

# **MIRELIS ADVISORS S.A.**

## **FORM ADV PART 2A Disclosure Brochure**

### **Item 1 – Cover Page**

**Mirelis Advisors S.A.**

(Incorporated under the laws of Switzerland)

Rue de la Corraterie 14  
1204 Geneva, Switzerland  
Telephone: + 41-22-310-7640  
Fax: +41-22-310-7639  
Email: [info@MirelisAdvisors.ch](mailto:info@MirelisAdvisors.ch)  
<http://www.MirelisAdvisors.ch>

**Date of Brochure: March 31, 2012**

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This brochure provides information about the qualifications and business practices of Mirelis Advisors S.A. (“Mirelis Advisors”).

If you have any questions about the contents of this brochure, please contact Mr. Elie G. Barzilay, General Manager of Mirelis Advisors, at +41-22-310-7640.

The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission (“SEC”) or by any state securities authority.

Additional information about Mirelis Advisors is also available on the Internet at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). You can view information about Mirelis Advisors on this website by searching for Mirelis Advisors. You may search for information by using its name or CRD number. The CRD number for Mirelis Advisors is 157400.

Registration with the SEC as an investment adviser does not imply a certain level of skill or training.

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## **Item 2 – Material Changes**

This item contains only material changes from the last annual update of this brochure, dated June 15, 2011.

### **Item 3 – Table of Contents (Material Changes)**

- New Attachment to this Brochure entitled “Information for Customers of Swiss Banks Concerning the Avoidance of Dormant Assets”, dated February 2000.
- New Attachment to this Brochure entitled “Information from the SBA regarding the disclosure of client details in payment transactions, securities transactions and other transaction types in connection with SWIFT, dated June 2009.

### **Item 4 – Advisory Business (Material Changes)**

- Since the first version of this Brochure, Mirelis Advisors S.A. has been registered with the SEC as of July 12, 2011.
- Since the first version of this Brochure, Mirelis Advisors S.A. has increased its client assets managed to 69'170'241 USD as of December 31, 2011, for a total of 15 clients.

### **Item 5 – Fees and Compensation (Material Changes)**

- The annual minimum fee of 1,000\$ is cancelled.
- The Fee Schedule has been slightly amended to reflect business standards.

### **Item 12 – Brokerage Practices (Material Changes)**

- This version of the Brochure clarifies the risks incurred by the clients when using directed brokerage, such as higher costs or no guarantee of a most favorable execution.
- This version of the Brochure clarifies the practice of order aggregation and its feasibility. Non-Aggregated orders may be more expensive for clients.

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## Item 4 – Advisory Business

Mirelis Advisors S.A. (referred to as “Mirelis Advisors” or “we” throughout this document) is an investment adviser registered with the U.S. Securities and Exchange Commission (“SEC”) since July 12, 2011. Mirelis Advisors was formed in March 2011 as a corporation under the laws of Switzerland.

Mirelis Advisors is wholly-owned by Mirelis InvesTrust SA, a private wealth management company based in Geneva, Switzerland. The parent company, Mirelis InvesTrust SA, is licensed in Switzerland to operate as a securities trading institution as defined by the Swiss Federal Act on Stock Exchanges and Securities Trading and is supervised by the Swiss Financial Market Supervisory Authority (FINMA).

The external auditor for both Mirelis Advisors and its parent company, Mirelis InvesTrust SA, is Ernst & Young SA, Switzerland.

The parent company, Mirelis InvesTrust SA, is 46% owned by SFM Holding S.A. (formerly known as Société Financière Mirelis SA), which is an independent Swiss holding company established in Geneva, Switzerland, in 1949. The shareholders of SFM Holding S.A. are individual members of the Lawi family. The other shareholders of the parent company, Mirelis InvesTrust SA, are individual members of the Lawi family and Maple Investment Ltd, which is owned in turn by individual members of the Kadoorie family. No individual member of the Lawi family or of the Kadoorie family directly or indirectly owns 25% or more of the parent company, Mirelis InvesTrust SA.

The following is a general description of the services of Mirelis Advisors.

### **Asset Management Services**

Mirelis Advisors offers discretionary asset management services (“Discretionary Asset Management Services”) for your account(s). This service involves providing you with continuous and ongoing supervision over your designated account. A specific investment strategy is crafted to focus upon your specific needs, objectives, risk tolerance and constraints disclosed to Mirelis Advisors. This means that Mirelis Advisors will continuously monitor your designated account and make investments in your designated account when it judges it necessary and in accordance with these individual needs, objectives, risk tolerance and constraints. If you engage Mirelis Advisors for these services, Mirelis Advisors will have discretionary authority over your designated account for the limited purpose of instructing qualified custodians to buy and sell securities and non-securities, including currencies and precious metals (i.e. “Investments”), in the account without consultation with you prior to each buy or sell decision. Mirelis Advisors will not act as a broker or dealer. The Discretionary Asset Management Services of Mirelis Advisors for your Investments will be provided to accounts held at qualified custodians selected by you. Mirelis Advisors maintains a list of preferred custodians, as described below in Item 12; however, the choice of custodian is entirely yours. A qualified custodian is a financial institution and you must designate Mirelis Advisors as the investment adviser on the account by executing a limited power of attorney for investment management in favor of Mirelis Advisors. Mirelis Advisors’ parent company and affiliates will not serve as a qualified custodian for accounts managed by Mirelis Advisors.

The qualified custodian will maintain actual custody of all your Investments. The qualified custodians will have different account fees, execution charges and execution capabilities. Consequently, your fees and execution charges may vary from those of other clients of Mirelis Advisors with similar investment management mandates based on the custodian you select.

## **Specialization**

Mirelis Advisors generally invests in the following areas:

- fixed income and equities investments
- currencies, commodities and precious metals investments
- Exchange Traded Funds (“ETFs”), mutual funds, hedge funds, fund of funds and non-traded funds selection.

In designing an investment allocation, Mirelis Advisors seeks to obtain a suitable asset mix (“Strategic Asset Allocation”) of currencies, commodities, metals, fixed income and equities investments focusing on the medium-term (3 to 5 years) horizon. In certain cases, Mirelis will deviate from the Strategic Asset Allocation to take advantage of short-term (up to 1 year) market opportunities.

## **Types of Investments**

Based upon the agreed investment needs, objectives, risk tolerance and constraints of your discretionary mandate, Mirelis Advisors will invest in a diversified portfolio in multi-currencies of securities and non-securities. The following are some of the general categories of Investments on which Mirelis Advisors will advise:

- Short/medium/long term deposits in various currencies
- Fixed income securities, sovereign and corporate debts
- Securities traded on recognized stock exchanges
- Money market funds, fixed income funds, mutual funds, hedge funds, funds of funds and non-traded funds
- Non-securities such as currencies and precious metals
- Exchange Traded Funds (ETFs)
- Warrants
- Options contracts on indices, currencies, securities and commodities
- Futures contracts

Your personal account may be diversified to include investments in multi-currencies such as deposits, fixed income securities, individual stocks, mutual funds and precious metals.

It is not Mirelis Advisors’ typical investment strategy to attempt to time the market but, from time to time, we may increase cash holdings as we deem appropriate, based on your risk tolerance and our expectations of market behavior and other factors expected to negatively affect the preservation of your capital.

Mirelis Advisors will rely on the accuracy of your representations to us in making corresponding representations on behalf of your account in connection with certain derivative, hedge fund and other investments where representations regarding your net worth, residency, and tax status are relevant to conform to applicable investor restrictions. Mirelis Advisors requires notification by you if your representations become inaccurate or change.

## **Tailored Advisory Services to Individual Requirements of Clients**

Discretionary Asset Management Services are provided by Mirelis Advisors tailored to your specific needs, objectives, risk tolerance and constraints to professionally manage your Investments. Mirelis Advisors provides you with the ability to impose restrictions including specific investment selections and sectors when utilizing the Discretionary Asset Management Services of Mirelis Advisors.

### **Client Assets Managed by Mirelis Advisors**

Mirelis Advisors, which is located in Geneva, Switzerland, is registered as an investment adviser with the SEC since July 12, 2011.

Mirelis Advisors managed 69'170'241 USD of client assets as of December 31, 2011 on a discretionary basis, for a total of 15 clients.

No client assets were managed as of December 31, 2011 on a non-discretionary basis.

The only representative of Mirelis Advisors who currently gives investment advice to clients is Mr. Elie G. Barzilay, General Manager.

## **Item 5 – Fees and Compensation**

This section provides details regarding the fees and compensation arrangements for the services of Mirelis Advisors.

Fees for Discretionary Asset Management Services will not exceed 2% and will be based on a fee schedule similar to the fee schedule listed below. The fee schedule below is a generic fee schedule and is not specific to every client. The actual Discretionary Asset Management Services fee that you are charged is negotiable based on the contents and the size of your portfolio. The exact fee for services will be agreed upon and listed in the Discretionary Asset Management Services Agreement signed between you and Mirelis Advisors prior to services being provided.

<b>Assets Under Management (in US Dollars)</b>	<b>Standard Annual Discretionary Asset Management Service Fee</b>
up to 500'000 USD	2.00%
500'001 to 1'000'000 USD	1.50%
1'000'001 to 5'000'000 USD	1.00%
Over \$5,000,000	Negotiable

All fees are subject to applicable Swiss value added tax at the rate in force at the time the fees are billed.

It should be noted that fees for Mirelis Advisors services may be higher than fees charged by other investment advisers offering similar services.

The annual Discretionary Asset Management Service fee ("Management Fee") is based on the average value of the assets in your designated account. The applicable annual percentage fee is divided and billed in arrears at the beginning of each calendar quarter for the preceding quarter, based on the average value of the assets in your designated account as of the last day of the three previous months. Mirelis Advisors relies on the qualified custodian to price assets in client accounts and Mirelis Advisors calculates its management fee based upon the value of the assets as reported by the qualified custodian.

The Discretionary Asset Management Service fee will be pro-rated based on the number of days the services are provided to you during the initial calendar quarter period if your agreement for services is entered into at any time other than at the beginning of the calendar quarter.

Discretionary Asset Management Service fees are generally deducted directly from your account. You must provide the qualified custodian with written authorization to have such fees deducted from your designated account and paid to Mirelis Advisors. The qualified custodian will send you account statements, at least

quarterly, showing all disbursements for your designated account, including the amount of the Discretionary Asset Management Service fee, deducted directly from your account.

Brokerage commissions, transaction fees, custodian fees and other related costs and expenses will be billed directly to you and deducted from your account by the qualified custodian and will be in addition to Mirelis Advisors' Discretionary Asset Management Service fee. Mirelis Advisors will not receive any portion of such commissions or fees from the qualified custodian or from you. More information on this subject is available below in Item 12.

In addition, you may incur additional charges such as stamp duties, taxes, commission charges, exchange rate and other fees imposed by third parties other than Mirelis Advisors in connection with investments made through your account, including, but not limited to, fees charged by brokers to execute securities transactions and internal management fees charged by mutual funds, hedge funds and exchange traded funds (ETFs).

Discretionary Asset Management Service fees charged by Mirelis Advisors are separate and distinct from the fees and expenses charged by investment company securities that may be recommended to you. A description of these fees and expenses are available in each investment company security's prospectus.

In order to hire Mirelis Advisors for Discretionary Asset Management Services, you must execute an agreement for services. Either party may terminate the agreement for services at any time. If services are terminated within five (5) business days of the effective date of your signature of the agreement, services will be terminated without penalty and no fees shall be due. If services are terminated after the initial five day period, the final fee will be pro-rated based on the amount of days that services were provided during the current quarter period prior to receipt of the termination notice and billed to you. There will be no penalty charge upon termination. The final fee will be calculated using the value of assets in your designated account as of the effective date of termination of the agreement. The termination shall be effective from the time the other party receives written notification or such other time as may be mutually agreed upon, subject to the settlement of transactions in progress and the final payment of the Discretionary Asset Management Service fees.

### **Referral of Unaffiliated Third-Party Investment Advisors**

Mirelis Advisors is a fee-only adviser. Mirelis Advisors' policy is not to accept compensation from third parties relating to the investment advice it provides to you. To the extent Mirelis Advisors receives a referral fee for an investment it recommends, it will reduce the fees owed by you to Mirelis Advisors or will credit your account for the applicable amount.

### **Other compensation**

Mirelis Advisors does not accept compensation for the sale of securities or other investment products, including asset-based sales charges or service fees from the sale of mutual funds. To the extent Mirelis Advisors receives such a compensation for an investment it recommends, it will reduce the fees owed by you to Mirelis Advisors or will credit your account for the applicable amount.

## **Item 6 – Performance-Based Fees and Side-by-Side Management**

### **Performance Fees**

This item is not applicable to this brochure because Mirelis Advisors does not charge or accept performance-based fees which can be defined as fees based on a share of capital gains or on capital appreciation of the assets held within an investor's account.



## Item 7 – Types of Clients

Mirelis Advisors offers Discretionary Asset Management Services to individuals, trusts, foundations, corporations and other business entities.

Mirelis Advisors imposes a minimum investment in the amount of \$500,000 for its Discretionary Asset Management Services. This minimum investment amount may be waived at the discretion of Mirelis Advisors in special cases (e.g. family members having individually smaller than \$500,000 accounts but preferring to be managed by the same investment adviser or small accounts with a potential of large increase in assets).

All clients must execute a formal, written contract when engaging Mirelis Advisors for Discretionary Asset Management Services.

## Item 8 – Methods of Analysis, Investment Strategies and Risk of Loss

### **Methods of Analysis & Investment Strategies**

Mirelis Advisors bases its investment strategies on market trends, economic and political environments, research received from financial institutions and paid subscriptions to financial periodicals and/or research institutions.

Mirelis Advisors offers the following discretionary investment strategies as a foundation of your tailored-made portfolio:

#### Fixed Income / Yield:

Asset allocation of Investments with the objective of income optimization coupled with capital preservation; time horizon of minimum 2 years; very low risk tolerance; limited value fluctuations; acceptance of value fluctuations due to interest rate evolution over the life of the investment.

Investment exclusively in fixed income securities, fixed income funds, short/medium/long term deposits, money market funds, multi-currencies and/or precious metals.

The maximum exposure outside the USD currency is not to exceed 20% of assets.

#### Conservative:

Asset allocation of Investments with the objective of income optimization; time horizon of minimum 3 years; low risk tolerance; limited value fluctuations; acceptance of value fluctuations due to interest rate evolution over the life of the investment.

Investments include fixed income securities, fixed income funds, short/medium/long term deposits, money market funds, multi-currencies, precious metals, equity securities, equity funds and/or alternative investments.

Possibility of investing in equity securities and equity funds not to exceed 30% of assets.

The maximum exposure outside the USD currency is not to exceed 30% of assets.

#### Balanced:

Asset allocation of Investments with the objective of a combination of capital gains and income; time horizon of minimum 3 years; medium risk tolerance; acceptance of value fluctuations.

Investments include fixed income securities, fixed income funds, short/medium/long term deposits, money market funds, multi-currencies, precious metals, equity securities, equity funds and/or alternative investments.

Possibility of investing in equity securities and equity funds not to exceed 50% of assets.

The maximum exposure outside the USD currency is not to exceed 40% of assets.

#### Growth:

Asset allocation of Investments with the objective of maximizing capital gains; time horizon between 3 to 5

years; high risk tolerance; acceptance of wide value fluctuations.

Investments include fixed income securities, fixed income funds, short/medium/long term deposits, money market funds, multi-currencies, precious metals, equity securities, equity funds and/or alternative investments.

