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Note from the Editors

The new Swiss Financial Services Act (FinSA) and Financial Institutions Act (FinIA) were enacted by the Swiss Parliament in June 2018, and are currently expected to enter into effect on 1 January 2020. While the FinSA introduces uniform prospectus rules generally applicable to all offerings of securities in Switzerland and comprehensive rules of conduct for providers rendering financial services in Switzerland, the FinIA introduces the prudential supervision of all financial services providers operating a portfolio or asset management business in Switzerland and uniform licensing requirements for financial intermediaries other than banks and insurance companies. With drafts of the implementing ordinances to the FinSA and FinIA having just been published, we deem it the right time to provide you with an update on this new legislation and a first assessment of the draft implementing provisions.

The editors.

The New Swiss Prospectus Regime

Reference: CapLaw-2018-56

In June 2018 the Swiss Federal Parliament passed the Financial Services Act and the Financial Institutions Act, and on 23 October 2018 the Swiss Federal Council presented the ordinances implementing these acts for public consultation until early February 2019. It is expected that the acts and its ordinances will become effective on 1 January 2020. Modeled largely after the EU prospectus framework, the new prospectus regime marks a veritable paradigm change to Swiss capital market regulation, introducing a number of novelties for issuers of securities in the Swiss market, such as the requirement for an ex ante approval for most financial instruments, coupled with some important long-awaited explicit exemptions from such requirement and the requirement for a prospectus for secondary public offerings.

By Christian Rehm / René Bösch

1) The Proposed Revision of the Swiss Prospectus Regime

On 15 June 2018, after almost 2 ½ years of deliberation the Swiss Parliament enacted the Financial Services Act (FinSA) and the Financial Institutions Act (FIA). The FinSA sets forth the new prerequisites for providing financial services, as well as requirements applicable to offerings of financial instruments. As far as the rules on the offerings of financial instruments are concerned, the FinSA introduces a number of fundamental changes to the Swiss prospectus regime. Most notably, a requirement for an *ex ante* approval of prospectuses, the long-awaited codification of private placement exemptions in line with international standards and a duty to publish a prospectus in the case of secondary public offerings.

The draft Ordinance on Financial Services published on 23 October 2018 for public consultation (Draft-FinSO) specifies several details of how the principles set out in FinSA shall be implemented. While it is still in draft form, at a minimum the part in the Draft-FinSO governing the new prospectus regime is expected to not receive significant contradictory comments and, therefore, to be in near final form.

2) Duty to Publish an Approved Prospectus

a) New Approval Requirement

The existing Swiss prospectus regime requires the publication of a rather short offering prospectus in the case of primary public offerings, but not for secondary offerings, and of a listing prospectus which is in line with international standards in the case of a listing on a Swiss stock exchange. It does not currently require offering prospectuses to be filed with, or approved by, any Swiss governmental or other authority or body. Only in the case of a listing of financial instruments in Switzerland, *e.g.*, on the SIX Swiss Exchange Ltd. (SIX), is such an approval required by the relevant stock exchange as the competent self-regulatory body.

The FinSA introduces an approval requirement for offering prospectuses by a new regulatory body, the so-called approval authority or reviewing body. This body, while still a private body, must be licensed by the Swiss Financial Supervisory Authority FINMA and will be vested with administrative powers. It is expected in the Swiss market that the SIX and BX Swiss will apply to be appointed as approval authorities. Once licensed these approval bodies will be the sole competent bodies to approve prospectuses under the FinSA regime. Admissions of new issues to market places, however, will be continue to be governed by the admissions bodies of the relevant market places. But the new framework should assure that such admission bodies have to accept an approved prospectus under FinSA without setting up its own additional disclosure requirements, aside from technical aspects relevant to the specific market place. It is further expected that Swiss market places will amend their rules such that the approval and admission-to-trading process can run in parallel and be coordinated.

This prospectus and approval requirement will apply to all public offerings, primary and secondary, in Switzerland and, independently, to all securities that are to be admitted to trading on a trading platform in Switzerland. Securities that are at the time publicly offered or are the subject of a request for admission to trading, in each case filed prior to the entry into effect of the FinSA, will benefit from a transitional period. The Draft-FinSO now proposes that the duty to prepare a prospectus under the authority of FinSA comes into effect 6 months after the first approval authority is licensed. Such licensing is expected to occur as of 1 January 2020; accordingly, the new approval requirement is expected to be fully in place as from 1 July 2020 onwards.

b) Ex Ante Approval and Exemptions

In principle, the approval authority will have to approve the prospectus *prior* to a public offering or an admission of securities to trading on a trading platform in Switzerland. First-time issuers (*i.e.*, issuers who either have not yet published a prospectus approved by the approval authority or do not have securities admitted on a Swiss trading platform) will be required to submit the prospectus for approval at least 20 calendar days prior to commencement of the envisaged offering or admission to trading, all other issuers at least 10 calendar days. These are the periods within which the approval authority would have to state that the prospectus is approved or that the prospectus has to be revised, in which case the applicable period for approval would start anew after re-submission. Yet, if the approval authority does not react within the required period, this does not mean that the prospectus is automatically deemed approved.

However, other than the European bond markets which are to a large extent wholesale markets targeted at institutional clients, the Swiss fixed income market is largely a retail market with standard denominations of CHF 5,000. This would mean that in a system requiring the pre-approval of prospectuses, bond issuers would always have to prepare a full-fledged prospectus prior to listing, in particular as for many issuers the Swiss market is not deep enough to warrant the preparation of a program documentation. This dilemma between having to obtain a pre-approval on the one hand and the issuers' need to be able to very quickly access the markets on the other hand has in the past been solved by the SIX by allowing the provisional admission to trading before the formal listing approval is obtained, but only for fixed income and structured products. Acknowledging the relevance of this practice for the Swiss market, FinSA now introduces an exception to the rule of *ex ante* approval for certain securities to be specified in the implementing ordinance. The Draft-FinSO names straight bonds, convertible and exchangeable bonds, bonds with warrants attached, mandatory convertible notes, contingent convertible notes (CoCos) and write-down bonds as such exempt securities, and structured products with a duration of 30 or more days.

Where this exemption applies, issuers must nonetheless ensure that a prospectus whose contents conform to the requirements of the FinSA is available and published no later than the day on which the public offering commences or admission to trading is applied for. The review and approval of such a prospectus by the approval authority will, however, only take place *ex post* (*i.e.*, after the offering has been completed or after the admission to trading) rather than *ex ante*. But to benefit from this exemption from the *ex ante* approval requirement, a Swiss bank or broker dealer will have to *confirm* in writing to the issuer / offeror that the most important information about the issuer and the relevant securities is available at the time the prospectus is published. Such prospectuses made available on the offering date or date of admission to trading will be required to contain a statement that it has not yet been approved by an approval authority.

c) Automatic Approval of Certain Non-Swiss Prospectuses

Another important feature of the FinSA is that foreign prospectuses qualify for approval by the approval authority if they are drafted according to standards of the International Organization of Securities Commissions (IOSCO) and the disclosure and ongoing reporting duties are equivalent to those of the FinSA. Prospectuses that have been approved in accordance with certain foreign standards to be specified by the approval authority will be automatically deemed approved.

A foreign prospectus automatically deemed approved must be published no later than at the time of commencement of the public offering or admission to trading and be deposited with the approval authority.

d) Publication and Validity of Prospectuses

In case of an initial public offering of equity securities, the approved prospectus must be published at least six business days prior to the end of the subscription period. This introduces a new statutory requirement for the length of the subscription period and will make discussions in the Swiss equity markets about the minimum duration of the subscription period obsolete. For the offering of non-equity securities, the approved prospectus must be published prior to the start of the public offering or before the admission of the security to trading. The publication may be made by electronic means only (*e.g.*, on the website of the issuer or guarantor or of the approval authority), but, in such case, the prospectus must also be made available free of charge in printed form upon request.

Once approved, the prospectus is valid for 12 months for purposes of a public offering in Switzerland and/or admission to trading on a Swiss trading platform, subject to the duty to update in case of material new developments (see below).

3) Contents of the Prospectus

Prospectuses must be prepared in an official language of Switzerland or in English. As to their contents, the FinSA only states the golden rule of prospectus drafting, *i.e.* that the prospectus must contain all information material for the investment decision of an investor, and lists some specific items with respect to the issuer and, if applicable, the guarantor, the securities, and the offering. The prospectus will also have to include a summary that contains the important information, presented in an easily comprehensible way. If benefiting from an exemption from the *ex ante* approval requirement, the prospectus must include the relevant disclaimer (see above).

The details of the required content of a prospectus are set out in annexes to the Draft-FinSO, as schemes for several classes of securities. As currently drafted the schemes are based on the well-established SIX regulations with some additional requirements as well as helpful clarifications. The schemes denote also where seasoned frequent issuers (issuers of equity securities included in a leading Swiss index or issuers having outstanding debt instruments in a principal amount of at least CHF 1 billion) benefit from alleviations.

The FinSA explicitly permits a prospectus to incorporate certain information by reference. Such incorporation by reference is not permissible in the summary, and is only possible for documents published prior to, or concurrently with, the prospectus; so-called forward incorporation is thus not possible. Apart from these limitations, the Draft-FinSO will allow incorporation by reference as much as possible. Incorporation by reference not only serves the interests of issuers, but also those of investors by precisely referencing the relevant information without unnecessary duplication.

In case of new developments that occur prior to the end of the subscription period or, for an admission to trading, prior to the start of trading on the relevant trading platform, if likely to materially affect the price of the securities, a supplement to the prospectus must be prepared and published. This supplement must also be approved by the approval authority prior to its publication within a maximum of seven calendar days. The approval authority is required to publish and maintain a list of events, the occurrence of which would generally *not* trigger an approval requirement, but simply a duty to publish a supplement to the prospectus.

4) Exemptions from the Duty to Publish a Prospectus

The FinSA introduces a set of explicit exemptions from the prospectus requirement largely in line with the Prospectus Directive and the Prospectus Regulation of the European Union and existing SIX regulations. Also, the Swiss National Bank, the Bank for International Settlements (BIS) and regulated insurance companies are generally exempted from the FinSA. For insurance companies this exemption may make sense as far as their activities are separately regulated or they are offering regulated insurance products; however, own capital market activities of insurance companies are in our view subject to the primary capital market rules of the FinSA.

a) Type of Offering

The list of exempted transactions includes, *inter alia*, public offerings limited to professional clients (*e.g.*, financial intermediaries within the meaning of the banking act, the financial institutions act (including asset managers) and the collective investment schemes act, insurance companies, companies with a professional treasury and investment vehicles for wealthy private clients which to have a professional treasury (likely to be family offices)), offerings addressed to less than 500 (non-professional) investors, and offerings with a minimum investment of CHF 100,000 or of securities with a denomination of at least CHF 100,000. Finally, offerings of less than CHF 8 million over a period of twelve months are exempted. While these exemptions largely mirror the new European Prospectus Regulation, including in particular the recently increased offering limit of CHF 8 million, the Swiss Parliament deviated from the EU regulation when in the final legislative efforts it increased the private clients exemption from 150 to 500 investors.

b) Type of Security

The public offering of certain types of securities may – subject to certain conditions – also be made without an approved prospectus. For example, the following transactions can all be made without an approved prospectus: the exchange of outstanding equity securities for equity securities of the same class, the delivery of equity securities following a conversion of debt instruments of the same issuer or any of its affiliates, the offering of securities to executives or employees, and the offering of money market instruments (including in particular commercial paper). For employee offerings the FinSA is more liberal than the European Prospectus Regulation in that it no longer requires that "details of the offer" be provided; while this requirement was still contained in the draft FinSA, the parliament acknowledged that this would have created substantial legal uncertainty.

c) Exemptions for Admission to Trading

There are also exemptions from the prospectus requirement in the case of admission to trading without a concurrent public offering in Switzerland. For example, starting on the basis of the current listing rules of the SIX but then going beyond, the admission to trading of securities that, calculated over a 12-month period, account for less than twenty (currently ten) percent of the equity securities of the same class that are already admitted to trading on the same trading platform, can be made without a new prospectus. This increase in percentage mirrors the new European Prospectus Regulation.

Most notably, the FinSA also continues the SIX practice (*e.g.*, regarding the Sponsored Segment of the SIX) of exempting securities that are already traded on a foreign trading platform that is either deemed eligible by the trading platform or where the transparency for investors is otherwise safeguarded from the prospectus requirement. The FinSA also introduces a new prospectus exemption for admission to trading on trading segments that are only open to professional clients.

By contrast to the European Prospectus Regulation, which contains a number of exemptions for admission to trading verbatim mirroring the offering exemptions, this technical duplication is missing in the FinSA. But in the final deliberations a provision has been introduced to clarify that these exemptions shall apply *mutatis mutandis* for the admission to trading.

d) Further Alleviations and Abridgment Options

The Draft-FinSO will provide for additional alleviations and abridgment options from the prescribed prospectus content for well-known seasoned issuers. It seems that for technical reasons within the government the published draft did not reflect the proposals of the expert group for such alleviations and abridgment options, but the government has assured that these proposals should largely be acceptable and be reflected in the final version of the Draft-FinSO.

e) Information outside of the Duty to Publish a Prospectus

The FinSA requires that if an offer is exempt from the duty to publish a prospectus the issuer or offeror must treat all investors equally if they provide relevant information to investors in connection with such offering.

f) Carve-out of Privately Placed Debt in the Banking Act

While the FinSA would allow non-regulated issuers to privately place debt to more than 20 offerees, such private placement would currently be considered deposit taking under the Banking Act triggering the requirement to obtain a banking license. To address this problem, the Draft-FinSO proposes that the Banking Ordinance be amended to specify that if the offeror prepares a basic information document no such licensing issues arise. This proposal is flawed and to be rejected because it is overly broad and would introduce the duty for all Swiss offerors of bonds to prepare such basic information document for all bonds while the regulation of the basic information document itself specifically exempts bonds from this duty.

5) Basic Information Document

The dispatch of the Federal Council required that whenever a financial instrument other than shares (or comparable equity securities) was offered to private clients, a so-called basic information document containing all information material for the client's investment decision, presented in an easily comprehensible way and designed to make financial instruments easier to compare, had to be prepared.

However, while such basic information document may be appropriate for short-term financial investment products, and in particular structured products, the document would not really be well-suited for debt offerings. Taking into account the wide criticism this proposal has drawn in the public hearing process, parliament has considerably limited this requirement; the FINSA now excludes debt instruments without derivative elements from the requirement of having to prepare a basic information document. The Draft-FinSO proposes to exempt, *inter alia*, the following securities from the basic information document: convertible bonds, provided they are convertible into shares of the issuer or an affiliate within the same group, subscription rights in a rights offering, employee options, dividends in kind, floating rate bonds to the extent referring to benchmarks, inflation protection bonds, bonds with call and early redemption features, and zero coupon bonds. With this enumeration the Swiss legislator follows a much more flexible approach than the EU under the PRIPPs Regulation.

The Draft-FinSO contains the specific details for the format and contents for such basic information document. While generally the Draft-FinSO follows the requirements for Key Investor Documents (KIDs) under the EU PRIIP Regulation, it contains helpful alleviations and more flexible standards. But FinSA also stipulates that instead of preparing a basic information document under the FinSA, one may also use a KID.

6) Prospectus Liability

Notwithstanding the new prospectus approval requirement, the prospectus liability regime applicable to anyone participating in the drafting of the prospectus that is currently provided for in Swiss civil law will continue to exist. Consequently, a person responsible for drafting or contributing to a prospectus may incur liability for false or misleading information contained in the prospectus or if the prospectus does not fulfill the legal disclosure requirements.

While the draft FinSA, as proposed by the Federal Council, required prospectus drafters to prove that they did neither act intentionally nor negligently, parliament did not adopt this reversal of the burden of proof, acknowledging that this would have constituted a novelty in Swiss law and in particular would have required defendants to prove the non-existence of certain facts, a proof that would have been extremely difficult to establish in practice. Consequently, the FinSA in our view retains the existing proven liability regime and in particular does not introduce the fraud-on-the-market theory, which would have assumed reliance on the prospectus by the investors when making the investment decision

While a prospectus will need to include forward-looking statements, liability for such statements is rightfully limited. Wrong or misleading forward-looking statements can only lead to prospectus liability if they are made against better knowledge or made without including a disclaimer that future developments are subject to uncertainty (similar to the bespeaks caution doctrine in the U.S.). Summaries can only lead to liability if they are still incorrect or misleading if read together with, or inconsistent with, the rest of the prospectus.

7) Criminal Liability

The FinSA also introduces criminal liability in the case of an intentional violation of the Swiss prospectus rules. While a similar provision can be found in the Swiss Federal Act on Collective Investment Schemes, this concept not only is at odds with traditional Swiss law concepts but also jeopardizes the overarching goal of introducing an attractive and competitive primary capital markets regime by ultimately discouraging issuers from using the Swiss markets for fear of criminal liability. Given that capital markets are extremely agile markets, adding criminal liability puts the Swiss market at a certain disadvantage, in particular as the European prospectus regulation does not provide for a similar criminal liability.

Also, the newly introduced criminal liability is unfortunately not really well-drafted. While the clause clearly states that only *material* omissions may trigger criminal sanctions, the wording is less clear for misstatements, and would theoretically allow that even minor misstatements could be sanctioned. Yet, in our view, the same standards must apply to misstatements and omissions, i.e. only *material* misstatements and only *material* omissions can be the subject of criminal sanctions.

8) Appraisal

Aside from the introduction of criminal liability for intentional non-compliance with Swiss prospectus rules, the FinSA introduces a modern and practical prospectus regime in Switzerland that in our assessment is largely compatible with the EU prospectus regime and other international standards.

In our view, by taking the Prospectus Directive and its exemptions as a model, by accepting that established Swiss practice should continue, and by giving regard to the needs of both small and medium-sized issuers as well as large well-known seasoned issuers, the proposed regime will not introduce major obstacles for Swiss and foreign issuers. Rather, it will enhance transparency for investors and create more legal certainty for issuers.

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The New Reviewing Body

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The Financial Services Act establishes a new prospectus regime in Switzerland requiring the publication of a prospectus for public offerings of securities and the admission to trading on a trading venue. It introduces a new regulatory body – the reviewing body (*Prüfstelle*) – to be authorized by FINMA and responsible for review and approval of prospectuses.

This article discusses the setup and operation of such reviewing body, the prospectus requirements and content as well as the review and approval of the prospectus.

By Sabir Sheikh / Peter Probst

1) Introduction

On 15 June 2018, the Swiss Parliament adopted two new laws: the Financial Services Act (FinSA) and the Financial Institutions Act (FinIA). The FinSA introduces, amongst others, a new prospectus regime in Switzerland that demands the publication of a prospectus for (i) any public offering of securities in Switzerland and (ii) admission to trading of securities on a trading venue in Switzerland. Such prospectus needs to be reviewed and approved by a new regulatory body, the so-called reviewing body (*Prüfstelle*). On 24 October 2018, the Swiss Federal Council initiated the consultation on the Financial Services Ordinance (Draft-FinSO), the Financial Institutions Ordinance (Draft-FinIO) and the Supervisory Organization Ordinance (Draft-SOO) outlining the implementing provisions for both the FinSA and the FinIA. The consultation procedure ends on 6 February 2019. It is expected that the two acts together with the ordinances will enter into force on 1 January 2020.

2) The Reviewing Body

The FinSA introduces a new regulatory body, the reviewing body (*Prüfstelle*), to be authorized by FINMA and responsible for the review and approval of the prospectuses pursuant to article 35 et seq. FinSA. Unlike the member states of the EU, where public authorities act as reviewing bodies, the Swiss approach provides for a private entity. FINMA may authorize more than one reviewing body provided this is objectively justified. If there is no private entity available as reviewing body, the Swiss Federal Council may designate a body for this task (article 52 (1) and (5) FinSA).

