Schweizerische Eidgenossenschaft
Confédération suisse
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Swiss Confederation

Der Bundesrat
Le Conseil fédéral
Il Consiglio federale
The Federal Council

Basic information

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Dispatch on Financial Services Act and Financial Institutions Act

1. Background

On 28 March 2012, the Federal Council instructed the FDF, in cooperation with the Federal Department of Justice and Police (FDJP) and the Swiss Financial Market Supervisory Authority (FINMA), to commence work on a project to prepare cross-sector regulation of financial products and services and their distribution. This decision was largely based on the FINMA position paper on distribution rules that was published in February 2012.

The FDF conducted a consultation on the Financial Services Act (FinSA) and the Financial Institutions Act (FinIA) from 25 June to 17 October 2014. While the majority of the more than 200 consultation participants welcomed the overall direction of the two draft laws explicitly or at least generally, some expressed major reservations regarding certain parts and recommended corresponding amendments. Taking account of the outcome of the consultation, the Federal Council took decisions on 13 March and 24 June 2015 regarding the direction to be taken for preparing the dispatch.

2. Financial Services Act (FinSA)

2.1 General

Aside from creating uniform competitive conditions and strengthening the competitiveness of the financial centre, the FinSA serves primarily to improve client protection. The term client is meant as an umbrella term here and includes investors, investment holders and insured persons covered by the act. The act contains rules on the provision of financial services and the offering of financial instruments that are consistent with each other and adapted to the risk and complexity of the corresponding activities for all financial service providers active on the financial centre on a commercial basis.

The FinSA stipulates that all financial service providers must observe codes of conduct under supervisory law which are transparent for clients and are consistent and thus comparable. The focal points of these provisions are duties to provide information and conduct research. Clients need the essential information on their financial service providers and on the content and functioning of the financial services and instruments offered to them in order to make investment decisions. Whenever financial service providers advise clients or manage their assets, they also have to give due consideration to their clients' knowledge, experience, financial circumstances and investment objectives.

The FinSA also introduces uniform prospectus requirements for all securities that are publicly offered or traded on a trading venue. The new prospectus requirements are designed in a proportionate manner and, in particular, simplify matters considerably for SMEs. In addition to prospectus requirements, there is the duty to prepare a key information document. This brief documentation should enable retail clients to make informed investment decisions and compare various financial instruments. The key information document is to be drafted in easily understandable language, contain key information on the product and be presented in a uniform manner irrespective of the type of financial instrument. The key information document will also make it easier for client advisers and intermediaries to find their bearings among the broad spectrum of financial products.

At the same time, sector-specific measures will partially facilitate and enhance enforcement under private law. In particular, the out-of-court settlement of disputes by recognised ombudsmen for all services rendered on the financial market should be introduced and the risks associated with procedural costs should be mitigated in a targeted manner. This straightforward option for dispute settlement is currently used only by banks and insurers.

The impact of each of the envisaged rules can be maximised on a regular basis only in combination with other rules. For example, the introduction of greater transparency at product level is meaningful only if financial service providers are obliged to pass on the corresponding information to their clients and enquire as to the requirements and expectations of their clients. The conduct obligations will in turn have the effect of improving client protection only if client advisers are aware of these obligations and possess a sufficient level of specialist knowledge. Only the coherent regulation of transparency, conduct, supervision and legal enforcement is capable of achieving the objectives of the new regulation effectively.

The proposed rules were drawn up after taking into account international requirements regarding the regulation of financial product development and distribution. Internationally valid standards, particularly those of the EU, should be adopted insofar as is reasonable and appropriate, without going beyond these, however. In this way, the aim is to establish a regime that is equivalent but yet adequately adjusted to conditions in Switzerland and differentiated accordingly. In particular, it is assumed that responsible clients can take their decisions only if they have the information required for the specific situation.

2.2 Key features of the new regulations

The proposed regulation takes account of the various features of financial service providers and financial instruments, as well as the different needs of the various client segments. It allows financial service providers and their clients to choose the level of protection appropriate for the specific constellation. In particular, it refrains from patronising clients or from creating high formal barriers for client support by financial service providers. Just like the FinIA, the FinSA builds on the existing supervisory legislation. Well-established provisions of existing law have been included and – insofar as necessary – harmonised across sectors and merged. Changes have been made to the following areas in particular:

- *Basic training and continuing professional development (CPD) duty*: Compared with the preliminary draft, a moderate extension of the rules on basic training and CPD is envisaged. The principle of only allowing persons with sufficient basic training and CPD to act as advisers and intermediaries, to which no objections were raised in the consultation, will be developed further to include the responsibility of financial service providers to guarantee this in their area. Furthermore, sector-specific minimum requirements should also be drawn up within the scope of self-regulation by the sectors themselves.
- *Client segmentation*: A distinction is made between two main categories of clients, i.e. retail clients and professional clients, as well as institutional clients as a subgroup of professional clients. This client segmentation is developed as a dynamic system which provides the possibility of switching between segments (opting system).