Possibility of investing in equity securities and equity funds not to exceed 75% of assets.

The maximum exposure outside the USD currency is not to exceed 50% of assets.

Market fluctuations may generate significant losses.

#### Dynamic:

Asset allocation of Investments with the objective of maximizing gains; time horizon of minimum 5 years; very high risk tolerance; acceptance of very wide value fluctuations.

Investments include fixed income securities, fixed income funds, short/medium/long term deposits, money market funds, multi-currencies, precious metals, equity securities, equity funds and/or alternative investments.

Possibility of investing total assets in equity securities and equity funds.

The maximum exposure outside the USD currency is not to exceed 60% of assets.

Market fluctuations may generate significant losses.

These discretionary investment strategies are given as an indication only and may vary given your special needs, objectives, risk tolerance and constraints.

Mirelis Advisors tailors its Discretionary Asset Management Services to the individual requirements of clients based on the information they provide in the "Client Investment Profile", as updated from time to time by the clients.

### **Risk of Loss**

Mirelis Advisors, as well as all other Swiss financial institutions, is required under Swiss legislation to inform you about types of transactions and investments that may involve special risks and to supply to each client the attached disclosure brochure entitled "*Special Risks in Securities Trading*".

You must understand that past performance is not indicative of future results. Therefore, current and prospective clients (including you) should never assume that future performance of any specific Investment or investment strategy will be profitable. Investing in securities (including stocks, bonds, mutual funds and alternative investments), currencies and precious metals involves risk of loss. Further, depending upon the different types of investments, there may be varying degrees of risk. Clients and prospective clients (including you) should be prepared to bear investment losses, including the loss of original principal.

Because of the inherent risk of loss associated with investing, Mirelis Advisors is unable to represent, guarantee, or even imply that its services and methods of analysis can or will predict future results, successfully identify market tops or bottoms, or insulate you from losses due to market corrections or declines. There are certain additional risks associated when investing in securities, currencies and precious metals through Mirelis Advisors' investment management programs, which include, but are not limited to, the following:

- Equity (Stock) market risk –The stock market as a whole goes down resulting in a decrease in the value of your investments. This is also referred to as systematic risk.
- Company risk – Common stocks are susceptible to general stock market fluctuations and to volatile increases and decreases in value as market confidence in, and perceptions of, their issuers change. If you hold common stock, or common stock equivalents, of any given issuer, you should generally be exposed to greater risk than if you hold preferred stocks and debt obligations of the issuer. When investing in stock positions, there is always a certain level of company or industry specific risk that is inherent in each investment. This is also referred to as idiosyncratic risk and can be reduced through appropriate diversification. There is the risk that the company will perform poorly or have its value

reduced based on factors specific to the company or its industry. For example, if a company's employees go on strike or the company receives unfavorable media attention for its actions, the value of the company may be reduced.

- ETF and mutual fund risk – When you are invested in a an ETF or mutual fund, it will bear additional expenses based on its pro rata share of the ETFs or mutual fund's operating expenses, including the potential duplication of management fees. The risk of owning an ETF or mutual fund generally reflects the risks of owning the underlying securities the ETF or mutual fund holds. You will also incur brokerage costs when purchasing ETFs or mutual funds.  
ETFs and mutual funds are also subject to «basis risk», the risk of the ETF/fund performance diverging from the benchmark.
- Management risk – Your results by engaging Mirelis Advisors for Discretionary Asset Management Services will be influenced by the success and failure of our investment strategies, the analysis of third party research studies and choice of portfolio Investments. If our investment strategies do not result in expected returns, the value of your portfolio of Investments may decrease.
- Currency risk – The currencies of some countries, more particularly emerging countries, are subject to unpredictable fluctuations in value. Some countries impose restrictions on the export of their currency or other form of currency restrictions, or stop pegging their currency to a reference currency. Hedging can help limit but not eliminate losses resulting from currency fluctuations.
- Precious metals risk – Markets for precious metals are speculative and highly volatile; the prices of precious metals is influenced by many factors including the performance of the economy as a whole, the changing and demand relationships for the commerce and the prevailing psychological characteristics of the relevant marketplace. Also, they are various methods of ownership of physical precious metals which require consideration and evaluation in light of the various costs, such as delivery charges and brokerage fees, which relate to those methods. Investment dollars put into physical precious metals can only be converted back into cash by selling; therefore, there is a cost which is the loss of interest which the investment dollars would earn if left in interest bearing instruments, and in order to offset the loss of interest income, the selling price must be sufficient to cover for the loss of interest.  
Precious metals are non-income generating assets, i.e. holding them does not provide any source of revenue other than the price appreciation.
- Option risk - An option is a financial derivative that represents a contract sold by one party (option writer) to another party (option holder). The contract offers the buyer the right, but not the obligation, to buy (call) or sell (put) a security or other financial asset at an agreed-upon price (the strike price) during a certain period of time or on a specific date (exercise date). Selling options can lead to a theoretical infinite loss.
- Structured products risk - Structured products are designed to facilitate highly customized risk-return objectives. This is accomplished by taking a traditional security, such as a conventional investment-grade bond, and replacing the usual payment features (e.g. periodic coupons and final principal) with non-traditional payoffs derived not from the issuer's own cash flow, but from the performance of one or more underlying assets. The payoffs from these performance outcomes are contingent in the sense that if the underlying assets return "x", then the structured product pays out "y". This means that structured products closely relate to traditional models of option pricing, though they may also contain other derivative types such as swaps, forwards and futures, as well as embedded features such as leveraged upside participation or downside buffers.  
Structured products include all risks from options, plus additional risks: model risk, liquidity risk (product will not be priced daily on a market), leverage risk, counterparty and credit risk of the issuer and a risk related to the lack of transparency on fees.
- Hedge fund risk - A hedge fund is an aggressively managed portfolio of investments that uses advanced investment strategies such as leveraged, long, short and derivative positions in both

domestic and international markets with the goal of generating high returns (either in an absolute sense or over a specified market benchmark). Hedge funds are most often set up as private investment partnerships that are open to a limited number of investors and require a very large initial minimum investment. Investments in hedge funds are illiquid as they often require investors to keep their money in the fund for at least one year. Redemption rights may be subject to specific restrictions. Hedge funds are similar to mutual funds in that investments are pooled and professionally managed, but differ in that the fund has far more flexibility in its investment strategies.

Hedge fund risk include risk of loss of capital due to wrong bets of the manager, hedge fund manager selection risk, fraud risk, legal risk (difficulty in suing the hedge fund which may be incorporated in foreign jurisdictions), low transparency of investments, lack of accurate valuations, illiquidity and high fees.

- Fund of funds risk – A fund of funds is an investment vehicle pooling various funds (mutual funds or hedge funds) together with the objective of diversifying the risks and varying the exposures to different markets, regions and investment styles. Funds of funds' risks include all risks previously mentioned regarding mutual funds and hedge funds, plus risks related to the double layer of fees, fund of funds manager selection risk and low transparency.
- Non-traded funds illiquidity risk - Depending upon the redemption policies of the respective funds, there is a risk that an investment in a non-traded fund cannot be liquidated except at specified times. Generally there is not a secondary market for non-traded funds and often the terms of the funds prohibit secondary sales without approval of the fund administrator. In certain cases, there can be other limits on transfers. For these reasons, investments in non-traded funds carry a risk of illiquidity and investment in such funds is appropriate only for clients who are able to accept these risks.
- Leverage - A derivative instrument or transaction may have the effect of disproportionately increasing an account's exposure to the market for the securities or other assets underlying the derivative position and the sensitivity of an account's portfolio to changes in market prices for those assets. Leverage will tend to magnify both the positive impact of successful investment decisions and the negative impact of unsuccessful investment decisions by Mirelis Advisors on an account's performance.
- Counterparty Credit Risk - An account's ability to profit from a derivative contract depends on the ability and willingness of the other party to the contract (a "counterparty") to perform its obligations under the contract.  
Although exchange-traded futures and options contracts are generally backed by a guarantee from a clearing corporation, an account could lose the benefit of a contract in the unlikely event that the clearing corporation becomes insolvent. A counterparty's obligations under a forward contract, over-the-counter option, swap or other over-the-counter derivative contract are not so guaranteed. If the counterparty to an over-the-counter contract fails to perform its obligations, an account may lose the benefit of the contract and may have difficulty reclaiming any collateral that an account may have deposited with the counterparty.
- Lack of Correlation - The market value of a derivative position may correlate imperfectly with the market price of the asset underlying the derivative position. To the extent that a derivative position is being used to hedge against changes in the value of assets in an account, a lack of price correlation between the derivative position and the hedged asset may result in an account's assets being incompletely hedged or not completely offsetting price changes in the derivative position.
- Illiquidity - Over-the-counter derivative contracts are usually subject to restrictions on transfer, and there is generally no liquid market for these contracts. Although it is often possible to negotiate the termination of an over-the-counter contract or enter into an offsetting contract, a counterparty may be unable or unwilling to terminate a contract with an account, especially during times of market instability or disruption. The markets for many exchange traded futures, options and other instruments are quite liquid during normal market conditions, but this liquidity may disappear during times of market instability or disruption.

- Less Accurate Valuation - The absence of a liquid market for over-the-counter derivatives increases the likelihood that the qualified custodian will not be able to correctly value these interests.

## Item 9 – Disciplinary Information

This item is not applicable to this disclosure brochure of Mirelis Advisors because there are no legal or disciplinary events listed at Item 9 of the Form ADV Part 2 instructions that apply.

## Item 10 – Other Financial Industry Activities and Affiliations

### **Affiliation with Mirelis InvesTrust SA**

Mirelis Advisors is wholly-owned by Mirelis InvesTrust SA, a private wealth management company based in Geneva, Switzerland. The parent company, Mirelis InvesTrust SA, is licensed in Switzerland to operate as a securities trading institution as defined by the Swiss Federal Act on Stock Exchanges and Securities Trading and is supervised by the Swiss Financial Market Supervisory Authority (FINMA). Mirelis InvesTrust SA, while not an investment adviser as defined by the U.S. securities laws, is a securities dealer under Swiss law and is allowed to perform asset management activities in Switzerland, including the provision of investment advice to its clients.

The external auditor for both Mirelis Advisors and its parent company, Mirelis InvesTrust SA, is Ernst & Young SA, Switzerland.

Mirelis Advisors' offices are separated from those of its parent company, Mirelis InvesTrust SA. Mirelis Advisors has arrangements with Mirelis InvesTrust SA only for corporate services unrelated to the investment services we provide to you. Those arrangements do not include the sharing of research or access to client information.

Mirelis Advisors believes that the relationship and arrangements with the parent company Mirelis InvesTrust SA does not create a conflict of interest with clients.

### **Other Arrangements**

Mirelis Advisors is **not**, and does **not** have a related company that is any of the following: (1) an investment company or other pooled investment vehicle (including a mutual fund, closed-end investment company, unit investment trust, private investment company or "hedge fund," and offshore fund), (2) an investment adviser or financial planner, (3) a futures commission merchant, commodity pool operator, or commodity trading adviser, (4) a banking or thrift institution, (5) an accountant or accounting firm, (6) a lawyer or law firm, (7) an insurance company or agency, (8) a pension consultant, (9) a real estate broker or dealer, or (10) a sponsor or syndicator of limited partnerships.

## **Item 11 – Code of Ethics, Participation or Interest in Client Transactions and Personal Trading**

### **Code of Ethics Summary**

Mirelis Advisors has established a Code of Ethics that will apply to all of its supervised persons. As a fiduciary, it is an investment adviser's responsibility to provide fair and full disclosure of all material facts and to act solely in the best interests of each of the clients (including you) at all times. This fiduciary duty is considered the core underlying principle for the investment adviser's Code of Ethics which also covers its Insider Trading and Personal Securities Transactions Policies and Procedures. Mirelis Advisors requires all of its supervised persons to conduct business with the highest level of ethical standards and to comply with all applicable laws and regulations at all times.

Upon employment or affiliation and when changes occur, all supervised persons will sign an acknowledgement that they have read, understand and agree to comply with Mirelis Advisors' Code of Ethics. Mirelis Advisors has the responsibility to insure that the interests of all clients (including you) are placed ahead of Mirelis Advisors' or its supervised person's own investment interest. Full disclosure of all material facts and potential conflicts of interest will be provided to you prior to any services being conducted. Mirelis Advisors and its supervised persons must conduct business in an honest, ethical and fair manner and avoid all circumstances that might negatively affect or appear to affect our duty of complete loyalty to all clients (including you).

Mirelis Advisors does not provide legal or tax advice. Compliance with all applicable tax and legal reporting and other applicable laws and regulations relating to your assets are your sole responsibility. Investment adviser representatives are not permitted to provide any advice to U.S. clients (including you) concerning taxes. Mirelis Advisors has developed supervisory procedures to insure that its investment advisory representatives are not providing tax advice to U.S. clients and are not encouraging nor recommending that U.S. clients violate any applicable tax laws or regulations.

Mirelis Advisors' policy is to comply with all applicable Swiss and U.S. laws and regulations, including the provisions relating to the detection and prevention of money laundering and terrorist financing. It will only provide its Discretionary Asset Management Services to clients and do business with qualified custodians who comply with such laws and regulations.

This disclosure is a brief synopsis of the Code of Ethics of Mirelis Advisors.

The Code of Ethics of Mirelis Advisors is available upon request to the Chief Compliance Officer, Mr. Sébastien Joliat, [sjo@MirelisAdvisors.ch](mailto:sjo@MirelisAdvisors.ch), tel.: +41-22-310-7641.

### **Affiliate and Employee Personal Securities Transactions Disclosure**

You should be aware that the personnel of Mirelis Advisors and the personnel of Mirelis InvesTrust SA, an affiliate of Mirelis Advisors, may buy or sell Investments that are also recommended to clients (including you). Mirelis InvesTrust SA will not be serving as a qualified custodian of the assets of Mirelis Advisors' clients (including you). In order to minimize the possibility of conflict of interest, Investments that Mirelis Advisors recommends and purchases for you are generally widely held and publicly traded. In addition, in accordance with Mirelis Advisors' fiduciary duty to you, it always places client interests ahead of the interests of Mirelis Advisors and its personnel. Mirelis Advisors and its personnel will not purchase or sell any Investment for their own account prior to a transaction for such investment being implemented for a client's account. Mirelis Advisors put in place procedures to monitor the activity of personal accounts of its supervised persons on a quarterly basis.

## Item 12 – Brokerage Practices

If you wish to utilize the Discretionary Asset Management Services of Mirelis Advisors, you will need to select a qualified custodian to hold your Investments. Mirelis Advisors maintains a list of Swiss-based preferred qualified custodians with which we work and we can make this list available to you at your request. However, the choice of qualified custodian is entirely yours. Mirelis Advisors' parent company and affiliates will not serve as a qualified custodian for accounts managed by Mirelis Advisors.

Securities transactions for Investments in your discretionary portfolio are normally handled by the broker-dealers with which the qualified custodian of your choice has a business relationship, unless you and your qualified custodian otherwise agree. These broker-dealers may either be affiliates of the qualified custodian which you select or may be ones with which your qualified custodian has an on-going business relationship for the execution of trades. The custodial charges, brokerage commissions and any other fees charged by your chosen qualified custodian and broker-dealer will be those agreed upon directly between you and your chosen qualified custodian/broker-dealer, without Mirelis Advisors' involvement. Mirelis Advisors' parent company and affiliates will not serve as a broker-dealer for accounts managed by Mirelis Advisors.

