Banking & Finance Brochure

OA LEGAL

SWISS INNOVATIVE LAW FIRM

FinSA - FinIA

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Financial Services Act (FinSA)

The FinSA, entered into force on January 1, 2020 seeks to protect clients of financial service providers and to establish comparable conditions for the provision of financial services by financial service providers.

FinSA contains legal requirements for diligence and transparency in the provision of financial services and governs the offering of financial instruments.

FinSA sets for new rules in the Swiss financial industry, including in terms of clients' segmentation, documentation, reporting to the client as well as internal organization.

Financial services are *any of the following activities* carried out for clients (whether retail, professional clients or institutional clients):

- acquisition or disposal of financial instruments, which includes the offering and marketing of financial instruments (FinSA replaced the word "distribution" by "offer")
- receipt and transmission of orders in relation to financial instruments (execution only)
- administration of financial instruments (portfolio management / gestion de fortune)
- provisions of personal recommendations on transactions with financial instruments (investment advice)
- granting of loans to finance transactions with financial instruments.

Financial Institutions Act (FinIA)

The FinIA, entered into force on January 1, 2020 governs the authorization and organizational requirements to act as a financial institution.

The following **“financial institutions”** are subject to authorization under the FinIA:

Individual portfolio managers:
A portfolio manager is a person mandated to manage assets on a commercial basis in the name of and on behalf of clients.

Trustees:
A trustee is a person who on a commercial basis manages or holds a separate fund for the benefit of the beneficiaries or for a specified purpose, based on the instrument creating a trust within the meaning of the Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on their Recognition.

Managers of collective assets:
A manager of collective assets is a person who manages assets on a commercial basis in the name and on behalf of collective investment schemes or occupational pension schemes.

Fund management companies:
A fund management company is an entity that manages investment funds independently in its own name and for the account of investors.

Securities firms:
A securities firm is an entity that, on a commercial basis:

a. trades in securities in its own name for the account of clients;

b. trades in securities for its own account on a short-term basis, operates primarily on the financial market and could jeopardise the proper functioning of the financial market or is a member of a trading venue; or

c. trades in securities for its own account on a short-term basis and publicly quotes prices for individual securities upon request or on an ongoing basis (market maker).

Persons operating primarily in the financial sector may perform the following activities only if they have authorization as a securities firm:

a. underwriting securities issued by third parties and offering these to the public on a primary market on a commercial basis;

b. creating derivatives in the form of securities and offering these to the public on the primary market on a commercial basis.

FINMA AUTHORIZATION

In order for a financial institution to obtain an authorization from the Swiss Financial Market Supervisory Authority (hereafter: "FINMA"), such financial institutions shall fulfil the conditions set out in the FinIA.

While all financial service providers have to be compliant with the FinSA, the FinIA is limited to a specific category of financial institutions (portfolio managers, trustees, managers of collective assets fund management companies and securities firms), subject to authorization. Providing "only" investment recommendations (advices) and/or offering financial products services does not - as such - fall under the FinIA, in other words is not subject as such to an authorisation by FINMA, but is subject to the duty to register in one of the existing registers of advisers.

As a general remark, the financial institution must implement specific appropriate corporate governance rules and be organised in such a way that it can fulfil its statutory duties.

The financial institution shall implement a risk management (including compliance) and internal control system to identify, measure, control and monitor its risks, including legal (compliance) risks, and organise effective internal controls. The financial institution and the persons responsible for its administration and management must provide the guarantee of irreproachable business conduct.

FINMA Authorization

Other requirements under FinIA relate to the effective place of management (which shall be in Switzerland for Swiss entities), delegation of tasks, minimum capital requirements, own funds ratio (ratio concernant les fonds propres), ombudsman’s office (organe de mediation), supervisory organisation (organe de surveillance) and audit firm.

As an exemple, portfolio managers & trustees should provide proof that they are subject to a supervisory organisation in accordance with art. 43a of the Federal Act on the Swiss Financial Market Supervisory Authority (hereafter: "FINMASA").

In addition to these general rules, specific requirements are set per category of authorisation.

As soon as the authorization is granted, the financial institution can register within the commercial register.

A transitional period applies for entities that were active before January 1, 2020.

Authorisation chain (FinIA)

The FinIA includes a so-called chain authorization system (autorisation en cascade).

Authorization to operate as a securities firm also authorises an entity to operate as a manager of collective assets, a portfolio manager and a trustee. Authorization to operate as a fund management company also authorizes an entity to operate as a manager of collective assets and a portfolio manager. Finally, authorization to operate as a manager of collective assets also authorizes an entity to operate as a portfolio manager.

