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Update

Newsflash December 2018

The Swiss Federal Council takes measures to protect Swiss stock exchanges

- **Trading of Swiss listed equities on foreign trading venues to be subject to regulatory approval in Switzerland as from January 2019**
- **Criminal sanctions contemplated in case of breach**
- **Temporary authorizations available to foreign securities firms willing to trade on Swiss trading venues**

On 30 November 2018, the Swiss Federal Council announced that it had adopted special regulations designed to protect Swiss financial markets infrastructures: the "Ordinance on the Recognition of Foreign Trading Venues for the Trading of Equity Securities of Companies with Registered Office in Switzerland (the "ORFTV"). The measure was announced only a few days after the European Commission indicated that it was considering not extending its equivalence decision for Swiss stock exchanges beyond December 2018.

Significance of an equivalence recognition for Swiss stock exchanges

EU legislation imposes a trading obligation for shares admitted to trading on a regulated market or traded on a trading venue in the EU by requiring EU investment firms to trade such shares only on a regulated market, MTF, systematic internaliser, or an equivalent third-country trading venue. Being recognised as an equivalent third-country trading venue is therefore of key importance for non-EU stock exchanges such as the SIX Swiss Exchange ("SIX") or BX Swiss ("BX"). Absent such recognition, EU investment firms could no longer place orders (either directly or through brokers) to trade shares on these two stock exchanges. The duty to place orders on recognised trading venues would trump any duty owed to clients to provide best execution. A non-recognition of equivalence would consequently result in the order flows from EU investment firms being redirected from SIX and BX to EU trading venues. Since most Swiss issuers currently have their equity securities traded on one or more EU trading venues (either at their request or based on a unilateral decision of the relevant trading venue), an acknowledgement of non-equivalence could significantly reduce the liquidity of Swiss equity markets.

The equivalence recognition and the Swiss-EU institutional framework negotiations

In December 2017, the European Commission recognised that the legal and supervisory framework applicable to SIX and BX was equivalent to the requirements imposed by EU's securities laws. However, the Commission unexpectedly limited the effect of its decision to a one-year period, expiring on 31 December 2018. The Commission had indicated at the time that, when deciding on whether to extend the applicability of its equivalence decision, it would "in particular consider progress made towards the signature of an agreement establishing [a] common institutional framework" between the EU and Switzerland. On 27 November 2018, the Vice President of the European Commission indicated that there was not sufficient progress in the discussions with the Swiss authorities to allow for the extension of the equivalence decision for Swiss stock exchanges beyond December 2018.

The Swiss Federal Council responded to that statement on 30 November 2018 by taking special measures to protect Swiss financial markets infrastructures, a move that it had announced in June 2018 as a possibility in the event that the Commission would refuse to extend its equivalence decision beyond December 2018.

Measures imposed by the Federal Council

The ORFTV reflects a distinct effort to find a balance between putting adequate pressure on the EU authorities and avoiding excessive collateral damage. When announcing the measures on 30 November 2018, the Swiss Federal Council insisted that it is "continu[ing] to advocate that the European Commission extend indefinitely Switzerland's stock market equivalence" and that a "swift and unlimited extension of stock market equivalence" remains in its view "the best solution for all affected market players in Switzerland and abroad". The fact that the ORFTV was adopted under Article 184 of the Swiss Federal Constitution – a provision that gives the Swiss Federal Council authority to adopt extraordinary legislation without involving the Swiss Parliament "[w]here safeguarding the interests of the country so requires" – illustrates the extraordinary character of the measures.

The ORFTV contemplates two key measures: an obligation for foreign trading venues to obtain a prior recognition from the Swiss Financial Market Supervisory Authority ("**FINMA**") to trade Swiss listed equities as from January 2019 and a grant of temporary authorization for foreign investment firms desiring to participate in Swiss trading venues.

a) Obligation for foreign trading venues to obtain a prior recognition from FINMA

The ORFTV makes the trading of equity securities of companies having their registered office in Switzerland and listed on a stock exchange in Switzerland or traded on a trading venue in Switzerland ("**Swiss listed equities**") by trading venues having their registered office outside of Switzerland ("**foreign trading venues**") subject to a prior recognition from FINMA.

