and worked out specific measures that are essential for continued success. Together with input from other members of the financial community, such as insurance companies, the funds industry and the SWX Swiss Exchange, these findings will provide the foundation for an overarching 2015 financial centre strategy. The objectives and measures drawn up are intended as a basis for discussions with politicians and government authorities aimed at ensuring that the economic contribution made by the financial sector remains high over the years to come and that Switzerland does not fall behind in global competition with other financial centres.

We are pleased to present this brochure, containing the key findings from the analysis for the banking sector.

Pierre G. Mirabaud
Chairman, Swiss Bankers Association

Summary

The financial industry accounts for 15% of Switzerland's economic value added, making it the most important sector of the country's economy and a crucial pillar of its prosperity. The Swiss financial centre is also the world's biggest cross-border asset manager. However, this success – which is based to a large part on the effective protection of privacy (bank-client confidentiality) – should not be taken for granted: competition in the global financial industry is fierce, both between individual players and, in particular, between the different financial centres.

With a view to ensuring that the Swiss financial centre remains competitive and can become even more successful in future, the banks in Switzerland, under the aegis of the Swiss Bankers Association (SBA), have conducted a comprehensive analysis of opportunities and risks and have drawn up a roadmap for the future of Switzerland as a banking centre. The resulting objectives and measures are intended as a basis for discussions with politicians and government authorities, and have been drawn up with a view to sustaining and fostering Switzerland's position as a financial location. This analysis is to be complemented by similar studies from other members of the financial community, ultimately resulting in a consolidated and coherent financial centre strategy.

Central to this investigation are areas of business which have major growth potential or already enjoy a very good position and need to be further strengthened. The focus is on the following eight areas of business:

- private banking;
- retail banking;
- investment funds;
- pensions business;
- hedge funds;
- private equity;
- Swiss capital market;
- commodity trade finance.

These eight areas of business have been analyzed in detail as part of a broad study. Developments in the different segments over the last ten years have been compared with those seen in the Swiss financial centre's direct competitors (London, New York, Luxembourg, Singapore or Ireland). This location analysis has been used to form a clear picture of the prospects for the future and to determine what action is needed in the different areas of business in order to enhance the competitiveness of the Swiss banking sector.

On this basis, more than seventy specific institutional, regulatory and tax-related measures have been drawn up, of which, after careful deliberation, twenty were given priority status and included in this position paper. Core elements of these proposed measures aimed at realizing the growth potential of the Swiss financial centre are:

- strengthening competitiveness in tax matters;
- strengthening competitiveness through appropriate implementation of international standards while maintaining bank-client confidentiality;
- fostering the effectiveness of the authorities in matters relating to Switzerland as a financial centre;
- fostering the attractiveness of Switzerland for collective investment schemes;
- improving the framework conditions for trusts and foundations;
- making the regulatory framework more flexible for pension funds business.

One key to success is to ensure better coordination of current and future measures with the authorities. With this in mind, regular discussions are to be put in place between the senior officers of the different associations, the authorities and politicians.

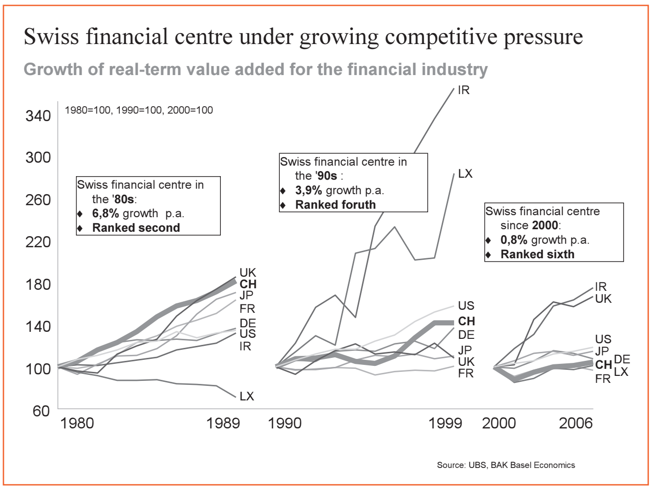
We firmly believe that a well-functioning and competitive financial sector is essential to every economy and ultimately helps to ensure the well-being of the country's citizens. We are pleased, therefore, to be able to make a contribution, through this position paper, to an in-depth discussion of the future path to be taken by an important part of the Swiss economy.

Overview of the study

Future success has to be earned

With a share in national economic value added of 15%, the financial industry is the most important sector of Switzerland's economy and makes a decisive contribution to the country's prosperity. However, this success is not set in stone and needs to be earned anew every day. Switzerland is internationally recognized as a financial centre and has a leading position in individual sectors such as asset management. Competition in the global financial industry is fierce, not just at company level, but also between the different financial centres. It is against this backdrop that the Swiss financial centre and its protagonists must make their presence felt. Many financial services are already being bought in from other countries, and it is there that the value added is being created. Competitive pressure on the Swiss financial centre remains at a high level.

If the Swiss financial centre is to remain competitive, action is needed. The banks, under the aegis of the Swiss Bankers Association (SBA), have therefore conducted a comprehensive analysis of opportunities and risks and have drawn up this position paper, based on a detailed study. The objectives and measures derived are to form the basis for discussions with politicians and government authorities. The analysis is to be complemented by similar studies from other members of the financial community, resulting finally in a consolidated and coherent financial centre strategy.



The institutional, regulatory and tax framework has a crucial role to play in the potential of individual areas of business. The way an initial advantage can be squandered more or less overnight, to the benefit of other financial centres, has been demonstrated in recent decades with the migration of the gold business or of fund production out of Switzerland. In contrast, the recent growth in structured products promises positive developments. Shares in a global marketplace will only be maintained or won if business, legislators and regulators are pulling in the same direction. There are clear examples of how focused measures can lead to very positive financial sector outcomes (e.g. the "Big Bang" in London).