It is therefore important that you understand that, when you select a qualified custodian to hold your Investments, you are also selecting the broker-dealer with which your chosen qualified custodian executes trades in your portfolio, unless you and your qualified custodian agree upon the selection of a different broker-dealer of your choice. In carrying out its discretionary portfolio mandate, Mirelis Advisors will then deal with your chosen qualified custodian and broker-dealer for the execution of transactions related to the Investments in your portfolio.

Mirelis Advisors does undertake an annual review of its list of preferred qualified custodians. Since these preferred qualified custodians are based in Switzerland, they must agree to obtain best execution practices in accordance with the custodian's duties under Swiss banking law, which may differ from that defined by the SEC.

Some of the other considerations included in this review are custody fees, brokerage practices, execution guarantees, the ability to provide timely duplicate client trade confirmations and bundled duplicate statements, convenient access to a trading desk, the ability to directly deduct Asset Management Service fees from client accounts, access to electronic communications networks for client order entry and account information, receipt of compliance publications, access to mutual funds that generally require significantly higher minimum initial investments or that are generally only available to institutional investors, and competitive fee schedules.

While no single criterion will validate or invalidate a qualified custodian from maintaining its position on Mirelis Advisors' list of preferred qualified custodians, all criteria as a whole are considered in determining whether a qualified custodian is on this preferred list.

Because you are the one who selects the qualified custodian for your Investments and thereby the broker-dealer to be used for transactions involving your account, you may have accounts at the same custodian than other clients, or you may have multiple accounts at different custodians. Therefore, you may pay an executing broker-dealer a higher commission for a transaction than might be charged by another broker-dealer executing the same transaction or than the commission charged by the broker-dealer executing a similar transaction for another client of Mirelis Advisors. Brokerage commissions may also vary among clients (including you). It also is possible that the broker-dealer chosen by you and used for the execution of transactions may not be a registered broker-dealer under the *U.S. Securities Exchange Act of 1934*, as amended (the "Exchange Act").

The choice of qualified custodian and broker-dealer ("Directed Brokerage") is the Client's and not Mirelis Advisors'. This may not be the standard applied by other investment advisers. With Directed Brokerage, Mirelis Advisors may be unable to achieve most favorable execution of client transactions and this practice may cost you more in fees.

## **Side-by-Side Management**

Conflicts related to side-by-side management of different accounts may exist for various reasons. For example, we may manage more than one account according to the same or a substantially similar investment strategy. Side-by-side management of different types of accounts may raise conflicts of interest when two or more accounts invest in the same securities or pursue a similar strategy. These potential conflicts include the favorable or preferential treatment of an account or a group of accounts, conflicts related to the allocation of investment opportunities, particularly with respect to securities that have limited availability such as initial public offerings, and transactions in one account that closely follow related transactions in a different account. In addition, the results of the investment activities for one account may differ significantly from the results achieved for other accounts, particularly as a result of our practice to individually tailor each client's investment portfolio to their particular requirements, objectives, constraints and risk tolerance.

We have policies and procedures in place aiming to ensure that all client accounts are treated fairly and equitably. For example, we strive to equitably allocate investment opportunities among relevant accounts over time. In addition, investment decisions for each account are made with specific reference to the individual needs, objectives, risk tolerance and constraints of the account. Accordingly, we may give advice or exercise investment responsibility or take other actions for some clients (including related persons) that may differ from the advice provided, or the timing and nature of actions taken, for other clients. Investment results for different accounts, including accounts that are generally managed in a similar style, also may differ as a result of these considerations. Some clients may not participate at all in some investments in which other clients participate, or may participate to a different degree or at a different time than other clients do.

In general, Mirelis Advisors will try to aggregate the purchase or sale of securities for various client accounts, in order to obtain the same price. However, it may not be feasible to aggregate orders for various reasons: different qualified custodians, different investment strategy, availability of cash in the accounts, etc. Non-aggregated orders should not be in general more expensive than aggregated orders for you.

## **Use of Soft Dollars**

Mirelis Advisors does not presently have any soft dollar arrangements. However, to the extent it may in the future, it will enter into such arrangements only in accordance with the safe harbor conditions provided by Section 28(e) of the Exchange Act. The "safe harbor" provisions of Section 28(e) permit an investment adviser to use brokerage commissions or "soft dollars" to obtain research and brokerage services that provide lawful and appropriate assistance in the investment decision-making process.

Research services within Section 28(e) may include, but are not limited to, research reports (including market research); certain financial newsletters and trade journals; software providing analysis of securities portfolios; corporate governance research and rating services; attendance at certain seminars and conferences; discussions with research analysts; meetings with corporate executives; consultants' advice on portfolio strategy; data services (including services providing market data, company financial data, certain valuation and pricing data and economic data); and advice from brokers on order execution.

Brokerage services within Section 28(e) may include, but are not limited to, services related to the execution, clearing and settlement of transactions and functions incidental thereto (i.e., connectivity services between an investment adviser and a broker-dealer and other relevant parties such as custodians); trading software operated by a broker-dealer to route orders; software that provides trade analytics and trading strategies; software used to transmit orders; clearance and settlement in connection with a trade; electronic communication of allocation instructions; routing settlement instructions; post trade matching of trade information; and services required by the SEC or a self-regulatory organization such as comparison services, electronic confirms or trade affirmations.



As mentioned in Item 14, Mirelis Advisors' employees or associated persons may be invited to attend seminars and meetings with the costs associated with such meetings borne by a sponsoring brokerage firm, qualified custodian or other party extending the invitation.

## **Item 13 – Review of Accounts**

Account reviews are provided in connection with Discretionary Asset Management Services. Your assigned investment adviser representative will contact you at least annually for the purpose of reviewing your account with you and to determine if there have been changes in your financial situation, investment objectives, risk tolerance or constraints. However, you should contact your investment adviser representative immediately if your financial situation, investment objectives, risk tolerance or constraints have changed. The calendar is the main triggering factor, although more frequent reviews may also be triggered by changes in your circumstances, requests, or changes within the market.

With respect to Discretionary Asset Management Services, your accounts and Investments are reviewed on a frequent basis. Portfolios are usually reviewed as frequently as daily or weekly, but no less frequently than monthly. Changing market conditions or economical and financial news may trigger a review. Mr. Elie G. Barzilay, General Manager of Mirelis Advisors, is responsible for day to day rebalancing, reallocation and ongoing trading services for accounts managed by Mirelis Advisors.

Mirelis Advisors is responsible for reviewing *all* client accounts (including yours) and providing *all* Discretionary Asset Management Services.

### **Statements and Reports**

With respect to Discretionary Asset Management Services, you will receive written account statements at least quarterly directly from your qualified custodians.

Mirelis Advisors does not transmit any statements, performance reports or valuation statements to you. All statements and performance reports, including valuation statements, are provided and transmitted directly to you by your qualified custodians.

## **Item 14 – Client Referrals and Other Compensation**

Mirelis Advisors may, from time to time, enter into solicitor arrangements under which unrelated asset managers or financial institutions ("solicitors") solicit investment adviser clients on Mirelis Advisors' behalf. In such instances, Mirelis Advisors will comply with SEC Rule 206(4)-3 under the *Investment Advisers Act of 1940* that requires an agreement between Mirelis Advisors and the third party solicitor and a separate proper disclosure statement signed by the client. Such disclosure statement will include a description of the arrangement between Mirelis Advisors and the solicitor and a description of the compensation arrangement. In such solicitor arrangements, Mirelis Advisors will pay cash referral fees to the solicitor, typically calculated at an agreed percentage of the fees Mirelis Advisors receives from managing the referred investment adviser client's assets. The solicitor will have no further involvement with the client after the client is referred to Mirelis Advisors as an investment adviser client.

Mirelis Advisors is a fee-only adviser. Mirelis Advisors' policy is not to accept compensation from third parties relating to the investment advice it provides to you. To the extent Mirelis Advisors receives a referral fee for an investment it recommends, it will reduce the fees owed by you to Mirelis Advisors or will credit your account for the applicable amount. For these purposes, referral fees include marketing fees, discounts, finder's fees, service fees, including shareholder service fees, referral fees, 12b-1 fees or bonus commissions paid by mutual funds, privately offered funds, insurance products, variable annuities or other investment products paid to Mirelis Advisors for recommending an investment, for investing your funds in

such product or for marketing assistance or the performance of certain administrative tasks associated with making an investment.

Mirelis Advisors' employees or associated persons may be invited to attend seminars and meetings with the costs associated with such meetings borne by a sponsoring brokerage firm, qualified custodian or other party extending the invitation.

## **Item 15 – Custody**

Custody, as it applies to investment advisers, has been defined by the SEC as having access or control over your funds and/or securities. In other words, custody is not limited to physically holding your funds and securities. If an investment adviser has the ability to access or control your funds or securities, the investment adviser is deemed to have custody and must ensure that proper procedures are implemented.

Mirelis Advisors is typically given authority to have its fees directly deducted from your account when providing Discretionary Asset Management Services; consequently, Mirelis Advisors is deemed to have custody of such funds and securities. However, Mirelis Advisors does not physically hold your Investments.

For accounts in which Mirelis Advisors is deemed to have custody of your Investments, Mirelis Advisors has established procedures to ensure all your Investments are held at a qualified custodian in a separate account for each client (including you) under that client's name. You or your independent representative may direct, in writing, the establishment of all accounts and therefore are aware of the qualified custodian's name, address and the manner in which the Investments are maintained. Finally, written account statements are delivered directly from the qualified custodian to you, or to your independent representative, at least quarterly. You should carefully review those statements and when you have questions about your account statements, you should contact Mirelis Advisors or the qualified custodian preparing the statement.

Mirelis Advisors does not transmit any statements, performance reports or valuation statements to you.

## **Item 16 – Investment Discretion**

Under its Discretionary Asset Management Services, Mirelis Advisors will maintain trading authority over your designated accounts and will implement trades on a discretionary basis upon receiving the proper written authorization, which generally is accomplished by you signing a limited power of attorney in favor of Mirelis Advisors. By allowing Mirelis Advisors to manage accounts on a discretionary basis, Mirelis Advisors will have the authority to determine the type of Investments and the amount of Investments that can be bought or sold for your portfolio, as well as the authority to diversify your portfolio through currencies and by investing in precious metals, without obtaining your consent prior to each transaction. Mirelis Advisors is in no instance a beneficial owner of the assets in your account. At no time is Mirelis Advisors authorized to withdraw funds from your designated accounts without your prior written authorization, e.g. you authorizing your qualified custodian to deduct and transmit Mirelis Advisors' Discretionary Asset Management Service fee.

Although Mirelis Advisors manages all accounts on a discretionary basis under its Discretionary Asset Management Services, you have the ability to impose reasonable restrictions on the types of investments that may be purchased in your account (i.e. asset classes, sectors, etc.). You may also place reasonable limitations on the discretionary power granted to Mirelis Advisors so long as the limitations are specifically set forth or included as an attachment to your client agreement with Mirelis Advisors.

Finally, Mirelis Advisors does not have discretionary authority to select a qualified custodian or broker-dealer for your account.

## **Sharing of Information with Regulatory Authorities and Providers of Financial Instruments**

Mirelis Advisors may be obliged to disclose some personal information about you to regulatory authorities in Switzerland, in the United States or in other countries. We will only do so as required or permitted by applicable laws and regulations.

Mirelis Advisors may also have to disclose personal information to providers of financial instruments (such as mutual funds managers, hedge funds managers, issuers of structured products). The disclosures may include your state of residence, tax identification number, or other information. We will only make those disclosures when required or allowed by law.

By signing the Discretionary Asset Management Services Agreement, you accept those potential disclosures and waive any rights to secrecy or confidentiality.

## **Item 17 – Voting Client Securities, Trade Errors and Class Actions**

### **Voting Client Securities**

In accordance with its fiduciary duty to you and Rule 206(4)-6 of the *Investment Advisers Act of 1940*, Mirelis Advisors has adopted and implemented written policies and procedures governing the voting of your securities. You may obtain a copy of our proxy voting policies and procedures upon request to the Chief Compliance Officer, Mr. Sébastien Joliat, [sjo@MirelisAdvisors.ch](mailto:sjo@MirelisAdvisors.ch), tel.: +41-22-310-7641. Mirelis Advisors does not have the authority to vote client proxies, as disclosed in Mirelis Advisors' Discretionary Asset Management Services Agreement. If Mirelis Advisors inadvertently receives any proxy materials on your behalf, Mirelis Advisors will promptly forward such materials to you.

### **Trade Errors**

Although Mirelis Advisors' goal is to have trades executed seamlessly in the manner intended by you and consistent with our investment decisions, Mirelis Advisors recognizes that errors can occur for a variety of reasons. Mirelis Advisors' policy in dealing with such errors is to:

- Identify any errors in a timely manner;
- Correct all errors so that any affected account (such as yours) is placed in the same position it would have been in had the error not occurred;
- Insure that all costs from corrective actions are not passed on to you;
- Evaluate how the error occurred and assess if any changes in any processes are warranted or if any continuing education is required.

The consequences and the required corrective measures may be different depending upon the nature of the error or the account affected.

### **Class Actions**

Mirelis Advisors will not be involved with your participation in any class action lawsuits. Mirelis Advisors will determine whether to return to the sender any documentation inadvertently received regarding your participation in class actions, or to forward such information to you.

## **Item 18 – Financial Information**

This item is not applicable to this disclosure brochure of Mirelis Advisors. Mirelis Advisors does not require or solicit prepayment of more than \$1,200 in fees per client, six months or more in advance. Therefore, Mirelis Advisors is not required to include a balance sheet for its most recent fiscal year.

Mirelis Advisors is not subject to a financial condition that is reasonably likely to impair its ability to meet contractual commitments.

Finally, Mirelis Advisors has not been the subject of a bankruptcy petition at any time.

# **MIRELIS ADVISORS S.A.**

## **FORM ADV PART 2B Brochure Supplement**

### **Item 1 – Cover Page**

**Mirelis Advisors S.A.**

(Incorporated under the laws of Switzerland)

Rue de la Corraterie 14  
1204 Geneva, Switzerland  
Telephone: + 41-22-310-7640  
Fax: +41-22-310-7639  
Email: [info@MirelisAdvisors.ch](mailto:info@MirelisAdvisors.ch)  
<http://www.MirelisAdvisors.ch>

**Date of Brochure: March 31, 2012**

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This brochure supplement provides information about Mr. Elie G. Barzilay that supplements the brochure of Mirelis Advisors S.A. ("Mirelis Advisors"). You should have received a copy of that brochure. Please contact Mr. Barzilay at +41-22-310-7640 if you did not receive the brochure of Mirelis Advisors or if you have any questions about the contents of this supplement.

The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission ("SEC") or by any state securities authority.

Additional information about Mirelis Advisors is also available on the Internet at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). You can view information about Mirelis Advisors on this website by searching for Mirelis Advisors. You may search for information by using its name or CRD number. The CRD number for Mirelis Advisors is 157400.

Registration with the SEC as an investment adviser does not imply a certain level of skill or training.

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## Item 2 – Educational Background and Business Experience

Mr. Elie G. Barzilay, born September 24, 1985

### Education Background

- **Passed Level III of the Chartered Financial Analyst Examination (CFA), 06/2011**

The Chartered Financial Analyst (CFA) charter is a globally respected, graduate-level investment credential established in 1962 and awarded by CFA Institute — the largest global association of investment professionals.

There are currently more than 90,000 CFA charterholders working in 134 countries. To earn the CFA charter, candidates must: 1) pass three sequential, six-hour examinations; 2) have at least four years of qualified professional investment experience; 3) join CFA Institute as members; and 4) commit to abide by, and annually reaffirm, their adherence to the CFA Institute Code of Ethics and Standards of Professional Conduct.

