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Swiss Parliament Adopts Innovative DLT Legislation

On 10 September 2020, the Swiss Council of States (the small chamber of Swiss parliament) unanimously resolved to approve the new Federal Act on the Adaptation of Federal Law to Developments in the Technology of Distributed Electronic Registers (the "**DLT Act**").¹ Previously, the National Council (the large chamber of Swiss parliament) had already passed the draft DLT Act with a few amendments, also unanimously. It is expected that the law will be passed in the final parliamentary vote scheduled for the end of September and that the DLT Act will come into force early next year.

The DLT Act is a framework act comprising a bundle of revisions to various existing Swiss federal acts. In a bold move demonstrating Switzerland's openness to the use of cutting edge technology, the new law is aimed at enhancing legal certainty, removing obstacles for applications of distributed ledger technology ("**DLT**") and limiting the risk of misuse.

Key Elements of the DLT Act

The DLT Act, as amended by parliament, introduces targeted amendments to financial regulation, insolvency law, international private law and – remarkably – civil securities law. The key elements of the DLT Act are as follows:

Civil Securities Law

Creation of a legal basis for **uncertificated register value rights** as an instrument for the digitisation or tokenisation of assets (rights) such as shares, bonds and other financial instruments, as well as for the transfer of such instruments.

Financial Regulation

Introduction of a **new regulatory licence category for DLT trading facilities**.

Insolvency Law

Specific rules on the **segregation of crypto-based assets from the bankruptcy estate**, both in general insolvency and bank insolvency, as well as on **the access to data**.

¹ See https://www.parlament.ch/de/services/news/Seiten/2020/20200910092808664194158159041_bsd039.aspx (in German).

Separately, the DLT Act includes an amendment to Swiss financial services and financial institutions regulation providing for an **exemption from the requirement for financial institutions and financial services providers to join an ombudsman's organisation**. The relief applies to institutions/providers who **render their services exclusively to institutional or professional clients** (as defined in the Financial Services Act; FinSA). This exemption had been urgently sought by the financial services industry and was primarily included in the DLT Act so that it could benefit from the accelerated process through which this bill has proceeded, though the revision may also benefit small DLT trading facilities.

Compared to the draft DLT Act originally submitted to parliament by the Federal Council (the Swiss federal executive government) at the end of 2019, only a few changes were introduced during the deliberations in the National Council, in particular with regard to the accessibility of data in a bankruptcy estate.

Introduction of Register Value Rights (Civil Securities Law)

A key piece of the DLT Act is the introduction of so-called "register value rights" (*Registerwertrechte; droits-valeurs inscrits*) into the canon of securities pursuant to the Swiss Code of Obligations (CO). These are uncertificated value rights that can serve the same functions as "traditional" paper securities or centrally registered book-entry securities (*Bucheffekten; titres intermédiés*), enabling e.g. the issuance of shares in a company as register value rights based on a decentralised electronic ledger. This change is particularly noteworthy as Swiss civil securities law has traditionally been rather rigid.

The new articles 973d *et seq.* CO provide for a non-deterministic set of rules on register value rights and their legal characteristics, outlining the principles of their establishment, transfer, pledge and cancellation. Specifically, register value rights are distinguished from "simple value rights" (*einfache Wertrechte; droits-valeurs simples*; formerly just called "value rights"), which are governed by the amended article 973c CO and which do not have the specific features

and rights attaching to register value rights. In particular, the provisions of the CO on register value rights protect the good faith of persons relying on the register entry (e.g. the debtor of a claim or the acquirer of a share in the form of a register value right, see article 973e CO) in a fashion similar to traditional securities, while simple value rights do not offer such protection.

Register value rights can only be created, exercised or transferred by way of a register fulfilling the eligibility criteria set out in the key provision of article 973d CO:

1. the register has to enable the creditors, but not the debtor, to dispose over their rights using technological processes;
2. the integrity of the register has to be protected against unauthorised modifications using adequate technological and organisational measures, such as the collective administration by various independent parties;
3. the content of registered rights, the functionality of the register and the registration agreement have to be saved in the register itself or in linked associated data;
4. the creditors must be able to view the information concerning them as well as the register entries and must be able to verify the integrity of the register content concerning them without the assistance of third parties.

The technical details of the implementation of an eligible register and register value rights in practice are left to the private sector. This is at the same time an expression of the principle of private autonomy in Swiss civil law and a safeguard against the law being overtaken by technical developments.

New DLT Trading Facility Regulatory Licence Type (Financial Regulation)

A further important element of the DLT Act is the creation of a new regulatory licence type in the Financial Market Infrastructure Act (FMIA) for the operation of a DLT trading facility, defined as a professionally operated venue for the multilateral trading of DLT securities. According to the new law, DLT securities (from a regulatory point of view) include (a) register value rights in the meaning of article 973d CO (see above), and (b) other value rights that are held on electronic registers and enable the creditors, but not the debtor, to dispose over their rights using technological processes.

Potential participants of a DLT trading facility are *inter alia* securities firms, other entities that hold a licence or recognition by FINMA, or foreign entities subject to an equivalent supervision. However, unlike stock exchanges and multilateral trading facilities (MTF) under the FMIA, DLT trading facilities can also admit unregulated entities and individuals to their systems if such participants declare that they act in their own name and on their own account. Entities holding a DLT trading facility licence may also operate an organised trading facility (OTF) which was so far only possible for banks, securities firms and authorised or recognised trading venues.

The new licence type is based on the existing regulatory concepts of the FMIA and the law refers to existing requirements for financial infrastructures where appropriate. The amendments to the FMIA in the context of the DLT Act include in particular specific rules around client protection, which are based on the requirements set forth in the FinSA.

Segregation of Crypto-Based Assets in Bankruptcy (Insolvency Law)

The main innovation of the DLT Act with respect to insolvency law is a newly introduced article 242a in the Debt Enforcement and Bankruptcy Act (DEBA) governing the segregation of "crypto-based assets" (*kryptobasierte Vermögenswerte; cryptoactifs*) in bankruptcy. Article 242a DEBA in particular provides a legal basis for segregation in scenarios where crypto-based assets are held in collective storage, provided it is possible to identify which part belongs to the specific claimant.

These changes to the DEBA have also been reflected in amendments to the provisions of the Federal Banking Act (BankA) on custody assets (articles 16 and 37d BankA).

Beyond this, the amended DEBA provides for new rules to govern the segregation of data. Article 242b DEBA creates a legal basis for creditors to claim access to data over which the bankruptcy estate has power of disposal. The claim is intended to cover physical and non-physical (digital) data, including in particular data required to access or dispose over digital assets.

Outlook

The fact that parliament treated the adoption of the DLT Act as a matter of urgency and that both the National Council and the Council of States approved it unanimously with minimal changes shows that there is broad consensus in the Swiss political landscape regarding the importance of a flexible, reliable, forward looking framework for blockchain and DLT businesses. It can be expected that the new law will be finalised and scheduled for entry into force with similar expediency and one may look forward to the rapid adoption of the new instruments by market participants.

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