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The New Registration Duty for Client Advisers – An Update on the Final FinSO

Reference: CapLaw-2019-55

On 6 November 2019, the Federal Council decided that the Financial Services Act (FinSA) would enter into force on 1 January 2020. Subject to a transition regime, the FinSA will introduce a new registration duty for client advisers of Swiss financial service providers not subject to prudential regulation and client advisers of foreign financial institutions. Today, no such registration requirement exists with the exception of similar obligations for untied insurance intermediaries, who have to register with the public register kept by the Swiss Financial Market Supervisory Authority (FINMA).

Under the new regime, client advisers will be required to register in a register maintained by one or more registration bodies licensed by FINMA. To register, they must evidence sufficient knowledge of the rules of conduct under the FinSA and the necessary expertise to perform their duties, adequate financial means as well as affiliate themselves with an ombudsman's office. Clients may check the register at any time to verify that their adviser has the required qualifications. The registration will, however, not imply any prudential or ongoing supervision by FINMA. If a client adviser no longer meets the registration requirements, the adviser will be deleted from the register by the competent registration body and may, consequently, no longer engage in activities as a client adviser.

By Martin Peyer

1) Introduction

Client advisers play an important role in implementing the new rules of conduct in articles 7 ff. FinSA. They are usually the primary point of contact for clients with their financial service provider and, only if they have sufficient knowledge of the new rules, they can comply with them in practice.

The responsibility to ensure that its client advisers will comply with the requirements of the FinSA lies with the financial service providers. In particular, they must ensure that their advisers have an appropriate education and the necessary skills for the specific services they provide (article 6 FinSA). For prudentially supervised financial service providers, FINMA or a supervisory organization pursuant to the Financial Institutions Act (FinIA) will monitor that client advisers comply with these requirements. No such controls exist, however, for Swiss and foreign financial service providers that are not supervised by FINMA.

To bridge this gap, the FinSA will require client advisers of Swiss financial service providers who are not prudentially supervised (such as insurance intermediaries and financial advisers) and financial service providers domiciled abroad to register themselves in the new register of advisers that will be established under the FinSA (article 28 (1)

FinSA) (*see* Dispatch by the Federal Council on the Financial Services Act and the Financial Institutions Act of 4 November 2015, Federal Gazette 2015 (Dispatch FinSA), page 8901 ff., page 8967). In addition, to protect clients, client advisers who have seriously breached the rules of conduct in the past will not be allowed to register themselves and, thus, to provide financial services. Further, advisers – or the financial service provider for which they work – must guarantee that they have sufficient financial resources to carry out their business activities (*see* Dispatch FinSA, page 8922).

The registration will, however, not imply any prudential or ongoing supervision by Swiss authorities. It only seeks to ensure that client advisers are aware of the rules of conduct and treat clients fairly. Yet, clients may check the register, which will be available over the internet, at any time if they have doubts about the qualifications or integrity of their client adviser (article 32 (5) FinSA), and, therefore, the new register is also expected to increase clients' confidence in their client advisers.

2) Duty to Register for Client Advisers

a) Definition of Client Adviser

According to article 3 (e) FinSA, a client adviser is a natural person who performs financial services on behalf of a financial service provider or in its own capacity as financial service provider. In most cases, the adviser is not identical with the financial service provider for which it acts. Only if a natural person provides financial services, it may at the same time be both, a client adviser and a financial service provider (Dispatch FinSA, page 8922 and 8947 f.).

The term "client adviser" has to be interpreted broadly and includes persons that carry out transactions in financial instruments for clients or advise them in connection with their investments such as asset managers, financial advisers and insurance intermediaries. Moreover, activities of distributors of collective investment schemes that are directed at a specific client aiming specifically to sell or purchase securities (*see* article 3 (2) Financial Services Ordinance (FinSO)), such as roadshows in which foreign collective investment schemes are advertised (Explanatory Report of the Federal Department of Finance of 6 November 2019, page 19), also constitutes a financial service pursuant to the FinSA if it is carried out on a professional basis. Thus, persons formerly holding a license as distributor of collective investment schemes will also have to register in the register of advisers if they provide true sales-related services to clients (unless an exemption applies). By no longer including distribution generally in the catalog of financial services, the FinSO departs from the much more extensive view taken in the draft ordinance. Nevertheless, substantial uncertainty remains whether certain other services for instance relating to roadshows and similar activities constitute a financial service under the FinSA considering the fact that an offer of financial instruments does not qualify as such (Explanatory Report, page 21). However, not every

employee of a financial service provider is deemed a client adviser. Employees who have no direct contact with clients or who support the provision of financial services only to a minor extent, *e.g.* by sending product information to a client in response to an expression of interest, coordinating meetings or working in technical support functions, have no duty to register (Dispatch FinSA, page 8948). In this context, it remains to be seen how persons who have contact with clients under the direct and ongoing supervision of a client adviser, such as a financial analyst providing specialist advice in a meeting conducted by a client adviser will be treated.

