

# Update

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## Case Review: FINMA confirms Bank Confidentiality with regard to Swiss Bank Branches

In its bulletin 3/2012 FINMA published in October 2012 a number of recent cases relating to bank regulatory matters. One of these cases related to outsourcing of IT services to the foreign head office of a Swiss bank branch. FINMA confirmed that bank and professional confidentiality obligations under Article 47 Banking Law and Article 43 Stock Exchange Law also apply in respect of the relationship between Swiss bank branch and its foreign head office. The Swiss bank branch is obliged to ensure that the technical maintenance of the IT system is made in accordance with the confidentiality obligations even after a change of the IT security head (FINMA Bulletin 3/2012, p. 106 et seq.).

### 1. Facts of the case

A Swiss bank branch ("**Branch**") had entered into a service level agreement with its foreign head office in relation to certain IT services. Under the service level agreement the data regarding the clients of the Branch which are subject to Swiss bank confidentiality had to be maintained in a separate data base and located on a server in Switzerland. Restrictions with regard to accessibility ensured that the head office could not access the client data located in Switzerland. After the departure of the person responsible for IT security of the Branch, employees of the head office took over the administration rights in a way that gave them access to the data from abroad. At that time, no employee of the Branch had the technical expertise to provide administration services in Switzerland. Neither the management board of the Branch nor the head office had knowledge of the transfer of the administration rights. Immediately after the auditor (PwC) discovered the irregularities, the Branch took the necessary actions in order to re-obtain the control over the administration rights. In addition, it retained the auditor to provide the necessary advice with regard to ensuring compliance with the law.

### 2. Legal considerations

#### a) Applicable principles

The Branch is a branch of a foreign bank and a foreign securities dealer and is in this capacity licensed by FINMA. The Branch is legally part of the head office and is not an independent legal entity. It is subject to the supervision of the home regulator of the head office. It is, however, also subject to the supervision of FINMA which has to verify that the licensing requirements are met at all times. With regard to the licensing requirements the foreign head office is responsible for putting in place for the Branch an adequate organisation, appropriate financial resources and sufficient personnel to meet at all times the license requirements of FINMA. The management of the Branch has to ensure the adequate organisation and proper conduct of its officers. The management and the employees of the Branch are subject to Swiss bank secrecy pursuant to Article 47 Banking Law and professional securities dealer secrecy pursuant to Article 43 Stock Exchange Law. Swiss bank branches have to comply with the relevant provisions of the Swiss Banking Act and the Swiss Stock Exchange Act, except as regards Swiss equity requirements and Swiss cluster risk rules that do not apply, as in this regard the home country rules of the head office apply. The

Branch must be properly organised in accordance with Swiss law and have internal regulations which describe the business activities and provide for an adequate organisation. Risks including operational, legal and reputational risks have to be identified, limited and managed by the Branch. The Branch has to put in place an effective internal control system which includes adequate structures and control procedures ensuring the good functioning and the achievement of the business objectives. The internal control system not only includes control activities "*a posteriori*" but also procedures in view of management and planning.

In this regard the FINMA Circular 2008/7 regarding outsourcing by banks specifies the organisational measures that have to be taken by the Branch to ensure the protection of client data and bank confidentiality in connection with the outsourcing of services. In particular, the principles 5 and 6 of the Circular have to be observed. Principle 5 relates to business and bank confidentiality and data protection and includes the obligation to ensure the confidentiality of client data. In case of outsourcing to foreign countries, adequate technical and organisational measures have to be put in place to ensure that bank confidentiality and data protection in accordance with Swiss law is maintained. Principle 6 relates to the information of clients and requires that clients are informed in advance of the outsourcing and the transmission of client data in the form of general business conditions or, in case the transfer is made abroad, a separate letter. The information must contain a description of the outsourced services and set out in detail the protective measures taken. In this connection FINMA, in particular, confirmed that in case of existing relationships the clients must be notified in advance of the transmission of data abroad as well as the protective measures taken in this regard and must be given the possibility to terminate the bank relationships in due time before the transfer.

#### **b) Decision of FINMA**

FINMA held that the Branch violated principle 5 of the FINMA Circular 2008/7 regarding outsourcing in that it did not ensure bank secrecy and data protection with respect to its head office by appropriate means in the period between the departure of the person responsible for IT security and the corrective measures taken by management after the discovery of the deficiencies by the auditors. Further, it held that the Branch only amended the general business conditions and informed its clients after the dis-

covery of the deficiencies in view of adequately informing them about outsourcing. In this regard it violated principle 6 of the outsourcing circular. As a result of these violations, the Branch was not adequately organised for its business activities and severely violated the licensing requirements of FINMA. The violations continued for eight months and exposed the clients of the Branch to the risk that client data were not kept confidential. The seriousness of the breach justified a declaratory decision in the meaning of Article 32 Financial Market Supervision Law.

FINMA further held that there was no evidence that confidential data effectively leaked to the head office and that, therefore, no further steps with regard to bank secrecy and professional secrecy had to be taken. In other words, FINMA did not inform the penal authorities of a possible violation of Swiss bank secrecy.

#### **3. Conclusions**

The FINMA decision confirms the well established principle that bank confidentiality and professional confidentiality also applies to the relationship between a Swiss bank branch and its head office. The decision further emphasizes the importance of the outsourcing circular, in particular in connection with the protection of bank confidentiality, data protection and information on clients. It highlights the fact that even violations of which the management of the Branch is not aware constitute a serious violation of licensing requirements. The decision emphasizes the importance of the control of the administration rights of the IT system, in particular in connection with the change in personnel. It also shows that only the absence of an effective data leak prevented a criminal investigation with regard to a possible violation of bank secrecy.

Finally, it must be pointed out that the same principles also apply to the relationship between a Swiss bank subsidiary and its foreign bank parent or foreign affiliates.

Please do not hesitate to contact us for any follow-up queries you may have.

### Your Contacts

#### Zurich

Stefan Breitenstein  
stefan.breitenstein@lenzstaehelin.com

Lukas Morscher  
lukas.morscher@lenzstaehelin.com

Telephone + 41 58 450 80 00

#### Geneva/Lausanne

Shelby R. du Pasquier  
shelby.dupasquier@lenzstaehelin.com

Fedor Poskriakov  
fedor.poskriakov@lenzstaehelin.com

Telephone +41 58 450 70 00

### Our Offices

#### Zurich

Bleicherweg 58  
CH-8027 Zürich  
Telephone +41 58 450 80 00  
Fax +41 58 450 80 01  
zurich@lenzstaehelin.com

#### Geneva

Route de Chêne 30  
CH-1211 Genève 17  
Telephone +41 58 450 70 00  
Fax +41 58 450 70 01  
geneva@lenzstaehelin.com

#### Lausanne

Avenue du Tribunal-Fédéral 34  
CH-1005 Lausanne  
Telephone +41 58 450 70 00  
Fax +41 58 450 70 01  
lausanne@lenzstaehelin.com

[www.lenzstaehelin.com](http://www.lenzstaehelin.com)

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