This investigation focuses on eight areas of business: private banking, retail banking, investment funds, pensions business, hedge funds, private equity, capital market business and commodity trade finance. All these areas have significant growth potential or already enjoy a very good position which needs to be maintained.[1]

In drawing up this paper, the aim of the Swiss Bankers Association (SBA) is to help foster Switzerland's position as a financial location: similar initiatives have been undertaken in the past, such as the SBA study of February 2003: "Swiss Banking: a programme for the future". In view of the strategic importance of systematically promoting Switzerland as a financial centre, a precise and fundamental analysis of the framework conditions needs to be carried out at regular intervals. With this in mind, the present document is part of a global and integrated study of developments in the financial sector in Switzerland and abroad.

In order to enhance the competitiveness of the Swiss financial centre, the banks aim to ensure that new business opportunities can be tapped and effectively exploited. Switzerland's banks need to pay particular attention to:

- the maintenance of financial privacy;
- outstanding advisory and service quality;
- a competitive cost-earnings relationship or a high level of productivity;
- innovation and technology (in particular, the ongoing development of different services);
- responsible reputation and risk management;
- overall attractiveness as a "location of choice" for internationally-mobile and highly-qualified employees.

Core elements and aspirations

From a strategic point of view, certain core elements of the national framework are essential for the well-being of the financial centre. They form the basis for the other framework conditions, which have to be adapted to current requirements from an "operational" point of view. One of these core elements is the importance attached to protecting financial privacy, which itself is based on a democratic decision of Switzerland's citizens. Additional core elements are

- political stability;
- the guarantee of Swiss National Bank policy aimed at ensuring stability;
- a modern, efficient, reliable and independent financial centre infrastructure;
- sound, market-based supervision and regulation, which ensures legal security and a level playing-field in the international context;
- the importance attached by government authorities to ensuring equal status and mutual recognition for our financial market rules in the international sphere and freedom from discrimination in market access;
- an attractive economic policy environment (in particular, tax framework);
- up-to-date, practice-based education and training at all levels.

The objectives or aspirations can be summarized as follows.

The Swiss financial centre

- is to remain the world's market leader in international asset management. The asset pool generated by this is central to the success of the financial centre as a whole.
- is to be a centre for innovative new financial instruments with global reach. Affluent international clients expect innovative products with significant potential for diversification.

In order to realize these aspirations, the Swiss financial centre

- depends on an independent legal framework that meets high international standards and enables providers to meet national and international needs in a tailored and flexible way.
- seeks further to reduce international barriers to market access in order to be able to take advantage of the opportunities arising from globalization.
- supports cooperation between different supervisory authorities and mutual recognition of equivalent regulation and supervision.

[1] No detailed analysis has been conducted of areas of business in which the Swiss financial centre has little chance of creating a significant cluster by international standards (see details on pg. 6f below).

Crucial to Switzerland's prosperity

The financial sector is of major importance to the Swiss economy as a whole. It accounts for 15% of overall value added and around 16% of all direct and indirect tax receipts. 200,000 people, or 5% of the entire workforce, enjoy above-average pay. Productivity in the financial industry, at CHF 337,000 per employee, is around three times higher than the Swiss average. Banks train 3,600 or 12% of all apprentices. Banks in Switzerland commission services from third parties to the value of several billion Swiss francs every year. Substantial contributions are made to education, sponsorship and charitable foundations. These services to the economy are recognized and appreciated by the people of Switzerland, with 90% stating that they think the sector makes an important contribution to the overall economy. A well-functioning and competitive financial centre is essential to any economy, featuring market-led capital allocation for investments, intermediation between savers and investors, and a platform for payment transactions. The financial sector is indispensable for the domestic and international operations of Switzerland's open economy.

Important domestically and internationally

The Swiss financial sector supports effective domestic regulation, which seeks to achieve its aims with the minimum possible intervention in the market. The guidelines on financial market regulation issued by the Federal Department of Finance in September 2005 are a step in the right direction, but they still need to be implemented. There is still a tendency to over-regulate, in Switzerland as elsewhere.

With regard to international operations, the banks wish to achieve as much freedom of market access as possible within the framework of the WTO. In relation to the EU, the analysis in almost all the areas of business shows that lack of access to the EU single market is of central importance, particularly on the retail side. The SBA has analyzed the advantages and disadvantages of a financial services agreement with the EU and found that currently the disadvantages outweigh the advantages. Switzerland would systematically have to take on board EU laws, which hardly equates to mutual recognition of legislation. Furthermore, the individual EU countries retain a great deal of autonomy in matters of consumer protection. The objective, rather, is non-discriminatory market access (based on mutual recognition of equivalent [but not the same] regulation) and the creation of concrete solutions at a technical level.

Tax, regulation and supervision in focus

The subject of this comprehensive investigation is national and international market structures and the regulatory, tax and supervisory framework conditions in Switzerland and the main rival financial centres such as London, New York, Luxembourg, Singapore and Ireland. The eight areas of business mentioned above were selected for close investigation because they appear to offer special business potential or to bear some relevance to the competitiveness of the financial centre. The emphasis was on looking at measures which can be initiated or implemented in Switzerland in the next legislative period. Of particular importance were the presence of clusters or conditions favourable for their emergence, i.e. situations in which a number of financial service providers form a critical mass for expertise and services, specialists are available, and related servicing sectors can establish themselves. For this reason, no detailed investigation was conducted for areas of business in which the Swiss financial centre has little chance of forming a significant cluster in international terms.

