

Federal Act on Financial Services : *paradigm shift for practitioners*

Association of International Business Lawyers (AIBL)

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I. Introduction : history and purpose

- Following the Madoff and Lehman cases, FINMA has clarified its objectives
- One of the objectives is to improve client protection in the Swiss financial market
- Analysis of the regulations (Switzerland, EU)
- Asymmetry in financial products (information) and providers' obligations
- FINMA report Distribution of financial products (October 2010)
- Position paper FINMA Distribution rules (February 24, 2012)
- One of the means contemplated : adopt a law on financial services

I. Introduction : history and purpose

- On June 27th 2014, the Federal Council has published the draft bill on the Financial Services Act (FinSA) and the Financial Institutions Act (FinIA) and opened a consultation
- The FinSA seeks to protect the clients of financial providers and to establish comparable conditions for the provision of financial services by financial service providers (FinSA 1 par. 1)
- On November 4th 2015, the Federal Council adopted the dispatch on the Financial Services Act (FinSA) and on the Financial Institutions Act (FinIA)

II. Scope of application

Financial service providers

(including client advisers, producers and providers of financial instruments) any persons who provide financial services on a professional basis in Switzerland or for clients in Switzerland (FinSA 2 al. 1 let. a *cum* 3 let. e).

There is a professional activity when the financial service provider carries out a self-employed economic activity generating a regular income under article 2 letter b Commercial Register Ordinance (ORC).

In accordance with the Banking Ordinance (OB), an activity is deemed to be carried out on a professional basis when the service provider

- Provides financial services to more than 20 clients, or
- Advertises for this purpose through advertisements in print or electronic media, using prospectuses or circulars.

II. Scope of application

Client advisers

Natural persons who perform financial services on behalf of a financial service provider or in their own capacity as financial service providers (FinSA 2 al. 1 let. b cum 3 let. f)

Producers and providers of financial instruments

(FinSA 2 al. 1 let. c)

III. Definitions

« **Financial service** » (FinSA 3):

- Acquisition or disposal of financial instruments;
- Receipt and transmission of orders in relation to financial instruments;
- Administration of assets (portfolio management);
- Provision of personal recommendations on transactions with financial instruments (investment advice);
- Granting of loans to finance transactions with financial instruments.

III. Definitions

« **Financial instruments** » (FinSA 3):

- Equity securities (ex. shares, participation certificates, dividend rights certificates)
- Debt instruments
- Collective investment schemes
- Structured products
- Derivatives within the meaning of art. 2 let. c of the Financial Market Infrastructure Act (FMIA)
 - Financial contracts whose value depends on one or several underlying assets and which are not cash transactions
- Redeemable life insurance policies
- Deposits whose redemption value or interest is risk- or price-dependent
- Bonds

III. Definitions

« **Professional clients** » (FinSA 4 par. 3):

- a. Financial intermediaries as defined in the Banking Act, the Financial Institutions Act and the Collective Investment Schemes Act;
- b. Insurance companies;
- c. Foreign clients subject to an equivalent form of prudential supervision to the persons listed under a and b above;
- d. Central banks;
- e. Public entities with professional treasury operations;
- f. Occupational pension schemes with professional treasury operations;
- g. Companies with professional treasury operations.

➔ Opting-in possible (FinSA 5 par. 2) : professional and institutional clients may declare that they wish to be treated as retail clients.

III. Definitions

« **Retail clients** » (FinSA 4 par. 2):

Clients who are not professional clients.

➔ Opting-out possible (FinSA 5 par. 1) : high-net-worth retail clients may declare that they wish to be treated as professional clients.

« **Institutional clients** » (FinSA 4 par. 4):

- a. Financial intermediaries as defined in the Banking Act, the Financial Institutions Act and the Collective Investment Schemes Act ;
- b. Insurance companies;
- c. Foreign clients subject to an equivalent form of prudential supervision to the persons listed under a and b above ;
- d. Central banks;
- e. National and supranational public entities with professional treasury operations.

IV. Code of Conduct

Duty to provide information before the provision of the service (FinSA 9 and 10) and in case of material changes (FinSA 10 par. 5) of the following:

- Their name and address;
- Their field of activity and supervisory status;
- The possibility of obtaining information on the basic training and continuing professional development of client advisers;
- The possibility of initiating mediation proceedings before a recognised ombudsman;
- The financial service offered (before providing an advisory service in investment or asset management, the financial service provider must inform its clients whether or not this service implies a continuous assessment of the adequacy of the recommended financial instruments) and the associated risks and costs;
- The business affiliations with third parties in connection with the financial service offered;
- The financial instruments offered and the associated risks and costs;
- The market offer taken into account when selecting the financial instruments;
- The form and manner of the custody of the financial instruments and the associated risks and costs.

