

Briefing June 2019

The Future of the EU Equivalence Assessment for Swiss Trading Venues: an Update

On 30 June 2019, the temporary recognition of the equivalence of the Swiss legal and supervisory framework applicable to SIX Swiss Exchange and BX Swiss for purposes of article 23 of Regulation (EU) No 600/2014 (MiFIR) will expire. This briefing analyses what could happen if the EU Commission does not extend the equivalence recognition. In particular, it outlines the impact of the Ordinance on the Recognition of Foreign Trading Venues for the Trading of Equity Securities of Companies with a Registered Office in Switzerland of 30 November 2018 (the Ordinance) on trading of shares in Swiss issuers in the EU and Switzerland in such event.

Background

The EU Commission is expected to reach a decision on how to proceed in the coming days. Three scenarios are possible:

- the best-case scenario would be a final recognition regarding the equivalence of Swiss law. This outcome is, however, unlikely given that the EU Commission has tied its determination to a binding overarching Institutional Framework Agreement governing the relations between Switzerland and the European Union;
- the most balanced scenario would see a further extension of the temporary recognition. This decision would be motivated by the fact that the Swiss government had concluded its consultation process and endorsed to a large extent the Institutional Framework Agreement, subject to certain clarifications.
- A third scenario is, however, also likely in light of the clarification requests voiced by the Federal Council. The EU Commission could find that the position of the Swiss Federal Council falls short of the "full,

final and clear endorsement" which the EU Commission had stated would be a precondition for future extensions of the equivalence, and therefore decide to refuse any further extension of the recognition.

If the last scenario were to play out, trading on the Swiss stock exchanges, SIX Swiss Exchange and BX Exchange, would be put at risk. Indeed, pursuant to article 23 (1) of MiFIR, adopted in connection with Directive 2014/65/EU (MiFID II), EU investment firms are required to ensure that the trades they undertake in shares admitted to trading on a regulated market or traded on a trading venue in the EU shall, subject to certain exceptions, take place either (i) on a regulated market or a multilateral trading facility (MTF) or through a systematic internalizer in the EU, or (ii) on a third-country trading venue assessed as equivalent in accordance with article 25(4)(a) of MiFID II. However, to avoid conflicts with best execution obligations, an exception to this requirement applies for trades where "their characteristics include that they are non-systematic, ad-hoc, irregular and infrequent" (article 23(1)(a) MiFIR).

Indirect Remedy: Loss of Recognition for EU Trading Venues to Trade Swiss Shares

To provide an indirect assurance that EU investment firms can continue to trade Swiss shares on Swiss stock exchanges notwithstanding a possible expiry of the equivalence recognition, the Swiss Federal Council passed the Ordinance on 30 November 2018 (see our [Briefing of December 2018](#)).

Pursuant to the Ordinance, foreign trading venues need a recognition from FINMA if they allow or facilitate trading of equity securities of issuers domiciled in Switzerland, which are also listed on a Swiss stock exchange or traded on a Swiss trading venue. This recognition is possible if two conditions are satisfied: if the foreign trading venue is "(a) subject to appropriate regulation and supervision; and (b) does not have its registered office in a jurisdiction that restricts its market participants in trading equity securities of companies with registered office in Switzerland at Swiss trading venues and thereby significantly adversely affects the trading in such equity securities at Swiss trading venues" (article 2 (1) of the Ordinance).

Following the extension of the temporary equivalence recognition assessments in December 2018, FINMA recognized EU trading venues under the Ordinance. However, if the equivalence is no longer extended, FINMA will have to revoke this recognition as the second condition will no longer be satisfied (see article 2 (1)(b) of the Ordinance). As a consequence, EU trading venues will no longer be allowed to trade Swiss equity securities listed in Switzerland (with a few exceptions for certain 'grandfathered' securities) and, consequently, it is expected that the Swiss shares will cease to be "admitted to trading on a regulated market or traded on a trading venue" in the European Union.

If some European trading venues continue to trade Swiss securities, and some trading in Swiss shares persists, then EU investment firms will need to consider whether they are permitted to continue trading on Swiss stock exchanges under the exception provided by article 23(1)(a) MiFIR in respect

of "non-systematic, ad-hoc, irregular and infrequent" trading. Prior guidance from ESMA suggests that it is sufficient, for this exception to apply, for the trading of Swiss shares in the EU to be non-systematic etc. (regardless of the global trading). Therefore, if the trading is limited, the exception will nevertheless still apply and EU investment firms will continue to be permitted to trade on Swiss exchanges notwithstanding the expiration of the equivalence decision in the EU.

Sanctions and Enforcement

To ensure compliance with the Ordinance, article 5 designates it as a Swiss financial markets act. Consequently, FINMA can take enforcement action against supervised entities, including foreign trading venues that are already recognized in Switzerland because they admit Swiss regulated financial institutions as participants. FINMA may also take enforcement action against supervised market participants who execute trades in Swiss shares on EU trading venues that are not recognized under the Ordinance. FINMA will have authority to act not only against Swiss banks and securities dealers but also against EU investment firms who have participant status on a Swiss stock exchange and are licensed to that effect by FINMA (article 40 of the Financial Market Infrastructure Act (FMIA)). In this context, the supervisory measures FINMA can order range from a declaratory ruling (article 32 FINMASA) to the revocation of the licence (article 37 FINMASA) and include the power to order measures to restore compliance with the law, even where the firms themselves are not guilty of a breach of their supervisory obligations (article 31 FINMASA).

Furthermore, article 44 of the Federal Act on the Swiss Financial Market Supervisory Authority (FINMASA) makes it a criminal offence to carry out wilfully or negligently an activity requiring a licence, recognition or registration under the Swiss financial market acts, without such licence, recognition or registration. In connection with the Ordinance, these criminal sanctions would apply primarily to the decision-makers (directors and executive managers) of non-compliant foreign trading venues.

Overall, these sanctions are likely to cause most trading venues to comply with the Ordinance and investment firms to avoid any trading venue that would continue to trade Swiss securities without being recognized by FINMA as soon as FINMA decides to revoke the recognition of EU trading venues.

It will still be possible to avert this consequence if the EU Commission extends the temporary equivalence recognition for Swiss stock exchanges or permanently recognizes the equivalence of the Swiss legal framework before 30 June 2019. In such an event, EU trading venues will maintain their recognition from FINMA under the Ordinance and trading of Swiss securities in the EU will not face disruption.

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