Offensive and defensive measures

For the individual areas of business, a range of primarily "offensive" measures were identified, i.e. measures which would serve to improve the relevant market environment in Switzerland. On the other hand, in the private banking area in particular, "defensive" measures predominate, aimed at preventing the framework conditions from deteriorating. It goes without saying that these defensive measures are central to the area of business which creates by far the biggest share of value added. In some areas of business, such as retail banking, investment funds and pension funds, international growth in terms of EU market access and cross-border business is limited. Here, efforts need to be focused on making individual, specific improvements. Swiss regulation should be adapted as far as is possible and appropriate to European legislation, and the competitiveness of the domestic sector should be strengthened such that efficient markets can be formed. There is a high level of potential in newer areas of business such as private equity and hedge funds, where things have not yet settled down and regional clusters are only just beginning to form. Switzerland as a financial centre with global reach must do everything it can to achieve a leading market position in these areas of business. Niche areas like trade finance need to be further expanded. One of the key prerequisites for sustained success in all business areas is world-class education and training at all levels. The establishment of the Swiss Finance Institute at university level was a good move. But similar efforts are also necessary at other levels.

The proposed measures aimed at achieving the ambitious objectives set, and their positive impact on the individual areas of business, are summarized in the table below.

Better coordination of all current and future measures with the authorities is vital if the proposed measures are to be implemented successfully. With this in mind, regular discussions are to be set up between the senior officers of the different associations, the authorities and, of course, politicians.

Measures	**Effects on areas of business**
Strengthen competitiveness in tax matters	Makes Switzerland more attractive for investment funds, private equity and hedge funds. Strengthens Switzerland's leading role in private banking. Impacts positively on retail, trade finance and capital market business.[2]
Strengthen competitiveness through appropriate implementation of international standards	Appropriate implementation of 40+9 FATF recommendations while maintaining bank-client confidentiality, clear procedures in administrative and legal assistance, credible insider trading provisions and a clear stance towards the EU are essential for private banking, retail banking, trade finance business and capital market business.[3]
Foster the effectiveness of the authorities in matters relating to Switzerland as a financial centre	Better staff resources and a more collaborative approach with the approval, tax and commercial register authorities will be favourable in particular for investment funds business, hedge funds business and private equity business.[4]
Foster the attractiveness of Switzerland for collective investment schemes	More flexible investment rules will enable a free and risk-based investment strategy for qualified investors. Easier registration will be favourable for investment funds and hedge funds business. Greater legal security in distinguishing between retail and qualified investors is a location advantage for private equity.[5]
Improve the framework conditions for trusts and foundations	Improved legal framework in Switzerland and in the taxation of foreign trusts are of great importance for private banking.[6]
Greater flexibility in the regulatory framework for pension funds business	Opens up greater scope in investments, more freedom to choose for investors and new business opportunities for the pensions business in Switzerland and abroad from Switzerland.[7]

[2] See proposed measures 1.3, 1.6, 2.1, 3.2, 5.1, 5.4, 6.1, 6.5, 7.1 and 8.3.
[3] See proposed measures 1.2, 1.4, 2.2, 7.2, 8.1 and 8.2.
[4] See proposed measures 1.5, 2.3, 3.3, 5.2, 6.2, 6.3 and 8.4.
[5] See proposed measures 3.1, 3.4, 5.3 and 6.4.
[6] See proposed measure 1.1.
[7] See proposed measures 4.1, 4.2 and 4.3.

1 Private banking

Aspiration

- Switzerland is to remain the world market leader in international asset management.

High value added per employee

Private banking is a core competence of the banks in Switzerland and is the biggest area of business overall. Private banking contributes around a half[8] of the banks' overall share of value added, making it a very important pillar of the Swiss economy. As well as the two big banks, private banking is carried out by 14 "pure" private banks with unlimited liability partners, almost 60 other private banks, some cantonal banks and 130 foreign banks. At the end of 2006, the value of securities held in bank custody accounts in Switzerland was almost CHF 5,017 billion.[9] Of this, around 42% is accounted for by domestic clients and around 58% by foreign clients; institutional investors have a share of around 57%. Value added per employee is about four times the Swiss average. With a share in the world market in cross-border asset management of around 30%, Switzerland easily outstrips all other international financial centres. Singapore, the biggest of the emerging Asian financial centres, is around ten times smaller than Switzerland in terms of assets under management, but is growing significantly more quickly than the Swiss financial centre.

Ongoing adjustment of the business model

This area of business is vital for Switzerland. The domestic and international framework conditions are of great importance. The banks are faced with a dual challenge. Firstly, they need to adapt their business models to prevailing business trends on an ongoing basis. Secondly, national and international regulation and tax frameworks need to be permanently monitored at all levels, and influenced with a view to retaining leadership of the world market.

Globalization presents both opportunities and risks. On the positive side, there is the chance further to expand onshore business worldwide as a result of improved market access. At the same time, however, competition among offshore centres is becoming stiffer, leading, for example, to increased pressure on Switzerland as a booking location. New competitors such as hedge funds and private equity are bringing additional impetus to the private banking market and are likely to drive fragmentation forward. The choice of an optimum business model is becoming ever more important. Clients want comprehensive financial advice and performance, not just investment tips. Banking is becoming more complex and makes considerable demands on bank staff. Recruiting and retaining highly-qualified and effective staff is a very critical factor for growth.

In terms of regulation, a number of legislative improvements have been introduced in Switzerland in

[8] The share of value added accounted for by the banks in Switzerland is around 9.6% (financial sector as a whole 15%), that of private banking 5%.

recent times. These include, for example, easier international administrative assistance in stock market supervision, ratification of the Hague Trusts Convention, and plans for integrated financial market supervision (FINMA), which should help further to improve the international reputation of the financial centre.

The internationally-accepted protection of privacy (bank-client confidentiality) remains important for the success of private banking. With the EU, the retention of bank-client confidentiality has been assured for the long term through three bilateral agreements (savings tax, fraud agreement and Schengen/Dublin). However, it is to be assumed that exchange of information in financial and tax matters will remain on the agenda at various international organizations. National provisions on the protection of privacy in financial matters could be called into question as much as the principle of double criminality or the principle of speciality.

