

# Financial Services Act: point-of-sale regulation

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## Introduction

The offering of financial instruments in Switzerland under the draft Financial Services Act is under debate before the Economic Affairs and Taxation Committee of the Council of the States (for further details please see "[Offering of financial instruments – a major change of direction](#)"). The draft act should enter into force from January 2018 at the earliest and will introduce new prospectus and basic information document requirements regarding the offering of financial instruments (eg, equity and debt securities, derivatives and structured products). These new requirements will be the responsibility of the financial instruments' offerors and manufacturers. The draft act will also impose new rules of conduct on financial services providers, which must be complied with at the point of sale.<sup>(1)</sup> While some of these rules only restate existing duties, others will lay down new obligations for the financial services industry.

## Subject activities

The rules of conduct will apply to the following activities to the extent that they are rendered by a financial services provider that is acting on a professional basis in or from Switzerland:

- acquisition or disposal of financial instruments;
- receipt and transmission of orders relating to financial instruments;
- investment management;
- provision of personal recommendations on transactions with financial instruments (investment advice); and
- financing of transactions relating to financial instruments.<sup>(2)</sup>

A broad array of services (including share deal financings) may possibly be subject to the rules of conduct. Conversely, these rules should disapply with respect to insurance and reinsurance services or real estate and commercial lending.

With respect to intra-group relationships, a company which receives financial services from an affiliated company is not regarded as a client of that company.<sup>(3)</sup>

## New rules of conduct

The rules of conduct are divided into categories of duties relating to:

- information to be provided by the financial services provider;
- an appropriateness and suitability assessment to be carried out by the financial services provider;
- documentation to be provided by the financial services provider; and
- dealing with conflicts of interest.

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The standard of protection varies based on the classification of the client involved in the subject transaction. In this regard, the draft act distinguishes between three types of client:

- Retail clients:(4)
  - any client that does not qualify as a professional or institutional client; or
  - any professional or institutional client that has declared that it wishes to be considered as a retail client (opting in).
  
- Professional clients:(5)
  - financial intermediaries that are subject to prudential supervision in Switzerland (eg, banks, securities dealers and fund management companies);
  - insurance companies;
  - foreign financial intermediaries and insurance companies that are subject to an equivalent form of prudential supervision;
  - central banks;
  - public entities with professional treasury operations;
  - companies with professional treasury operations;
  - occupational pension schemes and other institutions purported to serve occupational pensions with professional treasury operations;
  - a high-net-worth individual who has declared that he or she wishes to be considered as a professional client (opting out);
  - an institutional client that has declared that it wishes to be considered as a professional client; or
  - other professional clients that the Federal Council may designate in its implementing ordinance.
  
- Institutional clients:(6)
  - financial intermediaries that are subject to prudential supervision in Switzerland (eg, banks, securities dealers and fund management companies);
  - insurance companies;
  - foreign financial intermediaries and insurance companies that are subject to an equivalent form of prudential supervision;
  - central banks; and
  - national and supranational public entities with professional treasury operations.

### ***Information duties***

According to the draft act,(7) when carrying out any of the subject activities, financial services providers must disclose certain information to their clients in a comprehensible manner, including:

- Information relating to the relevant financial services provider:
  - name, address, field of activity and supervisory status of the financial services provider; and
  - the possibility of obtaining information on the basic training and continuing professional development of the relevant client advisers performing the services.
- Information relating to the services offered and the financial instruments:
  - the nature of the financial service offered and 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; and
  - the form and manner of the custody of the financial instruments and associated risks and costs.
- Information relating to the possibility of initiating mediation proceedings in case of dispute.  
(8)

This information must be provided before the execution of the financial services agreement or the provision of services and can be issued in standardised form and communicated electronically to the client.(9) Further, the financial services provider must communicate any material change to the information to the client. While such communication must be made immediately with respect to

information relating to services offered and the financial instruments, any substantial change to the information pertaining to the financial services provider may be made on the occasion of the next contact with the client.(10) The provision of false information or hiding material facts may lead to criminal fines of up to Sfr100,000.(11)