#### High Ethical Standards

The CFA Institute Code of Ethics and Standards of Professional Conduct, enforced through an active professional conduct program, require CFA charterholders to:

- Place their clients' interests ahead of their own
- Maintain independence and objectivity
- Act with integrity
- Maintain and improve their professional competence
- Disclose conflicts of interest and legal matters

#### Global Recognition

Passing the three CFA exams is a difficult feat that requires extensive study (successful candidates report spending an average of 300 hours of study per level). Earning the CFA charter demonstrates mastery of many of the advanced skills needed for investment analysis and decision making in today's quickly evolving global financial industry. As a result, employers and clients are increasingly seeking CFA charterholders—often making the charter a prerequisite for employment.

Additionally, regulatory bodies in 22 countries and territories recognize the CFA charter as a proxy for meeting certain licensing requirements, and more than 125 colleges and universities around the world have incorporated a majority of the CFA Program curriculum into their own finance courses.

#### Comprehensive and Current Knowledge

The CFA Program curriculum provides a comprehensive framework of knowledge for investment decision making and is firmly grounded in the knowledge and skills used every day in the investment profession. The three levels of the CFA Program test a proficiency with a wide range of fundamental and advanced investment topics, including ethical and professional standards, fixed-income and equity analysis, alternative and derivative investments, economics, financial reporting standards, portfolio management, and wealth planning.

The CFA Program curriculum is updated every year by experts from around the world to ensure that candidates learn the most relevant and practical new tools, ideas, and investment and wealth management skills to reflect the dynamic and complex nature of the profession.

To learn more about the CFA charter, visit [www.cfainstitute.org](http://www.cfainstitute.org).

- **Chartered Alternative Investment Analyst (CAIA), 09/2008**

The CAIA designation, recognized globally, is administered by the Chartered Alternative Investment Analyst Association and requires a comprehensive understanding of core and advanced concepts regarding alternative investments, structures, and ethical obligations. To qualify for the CAIA designation, finance professionals must pass a self-directed, comprehensive course of study on risk-return attributes of institutional quality alternative assets and complete both the Level I and Level II CAIA examinations. The CAIA examinations are administered in a computerized format at proctored test centers around the world. To qualify for membership, individuals are required to have met prerequisites of at least one year of professional experience and a U.S. bachelor's degree or its equivalent, or four years of professional experience. Professional experience includes full-time employment in a professional capacity within the regulatory, banking, financial, or related fields. Once a qualified candidate completes the CAIA program, he or she may apply for CAIA membership.

and the right to use the CAIA designation, providing an opportunity to access ongoing educational opportunities.

(source: Chartered Alternative Investment Analyst Association®, 100 University Drive, Amherst, MA 01002, USA)

- **Master of Science in Finance**, major in Financial Engineering, HEC Lausanne, Switzerland, 06/2008
- **Bachelor of Science in Management**, HEC Lausanne, Switzerland, 06/2006

### **Business Background**

- Pictet & Cie, Junior Quantitative Fund Analyst, 08/2008 to 02/2011

## **Item 3 – Disciplinary Information**

As previously stated in Item 9 of the Disclosure Brochure, Mr. Elie G. Barzilay has never been subject to a legal or disciplinary event.

## **Item 4 – Other Business Activities**

No other business activities except for Mirelis Advisors.

## **Item 5 – Additional Compensation**

Mr. Elie G. Barzilay receives no compensation related to advisory services provided to clients other than his remuneration from Mirelis Advisors.

## **Item 6 – Supervision**

Mr. Elie G. Barzilay is the sole investment adviser representative of Mirelis Advisors and ultimately responsible for all activities and services provided by Mirelis Advisors.

The Chief Compliance Officer of Mirelis Advisors is Mr. Sébastien Joliat (tel. +41-22-310-7640, [sjo@MirelisAdvisors.ch](mailto:sjo@MirelisAdvisors.ch)).

2008

# Special Risks in Securities Trading



Should you have any suggestions with regard to future editions of this information brochure, please send them to: [office@sba.ch](mailto:office@sba.ch). We are interested in your feedback, which we will evaluate at the earliest opportunity.

Swiss Bankers Association

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# Introduction

## What this brochure is about

Since 1 February 1997, commercial trading in securities is governed by the Stock Exchange Act (Swiss Federal Act on Stock Exchanges and Securities Trading of 24 March 1995). The Act requires securities dealers to inform their clients about types of transaction and investments that may involve special risks. This brochure contains information about these risks.

The term “**securities dealer**” is used in this brochure to mean your bank.

## Securities and the risks involved

**What are securities?** **Securities** are standardised certificates which are suitable for mass trading, as well as rights not represented by a certificate but with similar features (book-entry securities). They include equities, bonds, units of mutual funds and derivatives. They are offered to the public in a standardised form and denomination, or are sold to more than 20 clients.

**What are derivatives?** **Derivatives** are financial instruments for which the price is derived either from assets (underlyings) such as equities, bonds, precious metals and other commodities; or from benchmark rates such as currencies, interest rates and indices; or from credit or catastrophe events.

An equity option, for example, derives its value from the “underlying” equity. In the following chapters, we will go on to look at **different types** of derivatives, including forwards, futures and structured products as well as options.

**What do you particularly need to bear in mind when carrying out securities transactions?** Securities, and especially derivatives, entail **financial risks**. Derivatives are financial instruments based on a separate underlying and are often composed of different elements, which sometimes makes them difficult to understand. This is particularly true for “exotic” options. This brochure explains these financial instruments and their associated risks. However, it is no substitute for the product descriptions provided by issuers and securities dealers. If you have any further questions, consult your securities dealer.

**Can the risks be unlimited?** There are basically two types of **financial instruments**: those with **limited risk** and those with **unlimited** risk. The purchase of equities or options involves limited risk. At worst, you will lose the entire amount of your invested capital and not make a profit.

**CAUTION** On the other hand, there are certain types of derivatives that can require an additional outlay of capital over and above the original investment. The obligation to make such **margin payments** can amount to many times the purchase price of the investment. Unlimited risk is particularly associated with:

- selling (writing) an uncovered call option,
- selling (writing) a put option or
- forwards and futures transactions.

## Your right to information

**What must your securities dealer inform you about?**

The Stock Exchange Act obliges securities dealers to inform their clients about the risks associated with a given **type of transaction**. 8

The obligation to inform is dependent of the **client's level of experience and specialist knowledge in the area concerned**. Clients must be informed about transactions that entail higher levels of risk or have a complex risk profile, but not about the specific risks relating to individual transactions. 9

## Limits of the duty to provide information

**When can you waive your right to information?**

If you are already familiar **with the risks pertaining to a particular type of transaction**, you may choose not to receive this information from your securities dealer. 10

**What information are securities dealers not obliged to supply?**

Securities dealers are not obliged to inform you about **normal risks**. These are not covered in this brochure. Normal risks chiefly include: 11

- **The risks attached to conventional, widely used financial instruments, such as equities, bonds and collective investments (e.g. units in mutual funds)**

For example, the debtor (issuer) can get into financial difficulties, making him/her incapable of payment (credit and default risks). 12

- **Country risks**

A country risk can arise if a country restricts securities trading, for instance by imposing economic sanctions or currency restrictions. 13

- **Settlement risks**

A settlement risk occurs when you have to pay the purchase price of a security in advance but do not actually receive the security until later. In this event, the risk is that you will pay the purchase price and receive the securities late or even not at all. Conversely, when you are obliged to deliver securities that you have sold, you may not simultaneously receive the purchase price from the buyer. Settlement risks mainly occur in emerging markets (see 209). 14

- **Risks associated with custody of financial instruments**

Financial instruments can be held either in your country or abroad. Generally, they are held where they are most often traded, and are governed by the regulations that apply there. If your securities dealer becomes insolvent, Swiss law stipulates that the financial instruments deposited with that dealer will not form part of their bankruptcy assets, but will be kept separate for your benefit. However, insolvency proceedings can delay the transfer of the financial instruments to you or another securities dealer. If a third-party custodian becomes insolvent, the law in many countries provides that the financial instruments deposited with that custodian by your securities dealer are also normally protected. In less advanced markets (see 196 ff.), however, financial instruments deposited with a third-party custodian in the country concerned may be included in the custodian's bankruptcy assets. 15

- **Liquidity risk**

Liquidity risk is the risk that you will not always be able to obtain an appropriate price for your investment when you sell it. When certain securities and derivatives are impossible to sell, or can only be sold with difficulty and at a sharply reduced price, the market is said to be illiquid. Illiquidity risk occurs especially with shares in un- 16

listed or poorly capitalised companies, investments with sales restrictions, and certain structured products.

The Stock Exchange Act does not require securities dealers to inform you about risks associated with **investments in alternative (non-traditional) investments and emerging or developing markets**. Given the significance of these types of investment, we nonetheless explain the risks typically encountered in these markets in Section Two of this brochure (see 196 ff. below). 17

This brochure does not deal with the issues of **taxation or any other legal consequences** pertaining to securities transactions (e.g. duties of disclosure). We advise you to look into these matters yourself or obtain professional advice. 18

Please read through this brochure carefully and consult your securities dealer if you have any questions. 19

# 1 Section One: Transactions involving special risks

## Options

<b>What are your rights and duties in an option transaction?</b>	As the <b>buyer</b> of an <b>option</b> , you have the right to buy a specified amount of an <b>underlying asset</b> (often simply referred to as the “underlying”) from the <b>seller</b> ( <b>call option</b> ) or sell it to the <b>seller</b> ( <b>put option</b> ) at a predefined price ( <b>strike price</b> ) up until a set time ( <b>expiration date</b> ). The price you pay for this right is called the <b>premium</b> .	20
	As the <b>seller</b> ( <b>writer</b> ) of an option, you must sell the underlying to the buyer at the strike price (call option) or buy the underlying from him/her at the strike price (put option) up until the expiration date, irrespective of the market value of the underlying asset at the time, if he/she chooses to exercise the option.	21
<b>What is the leverage effect in the context of options?</b>	The price of an option is closely linked to that of the underlying asset. Any change in the market value of the underlying asset will result in a greater change in the price of the option. This is termed the <b>leverage effect</b> . It means you participate disproportionately in any rise or fall in the market value of the underlying asset.	22
<b>Which underlying assets can options be based on?</b>	The commonest underlying assets for options are: – assets such as equities, bonds, precious metals and other commodities, – benchmark rates such as currencies, interest rates and indices, – derivatives and – any combination of the above.	23
<b>What are “American-style” options?</b>	“ <b>American-style</b> ” options can normally be exercised on any trading day up to the expiration date.	24
<b>What are “European-style” options?</b>	“ <b>European-style</b> ” options can only be exercised on the expiration date, in other words the date set out in the contract. This does not, however, normally affect their tradability on the secondary market (e.g. on a stock exchange).	25
<b>When are options settled physically, and when are they settled in cash?</b>	Where a call option provides for <b>physical settlement</b> , you can require the seller of the option (writer) to deliver the underlying asset when you exercise the option. With a put option, the writer is obliged to buy the underlying asset from you.	26
	If an option provides for <b>cash settlement</b> , you are only entitled to a sum of money corresponding to the difference between the strike price and the current market value of the underlying asset.	27
<b>When is an option – in the money, – out of the money, – at the money?</b>	A call option is <b>in the money</b> if the current market value of the underlying asset is above the strike price. A put option is in the money if the current market value of the underlying asset is below the strike price. An option that is in the money is said to have an <b>intrinsic value</b> .	28
	A call option is <b>out of the money</b> if the current market value of the underlying asset is below the strike price. A put option is out of the money if the current market value of the underlying asset is above the strike price. In this case, the option has <b>no intrinsic value</b> .	29
	If the current market value of the underlying asset is the same as the strike price, the option is <b>at the money</b> . In this case, it has <b>no intrinsic value</b> .	30

What determines the price of an option?	The price of an option depends on its intrinsic value and on what is referred to as the <b>time value</b> . The latter depends on a variety of factors, including the remaining life of the option and the volatility of the underlying. The time value reflects the chance that the option will be in the money. It is higher for options with a long duration and a very volatile underlying and for options that are at the money.	31
What types of options are there?	<p><b>Warrants</b> are options in securitised form that are traded on an exchange or over the counter (OTC).</p> <p><b>Exchange Traded Options</b> are non-securitised, but are traded on an exchange.</p> <p><b>OTC (Over-the-Counter) options</b> are neither securitised nor traded on-exchange. They are agreed directly off-exchange between the seller and the buyer. If you wish to cancel (<b>close out</b>) an option of this type before the expiration date, you must make a corresponding offsetting trade with your counterparty. OTC options with precious metals and currencies as their underlying are offered publicly as standardised products. <b>Tailor-made OTC options</b>, by contrast, are specially created for individual investors.</p>	32 33 34
What is "margin cover"?	If you sell an option, you have to deposit either an amount of the underlying asset or another form of collateral for the entire duration of the contract. The level of this collateral or <b>margin</b> is determined by the securities dealer. The exchange stipulates a minimum margin for traded options.	35
	<b>CAUTION</b> If the <b>margin cover</b> proves insufficient, the securities dealer can require you to provide additional collateral (via a <b>margin call</b> ).	36
What risks do you face as the buyer of an option?	Generally speaking, if the market value of the underlying asset falls, so does the value of your <b>call option</b> . The value of your <b>put option</b> tends to fall if the underlying asset rises in value. Normally, the less your option is in the money, the larger the fall in the option's value. In such cases, value reduction normally accelerates close to the expiration date.	37
	The value of your call option can drop even when the value of the underlying remains unchanged or rises. This can happen as the time value of your option falls or if supply and demand factors are unfavourable. Put options behave in precisely the opposite manner.	38
	<b>CAUTION</b> You must therefore be prepared for a potential loss in the value of your option, or for it to expire entirely without value. In such a scenario, you risk losing the whole of the premium you paid.	39
What risks do you face as the seller (writer) of a covered call option?	If, as writer of a call option, you already have a corresponding quantity of the underlying at your disposal, the <b>call option</b> is described as <b>covered</b> . If the current market value of the underlying exceeds the strike price, your opportunity to make a profit is lost since you must deliver the underlying to the buyer at the strike price, rather than selling the underlying at the (higher) market value. You must have the underlying assets freely available as long as it is possible to exercise the option, i.e. they may not, for example, be blocked by being pledged for other purposes. Otherwise, you are essentially subject to the same risks as when writing an uncovered call option (see below).	40
What risks do you face as the seller (writer) of an uncovered call option?	If, as writer of a call option, you do not have a corresponding quantity of the underlying at your disposal, the <b>call option</b> is described as <b>uncovered</b> . In the case of options with physical settlement, your potential loss amounts to the price difference between the strike price paid by the buyer and the price you must pay to acquire the	41



underlying assets concerned. Options with cash settlement can incur a loss amounting to the difference between the strike price and the market value of the underlying.