In some EU countries there remain regulatory hurdles which make cross-border market access for banks based outside the European Economic Area (EEA) much more difficult. Globally, the trend towards international standard-setting in the supervisory field by overarching bodies is increasing. In principle, that makes sense, but their authority is not always clear, and Switzerland's position on these bodies also often lacks clarity.

In terms of regulation, benchmarking with other countries also needs to be better. This is not simply a matter of comparing regulations. Rather, Switzerland needs to look more towards what is implemented in comparable financial centres before striving for perfection itself.

Measures

In order to ensure the development and growth of private banking, the framework conditions need to be simple and flexible and provide a high level of legal security. Pragmatism, i.e. a willingness to solve problems practically and unbureaucratically, has played a significant part in the current success of private banking. This attitude must be retained and further fostered. To achieve this, the following measures are necessary:

1.1 Improvement of the framework conditions for foreign trusts and foundations by amending civil and tax law.

1.2 Consistent stance with regard to the Swiss-EU savings tax agreement with a view to continuing the co-existence model.

1.3 Elimination of turnover tax. This should preferably be phased out, i.e. the tax should be eliminated gradually through successive annual reductions in the rate (as for measure 2.1).

1.4 Appropriate implementation of the 40+9 FATF recommendations while maintaining bank-client confidentiality (no additional due diligence and monitoring obligations in trading and with regard to commodity and trade finance, see measures 2.2 and 8.2).

1.5 Ensuring clear processes and procedures in administrative and legal assistance (prevention of "fishing expeditions" and indiscriminate blocking of accounts, see also measure 8.4).

1.6 Clear and internationally-competitive tax framework for hedge funds and private equity fund managers in Switzerland (as for measures 5.1 and 6.1).

[9] At mid-2007 the value of securities held in custody accounts (excluding cash and fiduciary deposits) in Switzerland stood at CHF 5,400 billion.

2 Retail banking

Aspiration

- Provision of services for personal and corporate clients, which are of first-rate quality in international terms and are competitively priced.

Open, heavily fragmented market

The term “retail banking” refers, on the one hand, to mass-market banking services focusing on persons with net assets of up to around CHF 250,000 as a client group. The services offered include personal current and savings accounts, simple structured investment products, mortgages, consumer credit, debit and credit cards and payment transactions. On the other hand, retail banking also includes financial services provided to small and medium-sized firms, such as payment transactions and simple structured forms of financing. With the exception of those banks that focus exclusively on private banking, all banks operating in Switzerland offer all or some of these services. More so than in the case of other financial products, in retail banking it is not only the production of financial services but also their distribution which is very important. In Switzerland, banking density is very high and the market is heavily concentrated and competitive. From a regulatory point of view, the market, unlike some EU markets, is an open one.

The market for consumer credit is still relatively new in Switzerland and, in an otherwise saturated retail market, offers the greatest potential for growth. The Swiss credit card market is saturated, profitable and subject to increased competition from new providers. The leasing business is gaining in importance in various areas. Thus, in capital goods leasing, in particular, there is market potential. The leasing ratio in the years 1999–2004 was an average of 9.7%, while the average figure in the EU was almost 13%. The mortgage market posts growth rates in Switzerland which on average are above GDP growth. The Swiss market is the sixth-largest in Europe. For demographic reasons there is likely to be increased demand for apartment ownership and reduced demand, in particular, for house ownership. Bank credit is a central element in corporate finance. In recent years, clients have become more professional and sophisticated in their requirements. Competition in this market is mainly based on price. With the credit rating system introduced in the 1990s, the Swiss banks have a leading role in Europe.

Switzerland as a retail hub not a strategic option

Retail banking services are increasingly becoming “commodities”. They are following the classic path of industrial development, whereby prices fall as the market matures. Client processes have a high rate of recurrence, and therefore standardization offers significant potential for cost savings.

The monitoring of and adherence to laws result in high compliance costs. This revolves mainly around money laundering, consumer credit, stock market and data protection laws. In tax terms, the main taxes are those on individuals and companies as well as, in particular, withholding taxes and turnover tax, which is an anachronism in international terms. Regulatory measures abroad, such as MiFID, the introduction of a Single Euro Payments Area (SEPA) and more difficult market access for financial services from Switzerland in third countries also have implications for retail banking in Switzerland. From a location point of view, there are risks because of the differing regulatory developments between Switzerland and the EU. New barriers to market access may result. Without free market access, the creation of a hub in Switzerland for retail banking services in Europe is not an attractive option and thus does not represent a strategic priority.

Measures

The focus of the measures below is on the market perspective, i.e. competition and structures in the Swiss domestic market.

In comparison with other areas of the financial sector, there is no great need for action in terms of regulation and tax in retail banking. From a market perspective, positive conclusions can be drawn. The market for retail banking is open and liberal. The following measures remain necessary in this area of business:

2.1 Elimination of turnover tax. This should preferably be phased out, i.e. the tax should be eliminated gradually through successive annual reductions in the rate (as for measure 1.3).

2.2 Appropriate implementation of the 40+9 FATF recommendations while maintaining bank-client confidentiality (no additional due diligence and monitoring obligations in trading and with regard to commodity and trade finance) (as for measures 1.4 and 8.2).

2.3 Further development of the recently introduced measures and the complete revision of VAT reform to counter the excessively formalistic approach taken to VAT. Improvement of the "VAT climate" between tax payers and the authorities in assessment and procedural practice.

3 Investment funds

Aspiration

- To establish Switzerland as one of the top three production locations for investment funds in Europe.
- Provision of products to cover a broad investment spectrum for private and retail clients.