The obligation imposed by the ORFTV applies to all trading venues worldwide, and consequently has a transnational reach. Contrary to what is the case under the usual licencing regime for foreign trading venues, FINMA's authorization is not only required when the relevant venue intends to grant access to Swiss participants to its markets. An authorization is required for any foreign trading venue, wherever located, willing to trade Swiss listed equities on its markets after 31 December 2018. Trading Swiss listed equities without the necessary authorization after 31 December 2018 would constitute a criminal offense, sanctioned by a prison term of up to three years and a fine of up to CHF 540'000 in case of intentional breach, or a fine of up to CHF 250'000 in case of negligence.

b) Grandfathering for Swiss issuers having a secondary listing in the EU

Under the ORFTV, foreign stock exchanges are not required to obtain an authorization to continue trading Swiss listed equities that were already listed on their markets prior to 30 November 2018 with the consent of the relevant Swiss issuer. Swiss listed equities traded on venues such as MTFs without the consent of the relevant issuer do not benefit from this regime.

c) Authorization procedure

Under the ORFTV, FINMA will only authorize foreign trading venues to trade Swiss listed equities if the relevant venue (i) is subject to appropriate regulation and supervision in its home jurisdiction and (ii) does not have its registered office "in a jurisdiction that restricts its market participants in trading equity securities of companies with registered office in Switzerland at Swiss trading venues" and "thereby significantly adversely affects the trading in such equity securities at Swiss trading venues". The ORFTV further provides that the Swiss Federal Department of Finance (the "**FDF**") must set a list of the jurisdictions involved. The only jurisdictions mentioned on the tentative list that the FDF published on 30 November 2018 are the member states of the European Union.

In a communication published on 30 November 2018, FINMA indicated that it had already authorized, by way of a collective decision, several non-EU foreign trading venues to trade Swiss listed equities. The list includes trading venues from Mexico, Singapore, South Africa and the United States.

d) Temporary authorization for foreign investment firms desiring to participate in Swiss trading venues

Swiss law requires that foreign firms obtain an authorization from FINMA to participate in a Swiss trading venue. To make it possible for FINMA to deal with the surge of authorization requests that may result from the restriction imposed on foreign trading venues to trade Swiss listed equities after 31 December 2018, the ORFTV makes it possible for FINMA to grant temporary authorizations to participate in Swiss trading venues for up to one year. Firms having obtained such temporary authorizations will have to satisfy the record-keeping and reporting obligations contemplated by Swiss law by August 2019 (with trades executed between 1 January 2019 and 31 July 2019 being recorded and reported retroactively by 1 October 2019).

Conclusion

With the ORFTV, the Swiss Federal Council is walking a fine line between protection of Swiss financial markets infrastructures and potential disruptions to the international flow of capital. To do so, the Swiss Federal Council has been mindful to target foreign trading venues exclusively, and not to extend the ban to other market participants such as brokers, central counterparties or central securities depositories.

Whether EU investment firms trading Swiss listed equities on unauthorized trading venues after 31 December 2018 (as well as central counterparties clearing such trades and central securities depositories providing settlement services) could be imposed some liability for aiding and abetting the foreign trading venues is, however, an open question.

Please do not hesitate to contact us in case of any questions.

Your contacts

Geneva / Lausanne

Jacques Iffland
jacques.iffland@lenzstaehelin.com
Tel: +41 58 450 70 00

François Rayroux
francois.rayroux@lenzstaehelin.com
Tel: +41 58 450 70 00

Zurich

Hans-Jakob Diem
hans-jakob.diem@lenzstaehelin.com
Tel: +41 58 450 80 00

Patrick Schleiffer
patrick.schleiffer@lenzstaehelin.com
Tel: +41 58 450 80 00

Our offices

Geneva
Lenz & Staehelin
Route de Chêne 30
CH-1211 Genève 6
Tel: +41 58 450 70 00
Fax: +41 58 450 70 01

Zurich
Lenz & Staehelin
Brandschenkestrasse 24
CH-8027 Zürich
Tel: +41 58 450 80 00
Fax: +41 58 450 80 01

Lausanne
Lenz & Staehelin
Avenue de Rhodanie 58
CH-1007 Lausanne
Tel: +41 58 450 70 00
Fax: +41 58 450 70 01

www.lenzstaehelin.com