**CAUTION** Since the market value of the underlying can move well above the strike price, your potential loss cannot be determined and is theoretically unlimited. 42

As far as American-style options in particular are concerned, you must also be prepared for the fact that the option may be exercised **at a highly unfavourable time when the markets are against you**. If you are then obliged to make physical settlement, it may be very expensive or even impossible to acquire the corresponding underlying assets. 43

You must be aware that your potential losses can be far greater than the value of the underlying assets you lodged as collateral (margin cover) either when entering into the contract or thereafter. 44

**What risks do you face as the seller (writer) of a put option?**

As the writer of a put option, you must be prepared for potentially substantial losses if the market value of the underlying falls below the strike price you have to pay the seller. Your potential loss corresponds to the difference between these two values. 45

As the writer of an American-style put option with physical settlement, you are obliged to accept the underlying assets at the strike price if the buyer exercises the option, even though it may be difficult or impossible to sell the assets and may well entail substantial losses. 46

**CAUTION** Your potential losses can be far greater than the value of any underlying assets you may have lodged as collateral (margin cover). You could in a worst case lose your entire capital invested. 47

**What is a covered option?**

With a **covered option**, you purchase an underlying asset (equity, bond or currency) and simultaneously write a call option on that same asset. In return, you are paid a premium, which limits your loss in the event of a fall in the market value of the underlying asset. By the same token, however, your potential return from any increase in the asset's market value is limited to gains up to the option's strike price. **Traditional covered options** require that the underlying asset be lodged as collateral, which makes **you the covered writer**. 48

Synthetic **covered options** are based on the idea of replicating traditional covered options. However, this is achieved by means of only one transaction. Both the purchase of the underlying asset and the writing of the call option are carried out synthetically using derivatives. The purchase price of such a product is identical to that of the underlying, less the premium received for the sale of the call option. Hence, the synthetic product is sold more cheaply than its underlying. 49

**What are the risks of a covered option?**

Covered options do **not contain a hedge against falls in the market value of the underlying**. However, by writing a call option (traditional covered option) or by calculating the return from the sale of a call option into the product price (synthetic covered option), any loss in market value of the underlying has less impact than it would in the case of a direct investment. In effect, the option premium thereby limits any loss in the market value of the underlying. 50

Either cash settlement or physical delivery of the underlying takes place on the expiration date. If the market value of the underlying on expiration is higher than the strike price, the holder of an option with cash settlement is paid a specified cash amount as settlement. 51

**CAUTION** If, however, the market value of the underlying is lower than the strike price, the holder of an option with physical settlement receives physical delivery of the underlying asset. In this case, the option holder bears the full risk associated with the underlying. 52

**What are option strategies?** If you acquire two or more options, based on the same underlying, which differ in either the option type (call or put), the quantity, the strike price, the expiration date or the type of position (long or short), this is referred to as an **option strategy**. 53

**CAUTION** Given the large number of possible combinations, we cannot go into detail here about the risks involved in any particular case. Before entering into any such transaction, be sure to consult your securities dealer about the particular risks involved. 54

**What are exotic options?** Unlike the “plain vanilla” put and call options described above, **exotic options** are linked to additional conditions and agreements. Exotic options come in the form of tailor-made OTC options or as warrants. 55

Given the special composition of exotic options, their price movements can vary markedly from those of their “plain vanilla” cousins. 56

**CAUTION** You must be aware that larger transactions can trigger price movements even shortly before expiration and that these can render an option worthless. Before buying or selling any exotic options, be sure to seek comprehensive advice about the particular risks involved. 57

There is no limit to the possible structures for exotic options. We cannot describe in full here the risks involved in any particular case. 58

The examples of exotic options listed below can be broadly divided into two categories: path-dependent options and options on more than one underlying.

**What are path-dependent options?** Unlike “plain vanilla” options, for **path-dependent options**, it is not just when the option expires or is exercised that the market value of the underlying is important. You also need to take into account fluctuations in the market value of the underlying during the life of the option when contemplating such an investment. The following are examples of path-dependent options: 59

– **Barrier options**

Your exercise rights for **knock-in barrier options** only arise if the market value of the underlying reaches a fixed threshold (**barrier**) within a specified period. Exercise rights for **knock-out barrier options** expire if the market value of the underlying reaches the specified barrier during the given time period. 60

If this barrier is between the market value of the underlying at the time the option was entered into and its strike price, it is referred to as a **kick-in/kick-out** barrier option. 61

**Double-Barrier options** have both an upper and a lower barrier and may take the form of knock-in and knock-out barrier options. 62

**CAUTION** When buying a **barrier option**, you must be aware that your exercise rights only arise when the market value of the underlying reaches the barrier (knock-in/kick-in option) or that they expire irrevocably when that barrier is reached (knock-out/kick-out option). 63

### – Payout options

The **Payout options** accord you the right to payment of a fixed amount agreed in advance. 64

In the case of a **digital** (otherwise known as “**binary**”) **option**, you receive payment 65 if the market value of the underlying reaches a fixed value once during a specified time period (**one-touch digital option**) or precisely on the day of expiration (**all-or-nothing option**). For the one-touch digital option, payment occurs either immediately the barrier is reached or on the date of expiration (**lock-in option**).

With **lock-out options**, you only receive the fixed payment if the market value of the 66 underlying does not reach the agreed barrier during a specified time period.

**CAUTION** If you sell a payout option you owe the fixed amount if the barrier is reached, regard- 67 less of whether or not the option is in the money when exercised or on the expiration date, or to what extent. This means that the amount you owe can be considerably larger than the option’s intrinsic value.

### – Asian options

For Asian options, an average value is derived from the market value of the underly- 68 ing over a specified time period. This average is used to determine the underlying’s value for an **average-rate option** and to calculate the strike price for an **average-strike option**.

**CAUTION** The calculation of an average value for the underlying in the case of the average-rate 69 option can result in the value of the option on the expiration date being considerably lower for the buyer and considerably higher for the writer than the difference between the strike price and the current market value on expiry.

**CAUTION** For an average-strike option, the average strike price of a call option can be consid- 70 erably higher than the price originally set. For an equivalent put option, the strike price can similarly be lower than the price originally set.

### – Lookback options

With a **lookback option**, the market value of the underlying is recorded periodically 71 over a specified time period.

For a **strike-lookback option** the lowest value (call option) or the highest value (put 72 option) of the underlying becomes the strike price.

The strike price remains unchanged for a **price-lookback option**, with the highest 73 value (call option)/lowest value (put option) being used in calculating the option value of the underlying.

**CAUTION** For lookback options, both the calculated strike price and the calculated value of the 74 underlying can vary considerably from the market prices prevailing on the expiration date. If you sell an option of this type, you must be aware that it will always be exercised at the most unfavourable value for you.

### – Contingent options

When you buy a **contingent option** you must pay the premium only if the market 75 value of the underlying reaches or exceeds the strike price during the life of the option (American-style option) or on the expiration date (European-style option).

**CAUTION** You will have to pay the entire premium even if the option is only just at the money or just in the money. 76

– **Cliquet and Ladder options**

For **cliquet options** (also known as **ratchet options**), the strike price is modified for the following period, normally at regular intervals, in line with the market value of the underlying. Any intrinsic value of the option is locked in. All lock-ins arising over the entire life of the option are accumulated. 77

For **ladder options**, these modifications take place when the underlying reaches specified market prices, rather than at regular intervals. Normally, only the highest intrinsic value is locked in. In rare cases, all the intrinsic values recorded are added together. 78

**CAUTION** If you sell a cliquet option, you are required on the expiration date to pay the buyer all the accumulated lock-ins in addition to any intrinsic value of the option. If you sell a ladder option you must pay the buyer the highest lock-in amount, which can be considerably higher than the option's intrinsic value on the expiration date. 79

**What are options on more than one underlying?**

Examples of options on more than one underlying are:

– **Spread and outperformance options**

Both spread and outperformance options are based on two underlyings. With a **spread option**, the absolute difference in movement between the two underlyings forms the basis for calculating the option's value. By contrast, the value of an **out-performance option** is based on the relative difference, i.e. the percentage outperformance of one underlying compared to the other. 80

**CAUTION** Even if the underlying performs positively, the difference between the underlyings may be equal or lower in absolute as well as relative terms, thus having a negative impact on the value of the option. 81

– **Compound options**

The **Compound options** have an option as their underlying, i.e. they are options on options. 82

**CAUTION** Compound options can have an especially large leverage effect. If you sell an option of this type, you can be faced with very substantial obligations. 83

– **Credit default options**

With a **credit default option**, a credit risk of the original risk-taker (risk seller) is transferred to a third party (risk buyer), who receives a premium in return. If the defined credit event occurs, the risk buyer is obliged to effect a cash settlement or take on the non-performing loan (or another delivery obligation) by way of physical settlement at a previously determined price. Credit default options are a form of credit derivatives. 84

**CAUTION** The risk of chain reactions on the credit market is high and can easily be underestimated. There is also the risk that lack of liquidity will lead to price distortions when volumes are low. This may mean that the investment can only be sold at a low price, longer term or even not at all. 85

## Forwards and Futures

<b>What duties do you have with forwards and futures?</b>	With <b>forwards</b> and <b>futures</b> you undertake to deliver or take delivery of a defined quantity of an underlying on a specified expiration date at a price agreed on the contract date. Unlike with options, which (for the buyer at least) only give rise to rights, forwards and futures involve both parties entering into obligations. You do not have to pay a premium when the contract is concluded.	86
<b>CAUTION</b>	Forwards and futures can involve special risks. You should therefore only make investments of this type if you are familiar with this type of instrument, have sufficient liquid assets and are able to absorb any losses that may arise.	87
<b>What is the difference between futures and forwards?</b>	<b>Futures</b> are traded on an exchange. They take the form of contracts in which the quantity of the underlying and the expiration date are standardised.	88
	<b>Forwards</b> are not traded on an exchange; hence they are referred to as OTC (over-the-counter) forwards. Their specifications may also be standardised; otherwise they may be individually agreed between the buyer and seller.	89
<b>What underlying assets can forwards and futures be based on?</b>	The <b>most common underlyings</b> for forwards and futures are: – assets (equities, bonds, precious metals and other commodities), – benchmark rates such as currencies, interest rates and indices.	90
<b>What is a margin?</b>	When you buy or sell (short) an underlying asset on the futures market, you must supply a specified <b>initial margin</b> when entering into the contract. This is usually a percentage of the total value of the contracted instruments. In addition, a <b>variation margin</b> is calculated periodically during the life of the contract. This corresponds to the book profit or loss arising from any change in value in the contract or underlying instrument. The way in which the variation margin is calculated will depend on the rules of the exchange concerned and/or the conditions of the contract.	91
	As the investor, you are obliged to deposit the required initial and variation margin cover with the securities dealer for the entire life of the contract.	92
<b>CAUTION</b>	In the event of a book loss, the <b>variation margin</b> can be several times as large as the initial margin.	93
<b>How is a transaction closed out?</b>	As the investor, you are entitled to close out the contract at any time prior to the expiration date. How this is done depends on the type of contract or stock exchange practice. You either “sell” the contract or agree an offsetting trade with identical terms. Concluding such an offsetting trade means that the obligations to deliver and receive cancel one another out.	94
<b>How is the transaction settled?</b>	If you do not close out the contract prior to the expiration date, you and the counterparty must settle it.	95
	If the underlying in your contract is a <b>physical asset</b> , settlement is achieved by physical delivery or a cash payment. Generally, the asset is physically delivered. Only in exceptional cases do the contract provisions or stock exchange practice call for cash settlement. All other fulfilment specifications, especially the definition of the place of fulfilment, can be found in the relevant contract provisions.	96

The difference between **physical delivery** and **cash settlement** is that with physical delivery, underlyings amounting to the entire contractual value must be delivered, whereas with cash settlement, only the difference between the agreed price and the market value on settlement needs to be paid. This means that you need more funds available for physical delivery than for cash settlement. 97

If the underlying in your contract is a **reference rate** or **benchmark**, fulfilment by physical delivery is not permitted (except for currencies). Instead, settlement is always in cash. 98

**What special risks do you need to bear in mind?**

For **forward sales**, you must deliver the underlying at the price originally agreed even if its market value has since risen above the agreed price. In such a case, you risk losing the difference between these two amounts. 99

**CAUTION** Theoretically, there is no limit to how far the market value of the underlying can rise. Hence, your potential losses are similarly unlimited and can substantially exceed the margin requirements. 100

**CAUTION** For **forward purchases**, you must take delivery of the underlying at the price originally agreed even if its market value has since fallen below the agreed price. Your potential loss corresponds to the difference between these two values. Your maximum loss therefore corresponds to the originally agreed price. Potential losses can substantially exceed the margin requirements. 101

In order to limit price fluctuations, an exchange may set price limits for certain contracts. Find out what price limits are in place before effecting forward or futures transactions. This is important since closing out a contract can be much more difficult or even impossible if a price limit of this type is reached. 102

**CAUTION** If you sell forward an underlying which you do not hold at the outset of the contract, this is referred to as a **short sale**. In this case, you risk having to acquire the underlying at an unfavourable market value in order to fulfil your obligation to effect delivery on the contract's expiration date. 103

**What special factors apply to OTC forwards?**

The market for standardised **OTC forwards** is transparent and liquid. Hence, contracts can normally be closed out without difficulty. There is no actual market for OTC forwards agreed individually, and hence the positions they entail may only be closed out with the agreement of the counterparty. 104

**What special factors apply to combinations?**

Since **combinations** comprise a number of elements, closing out individual elements can considerably alter the risks inherent in the overall position. Before entering into any such transaction, be sure to consult your securities dealer about the particular risks involved. 105

Given the many possible combinations, we cannot go into detail in this brochure about the risks involved in any particular case. Before making a purchase, be sure to seek comprehensive advice about these risks. 106

## Structured Products

<b>What are structured products?</b>	Structured products are issued either publicly or privately. Their <b>redemption value depends on the performance of one or more underlyings</b> . They may have a fixed or unlimited term and consist of one or more components.	107
<b>What are the common types of structured products?</b>	Here is a list of the <b>common product categories</b> , based on the categorisation model used by the Swiss Structured Products Association (SSPA): <ul style="list-style-type: none"> <li>– capital protection products (see 116 ff. below)</li> <li>– yield enhancement products (see 126 ff. below)</li> <li>– participation products (see 130 ff. below)</li> <li>– leverage products (see 135 ff. below)</li> </ul>	108
<b>Can products of this type be traded on an exchange?</b>	Structured products may be listed for trading <b>on an exchange</b> , but do not have to be.	109
<b>Can you sell a structured product?</b>	The tradability of a structured product depends on whether the issuer or a market maker is prepared to make a price. Even if they are, <b>liquidity risks</b> can still arise. If the market is not liquid, you run the risk of having to either hold the financial instrument until the end of its term or sell it during the term at an unfavourable price. It can also be difficult or impossible to determine a fair price or even compare prices at all, as there is often only one market maker.	110
<b>What is the issuer risk?</b>	You bear the risk that the debtor of a structured product may become insolvent ( <b>issuer risk</b> ). The instrument's value is therefore dependent not only on the performance of the underlying asset but also on the creditworthiness of the issuer, which may change over the term of the structured product.	111
<b>What special risks do you need to bear in mind?</b>	Every structured product has its <b>own risk profile</b> , and the risks of its individual components may be reduced, eliminated or increased. In particular, it may profit to different degrees from rising, constant or falling market values of the underlying, depending on the product involved.	112
<b>CAUTION</b>	It is extremely important to find out exactly what the risks are before acquiring a product of this kind. This information can be found in, for example, the issue documents or the product description concerned.	113
<b>Are structured products covered by the Collective Investment Act?</b>	Structured products are <b>not categorised as collective investments</b> under the Collective Investment Schemes Act (Federal Act on Collective Investment Schemes of 23 June 2006). Unlike with collective investments, the issuer is liable with his or her own assets (as is any guarantor, to the extent of a guarantee they have provided), and there is no backing from specially protected assets. You therefore need to bear in mind that in addition to a potential loss resulting from a decline in the market value of the underlyings (market risk), you may in the worst case lose your entire investment because the issuer or guarantor becomes insolvent (issuer or guarantor risk).	114
<b>Do you have an entitlement to voting rights and dividends?</b>	You do not normally have any entitlement to voting rights or dividends if you buy a structured product.	115