Potential as a distribution location

The Swiss funds market is made up of distribution and production. However, currently Switzerland is only well positioned as a distribution location. Though previously a major production location, Switzerland has continually lost ground to Luxembourg and Ireland. Assets managed by investment funds domiciled in Luxembourg are around CHF 3,000 billion (and in Ireland the total is around CHF 1,200 billion), while assets managed by investment funds domiciled in Switzerland total CHF 200 billion. This "decline" can be partly ascribed to a lack of flexibility in the regulatory framework and the tax regime. In addition, lack of market access for Swiss funds in EU member states is a hindrance to Switzerland's growth as a production location. The new Collective Investment Schemes Act (KAG) is designed to provide focused assistance to Switzerland as a production location in the future. Since, in this area in particular, international framework conditions tend to change quickly, there is further need for adjustment in regulatory conditions.

Collective investment schemes are required by various sets of investors. Whereas, in the past, structured, traditional investment funds for a long time mainly attracted small savers, production innovations in the area of alternative investments have since led to a considerable increase in institutional funds business. Unlike in the area of retail funds, there is considerable growth potential here, as an attractive segment of investors can be provided with special, tailor-made solutions. With regard to jobs, the downstream value added chain is important. Over the lifetime of collective investment schemes, various services such as fund administration, global custody and portfolio management need to be provided.

Passive instruments such as exchange-traded funds (ETFs) have very low margins but are growing sharply overall and are becoming more and more popular. On the other hand, actively managed funds invested in traditional asset classes still make up a very large part of the market but are showing little growth now. Because of scale effects, retail products like these are produced at least expense in the major hubs of Luxembourg and Dublin. Another attractive growth segment is that of alternative instruments, which usually produce higher returns than traditional products. Though they are cost-intensive because of the research and portfolio management work involved, they nonetheless still enjoy high margins.

Unfavourable framework conditions in all areas

Two main factors will determine the future positioning of Switzerland as a fund location. The lack of EU market access is likely to have a negative impact on the future growth of Switzerland as a production location. Nonetheless, a services agreement with the EU on the basis of EU laws is not sought since the disadvantages outweigh the advantages currently, yet mutual product licensing on the basis of reciprocity should be looked into. In contrast, prospering asset management business will have a positive effect on Switzerland as a distribution location.

In comparison to the fund locations of Luxembourg and Dublin, Switzerland has significant regulatory, institutional and tax disadvantages.

Thus, for instance, in terms of regulation, the detailed design of the Swiss SICAV involved some stiffer requirements or requirements alien to actual practice, when compared with Luxembourg's regulations. Things are similar in the definition and handling of qualified investors. In institutional terms, insufficient staff resources at the supervisory authority are a negative factor. And the tendency towards an excessively formalistic approach, a lack of pragmatism and inconsistency in approval decisions will help little in promoting future growth. This means that investor protection practices and higher Swiss standards will hinder new areas of business being tapped successfully.

The unfavourable tax framework (stamp duty) which caused the migration of the Swiss funds business to Luxembourg in the mid-1980s has now been ameliorated somewhat. The main tax problem, however, is that earnings from Swiss investment funds continue to be subject to 35% withholding tax, disadvantaging Swiss funds as against foreign ones.

Measures

In the investment funds area, the measures are focused on improving growth potential in the domestic market. An aggressive positioning of Switzerland as an international production hub is a major challenge for the medium term in view of the uncompetitive regulatory, institutional and tax framework. It is unlikely that we will see a repatriation of the areas of business that have migrated to Luxembourg or Dublin. But we can learn from past errors. The following are the main measures:

3.1 In the case of collective investment schemes open only to qualified investors, investment rules are to be made more flexible in order to allow as much freedom as possible in designing investment strategies in line with the size and the risk capacity and profile of the qualified investor.

3.2 Creation of improved framework conditions for collective investment schemes in terms of withholding tax (as for measures 5.4 and 6.5).

3.3 Strengthening of staff resources at the supervisory authority from a quantitative and qualitative point of view, especially for investment funds and private equity. Of importance, for instance, is focused knowledge transfer (e.g. through secondments in the financial industry or training in certain subjects by experts from financial service providers). In addition, direct consultative discussions with the approval authority should be established (as for measure 6.3).

3.4 Registration of hedge funds should be made easier. Following the Luxembourg model, the introduction of a "shelf-registration" procedure would be a worthwhile aim, permitting hedge fund administrators with prior authorization to set up new funds structured along predefined lines within a short space of time (as for measure 5.3).

4 Pensions business

Aspiration

- To win market share across Europe in the extra-mandatory segment.
- Swiss clients should receive the best possible access to a broad range of investment products.

Three-pillar system an export hit

Since 1985, the Swiss pension system has been legally based on three pillars: state provision on a pay-as-you-go basis (federal old age and survivors' insurance), occupational provision on a fully-funded basis, and private voluntary pension plans. Switzerland's three-pillar approach is regarded as a model system internationally. The main strengths are the high level of capital cover at over 110% of GDP and the broad coverage. The target pension level from pillars 1 and 2 is around 60% of final salary.

The EU pension fund sector is growing rapidly. In the next ten years, average annual growth of assets under management can be expected to be almost 7%. Assets will double by 2015 to almost EUR 9,000 billion. This growth offers new business opportunities for the financial services industry, particularly with the ongoing improvement in the regulatory framework. The (potential) business opportunities (fee pool) from European pension funds are likely to increase by 7% a year to over EUR 24 billion by 2015. The estimated fee pool for the Swiss pension fund sector was EUR 1 billion in 2005, or around 8% of the European market.

Growth opportunities in the extra-mandatory segment

Despite its strengths, the Swiss three-pillar system also has some weaknesses. Parameters fixed by the authorities hinder efficient asset allocation, and cantonal supervision is no longer in line with modern governance principles. Furthermore, the pension fund market is too fragmented for Switzerland's small size, with over 8,000 pension schemes. Finally, lack of competition leads to inefficiencies in service provision. Ageing populations and insufficient cover are leading to improved regulatory frameworks for private pension plans in European countries. The trend is towards liberalization, with a view to extending the investment and risk management options of pension funds and strengthening supervision. A cross-border market will slowly be established. Ireland and Luxembourg have already introduced measures to benefit from this. In a similar way to the market for investment funds, the European pension fund market is likely to see the emergence of "centres of excellence" with favourable regulatory frameworks. The provision of integrated management services, i.e. of services covering the entire value added chain, is the way forward for the future. However, "centres of excellence" for pension management will only emerge where this demand can be satisfied. Switzerland is running the risk of being excluded from Europe's growing cross-border retirement provision business and the advantages this brings with it as a result of lack of market access or uncompetitive regulations.

