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Banking Regulation 2022

Switzerland: Trends & Developments
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Trends and Developments

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Dealing with Prospective Clients under Swiss Financial Services Legislation

The new Swiss financial services legislation came into force at the beginning of 2020. After a transitional period of two years, which will come to an end on 31 December 2021, all financial service providers will move to a new regime when dealing with prospective and actual clients in or from Switzerland. In that context, they will be required to comply with conduct of business and organisational rules.

As is the case under foreign legislation, Swiss law provides for certain exemptions from the application of the new rules. Such exemptions generally depend on the category of clients. In order to rely on such exemptions, and also as expressly required by law, the financial service providers will have to classify their clients in the relevant categories (institutional, professional or retail clients).

The new rules apply to the services rendered to actual clients. However, the law does not provide any guidance as to how the financial service provider should deal with prospective clients. Is the new legislation already applicable when one meets with a prospective client? What measures can be taken to mitigate potential issues? This article aims to outline these issues and put forward certain unforeseen consequences of the new legislation.

Regulation of financial services and promotion

Five different types of financial services are regulated under the Swiss Financial Services Act (FinSA):

- the receipt and routing of orders relating to financial instruments;
- the management of such instruments (portfolio management);
- the provision of personalised recommendations on such instruments (financial advice);
- the granting of credits to finance transactions on such instruments; and
- the acquisition or alienation of financial instruments.

Financial instruments include shares, bonds and other securities, units of collective investment schemes, derivatives and structured products and deposits.

The FinSA requires the classification of investors into the following three categories of clients.

- Professional clients include regulated financial intermediaries and insurance companies, central banks, large enterprises, public and private institutions (including pension funds) with professional treasury management, and professionally managed private investment structures.
- Retail clients comprise all investors that are not – or have elected not to be – considered as professional clients.
- Institutional clients is a third category that regroups a sub-category of professional clients (ie, the regulated institutions and the central banks) and national and supra-national institutions governed by public law, provided that they have professional treasury management.

Qualifying high net worth individuals may opt out from the retail investor protection regime and

elect to be considered as professional clients (elective professional clients).

Financial service providers operating from Switzerland are, in principle, licensed by the Swiss Financial Market Supervisory Authority (FINMA) and directly regulated by the FINMA or a surveillance body approved by the FINMA. If they are not regulated, they are required to register their relevant employees with a recognised registry of advisers. If they serve retail clients, they must also be affiliated with an ombudsman office that is recognised by the Swiss Federal Finance Department.

Before starting to provide financial services or entering into the respective contracts, financial service providers must furnish certain information to the client on the services provided, the risks involved and the costs payable by the client, among other matters. Financial advisers have to verify the appropriateness of the isolated recommendations they give to clients. If the advisory service takes into account the entire portfolio of the client, the adequacy of the advice must be warranted.

Certain obligations do not apply when the client served is an institutional or a professional client. In order to ascertain their obligations, financial service providers must, pursuant to Article 4 of the FinSA, classify their clients in the relevant categories; alternatively, they may consider all their clients as retail clients and afford them the highest level of client protection set out in the FinSA.

The elective professional clients must fulfil certain high net worth individual criteria in order to opt out from the retail client category, thereby waiving such highest level of protection. Their opting-out must be documented and cannot be presumed. Furthermore, any client classified in a particular category may opt in to a category with

a higher level of protection – eg, professional clients may declare in writing that they elect to be treated as retail clients. When a financial service provider has classified a client to a category other than that of retail clients, it must advise the client of the possibility for the client to opt in at any time to a category with greater protection.

In addition, by virtue of their status under the FinSA, professional and institutional clients are considered as qualified investors under the Swiss Collective Investment Schemes Act (CISA). Non-Swiss funds that have not been approved by the FINMA for marketing towards any type of investors may be proposed to qualified investors by way of private placement, subject to the designation of a representative and a paying agent in Switzerland if the qualified investors targeted by the marketing efforts include elective professional clients. Clients (including retail clients) who enter into a long-term discretionary management or advisory relationship with a financial intermediary regulated in Switzerland or abroad are also considered as qualified investors under the CISA.

The marketing of other financial instruments is subject to additional disclosure requirements. In particular, a key information document must be provided to retail clients when financial instruments (other than plain vanilla shares or bonds) are proposed to them. Special requirements apply with respect to the issuer when the financial instrument is a structured product.