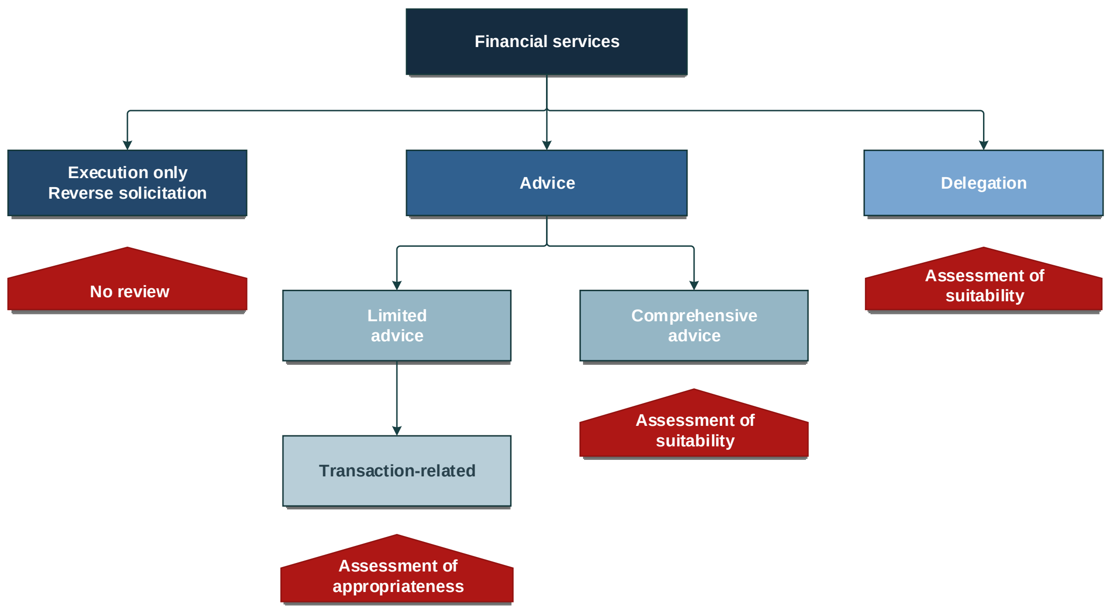
  The new conduct and product provisions are attuned to the protection needs of the respective client segment. Financial service providers may assume that professional clients have the required level of knowledge and experience with regard to the financial services and instruments that are relevant for them. All clients are free to invest in all financial instruments available on the financial markets. Even retail clients are not restricted by the new regulations in their choice of products. The FinSA does not prohibit them from acquiring even complex financial instruments without being advised by a financial service provider, including via execution only and reverse solicitation transactions. What is crucial, however, is that clients are correctly informed of their status and the associated personal responsibility beforehand.

– *Modular nature of the clarification duty*: For financial service providers to be able to support their clients, they must know their needs. The extent of this clarification is determined by the type of service and is of a modular nature: if the financial service consists solely in execution (execution only transactions) or if the transactions are carried out at the client's request without the provision of advice (reverse solicitation transactions), financial service providers do not have to perform a review. Even when they inform their clients on request of the general expectations of their institution or of third parties regarding the development of certain financial instruments, this is still a reverse solicitation transaction and does not constitute investment advice.

  However, if financial service providers offer their clients advice on certain transactions (transaction-related investment advice), they must at least know how much knowledge or experience the client has with the type of transaction in question. Financial service providers are obliged to perform an assessment of appropriateness before providing investment advice. If they consider a transaction to be inappropriate, or if they cannot perform the assessment of appropriateness due to certain information being absent, they should make the client aware of this fact. In this way, the transaction is not prohibited, but the financial service provider is obliged to give a warning.

  Financial service providers must go beyond the assessment of appropriateness if their advice relates not only to single transactions but to the entire client portfolio (portfolio-related investment advice and asset administration). In these cases, they must enquire not only about their clients' experience and knowledge but also about their investment objectives and financial situation, and they must perform a suitability assessment based on this information.