In this chain authorization system, the authorization for banks is considered as the highest authorization. Financial institutions shall at all times be compliant with the applicable requirements and duties of each specific authorization.

MAIN OBLIGATIONS UNDER FINSA

Execution only agreement, financial advisory agreement and investment management agreement & the rules of conduct.

Under FinSA, financial service providers are subject to a set of rules of conduct depending on the type of services provided and the clients' segmentation.

Client segmentation:

One of the novelties under the FinSA is that financial service providers must classify their clients under the three following categories: *retail clients, professional clients or institutional clients,* with the possibility to opt-out and to opt-in between the different categories.

Opting-out:

- High-net-worth retail clients and private investment structures created for them may declare that they want to be treated as professional clients.
- Professional clients may declare that they wish to be treated as institutional clients.

Opting in:

- Professional client may request that want the treatment of a retail client;
- Institutional clients may request to be treated as a professional client.

Before providing any financial services, financial service providers shall inform those of their clients who are not classified as retail clients of the possibility of opting in. The type and level of duties under the rules of conduct depend on the client classification.

Rules of conduct

- Duty to inform before entering into a contractual relationship
- Key information document
- Duty to review appropriateness & suitability of financial instruments
- Duty to be transparent and care in client orders
- Duty to provide documentation and rendering of account

Duty to inform before entering into a contractual relationship

Before signing an agreement such as a discretionary portfolio management mandate or an investment advisory agreement, financial service providers shall inform their clients about:

- **Information on the financial service provider such as**: name, address, field of activities and supervisory status, possibility to initiation a mediation proceeding before an ombudsman or general information on risks associated with financial instruments.
- **Information on the financial service and the financial instruments (including the risks)** such as: the nature of the financial service, its essential features and functionalities and the fundamental rights and obligations which arise from it for the clients and general risks linked to the essential features and functionalities of the financial instrument.
- **Information on costs** such as: details of the one-time and running costs of the financial service and the costs incurred in connection with the acquisition or disposal of the respective financial instrument.
- **Information on business affiliations s**uch as: information on business affiliations with third parties insofar as these affiliations may lead to a conflict of interest in connection with the financial service.
- **Information on the market offer taken into account:** financial service providers shall inform their client in particular whether the market offer taken into account when selecting the financial instruments comprises only their own or also other financial instruments (open architecture or not).

Key information document

As a general principle, where financial instruments are personally recommended, financial service providers shall make the key information document available to the retail client insofar as such a document must be produced for the financial instrument recommended.

Where a financial instrument is offered to retail clients, the issuer must first produce a key information document. However, as general exceptions:

- it is not required to prepare a key information document for financial instruments which may be acquired for retail clients solely within the scope of a portfolio management agreements;

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

Duty to review appropriateness & suitability of financial instruments

Financial service providers providing investment advice or portfolio management services shall perform an appropriateness or suitability review.

Appropriateness test

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

Suitability test

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. This knowledge and experience relates to the financial service and not to the individual transactions.

When enquiring about the client's financial situation, the financial service provider will take account of the nature and amount of their regular income, their assets as well as their current and future financial obligations.

When enquiring about the client's investment objectives, the financial service provider shall take into account the details they give in particular on the timeframe, need of liquidities, purpose of the investment, their capacity and willingness to take risks as well as any investment restrictions.

Duty to be transparent and care in client orders

An important obligation to be transparent is the obligation to inform the client **before providing a service** on the economic relationships of third party concerning the proposed financial services. This information includes whether compensation / retrocessions are received. Financial service providers may accept compensation from third parties in association with the provision of financial services only if they have expressly informed the clients of such compensation in advance and the latter relinquish such compensation or pass the compensation on to the clients in full.

The information for the clients must contain the type and scope of the compensation and must be given to them before provision of the financial service or conclusion of the contract. If the amount cannot be determined in advance, the financial service provider shall inform its clients of the calculation parameters and the ranges. If so requested, the financial service providers shall disclose the amounts effectively received.

Compensation is defined as payments from third parties accruing to the financial service provider in association with the provision of a financial service, such as brokerage fees, commissions, discounts or other financial benefits.

OA Legal highly recommends a review of the documentation on retrocessions for financial services providers who wish to keep retrocessions and distribution fees received in connection with asset management activities. This is due in particular to the decision of the Swiss Federal Supreme Court of 13 May 2020 interpreting strictly his previous well-known decision of 29 August, 2011 regarding the retrocessions in the context of discretionary mandates. The Federal Supreme Court decided that a clause stating that the retrocessions would amount to between 0% and 1% of the volume invested in certain types of products is not sufficient to constitute a valid waiver as this clause do not enable the client to determine the foreseeable amount of retrocessions received by the portfolio.