## Capital Protection Products

What types of capital protection are there?	Some structured products offer capital protection. The level of this protection is fixed by the issuer when the product is issued and indicates the percentage of the <b>nominal value</b> that will be repaid to the investor on expiration. However, capital protection generally only applies at the end of the term and may, depending on the product conditions, be (far) lower than 100% of the invested capital.	116
<b>CAUTION</b>	Some structured products offer only conditional capital protection, which can be lost if the value touches, falls below or rises above a predefined threshold (barrier, knock-out level). Repayment is then dependent on the performance of one or more underlyings.	117
What are structured products with capital protection?	<b>Structured products with capital protection</b> consist of two elements, such as a fixed-income investment (especially a bond or a money market investment) and an option. This combination enables the holder to participate in the performance of one or more underlyings (via the option or <b>participation component</b> ) while at the same time limiting potential losses (via the fixed-income investment or <b>capital protection component</b> ). The capital protection component may only cover a portion of the capital invested.	118
What is the purpose of the capital protection component?	The <b>capital protection component</b> determines the minimum repayment you receive on expiration, regardless of how the participation component performs.	119
What does the capital protection relate to?	The capital protection is linked to the nominal value rather than the issue price or purchase price. Hence, if the issue/purchase price you pay exceeds the nominal value, <b>only the nominal value</b> is capital-protected. The protection of your capital outlay drops accordingly. If, however, the issue/purchase price is less than the nominal value, the protection of your capital outlay rises accordingly.	120
Is the invested capital fully protected?	The capital protection component can be well under 100% of the capital invested, depending on the product. Capital protection does not therefore mean 100% repayment of nominal value or the purchase price for all products. Structured products with capital protection generally offer lower returns than direct investments in the underlying, as the capital protection costs money.	121
<b>CAUTION</b>	If you wish to sell a structured product with capital protection before it expires, you may receive less than the capital protection component as the capital protection only applies if you keep the product until the redemption date.	122
Does the capital protection still apply if you sell the product during its term?		
What is the purpose of the participation component?	The <b>participation component</b> determines how you benefit from price movements in the underlying(s) when you buy a structured product. In other words, it fixes the level of your potential return over and above the capital protection component. Some structured products with capital protection offer only a limited potential participation (those with a cap); some (those without a cap) offer unlimited potential participation. Others require the market value of the underlying to touch, rise above or fall below a specific barrier before you can make a profit.	123
How high is the risk on the participation component?	The risk on the participation component is <b>the same as that on the corresponding option or combination of options</b> . Depending on the movements in the market value of the underlyings, the participation component may therefore be zero.	124



**CAUTION** Your maximum loss on a structured product with capital protection is limited to the **difference between the purchase price and the capital protection**, provided you continue to hold the product until expiration. You may also miss out on a profit due to the fact that full or partial repayment of the capital is guaranteed but no income (interest) is paid. Please be aware that there is also issuer risk (see 111). 125

**What is the maximum possible loss?**

**What are structured products with yield enhancement?** **Structured products with yield enhancement** consist of two elements, such as a fixed-income investment and an option (mainly on equities or currencies), and possibly a currency swap. This combination enables you to participate in the performance of one or more underlyings (via the option component). However, these financial instruments offer **no or only conditional capital protection**. The interest that is paid means you receive a higher return than with a direct investment if the price of the underlying remains essentially unchanged. On the other hand, you will not benefit from the full potential return of the underlying. 126

If the market value of the underlying rises, you will receive the stipulated interest and the nominal value on expiration (equally, the product may provide for a discount on the issue price). If the market value of the underlying rises sharply, you could possibly have earned a higher return on a direct investment. However, if the market value of the underlying falls sharply, you will receive both the interest payment and the underlying on expiration (unless the product offered a discount on the issue price). 127

**What special risks do you need to bear in mind?** Many products with yield enhancement refer to several underlyings. You as investor receive the security with the worst performance on expiration (either physically or in the form of cash) if the underlying touches, rises above or falls below a predefined barrier during the term of the financial instrument. If the performance of the underlying is negative, the financial instrument can trade some way below the issue price during its term even if the barrier is not touched, exceeded or undershot. The level of interest rate is directly related to the level of the barrier. The nearer the barrier is to the market price of the underlying on the day of issue, the higher the interest you receive will generally be, but the higher the risk that the barrier will be reached, and vice versa. 128

**CAUTION** When you invest in a structured product with yield enhancement, you could in the worst case scenario lose the entire capital that you have invested. 129

**What is the maximum possible loss?**

**What are structured products with participation?** **Participation Products**  
**Structured products with participation** enable you to participate in the performance of one or more underlyings. However, they offer **no or only conditional capital protection**. If the participation product offers conditional capital protection, the risk is smaller than with a direct investment provided the market value of the underlying does not reach a specific barrier (termed the “knock-out”). 130

**CAUTION** If the market value of the underlying touches, rises above or falls below the barrier, you will lose the capital protection. 131

What special risks do you need to bear in mind?	The <b>risk of a structured product with participation</b> is generally the same as that of the underlying. Unlike with a direct investment, however, you do not receive voting rights and you are not entitled to a dividend. You do, though, bear the credit risk of the product's issuer.	132
	Many products with participation refer to several underlyings. You as investor receive the security with the worst (or sometimes best) performance on expiration (either physically or in the form of cash) if the market value of the underlying touches, rises above or falls below a predefined barrier during the term of the financial instrument. The financial instrument can trade some way below the issue price during its term even if the barrier is not touched, exceeded or undershot. Moreover, the level of participation is directly related to the level of the barrier. If you have a higher risk tolerance when selecting the barrier, you will enjoy a higher participation.	133
<b>CAUTION</b> What is the maximum possible loss?	When you invest in a structured product with participation, you could in the worst case scenario lose the entire capital that you have invested.	134
What are structured products with leverage?	<p><b>Leverage Products</b></p> <p><b>Structured products with leverage</b> enable you to achieve a leverage effect by investing less capital than you would have to if you invested directly in the underlying. This means you can benefit from short-term trends.</p>	135
	Structured products with leverage are suitable for short-term speculation but also for strategically hedging a portfolio.	136
What special risks do you need to bear in mind?	Because of the leverage effect, you need to <b>carefully and regularly monitor</b> the underlying, since structured products with leverage can experience a larger rise in profits but also a bigger loss than the underlying.	137
<b>CAUTION</b> What is the maximum possible loss?	When you invest in a structured product with leverage, you could in the worst case lose the entire capital that you have invested.	138
<b>Products Used for Financing or Risk Transfer</b>		
What exactly are these products?	The financial instruments discussed in this section have the <b>same or similar profit and loss structures as certain conventional financial instruments</b> (equities or bonds).	139
	Such financial instruments may be listed for trading on an exchange, but do not have to be.	140
	The risks associated with these products are not necessarily the same as those of the financial instruments they contain. It is therefore extremely important to find out exactly what the risks are before acquiring a product of this kind. This information can be found in, for example, the <b>product description concerned</b> .	141
What are credit and catastrophe derivatives?	There are some products that are mainly used to transfer risks. These include <b>credit and catastrophe derivatives</b> . They are financial instruments where the "underlying" is an event such as a credit event (default of a loan or bond) or a natural disaster.	142

Derivatives of this type can be used by the bearer of a risk to transfer it to others. Credit derivatives come in the form of swaps, options or hybrid financial instruments.

**CAUTION** Credit and catastrophe derivatives involve a **liquidity risk**. Often such instruments cannot be sold before the end of their term, because there is no market for them. 143

**Credit bonds** securitise the risks and transfer them to third parties as **credit-linked notes, collateralised debt obligations and asset-backed securities**. As a result, the buyer takes on the risk associated with a loan portfolio. 144

### **Credit-linked notes (CLN)**

CLN are bonds whose redemption and interest payments depend on the performance of a specific underlying or benchmark portfolio (e.g. loan, bond). 145

**CAUTION** Look closely at the creditworthiness of the debtor to which the CLN is linked, as the CLN can end up being valueless if a credit event occurs. There is an issuer risk, i.e. a credit risk of the issuing bank, just as with structured products. The secondary market for CLN is highly illiquid, and you should therefore assume that you will not be able to sell one before the end of its term. 146

### **Collateralised debt obligations (CDO)**

CDO are bonds backed by a diversified debt portfolio (mostly loans, bonds or credit default swaps). They give you access to investments that are unattractive or even unattainable for individual investors. Since CDO are often divided up into a number of tranches with differing credit risks, you can decide what credit risk you wish to take on. If a debtor in the debt portfolio experiences a credit event, the equity-like tranches are affected first: they may be only partially redeemed, or not redeemed at all. If a number of debtors default, this affects the remaining tranches in order of creditworthiness, until finally the tranche with the highest credit rating (comparable to that of first-class bonds) may only be partially redeemed, or not redeemed at all. The value of a CDO is based primarily on the probability of a credit event affecting the individual companies in the portfolio. This probability of default is determined using statistical methods and on the basis of historical data, and can cease to be meaningful in extreme market conditions. 147

Before you invest in a CDO, you should also look at the track record of the manager in charge of it: he or she will receive a performance-related bonus and will often have a holding in the CDO him/herself. If the portfolio is not run by a manager (which is termed a “static” portfolio), its composition remains unchanged throughout its term. In this case you should pay special attention to the composition of the portfolio. 148

**CAUTION** CDO typically have a term of several years. As there is generally no secondary market, you should assume that you will not be able to sell the CDO before the end of its term. 149

### **Asset-backed securities (ABS)**

In ABSs, risks (such as a range of receivables) are grouped together and transferred to a special purpose vehicle (SPV). The SPV finances this transaction by issuing securities backed by a pool of assets or a portfolio. If the collateral is a mortgage, this kind of instrument is called a **mortgage-backed security (MBS)**. The individual com- 150

ponents of the portfolio would be unattractive or even unobtainable in this form for individual investors. However, the composition of the portfolio makes it possible to combine together and sell a range of assets and risks. By grouping together different types of credit risk, different risk profiles can be created.

Even if a pool or portfolio is created, lack of diversification can lead to a concentration of risk. 151

**CAUTION** Credit bonds are often issued by particular types of offshore companies (SPV). In this event you should pay special attention to the issuer risk and the quality of government supervision of such SPVs. 152

## 2 Section Two: Additional Information

### Alternative (Non-Traditional) Investments

**What are alternative or non-traditional investments?**

**Alternative or non-traditional investments** are investments that do not fall within the traditional asset classes, such as equities, bonds or money market products. They include a **wide range of instruments and strategies**. This section focuses on the classes that are most important in terms of risk information:

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- hedge funds (see 159 ff. below)
- private equity (see 174 ff. below)
- real estate (see 182 ff. below)
- precious metals and other commodities (see 189 ff. below)

This list is not exhaustive and this brochure cannot point out all the risks and issues that need to be taken into account in connection with **alternative or non-traditional investments**.

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**CAUTION** Be sure to obtain comprehensive advice before investing in **alternative or non-traditional investments**, and examine the offering carefully.

**What do you need to bear in mind when making direct investments?**

Instruments allowing for **direct investment** can make sense in terms of diversifying a portfolio (risk distribution) because their returns are less dependent on factors such as the performance of the markets and levels of interest rates than those of conventional investments. However, the minimum outlay required for direct investments is generally very high, and they are often not accessible to all investors.

155

**What about indirect investments?**

To overcome these obstacles and avoid the risks of the large direct investments required, the financial sector has developed instruments for **indirect investment**. They include certificates, notes, investment funds, funds of funds, commodity futures and forward contracts. All these structures are based on one or more of the asset classes mentioned below. If you are interested in indirect investments, you need to bear in mind not just the risks of alternative investments as an asset class, but also the risks of the instrument concerned – the risks associated with structured products, for example. Please note that this section does not deal with the risks of structured products, forward contracts and futures, as these were discussed in the preceding sections (see “Forwards and Futures” and “Structured Products”).

156

**What are offshore funds?**

Offshore investments are often structured as funds or partnerships (such as limited partnerships) and domiciled in countries where legislation and supervision can be weak – hence the name “offshore funds”. The Swiss financial supervisory authority does not permit the public distribution of such funds in Switzerland.

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**CAUTION** The legislation and supervision applying to offshore funds are much less strict than for traditional investments, which means that **investors may enjoy less protection**. They may find it difficult to enforce their rights, and problems and delays may occur when settling buy and sell orders for units of such funds.

158

<b>What are hedge funds?</b>	<b>Hedge Funds</b> Hedge funds are the best-known form of alternative or non-traditional investments. Despite what their name suggests, <b>hedge funds</b> do not necessarily have anything to do with hedging. Indeed, they take on sometimes very high levels of risk in order to obtain an above-average return. Hedge funds include all forms of investment funds, investment companies and partnerships that use derivatives not just for hedging but also for investment, that are able to engage in short selling or take on significant leverage by borrowing. Other features typical of hedge funds include their freedom to choose their asset classes, markets (including emerging markets) and trading methods. Hedge funds normally require high minimum investments. They frequently offer only limited opportunities for subscription and redemption, with long notice periods. The portfolio managers of hedge funds receive performance-related bonuses and often hold a personal stake in the funds.	159
<b>CAUTION</b> <b>What should you particularly bear in mind about hedge funds?</b>	Pay special attention to the following: <ul style="list-style-type: none"> <li>– A hedge fund may be <b>less transparent than a traditional investment fund, for example</b>, as investors are not always informed about planned strategies and changes to them, or changes of portfolio manager. Hedge funds are also not subject to any disclosure requirements. 160</li> <li>– Unlike traditional collective investments, hedge funds have <b>limited liquidity (units may generally only be redeemed once a month, quarterly or annually)</b>. Normally, investors can only invest in a hedge fund at specific times. There are generally long notice periods for redemptions and long lock-up periods (periods during which investors are obliged to leave their capital in the fund). 161</li> <li>– Delays may occur, and unfavourable prices may result, when settling buy and sell orders for hedge fund units. There is no guarantee that investors will be able to enforce their rights. 162</li> </ul>	160 161 162
<b>What are funds of hedge funds or multi-manager hedge funds?</b>	Investors invest in <b>funds of hedge funds or multi-manager hedge funds</b> in order to reduce risk. These funds invest their capital in a number of hedge funds and spread it across a range of hedge fund managers that cover different investment styles, markets and instruments. There are also structured products that you can use to invest in hedge funds or hedge fund indices.	163
<b>What strategies do hedge funds pursue?</b>	The main hedge fund <b>strategies</b> seen on the market are as follows: <ul style="list-style-type: none"> <li>– <b>Equity hedge (“long,” “short”)</b>  Equity hedge funds identify undervalued (buy or long position) and overvalued (short selling or short position) equities in specific regions or market segments and attempt to make profits in the belief that sooner or later these positions can be closed out at a profit. 164 165</li> <li>– <b>Arbitrage strategies</b>  Arbitrage strategies identify price differences between identical or similar investments in different markets and try to exploit them. Such strategies include equity-market neutral, fixed-income arbitrage, convertible-bond arbitrage and mortgage-backed-securities arbitrage. 166</li> </ul>	164 165 166

### – Event-driven

Managers that pursue this kind of strategy try to make a profit from events such as upcoming changes in a company (mergers, takeovers, restructurings, turnarounds, etc.). Examples of such strategies are merger arbitrage, distressed securities and special situations. 167