Suitability and appropriateness of financial services



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- *Transparency of remuneration from third parties*: Complete transparency will be established with regard to all remuneration and other benefits received from third parties, but an overall or partial ban on remuneration such as retrocessions and brokerage fees, etc. will not be introduced. Based on the case law of the Federal Supreme Court, the client must be able to understand the amount of the total remuneration received for the service provided.
- *Register of advisers*: The register of client advisers and the register of foreign financial service providers envisaged in the preliminary draft will be merged. The new register of advisers still covers only advisers from Swiss financial service providers not subject to prudential supervision and advisers from foreign financial service providers that do not have a branch or are not subject to prudential supervision in Switzerland.
- *Same code of conduct requirements for foreign and Swiss financial service providers*: Foreign financial service providers should observe the same code of conduct in all areas of their activity in Switzerland as is observed by Swiss providers.
- *Uniform regulation of prospectus requirements*: The current prospectus requirements for shares, bonds and other listed financial instruments will essentially be extended to include all equity securities and debt instruments and brought into line with internationally recognised standards. Provision is made, however, for various exemptions by type of offer and type of security. There will also be far-reaching simplifications for SMEs, some of which have to be more clearly specified by the Federal Council. The prospectus requirements are largely based on the EU Prospectus Directive. In order to be prepared for possible developments in this area, the Federal Council will be granted the power to adapt the exemptions to the international environment, where necessary.
- *Introduction of a key information document*: A "key information document" should now be issued for all financial instruments offered to retail clients. A key information document does not need to be drawn up when offering shares. Furthermore, a key information document does not have to be drawn up if equivalent documents exist based on the requirements of foreign legislation.
- *Crowdfunding*: Crowdfunding in the form of a financial instrument is debt financing which does not involve established financial intermediaries. In the case of crowdlending, lenders expect reimbursement and generally a commensurate financial return. As this has to be qualified in certain circumstances as the acceptance of deposits from the public in accordance with financial market legislation and this activity is generally reserved for banks, the FinSA will establish an alternative investment option. In this respect, the FinSA stipulates that a key information document must be drawn up for crowdlending where the transaction is to be qualified as a bond. Not only does this ensure that clients have the necessary information for their investment decision, it also avoids the scenario of the acceptance of deposits from the public as defined by the Banking Act.
- *Ombudsman*: The ombudsman institution will be strengthened and introduced for all financial services. Just like the ombudsmen that already exist in banking and insurance, however, the ombudsman will have no decision-making powers so that it is not restricted in its role as arbitrator.
- *General regime for collective legal protection*: A regime for collective legal enforcement (group settlement proceedings and representative action) limited to financial services will not be established. In its place, the introduction of general group settlement proceedings has been proposed and the extension of the scope of representative action in the Civil Procedure Code (CPC) is being examined as part of the implementation of Motion 13.3931 (Birrer-Heimo).
- *Partial elimination of law enforcement instruments*: The reversal of burden of proof provided for in the preliminary draft, according to which a client is deemed not to have performed the transaction if the financial service provider failed to fulfil its information and disclosure obligations, will be eliminated. Similarly, provision will not be made for a procedural costs fund and an arbitration court; instead, a new and moderate cost settlement rule without cross-financing will be established in the CPC.

3. Financial Institutions Act (FinIA)

3.1 General

The FinIA sets the authorisation conditions and other organisational requirements for financial institutions subject to prudential supervision. The requirements for financial institutions are formulated on a cross-sector basis insofar as possible and relevant, and thus create a level playing-field for the supervised persons and entities. The implementation of the legal provisions and the setting of detailed regulations for the individual authorised parties should be determined at ordinance level in line with the system currently applied. The scope of application of the FinIA will cover managers of individual client assets, managers of collective assets, fund management companies and securities firms (previously securities dealers).

The new prudential supervision of managers of individual client assets will result in a significant increase in the number of supervised entities and persons. At the same time, the aim is to take account of those managers of individual client assets that are organised as sole proprietorships and to establish supervision that is as moderate, sector-specific and flexible as possible. It would therefore make sense for the prudential supervision of managers of individual client assets to be performed by one or several supervisory organisations (SO) to be authorised by FINMA. The model of a managed semi-public supervisory organisation is based on the US Financial Industry Regulatory Authority (FINRA) model[1]. FINRA is a nongovernmental, not-for-profit organisation that supervises securities firms and brokers in the USA and ensures client protection and market integrity. Like FINRA, the SO will be organised as an independent institution with the powers to grant authorisation, perform supervision and pass sanctions.