Necessary adjustments in occupational retirement provision in Switzerland should always be approached with a view to improving the country's competitive position in the future cross-Europe pension fund business. Two main legal differences between the EU and Switzerland will have a negative impact. Firstly, the EU relies much more on the precautionary principle, which replaces quantitative restrictions on asset allocation. Secondly, the EU is introducing the principle of origin in relation to the mutual recognition of supervision in all member states. This system is not compatible with the decentralized Swiss system, in which supervision lies with the cantons. The standardization of regulatory frameworks (in all cantons and the entire insurance and pension fund sector) for the whole of Pillar 2 provision should therefore be implemented as swiftly as possible in order to enable product recognition.

Full access to the growing European pension fund market for Swiss financial service providers is not realistic. Nonetheless, the regulatory framework for pension funds should be improved and adapted to European standards. The less regulated extra-mandatory segment in particular continues to offer international growth prospects.

Measures

We propose some changes and improvements which will strengthen the Swiss pension system and may help to close the gap vis-à-vis the changing regulatory frameworks for pension funds in Europe. The following measures are necessary:

4.1 Moving away from parameters fixed by the authorities for asset allocation and shifting towards use of the precautionary principle. Greater flexibility in investment rules through adjustment of requirements depending on size and risk capacity of pension funds.

4.2 Tapping of new business opportunities for pension fund pooling from Switzerland for recipients in Europe and other countries. In particular, an optimal tax framework needs to be ensured for this.

4.3 Distinction between mandatory and extra-mandatory segment of Pillar 2. Removing the capital guarantee for vested benefits would provide a genuine choice and would represent the first step towards freedom of choice for mandatory pension scheme provision.

5 Hedge funds

Aspiration

- Establishment of Switzerland as one of the top three locations for the production and distribution of hedge funds in Europe.

Enormous growth potential

Hedge funds (collective investment structures that have generally flexible investment strategies characterized by a low correlation with traditional investment products and an active and complex investment approach) have experienced dynamic growth in recent years. There is a structural distinction between single hedge funds (SHFs), i.e. investment vehicles which invest directly in the market, and funds of funds (FoFs), which invest in different single hedge funds. The global volume for hedge funds is estimated at USD 1,600 billion. Volumes in hedge fund investments in Switzerland are likely to be around USD 100 billion. Of this, more than 90% is invested in FoFs, managed by around 100 different companies. Overall in Switzerland, more than 2,000 people are employed directly and indirectly in this sector. Initial clusters have formed in the regions Geneva/Lausanne, Zurich/Zug/Pfäffikon and around Lugano.

The global hedge funds market is set to grow to USD 2,400 billion by 2009. The market is driven by the desire for risk diversification on the part of broad classes of investors and increased interest from institutional investors. Europe's relative share of 27% in 2006 will increase to 35% in 2009. As a location, Switzerland has benefited very little from this promising area of business. Only around 150 funds are domiciled in Switzerland, in contrast to more than 7,000 in the Cayman Islands. And while management companies based in Switzerland manage around USD 8 billion in assets in SHFs, the figure in the UK is around USD 270 billion. The siting of the administration and management of funds are particularly attractive for Switzerland.

Optimal starting position endangered by tax mistakes

Increased siting of hedge funds and their managers in Switzerland will generate new, highly skilled jobs with corresponding tax receipts, and will create work for other sectors (e.g. legal advisors, auditors, analysts, accountants and due diligence, IP and IT specialists). As a location, Switzerland would be predestined for a significant market share because of the high level of assets under management, the professionalism of the service providers working in related areas and the country's high standard of living. With regard to the regulatory framework for management companies, Switzerland has a liberal regime. And the costs for qualified staff and services in Switzerland, in comparison to other hedge fund domiciles such as the Cayman Islands or/and centres for management companies such as London and New York, are absolutely competitive.

Despite these positive factors in favour of the Swiss financial centre, Switzerland is relatively insignificant as a hedge fund domicile or location for SHF managers. The regulatory, institutional and tax framework works against the siting of SHFs in particular. With regard to institutional factors, for instance, approval processes are quite long in international terms, while at advisor level the lower numbers of well-trained staff at Swiss banking locations in comparison with London or the New York conurbation is a factor. The labour market for highly-qualified staff from non-EU countries therefore needs to be liberalised further if the hedge funds area of business is to meet its full potential. Taxation of fund managers is also a major hindrance. If this issue cannot be resolved in suitable fashion, the increase in attractiveness envisaged as a result of the Collective Investment Schemes Act (legal form of limited partnership for collective investment schemes) will remain nothing but a theory.

Measures

The distribution of hedge funds can make the biggest contribution overall to Switzerland's value added chain. In this regard, Switzerland is well positioned and will do well to ensure that framework conditions remain attractive. Particular catch-up potential and positive spill-over effects are available in fund domiciling and the siting of management companies. The following bundles of measures are thus focused on measures for the siting of hedge funds and ways of making Switzerland a more attractive location for hedge fund advisors. The following measures are necessary:

5.1 Clear and internationally competitive tax framework for hedge funds and private equity fund managers in Switzerland (as for measures 1.6 and 6.1).

5.2 For hedge funds in particular, it is important that the official bodies ensure a collaborative and consistent approach in their interaction with new and existing market players.