In order to become a reviewing body, the interested party will have to file an application with FINMA containing information about the place of actual management, internal organization, business management, planned controls of activities, the persons charged with the management and the delegation of functions to third parties (article 52(1) FinSA, article 71 Draft-FinSO). Both the reviewing body and the persons charged with management must provide guarantee of fit and proper business conduct. The persons charged with the management must enjoy a good reputation and must have the specialist qualifications required for their function (article 52(3) FinSA). To the extent necessary for the evaluation of the application FINMA may request further information (article 71(3) Draft-FinSO). Based on its general supervisory competence pursuant to the Financial Market Supervisory Authority Act (FINMASA) FINMA may also request a statement of an independent and competent person with regard to certain organizational aspects, especially with regard to the use of information technology; the costs of such mandated person will have to be borne by the reviewing body (cf. Explanatory report on the consultation on the FinSO, the FinIO and the SOO (Explanatory Report FinSO/FinIO/SOO), p. 53).

The cost for the application process will have to be borne by the applying reviewing body (article 76 Draft-FinSO).

The reviewing body must be domiciled in and actually managed out of Switzerland. Should the reviewing body not be a legal entity itself but part of a legal entity, such legal entity will have to fulfil such requirements (article 73 Draft-FinSO). The FinSA further provides that the reviewing body must guarantee the independent fulfilment of its tasks (article 52(2) FinSA). For that purpose its organizational structure must (a) be set out in organizational regulations, (b) ensure that its personnel has the specialist qualifications required for their function, (c) dispose of an internal control system and ensure that the applicable laws and regulatory requirements will be met and (d) ensure that conflicts of interests – especially with other profitable business units – are avoided (article 74(2) Draft-FinSO). Conflicts of interest may be avoided by the introduction of disclosure and abstention rules. If the reviewing body is part of an existing legal entity, the persons charged with its management need to be functionally and hierarchically separated from other profitable business units. Even though the reviewing body shall carry out its duty independently from other profitable business units, it shall be possible that the review and approval of the prospectuses shall be made by employees responsible for other tasks – provided this does not lead to any conflict of interest (cf. Explanatory Report FinSO/FinIO/SOO, p. 55).

The review and approval of the prospectuses may not be delegated to a third party. However, activities of secondary importance, such as maintenance of the IT infrastructure and the like (cf. Explanatory Report FinSO/FinIO/SOO, p. 55), may be transferred by written agreement to qualified third parties (article 75 Draft-FinSO).

The reviewing body is required to prepare an activity report on an annual basis to the attention of FINMA containing information about its organization, its balance sheet and profit and loss statement, statistics about the reviewed prospectuses as well as its expected challenges in the following business year. In addition, the reviewing body will have to present information about the coordination and collaboration with any other reviewing body (article 72 Draft-FinSO). This is especially relevant for areas where the reviewing bodies possess a certain degree of discretion (e.g. articles 41, 45, and 56 FinSA) and the coordination and collaboration among them is necessary in order to avoid distortions of competition and to ensure a uniform application of law (cf. Explanatory Report FinSO/FinIO/SOO, p. 54).

Should the reviewing body no longer fulfil the requirements under the FinSA, FINMA may order the measures necessary to remedy the deficiencies. If the reviewing body fails to remedy the deficiencies within a reasonable period, FINMA shall withdraw its authorization (article 52(4) FinSA).

3) Prospectus requirements and content

The current law requires the publication of an issuing prospectus in case of public offerings of shares and bonds (article 652a and article 1156 CO) and a listing prospectus in case of listings of securities on a Swiss exchange (*e.g.* pursuant to the listing rules of SIX Exchange Regulation). With the introduction of the new prospectus regime under the FinSA, that follows broadly the EU prospectus framework, uniform rules with regard to the publication of a prospectus will be created. The duty to publish a prospectus arises generally in case of primary and secondary public offerings of securities in Switzerland and the admission to trading of securities on a trading venue in Switzerland (article 35 FinSA).

The FinSA provides several exemptions from the duty to publish a prospectus that follow broadly European law and the rules of SIX Exchange Regulation AG. These include exemptions by type of offer, by type of security and for admission to trading (articles 36 et seq. FinSA).

A prospectus must contain the essential information for the investor's decision on the issuer, the guarantor, the security provider, the securities and the offering (article 40(1) FinSA). The prospectus shall be provided in one of the official Swiss languages or in English, must include a summary, may contain documents incorporated by reference and may consist of a stand-alone document or several individual documents (articles 40 and 42-44 FinSA). The minimum requirements as to the content of the prospectus are set out in five schemes annexed to the Draft-FinSO. These schemes follow broadly the regulations of SIX Exchange Regulation AG, materially comply with the guidelines by the International Organization of Securities Commissions (IOSCO) and are largely in line with the requirements of the EU prospectus regulation (cf. Explanatory Report FinSO/FinIO/SOO, p. 39).

Issuers, guarantors and security providers must apply an accounting standard recognized and published by the Swiss trading venue or the reviewing body, as applicable. The latter may accept further accounting standards on a case by case basis provided that the differences between the applied accounting standard and a recognized accounting standard will be explained in detail in the prospectus (article 51(3) Draft-FinSO).

Similar to article 36 of the listing rules of SIX Exchange Regulation AG, the reviewing body may, subject to certain conditions, permit that certain information may be omitted from the prospectus (article 41(1) FinSA). As long as the interests of the investors are safeguarded, it can provide further exemptions which may be subject to conditions and requirements (article 41 FinSA, article 52 Draft-FinSO).

Debt instruments issued under an offering program may be drafted in the form of a base prospectus and must contain all the information available at the time of publication on the issuer, guarantor, security provider, on the securities and at least indicative information on the final terms. After expiry of the subscription period, the final terms must be published and deposited with, but not approved by, the reviewing body (article 45 FinSA).

The duty to comply with the prospectus requirements under FinSA enters into force six month after admission of a reviewing body by FINMA; until then the current provisions of the CO (article 108 Draft-FinSO) shall remain applicable.

4) Review and approval of the prospectus

Currently, only issuers of securities to be listed on a Swiss exchange are required to file a prospectus for approval to the respective approval body, whereas under the new prospectus regime all prospectuses required by FinSA are subject to approval by the reviewing body. Prospectuses of collective investment schemes are, however, not subject to an approval by the reviewing body; prospectuses of foreign collective investment schemes are subject to approval by FINMA (article 51(3) FinSA). Key Information Documents for Financial Instruments in the meaning of article 58 et seq. FinSA will not have to be reviewed and approved by the reviewing body.

In general, the prospectus must be submitted to the reviewing body prior to publication (article 51(1) FinSA).

In order to enable a fast market access, a prospectus for bonds (including straight bonds, convertible bonds, warrant bonds, mandatory convertible notes, contingent convertible bonds and write-down bonds) and structured products with a term of 30 or more days (Annex 7 Draft-FinSO), must be reviewed by the reviewing body only after publication. However, such *ex post* filing is subject to the confirmation by a bank or a securities firm that the main information on the issuer and the securities is available at the time of publication (article 51(2) FinSA); such confirmation has to be submitted to the reviewing body upon filing of the prospectus. In addition, it has to be indicated on the cover page of the prospectus that the latter has not been reviewed (article 40(5) FinSA; article 60(2) Draft-FinSO). In line with the established practice of SIX Exchange Regulation AG the prospectus will generally have to be filed within two months from the beginning of the public offering or the admission to trading; for products with a term of 90-180 business days, the time limit is 10 business days, for products with a term of 30-89 days, 5 business days (cf. article 60 Draft-FinSO).

The reviewing body has no right to decide whether there is a duty to draft a prospectus under FinSA. Accordingly, the reviewing body will also have to review a prospectus in case there is no prospectus requirement under FinSA (e.g. because an exemption pursuant to article 36 or 37 FinSA applies) (cf. Explanatory Report FinSO/FinIO/SOO, p. 46).

The procedure carried out by the reviewing body will be in accordance with the Federal Act on Administrative Procedure (APA) (article 53(1) FinSA). Accordingly, decisions by the reviewing body are issued by rulings in accordance with article 5 APA.

The reviewing body will check the prospectus for formal completeness, coherence and understandability (article 51(1) FinSA, article 59(1) Draft-FinSO). The prospectus is, however, not reviewed as to material accuracy. According to the dispatch by the Federal Council to the Federal Assembly on the draft FinSA and the draft FinIA of 4 November 2015, coherence means that the prospectus may not contain any internal contradictions. In addition, the reviewing body is not required to investigate whether there is any other information about the issuer that must be included into the prospectus (cf. Explanatory Report FinSO/FinIO/SOO, p. 46). Compared to the current review of a listing prospectus pursuant to the rules of and carried out by SIX Exchange Regulation AG which is limited to the review of formal completeness, it is expected that the scope of the review to be undertaken by the reviewing body will increase substantially under the new legislation.

Generally, the deadline for the review of a prospectus for issuers is 10 calendar days. Such period begins to run once the reviewing body has received the complete prospectus, i.e. the prospectus does not contain any substantial gaps, respectively all parts pursuant to article 44 FinSA and all documents incorporated by reference in accordance with article 42 FinSA have been filed. If the reviewing body notices that a prospectus does not fulfil the statutory requirements, it informs the submitting party within 10 calendar days upon submission, giving a reason and requesting rectification. Upon receipt of a rectified version, a new review period of 10 calendar days starts again. For new issuers, the deadline is 20 calendar days (article 53 FinSA). An issuer is deemed to be a new issuer if it has not filed a prospectus with a reviewing body for securities issued or guaranteed by it within the last three years and at the time of filing of the prospectus no securities issued or guaranteed by it are admitted to trading on a trading venue in Switzerland (article 69 Draft-FinSO). This provision follows article 27 of the Additional Rules for the Listing of Bonds of SIX Exchange Regulation AG which is, contrary to the suggested wording in the Draft-FinSO, only applicable to new issuers of bonds. The provisions with regard to the deadlines are regulatory periods (*Ordnungsfristen*). Accordingly, should the reviewing body fail to issue its decision within the applicable deadlines, this shall not constitute an approval of the prospectus (article 53(6) FinSA). The aforementioned deadlines are principally subject to the provisions regarding legal holidays pursuant to article 22a APA. Given that the suspension of deadlines would disturb the proper functioning of the capital markets and hinder issuers to react fast to changes in the capital markets, it is expected that the reviewing body will unilaterally renounce the applicability of article 22a APA (cf. Explanatory Report FinSO/FinIO/SOO, p. 51).

Similar to the prospectus regime of the EU, the FinSA contains a rule of equivalence for the review of foreign prospectuses. A foreign prospectus may be approved if it was prepared in accordance with international standards established by international organizations of securities regulators (such as the international disclosure standards for cross-border offerings and initial listings by foreign issuers of September 1998, issued by IOSCO) and the duties to inform are equivalent to those under the FinSA. In addition, the reviewing body may foresee that prospectuses approved under specific legal frameworks are deemed as authorized in Switzerland as well. It will have to publish a list in this regard (article 54 FinSA).

After approval, prospectuses shall generally be valid for 12 months for public offers or admission to trading on a trading venue of securities of the same type and by the same issuer. Prospectuses for debt securities issued under an offering program shall, however, be valid until none of the debt securities concerned are constantly or repeatedly being issued anymore (article 55 FinSA).

If between time of approval of a prospectus by the reviewing body and final completion of a public offering or opening of trading on a trading venue new facts occur or are established that could significantly affect the valuation of the securities, a supplement to the prospectus needs to be prepared, reported to the reviewing body and approved within seven calendar days. The reviewing body shall keep a list of facts that must be reported only, but are not subject to formal approval (article 56 FinSA).

Any approved prospectus must be filed with the reviewing body and published no later than the beginning of the public offer or admission to trading. The reviewing body records all approved prospectuses on a list which is made publicly available for twelve months (article 64 FinSA).

The reviewing body may charge cost-effective fees in order to cover its expenses (article 57(1) FinSA; article 78, 79 and Annex 8 Draft-FinSO).

5) Conclusion

With the introduction of the FinSA and its implementing provisions the current listing process for securities to be listed on SIX Swiss Exchange will be split into two separate streams: the review and approval of a prospectus by the reviewing body and the admission to listing and trading by SIX Exchange Regulation AG.

The scope of review is likely to increase since the new regime not only requires the review of a prospectus as to formal completeness, as currently carried out by SIX Exchange Regulation AG, but also as to coherence and understandability.

The reviewing body has discretion to grant exemptions from the content of the prospectus subject to certain conditions. Hence, the new prospectus regime leaves room for adequate and market oriented solutions for individual cases as well as flexibly to adapt to new market developments.

SIX Exchange Regulation AG will file for recognition as a reviewing body approved by FINMA. With its long-standing and proven expertise in reviewing prospectuses it will ensure that the newly split process of (i) review/approval of the prospectus and (ii) admission to listing and trading will continue to be carried out efficiently and in line with market and issuers' needs.

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Point of Sale Regulation – Consultation Draft of Financial Services Ordinance: Key Points

Reference: CapLaw-2018-58

The publication for consultation of the draft Financial Services Ordinance represents the last milestone on the road to the new financial services architecture in Switzerland. For all those who aim to optimize the details of the point of sale code of conduct, the consultation to the Draft-FinSO until 6 February 2019 is the last possibility to do so. Considering whether to provide comments to the Draft-FinSO is important because the ordinance specifies a number of key provisions of the FinSA on the point of sale duties. Hereinafter, is an overview of the most important proposed ordinance rules.

By Sandro Abegglen / Luca Bianchi

1) Introduction

The publication of the consultation draft Financial Services Ordinance (*Finanzdienstleistungsverordnung*, Draft-FinSO) on 24 October 2018 opens the last phase towards finalization of the Financial Services Act (FinSA). Market participants and other interested parties can provide comments to the draft until 6 February 2019. Consequently, there will be changes to the proposed text of the Draft-FinSO. Nevertheless, the published draft provides for a good indication of the definitive content of the FinSO, and, thus, of what the industry has to prepare for.

The purpose of this article is not to recapitulate an overview of the point of sale duties of the FinSA. The authors have already outlined those on other occasions (see CapLaw-2017-3, 2016-3 and 2014-5 or the publication *Switzerland's New Financial Market Architecture*). Instead, the article focuses exclusively on key points of the Draft-FinSO which are relevant for the point of sale.

2) Point of Sale Key Points of the Financial Services Ordinance Consultation Draft

The Draft-FinSO contains the following new aspects and clarifies the following key points:

- ***Client segmentation***: The Draft-FinSO specifies that the client segmentation by a financial services provider (*i.e.,* the qualification of its clients as institutional, professional or private clients) applies throughout the whole relationship of a given client (article 4 (1) Draft-FinSO). However, according to the Explanatory Report to the Draft-FinSO of 24 October 2018 (the Explanatory Report, page 22) a client may have several client relationships with one financial services provider and can – depending on the relevant financial services – thereby be assigned to different client segments. The Draft-FinSO contains a transitory provision that allows the implementation of the new client segmentation within one year after the entering into force of the ordinance (article 103 Draft-FinSO), *i.e.*, until the end of 2020.

- ***New threshold for the opting-out (up) of private clients***: The Draft-FinSO provides for specifications of the eligible financial assets that are required for the opting-out of a private client (HNWI) into the professional investor status, namely, bank deposits, securities and uncertificated securities (including collective investment schemes and structured products), derivatives, precious metals, life insurances with repurchase value, and claims on assets that are based on fiduciary relationships (article 5 (1) (a-f) Draft-FinSO). Direct investments in real estate no longer qualify as eligible financial assets (article 5 (2) Draft-FinSO), in contrast to the current rule in the Collective Investment Schemes Ordinance (CISO), and this seems to be a reaction to the reduction of the relevant threshold of assets of HNWI without knowledge and experience from currently CHF 5 million to only CHF 2 million by the parliament (cp. article 5 (2) (b) FinSA). Due to this decrease, consideration of direct real estate investments would have caused a major expansion of the circle of potential professional clients. According to the Explanatory Report (page 23), this was not the intention of the legislator.

- ***Clarification of certain code of conduct duties***: The Draft-FinSO contains several provisions that further specify the conduct duties of financial services providers (article 6 et seq. Draft-FinSO; Explanatory Report, page 23 et seq.). In particular, it comprises details on the information duties, fee transparency (see lemma *Disclosure of (distribution) fees* below), conflicts of interests duties, and the required information on the considered investment product market universe.

  If a client obtains financial services from various financial services providers, the code of conduct (especially, the information duties) applies to all of them.

  Information on financial services and financial instruments must include their characteristics and functioning as well as the essential risks and duties that arise thereof for the clients (article 7 (1) (a) and (b) Draft-FinSO). Also, the financial services provider must clarify whether his service represents portfolio management, portfolio-related advice or mere transaction-related advice, or execution only services.

Conflicts of interests according to article 24 (a-d) Draft-FinSO include, in particular, situations where financial services providers:

(a) draw financial advantages or avoid financial losses in breach of good faith at the expense of their clients;

(b) have own interests which are conflicting the interests of their clients with respect to the outcome of a financial service rendered to its clients;

(c) have a financial or other incentive to put the interests of certain clients ahead of those of other clients when rendering financial services; or

(d) accept an incentive in the form of financial or non-financial benefits or services in breach of good faith from third-parties in relation to a financial service rendered to its client.

The new code of conduct rules (article 7-16 FinSA) must be implemented at latest with the end of the transitory period of one year after the entering into force of the Draft-FinSO (article 105 Draft-FinSO).

– ***Assessment of appropriateness / suitability in the case of proxy relationships***: With respect to appropriateness and suitability tests in general, the Draft-FinSO clarifies, in line with the private law rules on imputation of knowledge of the agent to the principal, that in cases of proxy relationships the knowledge and experience of the *representative* must be considered (article 16 Draft-FinSO). The legislator presumes that in such a scenario it is the representative who takes the investment decisions for the represented party (Explanatory Report, page 26).

– ***Assessment of financial situation / investment objectives***: For the assessment of the financial situation of the client in the context of a suitability test in particular, the financial services provider must evaluate the source and amount of the client's regular income, his wealth as well as his current and future financial obligations (article 17 (1) Draft-FinSO). For the assessment of the investment objectives of the client, the financial services provider must consider the time horizon, the purpose of the investment and the client's risk capacity and risk tolerance as well as investment restrictions, if any (article 17 (2) Draft-FinSO).

– ***Disclosure of (distribution) fees***: Financial services providers are obliged to inform clients on the personally recommended financial service and connected risks and costs (article 8 (2) (a) FinSA). The information on costs comprises, in particular, information on the one off and recurring fees that arise with the sale or purchase of the concerned financial instrument (article 8 (1) FinSO). One time fees that must be disclosed include production costs that arise with the purchase of the financial instrument, as well as related transaction costs such as, *e.g.*, distribution fees; recurring fees include, *e.g.*, management fees, advisory fees, or deposit fees (Explanatory Report, page 24). To the extent such information is included in the prospectus or the basic information sheet (KID), the information duty may be fulfilled by reference to these documents (article 8 (2) FinSO).

– ***Criteria for best execution***: The financial services provider is obliged to define the criteria relevant for the selection of the execution venue which is to be chosen for the execution of client orders (in particular, the price, the speed, as well as the probability of the execution and settlement according to article 21 (1) Draft-FinSO). If the client has given an explicit instruction in this regard, the financial services provider must comply with it (article 21 (2) Draft-FinSO).

– ***Organizational requirements and employee compensation***: The financial services providers must specify internal standards that are adequate relative to their size, complexity and legal form as well as the financial services offered (article 23 (1) (a) Draft-FinSO).

  Generally, employee compensation must not create incentives to disregard legal duties or to engage in damaging behavior towards clients (article 23 (1) (c) Draft-FinSO).