### – Global macro

Hedge funds that pursue global macro strategies attempt to identify macro-economic developments such as changes in interest or exchange rates at an early stage and exploit them for profit. This category includes growth funds and emerging market funds. 168

### – Managed futures

This type of hedge fund deals in futures (standardised, exchange-listed contracts) on financial instruments, currencies and commodities. 169

**What risks do you take on when you invest in a hedge fund?**

Generally speaking, hedge fund managers do not need to be licensed by an authority and are **largely unregulated**. In particular, hedge funds are not subject to the numerous investor protection regulations that apply to authorised collective investments. These include rules on liquidity, redemption of fund units at any time, avoiding conflicts of interest, fair prices for fund units, disclosure and limitations on borrowing. 170

Since these rules do not apply to hedge funds, they can use much more leverage than traditional authorised funds, and engage in complex investment transactions that are not permitted for traditional collective investments. A hedge fund is allowed to adopt **aggressive strategies** including the widespread use of short selling, leverage, swaps, arbitrage, derivatives and programme trading. Their investment strategies are often highly complex and very intransparent. You will often receive little or no information about changes of strategy that may lead to a significant increase in risk, or receive such information only at a late stage. 171

As part of their investment strategy, hedge funds can also use derivatives such as futures, options and swaps that may be listed for trading on an exchange but do not have to be. These instruments may be subject to significant price volatility, resulting in a **high risk of loss** for the fund. The low margins typically required to build up a position in such instruments mean that high levels of borrowing can be used. Depending on the instrument, a relatively small change in the price of the contract can therefore lead to a large profit or loss in comparison with the capital lodged as collateral and hence to further, unforeseeable losses that can exceed any margin cover. 172

**CAUTION Investment vehicles that are not listed on an exchange** also involve further risks as there is neither an exchange nor a secondary market where units can be sold or open positions closed out. It may be impossible to unwind an existing position or determine the value or risk of a position. If a hedge fund sells uncovered options on securities, it may be exposing itself to an unlimited risk of loss. 173

### Private Equity

**What is private equity?**

**Private equity** is a form of risk capital financing for companies that either are **not exchange-listed** or – occasionally – wish to delist. Investments are usually made at an early stage in a company's development, when its chances of success are uncertain and the risks are therefore high. 174



Where private equity flows into young companies (start-ups) or small companies with growth potential that are at an early stage in their development, the term **venture capital** is also used. Private equity now also extends to risk capital made available to a company immediately before it goes public (**late-stage financing, mezzanine financing**). Normally the financing is constructed in such a way that the proceeds of the initial public offering are used to wholly or partially redeem the holdings of the shareholder entrepreneurs. If a change of ownership is financed, for example a delisting, the term **“buyout”** is customarily used. 175

The success of a private equity investment depends on the correct timing of the “exit” or sale and – especially with indirect investments via a fund, for example – on the quality of the private equity manager. The exit can be effected by going public (initial public offering or IPO), a sale to another company (trade sale) or to another private equity fund (secondary sale), or a management buyout. The choice of solution will depend largely on the market conditions prevailing at the time. How easy or difficult the exit phase is, and whether the proceeds meet expectations, will depend on factors such as the performance of the equity markets. 176

**What are the risks of private equity investments?**

Private equity investments are **not regulated compared to equities listed for trading on an exchange**. This means that investors may be exposed to more risks, for example due to lack of transparency (e.g. limited access to financial statements, lack of publication). 177

Private equity investments involve considerable risks and can lead to substantial losses. They are based on a long-term approach and are much less liquid than exchange-listed equities. Normally, private equity investments cannot be sold until some years after the original investment. You should be aware that your capital will be tied up, either completely or with access subject to restrictions, for a long time. No distributions are made prior to exit from investments. You do not normally have any entitlement to exit early. 178

Companies that are potential candidates for private equity investments may have high levels of borrowing and therefore be more sensitive than established companies to negative market developments such as rising interest rates. There is also a greater danger of the company becoming insolvent and going bankrupt than with listed companies.

**CAUTION** It is not unusual for further calls for capital to be made at short notice after the initial investment. If you fail to comply with such a demand, you may lose all the capital you have invested up to that time. 179

**CAUTION** A change of management in a young company where the personality of the individuals occupying key functions is a particularly important factor can have a highly detrimental effect on a private equity investment. 180

**What do you need to bear in mind when making indirect investments**

With **indirect investments**, there is no guarantee that the manager of a private equity fund will be able to make investments and generate profits that fulfil the expectations for this form of investment. The abilities of the private equity manager are therefore crucial to the success of an indirect investment. 181



## Real Estate

How can you invest in real estate?	Investments in real estate can be made directly or indirectly. Real estate comprises <b>office buildings, retail and industrial premises, residential property and special real estate</b> (such as hotels or hospitals). The variables that determine the value of a property are its location, construction, equipment fittings and the variety of ways in which it can be used.	182
What do you need to bear in mind when making direct investments?	A <b>direct investment</b> involves actually buying property. This will usually require a high capital outlay, a long term investment horizon, in-depth knowledge of the sector, familiarity with the location and often personal involvement, as property needs to be professionally managed.	183
What about indirect investments?	<b>Indirect investments</b> in real estate generally require a lower capital outlay than direct investments. Indirect investments are divided into those that are exchange-listed and those that are not. Examples of unlisted indirect investments include real estate funds, shares of real estate companies that are not listed for trading on an exchange, and certificates on real estate funds. Real estate funds can reduce risk by diversifying across geographical areas and real estate categories. The main category of exchange-listed indirect investments is real estate investment trusts (REITs). These enable investors to invest in real estate without incurring certain disadvantages, such as illiquidity.	184
What risks do you need to be aware of?	Real estate investments are based on physical assets – land and buildings – that are ultimately <b>unique, and in which trading is not regulated</b> .	185
	Where real estate is concerned, it is therefore often <b>difficult, or even impossible, to spread risks adequately or diversify investments sufficiently</b> . With direct real estate investments especially, the high capital outlay required and the illiquidity of the property market makes diversification difficult or even impossible.	186
	Property markets are also frequently <b>intransparent</b> , and require precise knowledge of local circumstances. It is therefore vital to involve local experts, which hampers access to the market.	187
	Real estate often reacts to <b>interest rate changes</b> in a similar way to bonds: when interest rates are low, for instance, mortgages are cheap and it is easy to generate above-average profits. Conversely, high interest rates cause profits to contract. Fiscal incentives offered by the state to promote home ownership and attractive lending conditions can also lead to excessively high prices.	188
What are commodities?	<b>Precious metals and other commodities</b> Commodities are <b>physical goods that are produced via agriculture and mining, for example, and standardised for use as the underlying of a transaction</b> . Derivatives on commodities such as energy sources, precious and other metals, and agricultural products are traded on futures markets.	189
	Contractual agreements allow investors to buy or sell <b>futures</b> linked to the performance of a particular commodity. This means that they can buy a standardised amount of a commodity at a specific time in the future for a specific price.	190

The commonest way in which private individuals invest indirectly in commodities is via structured products (see 107 ff. above). There are other alternatives, such as **commodity swaps and options** that are not listed for trading on an exchange. These are traded directly between the parties concerned and are tailor-made products. More information on how forwards and futures work can be found in a separate section of this brochure (see 86 ff. above). 191

**CAUTION** With commodity futures, you may receive physical delivery of the commodity concerned on expiration, while structured products normally provide for cash payment. If you prefer cash settlement, you will have to sell the futures before their expiration date. Such products are therefore more risky than, for instance, equities or collective investments. 192

**What are the risks of commodity investments?** The price of commodities is influenced by a number of factors. These include: 193

- the relationship between supply and demand
- climate and natural disasters
- state programmes and regulations, national and international events
- state intervention, embargoes and tariffs
- movements in interest and exchange rates
- trading in commodities and the corresponding contracts
- provisions relating to monetary policy, trading, fiscal and currency controls.

These variables can lead to additional investment risks.

Commodities investments are **more volatile than conventional investments**, and yields on commodities can collapse at short notice. The volatility of commodity prices also affects the value, and hence the price, of a futures contract based on those commodities. 194

Conventional futures on oil, base and precious metals are normally easy to trade, regardless of their term.

**CAUTION** When market activity is limited, a contract can become illiquid. Depending on how the yield curve moves, such **illiquidity** can lead to **significant price changes**. This is a typical feature of commodities. 195

## Investments in Emerging Markets

**What are emerging markets?** There is no standard definition of the term “emerging markets”. In the broadest sense it includes **all economies that are not regarded as “advanced”** (see 197 below). Common criteria for defining what is an emerging market are per capita income, the level of development of the financial sector, and the proportion of the total economy that is made up by the service sector. 196

The creditworthiness of countries that fall within this definition can vary widely: from very high to very low, with – in the latter case – very high default risk. Although they can be at very different stages in their economic development, most emerging markets have a political system that is very new (for instance they have only recently become democracies) or is currently changing. This means that the political system and its institutions may be less stable than in an advanced nation.

<b>Which countries are deemed to be “advanced economies”?</b>	The list of emerging markets is changing constantly. According to the criteria applied by the International Monetary Fund in October 2007, they include all countries except: Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Germany, Greece, Hong Kong, Iceland, Ireland, Israel, Italy, Japan, Korea, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Singapore, Slovenia, Spain, Sweden, Switzerland, Taiwan, the UK and the US. These nations are <b>classed as having advanced economies</b> .	197
<b>Which factors should you be especially aware of when making investments in emerging markets?</b>	There are risks linked to investments in emerging markets that are not encountered in their advanced counterparts. This is also the case when the issuer or provider of a product has its headquarters or primary focus of activity in an emerging nation.	198
<b>CAUTION</b>	Investing in products linked to emerging markets is therefore often speculative. Before investing in emerging markets, you should form an impression of them that allows you to assess the risks involved.	199
<b>What are the individual risks involved?</b>	When investing in emerging markets, the following risks should be taken into account. The list is not exhaustive. Depending on the type of investment product, there may be additional risks involved as described elsewhere in this brochure.	200
	<b>Political risk</b> A government’s political inexperience or the instability of the political system increases the risk of short-term, fundamental shifts in a nation’s economy and politics. The consequences for you as an investor can include the confiscation of your assets with no compensation, the restriction of your rights of disposal over your assets, or government-imposed controls. State intervention in specific sectors of industry can result in a dramatic fall in the value of investments in those sectors.	201
	<b>Economic risk</b> Emerging market economies are more sensitive to changes in interest and inflation rates, which are in any case subject to greater swings than in the developed nations. The focus of such economies is often relatively narrow, allowing single events to have a magnified impact. In addition, emerging nations generally have a lower capital base. Finally, their financial markets often lack an adequate structure and sufficient supervision.	202
	<b>Credit risk</b> Investments in debt securities (e.g. bonds, notes) issued by emerging market governments or companies tend to entail higher levels of risk than advanced market debt. This can be due to inferior creditworthiness, a high level of government debt, debt restructuring, a lack of market transparency or a lack of information. It is also much more difficult to assess credit risk due to inconsistent valuation standards and the absence of ratings.	203
	<b>Currency risk</b> The currencies of emerging market nations are subject to unpredictable fluctuations in value that are larger than those of advanced countries. Some countries limit the export of their currency or can impose short-term restrictions, or stop pegging their currency to a reference currency such as the dollar. Hedging can help limit losses resulting from currency swings, but they can never be entirely eliminated.	204

**Inflation risk**

Large fluctuations in the value of the currency and an insufficiently developed financial market can make it difficult for an emerging market nation's central bank to stick to its inflation targets. As a result, inflation may fluctuate more than in advanced countries. 205

**Market risk**

Because there is little or no supervision of financial markets in emerging market nations, regulation, market transparency, liquidity and efficiency are often inadequate. Moreover, high volatility and large price differences are characteristic of these markets. Finally, the inadequacy or absence of regulatory measures gives rise to an increased danger of market manipulation or insider trading. 206

**Market liquidity risk**

Liquidity is dependent on supply and demand. The impact on the emerging markets of social, economic and political changes or natural disasters can involve a much more rapid and lasting change to this supply and demand equation than would be the case in the advanced markets. In an extreme case, illiquidity can be the result. This can make it impossible for an investor to sell his/her investments. 207

**Legal risk**

The absence or inadequacy of financial market supervision can lead to your legal rights being difficult or impossible to enforce. Moreover, legal uncertainty may exist due to the inexperience of the emerging nation's judiciary. 208

**Settlement risk**

Certain emerging markets have an array of different clearing and settlement systems. These are often outmoded and prone to processing errors as well as considerable delays in settlement and delivery. Some countries do not have any such systems at all (see 14 above). 209

**Shareholder risk and creditor risk**

Legislation to protect the rights of shareholders and creditors (e.g. duties of disclosure, insider trading ban, management responsibilities, minority shareholder protection) may often be inadequate or non-existent. 210



# Appendix: Definitions

<b>Advanced market</b>	197 ff.
<b>All-or-nothing option</b>	65
<b>American-style option</b>	24, 43, 46, 75
<b>Asian option</b>	68
<b>Asset-Backed Securities (ABS)</b>	144, 150 ff.
<b>At the money</b>	28 ff.
<b>Average-rate, average-strike option</b>	See Asian option
<b>Barrier Option</b>	60 ff.
<b>Binary option</b>	See Payout option
<b>Call Option</b>	7, 20 f., 26 ff., 37 ff., 48 ff., 72 f.
<b>Capital protection</b>	108, 116 ff.
<b>Cash Settlement</b>	27, 97 ff., 192
<b>Certificate</b>	156, 184
<b>Clearing and Settlement</b>	Exchange of securities for payment between securities traders, in Switzerland through SIS SegInterSettle AG
<b>Cliquet option</b>	77 ff., 79
<b>Closing out</b>	34, 94
<b>Code of conduct for securities dealers</b>	Professional rules of conduct issued by the Swiss Bankers Association for securities dealers (see Securities dealer) in Switzerland, describing their statutory (see Stock Exchange Act) duties of information, due diligence and good faith towards their clients
<b>Collateralized debt obligations (CDO)</b>	144, 147 ff.
<b>Collective Investment Schemes Act</b>	(Swiss) Federal Act on Collective Investment Schemes of 23 June 2006, which entered into force on 1 January 2007 (Classified Compilation of Federal Law 951.31)
<b>Combination</b>	105
<b>Compound option</b>	82 f.
<b>Contingent option</b>	75
<b>Covered option</b>	48 ff.
<b>Credit and catastrophe derivatives</b>	142
<b>Credit default swap (CDS)</b>	Credit derivative whereby one counterparty undertakes to compensate the other counterparty for future credit losses (i.e. take on credit risks) in return for a premium 147
<b>Credit-linked notes (CLN)</b>	144, 145 f.
<b>Credit risk</b>	84, 147, 203
<b>Creditor risk</b>	210
<b>Currency risk</b>	204
<b>Derivative</b>	Financial contract for which the price is derived either from assets such as equities, bonds, commodities or precious metals, or from benchmarks such as currencies, interest rates and indices 3 ff., 16, 23, 49
<b>Digital option</b>	See Payout option
<b>Double-barrier option</b>	See Barrier option
<b>Economic risk</b>	202
<b>Emerging market</b>	17, 159, 168, 196 ff.
<b>European-style option</b>	25, 75