5.3 Registration of hedge funds should be made easier. Following the Luxembourg model, the introduction of a "shelf-registration" procedure would be a worthwhile aim, permitting hedge fund administrators with prior authorization to set up new funds structured along predefined lines in a short space of time (as for measure 3.4).

5.4 Creation of improved framework conditions for collective investment schemes in terms of withholding tax (as for measures 3.2 and 6.5).

6 Private equity

Aspiration

- Doubling of market volume in Switzerland in the next five years.

Major growth

Private equity is a form of financing in which unlisted companies are provided with equity and/or management resources at a decisive stage of their development. This capital is used to develop new products, to tap new markets or to make acquisitions. Equity financing usually involves the equity provider bearing a full share of the risk. To reduce this risk, the equity provider is granted various controlling and co-decision-making rights at the company. The aim of the investment is subsequently to sell the holding at a profit or to float it (IPO). If the investment takes place at a very early stage of development, it is termed venture capital. Private equity can also involve listed companies "going private". The global volume of the private equity market is estimated at around USD 2,500 billion. The number of private equity funds globally is probably over 8,000. The private equity market is dominated by the US, with a share of 41%. However, Europe has gained swiftly in importance in recent years, with a share in the world market of around 39% in 2005. The private equity market in Switzerland, on the other hand, plays an absolutely marginal role in comparison with the European markets. From an investor's point of view, the advantages of private equity investments lie in an attractive medium-to-long-term risk-return profile and the relatively low correlation with the equity markets. On the other hand, investments in private equity usually involve a relatively large investment amount, specialized knowledge or professional advice, and a medium-to-long-term investment horizon.

In Switzerland, direct investments on the private equity market continue to play a very important role, with companies undertaking almost two-thirds of all private equity investments. However, Swiss pension funds have steadily increased the amounts they put into alternative investments in recent years.

Supervisory practice and taxes are decisive for future success

Low corporate taxes and income taxes should have a positive effect on Switzerland as a location. Negative factors include the poor tax incentives given for R&D investments.

The strengths of Switzerland's financial service providers in the area of alternative investments lie in the analysis, selection and combination of existing products within the framework of structuring funds of funds (FoFs).

The high standard of living and the attractiveness of the Swiss financial centre for highly-qualified staff make Switzerland an attractive location for the siting of management companies, although the conditions for employing highly-qualified staff from non-EU countries should be made more flexible. Another important factor in success is the flourishing asset management business with a heavy concentration of assets.

At a regulatory level, however, Switzerland has some significant disadvantages. The minimum of five limited partners stipulated for management companies is too high in comparison with other countries. Another major problem is a lack of legal security in the way the legal framework is handled by the supervisory authority. The practice of the supervisory authority will determine to a significant extent how competitive the newer forms of investment established in the collective investment schemes act will be as against tried-and-tested foreign structures.

In institutional terms, the main issues are the overly long approval procedures and a tendency to take an excessively formalistic approach. Finally, the legislative process is too time-consuming in comparison with other centres and there is often no consistent thinking between the supervisory authority, administrative bodies, auditors, lawyers and the financial industry.

With regard to the tax framework, the issue of taxation of "carried interest" for fund managers is of great importance.

Measures

For the major asset pool of affluent clients, the provision of innovative products is exceedingly important. As well as hedge funds, private equity also plays a significant role. The following measures are necessary:

6.1 Clear and internationally competitive tax framework for hedge funds and private equity fund managers in Switzerland (as for measures 1.6 and 5.1).

6.2 Ensuring pragmatic (approval) practice for private equity by commercial register offices and the Swiss Federal Banking Commission.

6.3 Strengthening of staff resources at the supervisory authority from a quantitative and qualitative point of view, especially for investment funds and private equity. Of importance, for instance, is focused knowledge transfer (e.g. through secondments in the financial industry or training in certain subjects by experts from financial service providers). In addition, direct consultative discussions with the approval authority should be established (as for measure 3.3).

6.4 Legal security in distinguishing between retail investors and qualified investors.

6.5 Creation of improved framework conditions for collective investment schemes in terms of withholding tax (as for measures 3.2 and 5.4).

7 Swiss capital market

Aspiration

- The Swiss capital market should be an attractive niche provider for the issuing and trading of corporate capital.
- Positioning as a world-leading location for the issuing and trading of innovative investment products in all currencies.
- Retention of the Swiss franc's position as an attractive issuing currency and diversification option for international issuers.

Major competition between financial centres

In the capital market area of business, the analysis focuses on issuing and trading. The capitalization of all outstanding domestic corporate bonds in Switzerland is less than 40% of GDP. This is well below the figure of around 120% in the US, but also below the values in Germany, the UK and Japan. With regard to financial intermediaries, the market is undergoing a period of consolidation, manifested by the fall in the number of domestic investment banks active in this area in recent years. The liberalization of international capital movements is bringing increased competition between individual capital markets. This means that medium-sized Swiss companies can also obtain capital outside the domestic market. Furthermore, the convergence of legal frameworks is accelerating the development of a pan-European capital market and brings with it the risk that the Swiss capital market will lose some of its importance. The Swiss franc bond market is becoming less important in an international context. In the equity market, the volume of IPOs is heavily dependent on the market environment. After a sharp rise at the end of the 1990s and a reduction from mid-2001, the market has grown again since 2004. The Swiss franc is the world's fifth-biggest convertible currency.

Stumbling blocks: stamp duty on new issues, double taxation, indirect partial liquidation

The optimal financing and capital structure for companies is determined to a significant extent by the fiscal framework. Taxes are therefore an important element in explaining the behaviour of companies on the capital market. Stamp duty on new issues and withholding tax continue to disadvantage investors and issuers. The negative effect is most conspicuous in the divergent development of issuing volumes in the foreign and domestic segment of Switzerland's bond market. The record volumes issued on the Swiss franc capital market in 2005 and 2006 show that the booming foreign segment has more than made up for the fall in the domestic segment. These record volumes also signal that the Swiss bond market remains attractive for issuers (when leaving out of account the stamp duty on new issues).