  In addition, feasible organizational measures for the prevention of conflicts of interests must be implemented as described in detail in article 25 (1) (a-g) Draft-FinSO. These include:

  (a) measures to recognize conflicts of interests;

  (b) barriers to or controls of the exchange of information to the extent contrary to the client interests;

  (c) functional separation of the organization and the management of employees (*i.e.*, Chinese walls) provided that their main tasks could cause a conflict of interest between clients among themselves, or between the clients and the financial services provider;

  (d) measures to avoid that employees, which are involved in providing different financial services at the same time, are assigned tasks that could impair the proper handling of conflicts of interests;

  (e) defining the compensation policy to the effect that variable compensation elements do not impair the quality of the financial services towards clients;

(f) the issuance of internal guidelines which enable the recognition of conflicts of interests between clients and employees and point out measures to avoid or resolve such conflicts of interests and regularly examine such guidelines; and

(g) enacting rules for the purchase and sale of financial instruments for the employees' own account.

With respect to organizational requirements the Draft-FinSO contains a transitory period of one year after the entering into force of the ordinance (article 106 FinSO).

- ***Employee selection***: Employees must be selected diligently and obtain education and training on the code of conduct rules and the specific subject expertise required to fulfill their concrete tasks (article 23 (1) (b) Draft-FinSO). As there is no obligation to develop industry standards for the education and training, every financial services provider may define its own standards.

3) Point of Sale Duties vs. Product Transparency

Interesting legal questions arise regarding the relationship of the point of sale duties (especially, suitability, appropriateness, information duties, service transparency, or code of conduct) and the point of production duties (in particular, prospectus and KID duties). Both groups of duties are interlocked and complement each other. In addition, the cross-sectoral rules of the FinSA, respectively, FinSO must sometimes be applied in interplay with the sector-specific rules of the Banking Act (BA) or the Collective Investment Schemes Act (CISA) and the respective ordinances. While this task may not always prove simple, the combination of point of sale duties and point of production duties represents a well-designed regulatory framework that serves the adequate protection of investors, which constitutes a quality feature of "Swiss made" financial services and products.

4) Conclusion

In conclusion, the Draft-FinSO clarifies many point of sale-related provisions of the FinSA and overall is well drafted and balanced. However, certain amendments would be welcome, *e.g.*, on the difficult distinction between portfolio-based and transaction-based investment advice – it will be interesting to see how the industry and other interested parties will comment the Draft-FinSO.

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Key Investor Document – the flexible brother of the EU PRIIPs KID

Reference: CapLaw-2018-59

On 15 June 2018, the Swiss parliament adopted the Financial Services Act and the Financial Institutions Act, which are expected to enter into force on 1 January 2020. One of the key changes introduced by the Swiss Financial Services Act is the obligation to prepare and make available to retail investors a short document setting out the key information, the so-called key information document (*Basisinformationsblatt*). The draft implementing ordinances the Federal Council has published on 24 October 2018 contains supplementary provisions on the content, language, layout and scope of the new regulatory leaflet. While the proposed template for the future key information document is almost identical to the EU PRIIPs KID template, the Swiss version of the key information document is far more flexible than its EU equivalent and reflects the pragmatic approach taken by the Federal Council in the draft ordinances to ensure a successful implementation of the new regulatory leaflet.

By Daniel Haeberli

1) Introduction – The new Swiss financial market regulation

On 15 June 2018, the Swiss parliament adopted the Financial Services Act (FinSA) and the Financial Institutions Act (FinIA) and on 24 October 2018 the Swiss Federal Council opened a consultation process regarding the draft ordinances implementing the new financial market regulations - the Financial Services Ordinance (Draft-FinSO), the Financial Institution Ordinance (Draft-FinIO) and the Supervisory Organisation Ordinance (Draft-SOO) - that will last until 6 February 2019. It is expected that the final ordinances will be published in the third quarter of 2019, just ahead of the expected entry into force of the Financial Services Act and the Financial Institutions Act and the implementing ordinances on 1 January 2020.

This article introduces the new key information document under the Swiss Financial Services Act (the KID or FinSA KID) and, in particular, the content and format requirements set out in the Draft-FinIO.

2) Key Information Document – Comparability requires standardization

One of the key changes introduced by the FinSA is the obligation to prepare and make available a short document setting out the key information, the so-called key information document (*Basisinformationsblatt*), when offering financial instruments to retail investors (private clients) in Switzerland.

The introduction of a short information document for financial instruments is not a novelty, neither internationally nor in Switzerland. The Regulation (EU) No. 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (the PRIIPs Regulation) requires manufacturers of packaged retail and insurance-based investment products to prepare a key information document (the PRIIPs KID). The PRIIPs KID is intended to show investors the key product features of a financial product on maximum three DIN A4 pages, allowing a cross-product comparison of different investment opportunities. The PRIIPs Regulation entered into force on 1 January 2018.

In Switzerland, the Collective Investment Schemes Act (CISA) introduced in 2007 the simplified prospectus for structured products. The simplified prospectus must describe the key characteristics of the product, its profit and loss prospects, together with the significant risks for investors. Instead of providing detailed regulations on the content and formation of the simplified prospectus, the Collective Investment Schemes Ordinances provides for a delegation to a self-regulatory body. The Swiss Bankers Association and the Swiss Structured Products Association have issued guidelines on informing investors about structured products. While setting out the information items that need to be addressed in the simplified prospectus, these guidelines neither limit the number of pages of a simplified prospectus nor provide a template or require a specific sequence of the information that must be included in the simplified prospectus. As a result, there is no standardized simplified prospectus across the structured products industry in Switzerland. This will change with the KID as contemplated by the Draft-FinSO.

The KID should not only be easy to understand and enable private clients to make a well-founded investment decision, but should also enable retail investors to compare the key features of different investment products. Achieving comparability of financial instruments is really a novel feature for a regulatory investor information document in Switzerland. In order to achieve comparability of financial instruments, the content and format of the KID must be standardized.

3) Content and Format of the Key Investor Document

a) Minimum requirements in the FinSA and supplementary provisions in the Draft-FinSO

Very similar to the current provision in the CISA relating to the simplified prospectus for structured products, the FinSA states the principle that the KID must contain the essential information of the financial instrument and sets out the minimum information that must be covered therein.

In particular, the following information must be covered in the KID according to article 60 FinSA:

(i) the type and characteristics of the financial instrument,

(ii) the risk/return profile of the financial instrument,

(iii) the costs of the financial instrument,

(iv) the minimum holding period and tradability of the financial instrument, and

(v) information on the authorization and approvals associated with the financial instrument.

The introduction of supplementary provisions on the KID was delegated to the Federal Council pursuant to article 63 FinSA.

The Draft-FinSO contains in articles 88 et seq. the supplementary provisions on the content, language, layout and scope of the KID. In particular, the Draft-FinSO provides for a template KID and specifications as to the content of the KID.

b) Format of the KID

As the introduction of the KID was inspired by the EU PRIIPs Regulation it does not come as a surprise that the template KID in the Draft-FinSO is almost identical to the PRIIPs KID template. The length of the KID is also limited to three DIN-A4 pages as is the PRIIPs KID. Identical to the PRIIPs Regulation, the sequence and headings as provided in the template must be strictly followed. There are no requirements regarding the sequence of information within the individual sections and the length of the individual sections.

The template contains 10 sections with the following headings, which are the same as in the PRIIPs template:

- Purpose
- Product
- Warning
- What kind of product is it?
- What are the risks and what might I get back in return?
- What happens if [name of the issuer] is unable to make the payment?
- What costs will be incurred?
- How long do I have to hold the investment and can I withdraw money early?

- How can I make a complaint?
- Other relevant information

Providing for a template in the Draft-FinSO that is very similar to the PRIIPs template has the benefit of ensuring the comparability of financial instruments for which a PRIIPs KID or a FinSA KID is made available. The comparability between the PRIIPS KID and the FinSA KID is very important since the FinSA allows the use of equivalents foreign key information documents instead of a FinSA KID and the Draft-FinSO expressly recognizes the PRIIPs KID as such equivalent foreign document.

c) Content of the KID

In respect of the content of the KID, the Swiss regulations are not as detailed as the PRIIPs regulations and provide far more flexibility than the PRIIPs regulations.

In the EU there are associated implementing regulations, in particular the Commission Delegated Regulation supplementing the PRIIPs Regulation by laying down regulatory technical standards with regard to, among other things, the content of the PRIIPs KID and there are guidelines published by the European Commission and further specifications in the form of questions and answers on the PRIIPs KID by the European Financial Supervisory Authorities (ESAs).

The Draft-FinSo specifies the content of the FinSA KID in schedules 10, 11 and 12 of the Draft-FinSO. These schedules specify the information that needs to be included in the sections "What kind of product is it?", "What are the risks and what might I get back in return?" and "What costs will be incurred?". In respect of the other sections of the KID template, the Draft-FinSO does not provide any further specific requirements other than the specifications that are directly included in the template.

Schedule 10 of the Draft-FinSo lists the information that are to be included in section "What kind of product is this?". In particular, a description of the legal form and a brief description of the nature of the financial instrument is requested. This is very similar to the information required to be included in a PRIIPs KID. An item that is not mandatory under the Draft-FinSO, but required under the PRIIPs Regulation is the description of a target group and target market. Since the FinSA does not contain any provisions similar to the MiFID 2 product governance regulations, including a target market concept, there is not really a need to mandatorily include a description of the targeted retail investor in the FinSA KID.

The biggest differences between the PRIIPs Regulations and the draft FinSO in respect of the content requirements are in respect of the description of the risk and rewards of the financial instrument (*i.e.*, "What are the risks and what might I get back in return?).

d) The risk and rewards description – the Swiss approach

The PRIIPs Regulation has introduced a summary risk indicator (SRI) of seven classes to present the risk of a product in the PRIIPs KID. The methodology to assign each product to one of the seven classes is rather complex and is composed of a market risk measure and a credit risk measure. The rewards of a product must be presented by including four performance scenarios. These require complex calculations based on the same date used for the purpose of calculating the market risk measure and may, as has recently been acknowledged even by the ESAs, result in misleading figures.

The Draft-FinSO does not follow the PRIIPs Regulations in respect of the risk and rewards description. The approach taken in the Draft-FinSO provides for a lot of flexibility and avoids some of the flaws of the summary risk indicator and performance scenarios of the PRIIPs KID.

The risk profile of a financial instrument can be described in generic terms. A risk indicator may be provided as an alternative to or in combination with the generic risk description. If the risk is described on generic terms, the typical product risks must be considered, such as:

- issuer risk
- market risk
- liquidity risk
- foreign exchange risk
- termination and reinvestment risk

These typical product risks are listed in Schedule 11 of the Draft-FinSO and shall serve as guidance when completing this section. This list is very much in line with the risks that are usually addressed in a simplified prospectus for structured products.

If a risk indicator is provided in the KID, it must be calculated and presented pursuant to the respective requirements applicable to a document which is recognized as being equivalent. Of course, the idea is that the SRI of the PRIIPS Regulation may be used since Schedule 14 of the Draft-FinSO expressly recognizes the PRIIPs KID as an equivalent foreign document. Including just any risk indicator, whether developed by the issuer of the financial instrument or introduced by an industry association such as the Swiss Funds & Asset Management Association SFAMA or Swiss Structured Products Association SVSP, is not permitted.

The KID must also inform investors of the loss and reward potential of a financial instrument by including performance scenarios. In principle, a positive, a neutral and a negative scenario must be presented. Schedule 11 of the Draft-FinSO does not provided for further specific requirements for the presentation of the performance scenarios. The performance scenarios used in a simplified prospectus for structured products may serves as a guideline for certain financial instruments. A possibility that is expressly permitted in the Draft-FinSO is to calculate and present the performance scenarios pursuant to the PRIIPs Regulation.

4) Final remark

The rather lean and flexible regulations in respect of the of the content and format requirements for the KID reflect the rather pragmatic approach taken by the Federal Council in the Draft-FinSO and should ensure a successful the implementation of the KID.

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The Enforcement of Clients' Rights in the Financial Services Act

Reference: CapLaw-2018-60

The new Financial Services Act will require all providers of financial services to be affiliated with an ombuds institution. This requirement is the only substantially new element remaining from a broad set of proposals to strengthen the enforcement of clients' rights. Parliament ultimately opposed the introduction of new procedural mechanisms specifically for the financial services industry, such as collective action instruments and changes to the 'loser pays' rule.

By Thomas Werlen / Jonas Hertner

1) Introduction

One of the primary drivers of a new law governing the provision of financial services was the realization, in the wake of the financial crisis of 2007/2008, that retail investors had insufficient means to enforce monetary claims against financial institutions. The insolvencies of the Lehman Brothers and Kaupthing groups had left scores of investors without an effective remedy, mainly for two reasons. First, both procedural and substantive law made it difficult for individual investors to establish proof of misconduct of their financial service provider. Second, litigation against financial service providers was costly to the point that damaged investors were discouraged from trying to enforce their rights if the damages incurred were below a certain threshold.

2) A brief legislative history of the ideas to strengthen the rights of clients

The original preliminary draft of the Financial Services Act (FinSA), issued by the Federal Council in June 2014, included a relatively far-reaching section on the enforcement of clients' rights. The envisaged strengthening of the rights of clients of financial service providers consisted of three key elements: (1) the providers' obligation to produce certain documents and clients' right to information (coupled with a reversal of the burden of proof), (2) a requirement for all service providers to be affiliated with an ombuds institution, and (3) measures to allocate the cost risks of litigation to services providers, either through a specialized arbitration court or through a new fund set up to finance litigation brought by clients under certain circumstances. The third element, a change in the allocation of the cost risks of litigation brought by clients against service providers, was specifically designed to address the lack of an effective collective action mechanism.

Following a consultation proceeding, in which these changes faced overwhelming criticism from financial service providers, the draft bill put forward in November 2015 significantly curtailed the proposed changes. The provisions governing the enforcement of clients' rights in the November 2015 draft bill were limited to the following elements:

a) Service providers' obligation to produce documents and clients' right to information

The client has a right to be provided a copy of all documents concerning the client. The client may enforce this right in summary proceedings. If a service provider refuses to provide such copy, the refusal may influence the allocation of costs in a subsequent dispute between the parties.

b) Ombuds system

All service providers are required to be affiliated with an ombuds institution. The ombuds proceeding needs to be "un-bureaucratic", fair, efficient, impartial, and cost-effective or free for the client. The ombuds system is designed to facilitate an agreement between the parties, but will not result in a resolution of the dispute against the will of either party.

c) Advance on Court Costs and Allocation of Litigation Costs

Retail clients are to be exempt from advancing court costs and a security for the defendant's legal fees. In addition, service providers prevailing in litigation brought by retail clients will only be entitled to claim their legal fees from the claimant if (1) the client did not go through the respective ombuds institution, (2) the client has extraordinary financial means, (3) the amount in dispute does not exceed CHF 250,000, and (4) if the claim was not frivolous. Finally, a court may diverge from the general rules of cost allocation in the Swiss Civil Procedure Code under certain circumstances, including if a client had reasonable grounds to bring a claim against the service provider in light of the ombuds proceedings.

The bill's provisions on the enforcement of clients' rights was subject to lively discussions in parliament. The proposed amendments regarding the advance on court costs and allocation of litigation costs were struck without replacement. Majorities in both chambers made reference to the ongoing plans to revise the Civil Procedure Code and argued that changes to the principles of cost allocation in civil procedure should not be specific to the financial services industry.

Towards the end, the debates in particular focused on the question whether the burden of proof for misconduct or false or misleading information by the service provider should be with the client, or whether certain assumptions benefitting the client should be introduced. Another hotly debated point was whether service providers should be able to exonerate themselves with respect to any civil law obligations if they could show that they met all regulatory requirements of the FinSA. Finally, on 15 June 2018, both chambers of parliament adopted the text in a final vote.

3) The provisions governing the enforcement of clients' rights in the new FinSA

The enforcement of clients' rights in final text of the FinSA rests on the two remaining pillars of (1) a client's right to be provided a comprehensive copy of all documents and records the service providers keep concerning the specific client and the client relationship, and (2) the ombuds system, requiring all service providers – not only the banks – to be affiliated with an ombuds institution recognized by the Federal Department of Finance.

a) The duty of the service provider to keep records and to provide these records to the client upon request

With respect to the scope of the records to be kept by the service provider, Art. 15(1) FinSA requires service providers to keep records on (a) the specific services to be provided as agreed upon with the client and the information gathered from the client, (b) any waiver from the requirement to assess the suitability and appropriateness pursuant to articles 13 and 14 FinSA, and (c) all financial services provided.

For advisory contracts, Art. 15(2) FinSA additionally requires the service provider to keep records on the client's requirements and the reasons for each recommendation that results in the purchase of the recommended product.

Art. 16(1) FinSA requires the service provider to transmit the information pursuant to Art. 15 FinSA by post to its client upon request or to provide it by any other suitable means.

In addition, Art. 16(2) FinSA requires the service provider to provide information regarding (a) the services which were agreed upon and executed, (b) the composition, valuation and development of the portfolio, and (c) the costs associated with the provision of the services.

The draft Financial Services Ordinance (Draft-FinSO) will further specify the scope and modalities of the information to be provided. The Draft-FinSO does not introduce any significant new requirements and merely reflects the current approach as commonly used by banks.

With respect to the client's right to be provided with the information described above, Art. 72(1) FinSA entitles the client to request a comprehensive copy of such information at any time.

Art. 72(2) FinSA requires the request to be made in writing. The service provider is required to provide the copy within 30 days free of charge.

Article 72(3) FinSA entitles the client to pursue the right to a copy of the records in summary proceedings if the service provider does not comply with client's request.

Article 72(4) FinSA notes that a refusal by the service provider to comply with the request may be taken into consideration by the court in a later litigation when allocating the costs of the proceedings.

The Draft-FinSO suggests that, while the first copy of information must be provided free of charge, any subsequent request, if not sufficiently justified, may incur an appropriate fee.

b) The ombuds system

Art. 74 et seq. FinSA stipulate the new ombuds system, which will require all service providers to fund and be affiliated with a particular ombuds institution. The funding of a particular ombuds institution shall be governed by an institution's own regulations, borne by its service provider participants in proportion to their use of the institution (Art. 80 FinSA).

Art. 75 FinSA requires the ombuds proceeding to be "un-bureaucratic", fair, swift, impartial, and free or cost-effective for the client. The ombuds proceeding is confidential, meaning that the statements made in the proceedings must not be used in another proceeding. The confidentiality also covers party submissions: neither party has a right to see the correspondence between the other party and the ombuds institution. The client may initiate a proceeding before the ombuds institution (1) in accordance with the respective regulations of the institution, (2) if the client can demonstrate that he or she notified the service provider of an issue and undertook a reasonable effort to resolve it, (3) if the client's claim is not manifestly ill-founded and was not subject to a previous conciliation proceeding, and (4) if the issue is not yet pending before a judicial body (*e.g.*, another ombuds institution, a state court or a conciliatory authority).

While the ombuds institution will not have discretion to issue a decision on the matter brought before it, it may give its own factual and legal assessment and include it in the final communication to the parties (Art. 75(8) FinSA).

Pursuant to Art. 76 FinSA, an ombuds proceeding does not preclude a civil proceeding covering the same matter. If, however, a judicial body seizes the matter, the ombuds institution concludes its proceeding. If an ombuds proceeding was undertaken but did not result in a resolution of the dispute, the claimant in a civil proceeding may unilaterally decide to waive the conciliation stage pursuant to the Civil Procedure Code.

Art. 77 ff. FinSA stipulates the obligations of service providers in connection with the ombuds system. Notably, service providers must affiliate themselves with a recognized ombuds institution; participate in an ombuds proceeding if so requested by a client; duly honor all requests to appear and submit statements in the proceeding.

Service providers must inform their clients about the possibility to request an ombuds proceeding in connection with the opening of a client relationship, when rejecting a claim made by a client, and anytime upon request.

With respect to the organizational aspects of the ombuds system, Art. 81–83 FinSA broadly govern the membership of service providers, providing that ombuds institution need to accept service providers if they meet the institution's own membership criteria, and that service providers may be excluded if they violate their obligations pursuant to Art. 78–80 FinSA. Ombuds institutions are required to notify the supervisory authority and the central register of ombuds institutions (both likely to be within the Federal Department of Finance) of all service providers accepted as members and of those not accepted or subsequently excluded (Art. 83 FinSA).