3.2 Key features of the new regulations

– *Prudential supervision of managers of individual client assets and managers of the assets of occupational benefits schemes*: The main change is the prudential supervision of managers of individual client assets and managers of the assets of occupational benefits schemes. Another new development is the description of managers of collective investment schemes and those who manage the assets of occupational benefits schemes as "managers of collective assets". More stringent requirements will apply for them than for managers of individual assets.

– *FINMA supervision*: Managers of collective assets, fund management companies and securities firms will be supervised by FINMA.

– *SO supervision*: The prudential supervision of portfolio managers, trustees and precious metal traders will be performed by one or several supervisory organisations to be authorised by FINMA but nevertheless independent in their supervisory activity.

– *Risk-based supervision*: In the area of portfolio management, the two supervisory authorities will be given the power to establish an audit frequency of several years taking account of the activity of those supervised by them and the associated risks. In doing so, consideration will be given to the cost implications in particular of the new prudential supervision of managers of individual client assets.

– *Grandfathering clause*: Portfolio managers currently not subject to prudential supervision can benefit from a grandfathering clause and will be subject to no prudential supervision if they have sufficient experience (at least 15 years of activity) and confine themselves to serving existing clients.

– *Authorisation chain*: The FinIA will introduce the authorisation chain system. As a rule, the more complete form of authorisation will now include the subsidiary authorisation forms too. However, the authorisation chain regime does not exempt entities from fulfilling the duties for their respective activity; it merely exempts them from formally obtaining additional authorisation.

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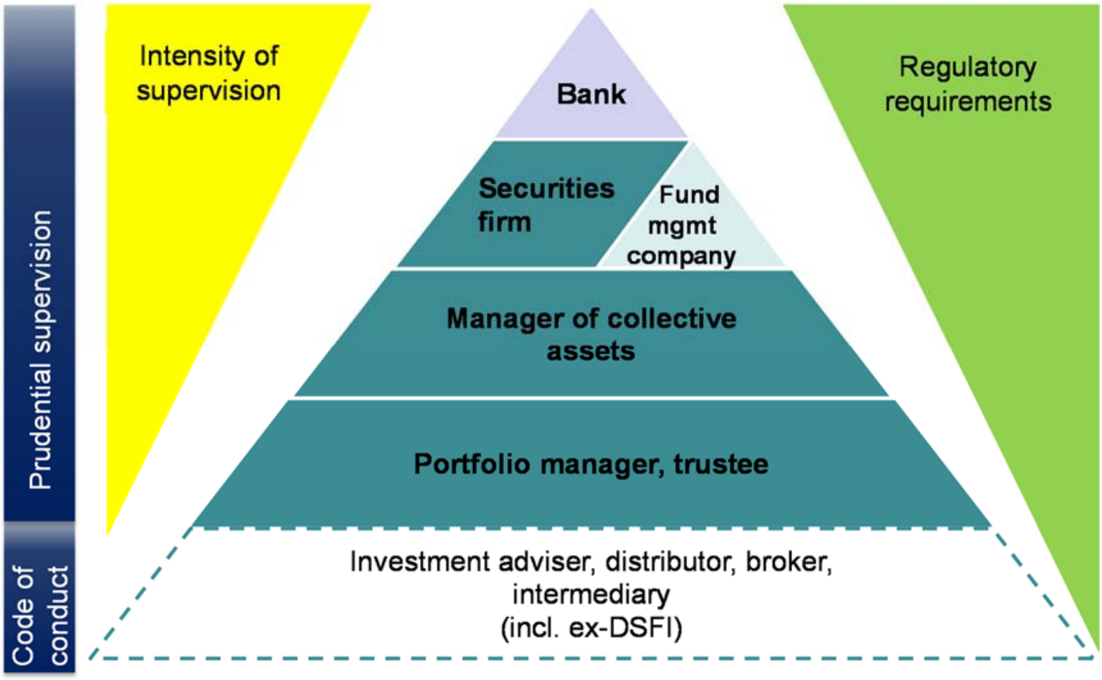
1 See www.finra.org.



– *Banks in the Banking Act*: Contrary to the preliminary draft, banks will remain governed by the Banking Act. Nevertheless, the provisions of the Banking Act will be amended to make them consistent with the requirements of the FinIA in terms of content. This will include ensuring that banks are integrated into the FinIA's new authorisation chain regime and can benefit accordingly.