Additionally, where the contemplated transaction relates to a financial instrument for which a basic information document is required,(12) the financial services provider should make the document available to its (retail) clients free of charge before subscription or conclusion of the relevant contract.(13) The same applies if the value of a financial instrument is based on the fluctuation of one or more other financial instruments for which a basic information document has been drawn up.(14) A breach of such duty may trigger criminal fines up to Sfr100,000.(15) By contrast, if the financial services provider's offer relates to a financial instrument for which only the drawing up of a prospectus is required,(16) the financial services provider must make the prospectus available if a retail client requests it.(17)

The extensive information duties apply regardless of client classification, with the exception of the obligation to hand over a basic information document or prospectus which is triggered only if the client is classified as a retail client.(18)

### ***Appropriateness and suitability assessment duties***

The second set of duties relates to the appropriateness/suitability assessment, first introduced in Europe under the first EU Markets in Financial Instruments Directive and, to some extent, already applied by the Swiss courts based on the Code of Obligations. These duties are applicable only to financial services providers acting as investment advisers or investment managers.(19) The type of assessment to be conducted by the relevant financial services provider is contingent on the nature of the services rendered and client classification.

The following assessments apply with regard to the nature of service rendered where a financial services provider:

- issues investment advice with respect to specific individual transactions (ie, without having regard to the client's portfolio), it must carry out the appropriateness assessment (ie, enquire about the client's knowledge and experience and ensure that the financial instruments are appropriate for its client); or(20)
- is either vested with a discretionary management mandate or dispenses investment advice taking into account the entire client's portfolio, it must conduct a suitability assessment, which consists of:
  - enquiring about the client's financial situation, investment goals, knowledge and experience; and
  - ensuring that the financial instruments advised or invested in on behalf of the client are suitable in view of all parameters.(21)

Financial services providers are dispensed with the appropriateness and suitability assessment requirements if the services are:

- limited to the execution or transmission of clients' orders; or
- rendered at the initiative of the client (reverse solicitation).

In such instances, financial services providers must inform their clients before providing their services that no appropriateness or suitability assessment will be performed.(22)

The following applies with regard to client classification if the client is classified as:

- an institutional client, no assessment is required; or(23)
- a professional client, financial services providers may assume, absent any indication to the contrary, that the client has the required knowledge and experience and can financially bear the investment risks associated with the relevant financial services.(24) Consequently, financial services providers are not required to collect detailed information regarding their professional clients' financial situation.(25)

Further, if the information received by the financial services provider is insufficient for assessing the appropriateness or suitability of a financial instrument, the financial services provider must inform its client before providing the services.(26) The same applies if the financial services provider concludes that a financial instrument is not appropriate or suitable for its client. This notification may be made in a standardised manner.(27) Notwithstanding such notification, if the client maintains its investment decision, the financial services provider remains free to execute the relevant transaction (although it should carefully document the warning to the client).(28)

A serious breach of the appropriateness and suitability assessment duties is subject to criminal fines up to Sfr100,000, not to mention other regulatory and contractual consequences for the non-compliant financial services provider.

### ***Documentation and accountability duties***

Under the draft act, financial services providers will be required to document in an appropriate manner:

- the financial services agreed with clients and the various information collected regarding the client;
- the absence of assessment in respect of a professional client or, as the case may be, the recommendation not to execute a transaction relating to a specific financial instrument;
- the financial services provided to the client;(29) and
- if the financial services provider renders advisory or management services to a retail or professional client,(30) the financial services provider must additionally document:
  - the client's need; and
  - the reasons for any recommendation to acquire, hold or dispose of any and all financial instruments.(31)

Financial services providers must provide their clients with a copy of the documentation or make it available to them through another appropriate manner.(32) Further, in case of advisory or management mandate, financial services providers will have to account for:

- the financial services agreed and provided;
- the composition, valuation and evolution of the client's portfolio; and
- the costs associated with the financial services.(33)

### ***Transparency and best execution duties***

The transparency and best execution duties apply regardless of client classification. In particular, they require that financial services providers:

- uphold the principles of good faith and equal treatment when handling client orders;(34)
- ensure in the execution of their clients' orders that the best possible outcome is achieved in terms of cost, timing and quality;(35)
- take into account not only the price of the financial instrument, but also the expenses incurred in the execution of the order and compensation from third parties;(36)
- issue and implement internal directives on the execution of client orders;(37) and
- comply with additional duties if the financial services provider is borrowing financial instruments from its client.(38)