The ombuds institutions themselves shall be recognized by the Federal Department of Finance if they meet the requirements of Art. 84 FinSA. Notably, they (and the ombudspersons engaged by the institution) are required to be impartial and independent, and that the ombudspersons are sufficiently competent. Institutions further need to have regulations governing its organization and membership of service providers, the ombuds procedure, and the financial contributions of service providers. Any amendment of internal regulations will have to be approved by the supervisory authority (Art. 85

FinSA). Ombuds institutions shall publish annual reports on their activities (Art. 86 FinSA).

4) Conclusion

What had started with an attempt to significantly strengthen the means of retail clients of financial service providers to litigate claims against service providers, produced little more than a restatement of the status quo.

The provisions governing the right of clients to be provided with a full documentation of records relevant to the client relationship with the service provider mirror the existing provisions governing the agency contract in the Code of Obligations, and the right of a person to be provided with copies of records held by an organization pursuant to the Data Protection Act.

As regards the provisions governing the ombuds system, the expansion of the system to cover all providers of financial services will not resolve the substantial and procedural problems clients have been facing when litigating claims against service providers.

With respect to the lack of tools for clients to pursue claims collectively, the decision to try to devise new collective action instruments within the general framework of the Civil Procedure Code – as opposed to an industry-focused approach in the FinSA – may be regarded as a wise one (c.f. *Werlen/Decurtins, The Proposed Strengthening of Group Action in Swiss Civil Procedure, in: CapLaw-2018-44*). However, in light of the current debate on the basis of the preliminary draft revision of the Civil Procedure Code published on 2 March 2018, it is unlikely that a consensus on a comprehensive collective action regime will be found in the immediate future.

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FinSA: New Registration Duty for Client Advisers

Reference: CapLaw-2018-61

The Financial Services Act (FinSA), which is expected to enter into force on 1 January 2020, will introduce a new registration duty for client advisers of Swiss financial service providers not subject to prudential regulation and client advisers of foreign financial institutions. Today, no such registration requirement exists with the exception of similar obligations for untied insurance intermediaries, who have to register with the public register kept by the Swiss Financial Market Supervisory Authority (FINMA).

Under the new regime, client advisers will be required to register in a register maintained by one or more registration bodies licensed by FINMA. To register, they must evidence sufficient knowledge of the rules of conduct under the FinSA and the necessary expertise to perform their duties, adequate financial means as well as affiliate themselves to an ombudsman's office. Clients may check the register at any time to verify that their adviser has the required qualifications. The registration will, however, not imply any prudential or ongoing supervision by FINMA. If a client adviser no longer meets the registration requirements, the adviser will be deleted from the register by the competent registration body and may, consequently, no longer engage in activities as a client adviser.

By Martin Peyer

1) Introduction

Client advisers play an important role in implementing the new rules of conduct in articles 7 ff. FinSA. They are usually the primary point of contact for clients with their financial service provider and only if they have sufficient knowledge of the new rules, they can comply with them in practice.

The responsibility to ensure that its client advisers will comply with the requirements of the FinSA lies with the financial service providers. In particular, they must ensure that their advisers have an appropriate education and the necessary skills for the specific services they provide (article 6 FinSA). For prudentially supervised financial service providers, FINMA or a supervisory organization pursuant to the Financial Institutions Act (FinIA) will monitor that client advisers comply with these requirements. No such controls exist, however, for Swiss and foreign financial service providers that are not supervised by FINMA.

To bridge this gap, the FinSA will require client advisers of Swiss financial service providers who are not prudentially supervised (such as insurance intermediaries and financial advisers) and financial service providers domiciled abroad to register themselves in the new register of advisers that will be established under the FinSA (article 28 (1) FinSA) (*see* Dispatch by the Federal Council on the Financial Services Act and the Financial Institutions Act of 4 November 2015, Bundesblatt 2015 (Dispatch FinSA), page 8901 ff., page 8967). In addition, to protect clients, client advisers who have seriously breached the rules of conduct in the past will not be allowed to register themselves and, thus, to provide financial services. Further, advisers – or the financial service provider for which they work – must guarantee that they have sufficient financial resources to carry out their business activities (*see* Dispatch FinSA, page 8922).

The registration will, however, not imply any prudential or ongoing supervision by Swiss authorities. It only seeks to ensure that client advisers are aware of the rules of conduct and treat clients fairly. Yet, clients may check the register at any time if they have doubts about the qualifications or integrity of their client adviser (article 32 (5) FinSA), and, therefore, the new register is also expected to increase clients' confidence in their client advisers.

2) Duty to Register for Client Advisers

a) Definition of Client Adviser

According to article 3 (e) FinSA, a client adviser is a natural person who performs financial services on behalf of a financial service provider or in its own capacity as financial service provider. In most cases, the adviser is not identical with the financial service provider for which it acts. Only if a natural person provides financial services, it may at the same time be both, a client adviser and a financial service provider (Dispatch FinSA, page 8922 and 8947 f.).

The term "client adviser" has to be interpreted broadly and includes persons that carry out transactions in financial instruments for clients or advise them in connection with their investments such as asset managers, financial advisers and insurance intermediaries. It is further likely that the distribution of collective investment schemes to clients also constitutes a financial service pursuant to the FinSA if it is carried out on a professional basis. Thus, distributors of collective investment schemes may also have to register in the register of advisers (unless an exemption applies).

However, not every employee of a financial service provider is deemed a client adviser. Employees who have no direct contact with clients or who support the provision of financial services only to a minor extent, *e.g.* by sending product information to a client in response to an expression of interest, coordinating meetings or working in technical support functions, have no duty to register (Dispatch FinSA, page 8948). In this context, it remains to be seen how persons who have contact with clients under the direct and ongoing supervision of a client adviser, such as a financial analyst providing specialist advice in a meeting conducted by a client adviser will be treated. Further, corporate finance experts, for example, who advise a company in an IPO in Switzerland will likely not fall in the scope of the new rules as long as they do not provide investment advice or other financial services pursuant to article 3 (c) FinSA at the same time.

b) Scope

Only client advisers who are not acting for a financial service provider that is prudentially supervised in Switzerland need to register, regardless of whether they carry out their business in Switzerland or from abroad or whether they are dealing with retail or professional clients (Dispatch FinSA, page 8918 and 8967). The requirement that all client advisers would have been obliged to register in the register of advisers proposed in the consultation draft of the FinSA (*see* article 29 of the consultation draft) has been dropped after criticism during the consultation process.

The Federal Council may exempt certain foreign client advisers from the scope of the registration duty (article 28 (2) FinSA). According to the current proposal, the exemption applies only to client advisers of prudentially supervised foreign financial service providers that are members of a financial group which is subject to consolidated supervision of FINMA if they provide their services in Switzerland exclusively to professional clients (including institutional clients) (article 31 of the draft Financial Services Ordinance (Draft-FinSO)). The scope of the proposed exemption is, thus, very limited. Most foreign institutions are not eligible for the exemption because they are not under FINMA's consolidated supervision and, thus, will need to ensure that their client advisers who provide financial services on a cross-border basis will be registered in the Swiss register of advisers. According to the explanatory report, the Federal Council does not intend to extend the exemption in the absence of reciprocity by the European Union (*see* Explanatory Report of the Federal Council dated 24 October 2018 (Explanatory Report), page 31).

3) Requirements for Registration

Client advisers will only be registered in the register if they meet the conditions of article 29 FinSA. According to this provision, they must prove that they have sufficient knowledge of the rules of conduct set out by the FinSA and the necessary expertise to perform their duties, that they have adequate insurance coverage or equivalent financial guarantees and that they in their capacity as a financial service provider or the financial service provider for which they act are affiliated to an ombudsman's office (*see* article 74 FinSA).

The Federal Council proposed that the liability insurance must cover damages resulting from a breach of the statutory obligations set out in the FinSA of at least CHF 500,000 per year and client adviser (article 32 (1) – (3) Draft-FinSO). Additional contractual liabilities to the client can be excluded from the insurance coverage (*see* Explanatory Report, page 31 f.). Alternatively, a financial guarantee in the same amount must be deposited with the consent of the registration body with a Swiss bank. For prudentially supervised foreign financial service providers, a minimum capital equivalent to at least CHF 10 million is considered adequate as a financial surety (article 33 Draft-FinSO). If a client adviser is employed by a financial service provider, the latter can arrange for the insurance coverage or the financial guarantee (article 29 (3) FinSA).

Article 29 (2) FinSA further requires client advisers to prove that they have not seriously breached the rules of conduct in the past by providing an extract from the register of criminal records to the registration body. Client advisers who have been convicted of offenses pursuant to article 89-92 FinSA (*e.g.* by providing false information or withholding material facts in connection with the information duties of article 8 FinSA, seriously violating the duties to assess appropriateness and suitability pursuant to article 14 ff. FinSA or violating the provisions regarding compensations from third parties in article 26 FinSA), article 86 of the Insurance Supervision Act or offences against property will not be entered into the register. This also applies to persons that have been banned from acting in a management capacity of a financial institution or from trading in financial instruments or acting as a client adviser (articles 33 and 33*a* of the Financial Market Supervision Act).

4) Registration Body

The register of advisers will be maintained by one or more privately organized registration bodies, which will have to be licensed by FINMA (article 31 (1) and (2) FinSA). The registration body must have its domicile in Switzerland and must be organized in a way to ensure independence in fulfilling its tasks. For this purpose, the register must implement adequate internal rules to prevent, *inter alia*, conflicts of interests of the persons concerned with the management and an internal control system ensuring compliance with the FinSA and the implementing ordinance (articles 36 ff. Draft-FinSO; Explanatory Report, page 34 f.).

If no privately organized operator is found to maintain the register, the Federal Council will designate a public registration body (article 31 (6) FinSA). According to the dispatch, however, this scenario is unlikely (Dispatch FinSA, page 8969) although no market participant has publicly announced yet that it will apply for being licensed as registration body.

5) Content of the Register

As minimum content, the register entry must include at least the name and the business address of the client adviser, its position within the financial service provider and its fields of activity, information about education and completed trainings, the name of the ombudsman's office to which it is affiliated and the date of the register entry. This basic information allows clients to verify that their client adviser has the required knowledge and skills. In case of a dispute between the financial service provider and the client, the register entry also permits the latter to identify the competent ombudsman to initiate a mediation proceeding pursuant to article 74 ff. FinSA (*see* Dispatch FinSA, page 8968).

6) Maintaining the Register and Notification Duty

The registration body verifies that the requirements for registering a client adviser are met and issues a decree (in the sense of article 5 of the Administrative Procedure Act (APA)) confirming the registration (article 32 (1) FinSA). Registered client advisers and the financial service providers for which they work must notify the registration body of all changes that are relevant for the registration (including outstanding certificates of unpaid debts (*Verlustscheine*), convictions for relevant criminal offences or a ban by FINMA from an activity in the financial industry or similar foreign measures) within 14 days (article 32 (2) FinSA and article 41 Draft-FinSO).

If the registration body becomes aware that the registration requirements are no longer met, it will issue a decree and deregister the respective client adviser from the register (article 31 (4) FinSA). The adviser may consequently no longer engage in activities as a client adviser. The decree of the registration body is subject to appeal to the Federal Administrative Court.

7) Applicable Rules of Procedure and Registration Fees

The procedure for the registration is governed by the APA (article 34 FinSA). If the registration body approves a registration of a client adviser, it is not required to provide a reasoning (article 35 (3) APA). However, if it rejects the registration without providing the applicant the possibility to amend the application, the applicant has a right to be heard (article 30 (1) APA; Dispatch FinSA, page 8970).

To cover the operating expenses, the registration body may charge cost-covering fees in line with the general principles applicable to levy fees by public authorities (article 33 (1) FinSA; Dispatch FinSA, page 8970). The Federal Council proposes a fee of CHF 500-2,500 for an entry into the register. For urgent requests, a 50 percent surcharge may be applied (article 42 (2) Draft-FinSO).

8) Outlook

Overall, the registration duty will affect non-regulated Swiss financial service providers and in particular foreign financial institutions which currently offer financial services or products to Swiss clients based on the current liberal inbound cross-border regime of Switzerland. Going forward, foreign financial service providers will be required to either register their client advisers in the register of advisers or establish a regulated branch or subsidiary in Switzerland.

The scope of the registration duty, however, is not entirely clear yet. It remains to be seen whether certain advisory services provided by foreign financial institutions will be qualified as financial services under the FinSA and, thus, the persons providing such services on a cross-border basis will have to be registered in the register of advisers. It is unclear, for example, whether financial analysts that support a client adviser in a client meeting or foreign based corporate finance experts who advise a company in an IPO in Switzerland will fall in the scope of the new rules.

It is currently expected that FinSA and FinIA, together with their implementing ordinances, will enter into force on 1 January 2020. If this timing holds, client advisers who have to register pursuant to article 28 FinSA will have time until 1 July 2020 to file their application with the registration body (article 95 (2) FinSA), although there is no guarantee that a registration body will be up and running by then.

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FinSA Business Conduct Rules and MiFID II

Reference: CapLaw-2018-62

The following article deals with the differences between the rules of conduct under MiFID II and FinSA. In the first part, the initial situation is described. Subsequently, the individual differences are discussed in more detail. The main differences in regulation can be found in the areas of client segmentation, definition of the service types, appropriateness and suitability test and dealing with retrocessions.

By Peter Sester / Dario Sutter

1) Starting Point – desired equivalence of Swiss Financial Market Regulation

In addition to the creation of a level playing field for financial service providers and the improvement of the competitiveness of the Swiss financial sector, the main objective of the Financial Services Act (FinSA) is to improve customer protection, in particular through the instrument of codes of conduct. The goal of ensuring access to the EU internal market should not be underestimated: the increasing international integration of financial markets forced the European Union to introduce a so-called third-country regime. While under MiFID I, the third-country regulations differed from one Member State to the other, MiFID II created a consistent regulatory framework. Market access for non-EU financial service providers is now equal across all Member States. In doing so, the EU requires either the establishment of a branch in the European Union and compliance with EU legal provisions or that the third country – such as Switzerland - has an equivalent financial market law. The EU is therefore examining whether Switzerland's legal and supervisory framework is comparable to that of the European Union. If the equivalence exists, Swiss financial service providers would get an EU passport and could thus - without the need of establishing a branch - do business across the EU.

Driven by the fact that the access to the European market is of the utmost importance for Swiss financial service providers, Switzerland's regulation of financial markets has changed considerably in recent years and today it offers a completely new architecture adapted to the EU law. This alignment of the Swiss financial market regulation with the EU regulations is carried out through the autonomous reproduction of European law by Switzerland. The autonomous reenactment can be achieved either through the unchanged or almost unchanged adoption of foreign law or through the creation of an equivalent legal framework.

The (only) temporary recognition of the equivalence of the Swiss stock exchange regulation by the EU following the introduction of the Financial Market Infrastructure Act (FMIA) made it once again clear that the access to the EU internal market is crucial for

Swiss financial service providers. This market access would be easiest to achieve via a permanent equivalence recognition, which should now be achieved for the FinSA.

This article deals with the differences regarding the rules of conduct in the Swiss and European regulation. Thereby, the different regulations and definitions of the customer segments and service types are discussed. They are particularly important since they have an impact on the appropriateness and suitability test, which is then discussed in more detail. Furthermore, the differences regarding the treatment of retrocessions between the EU and Switzerland will be discussed.

2) Comparison of the Rules of Conduct according to FinSA and MiFID II

a) Customer Segmentation

Customer segmentation under FinSA and MiFID II is of particular relevance for the application of the Code of Conduct. Basically, both regulations are familiar with the following three types of customers: retail customers, professional customers and institutional clients. Retail customers are referred to as private customers (*Privatkunde*) in Switzerland (see article 4 (1) (a) FinSA), while the EU uses the term retail clients (*Kleinanleger*) (article 4 (1) (11) MiFID II). Retail customers in both jurisdictions are those customers who cannot be classified as professional customers. This group enjoys the highest possible level of protection. The second group consists of professional clients, while the third group is defined by both regulations as institutional customers, whereby this last customer segment is a subset of the second customer group – professional customers. In the EU, institutional clients are called eligible counterparties (see articles 4 (3) and 4 (FINSA) and Annex II (MiFID II)).

Both systems allow customer groups to switch to a higher or lower level of protection if certain conditions are met:

- In both jurisdictions retail customers can demand to be treated as professional clients. According to Annex II, MiFID II such an opt-up is possible if such retail customers (2 out of 3 points have to be fulfilled) (1) conduct an average of 10 trades a year, (2) have at least 500,000 Euros of bankable assets, or (3) have professional financial knowledge of one year or more. In Switzerland, an opt-out (which corresponds to the opt-up as defined by EU regulations) is possible if relevant knowledge is given and the private customer has bankable assets of at least CHF 500,000 or if a client has assets of at least CHF 2 million - whereby the criterion of knowledge is irrelevant. Thus, in contrast to MiFID II, the FinSA does not acknowledge the criterion of the number of investment activities carried out and the qualification as a professional client based solely on available assets is also not recognized by European regulation.

– Pension funds, occupational pension funds, and companies with professional treasury operations, according to article 5 (3) FINSA, are required to be treated as Institutional Clients. This is also possible for Swiss and foreign collective investment schemes (article 5 (4) FinSA).

Furthermore, according to MiFID II as well as to FinSA, there is the possibility for certain customer groups to benefit from the protection of the next lower customer group:

– In Switzerland professional clients who are not institutional clients can be treated as private clients (opt-in) (article 5 (5) FinSA).

– For institutional clients it is possible to switch to the protection level of professional clients (opt-in) (article 5 (6) FinSA).

– According to Annex II MiFID II, professional clients must also be able to benefit from the higher level of protection of the next-lower customer group (opt-down).

b) Definition of the service types

Concerning the segmentation of the different services, there is a difference between the EU and Swiss regulation regarding investment advice and execution-only services. On the other hand, portfolio management is treated similarly in both regulations, but in Switzerland the FinSA uses the term "*Vermögensverwaltung*". In terms of investment advice, MiFID II relies on the criterion of independence regarding specific clients and the FinSA differentiates between whether the advice was given based on a portfolio context or if it was related to a single transaction. Execution-only business relationships are - in contrast to Switzerland - further subdivided across the EU by differentiating between complex and non-complex financial instruments.

c) Appropriateness and Suitability of Financial Services

The primary objective of both MiFID II and FinSA is to improve customer protection, which is achieved through the means of assessing appropriateness and suitability. First of all, both article 10 FinSA and article 25 MiFID II require financial service providers to carry out appropriateness and suitability assessments.

The appropriateness test regulated in article 11 FinSA refers to individual transactions carried out by the financial service providers and does not take into account the entire customer portfolio. In this purely transactional investment advice the examination of the appropriateness with regard to the investment objectives and the financial circumstances of the customer are eliminated; it is only checked whether the financial instrument is appropriate with regard to the knowledge and experience of the client. In doing so, the client advisor must inform himself about the knowledge and experience of the customer and check whether the recommended financial instruments are appropriate for the corresponding clientele. MiFID II does not recognize such a distinction, but always requires the full assessment of appropriateness and suitability in investment advice.

However, if a holistic investment advice or asset management service related to the client's portfolio is provided, the suitability must be examined, part of which is the appropriateness test. In addition to the appropriateness test, however, the financial circumstances and investment objectives of the customer must also be taken into account in order to identify the suitability. The suitability test (article 12 FinSA) refers to investment advice taking into account the whole customer portfolio or the asset management in general. Hereby, the financial service provider should inquire about the financial circumstances and investment objectives as well as the knowledge and experience of the customer.