<b>Exotic option</b>	55, 58 f.
<b>Expiration date</b>	20 f.
<b>Financial instrument</b>	Generic term for all securities, book-entry securities and derivatives, including those that are not standardised and suitable for mass trading (on standardised securities suitable for mass trading, see Security)
<b>Force majeure</b>	Events neither party in a transaction can influence or be held liable for, such as natural or man-made disasters, armed conflicts, terrorist attacks, uprisings, employment disputes (strikes and lockouts), embargoes, etc.
<b>Hedge fund</b>	159 ff.
<b>Hedge fund strategies</b>	164 ff.
<b>In the money</b>	28, 37, 67, 76
<b>Indirect investments</b>	156
<b>IPO (Initial public offering)</b>	The first sale of previously unlisted shares by a company to the public, commonly known as “going public” (as distinct from issuance) 176
<b>Issuance</b>	Creation and placement of securities in the primary market (as distinct from “Initial public offering [IPO]”) 113, 116, 120 f.
<b>Issuer</b>	5, 12, 107, 110 ff., 114, 132, 146, 152, 198
<b>Issuer risk</b>	111, 146, 152
<b>Kick-in, kick-out barrier option</b>	See Barrier option
<b>Knock-in, knock-out barrier option</b>	See Barrier option
<b>Ladder option</b>	77 ff.
<b>Legal risk</b>	208
<b>Leverage effect</b>	Enhanced exposure to losses and gains due to price changes 22, 135, 159
<b>Lock-in, lock-out option</b>	See Payout option
<b>Lock-up period</b>	161
<b>Lookback option</b>	71 ff.
<b>Margin, margin cover, variation margin, margin requirement</b>	35 ff., 44, 47, 91 ff., 100 f.
<b>Market liquidity risk</b>	207
<b>Market maker</b>	A securities dealer (see Securities dealer) who undertakes, either permanently or on request, to maintain firm bid and offer prices for one or more financial instruments (see Financial instrument)
<b>Market risk</b>	114, 206
<b>Mortgage-backed securities (MBS)</b>	150
<b>Nominal Value</b>	Face value or par value
<b>Non-traditional investments, non-traditional funds</b>	153 ff.
<b>Off-exchange trading</b>	See OTC trading
<b>Offshore investments</b>	Investments (often in form of funds or limited liability partnerships) domiciled in countries where they are subject to a comparably weaker legislation and supervision 157 f.
<b>One-Touch digital option</b>	65
<b>On-exchange trading</b>	Trading, especially with securities and rights not embodied in a certificate but with similar functions (book-entry securities; see Securities) on an organised, regulated market (the “secondary market”), as opposed to issuance (which takes place on the “primary market”; see Issuance)

<b>Option</b>	4 ff., 20 ff.
<b>OTC</b>	Trading with securities which are not traded on a stock exchange, are agreed on an individual basis and not standardised
<b>OTC (over-the-counter) forward</b>	89, 104
<b>OTC option</b>	34, 55
<b>Out of the money</b>	29
<b>Outperformance option</b>	80
<b>Participation component</b>	118 f., 123 f.
<b>Path-dependent option</b>	58 ff.
<b>Payout option</b>	64 ff.
<b>Physical settlement, physical delivery</b>	26, 41, 46, 51, 84
<b>Plain vanilla option</b>	55 f., 59
<b>Political risk</b>	201
<b>Price-lookback, strike-lookback option</b>	See Lookback option
<b>Private equity</b>	174 ff.
<b>Put option</b>	7, 20 f., 26, 28 f., 37 f., 45 f., 55, 72 f.
<b>Ratchet option</b>	See Cliquet option
<b>Real estate investment trust (REIT)</b>	184
<b>Securities dealer</b>	Natural person or legal entity that offers new securities (see Security) publicly on the primary market on a professional basis, and/or trades securities on the secondary market or creates derivatives (see Derivative) which it offers publicly. 1, 5, 8, 10 f., 15, 17, 19, 35 f., 54, 92, 105
<b>Security</b>	Standardised certificate which is suitable for mass trading, as well as rights not embodied in a certificate but with similar functions (book-entry securities). They include equities, bonds, units of investment funds and derivatives (see also Derivative), and must be offered to the public in a standardised form and denomination, or sold to more than 20 buyers 1, 2, 5, 13
<b>Settlement risk</b>	14, 209
<b>Shareholder risk</b>	12, 210
<b>Short put option</b>	Sale of a put option whereby the seller (writer) undertakes to buy the underlying at the strike price on the strike date
<b>Short selling</b>	91, 103, 165
<b>Spread option</b>	80
<b>Stock Exchange Act</b>	(Swiss) Federal Act on Stock Exchanges and Securities Trading of 24 March 1995, which entered into force on 1 February 1997, with subsequent amendments (Classified Compilation of Federal Law 954.1) 1, 8, 17
<b>Strike price</b>	20 f., 27 ff., 40 ff., 45 ff., 51 ff., 61, 68 ff.
<b>Structured product</b>	107 ff.
<b>Swap</b>	Contract for the exchange of payment streams; not traded on-exchange or en masse. See OTC 142, 147, 171 f.
<b>Time value</b>	31, 38
<b>Traded option</b>	33, 35
<b>Underlying, underlying asset</b>	The asset on which a derivative financial instrument is based. Examples include interest rates, equities, bills, etc. Increasingly, derivatives are also traded on alternative underlyings such as catastrophe risks and weather as well as credit risks, although these underlyings are not traded assets in their own right. 3, 20 ff., 26 ff., 59 ff., 80, 86 f., 96 ff., 107 ff.



**Volatility** Range within which a price or rate is expected to fluctuate  
31, 206

**Warrant** 32, 55

**Writer (of an option)** Seller (of an option)  
21, 26, 40 f., 45 f.

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## Tips to avoid dormancy

### CHANGE OF NAME AND ADDRESS

Please inform your bank immediately if you change your address, or if you use a different name, e.g. following marriage.

### SPECIAL INSTRUCTIONS

Inform your bank if you go away for an extended period of time and arrange for correspondence from your bank to be sent to a third party or kept at the bank during your absence.

### DESIGNATING A PROXY

It is generally advisable to designate a proxy or representative with full power of attorney who can be contacted by your bank should your assets become “dormant”.

### INFORMING TRUSTED PERSONS / YOUR WILL

Another possibility to avoid dormant assets is to inform a trusted person about your bank details. The bank can only give information to such a person if you have first authorised him or her in writing to act on your behalf. You could also list your assets and the name of the respective bank(s) where they are deposited in your will.

### INDIVIDUAL ADVICE

Your bank would be pleased to advise you individually and to help where possible.

## Measures that banks can take in cases of dormancy

The Board of Directors of the Swiss Bankers Association has drawn up the following professional rules that Swiss banks are to follow in cases of dormant customer relations:

### IMMEDIATE MEASURES

As soon as a bank determines that mail sent by post to a customer cannot be delivered e.g. because of a change of address, then the bank will attempt with due diligence to discover the new address. The bank can appoint third parties to investigate. Such third parties are of course subject to the same laws concerning confidentiality as the bank itself. Bank customer confidentiality is thereby preserved. The bank is also to follow special or other customer instructions within the framework of legislation and professional rules.

### MEASURES TO BE TAKEN WHEN DORMANCY IS ESTABLISHED

If the inquiries by the bank are unsuccessful or contact with the customer is not possible for other reasons, then the Swiss banks are bound by the professional rules laid down by the Swiss Bankers Association to proceed as follows:

- register the customer’s assets centrally,
- specially earmark the assets in order to report them to the Central Claims Office. This office, which is equipped with modern security measures, is subject to the same banking confidentiality (bank customer confidentiality) laws as the banks themselves.

## Continued rights in cases of dormancy

The customer’s rights remain intact even in the case of dormancy. Banks may only take action that diverges from the contractual agreement with the customer when such action is in the customer’s assumed interest. So, for example, current accounts and similar assets can be transferred to low-risk instruments such as savings accounts, medium-term notes or unit trusts. Savings accounts will be continued as usual and interest paid at the bank’s valid rates. Commissions to administer assets are to be continued unaltered unless it becomes obvious that the investment aims are in conflict with the customer’s interests.

For further details please contact your bank.

### COSTS

The bank’s usual debited costs and expenses also apply in cases of dormancy. Furthermore, the banks can charge the customer for costs incurred for their inquiries as well as for the special handling and supervision of dormant assets. The extent of the bank’s inquiries must be guided by the principles of proportion and in particular be reasonable with the value of the assets in question.

**Dear Customer,**

Every now and again contact between a bank and a customer can become lost for one reason or another and as a result assets deposited with the bank become “dormant”.

This can lead to difficulties and an undesirable situation for all concerned, especially when the assets are totally forgotten about by customers and their heirs.

To help prevent the problem of dormant assets from arising, the Swiss Bankers Association, in conjunction with Swiss banks, has produced this present leaflet containing tips and advice for bank customers.

Swiss Bankers Association

Basel, February 2000



February 2000

# Information for Customers of Swiss Banks Concerning the Avoidance of Dormant Assets

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June 2009

# Information from the SBA regarding the disclosure of client details in payment transactions, securities transactions and other transaction types in connection with SWIFT

Swiss Bankers Association (SBA)

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## Information from the SBA regarding the disclosure of client details in payment transactions, securities transactions and other transaction types in connection with SWIFT

Banks primarily use the services of SWIFT for payment transactions and the processing of securities transactions. At present, there is no other company that offers such services worldwide. Below we answer the questions that are posed to us most frequently with regard to SWIFT and the risks connected with disclosing data abroad.

### What is SWIFT?

S.W.I.F.T. stands for "Society for Worldwide Interbank Financial Telecommunication". It is a cooperative headquartered in Belgium and its members are made up of banks from numerous countries. SWIFT standardises the exchange of messages between financial institutions, i.e. the transmission of information between financial institutions, in connection with payment transactions and securities transactions, for example. The main participants in the message transmission system are banks, brokers, asset managers and national and international central securities depositories. SWIFT has very high standards with regard to data security and uses a secured network, which sends messages in an encrypted form, for the transmission of information. You can find more information about SWIFT on its homepage at [www.swift.com](http://www.swift.com).

### How does SWIFT work?

In order to demonstrate how SWIFT works, we will use the following example: If you authorise your bank to send EUR 500 to a friend in Italy, the bank enters the order in an electronic form known as a SWIFT message, which is provided by SWIFT. The bank debits EUR 500 to your account and sends the SWIFT message via SWIFT to your friend's bank in Italy. The encrypted SWIFT message informs your friend's bank that there is a transfer order for him and that the equivalent of EUR 500 should be debited to the offset account that your bank has with this particular receiving bank and credited to your friend. **Please note: SWIFT only exchanges encrypted messages. No funds are exchanged via SWIFT.**

### What does SWIFT do with your data?

In addition to its message transfer network, SWIFT currently also operates two computer centres for data processing, in the US and the Netherlands, with a further centre in the pipeline for Switzerland. At these computer centres, the messages within the SWIFT network are encrypted, checked to ensure they have the correct structure, uniquely referenced, stored in a cache and inspected for alterations. The data is processed in one computer centre and saved at a second for security reasons (backup). The storage period at SWIFT is a maximum of 124 days. During this time, the messages are saved at both computer centres. Following this period, the messages are deleted from all databases at all locations. The information is stored for reasons of operational security, in case a financial institution requests that SWIFT reproduce messages. From the end of 2009 SWIFT will make available a facility which will allow participants to store data about

transactions in Europe not only at a computer centre in the Netherlands but also at one in Switzerland.

## Disclosure of data

### What does this mean for your payment transactions?

For the processing of domestic and cross-border **payments**, information about the ordering customer is disclosed to the banks and system operators involved in Switzerland and abroad. This information is required primarily under the applicable provisions for the combating of money laundering and financing of terrorism. The main information provided includes the name, address and account or identification number of the ordering customer although date of birth and place of birth may be provided in place of the address. In the case of domestic payment transactions, this information may be omitted, with the exception of the account or identification number, although it must be forwarded to the beneficiary's bank within three working days if it is requested. The banks and system operators in question are primarily correspondent banks of the bank issuing the payment, payment system providers (e.g. SIX Interbank Clearing AG in Switzerland) or SWIFT. It is also possible that the parties involved in the transaction may pass on the data, for processing or data backup to mandated third parties in other countries for instance. Furthermore, details about the ordering customer are provided to the beneficiary in Switzerland or abroad.

For **domestic payments in foreign currencies**, information on the person issuing the order is also disclosed to the banks and system operators abroad which are involved in the transaction. In the case of **domestic payments in Swiss francs**, it can also not be ruled out that information on the person issuing the payment will be sent abroad. This can occur, for example, if a bank is connected indirectly to the Swiss interbank payment system ("SIC") via remoteGate rather than having a direct connection or if SWIFT is used to make clarifications regarding a transaction.

### What does it mean if a bank is connected to SIC via remoteGate?

Domestic payments in Swiss francs are processed via SIC. This payment system is operated by SIX Interbank Clearing AG by mandate of the Swiss National Bank. Most financial institutions in Switzerland have direct access to SIC. However, there are some banks in Switzerland that execute only a few domestic transactions in Swiss francs, meaning that a connection to SIC would be relatively expensive. In 2000, banks such as these and institutions abroad were given the option of accessing SIC via SWIFT when SIX Interbank Clearing AG, commissioned and supported by the Swiss National Bank, developed remoteGate. When accessing SIC via SWIFT, data on the principal and the beneficiary are sent abroad and saved in SWIFT's computer centres. This is the case with banks that use remoteGate. However, it is not only the clients of banks that use remoteGate who are affected by the transfer of information abroad. Clients of banks which execute transactions with the users of remoteGate are also affected. If a bank that uses SIC sends a payment order to a bank that is connected to SIC via remoteGate, the payment order is transferred from SIC to the SWIFT system, meaning that data on the principal and the beneficiary is sent abroad.



## What does this mean for securities transactions?

For the **processing of domestic and cross-border securities transactions and inquires in connection with such transactions**, there are *two main areas* which involve the disclosure of data to the banks and central depositories involved in Switzerland and abroad.

For **deliveries and withdrawals of securities to and from custody accounts and custody account transfers**, the *custody account number, the name and the address* of the end beneficiary in Switzerland may be sent abroad when this data is transmitted via SWIFT by the involved banks and central depositories to ensure orderly processing.

Furthermore, for **securities held abroad** on behalf of bank clients, the *name of the securities holder* or the *name of the registered shareholder*, and in some cases address details, are included in SWIFT messages. These SWIFT messages affect, for example, special transactions of the foreign depositories of Swiss banks, such as the opening of special custody accounts (in the name of the client), subscriptions and redemptions of foreign funds made in the name of the client, physical transfers of a client's special holdings held abroad, the entry and re-registration of shareholders in foreign registers and other special cases involving foreign capital transactions and the exercise of voting rights.

## What does this mean for other transactions?

For **other transactions** such as documentary credits, guarantees, collections and foreign exchange transactions, all details on the transaction in question (e.g. names, addresses and account numbers of the parties involved in the transaction) are communicated to the banks and system operators involved via SWIFT and are therefore communicated abroad. As is the case with payment transactions and securities transactions, inquiries regarding transactions may also be made via SWIFT.

## Why is data disclosed?

The information discussed above is disclosed in order to fulfil statutory and regulatory requirements in Switzerland and abroad. For example, in the case of cross-border payments, data on the ordering customer must be provided. The provision of this information also enables the orderly, efficient processing of transactions.

## Are your details abroad protected?

Data sent abroad is no longer protected by Swiss law and is subject to the respective foreign legal system. Foreign laws and regulations may require that this data be passed on to authorities or other third parties, for instance. This was the case in 2001 when the US Treasury required the release of data from the SWIFT computer centre in the US following the terrorist attacks on the World Trade Center in New York. The US Treasury assured the EU authorities that it would adhere to European data protection standards and agreed to the relevant controls.