Duty to document

Financial service providers are subject to new documentation and reporting requirements under the FinSA.

Documentation

Financial service providers shall document in an appropriate manner:

- the financial services agreed with clients and the information collected about them;
- the notification that an appropriateness or suitability assessment will not beperformed or the fact that they advised the clients in accordance against availing of the service;
- the financial services provided for clients.

Reporting

If so requested, financial service providers shall provide their clients with a copy of the documentation mentioned in the previous paragraph or shall make it accessible to them in another appropriate manner.

At clients' request the financial service providers shall render account of :

- the financial services agreed and provided;
- the composition, valuation and development of the portfolio;
- the costs associated with the financial services.

The financial service provider must structure the documentation such that they are able as a rule within ten working days to render account to the client about the financial services provided.

REGISTER OF ADVISERS (FINSA)

*When you are a financial service provider not supervised by FINMA you should be aware that only persons/employees listed in the **Register of advisors** may act as a client advisor.*

The Register of advisors is kept by a licensed registration body.

A natural person who performs financial services on behalf of a financial service provider or in its own capacity as financial service providers is considered as a “client advisor” under the FinSA. Client advisors have the duty to register in the register of advisors, unless there are already supervised by FINMA or, for individuals, unless they work for an entity subject to supervision by FINMA (such as individual portfolio managers or managers of collective assets).

The main requirements to be registered in the register of advisers are the followings:

- Client advisers must have sufficient knowledge of the code of conduct set out in the FInSA and the necessary expertise required to perform their activities (training);
- Client advisers have taken out professional indemnity insurance or equivalent collateral are is available; and
- Client advisers are themselves affiliated to an ombudsman's office (organe de mediation) in their capacity as a financial service provider or the financial service provider for which they work is affiliated to an ombudsman's office.

MEDIATION BODY (OMBUDSMAN)

Financial service providers (including financial institutions) as defined under FinSA (respect. FinIA) have the obligation to affiliate with an approved mediation body (ombudsman). In order where possible to settle legal disputes between clients and financial service providers. The declarations made by the parties before an Ombudsman as well as any correspondance between the parties and an ombudsman are confidential and cannot be used in the framework of other proceedings.

The financial service providers must inform their clients of the possibility of mediation of initiating mediation proceedings before the Ombudsman to which the financial service provider is affiliated:

- upon entering into a business relationship in accordance with the duty to provide information
- in the event of the rejection of a legal claim asserted by a client; and
- at any time upon request.

DEADLINES

Managers of collective assets / securities firms

Financial institutions that already possess authorization by virtue of a financial market act pursuant to Article 1 paragraph 1 of the Financial Market Supervision Act (FINMASA), such as managers of collective assets and securities firms, must fulfil the requirements of this FinIA before 31 December 2020. This requires in particular making sure that the internal organizational management (règlement interne d'organisation) complies with the FinIA.

New individual portfolio management (or trustee) activity

Companies that were performing individual portfolio management activities before January 1, 2020 and which have complied with the annoucement deadline (as of June 30, 2020) benefit from a transitional perdiod. They shall (i) comply with the FinSA requirements before December 31, 2021 and (ii) file a request to be authorized as such by FINMA before December 31, 2022.

Companies who started their activities as of or after the 1st of January 2020 and before 31 December 2020 must (i) immediately inform FINMA accordingly (upon the incorporation of the company), (ii) join a recognised AML self-regulatory organisation for AML purposes (prior to any regulated activity) and (iii) have a deadline as of 6 July 2021 (a) to be admitted as a member of one of a supervisory organisations and (b) to file a licence application with FINMA via the FINMA platform (EHP).

Financial advisors

Financial advisors (including the ones active in a company not subject to FINMA authorisation, such as individuals providing for investment recommendations / advices) shall be registered in the advisor register of advisers before January 19, 2021 and comply with the organizational rules under the FinSA before December 31, 2021.

Ombudsman

Financial institutions (FinIA) and financial service provider (FinSA) must file an application with an ombudsman's by 24 December 2020.

In order to demonstrate an internal organization complying with FinSA and FinIA but also with the Anti-Money Laundering Act (AMLA), internal organizational management rules (*Règlement interne d'organisation*) as well as various internal directives up to date with the new regulation are required, in particular concerning compliance and risks.

Please contact our specialists if you would like to use our FinIA & FinSA templates of documentation and/or update some your existing internal directives or external documentation (including discretionary portfolio management mandate or financial advisory agreements).

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