The final version of the FinSO clarifies though that corporate finance experts, who advise a company in an IPO in Switzerland, for example, will not fall in the scope of the new rules (*see* article 3(3)(a) FinSO; Explanatory Report, page 19 f.) as long as they do not provide investment advice or other financial services pursuant to article 3 (c) FinSA at the same time.

b) Scope

Only client advisers who are not acting for a financial service provider that is prudentially supervised in Switzerland need to register, regardless of whether they carry out their business in Switzerland or from abroad or whether they are dealing with retail or professional clients (Dispatch FinSA, page 8918 and 8967). The requirement that all client advisers would have been obliged to register in the register of advisers proposed in the consultation draft of the FinSA (*see* article 29 of the consultation draft) has been dropped after criticism during the consultation process.

The Federal Council may exempt certain foreign client advisers from the scope of the registration duty (article 28 (2) FinSA). Whereas the draft ordinance only foresaw a very narrow exemption for client advisers of prudentially supervised foreign financial service providers that are members of a financial group which is subject to consolidated supervision of FINMA if they provide their services in Switzerland exclusively to professional clients (including institutional clients) (article 31 draft FinSO), the Federal Council opted for broadening this exemption in the final version of the ordinance. Following criticism in the consultation proceedings, it extended the exemption from the registration duty to all client advisers of foreign financial service providers who are subject to prudential supervision in their home country provided they exclusively provide financial services to professional or institutional clients in the final version of the FinSO (article 31 FinSO).

Consequently, only client advisers of foreign financial service providers who are either not prudentially supervised in their home jurisdiction or who provide financial services to retail clients will be required to register in the Swiss register of advisers if they provide financial services on a cross-border basis.

The FinSO does not condition this exemption on the equivalence or adequacy of the prudential supervision in the home country of the foreign financial service provider. While this will decrease the administrative burden related to registration, it does not exempt foreign financial service providers from complying with the regulatory framework in Switzerland. Indeed, they will need to comply with the FinSA and ensure that they follow the Swiss rules of conduct and have an appropriate organization. Further, foreign financial service providers are required to join an ombudsman's office even if they are subject to similar duties abroad or provide services to institutional and professional clients only which generally do not relay on the a proceeding before an ombudsman.

3) Requirements for Registration

Client advisers will only be registered in the register if they meet the conditions of article 29 FinSA. According to this provision, they must prove that they have sufficient knowledge of the rules of conduct set out by the FinSA and the necessary expertise to perform their duties, that they have adequate insurance coverage or equivalent financial guarantees and that they (in their capacity as a financial service provider or the financial service provider for which they act) are affiliated to an ombudsman's office (*see* article 74 FinSA).

The liability insurance must cover damages resulting from a breach of the statutory obligations set out in the FinSA of at least CHF 500,000 per year. Coverage must be increased in several steps for additional client advisers to a maximum of CHF 10 million if a financial service provider employs more than 10 client adviser (article 32 (1) – (3) FinSO). Additional contractual liabilities to the client can be excluded from the insurance coverage (*see* Explanatory Report, page 34). Alternatively, a financial guarantee in the same amount must be deposited with the consent of the registration body with a Swiss bank. For prudentially supervised foreign financial service providers, a minimum capital equivalent to at least CHF 10 million is considered adequate as a financial surety (article 33 FinSO). If a client adviser is employed by a financial service provider, the latter can arrange for the insurance coverage or the financial guarantee (article 29 (3) FinSA).

Article 29 (2) FinSA further requires client advisers to prove that they have not seriously breached the rules of conduct in the past by providing an extract from the register of criminal records to the registration body. Client advisers who have been convicted of offenses pursuant to article 89-92 FinSA (*e.g.*, by providing false information or withholding material facts in connection with the information duties of article 8 FinSA, seriously violating the duties to assess appropriateness and suitability pursuant to article 14 ff. FinSA or violating the provisions regarding compensations from third parties in article 26 FinSA), article 86 of the Insurance Supervision Act or offences against property will not be entered into the register. This also applies to persons that have been banned from acting in a management capacity of a financial institution or from trading

in financial instruments or acting as a client adviser (articles 33 and 33*a* of the Financial Market Supervision Act).

4) Registration Body

The register of advisers will be maintained by one or more privately organized registration bodies, which will have to be licensed by FINMA (article 31 (1) and (2) FinSA). The registration body must have its domicile in Switzerland and must be organized in a way to ensure independence in fulfilling its tasks. For this purpose, the register must implement adequate internal rules to prevent, *inter alia*, conflicts of interests of the persons concerned with the management and an internal control system ensuring compliance with the FinSA and the implementing ordinance (articles 36 ff. FinSO; Explanatory Report, page 37 f.).

Earlier this year, BX Swiss AG announced that it will apply for being licensed as registration body. Further, it is expected that at least one additional registration body also intends to file a license application.

In case FINMA approves more than one registration body, FINMA must ensure appropriate coordination between them with respect to their practice (article 35 (4) FinSO).