Moreover, article 13 FinSA regulates the exemptions from the obligation to prove suitability and appropriateness. For example, in the case of mere execution or submission of customer orders (*i.e.*, execution-only), no appropriateness or suitability test must be carried out. According to paragraph 2, the client has to be informed that no such examination has been carried out. In contrast to the FinSA, MiFID II makes an additional distinction in article 25 (4) and assumes that the appropriateness test can only be skipped if it concerns non-complex financial instruments such as equities.

d) Treatment of Retrocessions

Article 17 FinSA establishes the principle of good faith in the processing of customer orders. In addition, the financial service provider must ensure that clients' orders are executed in a manner that achieves the best possible result. From a financial point of view, not only the price of the financial instrument, but also the costs incurred by its execution and the compensation of third parties (*e.g.,* retrocessions) must be taken into account. The acceptance of such third-party compensation is governed by article 26 FinSA; specifically, they must either be passed on completely to the customer, unless the customer having all relevant information willingly gives up his respective rights. While the FinSA, taking into account the case law of the Swiss Supreme Court, allows the receipt and retention of retrocessions under certain conditions, the requirements under MiFID II are so strict that withholding of retrocessions by financial service providers seems virtually impossible. MiFID II basically prohibits any retention of retrocessions. The only exception - depending on the type of service – would be if the retrocessions are non-monetary as well as insignificant or service quality improving (see article 24 MiFID II). However, it would be extremely difficult for financial service providers to bring the proof of evidence.

3) Conclusion

In view of the above stated differences, it remains questionable whether the parliament's changes to the MiFID II-compliant draft will ultimately result in a non-compliant final version of the regulation. However, only full compliance with the EU law would lead to the recognition of the Swiss regulation by the EU and, therefore, to direct access to the EU internal market for Swiss service providers. This market access would lead to the fact that Swiss service providers would not need to deal with various different regulations, thus reducing the total costs of being compliant. Nonetheless, it is important for the Swiss financial sector, that EU regulations are only adapted to the level which is required by the European Union in order to receive equivalence acceptance and not beyond. Introducing an even stricter regulation than the one of the EU would only lead to a discrimination of Swiss financial service providers compared to those of the EU. It should also be noted that the FinSA regulation affects service providers that do not serve EU customers. In any case, institutions serving EU clients are expected to be MiFID-compliant since the Lugano Convention allows EEA clients to denounce a MiFID II infringement in a national court. Due to this fact, most of such financial service providers have already implemented EU-compliant business policies. A pragmatic solution would therefore be that the Swiss legislator not only accepts compliance with FinSA, but also with the more stringent MiFID II rules - in a way a reverse equivalence recognition. While this would allow the FinSA to be less restrictive and non-EU-serving institutions to not bother with stricter EU-equivalent regulation, it is important not to forget that customer protection is also an important topic within the Swiss financial industry.

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Funds Distribution under FinSA/FinIA: A change of paradigm

Reference: CapLaw-2018-63

The introduction of the concept of an "offer" according to Art. 3 let. g FinSA as a replacement of the current notion of a "distribution" pursuant to Art. 3 CISA will lead to a number of consequences for the Swiss financial industry as well as for foreign financial services providers acting on a cross-border basis into Switzerland. The new concept is more flexible as the current notion of a "distribution", but also raises a number of delicate questions which need to be clarified. The object of this article is to provide a first analysis of the salient features and challenges of the current and future regimes and their practical consequences with a specific focus on the placement of collective investment schemes in Switzerland.

By Diana Imbach / François Rayroux

1) Introduction

a) The new financial market law architecture

With the new Financial Services Act (FinSA) and the Financial Institutions Act (FinIA), the existing financial market law architecture will be subject to sweeping reforms. Today, financial market regulation has a primarily sectoral structure. Thus, the provisions governing the management and distribution of collective investment schemes are primarily governed by the Collective Investment Schemes Act (CISA) and its implementing ordinances, FINMA Circulars and SFAMA self-regulation. With the FinSA and the FinIA, the current regulatory framework will be transformed into a horizontal structure. This means, in particular, that the FinSA will introduce, among other things, uniform cross-sector regulations for the provision of financial services and the offering of financial instruments.

b) Impact of the legal framework on collective investment schemes

Today, the CISA governs three different areas: (1) the authorization and supervision of financial institutions, (2) the licensing of collective investment schemes (product licensing), and (3) the distribution of collective investment schemes.

With the new financial market law's architecture, the authorization and supervision of fund management companies and asset managers of collective investment schemes will be regulated exclusively in the FinIA. Most of the corresponding provisions are to be "transferred" unchanged in its substance from the CISA. The product licensing requirements are solely applicable to collective investment schemes and will therefore remain in the CISA. However, the requirement to obtain a product license for foreign collective investment schemes is closely related to the question whether the specific fund will be offered to non-qualified investors in Switzerland. As the distribution – respectively the offering of collective investment schemes – and the corresponding rules of conduct will be regulated comprehensively in the FinSA, there is a close link between the two areas of regulation. Consequently, the current distribution concept in CISA will be abandoned in favor of the concept of an "offer". Furthermore, the current authorization requirement for distribution activities (fund distributor license) will be abolished in the CISA. As the FinSA governs the rules of conduct applicable at the point of sale in general, the corresponding provisions in the CISA (Art. 10, Art. 20 et seqq. CISA) will be limited to product-specific aspects. The same applies in principle to the product documentation, *i.e.*, the obligation to publish a prospectus and the requirement to provide for a Key Information Document (KID) for private clients. However, all product-specific regulations, such as the regulations for SICAVs, SICAFs, limited partnerships for collective investments or the obligation to appoint Swiss representatives and paying agents, will remain to be governed by CISA in the future.

c) Challenges

As the offering of collective investment schemes to non-qualified investors is intrinsically tied to the provisions in the FinSA, it was the intent of the legislator that the provisions of the FinSA and of the CISA, as well as the respective ordinances (*i.e.,* the Financial Services Ordinance (currently in draft form, Draft-FinSO) and the Collective Investment Scheme Ordinance (CISO)), be carefully coordinated. In this context, the particular challenge is to transfer and embed the product-specific obligations for the offering of collective investment schemes into the new concepts introduced by the FinSA and thereby to ensure an equivalent, but different, concept for the purposes of the protection of the investors. The legislator's intent was not to reshape the entire legislative framework based on a one-sided reduction of the investors' protection on the side of the CISA, but to implement a new balanced and consistent concept in the FinSA and Draft-FinSO. An illustration of this approach is the abolition of the authorization regime for fund distributors which, in the opinion of the legislator, is to be compensated by the new prudential supervision over all asset managers in the FinIA, on the one hand, and by the registration requirement for client advisors provided for in the FinSA, on the other hand (see Dispatch FinSa/FinIA, BBl 2015 8901 et seqq, page 9010 (German version), page 9050). A one-sided levelling down of customer protection in the fund area would in our view contradict the legislator's intent and moreover contradict international developments.

2) From "Distribution" to "Offer" of Collective Investment Schemes

a) Current Legal Framework

i. Notion of "distribution"

With the revised Collective Investment Scheme Act of September 28, 2012, which entered into force in 2013, the historical concept of a "public solicitation" (*"öffentliche Werbung"/"appel au public"*) has been replaced by the notion of "distribution" (*"Vertrieb"/"distribution"*) (see Dispatch CISA, BBl 2012 3639 et seqq., page 3647 (German version). The concept of a "public solicitation" was not only fundamental for the Investment Funds Acts of 1966 and 1995 as well as for the Collective Investment Schemes Act before its revised version of 2012, but it is also a basic principle for the offer of securities under the Swiss Code of Obligations (CO). The origin of this change of paradigm was a Swiss Supreme Court Ruling, dated February 10, 2011, resolving that FINMA's interpretation, pursuant to which there was no "public solicitation" as long as the offer was exclusively directed towards qualified investors, was not supported by the text and historical interpretation of the former Art. 3 CISA (BGE 137 II 284, 291 consideration 5.1 et seqq.). In the view of FINMA and of the authors of the Federal Council's supporting dispatch, this ruling triggered a legal uncertainty. For this reason, the legislator replaced the principle-based test of a "public solicitation", whose combination of numerical and qualitative criteria by taking into consideration the circumstances of each case had allowed a flexible regulation, by the more narrow principle of the "distribution".

The new, more restrictive test of a "distribution" pursuant to Art. 3 CISA is based on one single criterion, covering any offer or marketing of collective investment schemes which is not exclusively directed to prudentially supervised financial intermediaries, such as banks, securities dealers, fund management companies and asset managers of collective investment schemes, central banks as well as supervised insurance companies, without any numerical or qualitative factor, which would allow taking into consideration the circumstances of each case. Moreover, all exemptions to the notion of a "distribution" are enumerated in an exhaustive manner in the CISA. As a result, a simple reference to a collective investment scheme, such as in a press article, even without intent to distribute, such as in the context of a conference or of an article, would constitute a distribution, if not otherwise covered by exemption provided for within the meaning of Art. 3 CISA.

More specifically, the concept of a "distribution" has also been extended to include the offer or marketing of funds to so-called non supervised qualified investors, *i.e.*, all qualified investors according to Art. 10 CISA who are not prudentially supervised, such as pension funds or corporates with a professional treasury management. By contrast, this category of investors was under the "public solicitation test" characterized as "institutional investors" and considered not to form part of the "public" in application of the qualitative criteria under the CISA's previous "public solicitation test". The notion of a "distribution" has been further defined by FINMA Circular 2013/9. As a result, so-called "independent asset managers", which are not expressly included by the CISA as qualified investors, may, subject to certain conditions, be treated as non-supervised qualified investors pursuant to Art. 10 CISA if their clients are qualified investors.

ii. Consequences of a "distribution"

The notion of distribution according to Art. 3 CISA triggers the following consequences: (1) Distributors of Swiss or foreign collective investment schemes require FINMA authorization, provided none of the specific exemption applies; (2) on the level of the product, a distribution of foreign funds to non-qualified investors requires additionally a prior FINMA approval for each fund according to Art. 120 para. 1 CISA; (3) moreover, the distribution of foreign funds triggers the obligation to appoint a Swiss representative and a paying agent, the former being the gatekeeper for compliance with Swiss regulatory provisions. With the revision of the CISA in 2012, this obligation has been extended to the distribution of foreign funds to all investors, qualified investors as well; and (4) finally, the specific conduct rules under Art. 20 et seqq. CISA apply. This includes, in particular, an enhanced information duty within the meaning of Art. 20 para. 1 let. c CISA as well as Art. 34 CISO. Compliance with these conduct rules, also by foreign distributors, is ensured by distribution agreements and respective requirements to monitor and audit distributors.

Furthermore, the concept of a "distribution" is of essence in the context of the placement of structured products in Switzerland and serves also as an element to distinguish a Swiss collective investment scheme, subject to the supervision of FINMA, from internal collective pools of assets, which was already the case before the revision of CISA in 2012.

iii. Exemptions to the concept of a "distribution"

As an exception to the broad concept of a "distribution", the CISA describes exhaustively in Art. 3 para. 1 and 2 CISA those actions and circumstances, which do not constitute an "offer" or "marketing" within the meaning of Art. 3 para. 1 CISA in relation to Art. 3 para. 1 and 5 CISO. This applies most importantly to offers and marketing to supervised financial intermediaries and insurance companies within the meaning of Art. 10 para. 3 let. a and b CISA as well as Art. 3 para. 4 CISO. With this exemption, the legislator intended to continue allowing Swiss banks and insurance companies to offer without restrictions funds offered by foreign promoters.

With a similar intent to safeguard the traditional private banking activity based on the rules provided for under the 1996 Investment Funds Act and under CISA before its revision of 2012, the legislator has also carved out from the notion of a "distribution" the provision of information as well as the placement of collective investment schemes in the context of discretionary asset management agreements (Art. 3 para. 2 let. b-c CISA). This exception was extended to independent asset managers, provided that those independent asset managers have adhered to rules of conduct within the meaning of Art. 3 para. 2 let. c CISA and meet other additional requirements.

As provided for in many foreign jurisdictions, information in relation to collective investment schemes as well as to the placement of collective investment schemes in the context of so-called "execution only transactions" are carved out from the concept of a distribution (Art. 3 para. 2 let. a CISA und Art. 3 para. 2 let. b CISO). It has to be noted that this includes not only circumstances where there is an execution only transaction, but also circumstances of so-called "reverse solicitation" (or "reverse inquiry"), which were not considered to constitute a distribution activity. Similarly, in light of the restrictive nature of the "distribution" test, during its debates the Swiss Parliament has also introduced an exemption to a "distribution" within the meaning of Art. 3 CISA, allowing the offer of information as well as the placement of collective investment schemes within the context of written and remunerated advisory agreements.

Finally, the publication of prices, NAVs and tax information by supervised financial intermediaries are also expressly carved out as not constituting a distribution (Art.

3 para. 2 let. d CISA). There is also a carve-out for the offer of employee benefit schemes to employees within the restrictive conditions of Art. 3 para. 2 let. e CISA and Art. 3 para. 6 CISO in a consistent manner to the long-standing FINMA practice.

iv. Assessment of the concept of a "distribution"

The test of a "distribution", which is based on the sole trigger of the existence of an offer or marketing of a fund, can only be applied in practice as a result of a series of exemptions expressly provided for in the CISA. A number of those exemptions had to be introduced by the Swiss Parliament in the context of the parliamentary debates and, therefore, given the "last minute nature" of certain of these amendments, lack thorough and conceptual systematics. While the new system is now widely implemented in the Swiss market practice, this change of paradigm has raised a multitude of questions. Indeed, the test has shown to be very restrictive and not taking into account many circumstances on which distribution activities were traditionally based. It still results in a rather inflexible and restrictive system that lacks comparable concepts in other foreign jurisdictions, including in the European Union. As a final note, it is to be mentioned that it was not an element required to be implemented under the so-called "third country rules" imposed by AIFMD in view of a potential recognition of CISA as an equivalent jurisdiction and which ultimately was the trigger for the 2012 revision of the CISA.

b) The new concept of an offer of collective investment schemes

i. Legal Framework

The legislator has resolved to implement, among all categories of financial services providers and, furthermore, across all types of financial products, to the extent possible, the principle of a "level playing field". As a consequence, the specific test of a "distribution" introduced in the context of the 2012 revision of the CISA will be replaced by what the Dispatch of the Federal Council refers to the more general rule of an *offer*. The reference to a "distribution" in today's context of Art. 3 CISA will be replaced by a reference to the "offer" as defined in Art. 3 let. g and h FinSA. As a further consequence, the obligation to obtain an authorization from FINMA as a distributor of investment funds will be abolished . Furthermore, the entire system of express legal exemptions to the concept of a "distribution" under Art. 3 para. 2 CISA, as well as the detailed and exhaustive catalogue of exemptions, is replaced in its entirety by the new concept of an "offer" of collective investment schemes. An important aspect in this regard is further the definition of *financial services* according to Art. 3 let. c FinSA. Similarly, various references in the CISA and the CISO to a "distribution" shall be replaced by the one of an "offer", most importantly in Art. 120 CISA relating to the obligation for foreign funds to be approved by FINMA before an offer is made to non-qualified investors. The Federal Department of Finance (FDF) has further specified the concept of an offer in Art. 3 para. 3 Draft-FinSO.

ii. Notion of an "offer"

During the parliamentary debates, the notion of an offer has been expressly specified as one which has to be specific, meaning formulated in such a manner that it can be accepted or refused immediately by the investors. Within this line of argument, an offer has necessarily to contain all essential aspects of the future agreement between the investor and the financial services provider. By contrast, a more general communication, which still has to be specified and cannot be accepted as such, is not a relevant "offer" within the meaning of the FinSA (Votum Guillaume Barazzone AB 2017 N 1310/BO 2017 N 1310). Since the notion of a "public offer" according to Art. 3 let. h FinIA only triggers limited legal consequences in the field of the offer of collective investment schemes, it will not be further addressed below.

The concept of an offer pursuant to Art. 3 let. g FinSA is not the one of the historical principle of a "public solicitation", which was fundamental for the Investment Funds Acts of 1966 and 1995 as well as for the Collective Investment Schemes Act before its revised version of 2012. In the first instance it has to be interpreted based on the general principles of Art. 3 CO. However, the notion of an "offer" pursuant to Art. 3 let. g FinSA goes beyond the one of Art. 3 CO, as the FDF in its explanatory report expressly states that such an offer also includes a so-called invitation to formulate an offer (*Einladung zur Offertstellung/invitation à presenter une offre*), which in turn has to be accepted or refused by the financial services provider.

Whether an offer within the meaning of Art. 3 let. g and h FinSA as well as Art. 3 para. 3 and 4 Draft-FinSO exists in a specific case has to be determined based on the circumstances at hand and in particular on the structure and content of the relevant communication. The assessment as to the existence of an offer is always to be made based on whether or not a general member of the public can in good faith understand that the communication is a proposal to enter into an agreement in respect of a specific financial instrument.

The explanatory report of the FDF specifies in this context on page 20 that, if potential customers are made aware of financial instruments at advertising events and if said financial instruments can be purchased at the event itself or subsequently from any financial services provider with a simple acceptance or offer, it can be concluded that a prior offer to provide a financial service has been provided. In our view, this presupposes a causal link between the communication at the event and the conclusion of the financial contract and, moreover, that during the event, all details which are necessary are conveyed. The situation would in our view be different if, at such events, only a strategy or some of the characteristics, but not all key elements, are presented. This may however presuppose that no remuneration is paid to the organizers of the events which would be performance driven and, for example, depend on the commercial success of the event, as this may suggest that there is still a causal link between the sales event and the conclusion of the financial contract. In such a case, however, the new rules on advertisement for financial instruments according to Art. 68 FinSA and Art. 95 Draft-FinSO are likely to apply.

Furthermore, as an offer is always based on the direct or indirect intent of the financial services provider to trigger with the investor an investment decision (*i.e.*, the reason why its content has to be so specific to contain all essential elements of the future contractual relationship with the investor), we are of the opinion that analytical presentations, or research reports, or scientific contributions, should not be in scope of the concept of an offer if they are not published with the intent to specifically sell a financial product. In this context, clear communications, for example in the form of disclaimers, as to the absence of any intent to sell a specific financial instrument, may have to be published in order to exclude that a communication can be understood as an offer.

The notion of an "offer" is neutral in terms of technology and these principles should apply *mutatis mutandis* to platforms. If those platforms contain all key elements for an investor to take an investment decision, or if their content is a so-called invitation to formulate an offer, their content may constitute an offer within the meaning of Art. 3 let. g FinSA. We assume that this condition should always be met if investors have the possibility to subscribe on-line, as this presupposes that they receive all the relevant information for their investment decisions. In this context, it should, based on the report of the FDF, not be relevant whether this subscription is made directly with the platform or with another financial intermediary, but caused as a result of the consultation of the platform (see Explanatory Report, page 20). The situation is different if the platform contains information, which is as such not sufficient for the investor to take an investment decision, in which case the new rules on advertisement for financial instruments will apply. As such, the new concept of an "offer" seems to clearly be more flexible than the one of a "distribution", therefore, the reference made by the FDF to the current more restrictive FINMA Circular 2013/9 on the distribution of collective investment schemes seems not to be in line with the intent of the legislator (see Explanatory Report, page 21).

Neither the FinIA nor the FinIO provide, by contrast to what applies in the context of a distribution pursuant to Art. 3, para. 2 CISA, for an express exemption, confirming that there is never an offer on the part of a financial intermediary in case of a specific reverse solicitation by an investor, based on the latter's own initiative, including when the specific conditions of an execution only transaction are not met. The *reverse solicitation* rules provided for in Art. 2 para. 2 Draft-FinSO only relate to a reverse solicitation in relation to financial services and, moreover, only in a cross-border context. We assume that the reverse solicitation-exemption implicitly also applies under FinSA (see also M. Andreas Josuran/Vanessa Isler, Änderungen beim Vertrieb kollektiver Kapitalanlagen unter dem FIDLEG/FINIG, GesKR 2016, page 205, 209 (hereafter Josuran/

Isler)). However we consider that such a clarification in the context of the offering of financial instruments within Switzerland, in line with the current Art. 3 para. 2 CISA, would be helpful in Art. 3 Draft-FinSO, in particular to clarify the application or not of the new offer rules.