As the only western industrialized nation to do so, Switzerland still partly retains largely unmitigated double taxation of joint stock companies. For Swiss companies this makes equity financing more expensive in comparison with internal financing from accumulated earnings or financing through bank loans. This is particularly disadvantageous for new companies without access to the international capital markets. The latent danger of taxation of capital gains as a result of indirect partial liquidation, which made financially sensible succession arrangements more difficult in particular, was fortunately eased in the corporate tax reform of January 2007.

Measures

These facts and trends underline the importance of measures aimed at ensuring the competitiveness of the Swiss capital market. We also need to look into the extent to which niches can be expanded and further developed. The attractiveness of a capital market is determined by a range of factors. But a direct influence can be had only on taxes, the amount of regulation and the financial market infrastructure. The measures derived therefore concentrate on these, as outlined below:

7.1 Abolition of the stamp duty on new issues.

7.2 Ensuring Swiss regulation is in line with international standards in order to safeguard Switzerland's international reputation.

8 Commodity trade finance

Aspiration

- To extend Switzerland's position as a leading financial centre for structured commodity trade finance.

Switzerland is still well positioned . . .

Commodity trade finance (CTF) involves short-time loans made to globally-active trading companies ("traders") for specific purposes. They are usually granted to finance a specific business transaction and allow the trader to pay the purchase price of merchandise acquired for export (this is mainly raw materials and/or semi-finished products, such as crude oil, metals or agricultural products, in large amounts) directly on delivery by the trader's supplier, and to pay the logistics costs (freight, insurance premiums, storage costs, currency and price hedging costs, etc.) directly connected to the transaction. As a general rule, the purchase price for the merchandise is due for payment to the supplier before the proceeds from the sale thereof can be collected. The role of the banks is mainly to bridge the trader's financing gap and to handle the flow of payments and goods through use of suitable instruments (e.g. documentary credits, documentary collections, standby letters of credit, bank guarantees, etc.).

Commodity trade finance is almost without exception a cross-border business. The purchase markets are mostly in developing and emerging countries with significant raw materials. The traders are not in general tied to a specific location and can therefore choose the location which is most favourable for them (whether from a legal, regulatory, tax-related, political or other perspective).

CTF currently offers good business opportunities for the Swiss financial centre (especially in Geneva and Zug). This area of business has grown steadily in recent years and is profitable for the traders and for the banks and service providers.

. . . but not without downside risks

Despite currently favourable location and framework conditions for Switzerland, downside risks exist and there is also room for further optimization:

The credit risk for the banks which provide commodity trade finance has always been seen as the most important risk in their business. Accordingly, the changes resulting from Basel II have undeniable implications for commodity and trade financing. National features of the implementation of Basel II may lead to significant distortions in the capital-backing costs of domestic banks in comparison with foreign competitors.

An important aspect for commodity trade finance dealt with from Switzerland is the taxation rules which apply at cantonal level for holding companies, domiciliary companies and conglomerates. These regimes have recently been subject to criticism from the European Commission. The retention of competitive taxation regimes for CTF holding companies, domiciliary companies or conglomerates is therefore important from the point of view of the financial industry.

Furthermore, trading companies are only subject to the provisions of Swiss money laundering law insofar as the trading is carried out for the account of third parties and the transactions take place over the stock market. Traditional commodities trading, i.e. buying and selling for one's own account, does not form part of the legislation. Commodities trading with derivatives, on the other hand, is monitored above a certain transaction amount. Commodities traders are subject to little regulation in other countries. Trading houses in London and New York are not subject to the provisions of national money laundering legislation.

International legal assistance in criminal matters and domestic proceedings can lead to an avalanche of indiscriminate blocking of accounts, paralyzing the business activities of a trading company and finally causing it to default. It is often the case that trading companies based in Switzerland are prevented by such measures from paying their suppliers, salaries, rent, taxes, etc., and cannot even be informed by the bank about the account block and the reasons for it.

Finally, payments from the bank to payees in documentary credits and bank guarantees can be prevented by temporary decrees. Court practice differs greatly from canton to canton. Often a major loss of trust and a loss of international standing are the result.

Measures

8.1 The Basel Accord (Basel II) should be interpreted and applied in Switzerland such that freedom of choice as to the most suitable approach is maintained. In addition, the "Swiss finish" should not add further to equity costs in comparison with foreign competitors.

8.2 Appropriate implementation of the 40+9 FATF recommendations while maintaining bank-client confidentiality (no additional due diligence and monitoring obligations in trading and with regard to commodity and trade finance, see measures 1.4 and 2.2).

8.3 Competitive taxation regime for CTF holding companies, domiciliary companies and conglomerates.

8.4 Ensuring clear processes and procedures in administrative and legal assistance (prevention of fishing expeditions and indiscriminate blocking of accounts, see also measure 1.5).

The Swiss Bankers Association

The Swiss Bankers Association is the leading organisation of the Swiss financial centre and

- represents the interests of the banks and securities dealers vis-à-vis the authorities in Switzerland and abroad;
- promotes Switzerland's image as a financial centre throughout the world;
- fosters open dialogue with a critical public in Switzerland and worldwide;
- develops the system of self-regulation in consultation with regulatory bodies;
- supports the training of junior staff and established executives in the banking industry;
- facilitates the exchange of information and knowledge between banks and bank employees;
- coordinates joint projects undertaken by the Swiss banks.

The Swiss Bankers Association was founded in 1912 in Basel and today has a membership of 363 institutions and approximately 11,300 individual members. The Association's Office employs a staff of 54. A total of 12 commissions deal with key issues affecting the industry. Serving on these commissions are representatives of various banking groups as well as specialists from the SBA. The SBA's main objective is to safeguard and promote an optimal environment for the Swiss financial services industry at home and abroad.

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