5) Content of the Register

As minimum content, the register entry must include at least the name and the business address of the client adviser, its position within the financial service provider and its fields of activity, information about education and completed trainings, the name of the ombudsman's office to which it is affiliated and the date of the register entry. This basic information allows clients to verify that their client adviser has the required knowledge and skills. In case of a dispute between the financial service provider and the client, the register entry also permits the latter to identify the competent ombudsman to initiate a mediation proceeding pursuant to article 74 ff. FinSA (*see* Dispatch FinSA, page 8968).

6) Maintaining the Register and Notification Duty

The registration body verifies that the requirements for registering a client adviser are met and issues a decree (in the sense of article 5 of the Administrative Procedure Act (APA)) confirming the registration (article 32 (1) FinSA). Registered client advisers and the financial service providers for which they work must notify the registration body of all changes that are relevant for the registration (including changes of the affiliation with the ombudsman's office, a termination of the liability insurance, convictions for relevant criminal offences or a ban by FINMA from an activity in the financial industry or similar foreign measures) within 14 days (article 32 (2) FinSA and article 41 FinSO).

Further, client advisers have to renew their registration every 24 months. Otherwise, the registration will be deleted from the register (article 41 (2) FinSO).

If the registration body becomes aware that the registration requirements are no longer met, it will issue a decree and remove the respective client adviser from the register (article 31 (4) FinSA). The adviser may consequently no longer engage in activities as a client adviser. The decree of the registration body is subject to appeal to the Federal Administrative Court.

7) Applicable Rules of Procedure and Registration Fees

The procedure for the registration is governed by the APA (article 34 FinSA). If the registration body approves a registration of a client adviser, it is not required to provide a reasoning (article 35 (3) APA). However, if it rejects the registration without providing the applicant the possibility to amend the application, the applicant has a right to be heard (article 30 (1) APA; Dispatch FinSA, page 8970).

To cover the operating expenses, the registration body may charge cost-covering fees in line with the general principles applicable to levy fees by public authorities (article 33 (1) FinSA; Dispatch FinSA, page 8970). For first time registrations, the fee will amount to CHF 500-2,500. A renewal of an existing entry in the register will cost CHF 200-1,000. For urgent requests, a 50 percent surcharge may be applied (article 42 (2) and (6) FinSO). In addition, a registration body may charge an annual fee to cover its running costs (article 42 (1) FinSO).

8) Breach of Registration Duty

A breach of the registration duty may trigger administrative measures by FINMA pursuant to articles 31 ff. of the Financial Market Supervision Act (FINMASA) or the respective person may become criminally liable pursuant to article 44 FINMASA.

9) Transition Regime

Client advisers who have to register pursuant to article 28 FinSA will have until 1 July 2020 to file their application with the registration body (article 95 (2) FinSA). If on 1 January 2020 (upon the entry into force of the FinSA), no registration body will have been approved, the six month period to register will only start with the authorization of the first such registration body by FINMA. The deadline will be met with the filing of the application for being registered (article 107 FinSO).

10) Outlook

Overall, the registration duty will affect non-regulated Swiss financial service providers and, in particular, foreign financial institutions that are not prudentially supervised in their home jurisdiction or, if they are subject to supervision, which also provide financial

services to retail clients in Switzerland and currently offer financial services or products to Swiss clients. Going forward, such foreign financial service providers can no longer rely on Switzerland's current liberal inbound cross-border regime and will be required to either register their client advisers in the register of advisers or establish a regulated subsidiary in Switzerland and.

The scope of the registration duty, however, is not entirely clear yet. While the final version of the FinSO clarified that corporate finance experts, who advise for example a company in an IPO in Switzerland, will not fall in the scope of the new rules as long as they do not also provide investment advice or other financial services, the situation with regard to the activities of distributors of collective investment schemes, for instance, is less clear. Activities that are directed at specific clients aiming specifically to sell or purchase securities, such as a roadshow in which foreign collective investment schemes are advertised, also constitute financial services pursuant to the FinSA and, thus, the persons providing such services on a cross-border basis will need to be registered in the register of advisers. It remains to be seen, however, whether certain other services, for instance relating to roadshows and similar activities, constitute a financial service under the FinSA considering the fact that an offer of financial instruments does not qualify as such.

With the entry in force of the FinSA and the FinIA, together with their implementing ordinances, on 1 January 2020, client advisers will have six months until 1 July 2020 to register if a registration body is authorized upon entry in force of FinSA and, otherwise, six months from the authorization of a registration body (article 95 (2) FinSA and article 107 FinSO).

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Funds Distribution under the new financial market law architecture

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On 1 January 2020, the new Financial Services Act (FinSA) and the Financial Institutions Act (FinIA) will enter into force. This entails various changes of existing regulatory concepts in the context of distribution and management of collective investment schemes. From today's CISA perspective, the term "distribution" under Art. 3 CISA plays a fundamental role. Under the new regulatory regime, an exclusive focus on the new concept of the offer falls short in explaining the rules governing the distribution of funds. Particularly with regard to the behavior at the point of sale, the concept of financial services is of primary importance.

By Diana Imbach Haumüller / François Rayroux