This being said, the legislator has expressly provided for a negative catalogue which may serve as guidance and specify a number of non-exhaustive circumstances which exclude the existence of an offer within the meaning of Art. 3 let. h FinSA. These circumstances include a simple reference to financial instruments, such as a reference to their ISIN codes, or the NAVs of collective investment schemes, the provision of factual information as well as any publication linked to legally imposed communication, including corporate communications (Art. 3 para. 5 Draft-FinSO). Within this line of idea, the publication of information on collective investment schemes as required pursuant to Swiss or foreign legal obligations, including the changes of investment policies, risk profiles, cost structures, etc., should not be deemed to be an offer.

In summary, the narrow definition of an "offer", which has to be formulated in such a manner that it can be accepted or refused immediately by the investors, provides in many instances for much more flexibility than the one of a "distribution" pursuant to Art. 3 CISA. The concept of an "offer" pursuant to Art. 3 let. g FinSA can however not be analyzed without considering certain delimitations and a reference to the two new other concepts introduced by the FinSA, the concept of "advertisement" (*Werbung/ publicité*) for financial instruments and, in particular, the concept of "financial services" within the meaning of Art. 3 let. c FinSA.

iii. Delimitations

(1) Offer vs. advertisement

The FinSA introduces in Art. 68 specific regulations regarding the advertisement for financial instruments. So far, the only regulations under the Swiss law on financial instruments governing marketing and advertisement are laid down in the definition of a "distribution" pursuant to the current Art. 3 CISA, *i.e.*, its definition as any marketing or offer of funds. Art. 95 Draft-FinSO further defines the concept of "advertisement" as any communication relating to financial instruments whose content aims at drawing the attention of investors to such financial instruments. Advertisement has to be specifically declared.

At this stage, there seems to be a lack of clarity as to the precise meaning of "advertisement" and, in particular, its delimitation to an "offer" and also to circumstances where there is also a "financial service". Interestingly, while nothing in the parliamentary debates or the provisions of the FinSA would confirm this, the FDF seems to define the concept of "advertisement" by reference to the current FINMA Circular 2013/9

"Distribution of collective investment schemes", which is expected to be abolished with the entry into effect of FinSA (see Explanatory Report, page 62). As a consequence, it would appear that the notion of "advertisement" will in the view of the FDF in substance be in line with the one of the current notion of a distribution pursuant to Art. 3 CISA. To the extent that the legislator wanted to abolish the current concept of a "distribution" pursuant to Art. 3 CISA, it would in our view be necessary to provide for a new and autonomous interpretation of the concept of "advertisement", but not only by reference to the narrow and rigid principle of a "distribution" pursuant to Art. 3 CISA.

Art. 95 para. 3 Draft-FinSO expressly specifies that advertisement may not be addressed to investors who are not eligible for an investment in the specific financial instrument, as this would be contrary to the provision of Art. 3 para. 2 let. b of the Swiss Federal Law on Unfair Competition. This implies in our view, based on the principle *e maiore minus*, that no advertisement can be made for a collective investment scheme to any investor who would not be eligible for an offer of such an investment, *i.e.*, mainly in case of an offer to non-qualified investors of a fund which has not been previously registered with FINMA or appointed a representative and a paying agent pursuant to Art. 120 CISA. The text of Art. 95 para. 3 Draft-FinSO should be further clarified to this effect. This restriction seems to be in line with the intent of the legislator, but is in practice only relevant with respect to advertisement made for foreign collective investment schemes. Thus it would make sense to specify this reservation in the CISO, rather than in Art. 95 para. 3 Draft-FinSO which has a more general application. This clarification is particularly important with regard to funds bought in the context of an asset management agreement.

(2) Offer vs. Financial Services

Shares or units in collective investment schemes are financial instruments pursuant to Art. 3 let. a cipher 3 FinSA. An "offer" of financial instruments and, hence, of collective investment schemes pursuant to Art. 3 let. g FinSA is, however, not *per se* a financial service within the meaning of Art. 3 let. c cipher 1 to 5 FinSA. An offer can, depending on the circumstances, be made outside the context of any financial service or alternatively be formulated in conjunction with such financial service pursuant to Art. 3 let. C cipher 1 to 5 FinSA. Unfortunately, an explicit link was not established between the two terms in the FinSA (see also Sandro Abegglen/Yannick Wettstein, Zum Anbieten kollektiver Kapitalanlagen unter dem FIDLEG – und ausgewählte Aspekte der dabei einzuhaltenden Verhaltenspflichten, SZW 2018 page 131, 133). However, the question is how extensive the new Art. 3 para. 1 Draft-FinSO ("any activity which, such as "intermediation", is specifically aimed at the acquisition or disposal of a financial instrument") should be interpreted. This being said, with the now specified Art. 3 para. 1 Draft-FinSO, the question arises, if there will be any cases in practice where an offer does not constitute also a financial service.

Further, it should be analyzed under which circumstances the marketing of collective investment schemes, whether there is an "offer" within the meaning of Art. 3 let. g FinSA or not, may be characterized as a financial service pursuant to Art. 3 let. c FinSA.

Within the context of a discretionary asset management agreement, there is in our view no offer for the transactions thereunder as each investment decision is made by the asset manager based on the discretionary powers conferred to him. There is eventually an offer by the financial services provider towards the asset manager, but the latter will, as a matter of principle, be an institutional investor, hence triggering no further rules of conduct under the FinSA. A general exemption applies with respect to the obligation to provide investors with a KID, while a specific general exemption regarding the prospectus is expected to be granted by FINMA (see Explanatory Report, page 45). Such an exemptions should in any event, by contrast to what is currently referred to by the FDF, be extended to all qualified investors, and not only professional investors.

In the context of an advisory agreement, there may be an offer for each transaction thereunder, but only where a sufficiently detailed recommendation under such advisory agreement is provided, but not where the investor has requested himself a financial instrument. Similarly, there will be a separate financial service in the context only if a specific advice is given, but not when there is a general recommendation or even a reverse solicitation by the investor. However, the consequences of a potential offer are mitigated by a series of exemptions, such as the categorization of the clients as "qualified investors", which aim at not introducing any additional burden or limitation within the context of such advisory agreements as compared to the current legal framework of Art. 3 CISA, in particular as to the obligation to register collective investment schemes with FINMA or to mandate a Swiss representative or paying agent and as to the obligation to establish and hand over a prospectus and a KID.

An offer may in practice be in many cases linked to a transfer of an order or a purchase or sale of a financial instrument, both circumstances characterized by Art. 3 lit c FinSA as a "financial service". In this case, the crucial question is the meaning which shall be given to the concept of a purchase or sale of a financial instrument pursuant to Art. 3 lit. c cipher 1 FinSA. In this respect, the report of the FDF expressly clarifies, in line with what seems to be the intent of the legislator expressed in the Dispatch of the Federal Council, that the term of a "purchase" or "sale" of financial instruments pursuant to Art. 3 let. c cipher 1 FinSA goes beyond circumstances where there is an effective purchase or sale of a financial instrument and that this concept also includes any activity in relation thereto, such as any other action which specifically aims at the purchase or sale of a financial instrument; the FDF refers in this context to any "intermediation", which also covers circumstances where no advice is given to the client, whether transaction-based or in a general form (see Art. 3 para 1 Draft-FinSO and Explanatory Report, page 18).

iv. Consequences of the new concept

The abolition of the concept of a "distribution", with its complicated system of legal exemptions, lacking any systematic or logic character, is rendered obsolete with the introduction of the new concept of an "offer" pursuant to Art. 3 let. g FinSA. The FinSA has yet to introduce another system with a series of exemptions, aiming at ensuring the implementation of the express intent of the legislator which was that no further restrictions should, as a matter of practice, be imposed in the specific context of an offer of financial instruments, and in particular of collective investment schemes, into the Swiss financial services framework.

An offer of collective investment schemes will trigger the obligation to register the funds with FINMA pursuant to Art. 120 CISA, but only where such offer is made to non-qualified investors, and as a consequence the obligation to appoint a Swiss representative and paying agent. In this respect, the current registration obligation which was historically provided for in the CISA will remain substantially unchanged, except that due to the more flexible nature of an "offer" as opposed to a "distribution" pursuant to the current Art. 3 CISA, the circumstances where registration of a foreign fund with FINMA is required may in practice be more limited. Similarly, the obligation to appoint a representative will be limited under the new system to an offer to non-qualified investors as well as to so-called opt-in qualified investors (Art. 120 CISA in conj. with Art. 5 para. 1 FinSA). An offer to *per se* qualified investors will, by contrast to the current system introduced by the 2012 revision, no longer require the appointment of a Swiss representative and paying agent, as this does not constitute a distribution anymore.

Wherever the CISA provides in its current version for express legal exemptions, pursuant to which there is no "distribution", mainly within the context of discretionary asset management agreements or long-term advisory agreements, the FinSA will define the relevant investors as "qualified investors" in order to obviate the requirement to register the fund with FINMA pursuant to Art. 120 CISA More specifically, if there is an offer within the context of an advisory agreement, there is a general exemption to appoint a Swiss representative and paying agent, even though an advisory agreement can also be entered into by private clients (see Art. 129a CISO in its revised version).

The obligation currently provided for by CISA to obtain authorization as distributor of collective investment schemes will be replaced by the obligation to register with the Client Advisors Register according to Art. 28 FinSA, but only where an offer is linked to the provision of financial services pursuant to Art. 3 let. c FinSA and, furthermore, if no exemption to the registration obligation according to Art. 31 Draft-FinSO applies.

The foregoing shows the intent of the legislator to compensate the narrower concept of an "offer" as compared to a distribution with the new concept of "financial services", triggering specific rules of conduct under the FinSA and the duty to register with the

Client Advisors Register, thereby namely replacing the authorization regime for distributors pursuant to Art. 19 and the specific rules of conduct provided for in Art. 20 of the current version of the CISA (see also Josuran/Isler, page 207). Against this background, it seems consistent that there is no room for a restrictive interpretation of the new concept of "purchase" or "sale" of financial instruments pursuant to Art. 3 let. c cipher 1 FinSA, in particular if one intends to limit its scope of application to an effective transfer of the financial instrument.

There is however in our view room for a further specification of the notion of an "intermediation" which, according to the FDF, should be covered by the term of a "purchase or sale" of financial instruments pursuant to Art. 3 let. c cipher 1 FinSA (see Explanatory Report, page 18). Such an intermediation has to specifically aim at the purchase or sale of a financial instrument by an investor. This seems in our view namely to imply that an "intermediation" as a rule directly aims at an end investor. As a result, this excludes many circumstances arising in the context of a classical third party fund distribution activity towards other supervised financial intermediaries. Should such supervised financial intermediaries be contacted to act as end investors, such as in the context of a fund-of-funds structures, there would be an intermediation, but the FinIA rules of conduct would not apply based on the exemption according to Art. 20 para. 1 FinSA. An "intermediation" in our view further presupposes that its author has directly or indirectly an economical interest therein, either because he intermediates his own funds or is directly or indirectly remunerated to this effect. The existence of a "delegation arrangement" between the author of the intermediation and a Swiss or foreign financial services provider may also be relevant, but always provided that either the "intermediary" or the Swiss or foreign financial services provider, which has appointed the intermediary, has contact with the end investors. In such cases the provisions of Art. 23 FinSA, regulating the involvement of third parties, may also be relevant. Finally, as already indicated, we are of the view that, if an intermediary organizes an advertising event regarding a financial instrument, which can be purchased subsequently from another financial service provider, a direct causal link between an offer and a subsequent purchase or sale of a fund must exist before one can conclude that there is an offer for a financial service by the intermediary within the meaning of Art. 3 let. c, cipher a FinIA, as the Explanatory report of the FDF specifies on page 20.

The definition of an "intermediation" covered by Art. 3 let. c cipher 1 FinSA may need further reflection and debate which cannot be covered in this article. That being said, we are of the view that potential issues in practice will arise as a result of a few rules of conduct or organizational requirements, mainly the transparency obligations in relation to retrocessions pursuant to Art. 26 FinIA. In particular the obligation to transfer retrocessions to a client pursuant to Art. 26 para. 1 let. b FinIA can only exist in our view where a contractual link exists between the financial services provider and an end investor providing also for a claim as a matter of civil law for the benefit of the investor, including in case of an execution only transaction, but not if there is no contractual relationship between the author of an "intermediation" and the end investor. There is in other words, if at all, rather a need to clarify or limit some organization requirements in this context, rather than to narrow the concept of a purchase or sale under Art. 3 let. c cipher 1 FinSA, thereby creating potential loopholes in the investors' protection. Indeed, one would in this case have to conclude that there is no "financial service" which will in turn lead to the disapplication of the investors' protection under the FinSA in a number of cases where the legislator wanted to compensate the current protection under the CISA which is to be abolished. Such disapplication would also be inconsistent with international developments, in particular with regard to retail clients. In this regard an outcome based approach is important. Particularly with regard to the regulation in the EU, where besides the regulations in MiFID also product-specific provisions in AIFMD and UCITS have to be taken into account.

3) Comparison and Assessment

The FinSA and the relating amendments of the CISA introduce a new concept of investor's protection based on the notion of an "offer" which is based on different levels of legislative intervention, both in the FinSA and the CISA, by contrast to the current system based on Art. 3 CISA. The latter triggers as a consequence of one single test (1) the rules of conduct under the CISA, (2) the obligation to register a fund with FINMA pursuant to Art. 120 CISA, where the distribution is made to non-qualified investors, (3) the obligation to appoint a Swiss representative and paying agent as well as (4) the obligation to obtain authorization as distributor, provided no exemption applies.

By contrast, the FinSA introduces different levels of legislative intervention, *i.e.*, three tests, meaning consequences linked to (1) an "offer" pursuant to Art. 3 let. g FinSA, other consequences linked to (2) the existence of a financial service pursuant to Art. 3 let. a cipher 3 FinSA (mainly the rules of conduct, where applicable) and (3) obligations triggered by the existence of advertisement within the meaning of Art. 68 FinSA and Art. 95 Draft-FinSO. With the draft of the Draft-FinSO, the link between these three tests has been clarified further.

The concept of financial services is central to the question of the applicability of the FinSA, in particular, with regard to the duties of conduct and organization as well as the obligation to register as a client advisor. Art. 3 let. c FinSA defines which activities will be regarded as financial services in the future. It has already been pointed out in the Dispatch of the Federal Council that "classical" fund distribution - outside of an advisory or asset management agreement - must also qualify as a financial service (see Dispatch FinSa/FinIA, page 8922, 9010, 9050). Unfortunately, the Federal Counsel has not further specified under which of the activities mentioned in Art. 3 let. c FinSA it should qualify. This has led to discussions whether the distribution of funds will no longer be regulated, *i.e.*, not be covered at all by the conduct rules and the obligation to register as a client advisor according to FinSA. This has now been clarified in Art. 3 para. 1 Draft-FinSO, making it clear that the acquisition or sale of a financial instrument according to Art. 3 let. c cipher 1 is to be understood in such a way that it also covers the classical fund distribution.

It is debatable whether the wording chosen in the Draft-FinSO is perfect or could be further specified. However, the outcome is, as a matter of principle, in accordance with the intention of the legislator. Also from the perspective of the fund industry, it is crucial to close potential loopholes in the new regulation, without reintroducing the obsolete concept of a "distribution" pursuant to Art. 3 CISA, mainly for the following reason: with the introduction of the new conduct rules for financial services providers at the point of sale and the corresponding registration obligation in the FinSA, the "point of sale"-specific conduct rules in Art. 20 and the distributor license in the CISA were deliberately abolished. This also only makes sense if "classical" fund distribution, which typically does not yet have the quality of transaction-based advice, qualifies as a financial service according to FinSA. This corresponds to the intention of the legislator and must also be seen in the light of the large number of rules where more flexibility has been introduced in the course of the legislative process, such as the abolition of the obligation to appoint a representative, being the gatekeeper for compliance with Swiss regulatory provisions today, for "per se" qualified investors or to contractually structure any fund distribution based on formal distribution agreements, thereby reinforcing the supervision of the distribution networks in the interest of the investors protection.

To conclude, the interaction of three different tests in our view adequately ensures the investors' protection, depending on the need of such a protection, depending on whether the investor is a private investor, a professional investor or an institutional investor. As a result, the new regulatory framework introduced by FinSA, and in particular as a result of the introduction of the new concept of an offer, favorably compares to the current regime which is based, for the purpose of the regulation of the offer and marketing of collective investment schemes, on the narrow and rigid concept of a "distribution", with its intricate set of legal rules and exemption provided for in the CISA.

The content of this article is the personal opinion of the authors. This opinion is not necessarily identical with the position of SFAMA or Lenz & Staehelin.

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Something Old, Something New: The Supervision of Financial Institutions under the Federal Act on Financial Institutions – FinIA Update

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On 15 June 2018, the Federal Act on Financial Institutions was passed into law. The FinIA revises the regulatory architecture for financial institutions. Instead of the current sectorial approach, the FinIA proposes to introduce a regulatory pyramid with a light regulatory framework for asset manager and trustees, and an increasingly more stringent regime for managers of collective assets, securities firms – the new denomination for securities dealers – and, at the top, banks, although they will be continue to be governed by the Federal Act on Banks and Saving Banks of 8 November 1934 (Banking Act, SR 952.0) and remain out of scope of the FinIA. Furthermore, the FinIA introduces several new regulatory regimes: first of all, it subjects portfolio managers and trustees to prudential supervision. Second, it extends the current regime applicable to asset managers of collective investment schemes to asset managers of pension funds. Third, it recasts the existing regime applicable to securities dealers under the Federal Act on Stock Exchanges and Securities Dealing of 24 March 1995 (SESTA, SR 954.0) into a slightly modified new regime for securities firms. Fourth, it amends the Banking Act to introduce a new regulatory status for persons who hold public deposits of a total amount of less than CHF 100 million without engaging in commercial banking by lending the funds on (article 1*b* Banking Act). Finally, it also amends other regulations, including the Federal Act on Consumer Credits of 23 March 2001 (SR 221.214.1).

By Rashid Bahar

1) Financial Institutions: Definition and Scope

The FinSA governs the regulatory framework applicable to five types of financial institutions: (a) portfolio managers; (b) trustees; (c) managers of collective assets; (d) fund management companies; and (e) securities firms.

Portfolio managers are defined as whoever can, on a commercial basis dispose of the financial assets based on a mandate in the name and on behalf of clients (article 17 (1) FinIA). Trustees are defined as whoever can on a commercial basis manage or dispose of a separate fund for the benefit of the beneficiary or a specific purpose on the basis of an instrument establishing a trust as defined in the Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on Their Recognition (article 17 (2) FinIA). Portfolio managers and trustees will be deemed to act on a commercial basis if their activity generates a gross revenue of more than CHF 10 million; if they have at any given point more than 20 long-term contractual partners or if they have in a given calendar year more than 20 such relationships; if they have the power to dispose over assets worth more than CHF 5 million or if they undertake transactions worth more than CHF 2 million in a given calendar year.

Managers of collective assets are defined as whoever manages on a commercial basis assets in the name and on behalf of collective investment schemes and occupational pension schemes (article 24 (1) FinIA). The FinIA provides for a *de minimis* exemption and provides that the licensing requirements as managers of collective assets apply only if the quantitative thresholds set for the in article 24 (2) FinIA are exceeded. Otherwise, a license as portfolio manager is sufficient. The regime for managers of collective assets is based on the current regime for managers of collective investment schemes. However, its scope is broader since it will also cover asset managers who act in the name and on behalf of pension schemes. In this context, the FinIA exempts occupational pension schemes, including so-called employer sponsored funds, as well as employers, who manage the assets of their occupational pension schemes and employer and employee unions, who manage their assets (article 3 (2)(f) FinIA).

Fund management companies will continue to be responsible for the management of investment funds in their own name but for the account of investors (article 32 FinIA) and be subject to fundamentally the same regulatory framework as under the Federal Act on Collective Investment Schemes of 23 June 2006 (CISA, SR 951.31). As is currently the case, they will be allowed to custody and administer units of collective schemes and administer SICAVs (article 34 FinIA). Strictly speaking these activities constitute ancillary businesses that do not trigger the license requirement (and the right to obtain a license), although the latter activity is reserved to fund management companies (*see* article 51 (5) CISA as amended by the FinIA). Nevertheless, the Draft-FinIO assumes that FINMA will need to entertain requests for a license as a fund management company for persons only seeking to administer SICAVs (*see* article 51 (5) Draft-FinIO).