IV. Code of Conduct

Assessment of appropriateness (FinSA 12):

A financial service provider that provides investment advice for individual transactions without taking account of the entire portfolio must enquire about its clients' knowledge and experience and must check whether financial instruments are appropriate for its clients before recommending them.

Exemption: « *execution only* » or « *reverse solicitation* »

In this case, the client shall be informed that an appropriateness or suitability assessment will not be performed (FinSA 14).

IV. Code of Conduct

Suitability (FinSA 13)

A financial service provider that provides investment advice taking account of the client portfolio or portfolio management must enquire about its clients' financial situation and investment objectives as well as their knowledge and experience before recommending suitable financial instruments to them within the framework of investment advice or before making corresponding investments within the framework of portfolio management.

Establishment of an individual profile for each client.

Currently: case law of the Federal Court and duty to establish a client's risk profile (entry into force on July 1st 2013) pursuant to the cm 7.1 and 7.2 of the Circ. FINMA 2009/1 Règles-cadres pour la gestion de fortune.

IV. Code of Conduct

Non-assessable or lack of appropriateness or suitability

If the information received by the financial service provider is insufficient for assessing the appropriateness or suitability of a financial instrument, it shall inform the client before providing the service that it cannot perform this assessment (FinSA 16 par. 1).

If the financial service provider is of the opinion that a financial instrument is not appropriate or suitable for its clients, it shall advise them against it before providing it (16 par. 2 FinSA).

IV. Code of Conduct

Financial service providers shall document in an appropriate manner (FinSA 17):

- the financial services agreed with clients and the information collected about them;
- the notification described in Article 14 paragraph 2 (execution only or reverse solicitation), or the fact that they advised the clients in accordance with Article 16 against provision of the service;
- the financial services provided for clients.

When providing portfolio management and investment advice, they shall also document clients' needs and the grounds for each recommendation leading to the acquisition, holding or disposal of a financial instrument.

Financial service providers shall provide their clients with a copy of the documentation (FinSA 18) : financial services provided, valuation and development of the portfolio, costs associated with the financial services.

V. Organisation

Appropriate organisation (FinSA 23), staff (FinSA 24) and delegation (FinSA 25 et 26)

Financial service providers shall ensure that they fulfil their duties under this Act through internal regulations and an appropriate organisation of operations (FinSA 23).

Financial service providers shall ensure that their staff possess the necessary skills, knowledge and experience to perform their work (FinSA 24).

Financial service providers that mandate another financial service provider to provide a financial service for clients remain liable for the completeness and accuracy of the client information and for fulfilling the duties set out in Articles 9 to 18 FinSA (FinSA 26).

V. Organisation

Conflicts of interest (FinSA 27) and compensation from third parties (FinSA 28)

Financial service providers shall take appropriate organizational measures to prevent conflicts of interest that could arise. If disadvantages for clients cannot be excluded, this possibility must be disclosed to them (FinSA 27);

Financial service providers may accept compensation from third parties in association with the provision of financial services only if they (FinSA 28) :

- a. have expressly informed the clients of such compensation in advance (type, size/amount or extent, calculation criteria); or
- b. pass the compensation on to the clients in full.

VI. Client advisers

- Definition: natural persons who perform financial services on behalf of a financial service provider or in their own capacity as financial service providers (FinSA 3 let. f);
- Client advisers of Swiss and foreign financial service providers not subject to the supervision in accordance with article 3 of the Financial Market Supervision Act (FINMASA) (i.e. they are not subject to an authorization) may carry out their activity in Switzerland only if they are entered in a register of advisers (licensed by FINMA), whether the advisers carry out their activity in Switzerland or abroad.

VI. Client advisers

- Registration conditions:
 - To have completed the basic training and continuing professional development set out in Article 6 to be entered in the register;
 - To have taken out professional indemnity insurance or that equivalent collateral exists;
 - To be affiliated to an ombudsman (FinSA 77);
 - No conviction of criminal charges mentioned at article 31 par. 2 FinSA (e.g. property offences under articles 137 to 172 ter of the Swiss Criminal Code);
 - No prohibition from performing the activity to be registered in accordance with article 33a FINMASA.

VII. Offering of Financial Instruments

Duty to publish a prospectus

Any person in Switzerland who makes a public (FinSA 3 let. i) offer (FinSA 3 let. h) for the acquisition of securities or any person who seeks admission of securities to trading on a trading venue in accordance with art. 26 of the Financial Market Infrastructure Act must first publish a prospectus (FinSA 37), unless the offer:

- Is addressed solely at investors classified as professional clients;
- Is addressed at fewer than 150 investors classified as retail clients;
- Is addressed at investors acquiring securities to the value of at least CHF 100,000.-;
- Has a minimum denomination per unit of CHF 100,000.-;
- Does not exceed a total value of CHF 100,000.- over a 12-month period.