While Swiss law does not expressly include financial promotion legislation, the marketing of financial instruments is still regulated, even if it does not involve any recommendation or advice. Due to the inclusion of the acquisition of financial instruments in the list of financial services regulated under the FinSA, any activity aimed specifically at (ultimately) the acquisition or sale of a financial instrument is considered a financial

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service, even if no advice is provided nor offer made at that relatively early stage. This does not include the sharing of information with other financial intermediaries – eg, within the framework of roadshows.

Nevertheless, when a prospective client is not evidently a financial intermediary, the FinSA implies that no financial instruments are marketed to such client if such marketing would qualify as a financial service, in the event that the financial service provider has not classified the client and, therefore, is not in a position to determine whether the relevant product may or may not be offered to the relevant client. For instance, a foreign fund that has not been approved by the FINMA cannot be offered to a Swiss retail client. Even the pre-marketing of the product is potentially a financial service, even though it does not yet involve an offer to subscribe. A pre-classification of clients may not be fully sufficient to avoid the issue, due to the possibility for the client to opt out or opt in for another category.

Relying on exemptions

Reverse solicitation

As is the case in the European Union, the FinSA does not apply in the case of reverse solicitation, but that concept is narrowly defined. The exemption applies exclusively to financial services provided at the express initiative of the client – or within the framework of a pre-existing clientele relationship established at the express initiative of the client. The exemption is only applicable, therefore, if the financial service provider has not first been in touch with the potential client; practically speaking, any prior contact made at the initiative of a financial service provider excludes subsequent reliance on reverse solicitation. Hence, when dealing with prospective clients, financial service providers may rarely rely on that exemption. They must define a process whereby they can classify their clients as early as possible.

Category of clients

If the clients are considered as institutional and professional clients per se (eg, retirement benefit institutions with professional treasury management) or are elective professional clients, the financial service provider may assume, absent any contrary indication, that the client is able to independently assess the appropriateness and suitability of the service. Furthermore, no disclosure requirements apply in relation to the offering documentation relating to financial instruments proposed to professional clients. The financial service provider is, therefore, relieved from the duty to provide the client with a key information document, and no prospectus requirement applies. Provided that the professional client is an institutional or professional client per se, there is no need to appoint, for foreign funds, a representative and paying agent in Switzerland, nor does the ombudsman affiliation requirement apply. These requirements are only triggered when the client is an elective professional client. Therefore, even if a particular fund has appointed a representative and a paying agent in Switzerland, a financial service provider cannot pre-market such a fund to a prospective client if such client is a retail client, for as long as he/she has not delivered an opting-out statement to the financial service provider – a step that is generally completed only after the client has been onboarded. This issue significantly reduces the range of financial instruments that a private bank or portfolio manager can emphasise when meeting with a potential client.

Furthermore, only institutional clients per se may be served without first fulfilling the information duties applicable to financial service providers. Indeed, while professional clients who are not institutional clients may waive such information duty, such a waiver has to be given in writing or in an equivalent form. Such a waiver would obviously be granted during the onboarding process only; as a result, the financial service provider

may be tempted to treat professional clients who are not institutional clients (eg, private investment vehicles with professional treasury management) similarly to retail clients for as long as they have not been onboarded as clients.

Foreign financial service providers

Regulated foreign financial service providers may target Swiss institutional and professional clients per se without registering their client advisers in Switzerland. Again, this exemption requires a pre-classification of clients. Once the classification has been made, the client must be informed that it may opt in to a new regime. Again, due to the broad description of financial services, such notification should be done prior to marketing financial instruments.

Conclusion

The objective of the FinSA was to ensure the fair treatment of all financial service providers and the application of similar duties to them, regardless of the level of regulation to which they are subject. Banks, for instance, are pleased with the idea that competitors such as independent asset managers are eventually subject to the same rules as those applicable to banks, with one of the objectives of the FinSA being to create a level playing field for all institutions that provide similar services. However, the new rules have some side effects, with which financial service providers are becoming progressively familiar.

Except for potential clients whose status appears evident, such as that of a retirement benefit institution or large enterprises, pre-classifying clients under the FinSA is not an easy task. Eventually, it does not always seem practical to restrict the scope of prospective clients to whom one may freely present a full range of services and products to institutional clients. One of the consequences of the FinSA, therefore, is to complicate the marketing process for financial services.

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vate individuals in Switzerland and around the world. Most of the firm's work has an international component, and its extensive network consists of correspondent law firms that are all market leaders in their jurisdictions. The team has broad experience in handling cross-border proceedings and transactions.

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