The same issue arises with securities firms, the new terminology for securities dealers under the SESTA: the FinIA defines securities firms as whoever, on a commercial basis, trades securities in its own name but on behalf of clients (article 51 (a) FinIA), trades in securities for its own account on a short-term basis, operates primarily on the financial market and can endanger the proper functioning of the financial market or participates in a trading venue (article 51 (b) FinIA) or trades in securities for its own account on a short term basis and quotes a price for specific securities publicly on an ongoing basis or on request (article 51 (c) FinIA). In this context, the activities of underwriters and derivative houses, which triggered a licensing requirement under SESTA, strictly speaking do not warrant a right to a license although they are reserved to banks and securities firms pursuant to article 12 FinIA.

In addition to the usual catalogue of exemptions for, among others, the Swiss National Bank, the Bank for International Settlements (article 2 (e) FinIA) occupational pension schemes (article 2 (f) FinIA), social security institutions (article 2 (g) FinIA, *see also* article 2 (i) FinIA), the FinIA exempts banks under the Bank Act and insurance companies under the Federal Act on the Oversight of Insurance Companies of 17 December 2004 (ISA, SR 961.01) from the scope of the act (article 2 (h) and (j) FinIA). Therefore, banks and insurance companies, can as a matter of principle carry out all the activities contemplated by the FinIA without requiring a license under the FinIA, with the exception of fund management, which is reserved to fund management companies under the CISA. By contrast, the inventory of exemptions does not mention other insurance companies that are not subject to the ISA, such as cantonal building insurers, who are thus required to obtain a license under the FinIA if they intend to engage in a business covered by the FinIA.

2) Regulatory Pyramid

The FinIA will revise the regulatory architecture governing financial institutions. Instead of the current sectorial approach based on the activity of financial institutions, the FinIA proposes to introduce a regulatory pyramid with a light regulatory framework for portfolio managers and trustees, and an increasingly more stringent regime.

Following this approach, a more stringent license automatically carries the license to carry out the business of a less stringent entity. Banks will – although they are not subject to the FinIA –be allowed to carry out the business of entities with a less stringent license. Specifically, banks will be automatically authorized to engage in the business of a securities house, a manager of collective assets, a trustee or a portfolio manager (article 6 (1) FinIA). Securities firms will be authorized to manage assets of collective investment schemes and pension funds, act as portfolio manager and as trustee (article 6 (1) and (2) FinIA). Collective assets managers will similarly be entitled to engage in "simple" portfolio management (article 6 (4) FinIA).

The pyramid is, however, not complete: first, it branches out for fund management companies: although they will have the right to engage in the business of managers of collective assets and asset managers (article 6 (3) FinIA), banks or securities firms will not be entitled to engage in fund management (article 6 (1) and (2) FinIA *a contrario*). Similarly, only banks and securities firms will be automatically licensed to act as trustees. Fund management companies and collective investment managers will not be authorized to act as trustees although they hold a more stringent license (article 6 (3) and 5 (4) FinIA *a contrario*). Furthermore, trustees will need a supplemental license to act as portfolio managers and vice versa (article 12 Draft-FinIO).

Moreover, banks will not be integrated in the regulatory framework defined by the FinIA. They will continue to be the subject of the Banking Act. Furthermore, insurance companies are completely out of scope of the FinIA and the FinSA although they regularly engage in asset management and offer investment products tied with life-insurances. This gap will, however, be closed in connection with the partial revision of Insurance Oversight Act, which was put in consultation on 14 November 2018 by introducing a dedicated regime for insurance companies (*see* Press release of 14 November 2018, Federal Council initiates consultation on partial revision of Insurance Oversight Act, available https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-72921.html)

Finally, the system will not be as elegant as it may seem: several functions under the CISA will continue to require a specific license, even for banks: Banks will continue to need to apply for a specific license to act as a depository bank (article 13 (2) (e) CISA). Banks, securities firms, and managers of collective assets will also continue to need a specific license to act as representatives of foreign collective investment schemes (article 13 (3) CISA and article 8 (1) and (3) of the Ordinance on Collective Investment Schemes of 22 November 2006, SR 951.311).

3) Licensing Requirements and further duties of financial institutions

a) Common Requirements

At the heart of the regulatory model lies a set of common provisions that apply to all financial institutions (*see* articles 5 to 16 FinIA, articles 52 to 60 FinIA on branches and representative offices of financial institutions and articles 61 to 67 FinIA on prudential supervision) which are complemented by rules that apply specifically to each type of financial institution (*see* articles 17 to 23 for trustees and portfolio managers, article 24 to 31 for managers of collective assets, articles 32 to 40 for fund management companies, articles 41 to 51 for securities firms).

All financial institutions will be licensed by FINMA (article 5 (1) FinIA). Once licensed, they will be required to announce any change of circumstances underlying their license to FINMA (article 8 (1) FinIA), and seek the prior authorization of FINMA for fundamental changes (article 8 (2) FinIA), which are defined in the Draft-FinIO as changes to the organization and business regulations, changes in the board of directors and executive management, changes to share capital and regulatory capital, facts that are likely to question the ongoing satisfaction of the fit and proper requirement by the institution, its directors, senior management, and shareholders, as well as changes of regulatory auditor or supervisory organization (article 5 Draft-FinIO).

As to their substance, the common requirements will be largely modelled on the current regime applicable to banks and securities dealers as applied by FINMA: all institutions will be required to have an appropriate organization (article 9 FinIA), including risk management and an effective internal control system (article 9 (2) FinIA). The Draft-FinIO elaborates further by providing that geographic and business scope of financial institutions will need to be set out in the relevant documents, meaning the articles of incorporation, partnership agreement or the organization and business regulations (article 6 (1) Draft-FinIO) and by conditioning any extension of the business activities or the geographic reach to the availability of sufficient resources and an appropriate business organization (article 6 (2) Draft-FinIO).

In line with the current practice of FINMA, both the institution as such and the members of the board of directors and executive management will be subject to a fit and proper requirement, which extends also to their reputation and professional qualifications (article 11 (1) and (2) FinIA). Notably, the Draft-FinIO provides detailed professional qualification requirements for senior executives portfolio managers and trustees (article 18 Draft-FinIO), but does not provide specific requirements for other financial institutions.

Qualified shareholders also need to comply with a fit and proper requirement and provide the assurance that their influence will not have a negative effect on a proper and prudent conduct of business (article 11 (3) FinIA). They will, as is currently the case, be subject to a duty to disclose their shareholding prior to reaching or crossing thresholds of 10, 20, 33 and 50 per cent of the shares or capital of a financial institution (article 11 (5) FinIA).

The FinIA, further, generalizes the rules of the CISA on outsourcing by permitting financial institutions to third parties only if they have the requisite skills, knowledge and experience and hold the requisite licenses to carry out their business (article 14 (1) FinIA). In this context, the FinIA empowers FINMA to condition the delegation of investment management to persons in other jurisdictions on the existence of an agreement between FINMA and the foreign regulator on cooperation and exchange of information (article 14 (2) FinIA).

Moreover, the FinIA requires financial institutions to notify FINMA before they establish or close a subsidiary, a branch or a representative office abroad or before they purchase or dispose of qualified participation in a foreign company (article 15 FinIA). This notification will need to include a business plan and further information on the foreign operations, its directors and senior management, its auditors as well as its regulators and supervisors abroad.

Finally, all financial institutions will be required to join an ombuds-organization upon starting their business (article 15 FinIA). This requirement ensures the effectiveness of the rules on alternative dispute resolution for investor disputes provided for by the FinSA.

b) Specific Requirements

The general requirements will, however, be modulated to account for the particular business of each type of financial institution. Therefore, although all financial institutions are subject to an obligation to have an appropriate organization pursuant to article 9 FinIA. The requirements will vary from one type of financial institution to another and must account for the size and complexity of the business when implementing and applying the regulations (*see*, *e.g.*, articles 9 (3) and 20 (2) FinIA, article 43*b* (3) Federal Act on the Swiss Financial Market Supervisory Authority of 22 June 2007 (FINMASA, SR 956.1)). In parallel, each type of institution will be subject to specific requirements. As the institutions raise in the regulatory pyramid, they become increasingly stringent.

Portfolio managers and trustees enjoy a relatively lenient regulatory framework: for example, qualified shareholders will be expressly allowed to exercise an executive role in a portfolio manager or a trustee (article 11 (8) FinIA). Furthermore, they are exempted from the requirement to announce to FINMA the fact that person took a substantial shareholding or reached or crossed the thresholds of 20, 33 or 50 per cent of the shares or the capital (article 11 (7) FinIA). In terms of governance, the requirements are limited: their executive management must, in principle, consist of two qualified persons with a joint signatory power (article 20 (1) FinIA and article 15 (1) Draft-FinIO). The act, however, expressly allows them to have only one qualified person, if they have ensured that business continuity is ensured (article 20 (2) Draft-FinIO). Similarly, the Draft-FinIO expressly provides that the risk management and compliance functions can be exercised by a duly qualified member of the senior management, another duly qualified member of staff or even delegated to qualified third party (article 21 (2) Draft-FinIO). Smaller financial institutions will even be entitled to waive the independence requirements for risk management and compliance (article 19 (2) Draft-FinIO). At the same time, larger portfolio managers with a gross revenue of more than CHF 10 million may be subject to the obligation to appoint an independent internal audit (article 19 (3) Draft-FinIO).

Similarly, portfolio managers and trustees are also subject to fairly limited specific requirements in terms of capital: for example, they will be subject to minimal regulatory capital requirements and be expected to either post collateral or have appropriate professional liability coverage (article 22 FinIA). The draft ordinance is, however, more lenient and conceives professional liability coverage as a means to meet the own fund requirements (article 24 (2) Draft-FinIO). The own fund requirements will amount to 25% of the fixed costs, but no more than CHF 10 million (article 23 (2) FinIA)

Managers of collective assets will be subject to an intermediate regime, which is fundamentally comparable to the existing regime for asset managers of collective investment schemes under the CISA. The FinIA provides only for fairly straightforward specific organizational requirements, which focus on the delegation of duties (article 27 FinIA). By contrast, the requirements regarding organization in the Draft-FinIO go well beyond the ones applicable to portfolio managers: managers of collective assets will, as a matter of principle, be required to have a board of directors (article 29 (6) Draft-FinIO) that is in majority non-executive (article 30 (1) Draft-FinIO) and composed of at least a third of independent directors (article 30 (3) Draft-FinIO). Furthermore, the chairman of the board is not allowed to act as chief executive officer (article 30 (4) Draft-FinIO). Similarly, the requirements regarding risk management and compliance are more detailed.

Managers of collective investment schemes will not be subject to full capital adequacy and liquidity requirements. Instead, they will be expected to maintain a certain level of capital, post collateral or subscribe a professional insurance policy (articles 28 and 29 FinIA) as well as minimal capital requirements. Based on the Draft-FinIO, managers of collective assets will require to have sufficient own funds to cover 25% of their fixed costs. In addition they are also required to hold further capital amounting to 0.01% of the asset under their management unless they have sufficient professional liability coverage. Overall, however, their capital requirements cannot exceed CHF 20 million. However, rules for consolidated supervision requirements kick in at this stage (article 30 FinIA).

Fund management companies are subject to extensive rules, which mirror the existing regime under the CISA. These consist in strict governance requirements: they will need to have a board of directors composed of at least three members (article 44 (1) Draft-FinIO) and which is composed in majority of non-executive directors (article 44 (2) Draft-FinIO) and include at least a third of independent directors (article 44 (4) Draft-FinIO). As with managers of collective assets, the chairman of the board will be barred from being the chief executive office (article 44 (3) Draft-FinIO). Moreover, the Draft-FinIO contemplates further requirements to ensure that the fund management company is independent from the depository bank. Among others, members of the management of the fund management company cannot be at the same time a member of the management of the depository bank (article 45 (2) Draft-FinIO), while directorships within both entities is permissible, as long as a majority of the members of the board are independent from the depository bank (article 45 (1) and (3) Draft-FinIO).

In terms of capital requirements, they are required to hold at least CHF 1 million in equity (article 50 Draft-FinIO) and comply with own funds requirements calculated on the basis of the assets under management (article 51 (2) and (4) Draft-FinIO) and the general framework applicable to banks for operational risks related to the custody and administration of units of collective investment schemes (article 51 (3) Draft-FinIO), subject to a cap at CHF 20 million (article 51 (1) Draft-FinIO).

Securities firms remain fundamentally subject to the current regime, including in terms of consolidated supervision. They are subject to full capital adequacy, liquidity and risk diversification requirements imposed by Basel III at entity and on a consolidated basis (article 46 (1) and (3) FinIA), unless they do not maintain settlement accounts for their clients. The flip-side of this regime is the possibility offered to securities firms to rely, like banks, on additional capital instruments to prevent or overcome a situation of financial distress (article 47 FinIA and article 13 (1) Banking Act). This being said, the FinIA introduces some novelties: for example, securities houses will be authorized to accept public deposits in connection with its regulated activities (article 44 (2) FinIA) and credit such deposits to interest-bearing accounts. This regulatory framework falls, however, short from an English-style client-money protection regime, although the FinIA mandates the Federal Council to issue provisions on the use of public deposits (article 44 (3) FinIA).

Finally, the regime for branches and representation offices of foreign financial institutions is closely mirrored on the current regime for foreign banks and securities dealers. In this respect, the greatest novelty is the new scope of this regime which will also apply to foreign portfolio managers and trustees as well as well as managers of collective assets that were unregulated until now. As a consequence, foreign groups with a local presence in Switzerland may need to reconsider their business model if they effectively carry out activities in Switzerland, including mere marketing activities, since they would trigger licensing requirements.

4) Dual Supervision of Portfolio Managers and Trustees

The most important change introduced by the FinIA is the prudential supervision of portfolio managers and trustees under a two-tiered supervisory approach, where the supervisory responsibility will be shared between FINMA and supervisory organizations, a new hybrid supervisor, which will be responsible to supervise portfolio managers and trustees under the FinIA as well as trade assayers under the Federal Act on the Control of the Trade in Precious Metals and Precious Metal Articles of 20 June 1933 (SR 941.31) and be licensed and supervised by FINMA (article 43*a* (2) FINMASA). Supervisory organizations will also be allowed to act as a self-regulatory organization under the Federal Act on Combating Money Laundering and Terrorist Financing of 10 October 1997 provided it was recognized as such (article 43*a* (3) FINMASA).

Under this model, FINMA will license and supervise portfolio managers and trustees (article 5 (1) and 61 (1) FinIA). However, portfolio managers and trustees will be required to join a supervisory organization (article 7 (2) FinIA, which will be responsible for the day-to-day supervision (article 61 (2) FinIA and article 43*b* (1) FINMASA). As an exception to this rule, portfolio managers and trustee belonging to a group that is subject to consolidated supervision will not be required to join a supervisory organization, but will be supervised directly by FINMA as part of the consolidated supervision. The supervisory organizations will be entitled to rely on audit firms to inspect portfolio managers and trustees following the dual-supervisory model applied by FINMA or carry out the inspection themselves, as some self-regulatory organizations already do in the realm of anti-money laundering regulations (article 62 (1) FinIA and article 43*k* (1) FINMASA).

Under normal circumstances, the supervisory organization will be responsible for the day-to-day supervision (article 43*b* (1) FINMASA), while FINMA will stay in the background. This supervision will be exercised mainly through periodic regulatory audits. Furthermore, portfolio managers and trustees will be required to respond to any request for information that the supervisory organization requires to carry out its statutory duties and to inform the supervisory organization of the occurrence of any event that is of material importance for the supervision (article 43*l* (1) and (2) FINMASA).

The supervisory organization will not have formal administrative powers, however. This role will remain with FINMA, who will be in charge of licensing (article 5 (1) FinIA) and taking formal enforcement action against portfolio managers and trustees as with any other supervised entity. If, in the course of their supervision, a supervisory organization finds that an portfolio manager or a trustee breached its obligation, it will be required to set a deadline to the regulated entity to remedy the situation and if it fails to act within the deadline, it will be required to report the matter to FINMA (article 43*b* (2) FINMASA). FINMA will then take over the case and will be empowered to use the full palette of administrative measures available to it, including issuing a declaratory ruling (article 32 FINMASA), ordering remedial measures (article 31 FINMASA), prohibiting a person from exercising a controlling function within a supervised entity (article 33 FINMASA), naming and shaming (article 34 FINMASA), confiscating undue profits (article 35 FINMASA), appointing an investigating agent to clarify the facts or manage the institution (article 36 FINMASA) or even withdraw the license (article 37 FINMASA).

The split between supervisory organizations and FINMA will, however, need to be clarified in practice. Indeed, the line between supervision and enforcement is not clear. It is, therefore, likely that FINMA will create a halfway house to deal with entities that need to be monitored closely although their actions would not justify taking formal enforcement proceedings, as it already does in connection with banks and securities dealers that are subject to so-called intensive supervision.

Similarly, further clarifications will be needed to define the threshold for FINMA to take enforcement actions. Although the FinIA suggests that FINMA will be required to take enforcement action only against characterized offenders who failed to remedy breaches after the deadline set forth by the supervisory authority (*see* article 43*b* (2) FINMASA), it seems unlikely that FINMA can turn a blind eye to serious breaches. In such cases, it is likely to need to take action, and issue blame or take other enforcement action, .*e.g.* confiscate undue profits, without giving the entity the chance to clean up.

5) FinTech

A further change brought by the FinIA relates to the broader initiative to create a suitable regulatory framework for FinTechs, which is spearheaded by the Federal Council and FINMA. In line with the reforms announced by the government, the FinIA introduces two exemptions which seek to remove undue hurdles for technological innovation in the financial industry. The driving force of this regulation is that financial institutions that accept deposit without engaging in traditional commercial banking should not bear the full brunt of complying with banking regulations. This new regime should allow Fin-Techs, *e.g.*, crowdfunding platforms and payment service providers broadly speaking, to carry out their business without being fully regulated as a bank.

The FinIA limits the scope of banking regulations to institutions that accept or publicly solicit deposits in excess of CHF 100 million or entities which accept deposits below this threshold, but either invest the deposits or pay interest on them (article 1*a* (1) Banking Act as amended by the FinIA). Instead, entities that do not pay interest or invest deposits will be subject to a dedicated 'FinTech' licensing regime that will be analogous to the one applicable to banks (article 1*b* (1) Banking Act as amended). The FinIA also allows FINMA to grant a similar exemption to entities that accept deposits in excess of the CHF 100 million threshold provided they do not invest or pay interest on the deposits and take additional measures to protect their clients (article 1*b* (5) Banking Act as amended).

These entities will be required to inform their clients in writing or on a comparable text medium of their business model, their services and the fact that deposits are not covered by the deposit protection scheme (article 7*a* (1) Ordinance on Banks and Saving Banks of 30 April 2014 (Banking Ordinance, BankO, SR 952.02) as amended). Furthermore, the deposits they hold will need to be either held separately from their own funds or booked in such a manner that they can be at any time separated from their own funds (article 14*f* (1) Banking Ordinance as amended). Furthermore, the funds will need to be either held on sight-deposits with a bank or another entity subject to the amended article 1*b* BankA or in high-quality liquid assets in the same currency as the underlying deposit (article 14*f* (2) and (3) Banking Ordinance as amended). As an exception, crypto-currency deposits will be required to be held in the same form as they were accepted (article 14*f* (14 Banking Ordinance as amended).

As part of the regulatory relief, the entities subject to article 1*b* of the amended Banking Act are subject to considerably less stringent governance and capital requirements. Their board of directors may include executive directors and must include at least a third independent directors (article 14*d* (1) and (2) Banking Ordinance as amended). They will be allowed to outsource compliance and risk management (article 14*e* (4) Banking Ordinance as amended) and may even be exempted from the requirement of establishing an independent risk management and compliance department, if their annual revenue does not exceed CHF 1.5 million and their business model has limited risks (article 14*e* (5) Banking Ordinance as amended). Moreover, they will be entitled to prepare audited financial statements in accordance with the Swiss Code of

Obligations rather than the more stringent rules applicable to banks (article 1*b* (3) Banking Act as amended).