### ***Prevention of conflicts of interest***

As a result of the organisation measures imposed by the draft act, financial services providers are under a general duty to avoid or, as the case may be, disclose such conflicts of interest.(39) In particular, the act addresses which conditions a financial services provider may receive from third parties regarding compensation (ie, brokerage fees, commissions, discounts or other financial benefits).(40) Reflecting the current requirements laid down by case law,(41) financial services providers may accept such compensation provided that they either:

- pass the compensation on to the clients in full; or
- expressly inform the clients before concluding the provision of the services or concluding the contract on the type and scope of the compensation or, if the amount of such compensation may not be determined in advance, the calculation parameters and the ranges of the

## **Interplay with offering rules**

Absent any indication to the contrary in the draft act, offerors or manufacturers of financial instruments are not responsible for ensuring compliance with the rules of conduct, unless they are acting in a financial services provider capacity. However, offerors and manufacturers of financial instruments remain liable for any inaccurate or misleading information disseminated in a prospectus, key information document or similar communication to a client.(43) The client that would incur any loss resulting from a financial services provider breaching its obligations in connection with the acquisition or sale of financial instruments would thus have no recourse against the offeror or manufacturer of such financial instruments.

Conversely, a financial services provider should in principle incur no liability in case of inaccurate or misleading information contained in a prospectus or key information document that it would have handed over to its clients when performing its services. The conduct that a financial services provider should adopt if such documents are unavailable is less clear. In particular, it is uncertain whether a financial services provider may still provide services with respect to a financial instrument for which no prospectus or key information document has been drawn up or whether the financial services provider should refrain from providing any such services.

## **Comment**

While many of the rules of conduct are already known by financial services providers, the draft act and its implementing ordinance will impose clearly defined requirements, which will require financial services providers to adapt their day-to-day operations and take organisational measures to ensure continuing compliance. However, offerors and manufacturers of financial instruments should not be responsible for monitoring compliance with the rules, subject to their involvement in a specific transaction as financial services providers.

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## **Endnotes**

(1) The new rules do not prejudice the sector-specific rules of conduct which already apply to certain financial services providers, such as the holders of a licence pursuant to the Collective Investment Schemes Act (see Article 8(3) of the Financial Services Act).

(2) Article 8(1) *cum* Article 3(d).

(3) Article 4(6).

(4) Article 4(2) and 5(2).

(5) Article 4(3) and 5(1).

(6) Article 4(4).

(7) Article 9.

(8) Article 77 *et seq.*

(9) Article 9(3) and 10(1).

(10) Article 10(5).

(11) Article 92(1)(a).

- (12) Article 60 *et seq.*
- (13) Article 10(2).
- (14) Article 10(3).
- (15) Article 93(2).
- (16) Article 37 *et seq.*
- (17) Article 10(4).
- (18) Article 22 *cum* 10(2) to (4).
- (19) Article 11.
- (20) Article 12.
- (21) Article 13.
- (22) Article 14.
- (23) Article 22 *a contrario*.
- (24) Article 15.
- (25) Federal Council, Dispatch on Financial Services Act and the Financial Institutions Act, November 4 2015, page 53.
- (26) Article 16.
- (27) *cf* Federal Council, Dispatch on Financial Services Act and the Financial Institutions Act, November 4 2015, page 54.
- (28) *Ibid.*
- (29) Article 17(1).
- (30) Article 22.
- (31) Article 17(2).
- (32) Article 18(1).
- (33) Article 18(2). The minimum information and timing of communication will be set out in the implementing ordinance. Article 18(3).
- (34) Article 19(1). These principles, including the procedures and systems for processing clients orders, will be set out in detail in the implementing ordinance (Article 19(2)).
- (35) Article 20(1).
- (36) Article 20(2).
- (37) Article 20(3).
- (38) Article 21.
- (39) Article 27(1) to (2).

(40) Article 28(3).

(41) See Supreme Court decisions ATF 138 III 755; ATF 137 III 393; ATF 132 III 460.

(42) Article 28.

(43) Article 72(1).

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