VII. Offering of Financial Instruments

Duty to publish a prospectus

List of exemptions (FinSA 39) by type of securities

- For instance: in case of merger, provided that there are indications equivalent to the prospectus.

Relaxation of requirements (FinSA 49):

- If the issue is subject to a limited control, i.e. if the two of following volumes in the preceding financial year has not been exceeded:
 - Balance sheet total of CHF 20 million;
 - Turnover of CHF 40 million;
 - 250 FTEs on average for the year.

VII. Offering of Financial Instruments

Duty to publish a prospectus

- The prospectus' content (FinSA 42), abolition of the articles 652a and 1156 CO, as well as the art. 752 CO on liability
- Specific rules for collective investment schemes (FinSA 50)
- Review of the prospectus by a reviewing body licenced by the FINMA (FinSA 53) and duty to publish (FinSA 67)

VII. Offering of Financial Instruments

Duty to produce a key information document

Where a financial instrument is offered to retail clients, the producer must first produce a key information document which meets the requirements listed in article 63 FinSA (FinSA 60).

Persons who offer securities in the form of shares, including share-like securities allowing for participation rights, such as participation certificates and dividend rights certificates, are not obliged to prepare a key information document.

VII. Offering of Financial Instruments

Duty to produce a key information document

- Contents (FinSA 63)
- Duty to publish (publication means in art. 67 FinSA, possible in electronic form)
- Liability (FinSA 72) for the «resultant losses »

VIII. Provision of Documents

- The financial service provider shall provide the client with a copy of the documents in question free of charge within 30 days after receipt of such request (FinSA 75 et 76)
- A refusal by the financial service provider to supply the requested documents may be taken into account by the competent court in any subsequent legal dispute when deciding on procedural costs (FinSA 76 par. 4)

IX. Mediation proceedings

- Disputes regarding legal claims between the client and the financial service provider should be settled by an **ombudsman** in mediation proceedings if possible (FinSA 77);
- Proceeding principles in art. 78 sqq. FinSA:
The statements made by the parties within the framework of mediation proceedings and the correspondence between a party and the ombudsman may not be used in other proceedings (FinSA 78 par. 2).

IX. Mediation proceedings

- Ling a mediation request with an ombudsman does not rule out civil action and does not prevent such from being initiated (FinSA 79 par. 1);
 - The ombudsman shall terminate the procedure once a conciliation authority, a court, a court of arbitration or an administrative authority begins dealing with the case (FinSA 79 par. 3);
 - After bringing proceedings before an ombudsman, the plaintiff may unilaterally waive a conciliation procedure under the Civil Procedure Code (FinSA 79 par. 2).
- Duty to affiliate to an ombudsman (FinSA 80 and 31 par. 1 let. c);
- Financial service providers shall inform their clients – upon entering to a business relationship – about the possibility of mediation proceedings through an ombudsman (name and address of the ombudsman, FinSA 82 par. 2)

X. Civil action

Modification of the CPC: art. 114a nCPC

In litigation proceedings for dispute involving financial services or claims from the deposit, loan or insurance business:

- No advance payment of costs (CPC 98)
- No security for the party costs (CPC 99)

X. Civil action

The financial service provider must bear its own costs, even if it has obtained a favorable ruling, provided that the following conditions are met cumulatively:

- The retail client (plaintiff) has filed for the same case a request for mediation to the ombudsman, to which is affiliated the service provider or has participated in the proceedings;
- The financial situation of the retail client (plaintiff) is not exceptionally good;
- The litigation value (the amount of claims) does not exceed CHF 250,000; and
- The retail client has not act in bad faith or recklessly.

XI. Entry into force

Possible entry into force : 2017-2018

The Federal Council can make provision for a transitional period for the acquisition of the basic training and continuing professional development set out in Article 6 FinSA.

Transitional period:

- Within 6 months of the Act coming into force:
 - Client advisers must report to the registration body;
 - Financial service providers must be affiliated to an ombudsman.
- Provisions of the Act will apply two years after entry into force :
 - In case of securities for which a public offer was made or a request was made for admission to trading on a trading venue before entry into force;
 - In the case of financial instruments that were offered to retail clients before into force.

XII. Questions

Thank you for your attention

Le projet de loi présenté dans le présent document est au stade de la consultation. Certaines règles présentées dans le présent document peuvent être modifiées à l'avenir en fonction de l'évolution du projet de loi. Par ailleurs, les informations contenues dans ce document ne sont pas exhaustives et ne constituent en aucun cas un conseil juridique.

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