The entities will be subject to limited capital requirements: instead of the complex and stringent capital and liquidity requirements applicable to banks (article 17*a* (3) Banking Ordinance as amended), they will need to hold 3% of the public deposits they have on their books and at least CHF 300,000 in equity (article 17*a* (1) Banking Ordinance as amended).

6) Other Changes

The FinIA also amends a number of other acts. The main changes relate to the CISA. These amendments are related on the one hand to the new regulatory framework which regulates institutions, such as managers for collective assets and fund management companies in the FinIA rather than in the CISA. However, the FinIA amends the CISA in a more substantial manner: first, the status of distributors of collective investment schemes will be repealed and, where applicable, replaced by the obligation to register client advisors under the FinSA. Furthermore, it amends the regime for offering foreign collective investments schemes. First, it substitutes the concept of distribution of collective investment schemes with the concept of offering borrowed from the FinSA. Second, it limits the scope of the obligation to appoint a Swiss representative and paying agent to funds offered to high net worth individuals who elected to be treated as qualified investors and thus releases collective investments schemes that are exclusively offered to other qualified investors from the scope of the CISA. Finally, the FinIA removed offerings 'from Switzerland' from the scope of the investments on collective schemes (articles 120 (1) and 123 (1) CISA, as amended). Doing so, the FinIA arguably removed pure outbound offerings of collective investment schemes from the scope of the Collective Investment Schemes Act, which is likely to significantly decrease the regulatory burden of collective investment schemes that are managed or administered in Switzerland without being offered locally.

In the realm of anti-money laundering, the FinIA entails two important changes: first, portfolio managers, trustees and trade assayers will be subject to the same regulatory regime as banks and securities dealers. Instead of having the possibility to join an SRO, compliance with the Federal Act on Combating Money Laundering and Terrorist Financing of 10 October 1997 (SR 955.0) will be supervised as part of the overall prudential supervision, albeit following the dual supervisory model with the supervisory organization in charge of ongoing supervision and FINMA intervening on a more ad hoc basis, with the sole power to grant license and take formal enforcement action. Second, the current regime of directly supervised financial intermediaries will be repealed and financial intermediaries that are not already supervised by FINMA as part of the overall prudential supervision will have to join a self-regulatory organization.

Among other further amendments, the FinIA introduces a new regime for crowd-lenders which will require persons running crowd-lending platforms which provide consumer credits under the Consumer Credit Act to comply with the same obligations as a person extending on consumer credits on a commercial basis, including the obligation to carry out a creditworthiness test pursuant to the Consumer Credit Act. It also introduces a licensing obligation for trade assayers who deal in bankable precious metals, which is based on the same model as the one applicable to portfolio managers and trustees.

7) Next Steps and Phasing-in

As mentioned at the outset, the FinIA was adopted by the Swiss parliament on 15 June 2018 and, since no referendum was requested, has become good law. The Federal Council can now decide when the FinIA will come into force. Currently, the general expectation can be summarized as follows. The amendments to the Banking Act aiming to introduce a 'light' banking license also known as a FinTech license and the new rules on consumer credits are due to enter into force on 1 January 2019. By contrast, the process for the rest of the act is more protracted: the implementing ordinances are currently in consultation and the consultation process for the Draft-FinIO will last until 6 February 2019. The Federal Council will then need to finalize the ordinance before the act can enter into force. Currently, the Federal Department of Finance announced that it expects the act to enter into force on 1 January 2020.

Even then, the FinIA provides for a generous phasing in process: financial institutions that were previously supervised by FINMA, such as asset managers for collective investment schemes and fund management companies under CISA as well as securities dealers under SESTA, will be automatically grandfathered into their new status under the FinIA (article 74 (1) FinIA), but will need to join an ombuds-organization within six months of the recognition of the first ombuds organization by the Federal Department of Finance (article 87 (2) Draft-FinIO)

Trustees, asset managers and managers of collective assets that are newly subject to licensing requirements will need to report themselves with the FINMA within six months of the entry in force of the FinIA and will have three years to submit their licensing application, provided they are already member of a self-regulatory organization under the AMLA (article 74 (2) FinIA). Otherwise, they will need to report themselves within six months and have joined an SRO within a year of the entry in force of the FinIA, unless they joined a supervisory organization and filed their application with FINMA in the meanwhile, although there is no certainty that the supervisory organizations will be up and running by then.

Furthermore, during the first year following the entry in force of the FinIA, new asset managers and trustees will be entitled to commence their operations provided that they immediately announce themselves to FINMA and comply with all requirements under the FinIA, with the exception of joining a supervisory organization. They will then have a year counting from the first licensing of a supervisory authority by FINMA to file their own application to be licensed and join a supervisory authority, provided they joined a self-regulatory organization under the AMLA (article 74 (3) FinIA).

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Supervision of Portfolio Managers and Trustees

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Under current Swiss law, portfolio managers and trustees are not subject to a comprehensive prudential supervision, a situation that will change under the recently passed new Financial Institutions Act (FinIA). After the Swiss parliament passed the new legislation in June 2018, the Swiss Federal Department of Finance released its draft implementing ordinance (Draft-FinIO) for consultation. Under the new legislation, portfolio managers and trustees will have to apply for a license from the Swiss Financial Market Supervisory Authority (FINMA) and they will be subject to ongoing prudential supervision by new supervisory organizations. The FinIO specifies the license requirements for portfolio managers and trustees, taking into account the nature of these businesses and providing a certain amount of flexibility with respect to the requirements to be fulfilled by smaller businesses. While the new rules will come as a challenge for many of the existing portfolio managers and trustees, the FinIA and the FinIO also provide for transitional periods allowing these existing portfolio managers and trustees to transition gradually into the new regulatory regime.

By Patrick Schleiffer / Patrick Schärli

1) Portfolio Managers and Trustees will be FINMA-licensed Entities

While the new FinIA will only bring limited changes to the regulatory landscape within which the already licensed Swiss financial institutions operate, the changes with respect to portfolio managers and trustees will be substantial. These previously unlicensed businesses will have to apply for a license with the Swiss regulator FINMA and they will be subject to comprehensive licensing requirements. In addition, under the new law and regulations these businesses will be subject to ongoing prudential supervision by the yet to be established supervisory organizations. Thus, the FinIA (and its implementing ordinance) will, for the first time, subject portfolio managers and trustees to license requirements and an ongoing prudential supervision. As a result, portfolio managers and trustees will generally be subject to the same type of rules that also apply to other financial institutions. Needless to say that this new regulatory framework is significantly different than the situation under current law, where these types of financial intermediaries were only required to register themselves with a self-regulatory organization (SRO) for purposes of compliance with the Swiss anti-money laundering laws.

a) Scope of the New Rules

The FinIA defines portfolio managers as someone that, based on a mandate agreement, can dispose of a client's asset by way of the following activities: (i) purchase or sale of financial instruments, (ii) acceptance and transmission of client orders relating to financial instruments, (iii) management of financial instruments (asset management), or (iv) advice relating to financial instruments (investment advice).

The FinIA and the FinIO provide for certain exemptions with respect to the activity as portfolio managers. In particular, there will be exemptions for persons managing the assets of persons with whom they have "economic" or "family" ties. In this respect, the FinIO further specifies what is considered as "economic" or "family" ties (including a list of the relevant family relationships). This exemption allows, for example, single family offices to continue to operate without the need for a license. Multi-family offices can, however, not benefit from this exemption as they manage assets of a number of unrelated clients. Further, the FinIA and the FinIO also exclude from the licensing requirements persons that are acting based on a statutory mandate (*e.g.*, guardians).

A trustee is defined as someone that based on a trust deed can dispose of the assets of a trust within the meaning of the Hague Trust Convention. This rather specific definition excludes other trust-related service providers, such as protectors, from the scope of application of the new licensing requirements. Also, persons providing similar types of services (*e.g.*, nominee directors) will not be covered by the new rules.

In addition, in order to fall within the scope of the new rules, the activities of a portfolio manager and a trustee, respectively, have to be undertaken on a commercial basis. According to the draft FinIO, an activity is considered to be undertaken on a commercial basis if any of the following thresholds are exceeded: (i) annual gross profits in excess of CHF 50,000, (ii) having relationships with more than 20 contractual counterparties in a calendar year, (iii) assets under management/assets under trust in excess of CHF 5 million, or (iv) transaction volume in excess of CHF 2 million. These thresholds largely follow the rules already set out today in the current Swiss Anti-Money Laundering Ordinance and accordingly, as a rule of thumb, portfolio managers that are currently subject to the Swiss anti-money laundering obligations will also be subject to the licensing requirements under the FinIA and FinIO.

b) License Requirements

As a financial institution, a portfolio manager or a trustee has to meet the general licensing requirements applicable to all types of financial institutions as well as specific requirements applicable to portfolio managers and trustees. Among the general requirements are such things as (i) the requirement to manage the relevant company from Switzerland, (ii) "fit and proper" requirements with respect to the board of directors, senior management and qualified participants (*i.e.*, each direct or indirect holding of 10 % or more of the voting rights or the capital), (iii) duty to notify FINMA of activities outside of Switzerland, and (iv) the requirement to be affiliated with a mediation body.

Non-Swiss portfolio managers rendering their services on a pure cross-border, i.e. without permanently employing staff in Switzerland, to clients in Switzerland, will not need license from FINMA. However, they will have to comply with the regulatory rules under the new Financial Services Act (FinSA), and their staff providing the relevant financial services to their clients in Switzerland (so-called client advisers) have to register in a new register of advisers in Switzerland and meeting the requirements for being registered (including having the necessary know how and skills to comply with the regulatory rules under the FinSA and being affiliated to an ombudsman in Switzerland) before providing financial services in Switzerland.

In terms of specific requirements, the following applies to portfolio managers and trustees:

– **Affiliation with a supervisory organization:**

  Portfolio managers and trustees will have to apply for affiliation with one of the new supervisory organizations (SO, see section 2 below) which will be responsible for the day-to-day prudential supervision of the portfolio managers and trustees. The FinIO specifies that a portfolio manager or a trustee has a right to be affiliated to an SO (*i.e.*, the SO has to accept the application for affiliation) if such portfolio manager and trustee has put in place internal regulations and an organization of its business that ensures compliance with the regulatory requirements (including those set out in the FinSA and those under the Swiss anti-money laundering laws, in each case to the extent applicable).

– **Composition of the management:**

  Unlike other financial institutions (such as banks or securities firms), portfolio managers and trustees are not required to set up a two-tiered management structure. FINMA may, however, on a case-by-case basis require certain portfolio managers and trustees to put in place a two-tiered management structure with a board of directors (composed mostly of independent directors) and an executive management. According to the draft FinIO, portfolio managers and trustees may become subject to such additional FINMA requirements if they have annual gross revenue of at least CHF 5 million or if required in light of the type and nature of their business.

As a rule, the management of a portfolio manager or a trustee must be composed of at least two qualified individuals. An individual is qualified within the meaning of the FinIA if such individual has an adequate education and sufficient professional experience when taking over the management of a portfolio manager or a trustee. The draft FinIO further specifies the requirements in terms of education and professional experience as follows (with FINMA having the power to grant exemptions on a case-by-case basis):

- professional experience of at least 5 years;
- relevant education in the area of portfolio management or trust matters; and
- obligation for ongoing training.

In line with European regulations, the draft FinIO also requires portfolio managers and trustees to set in place appropriate business continuity procedures that ensure the functioning of the management in case of a prolonged absence or death of a qualified individual.

- **Risk management, internal controls and compliance**

A portfolio manager or a trustee will have to implement an adequate risk management and effective internal controls, including a compliance function. As a rule, risk management and compliance functions have to be independent from the business side.

Taking into account that internal control systems and compliance can be quite a burden for smaller companies, the draft FinIO provides for certain exemptions. More specifically, a portfolio manager or trustee does not need to have a risk management and compliance function that is independent from the business, if it has:

- annual gross sales of less than CHF 1.5 million or no more than 5 employees; and
- a business model without increased risks.

On the other hand, where a portfolio manager or a trustee has annual gross sales of more than CHF 10 million, FINMA may require such portfolio manager or trustee to put in place an independent internal audit.

The risk management and compliance functions may be delegated to qualified third parties. Such delegation will be subject to the general delegation rules applicable to all financial institutions, including the requirements to have the necessary technical know-how and internal procedures to adequately supervise the delegated functions and to document the delegation in the portfolio manager's or trustee's organization documents.

– **Minimum capital requirements:**

  Portfolio managers and trustees will be required to have a minimum capital of CHF 100,000. In addition, they need to maintain additional equity in an amount equal to one quarter of their fix costs, but no more than CHF 10,000,000. The draft FinIO further specifies the requirement for additional equity as follows:

  – The following qualifies as fix costs: (i) salaries (not including discretionary and/or performance-based bonus payments), (ii) operational costs, (iii) amortization of immovable property, and (iv) revaluation reserves.

  – When calculating the additional capital, companies can take into account the following: (i) fully paid up capital, (ii) legal reserves, (iii) undistributed profits, (iv) latent/hidden reserves, and (v) certain subordinated loans (provided they have a minimum term of at least 5 years).

  – On the other hand, when calculating whether the additional equity requirement is met, companies need to deduct (i) goodwill, (ii) book value of participations, (iii) 20% of any subordinated loans during the 5 years preceding the reimbursement, (iv) and certain other values as further set out in the draft FinIO.

  – Finally, the draft FinIO states that a professional liability insurance can cover up to 50% of the additional equity requirement.

2) Supervisory Organizations

Under the FinIA, one or more FINMA-licensed privately organized supervisory organizations (SO) will be responsible for the ongoing day-to-day supervision of portfolio managers and trustees. Currently, there are already a number of the existing SRO in the process of getting ready to apply for a license as SO. In terms of timing, the license applications for the new SO have to be filed with FINMA within six months of the entry into force of the FinIA (*i.e.*, by end of June 2020) and FINMA will then have to decide on the license applications by the end of 2020.

Once operational, the SO will be responsible for the ongoing day-to-day prudential supervision of portfolio managers and trustees. As part of this supervision, an SO may conduct audits of portfolio managers and trustees themselves or they can require the portfolio managers and trustees to appoint an external auditor for purposes of the regulatory audit. This rule allows existing SROs with their own audit organization to continue to conduct their own audits (should such SRO decide to apply for a license as SO).

The SO will also have the possibility to reduce the audit frequency of the portfolio managers and trustees supervised by them. This risk-based approach allows smaller entities to benefit from a reduced supervisory burden. In years where there is no audit, the supervised entities will have to prepare and file a (standardized) report on their compliance with the relevant laws and regulations. FINMA will issue further regulatory guidance on the risk-based approach and the requirements for the standardized report.

As mentioned above, the SO will be responsible for the ongoing day-to-day prudential supervision of portfolio managers and trustees. Should an SO learn that a portfolio manager or a trustee does not comply with its obligations, it can set a deadline within which the respective portfolio manager or trustee has to remedy the situation. Other than that and a general right to obtain information from the supervised entities, the SO do not have any other supervisory or enforcement tools at their disposal. In particular, the SO will not be able to open their own enforcement action. Accordingly, if a supervised entity does not comply with its duties, the SO will have to notify FINMA who will then take up appropriate enforcement actions.

In order to avoid duplication of audit work and in order to ensure a harmonized supervision, FINMA will issue further implementing regulations applicable to the organization of SO and FINMA can also coordinate its work with SO.

3) Transitional Period

Taking into account the amount of changes that the new regulatory framework will bring to existing portfolio managers and trustees, the FinIA and the FinIO provide for rather long transitional periods. The transitional periods can be grouped in the following three different scenarios:

- **Portfolio managers/trustees that are already operating at the time the FinIA enters into force** (*i.e.*, activities started before 1 January 2020):

  Existing portfolio managers and trustees have to notify FINMA within 6 months of the entry into force of the FinIA, *i.e.*, until 30 June 2020. Following this initial notification, such existing portfolio managers and trustees have to meet the license requirements and file a license application with FINMA within 3 years after the entry into force of the FinIA, *i.e.*, until the end of 2022. Once a license application has been filed, such portfolio managers and trustees can continue their activities until FINMA has decided on the license application; provided, however, such portfolio managers and trustees are affiliated with an SRO for AML purposes.

- **Portfolio managers/trustees that start their activities after 1 January 2020 but before the end of 2020:**

These portfolio managers and trustees have to immediately notify FINMA of their activities and they have to generally comply with the FinIA licensing requirements from day one. The only exception is the requirement to be affiliated with an SO. For this obligation, the FinIA provides for a transitional period of one year following the point in time FINMA has authorized the first SO. At the same time, these type of portfolio managers and trustees also have to file a license application with FINMA. As is the case with the existing portfolio managers and trustees, once a license application has been filed, such portfolio managers and trustees can continue their activities until FINMA has decided on the license application; provided, however, such portfolio managers and trustees are affiliated with an SRO for AML purposes.

– **Portfolio managers and trustees that start their activities after 1 January 2021:**

  All other portfolio managers and trustees, i.e. all that start their activities after 1 January 2021, first have to apply for a license and an affiliation with a SO. They may only start operating their business once FINMA has decided on the license application.

4) Conclusion

The FinIA provides for a number of significant changes to the regulatory framework within which portfolio managers and trustees will have to operate in the future. Most importantly, portfolio managers and trustees will be subject to stringent licensing requirements and ongoing supervision by yet to be established SO. However, the draft implementing ordinance to the FinIA (FinIO) takes into account that many of the existing portfolio managers and trustees are smaller businesses with a lean management structure and accordingly, the implementing rules and regulations as currently provided for in the FinIO do provide certain regulatory flexibility. Furthermore, the transitional periods provided for in the FinIA allow for a gradual transition of existing portfolio managers and trustees into the new regulatory regime. It is however expected that the custodian banks with which a portfolio manager deposits the assets of its clients will urge such portfolio manager to obtain the relevant license as soon as reasonably possible as the regulatory duties of a custodian bank towards a prudentially supervised portfolio manager will be less demanding than those in respect of a non-supervised portfolio manager during the transitional period.

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ARYZTA completed a rights offering in the amount of approximately CHF 900 million

Reference: CapLaw-2018-66

On 19 November 2018, ARYZTA, a global food business with a leadership position in speciality bakery, completed a capital increase by way of a rights offering structured as a volume underwriting in the amount of approximately CHF 900 million.

Amun issues cryptocurrency-linked Exchange Traded Products

Reference: CapLaw-2018-67

On 13 November 2018, Amun AG, a Zug-based special purpose issuance vehicle of the fintech group Amun, successfully registered its issuance program for the issuance of Exchange Traded Products (ETP) on the SIX Swiss Exchange. On 20 November 2018, Amun successfully issued its first series of cryptocurrency-linked ETP. These products are linked to the performance of the "Amun Crypto Basket Index (HODL5)", an index that tracks the performance of the top 5 eligible cryptocurrencies. First trading day on the SIX Swiss Exchange was on 22 November 2018.

Zur Rose Group completed a rights offering in the amount of approximately CHF 190 million

Reference: CapLaw-2018-68

On 29 November 2018, Zur Rose Group AG, Europe's largest online pharmacy and one of the leading medical wholesalers in Switzerland, completed its rights issue to support the financing of the medpex acquisition as well as other organic growth initiatives.

Finanz '19
(*Die 21. Finanzmesse für professionelle Anleger*)

22-23 January 2019, Zurich

https://finanzmesse.ch/de

Seminar: 16th Zurich Stock Corporation Conference (*16. Zürcher Aktienrechtstagung*)

5 March 2019, Zurich

http://www.eiz.uzh.ch/weiterbildung/seminare

Seminar: FinTech 4.0 (*Das FINternet*)

28 March 2019, Metropol Zürich

http://www.eiz.uzh.ch/weiterbildung/seminare